Rambus Dodges an Antitrust Bullet from the FTC

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In a case closely-watched by the high technology community, this week the D.C. Circuit Court set aside the FTC's landmark order against Rambus Incorporated, which had sought to limit royalties Rambus could charge for certain patented DRAM technology that had been incorporated into various industry standards. *Rambus, Inc. v. Federal Trade Commission*, No. 07-1086 consolidated with 07-1124, 2008 U.S. App. LEXIS 8662 (D.C. Cir. April 22, 2008). The decision sharply undercuts the FTC's effort to limit so-called "patent hold-up" threats to standard-setting activities, and consequently highlights the need for standard-setting organizations ("SSOs") and their participants to establish clear IP rules and self-police compliance in order to avoid later problems regarding the use of proprietary technology in a standard.

The FTC found that Rambus had violated Section 5 of the FTC Act by engaging in deception when it failed to disclose its plans to patent key technology that was ultimately incorporated in JEDEC standards for SDRAM chips. In so holding, the FTC applied the standards of Section 2 of the Sherman Act for illegal monopolization. The D.C. Circuit reversed. The court read the FTC's opinion to rely on alternative grounds: Rambus's deception *either* caused JEDEC (i) not to use alternative technologies that it otherwise would have used had Rambus fully disclosed its intentions *or* (ii) not to obtain commitments from Rambus to license on RAND (reasonable and non-discriminatory) terms or other royalty-limiting bases that it otherwise would have obtained with full disclosure by Rambus.

The court agreed that deception would violate Section 2 if it caused JEDEC to incorporate proprietary technology rather than available alternative technology. However, the court relied on the alternative grounds in the FTC's initial opinion, statements in the remedy order, and concessions by counsel at oral argument to conclude that the FTC had not made this crucial finding. While Rambus thus escaped on this theory, it remains a potential weapon against other companies.

Turning to the alternative theory of higher than RAND pricing, the court held that it did not establish a violation of the antitrust laws. The court read Supreme Court authority to establish that the *mere* fact that consumers pay more as a result of deception does not establish harm to the competitive *process*, as is necessary to prove an antitrust violation.

Recognizing the possibility of further proceedings on remand, the court also addressed the basis for the FTC's finding of deception. In short, the court expressed significant skepticism that the rules of JEDEC clearly required the disclosure of the patent plans that ultimately led to the patents in question. The rules required disclosure of patents and patent applications. According to the court, Rambus had neither at the relevant time, although it arguably had plans for such applications. The court was unconvinced by the FTC's efforts to bootstrap a requirement to disclose from ambiguous "expectations" of other JEDEC participants.

Analysis

Everyone agrees that standard setting organizations have the potential for both pro-competitive and anti-competitive effects. With particular reference to the *Rambus* situation, once technology is embedded in a standard that is widely accepted, a company with patent rights over that technology may have significant market power.

If there are other technology choices that could reasonably substitute for the patented technology, the inclusion of one of the choices in the standard may create market power that otherwise would not have existed. In that situation, it makes sense for the standard setting organization to demand that participants reveal their patents and planned patents and to require the agreement to RAND royalty rates in order to protect users of the standard from patent hold-up. On the other hand, if the patented technology is the only feasible choice, the monopoly comes from the patent rights, and the inclusion in the standard may not add to the market power. The court in *Rambus* held that the FTC did not make a clear finding that the case involved the former situation and not the latter.

If one assumes that Rambus had fundamental patents that would have to be included in any standard anyway, the FTC's second theory that the deception prevented JEDEC from obtaining RAND royalty concessions arguably does not make economic sense. On that view of the facts, Rambus would not have to engage in deception; it simply could decline to participate in the development of the standard if the price of doing so was agreement to RAND terms.

It remains to be seen whether the FTC will attempt to proceed against Rambus on an alternative theory of unfair practices, which would not require the same strong showing of harm to the competitive process. The court's strongly stated skepticism about the foundation for the finding of deception certainly makes such a case more difficult. While the FTC's most recent action in this area (its November 2007 settlement with Negotiated Data Solutions LLC) relied solely on Section 5's general prohibitions against unfair competition and unfair or deceptive acts or practices—and not the standards of a Section 2 monopolization case—proof of deception is still a necessary element.

Lessons

Under the D.C. Circuit's analysis, to sustain an antitrust claim for patent hold-up in a standard-setting context, the FTC or private plaintiff must prove that the SSO would not have adopted the patentee's technology absent the patentee's deceptive conduct—so there must be evidence of one or more viable substitutes. Proving that the SSO might have been able to negotiate a lower price for the technology is not enough. Also, any claim based on deception must as a preliminary matter show conduct that violated clearly-articulated or understood rules of the SSO.

Going forward, SSOs need to review their rules to state clearly what disclosure is required from participants, and to consider requiring RAND (or more specific licensing) commitments early in the technology evaluation process in order to avoid being locked-in to a technology that may come with unfavorable license terms. Many standard setting organizations have been reluctant to impose firm rules in these areas because of the concern that they might be subject to challenge as a form of horizontal conspiracy among competitors. While there is still risk in that area, the enforcement agencies are increasingly sympathetic to the competitive benefits of clearer rules regarding disclosure and even maximum royalty levels for technology included in a standard.

Similarly, companies participating in standard setting organizations need to review those rules to be sure they understand what commitments they are making by participating, and closely monitor the development of any proposed standard in order to maintain the ability to opt-out—or even drop out—if appropriate to preserve IP rights.

If you have questions about this Alert, please contact Mark Ostrau *or* Tyler Baker*, the co-chairs of our Antitrust Practice Group.*