

February 13, 2018

Assistant Attorney General Makan Delrahim
Department of Justice Antitrust Division
950 Pennsylvania Ave. NW
Washington, DC 20530-0001

Dear Assistant Attorney General Delrahim,

As judges, former judges and government officials, legal academics and economists who are experts in antitrust and intellectual property law, we write to express our support for your recent announcement that the Antitrust Division of the Department of Justice will adopt an evidence-based approach in applying antitrust law equally to both innovators who develop and implementers who use technological standards in the innovation industries.

We disagree with the letter recently submitted to you on January 24, 2018 by other parties who expressed their misgivings with your announcement of your plan to return to this sound antitrust policy. Unfortunately, their January 24 letter perpetuates the long-standing misunderstanding held by some academics, policy activists, and companies, who baldly assert that one-sided "patent holdup" is a real-world problem in the high-tech industries. This claim **rests entirely on questionable models** that predict that opportunistic behavior in patent licensing transactions will result in higher consumer prices. These predictions are inconsistent with actual market data in any high-tech industry.

It bears emphasizing that no empirical study has demonstrated that a patent-owner's request for injunctive relief after a finding of a defendant's infringement of its property rights has ever resulted either in consumer harm or in slowing down the pace of technological innovation. Given the well understood role that innovation plays in facilitating economic growth and well-being, **a heavy burden of proof** rests on those who insist on the centrality of "patent holdup" to offer some tangible support for that view, which they have ultimately failed to supply in the decade or more since that theory was first propounded. Given the contrary conclusions in economic studies of the past decade, there is no sound empirical basis for claims of a systematic problem of opportunistic "patent holdup" by owners of patents on technological standards.

Several empirical studies demonstrate that the observed pattern in high-tech industries, especially in the smartphone industry, is one of constant lower quality-adjusted prices, increased entry and competition, and higher performance standards. These robust findings all contradict the testable implications of "patent holdup" theory. The best explanation for this disconnect between the flawed "patent holdup" theory and overwhelming weight of the evidence lies in the institutional features that surround industry licensing practices. These practices include bilateral licensing negotiations, and the reputation effects in long-term standards activities. Both support a feed-back mechanism that creates a system of natural checks and balances in the setting of royalty rates. The simplistic models of "patent holdup" ignore all these moderating effects.

Of even greater concern are the likely negative social welfare consequences of prior antitrust policies implemented based upon nothing more than the purely theoretical concern about opportunistic "patent holdup" behavior by owners of patented innovations incorporated

**mpatterson
Sticky Note**

This claim apparently finds no significance in the January 24 industry letter or in the many previous statements regarding hold-up, which are detailed in responses to this letter. Perhaps those other views are incorrect, but it seems inappropriate to deny their existence.

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Sticky Note**

Nor has any empirical study demonstrated the slowing of innovation from not allowing such requests from patentees that have made FRAND commitments. Moreover, since this sentence refers only to injunctions, it says nothing about effects of FRAND patentees' demands for high royalties, making the remainder of the paragraph something of a non sequitur.

**mpatterson
Sticky Note**

The burden of proof in litigation rests on the patentee seeking royalties or an injunction. It is not clear why, even if there were not evidence of hold-up or hold-out, that the burden would be on implementers.

**mpatterson
Sticky Note**

As the response to this letter pointed out, this does not establish that industry performance could not have been better. Moreover, given the past concern about hold-up, perhaps this progress is owed to that concern. In any event, it raises just as many questions about the significant "hold-out" effects posited by AAG Delrahim.

**mpatterson
Sticky Note**

They "include" those effects, but in the context of widespread FRAND commitments and licensing, there is no evidence that these practices are the "best explanation" for industry performance.

into technological standards. For example, those policies have resulted in demands to set royalty rates for technologies incorporated into standards in the smartphone industry according to particular components in a smartphone. This was a change to **the longstanding industry practice of licensing at the end-user device level**, which recognized that fundamental technologies incorporated into the cellular standards like 2G, 3G, etc., optimize the entire wireless system and network, and not just the specific chip or component of a chip inside a device.

In support, we attach an Appendix of articles identifying the numerous substantive and methodological flaws in the “patent holdup” models. We also point to rigorous empirical studies that **all directly contradict the predictions of the “patent holdup” theory.**

For these reasons, we welcome your announcement of a much-needed return to evidence-based policy making by antitrust authorities concerning the licensing and enforcement of patented innovations that have been committed to a technological standard. This sound program ensures balanced protection of all innovators, implementers, and consumers. We are confident that consistent application of this program will lead to a vibrant, dynamic smartphone market that depends on a complex web of standard essential patents which will continue to benefit everyone throughout the world.

Sincerely,

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Richard A. Epstein
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James Parker Hall Distinguished Service Professor of Law Emeritus,
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The Honorable Douglas H. Ginsburg
Senior Circuit Judge,
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Professor of Law,
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Assistant Professor of Law
University of Nebraska College of Law

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Even with “licensing at the end-user device level,” the royalty rate can be based on the contributions of particular patents, and the rate might best be assessed by focusing on particular components. The focus on individual patent contributions is one of the *Georgia-Pacific* factors, and since that case was decided in 1970, it seems that it in fact is the “longstanding industry practice.”

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This is a dramatic assertion. Notably, a number of the authors of the cited studies did not sign this letter.

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APPENDIX

Richard A. Epstein & Kayvan Noroozi, *Why Incentives for Patent Hold Out Threaten to Dismantle FRAND and Why It Matters*, BERKELEY TECH. L. REV. (forthcoming), <https://ssrn.com/abstract=2913105>

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Anne Layne-Farrar, *Patent Holdup and Royalty Stacking Theory and Evidence: Where Do We Stand After 15 Years of History?*, OECD INTELLECTUAL PROPERTY AND STANDARD SETTING (Nov. 18, 2014), <http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/WD%282014%2984&doclanguage=en>

Alexander Galetovic & Stephen Haber, *The Fallacies of Patent Holdup Theory*, 13 J. COMP. L. & ECON., 1 (2017), <https://academic.oup.com/jcl/article/13/1/1/3060409>

Alexander Galetovic, Stephen Haber, & Lew Zaretzki, *An Estimate of the Average Cumulative Royalty Yield in the World Mobile Phone Industry: Theory, Measurement and Results* (Feb. 7, 2018), <https://hooverip2.org/working-paper/wp18005>

Alexander Galetovic, Stephen Haber, & Ross Levine, *An Empirical Examination of Patent Hold-Up* (Nat'l Bureau of Econ. Research, Working Paper No. 21090, 2015), <http://www.nber.org/papers/w21090.pdf>

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Gerard Llobet & Jorge Padilla, *The Optimal Scope of the Royalty Base in Patent Licensing*, 59 J. L. & ECON. 45 (2016), <https://ssrn.com/abstract=2417216>

Keith Mallinson, *Theories of Harm with SEP Licensing Do Not Stack Up*, IP FIN. BLOG (May 24, 2013), <http://www.ip.finance/2013/05/theories-of-harm-with-sep-licensing-do.html>

Jorge Padilla & Koren W. Wong-Ervin, *Portfolio Licensing to Makers of Downstream End-User Devices: Analyzing Refusals to License FRAND-Assured Standard-Essential Patents at the Component Level*, 62 THE ANTITRUST BULLETIN 494 (2017), <https://doi.org/10.1177/0003603X17719762>

Jonathan D. Putnam & Tim A. Williams, *The Smallest Salable Patent-Practicing Unit (SSPPU): Theory and Evidence* (Sept. 2016), <https://ssrn.com/abstract=2835617>

Gregory Sidak, *The Antitrust Division's Devaluation of Standard-Essential Patents*, 104 GEO. L.J. ONLINE 48 (2015), <https://georgetownlawjournal.org/articles/161/antitrust-division-s-devaluation-of/pdf>

Joanna Tsai & Joshua D. Wright, *Standard Setting, Intellectual Property Rights, and the Role of Antitrust in Regulating Incomplete Contracts*, 80 ANTITRUST L.J. 157 (2015), <https://ssrn.com/abstract=2467939>

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