Don’t Settle for Less?

Antitrust Risks of Settling Your Intellectual Property Lawsuit After *Actavis*

By Frederick R. Juckniess

The aspirational purposes of the antitrust laws and the competing incentives of intellectual property laws have struggled against each other for decades. The complex task of understanding whether and how intellectual property agreements may be challenged under the antitrust laws has been amplified by the Supreme Court’s *Federal Trade Commission v Actavis, Incorporated*[1] decision from June 2013, which removed strong presumptive protection of intellectual property agreements negotiated to settle litigation from antitrust scrutiny. The impact of the decision and how it fits into antitrust limitations on patent rights generally should be of considerable importance to any companies that own, license, or use patented technologies—which includes virtually everyone.

Imagine a court telling you that you cannot settle a patent claim you have brought against an alleged infringer because the settlement violates the antitrust laws; instead, you must litigate the questions of validity, construction, and infringement through judgment. The decision is based on the antitrust laws’ policy of protecting competition and market entry, in this instance by ridding the patent rolls of overbroad or invalid patents and getting noninfringing competitors into the market. Many settling parties have faced these situations when their settlement agreements have been challenged as violative of the antitrust laws.

So when does a settlement agreement become an antitrust conspiracy between competitors, restraining trade by preserving an invalid patent or preventing a competitor from entering the market? And what happens when the patent holder pays the alleged infringer not to compete or provides other consideration? The answer is complicated, and one of the few bright-line rules has been narrowed by the *Actavis* decision.

Balancing the antitrust laws with the legal monopoly of patents

Intellectual property laws share many of the same goals as the antitrust laws. Each is intended to increase innovation and incentivize beneficial competition, but intellectual property laws do so by *preventing* competition. As a result, there is a natural tension between intellectual property agreements and the antitrust laws.

Despite the unquestionable value of copyrights, trademarks, trade dress, and trade secrets, the preeminence of patents in intellectual property law is rarely challenged. It is in the patent realm where issues of agreements violating the antitrust laws arise most frequently.

United States patent law grants those who disclose their inventions to the public a lawful monopoly, and grants the patentee the right to exclude any others from competing with it. However, monopolies are costly to society and we know from more than a century of experience that they result in reduced output and higher prices. Accordingly, patent holders are limited so that they are not allowed to turn their patent rights into an unlimited pass from antitrust scrutiny.

In general, limitations on the rights of patent holders can be thought of in three categories: (1) limits on when patents are granted, (2) limits on patent agreements and licenses, and (3) limits on enforcement including settlement of litigation.

Limits on patent grants

Patents are granted only under certain limited conditions, which are intended to ensure that society gets the benefit of a useful invention in exchange for granting the monopoly. Patents should not be issued, and issued patents may be invalidated, if these conditions are not met:

- Requiring that the submitted invention is novel by comparison to prior patents and technology
- Requiring that the invention is not obvious to someone skilled in the technology
- Requiring that the invention has utility (i.e., is useful)
- Preventing patent protection if the invention was publicly disclosed, in public use, or on sale more than one year before the date on which the patent application is filed
- Requiring a sufficient disclosure in the patent that permits others to make and use the invention, so that after expiration the public can make use of the invention
- Limiting the patent monopoly to 20 years, after which the public has the right to make, use, or sell the invention

As an added limitation, patentees may be subject to an antitrust counterclaim for attempting to enforce a patent that is known not to be valid, such as when the patent was procured by fraud (e.g., by withholding relevant prior art from the patent application). An enforcement action under those conditions may violate the Sherman Act and subject the patent holder to treble damages.[2]

Limits on patent licenses and agreements

Patentees are given the right to exclude competitors from making, using, or selling their inventions. However, they also are entitled to license some or all of those rights as long as the arrangement does not violate the antitrust laws.

The starting point in analyzing licenses has long been to assume that any agreed-upon restrictions within the scope of a valid patent are exempt from the Sherman Act. This broad principle derives from a venerable but less-than-clear pronouncement of the Supreme Court in 1926 that the possession of a valid patent or patents does not give the patentee any exemption from the provisions of the Sherman Act beyond the limits of the patent monopoly.[3] Though perhaps not an ironclad endorsement of exemption from the Sherman Act for any conduct *within* the limits of the patent monopoly, this principle has long guided examination of patent license agreements.

The economics support expansive freedom in licensing. Because the licensing of a patented invention allows at least some competition where a full monopoly would otherwise exist, courts have traditionally allowed otherwise clearly anticompetitive agreements to stand when those agreements are challenged under the antitrust laws. As a result, patentees have been given broad leeway in setting the conditions on which licensees can compete in their monopoly space, including setting maximum or minimum prices,[4] limiting output, and restricting the geographic territory in which a licensee may compete.[5]

FAST FACTS

Agreements concerning patent rights, including in litigation settlements, can potentially violate the antitrust laws.

Litigation settlements within the scope of the patent (claims and terms) were presumptively safe from antitrust scrutiny. *Actavis* has cast doubt on this rule.

Payments by the patent holder to the potential infringer in exchange for an agreement concerning when and how to compete, even within the scope of the patent, may draw antitrust scrutiny.

Courts and litigants have become sophisticated in examining patent agreements to determine if they in fact increase competition as contemplated previously, or instead serve to restrict competition in ways that go beyond the rights granted in the patent. Thus, in many cases, patent holders have constructed licensing agreements that result in an unlawful restraint of competition. While any agreement that restricts commerce beyond the scope of the patent may be suspect, examples of antitrust violations arising out of patent agreements include:

- Using patent licenses to coordinate pricing in products not covered by the patent[6]
- Cross-licensing patents with the purpose of excluding a common competitor by enforcement of the patents[7]
- Using cross-licenses to coordinate and set prices for competing products[8]
- Using patent licenses to eliminate production of (and thus competition from) unpatented products[9]

It is a short journey from antitrust scrutiny of agreements to license patents to antitrust scrutiny of settlements arising out of patent litigation.

Limits on enforcement actions and settlement of patent cases

The typical economic factors favoring litigation settlements are well known and obvious: reduction of risk, certainty of result, and limiting litigation cost. When intellectual property rights are involved, the economics of settlements can be more complicated, raising competing issues important to rights holders, enforcement agencies, and consumers. For example, patent holders often face challenges to the validity or scope of their patents. Settlement allows them to preserve their patent rights and avoid a construction that narrows their lawful monopoly. Similarly, there is a strong societal and economic interest in resolution of patent disputes by settlement. As a result, despite being agreements between competitors, patent settlements have been given a wide berth and rarely run afoul of the antitrust laws.

However, settlement of a dispute may deprive society of the benefit of competition that the antitrust laws are intended to protect. There are real costs to society in allowing the settlement of a patent dispute if the result is something less than unrestrained competition, or if an otherwise invalid or overbroad patent is allowed to remain valid and enforceable.

And it is usually the case that settlement agreements are still agreements between competitors that effectively restrain competition. As a result, patent holders and defendants are not free to set any conditions they conceive of as part of a settlement agreement.

The starting point for establishing whether a resulting settlement agreement is likely to be scrutinized is determining if the agreement is within the grant of patent rights under the limitations noted previously—do any agreement terms reach beyond the claimed scope or time limitations of the patent? If so, expect examination of those terms under the antitrust laws.

Even if not, the agreement may still unreasonably restrain trade and thus violate the Sherman Act. Some of the principal ways in which settlement agreements violate the antitrust laws include:

- Settlements that include provisions prohibiting or limiting competition with products not covered by the patent[10]
- Settlements that are designed to preserve an invalid or overly broad patent, such as by depriving the United States Patent and Trademark Office of critical information or prior art[11]
- Settlements designed to allow the parties to gain power over the relevant market, typically involving the sharing of patent rights or cross-licensing[12]
- Settlements designed to restrict the parties' ability to grant future licenses to other competitors[13]
- Reverse payment settlements in which the patent holder pays a potential infringer to resolve litigation, coupled with an agreement not to compete (even if within the scope of the patent)

The last type of agreement previously enjoyed protection from antitrust scrutiny, but *Actavis* has rewritten the law.

The *Actavis* decision

In June 2013, the Supreme Court issued its decision in *Actavis*,[14] resolving a dispute concerning the point at which settlements cross the line into territory that violates the antitrust laws. In its simplest terms, the *Actavis* decision narrowed the freedom patent holders have to settle disputes and reinforces the existing law that intellectual property settlements will be treated as agreements between potential competitors and, as such, will need to pass antitrust muster.

Actavis arose from the settlement of a patent infringement dispute. To state the terms in summary fashion, Solvay Pharmaceuticals held the patent for a testosterone gel. Two other companies, including Actavis, sought to produce a generic version. Solvay claimed infringement of its patent, while the defendants asserted both noninfringement and invalidity of the Solvay patent.

Before the court could determine infringement or invalidity of the Solvay patent, a settlement was reached with two principal terms: (1) Actavis agreed not to produce its product until close to the date the Solvay patent expires and (2) Solvay agreed to pay Actavis millions of dollars. Since infringement and validity remained undetermined, the patent monopoly would continue to exist and consumers would continue to pay (and Solvay would continue to reap) monopoly prices for the patented product.

The Federal Trade Commission filed a complaint challenging the *Actavis* settlement agreement as unlawful under the antitrust laws, but the Eleventh Circuit held that the agreement could not support an antitrust violation because it was limited in time and scope: *Actavis*'s agreed limitations on competitive activities were limited only by the term of the patent, and only to the infringing product. As a result, the Eleventh Circuit held that the settlement is "immune from antitrust attack so long as its anticompetitive effects fall within the scope of the exclusionary potential of the patent."[15] An important piece of the holding is the recognition that the public policy favoring settlement meant that the courts could not simply force litigants to continue litigating until validity or infringement was finally determined.

The Supreme Court reversed and thus eliminated a bright-line rule protecting patent holders and defendants/counterclaimants in settling patent claims. In short, the Court rejected use of the test of whether the settlement terms fall within the scope of the patent as a proxy for whether an agreement is unreasonably anticompetitive. Instead, the Court held that both patent and antitrust policy must be considered in determining the scope of antitrust law immunity conferred by a patent. As a result, only by considering what the Court called "the antitrust question," rather than just the question of the legitimate scope of a patent, can a determination be made as to whether a particular restraint violates the antitrust laws. In other words, an analysis of "traditional antitrust factors such as likely anticompetitive effects, redeeming virtues, [and] market power"[16] is required to determine the validity of these settlements under the antitrust laws.

The Court also found that the validity of the patent need not be determined in order to examine the antitrust validity of the challenged agreement. Instead, the size of the reverse payment "can provide a workable surrogate for a patent's weakness, all without forcing the court to conduct a detailed exploration of the validity of the patent itself."[17] The analysis will focus instead on whether the purpose of the agreement is to "share patent-generated monopoly profits" which is "likely" unlawful under the antitrust laws.[18]

In testing the limits of *Actavis*'s reach, courts are faced with the question of whether the reevaluation of their deferential approach to intellectual property settlements is limited to agreements with any consideration flowing from the patent holder to the alleged infringer or more narrowly to *cash* agreements involving reverse payments, or perhaps even limited to pharmaceutical cases in which special legislation exists to regulate patent rights (i.e., Hatch-Waxman).

Some courts have already interpreted *Actavis* as limited in application and triggered only when (1) there is a reverse monetary payment and (2) the reverse monetary payment is "large and unjustified."[19] Only if the agreement passes those tests will it be subjected to rule of reason analysis for antitrust compliance.

Other courts have not limited this renewed antitrust scrutiny to settlements where "reverse payment" means a monetary payment, and have held that the concept must be interpreted broadly to align the law "with modern day realities."[20] Thus "outsized payments for other services" can suffice, and courts can look behind the form of the contract to determine the competitive purpose. The FTC has also filed antitrust claims post-*Actavis* challenging agreements that involve consideration other than reverse cash payments.[21] On September 8, 2014, the FTC accused AbbVie Inc. of violating the antitrust laws with a settlement that delayed Teva's generic launch in exchange for an agreement granting Teva a license to market a generic version of AbbVie's cholesterol drug, TriCor. The case will stretch the meaning of *Actavis* and continue to cause uncertainty in antitrust limitations on intellectual property settlements. Market participants can expect plaintiffs' counsel to use similarly expansive interpretations.

Conclusion

Whether the *Actavis* decision will come to mean that all patent settlements will be analyzed as restraints on trade without the deference previously accorded them may not be resolved for some time. For now, the focus will be on whether any agreement term can be characterized as a reverse payment—regardless of the presence of monetary terms. Patent holders and settling parties can take heart that courts have long recognized the interests served by allowing patent settlements, with at least one court reasoning that if *anything* can be characterized "as involving a forbidden 'reverse payment,' we shall have no more patent settlements."[22] While the debate about the impact of *Actavis* continues, patent holders and defendants will want to undertake additional analysis to ensure that their agreements avoid full antitrust scrutiny, or will survive if challenged. And they may want to settle for less. ■

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ENDNOTES

1. *FTC v Actavis, Inc*, ___ US ___; 133 S Ct 2223; 186 L Ed 2d 343 (2013).
2. See *Walker Process Equipment, Inc v Food Machinery & Chemical Corp*, 382 US 172, 174; 86 S Ct 347; 15 L Ed 2d 247 (1965); *Handgards, Inc v Ethicon, Inc*, 743 F2d 1282 (CA 9, 1984).
3. *United States v Gen Electric Co*, 272 US 476; 47 S Ct 192; 71 L Ed 362 (1926).
4. *Bement & Sons v Nat'l Harrow Co*, 186 US 70; 22 S Ct 747; 46 L Ed 1058 (1902); *United States v Gen Electric*, 272 US 476; 47 S Ct 192; 71 L Ed 362 (1926).
5. *Clorox Co v Sterling Winthrop, Inc*, 117 F3d 50, 55–56 (CA 2, 1997).
6. *United States v United States Gypsum Co*, 333 US 364; 68 S Ct 525; 92 L Ed 746 (1948).
7. *United States v Singer Mfg Co*, 374 US 174; 83 S Ct 1773; 10 L Ed 2d 823 (1963).
8. *United States v Line Material Co*, 333 US 287; 68 S Ct 550; 92 L Ed 701 (1948).
9. *Standard Oil Co v United States*, 283 US 163; 51 S Ct 421; 75 L Ed 926 (1931); *United States Gypsum*, 333 US at 390–391.
10. *In re Cardizem CD Antitrust Litigation*, 105 F Supp 2d 682 (ED Mich, 2000), aff'd 332 F3d 896 (CA 6, 2003).
11. *Charles Pfizer & Co v FTC*, 401 F2d 574 (CA 6, 1968); *Duplan Corp v Deering Milliken, Inc*, 444 F Supp 648, 675–683, 686–687 (D SC 1977); *Singer Mfg Co*, 374 US at 198 (1963).
12. *United States v Besser Mfg Co*, 96 F Supp 304, 310–311 (ED Mich, 1951); *United States v Krasnov*, 143 F Supp 184 (ED Pa, 1956).
13. *Moraine Products v ICI America, Inc*, 538 F2d 134 (CA 7, 1976); *United States v Besser Mfg Co*, 96 F Supp 304, 310–311 (ED Mich, 1951).
14. *Actavis*, 133 S Ct 2223.
15. *FTC v Watson Pharmaceuticals, Inc*, 677 F3d 1298, 1312 (CA 11, 2012).
16. *Actavis*, 13 S Ct at 2231.
17. *Id.* at 2236–2237.
18. *Id.* at 2237.
19. *In re Lamictal Direct Purchaser Antitrust Litigation*, ___ F Supp 2d ___ (D NJ, 2014); *In re Loestrin 24 Fe Antitrust Litigation*, ___ F Supp 2d ___ (D RI, 2014).
20. *In re Nexium Antitrust Litigation*, 968 F Supp 2d 367 (D Mass, 2013); *In re Niaspan Antitrust Litigation*, ___ F Supp 2d ___ (ED Pa, 2014); *Time Insurance Co v Astrazeneca AB*, ___ F Supp 3d ___ (ED Pa, 2014).
21. *FTC v AbbVie Inc*, ___ F Supp 3d ___ (ED Pa, 2014).
22. *Asahi Glass Co v Pentech Pharm, Inc*, 289 F Supp 2d 986 (ND Ill, 2003); see also *Walker Process Equip, Inc v Food Machinery & Chemical Corp*, 382 US 172, 174; 86 S Ct 347; 15 L Ed 2d 247 (1965); *Handgards, Inc v Ethicon, Inc*, 743 F2d 1282 (CA 9, 1984).