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**Joshua D. Wright,
George Mason University School of Law**

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Why the Supreme Court Was Correct to Deny Certiorari in *FTC v. Rambus*

Joshua D. Wright[♦]

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Abstract

In November 2008, the Federal Trade Commission petitioned the Supreme Court to review the D.C. Circuit's decision in *FTC v. Rambus*. That decision reversed the Commission's finding that Rambus knowingly failed to disclose a patent to a standard setting organization and, in so doing, acquired monopoly power in violation of Section 2 of the Sherman Act. In February 2009, the Supreme Court denied the Commission's petition. This article examines some deficiencies in the Commission's arguments, concluding ultimately that the Supreme Court was correct to deny review. Moreover, the article suggests that the patent holdup problem, and ex post opportunism generally, is more effectively handled by contract and patent law. Because parties cannot contract around heavy mandatory antitrust remedies, contract and patent law offer superior substantive doctrine designed to distinguish good faith contractual modifications from bad faith holdup, thereby minimizing the social welfare reducing decision errors.

[♦] Visiting Professor, University of Texas School of Law; Assistant Professor, George Mason University School of Law (on leave). I thank Bruce Kobayashi for valuable discussions on this topic and Jan Rybnicek for excellent research assistance. Email: jwrightg@gmu.edu.

In November 2008, the Federal Trade Commission petitioned the Supreme Court to review the D.C. Circuit's decision in *FTC v. Rambus*.¹ That decision reversed the Commission's finding that Rambus, a memory chip developer, knowingly failed to disclose a patent to a standard setting organization (SSO) and, in so doing, acquired monopoly power in violation of Section 2 of the Sherman Act. In its petition, the Commission asks the Court to resolve two questions: (1) what level of causation must be shown to prove a deceptive act contributed to the acquisition of monopoly power, and (2) whether a deceptive act that allows a party to avoid an otherwise inevitable pricing constraint constitutes an antitrust violation. In February 2009, the Court issued an order declining to hear the Commission's appeal. This article examines some deficiencies in the Commission's arguments in support of review, concluding that the Supreme Court was correct to deny the petition.

The Commission offers five distinct reasons in support of the Court granting its petition. First, the Commission argues that the D.C. Circuit applied a restrictive causation standard that unduly required a showing that Rambus's conduct was anticompetitive. Second, the Commission contends that the D.C. Circuit misapplied relevant precedent to conclude that the loss of an opportunity to obtain a RAND commitment by the SSO was not an anticompetitive effect. Third, the Commission argues that current requirements for causation under Section 2 are unclear and in need

¹ 522 F.3d 456 (D.C. Cir. 2008), *cert. denied*, No. 08-694, 2009 WL 425102, at *1 (Feb. 23, 2009).

of further guidance from the Court. Fourth, the Commission points to what it believes is a split between the Third and D.C. Circuits on the question of whether deception is a proper basis for liability under Section 2. Fifth, and finally, the Commission suggests that inconsistent application of antitrust laws in the context of SSO agreements has the potential to create confusion that will lead to decreased participation and ultimately consumer harm.²

In this article, I evaluate the Commission's case in support of Supreme Court review, concluding that it is ultimately unpersuasive. Moreover, the article suggests that the patent holdup problems, and ex post opportunism generally, is more effectively handled by contract and patent law. Because parties cannot contract around heavy mandatory antitrust remedies, contract and patent law offer superior substantive doctrine designed to distinguish good faith contractual modifications from bad faith holdup, thereby minimizing the social welfare reducing decision errors. We begin by evaluating the centerpiece of the Commission's case in favor of certiorari.

I. A Defense of the D.C. Circuit's Causation Standard

The Commission argues that the D.C. Circuit imprudently adopted an overly stringent "but-for" causation standard. According to the Commission, the D.C. Circuit incorrectly required the Commission to demonstrate that the SSO (JEDEC) would have selected an alternative non-proprietary standard but-for Rambus's deceptive acts. In its

² Petition for Writ of Certiorari, *FTC v. Rambus*, No. 08-694 (Nov. 24, 2008).

earlier decision, the Commission concluded that in the absence of Rambus's deceptive conduct two mutually exclusive scenarios were possible: (1) JEDEC would have selected alternative non-proprietary technologies, or (2) JEDEC would have still selected Rambus but secured a RAND commitment ("Rambus with RAND"). In other words, there are two possible causal paths linking Rambus's conduct to an anticompetitive effect and a violation of Section 2. Importantly, the Commission contends that Rambus's conduct under either causal path constitutes a violation of Section 2.

While the D.C. Circuit and the Commission disagree over the appropriate standard of causation to apply in the patent holdup context, they appear to agree on two important propositions. First, both agree that deception that significantly contributes to the acquisition of market power can constitute actionable conduct under Section 2. Second, both agree that price-increasing deception by a firm already possessing lawfully acquired monopoly power is not actionable under Section 2 under *NYNEX v. Discon*.³ The timing of Rambus's acquisition of market power thus becomes significant. Did Rambus's market power come before or after the allegedly actionable deceptive conduct? We'll return to this issue shortly.

First, note that if Rambus acquired its monopoly power prior to its deceptive and price-increasing conduct then *NYNEX* does apply. And if *NYNEX* applies, it follows

³ 525 U.S. 128 (1998).

that the “Rambus with RAND” causal path (the one where Rambus’s deception did not result in inclusion in the standard but only the loss of a RAND commitment) does not constitute a violation of Section 2. Thus, it becomes clear that the Commission had the burden, in order to establish a violation of Section 2, of demonstrating that Rambus did not have market power prior to its deceptive conduct. There is no dispute that it is actually the Commission’s burden to establish as much. The critical antitrust question becomes specifying the precise burden the Commission should bear in establishing that Rambus’s deceptive conduct traveled a potentially illegal path that is non-*NYNEX* protected. While the *NYNEX* question and the causation question appear to be two separate inquiries, they are inextricably intertwined. Many commentators seem to have simply assumed that *NYNEX* does not apply because the Commission alleged that deception caused Rambus’s inclusion in JEDEC. While these allegations, if proven, would indeed render *NYNEX* inapplicable, it does not follow that *NYNEX* would not immunize Rambus’s conduct under the “Rambus with RAND” scenario.

The Commission characterizes the D.C. Circuit’s causation test as “a strict ‘but for’ causation test for Section 2 cases” that “finds no support in this Court’s prior pronouncements.”⁴ The Commission contends it should not have been required to identify a specific anticompetitive effect, but rather that both causal paths characterize anticompetitive conduct under Section 2. If one accepts that both causal paths violate

⁴Petition for Writ of Certiorari at 16-17, *Rambus*, No. 08-694 (Nov. 24, 2008).

Section 2, it appears the D.C. Circuit erred in requiring the Commission to show that one “but-for” scenario was more probable than the other because both paths involved illegal conduct. But such an analysis merely begs the question of whether *NYNEX* applies under the alleged facts.

The D.C. Circuit argued that the causal path involving deception that merely avoids the imposition of a RAND term is not *necessarily* actionable under Section 2. The court was clear that demonstrating that deception resulting in the evasion of a RAND pricing constraint violates Section 2 requires a showing that the conduct is not *NYNEX* protected. In order to perform a *NYNEX*-analysis, one must know whether the deceptive conduct came before or after the acquisition of monopoly power. Again, if *NYNEX* applies, the antitrust analysis for the course of events in which Rambus would have been selected in the absence of bad conduct, but with a RAND commitment, reveals that such conduct is simply not illegal because Rambus already maintained monopoly power.

Under this alternative view, the D.C. Circuit’s causation standard should not be controversial and appears eminently reasonable. Requiring that the Commission prove that Rambus engaged in illegal behavior rather than activity protected under *NYNEX* is not novel. The divergence of views on what conduct implicates *NYNEX* is key to understanding the differences between the Commission’s and the D.C. Circuit’s positions. Both the Commission and the D.C. Circuit accept that there must be a causal

showing that deception significantly contributes to *some* anticompetitive effect. The disagreement is over whether both possible paths actually involve anticompetitive effects. If one agrees with the Commission that both causal paths violate Section 2, a requirement that a plaintiff specify precisely which path resulted in an anticompetitive effect is unnecessary and likely unwise. However, if one believes that only one causal path constitutes a violation of Section 2, such a requirement is necessary. The resolution of the causation issue turns on whether *NYNEX* renders the “Rambus with RAND” path immune from liability. We will turn to this issue in Part II, concluding that the D.C. Circuit decision is correct and the Commission failed to meet its burden of demonstrating that the *NYNEX* conditions were not satisfied.

II. When Is Deceptive and Price-Increasing Conduct Exclusionary Under Section 2?

Whether deception can potentially constitute actionable exclusionary conduct under Section 2 depends both on when it occurs relative to the acquisition of monopoly power and whether it results in the exclusion of rivals or a mere increase in price. *NYNEX* immunizes a firm from antitrust liability if the firm (1) first lawfully acquired monopoly power and (2) then committed fraud or engaged in other deceptive conduct (3) that allowed it to evade pricing constraints to the detriment of consumers. On the other hand, *NYNEX* would not immunize a firm that (1) committed fraud and (2) thereby acquired market power (3) exercised in the form of evading a RAND commitment. Accordingly, if Rambus’s deception preceded its possession of monopoly

power, the Commission is correct in arguing that either causal path—(1) exclusion of non-proprietary technology or (2) Rambus with a RAND pricing constraint—involves an anticompetitive effect that is actionable under Section 2. However, if Rambus acquired its monopoly power prior to committing its deceptive acts *NYNEX* precludes the Commission from asserting that causal path as an actionable Section 2 violation.

How could Rambus have acquired monopoly power prior to its deceptive conduct? Consider two possible scenarios. In the first, Rambus has a strong patent and strong technology compared to rivals that it is highly likely to be selected for the standard, or at the least become the de facto standard. In the second, Rambus has a weak patent and weak technology that is unlikely to be included in a standard on the merits. Under the first scenario, Rambus's technology would have been adopted irrespective of the deceptive conduct. The obvious corollary is that the deception did not create the monopoly power. The conduct would be *NYNEX*-protected because the monopoly power preceded the deception. The second scenario is significantly different because the deception caused the acquisition of monopoly power, which precludes the application of *NYNEX*.

The two scenarios above make clear how the causation and anticompetitive effect arguments are inextricably linked. Specifically, the causation issue turns on whether or not the "Rambus with RAND" causal path is characterized as actionable under Section 2. As a result, in addition to the standard burden in Section 2 cases, *NYNEX* demands

that the Commission demonstrate, among other things, that Rambus's monopoly power did not precede the "merely" price-increasing deceptive act. The Commission did not adequately address *NYNEX* and its requirements. Instead the Commission asserted, both as a matter of fact and law, that Rambus's deception was the cause of its market power.

While the D.C. Circuit's opinion is not a model of clarity on this issue, the court's conclusions are not erroneous. The court should have laid out more explicitly the factual burden that *NYNEX* imposes on plaintiffs in patent holdup cases. Nevertheless, given the Commission's failure to establish that one of the two possible causal paths was illegal, the court correctly required that the Commission demonstrate that Rambus's conduct had indeed resulted in the exclusion of non-proprietary technologies. The critical point is that the Commission bore the burden of demonstrating that Rambus's deception caused the unlawful acquisition of monopoly power. Instead, the Commission left open the possibility of the *NYNEX*-protected scenario in which Rambus lawfully acquired monopoly power by virtue of a superior patented product, only after which it deceived the SSO and achieved higher prices. The D.C. Circuit's decision can reasonably be interpreted as articulating the contours of what *NYNEX* immunizes, and explaining that the Commission failed as a factual matter to make a convincing showing that Rambus did not lawfully acquire monopoly power prior to the deception.

III. Certiorari Was Not Necessary to Resolve Confusion Over the Causation Standard Under Section 2

The Commission also raises the concern that confusion over the correct causation standard under Section 2 warrants the Supreme Court's attention. For the reasons discussed above, the D.C. Circuit correctly required the Commission to separate the causal link between Rambus's deceptive conduct and any effects because, depending on when Rambus obtained monopoly power, the bad acts may be immunized under *NYNEX*. This causal requirement is not novel. Nor does a significant legal dispute exist over the appropriate causation standard to apply under Section 2. The causation debate is simply a factual dispute over whether the Commission demonstrated that illegal conduct occurred—hardly a matter requiring Supreme Court review.

IV. *Rambus and Broadcom*: Circuit Split, Conflict, or Neither?

The Commission also contends that a conflict exists between the D.C. Circuit's decision in *Rambus* and the Third Circuit's decision in *Broadcom v. Qualcomm*.⁵ The Commission claims that, contrary to the D.C. Circuit, the Third Circuit has concluded that deception that results in the avoidance of a RAND commitment is an anticompetitive effect under Section 2. More specifically, the Commission argues that *Broadcom* adopted the Commission's position in *Rambus* by holding that misrepresentation of license terms in the context of a standard setting process

⁵ 501 F.3d 297 (3d. Cir. 2007)

constitutes a Section 2 violation because such conduct harms competition for the standard and increases the probability the patent holder will obtain monopoly power.

According to the Commission, a conflict arises between the circuits because unlike the D.C. Circuit, the Third Circuit does not require a showing that deception actually caused an SSO to include the patent holder's technology. While the D.C. Circuit noted that *Broadcom* "may have rested on the allegation that the deceit lured the SSO away from non-proprietary technology,"⁶ the Commission criticized the court for failing to recognize that the Third Circuit disapproved of the impact of the patent holder's deception on the standard setting process itself, rather than on the SSO's ultimate decision to adopt the standard.

Even accepting the Commission's description of both decisions, *Rambus* and *Broadcom* do not amount to a circuit split. First, *Broadcom* is an appeal from a district court order granting Qualcomm's motion to dismiss. The court's decision merely holds that Broadcom's allegations are sufficient to state a claim under Section 2. Moreover, the allegations *included* facts showing Qualcomm's deception induced the SSO to select the firm's patented technologies. Unlike *Rambus*, *Broadcom* presented a set of facts that alleged Qualcomm acquired monopoly power by engaging in a course of deceptive conduct that led to the inclusion of its patent in a standard. The Third Circuit's decision thus does not speak to the issue of causation presented in *Rambus*. Moreover, to the

⁶ *Rambus*, 522 F.3d at 466.

extent that the decision is based on the court accepting as true the allegation that Qualcomm's deception induced the selection of its technologies as part of the standard, the opinion also does not address whether mere avoidance of a RAND commitment is anticompetitive under Section 2.

The Third Circuit's analysis must be stretched considerably to create a circuit split with *Rambus* on the issues of causation and applicability of *NYNEX*. Perhaps such a split will ultimately develop when and if the Third Circuit addresses these questions with facts in the record. As it stands, however, the holdings in *Rambus* and *Broadcom* are largely a function of the specific factual allegations, procedural posture, and relevant records in each, rather than an underlying and fundamental doctrinal disagreement over Section 2 that requires the Supreme Court's attention.

V. Will Consumers Be Harmed and Confused If The Supreme Court Denies Certiorari?

Finally, the Commission argues the *Rambus* and *Broadcom* decisions create a level of confusion that will deter participation in the standard setting process, ultimately harming consumers. This is unlikely because adequate remedies aside from those offered by antitrust laws already exist under state and federal law.

The debate in patent holdup cases such as *Rambus* and *Broadcom* is whether to layer antitrust remedies on top of whatever breach of contract, tort, or patent law remedies are already available to the aggrieved parties. Breach of contract remedies will be available to SSO members, but generally not to non-member third parties, when

patent holders violate by-laws that require RAND commitments or disclosure. Indeed, some have argued that damages for breach of contract are in fact superior to antitrust damages, from an optimal deterrence standpoint.⁷

First, Section 2 provides for treble damages for any violation, plus follow-on private actions in state and federal court. If determination of optimal damages turns on the probability of detection—for example, trebling is required to deter Section 2 violations because the probability of detecting bad behavior is low—it appears that damages need not be as high for patent holdup violations as for antitrust actions. This follows from the fact that holdups typically have a high probability of being detected because, by their very nature, holdups must be announced to SSO members to work. So while third parties may not be able to bring claims, SSO members certainly have the incentive to bring an action. Moreover, it may be the case that expectation damages are closer to optimal deterrence than the alternative antitrust damages.⁸ Contract law also has the advantage of providing substantive law designed to distinguish holdup from good faith modification in response to changes in market conditions. This substantive doctrinal advantage becomes much more important when one considers, as discussed

⁷ See Bruce H. Kobayashi and Joshua D. Wright, *Substantive Preemption, Federalism, and Limits on Antitrust: An Application to Patent Holdup* (forthcoming, J. COMP. L. & ECON (2009)); Luke Froeb and Bernhard Ganglmair, *An Equilibrium Analysis of Antitrust as a Solution to Patent Holdup* (working paper, 2009), available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1340722.

⁸ See Kobayashi & Wright, *supra* note 7.

below, the Commission's willingness to challenge deviations from ex ante contractual commitments even in the absence of deception.⁹

Second, the patent doctrine of equitable estoppel provides another appropriate means of relief in patent holdup cases and has already been applied in cases where the patentee engaged in deception. The inclusion of a patent in a standard without first obtaining price constraining licensing terms typically awards the patent holder supra-competitive prices. Courts have used equitable estoppel to preclude patent holders from asserting their rights to supra-competitive prices in circumstances in which the patent holder misled the SSO prior to the adoption of a standard including the patentee's technology. The equitable estoppel doctrine thus provides a remedy that effectively corrects the holdup problem by prohibiting the patent holder from asserting the rights maintain under the patent.¹⁰ In addition, the doctrine has the benefit of not extending to circumstances where the SSO does not rely on the patent holder's deception. A patent holder's duty to disclose would be assessed in light of the SSO's requirements. This approach also has the benefit of allowing SSOs to create requirements that encourage ex ante disclosure without eliminating the incentive to improve on the current standard.¹¹ Moreover, this approach would not apply to

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.*

situations in which deception is not involved—such as *N-Data*¹²—thus ensuring good faith breaches of FRAND commitments are not unnecessarily discouraged.¹³ Finally, this approach also has the benefit of not extending antitrust law to cover circumstances that lack adequate proof of competitive harm.¹⁴

While the Commission worries that participants in standard setting will not be able to defend themselves against manipulation, it is important to remember that SSOs are sophisticated organizations with a host of state and federal remedies at their disposal that do not involve the heavy hammer of antitrust law, which may deter pro-competitive innovation by encouraging opportunism by SSO members. Importantly, the Supreme Court has acknowledged that the presence of alternative remedies and regulatory options can render expansion of antitrust liability inappropriate when there is a serious potential for false positives. As a normative matter, the patent holdup is exactly this type of conduct where alternative regulatory institutions, such as state and federal laws, render the marginal benefit of antitrust small and the marginal cost high because of the social costs of false positives in this setting.¹⁵

Finally, it is not without some irony that the Commission complains about the confusion in patent holdup doctrine. The Commission's enforcement action in *N-Data* extends the patent holdup agenda to cases which do not involve deception at all.

¹² In re Negotiated Data Solutions LLC (N-Data), No. 051-0094 (F.T.C. Jan. 23, 2008).

¹³ See Kobayashi & Wright, *supra* note 7.

¹⁴ *Id.*

¹⁵ *Id.*

Indeed, the Commission wielded its Section 5 enforcement power to address the re-negotiation of a nominal \$1,000 commitment to a RAND license several years after the commitment had been made. One might argue that if anything is likely to deter participation in standard setting activities it is unpredictable enforcement actions such as *N-Data*, which threatens to extend antitrust liability to good faith modification of contractual arrangements the Commission determines to result in prices that are too high.¹⁶

The Commission's critique of the D.C. Circuit's causation standard did not fully appreciate the scope of *NYNEX* as it relates to defining the plaintiff's burden in patent holdup cases. The D.C. Circuit's causation standard quite appropriately and reasonably requires the Commission to establish that Rambus's allegedly deceptive conduct, to the extent it resulted merely in the evasion of a RAND commitment, was not *NYNEX*-protected. Interpreted as such, *Rambus* does not conflict with *Broadcom* and therefore there is no circuit split for the Supreme Court to resolve. Moreover, the adequacy of contract and patent remedies available to holdup victims and the questionable economic case for providing mandatory antitrust remedies on top of these alternatives render Supreme Court involvement unnecessary and unwise. While there is little doubt that the Commission's patent holdup enforcement agenda will continue in the years to come, the Supreme Court was correct to deny the Commission's petition.

¹⁶ *Id.*