***Refusals to License Intellectual Property under Section 2 of the Sherman Act*[+]**

Michael A. Carrier[*]

The antitrust and intellectual property (IP) laws often conflict. The foundation of IP is the right to exclude. The centerpiece of antitrust is competition. Since exclusion-based activity often restricts competition, courts face a conundrum.

The provision of the U.S. antitrust laws that targets monopolies, Section 2 of the Sherman Act, exposes this tension most dramatically.[1] A company could violate Section 2 merely by excluding others from its patented or copyrighted products. In contrast, Section 1 of the Sherman Act, for example, applies to agreements, in which the objectionable conduct relates to actions other than pure exclusion.

While courts have analyzed several types of activity under Section 2, it is the refusal to license that presents the most vexing issues. The courts have promulgated a number of inconsistent tests in determining whether IP refusals to license constitute monopolization. They have granted absolute immunity to the patentee, applied various rebuttable presumptions, and examined whether an "essential facility" was denied. Throughout this disarray, the Supreme Court has stayed on the sidelines.

In this presentation, I focus on five cases demonstrating the U.S. courts' approaches to monopolists' refusals to license IP. The tests offer analyses based on (1) absolute immunity, (2) near-absolute immunity, (3) presumptive legality, (4) presumptive legality with an intent-based rebuttal, and (5) essential facilities.

---

[*] Associate Professor, Rutgers University School of Law – Camden.
[1] Section 2 punishes "[e]very person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States . . . ." 15 U.S.C. § 2.

1.Absolute immunity: *SCM*

The first approach is presented by *SCM Corp. v. Xerox Corp.*[2] In this case, Xerox acquired a patent on a process for copying documents that allowed images to be reproduced on plain paper.[3] It refused to grant a license to a competitor, SCM, that wished to manufacture its own plain-paper copier.[4] SCM sued, claiming that Xerox's acquisition of patents and subsequent refusal to license the patents constituted monopolization.[5]

The Second Circuit began by explaining that the patent and antitrust laws "necessarily clash" when "the patented product is so successful that it evolves into its own economic market . . . or succeeds in engulfing a large section of a preexisting product market."[6] A patentee, however, that merely exercises its right to exclude by unilaterally refusing to license the patent undertakes activity that is "expressly permitted by the patent laws."[7] Moreover, it "would seriously threaten the integrity of the patent system" if a patentee were to be punished with treble damages "based on what a reviewing court might later consider, with the benefit of hindsight, to be too much success."[8] The court concluded: "[W]here a patent has been lawfully acquired, subsequent conduct permissible under the patent laws cannot trigger any liability under the antitrust laws."[9] Because the court found that Xerox had lawfully acquired the patents, its refusal to license was permissible.[10] Other courts have similarly provided absolute immunity to the patentee under Section 2 of the Sherman Act, reasoning that the patentee is merely exercising its rights under the patent laws.[11]

[2] 645 F.2d 1195 (2d Cir. 1981).
[3] *Id.* at 1197.
[4] *Id.* at 1200.
[5] *Id.* at 1197.
[6] *Id.* at 1203.
[7] *Id.* at 1204.
[8] *Id.* at 1206.
[9] *Id*.
[10] *Id.* at 1209.
[11] *See, e.g.*, Miller Insituform, Inc. v. Insituform of N. Am., Inc., 830 F.2d 606, 609 (6th Cir. 1987) ("[A] patentholder who lawfully acquires a patent cannot be held liable under Section 2 of the Sherman Act for maintaining the monopoly power he lawfully acquired by refusing to license the patent to others."); *In re* Indep.

2.Near-absolute immunity: *Xerox*

The Federal Circuit's decision in *In re Independent Service Organizations Antitrust Litigation* ("*Xerox*")[12] provides another example of an approach offering substantial deference to patentees. Xerox manufactured, sold, and serviced high-volume photocopiers.[13] It instituted a policy of not selling parts for one (and later, all) of its lines of copiers to independent service organizations (ISOs) unless they also were end-users of the copiers.[14] At one point, Xerox cut off certain ISOs' abilities to directly purchase such restricted parts.[15] A class of ISOs filed an antitrust lawsuit, and Xerox settled the suit by agreeing to suspend its parts policy and licensing its diagnostic software for a period of time.[16] One ISO opted out of the settlement and filed suit, alleging that Xerox violated the antitrust laws by setting the prices on its patented parts higher for ISOs than for end-users in an attempt to force ISOs to raise their prices.[17] Such conduct ostensibly was designed to eliminate ISOs as competitors in service markets for Xerox copiers.

Serv. Orgs. Antitrust Litig., 989 F. Supp. 1131, 1135 (D. Kan. 1997) (holding that there can be no unlawful leveraging of monopoly power when a patentholder exercises its patent rights); Tricom, Inc. v. Elec. Data Sys. Corp., 902 F. Supp. 741, 743 (E.D. Mich. 1995) ("Under patent and copyright law, [the patentholder] may not be compelled to license its proprietary software to anyone."); Bell Atl. Bus. Sys. Servs., Inc. v. Hitachi Data Sys. Corp., No. C93-20079 JW, 1995 WL 798935, at *7 (N.D. Cal. Mar. 10, 1995) ("[I]t is not a violation of antitrust law . . . to refuse to sell, license or commercially transfer copyrighted information to anyone . . . even if customers are put in the position of only getting the benefit of the copyrighted items if they hire [the copyright owners]."); Advanced Computer Servs., Inc. v. MAI Sys. Corp., 845 F. Supp. 356, 370 n.17 (E.D. Va. 1994) (deciding that protecting a copyright is a valid business justification for limiting a license).

[12] 203 F.3d 1322 (Fed. Cir. 2000).

[13] *Id.* at 1324.

[14] *Id.*

[15] *Id.*

[16] *Id.*

[17] *Id.*; *see also* 989 F. Supp. 1131, 1133 (D. Kan. 1997) (setting forth the factual history concerning Xerox's efforts to "use price as a weapon to defeat ISO competition in the service market").

The Federal Circuit held that Xerox did not violate Section 2.[18] The court emphasized the centrality of the right to exclude in the patent system before carving out three limited categories in which a patentholder would not be immune from antitrust liability: (1) tying patented and unpatented products, (2) obtaining a patent through knowing and willful fraud, and (3) engaging in sham litigation.[19] The Federal Circuit also refused to examine the patentee's subjective intent in refusing to deal with a competitor.[20] And it confirmed that action "within the scope" of the patent grant could not violate the antitrust laws.[21] Because the court concluded that Xerox's refusal to sell its patented parts did not exceed the scope of the patent grant and did not fall within any of the three exceptions, it concluded that Xerox did not violate the antitrust laws.[22]

3.Presumptive Legality: *Data General*

Several cases have applied a rebuttable presumption that a refusal to license IP does not violate Section 2 of the Sherman Act. The first case to offer such a presumption was *Data General v. Grumman Systems Support Corp.*[23] In that case, Data General created a sophisticated computer program that diagnosed problems in its computers.[24] Data General occupied approximately 90 percent of the "aftermarket" for the service of its computers; Grumman had approximately 3 percent.[25] Data General had initially pursued liberal policies that allowed third

---

[18] As a result of the Supreme Court's holding in *Eastman Kodak Co. v. Image Technical Services, Inc.* ("*Kodak I*"), 504 U.S. 451 (1992), that one brand of a product could constitute an antitrust market and that a manufacturer in a competitive "primary" market thus could have monopoly power in the "secondary" market of the servicing or parts of its own equipment, many manufacturers of durable products requiring service or parts – such as Xerox – could be treated as monopolists. *Id.* at 481-82.

[19] *Id.* at 1326. "Fraud" is to be determined by reference to the case of *Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp.*, 382 U.S. 172 (1965). To prove the "sham" exception, a plaintiff must demonstrate that the suit is objectively baseless and "motivated by a desire to impose collateral, anticompetitive injury rather than to obtain a justifiable legal remedy." 203 F.3d at 1326 (citation omitted). The court borrowed its exceptions to immunity from patent infringement lawsuits even though the exceptions are largely irrelevant for refusals to license.

[20] 203 F.3d at 1327.

[21] *Id.*

[22] *Id.* at 1326-28. The court also adopted an approach immunizing copyright-based action as long as the copyrights were obtained lawfully and not used to gain monopoly power beyond the copyright grant. *Id.* at 1329.

[23] 36 F.3d 1147 (1st Cir. 1994).

[24] *Id.* at 1152.

[25] *Id.* Data General had approximately 5 percent of the primary market for mini-computers. *Id.*

parties to use the diagnostic software.[26] But it subsequently altered these policies, restricting the licensing of the software to its own technicians and equipment owners who performed their own service.[27] As a result, Grumman was not able to use the software. Data General sued Grumman for copyright infringement and trade secret misappropriation, and Grumman filed an antitrust counterclaim challenging Data General's refusal to license the diagnostic software.[28]

The First Circuit began by exploring the purposes of the antitrust and IP laws and the history of courts' treatment of the intersection.[29] It then articulated the legislative assumption underlying the copyright laws that the right to exclude "creates a system of incentives that promotes consumer welfare . . . by encouraging investment in the creation of desirable artistic [] works of expression."[30] Antitrust defendants, according to the court, cannot be required "to prove and reprove the merits of [the] legislative assumption in every case where a refusal to license a copyrighted work comes under attack."[31]

The court therefore concluded that a party's "desire to exclude others from [use of] its [protected] work is a presumptively valid business justification."[32] But it never explained precisely how the presumption could be rebutted, stating only that "there may be rare cases in which imposing antitrust liability is unlikely to frustrate the objectives of the Copyright Act."[33] In this case, Data General's exercise of its right to exclude "is a presumptively valid business justification" which Grumman could not rebut.[34]

---

[26] *Id.* at 1154.
[27] *Id.*
[28] *Id.* at 1155-56. Grumman also challenged as a "tying arrangement" Data General's requirement that consumers wishing to utilize the software also purchase support services from the company.
[29] *Id.* at 1186.
[30] *Id.* at 1186-87.
[31] *Id.* at 1187.
[32] *Id.*
[33] *Id.* at 1187 n.64. For a recent example of a court following *Data General*, see *Telecom Tech. Servs. Inc. v. Rolm*, 388 F.3d 820, 826-27 (11th Cir. 2004) (finding no harm to consumers from refusal to sell repair parts).
[34] 36 F.3d at 1187-88.

4. Presumptive Legality with Intent-Based Rebuttal: *Kodak II*

One way in which the presumption could be rebutted is based on the defendant's intent. Such an approach was famously applied by the Ninth Circuit in *Image Technical Services, Inc. v. Eastman Kodak Co.* ("*Kodak II*"),[35] another case in which ISOs sued the manufacturer of a durable product.

Kodak manufactured high volume photocopiers. The market for such copiers was competitive, and it included Xerox, IBM, and Canon.[36] Kodak also sold and installed replacement parts for its equipment; in this activity, Kodak competed with ISOs.[37] Kodak repaired at least eighty percent of the machines it manufactured.[38] Although the company had, at one time, sold parts for repair service to ISOs, it began to restrict this practice as competition from the ISOs increased.[39] As a result of the limited access, ISOs lacked a reliable supply of parts, and thus were not able to compete with Kodak in providing multi-year service contracts.[40] Several ISOs claimed that the parts shortage forced them out of business.[41]

The ISOs sued Kodak, claiming that its restrictive parts policy violated Sections 1 and 2 of the Sherman Act.[42] The district court granted summary judgment for Kodak,[43] but the Ninth Circuit reversed.[44] The Supreme Court affirmed the reversal,[45] and, on remand from the Supreme Court, a jury entered a verdict against Kodak.[46]

---

[35] 125 F.3d 1195 (9th Cir. 1997).
[36] *Id.* at 1200.
[37] *Id.*
[38] *Id.* at 1200-01.
[39] *Id.* at 1201.
[40] *Id.*
[41] *Id.*
[42] No. C-87-1686-WWS, 1988 U.S. Dist. LEXIS 17218 (N.D. Cal. Apr. 18, 1988).
[43] *Id.*
[44] 903 F.2d 612 (9th Cir. 1990).
[45] 504 U.S. 451 (1992).
[46] No. C-87-1686-AWT, 1996 U.S. Dist. LEXIS 2386, at *2 (N.D. Cal. Feb 28, 1996).

The Ninth Circuit affirmed the verdict.[47] To ensure that the jury would account for the "procompetitive effects and statutory rights extended by the intellectual property laws," the court adopted the *Data General* presumption that a party's "desire to exclude others from [use of] its [protected] work is a presumptively valid business justification."[48] But the Ninth Circuit held that the presumption could be rebutted by evidence of pretext.[49] The court explained: "Neither the aims of intellectual property law, nor the antitrust laws justify allowing a monopolist to rely upon a pretextual business justification to mask anticompetitive conduct."[50]

In applying its rebuttable presumption, the court found that "the proffered business justification played no part in the [defendant's] decision to act."[51] The court explained that "Kodak photocopy and micrographics equipment requires thousands of parts, of which only [sixty-five] were patented" and that Kodak's parts manager testified that patents "did not cross [his] mind" when the company instituted its parts policy.[52] As a result, the court concluded that "it is more probable than not that the jury would have found Kodak's presumptively valid business justification rebutted on the grounds of pretext."[53] Even though the district court's instructions to the jury "fail[ed] to give any weight" to Kodak's IP rights, the court concluded that such error was harmless.[54]

5.Essential Facility: *Intel*

The district court in *Intergraph Corp. v. Intel Corp.*[55] demonstrated the final approach, one relying on the "essential facilities" doctrine.

[47] 125 F.3d 1195 (9th Cir. 1997).
[48] *Id.* at 1218.
[49] *Id.* at 1219.
[50] *Id.*
[51] *Id.*
[52] *Id.*
[53] *Id.* at 1219-20.
[54] *Id.* at 1218.
[55] 3 F. Supp. 2d 1255 (N.D. Ala. 1998), *vacated*, 195 F.3d 1346, 1357-58 (Fed. Cir. 1999).

Intel is the world's largest designer, manufacturer, and supplier of high-performance computer microprocessors, which are often described as the "brains" of a computer that control the central processing of data.[56] Intergraph used Intel microprocessors in the computer workstations that it developed and sold.[57] At one time, Intergraph manufactured microprocessors, but it then ceased production, converting its products to incorporate Intel's microprocessors.[58] It made this transition based on Intel's assurances that its central processing units (CPUs) could support Intergraph's workstations and that it would supply its CPUs to Intergraph on fair terms.[59] But when Intel developed its Pentium II microprocessors, it shifted away from the "open architecture" that it had made available to all participants in the industry and embraced a proprietary architecture.[60] As a result of this change, computers manufactured by original equipment manufacturers (OEMs) had to meet the technical requirements of the Intel architecture in order to use Intel microprocessors.[61] After this development, an unrelated patent dispute between the parties arose; as a result, Intergraph filed patent infringement claims against OEM customers of Intel. Intel responded by refusing to provide to Intergraph confidential information necessary for product development that it had previously provided.[62] Intergraph thus was not able to receive advance samples of Intel microprocessors and could not deploy its products at the same time that competitors could.[63]

The court first found that Intel had a monopoly in markets for CPUs and in markets for Intel CPUs.[64] It then treated Intel's refusal to deal as the denial of an essential facility.[65] The

[56] *Id.* at 1259.
[57] *Id.* at 1263.
[58] *Id.* at 1264.
[59] *Id.*
[60] *Id.* at 1262.
[61] *Id.*
[62] *Id.* at 1267.
[63] *Id.* at 1269.
[64] *Id.* at 1275-76.
[65] *Id.* at 1278.

essential facilities doctrine provides that a monopolist cannot deny to its competitors facilities that are necessary to compete in a particular market.[66] A plaintiff relying on the theory must show (1) control of the essential facility by the monopolist, (2) an inability to duplicate the facility, (3) the denial of the use of the facility, and (4) the feasibility of providing the facility.[67]

The court found that "[r]easonable and timely access to critical business information that is necessary to compete is an essential facility."[68] It then elevated the protection of competitors to a critical objective of the antitrust laws: "[A] monopolist's unilateral refusal to deal violates [Section] 2 of the Sherman Act where such conduct unreasonably handicaps competitors or harms competition."[69] The court concluded that Intel withheld an essential facility: "Intel's refusal to supply advanced CPUs and essential technical information to Intergraph likely[70] violates [Section] 2 of the Sherman Act, because they are not available from alternative sources and cannot be feasibly duplicated, and because competitors cannot effectively compete in the relevant markets without access to them."[71] Even though the *Intel* district court decision was vacated by the Federal Circuit on the ground that Intel and Intergraph were not competitors in any relevant market,[72] the approach (which has garnered attention in recent years) counsels considerable caution, as it could apply in any market in which a monopolist relies on intellectual

---

[66] *See, e.g.*, Otter Tail Power Co. v. United States, 410 U.S. 366, 377 (1973) (holding that an electric utility company could not prevent towns from using its transmission system after its retail electric power distribution franchise expired).
[67] *See, e.g.*, MCI Communications Corp. v. AT&T, 708 F.2d 1081, 1132-33 (7th Cir. 1982) (summarizing the four prongs of the essential facilities doctrine necessary to establish liability).
[68] 3 F. Supp. 2d at 1278.
[69] *Id.*
[70] The court did not definitively find a substantive violation because it considered the issue in the context of a motion for a preliminary injunction. *Id.* at 1258.
[71] *Id.* at 1278. The court also concluded that Intel "ha[d] no legitimate business reason to refuse to deal with Intergraph" since it had been a "loyal and beneficial customer" and the dispute over Intergraph's patent claims "could [have been] resolved separately without Intel denying Intergraph information it need[ed]." *Id.* In addition, the court dismissed any defense based on intellectual property, finding that Intel "has no legitimate intellectual property basis with which it can refuse to supply Intel microprocessors and technical information to Intergraph." *Id.* at 1279.
[72] 195 F.3d 1346, 1357-58 (Fed. Cir. 1999); *see also id.* at 1358 ("The district court erred in holding that Intel's superior microprocessor product and Intergraph's dependency thereon converted Intel's special customer benefits into an 'essential facility' under the Sherman Act.").

property, with an excluded party claiming that the property is "essential" to compete in the market.[73]

*　　　*　　　*

In conclusion, the conflict between the exclusion at the heart of IP and the competition at the heart of antitrust is most apparent in the context of IP refusals to license. The array of disparate approaches presented in the *CSU*, *Xerox*, *Data General*, *Kodak II*, and *Intel* cases confirms the difficulty of this issue.

---

[73] For additional criticism of this doctrine, see, *e.g.*, Phillip Areeda, *Essential Facilities: An Epithet in Need of Limiting Principles*, 58 ANTITRUST L.J. 841 (1990). For another application of the doctrine to IP, see Aldridge v. Microsoft Corp., 995 F. Supp. 728 (S.D. Tex. 1998) (rejecting claim by seller of disk caching program that Microsoft denied essential facility by including disk caching function in operating system).