

## The Federal Trade Commission's (FTC) Recommendations to the International Trade Commission (ITC): Unsound, Unmeasured, and Unauthoritative<sup>1</sup>

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### I. Introduction

In March 2011, the FTC issued a Report entitled "The Evolving IP Marketplace: Aligning Patent Notice and Remedies with Competition" (Report).<sup>3</sup> In it, the FTC recommends that the ITC adopt the view that "only those licensing activities that promote technology transfer 'exploit' patented technology within the meaning of Section 337, and therefore satisfy the domestic industry requirement."<sup>4</sup> Also, the FTC recommends that the ITC "incorporate concerns about patent hold-up, especially of standards, into the decision of whether to grant an exclusion order in accordance with the public interest elements of Section 337."<sup>5</sup>

The recommendations appear to be outcome-driven, as they overlook legal and policy-based factors that counsel against implementation of the recommendations. As such, the ITC should decline to adopt the FTC's "recommendations," and instead should continue to follow the path it has carefully and deliberately taken in

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<sup>3</sup> The Report is available at <http://www.ftc.gov/os/2011/03/110307patentreport.pdf>.

<sup>4</sup> Report at 30; *see also id.* at 243. The reference to "Section 337" is shorthand for 19 U.S.C. § 1337, which is the ITC's enabling statute for the proceedings it conducts to determine infringement of intellectual property and other unfair competition-based violations. Satisfaction of the "domestic industry" requirement is one of the prerequisites for a holder of IP rights to obtain a remedy, in the form of an exclusion order, from the ITC. 19 U.S.C. § 1337(a)(2) and (3). Particularly relevant here is 19 U.S.C. § 1337(a)(3)(C), which provides, among other things, that a patentee may satisfy the domestic industry requirement by demonstrating a substantial investment in the "exploitation," including licensing, of the patent. 19 U.S.C. § 1337 (a)(3)(C).

<sup>5</sup> Report at 30; *see also id.* at 243.

interpreting and implementing Section 337 — the statute that enables its core adjudicative function.

## II. The FTC's Recommendations Are Contrary to Controlling Authority And Will Stifle Innovation

The FTC's first recommendation is that the ITC should construe "exploitation," as that word appears in 19 U.S.C. § 1337(a)(3)(C), to include only those licensing activities that promote technology transfer.<sup>6</sup> The FTC explains that that word "can be interpreted as encompassing *ex ante* but not *ex post* licensing because only the former seeks to 'exploit' the patent by putting it into productive use to create an industry."<sup>7</sup> The FTC also recommends that the ITC incorporate "concerns about patent hold-up" as a "public interest" factor in determining whether to grant an exclusion order.<sup>8</sup> There are several reasons that these recommendations are faulty.

As to its first recommendation, the FTC's interpretation of the statute is inconsistent with the plain language, with the legislative history, and with the ITC's interpretation. The statute contains no limitation on the types of licensing activities that may constitute "exploitation."<sup>9</sup> The legislative history also suggests no limitation on the types of covered licensing activities.<sup>10</sup> Indeed, not only does the legislative history suggest that the FTC's interpretation is incorrect, it also suggests that the FTC has overlooked the *quid pro quo* that lies at the heart of the U.S. patent system.<sup>11</sup> In this regard, the FTC's second recommendation (i.e., that "patent hold-

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<sup>6</sup> Report at 30; *see also id.* at 243. The FTC actually made dozens of recommendations, including recommendations to the executive, legislative, and judicial branches of government. *See, e.g.*, Report at 11-30 (making recommendations to the U.S. Patent & Trademark Office, Congress, and the federal Courts); *see also id.* at 243 n.133 (advocating increased use of the Presidential veto of the ITC's remedy determinations). This paper focuses on the two recommendations made to the ITC, which is a quasi-judicial, independent federal agency.

<sup>7</sup> Report at 242.

<sup>8</sup> Report at 30; *see also id.* at 243.

<sup>9</sup> A domestic industry shall exist if there is "substantial investment in its exploitation, including engineering, research and development, or licensing." 19 U.S.C. § 1337(a)(3)(C).

<sup>10</sup> S. Rep. 100-71 at 130 (1987) ("The Committee *does intend* this language, however, to protect from infringement those holders of U.S. intellectual property rights who are engaged in activities *genuinely designed to exploit* their intellectual property within a reasonable period of time.") (emphases added).

<sup>11</sup> S. Rep. 100-71 at 128 ("The owner of intellectual property has been granted a temporary statutory right to exclude others from making, using or selling the protected property. The purpose of such temporary protection, which is provided for in Article I, Section 8, Clause 8 of the United States Constitution, is 'to promote the Progress of Science and Useful Arts, by securing for limited Times to Authors and Inventors the exclusive Rights to their respective Writings and Discoveries.' In return for temporary protection, the owner agrees to make public the intellectual property in question. This trade-off creates a public interest in the enforcement of protected intellectual property rights. *Any* sale in the United States of a

up” should be viewed as a public interest factor) also would not be consistent with the legislative history’s consideration of the public interest.<sup>12</sup>

The ITC, however — consistent with both the plain language of the statute and with the legislative history — has explicitly interpreted its enabling statute to cover licensing activities “that ‘take advantage of’ the patent, i.e., solely derive revenue.”<sup>13</sup> The ITC, therefore, has concluded that “in assessing whether the domestic industry requirement has been met, [it] will also consider licensing activities for which the sole purpose is to derive revenue from existing production.”<sup>14</sup>

The FTC offers only one legal, non-policy-based, justification for its first recommendation, and none for its second. In a footnote, the FTC simply suggests that the ITC rely on only one of the two dictionary definitions for the word “exploit” and presumably just ignore the other.<sup>15</sup> Such outcome-oriented results are telling of the infirmity of the FTC’s recommendations.

Similarly, the policy-based rationales are unconvincing as they do not take into account that “the balance of trade related to IP licensing is one of the top two ways that we make money in the United States of America.”<sup>16</sup> Nor do the recommendations properly consider the problem of “patent holdout.” This describes the situation in which a certain percentage of the market is licensing a patentee’s innovations but the remaining percentage chooses not to pay for a license despite using those innovations; this leads to unfair price undercutting and market distortions.<sup>17</sup> To the extent the FTC targets its recommendations to those entities that purchase patents in order to license them, the FTC apparently forgets that for every patent buyer there is a patent seller, and money received by a patent seller is often invested in additional inventive activities.<sup>18</sup>

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product covered by an intellectual property right is a sale that rightfully belongs only to the holder or licensee of that property.”) (emphasis added).

<sup>12</sup> S. Rep. 100-71 at 128-29 (“The importation of *any infringing merchandise* derogates from the statutory right, diminishes the value of the intellectual property, and thus indirectly harms the public interest.”) (emphases added); see also note 11 *supra*.

<sup>13</sup> *Certain Coaxial Cable Connectors and Components Thereof and Products Containing Same*, Inv. No. 337-TA-650, slip op. at 49-50 (Int’l Trade Comm’n April 14, 2010).

<sup>14</sup> *Coaxial Cable Connectors*, slip op. at 50.

<sup>15</sup> Report at 242 n.129 (“However, the availability of multiple dictionary definitions for the statutory term ‘exploit’ could equally well support the reasonableness . . . of [the FTC’s] interpretation”).

<sup>16</sup> Statement of Bernard J. Cassidy during Panel 2 of the May 26, 2010, FTC workshop (Workshop), Transcript at 125-26 (available at <http://www.ftc.gov/bc/workshops/ipmarketplace/may26/transcript.pdf>); see also *id.* at 128 (licensing “is the way that Americans are making money in the global economy”).

<sup>17</sup> See Cassidy, Workshop, Tr. at 131-33.

<sup>18</sup> See Colleen Chien, Workshop, Tr. at 162.

The FTC recognizes that implementation of its recommendations “will limit access to the ITC of those patent owners most likely to be denied an injunction under the *eBay* analysis.”<sup>19</sup> Curiously, the FTC makes its recommendations despite acknowledging that: (i) the Federal Circuit has ruled that *eBay* does not apply to the ITC’s remedy determinations under Section 337, and that (ii) the ITC’s remedy determinations are not governed by equitable principles (as in *eBay*), but instead are governed by a statute that dictates that the ITC “shall” enter exclusion orders.<sup>20</sup>

### III. Conclusion

The patent system was deemed so important by our Founding Fathers that it is enshrined in our Constitution.<sup>21</sup> Indeed, our founders noted that “the public good fully coincides” with a patent’s grant of exclusivity.<sup>22</sup> Although Section 337 is a trade statute, it affords *all* patent owners relief, as Congress has observed, provided those patent owners satisfy certain statutory requirements.<sup>23</sup>

The only right conferred by a U.S. Patent is the right to exclude.<sup>24</sup> The Report advocates what is essentially a two-tiered class of patentees: those patentees who are entitled to attempt to satisfy the requirements of Section 337 and those who are not. The Report offers no legitimate basis to impose a sliding scale of patent rights

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<sup>19</sup> Report at 242. The reference to *eBay* is to the Supreme Court’s decision in *eBay, Inc. v. MercExchange, LLC*, 547 U.S. 388 (2006), in which the Court ruled that the traditional equitable test for injunctive relief must be satisfied before a federal District Court can issue a permanent injunction for patent infringement.

<sup>20</sup> Report at 240 & nn.117 and 118. As if the statute and the decision of the Federal Circuit were not enough, these points were reiterated to the FTC by an audience member, an attorney from the ITC’s Office of General Counsel, during the question and answer session following the Panel 2 Workshop. See Sid Rosenzweig, Workshop, Tr. at 179 (“We don’t live in a world where the Commission’s goal from Congress is only to exclude knock off goods against foreigners . . . . And if we attempted to restrict our jurisdiction to that, we would get shot down as a matter of statutory interpretation. We would also probably be found to violate our treaty obligations. And then secondly is, the statute is replete with the word ‘shall’: . . . the Commission shall exclude goods that infringe.”). It is worth further noting that although an ITC economist was on Panel 2, no attorney from the ITC was on that panel which, ostensibly, was devoted to examining the ITC’s enabling statute. For these reasons as well, the soundness and authority of the FTC’s recommendations are called into question.

<sup>21</sup> U.S. Const., Article I, Section 8, Clause 8.

<sup>22</sup> Federalist No. 43 (“The utility of this power [to promote the progress of science and the useful arts by securing, for a limited time, to authors and inventors, the exclusive right to their respective writings and discoveries] will scarcely be questioned. . . . The right to useful inventions seems with equal reason to belong to the inventors. The public good fully coincides in both cases with the claims of individuals.”).

<sup>23</sup> See notes 11 and 12 *supra*.

<sup>24</sup> See 35 U.S.C. § 154(a)(1).

based only on the patentee's status as a manufacturer, technology transfer entity, or on any other wholly-arbitrary basis.