Foreword

to the presentation by the Swiss Review of International Antitrust Law of the United States Department of Justice's "Antitrust Guide Concerning Research Joint Ventures"

by

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and

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From the beginning U.S. antitrust authorities have been concerned with preventing joint activity among firms which unreasonably restrains competition. The language of the opening section of the Sherman Act ("contract, combination,...or conspiracy") [1] evidences this concern, as do the earliest successful prosecutions by the Department of Justice under that statute. [2] It was recognized very early that the distinction between reasonable (and thus lawful) and unreasonable restraints of competition could usually be made on the basis of whether the restraints were merely ancillary to a valid business purpose or were instead "naked" restraints which served only to suppress competition.[3] This distinction plays a large part in the subsequent history of U.S. antitrust law.

The doctrine of ancillary restraints has figured prominently in the application of antitrust laws to transactions between firms involving technology. A patent licensing arrangement, for example, is the type of legitimate activity

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[1] 15 U.S.C. § 1.

[2] *United States* v. *Jellico Mountain Coal & Coke Co.*, 46 Fed. 432 (M. D. Tenn. 1891); *United States* v. *Trans-Missouri Freight Association*, 166 U.S. 290 (1897). Both cases involved combinations among firms for the purpose of fixing prices; *Jellico Mountain* involved output restriction as well.

[3] *United States* v. *Addyston Pipe & Steel Co.*, 85 Fed. 271, 281-282 (6th Cir. 1898), *modified and aff'd*, 175 U.S. 211 (1899). See also R. Bork, *The Antitrust Paradox* 26-30 (1978).

which will support ancillary restraints on the use of the information licensed. A cartel, however, is not a legitimate business to which restraints on the use of information can be ancillary. Field of use restrictions which may be lawfully utilized in an ordinary patent licensing arrangement would be unlawful if they were merely inserted to enable the members of a cartel to make more effective an agreement not to solicit each other's customers.[4] A number of the post-war cases involving cartels with U.S. and non-U.S. members attempted unsuccessfully to justify their activities by invoking the doctrine of ancillary restraints.[5]

Virtually all of the attention antitrust enforcers gave to joint activity, whether in technology or in the buying and selling of ordinary goods and services, was devoted to existing technologies or existing markets. Joint activity which did not threaten competition in the use of existing technologies or in the provision of existing goods and services was of little interest to antitrust enforcers.[6]

Gradually it became apparent, however, that competition had a dynamic as well as a static component, and that joint activity—including joint research—which unreasonably impeded the development of new products and processes was as great a threat to competition in its dynamic aspect as traditional restraints of trade were to competition in the static sense.

It is not surprising that antitrust enforcers took a good many years to come to this realization—after all, economists displayed little interest in innovation as a source of economic growth until about thirty years ago.[7] In addition, innovation as a method of competition was an idea popularized by the pioneering work of Joseph Schumpeter, an economist whose enthusiasm for this type of rivalry was matched only by his admiration for monopoly as the best means of achieving

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[4] It should be noted that an ancillary restraint, whether imposed in the context of a technology transaction or in another context, may be unlawful because it is supported by no underlying valid business purpose, *United States* v. *Addyston Pipe & Steel Co.*, *supra* n. 3 at 282-283, or because it goes beyond what is reasonably necessary to protect a valid business purpose. *United States* v. *Topco Associates*, 405 U.S. 596 (1972). An example of the latter type of restraint in the patent licensing context is a restriction on the licensee requiring the latter to purchase, use or sell another article of commerce not within the scope of the patent. *International Salt Co.* v. *United States*, 332 U.S. 392 (1947).

[5] See, *e. g.*, *United States* v. *National Lead Co.*, 63 F. Supp. 513 (S.D.N.Y. 1945), *aff'd* 332 U.S. 319 (1947).

[6] This attitude is mirrored in the frequently quoted dictum of Justice Reed in *United States* v. *Line Material Co.*, 333 U.S. 287, 310 (1948):

> "The development of patents by separate corporations or by cooperating units of an industry through organized research group is a well known phenomenon. However far advanced over the lone inventor's experimentation this method of seeking improvement in the practices of the arts and sciences may be, there can be no objection, on the score of illegality, either to the mere size of such a group or the thoroughness of this research."

[7] F. Scherer, *Industrial Market Structure and Economic Performance* 407-408 (2d ed. 1980).

it.[8] Antitrust, so it appeared, could only promote innovation competition at the cost of fostering greater industrial concentration. While subsequent studies of industrial research have tended to show that market power is not a prerequisite for effective innovation,[9] enforcement authorities of an earlier day must have been considerably inhibited in developing a policy to deal with joint research activities by the Schumpeterian paradox that competition in the static sense inhibited competition in the dynamic sense.

Of greater importance in delaying the emergence of an antitrust policy for dealing with joint research was the difficulty of adapting legal rules which had been developed for joint activities in manufacturing and selling to cooperative work in scientific and industrial research. Simply applying the rules for joint sales agencies and joint manufacturing ventures seemed too drastic a solution—it failed to take into account the differences between industries in which research could be conducted independently by all participants and industries in which no firm was able to conduct research on its own, between research into basic scientific principles and research devoted to adapting an existing product to a new use, between research necessary to enable companies to meet government health and safety regulations and research designed to enable firms to imitate a rival's successful new product. Lacking experience in making these differentiations, antitrust enforcers were compelled to move cautiously in this area.

Although joint research was a new field to enforcement authorities, they had, of course, great expertise in distinguishing between ancillary and anticompetitive restraints contained in otherwise lawful contracts.[10] It was entirely reasonable, therefore, that the first enforcement proceedings brought against joint research projects involved ventures which imposed unnecessary restraints upon the parties or outsiders. In this way action could be taken in an unfamiliar field without the necessity of dealing with wholly novel questions. The first of these cases was *United States* v. *Automobile Mfgrs. Ass'n*, [11] in which the Department of Justice proceeded against the four major automobile manufacturers and their trade association because the joint research project established by them actually retarded innovation in the development, and caused delay in the installation, of vehicular air pollution control devices. Among the many unnecessary collateral restraints charged by the Department in its complaint against that venture were:

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[8] J. Schumpeter, *Capitalism, Socialism and Democracy* 87-106 (3rd ed. 1950).

[9] See generally Kamien and Schwartz, "Market Structure and Innovation: A Survey," 13 J. Econ. Lit. 1 (1975).

[10] See text at nn. 3-4, *supra*.

[11] 307 F. Supp. 617 (C.D. Cal. 1969), *aff'd sub nom. City of New York v. United States*, 397 U.S. 248 (1970); [1969] TR. CAS. (CCH) §72,907 (C. D. Dal. 1969) (consent decree).

(1) an agreement to perform all research on vehicular pollution jointly, thus precluding individual firm research on the problem; (2) a restrictive agreement on patents relating to pollution control, which required the parties to cross-license each other on all such patents and made it impossible for a party to purchase such patents and technology from outsiders unless it was available for purchase by all other parties (this meant, of course, that an outsider had to agree to sell to all such firms if it sold to any); (3) an agreement to install pollution equipment only on a uniform date determined by agreement; and (4) an agreement to restrict publicity on research relating to the pollution problem. This venture was ended by a consent decree which prohibited all the foregoing restraints which had had the effect of suppressing research competition and delaying the marketing of pollution control devices. Significantly, the decree did not forbid joint research projects on vehicular pollution control, and a number of such projects have been engaged in by automobile manufacturers in the last decade.

The next case brought by the Department was *United States* v. *Wisconsin Alumni Research Foundation*.[12] Here the charge was that the Foundation used exclusive grantback licensing arrangements to acquire exclusive control over patents involving the Wurster process for coating pharmaceutical products. The grantback provision, collateral to the joint research effort, licensed the patents on condition that the licensees assign back to the Foundation all patents flowing from improvements. This restriction, the Department charged, resulted in less innovation, for it deprived the licensees of incentive to make improvements.

Three years later the Department challenged the longstanding patent pooling and cross-licensing agreement among 20 major aircraft firms and the Manufacturers' Aircraft Association.[13] Once again it was the collateral restraint—the patent agreement, requiring all patents to be shared among the members—which was challenged because it suppressed competition for the purchase of patents and patentable inventions. Again the objection was that the venture threatened to retard, rather than advance, innovation and competition.

Despite the care with which the Department had chosen its cases, and despite the fact that no enforcement proceedings had been brought against pure joint research ventures involving no collateral restraints, many Americans became concerned that antitrust rules developed in other contexts might be applied to joint research,[14] and that the possibility of antitrust proceedings against

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[12] [1970] TR. CAS. (CCH) §73,015 (W.D. Wisc. 1969) (consent decree).

[13] *United States* v. *Manufacturers' Aircraft Association*, [1976-1] TR. CAS. (CCH) §60,810 (S.D.N.Y. 1975) (consent decree).

[14] See *supra*.

cooperative research projects was inhibiting firms from entering into ventures which promised to promote innovation while posing no threat to competition.[15] This concern was made more acute by the large decline in the rate of productivity growth experienced by the United States in the 1970s.[16] If, as some prominent economists thought,[17] lower spending on research was part of the reason for the productivity decline, it followed that antitrust might be discouraging research and thereby reducing competition while contributing to the fall in productivity growth. It was for this reason that President Carter, at the conclusion of the White House Domestic Policy Review of Industrial Innovation, stated in his message to Congress on October 31, 1979, and in the materials accompanying that message, that he was directing the Department of Justice to clarify its position on joint research to make certain that the antitrust laws are not "mistakenly understood to prevent cooperative activity, even in circumstances where it would foster innovation without harming competition"[18]. The *Antitrust Guide Concerning Research Joint Ventures* is the Department's response to that directive.

The *Research Guide* begins with an introduction setting forth the Antitrust Division's analytical approach to research joint ventures. The introduction explains that effects of the essential elements (participants in, scope and duration of and problems sought to be solved by, the venture, together with the market setting in which the venture will take place), collateral restraints (in general, and with specific reference to patents and know-how) imposed on the venturers or outsiders, and limitations upon access to the venture or to its results, all play vital roles in determining whether the venture is in harmony with U.S. antitrust laws.

In the common law tradition,[19] and in accordance with the precedent set by the Department's 1977 *Antitrust Guide for International Operations*, the principles set forth in the introduction to the *Research Guide* are illustrated by a series of hypothetical cases. Each case contains an analysis of the approach the Department is likely to take in that factual situation. These cases are followed by an explanation of the Department's business review procedures, which enable firms to seek a statement of enforcement intention concerning proposed conduct

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[15] See generally the U.S. Department of Commerce publication *Advisory Committee on Industrial Innovation: Final Report* 103-110 (1979). The influence of antitrust enforcement on the level of investment in industrial research had been noted by earlier observers, though usually in the context of single-firm conduct. See R. Nelson, M. Peck and E. Kalachek, *Technology Economic Growth and Public Policy* 168 (1967).

[16] For details of this decline see E. Denison, *Accounting for Slower Economic Growth* 61-63 (1979).

[17] *Id.* at 122-123.

[18] *Antitrust Guide Concerning Research Joint Ventures*, Preface (1980).

[19] Compare the various *Restatements of the Law* issued by the American Law Institute.

and three appendices. The most significant of the latter is Appendix B, a collection of summaries of research and development joint venture business reviews and clearances issued by the Department from 1968 to 1980.

The *Research Guide*, although promulgated by U.S. antitrust authorities and intended primarily for the guidance of U.S. companies, has significance for non-U.S. competition authorities and non-U.S. companies. The analytical approach to joint research ventures embodied in the *Research Guide* employs legal principles concerning restrictive business practices which are widely accepted in the world community. Thus, it is hoped that the *Research Guide* may prove helpful to national or multinational competition authorities and experts outside the U.S. seeking to set standards relating to research joint ventures and associated restrictive practices. In addition the *Research Guide* may be of service to firms outside the U.S. contemplating joint ventures with American partners. Such international joint ventures have been numerous in the past, and there is every reason to expect them to continue to take place in the future. While the *Research Guide* does not deal specifically with ventures which involve only non-U.S. companies, the general principles it sets forth provide some indication as to how these ventures might be treated under U.S. antitrust laws, if they are subject to U.S. law at all because of their intended locus and effects.[20]

As the discussion in Part III of the *Research Guide* indicates, enterprises which contemplate that they may have antitrust problems if they enter into a proposed joint venture may avail themselves of the business review procedures, which enable enterprises doing business in or with the U.S. to seek a letter of enforcement intentions from the Department of Justice. The *Research Guide*, while it should prove useful as a source of advice on general antitrust problems that may arise from joint research, is not a substitute for the more particularized advice provided by the business review procedures or for the expert counselling of a lawyer knowledgeable in American antitrust law and familiar with all the facts regarding a particular joint venture.

It has been U.S. policy and the practice of the Department of Justice that documents such as the *Research Guide* are non-partisan, and thus the *Research Guide* would normally be expected to remain authoritative even with a change in political administrations such as recently occurred in the U.S. As additional experience is gained with the economic effects of research joint ventures, however, the *Research Guide* may be modified in light of that experience.

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[20] On ventures between non-U.S. firms, see also Appendix B, Item 19 in the *Research Guide*.