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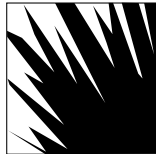
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The Sedona Conference Journal[®] designed by
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Cite items in this volume to "10 Sedona Conf. J. ____ (2009)."

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Welcome to Volume Ten of *The Sedona Conference Journal*[®] (ISSN 1530-4981), an annual collection of articles originally presented at our conferences and papers prepared by our Working Groups over the past year. The Sedona Conference[®] was founded in 1997 to provide a forum for advanced dialogue by the nation's leading attorneys, academics and jurists of cutting-edge issues of law and policy in the areas of antitrust, intellectual property rights, and complex litigation. We host Regular Season Conferences and several Working Group Meetings each year, providing unique and rewarding opportunities to seriously explore the boundaries of various areas of the law with those who are creating them. This volume of the *Journal* contains articles selected from our most recent Conferences on antitrust law and litigation (Fall 2008), patent litigation (Fall 2008), complex litigation (Spring 2009), Cross-Border Data Transfer Conflicts (Summer 2009), and our Working Group on Electronic Document Retention and Production (WG1).

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*Richard G. Braman
Executive Director
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Sedona, Arizona USA
September 2009*

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A NEW U.S. ADMINISTRATION AND U.S. ANTITRUST ENFORCEMENT

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I. INTRODUCTION

Come January of 2009, one thing is certain: the Bush Administration will be gone and there will be a new Administration in Washington. The question to be considered by this paper is what difference, if any, will a new Administration make in United States antitrust enforcement. The answer of course depends somewhat, if not a great deal, on whether Barack Obama or John McCain is the next President. Predicting the outcome of the coming election, however, is beyond the scope of this paper.¹

Indeed, one can argue that the outcome of the impending election as an influence on future antitrust enforcement pales as a causative factor in comparison with the state in which the outgoing Administration leaves both substantive and procedural antitrust law. Before one can predict what future antitrust enforcement will look like, one had better take a good long look at the present state of antitrust jurisprudence to see whether there is anything still left alive, and, if so, whether the patient can be revived and to what degree of health and vigor.

Accordingly, this paper will look first at the condition in which the Bush Administration is leaving antitrust, and then hazard a few predictions about the nature and extent of its possible resuscitation.

II. THE BUSH LEGACY IN ANTITRUST

A. What the Supreme Court Hath Wrought

Beginning in 2004, the Supreme Court decided a series of eight antitrust cases, each of which significantly narrowed and placed limitations on private antitrust enforcement and, one would argue, also on Government enforcement, in that the Supreme Court in each case either found conduct not to be subject to *per se* treatment, or not to be reachable at all under the antitrust laws.² The cumulative effect of these decisions has been greatly to restrict antitrust enforcement, whether public or private.

The cases, each of which will be briefly discussed, include *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004); *Volvo Trucks No. Am., Inc. v. Reeder-Simco GMC, Inc.*, 546 U.S. 164 (2006); *Illinois Tool Works, Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006); *Texaco, Inc. v. Dagher*, 547 U.S. 1 (2006); *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., Inc.*, 549 U.S. ____, 127 S. Ct. 1069 (2007); *Bell Atlantic Corp. v. Twombly*, __ U.S. ____, 127 S. Ct. 1955 (2007); *PSKS, Inc. v. Leegin Creative Leather Prods.*, __ U.S. ____, 127 S. Ct. 2705 (2007); *Billing v. Credit Suisse First Boston, Ltd.*, __ U.S. ____, 127 S. Ct. 2383 (2007); and *Pacific Bell Telephone Co. v. linkline Communications, Inc.*, __ U.S. ____, 555 U.S. ____, No. 07-512 (U.S. 2/25/2009) (2009).

¹ Of course, we now know the outcome of the election. I have taken this into account, where appropriate, in this paper, which was originally written in July of 2008.

² Since the writing of this paper, there has now been a ninth Supreme Court antitrust decision, *Pacific Bell Telephone Co. v. linkline Communications, Inc.*, No. 07-512 (U.S. 2/25/2009) (2009). This decision fits exactly with its predecessors in the pattern discussed in this article. The Court has also granted certiorari in another antitrust case, *American Needle, Inc. v. National Football League*, 538 F.3d 736 (7th Cir., 2008), certiorari granted, No. 08-661 (U.S. 6/29/2009), which does not fit the pattern, but does portend a further shrinking of antitrust, as will be discussed, *infra*.

In *Verizon v. Trinko*, the Supreme Court significantly narrowed the duty of an alleged monopolist to deal with customers or rivals. The plaintiff claimed that the defendant's refusal to interconnect with other carriers violated the Telecom Act and was therefore unlawful predatory conduct under Section 2 of the Sherman Act. The Court held not only that there was no Section 2 violation that could be premised on a violation of the Telecom Act, but also that there was no otherwise unlawful refusal to deal. In so holding, the Court stated that generally a monopolist has no duty to deal with or assist rivals or customers, and that the "outer limits" of the refusal to deal doctrine are those enunciated in *Aspen Skiing Co. v. Aspen Highland Skiing Corp.*, 472 U.S. 585 (1985). The Supreme Court also cast doubt on the so-called essential facilities doctrine from *United States v. Terminal R.R. Ass'n*, 224 U.S. 383 (1912). The effect of *Trinko* is unquestionably to limit, if not eliminate, a monopolist's duty to deal, except in limited circumstances akin to those of *Aspen Skiing*, where the alleged monopolist terminates a prior long-standing relationship without a valid business justification.

In *Volvo v. Reeder-Simco*, the Court reversed a decision for the plaintiff in a secondary line Robinson-Patman case involving bidding by Volvo dealers for truck sales. The Court reversed the decision on the very narrow ground that the plaintiff had failed to show that it competed against favored Volvo dealers for sales to the same buyers. The Court failed to reach the issue of whether the Robinson-Patman Act can ever apply to competitive bidding situations, which might appear, by definition, not to involve two sales. It is difficult to know what precedential value the *Volvo* decision has, or even to understand why the Supreme Court took the case, except perhaps that the Court disapproved of the result in the lower court. One cannot conclude that the decision bespeaks any hostility by the Court towards secondary line Robinson-Patman cases, although one can expect that if this Court takes any such cases in the future, it will be to narrow their scope.

In *Illinois Tool v. Independent Ink*, the issue was whether, in a tying case, a patented tying product requires a presumption of market power, as the Court had previously held in *International Salt v. United States*, 332 U.S. 392 (1947), and *United States v. Loew's*, 371 U.S. 38 (1962). Overruling *International Salt* and *Loew's*, the Court held that there would be henceforth no presumption of market power in the tying product based solely on the tying product's intellectual property protection. Instead, the plaintiff in a tying case will have to prove a relevant market and market power in the relevant market, with no assistance from a presumption arising from the product's intellectual property. Obviously, the effect of this will be to make tying cases much harder for plaintiffs. The opinion is also illuminating in the light it throws on the present Court's regard, or disregard, for precedent.

In *Texaco v. Dagher*, the Court reversed a Ninth Circuit decision that permitted a finding of *per se* price-fixing liability against Shell and Texaco, after they formed a joint venture and ordered the venture to charge identical prices for the Shell and Texaco brands of gasoline. The Court said there could be no *per se* price-fixing when a fully-integrated joint venture sets prices for its own products. The Court also said that the ancillary restraints doctrine articulated in *Addyston Pipe & Steel Co. v. United States*, 175 U.S. 211 (1899), was inapplicable to intraventure decisions, and applied only to decisions that affected activities of the venture partners outside the joint venture. What the case appears to stand for is the proposition that the *per se* rule cannot be applied to decisions by joint venture participants regarding the operations of their venture, although such a holding appears inconsistent with the Court's decisions in *Citizen Publishing Co. v. United States*, 394 U.S. 191 (1969) and *Arizona v. Maricopa County Med. Soc'y*, 457 U.S. 332 (1982), as well as at least one lower court decision, *Freeman v. San Diego Board of Realtors*, 322 F.3d 1133 (9th Cir. 2003).

In *Weyerhaeuser v. Ross-Simmons*, the plaintiff made a claim of predatory bidding against the defendant, which allegedly violated Section 2 by paying excessive prices to corner the market for timber, an input in the defendant's lumber business. The Supreme Court held that in order to establish predatory bidding for an input product in violation of Section 2, the plaintiff had to show, with respect to the defendant's output product, finished lumber, that the defendant sold the product below cost and was likely to be able to recoup its losses after driving competitors from the market. In other words, the Supreme Court extended the rule of *Brooke Group v. Brown & Williamson*, 509 U.S. 209 (1993), a predatory selling case, to predatory buying cases. What *Weyerhaeuser* appears to hold

and portend is that in any Section 1 or 2 case challenging the defendant's pricing (other than a horizontal price-fixing case), the plaintiff must show that the defendant sold the product below an appropriate measure of cost (which the Supreme Court has not yet specified) and had a reasonable likelihood of being able to recoup any losses by future supracompetitive pricing.

In *Bell Atlantic v. Twombly*, the issue for the Supreme Court was the sufficiency of a complaint under Section 1 alleging parallel conduct. The Supreme Court held that a complaint alleging only parallel conduct with a conclusory allegation of agreement fails to state a claim of unlawful concerted action. The Court said that a complaint must now allege facts beyond parallel conduct tending to exclude the possibility of independent conduct, and establishing a plausible claim of conspiracy. The impact of *Twombly* has been that complaints are now routinely being challenged, and often dismissed, for being insufficiently specific not only with regard to the particulars of unlawful agreement, but also with regard to every other element of the claim asserted and the insufficient plausibility of the claim alleged. Although the Supreme Court disavowed any intention of doing so, *Twombly* has without question created a heightened pleading standard in antitrust cases, and has caused Rule 12 motion practice to burgeon and proliferate. *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574 (1986), encouraged the use of summary judgment to dispose of antitrust claims; *Twombly* has now done the same with regard to Rule 12(b)(6) motions.

In *PSKS v. Leegin*, the issue for the Court was whether the *per se* rule against minimum resale price maintenance, first announced in *Dr. Miles Med. v. Park & Sons*, 220 U.S. 73 (1911), should be overruled. Overruling *Dr. Miles*, the Court held that minimum vertical price-fixing would now be subject to analysis under the rule of reason, just as maximum resale price-fixing is treated. The ease with which the Supreme Court overruled *Dr. Miles* after roughly a century is hard to reconcile with the Court's decision in *Flood v. Kuhn*, 407 U.S. 258 (1972), in which the Court refused to overrule its prior decisions that baseball was exempt from the antitrust laws as not being commerce, because the Court construed Congressional inaction to be satisfaction with the status quo. After *Leegin*, all vertical restraints, whether price or non-price, are now subject to the rule of reason.

In *Billing v. Credit Suisse*, the issue was whether the securities laws preempted application of the antitrust laws to an alleged conspiracy of underwriters to fix prices in connection with initial public offerings of stock. The Court held that there was preemption. The Court's decision casts doubt on numerous prior Supreme Court decisions holding that implied antitrust immunity is disfavored and to be strictly limited. *E.g.*, *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 231 (1979); *Abbott Labs v. Portland Retail Druggists Ass'n, Inc.*, 425 U.S. 1, 11-12 (1976). The decision in *Credit Suisse* is also noteworthy because it contradicts extensive scholarship by economists, which led to significant deregulation in the 1970s, showing that the regulatory agencies, like the Securities and Exchange Commission, cannot be relied upon to regulate the industries they watch because of "regulatory capture," *i.e.*, viewing the regulated industries more as clients than as businesses needing close and skeptical oversight. The opinion also contains language expressing the Court's concern with the high costs of antitrust litigation and the likelihood that lower courts might make mistakes in analyzing complex economic issues. The decision shows a surprising and distressing lack of confidence in a judicial system that most litigating attorneys, both plaintiff and defense counsel, believe has worked extraordinarily well for a very long period of time.

In *Pacific Bell Telephone Co. v. linkline Communications, Inc.*, the issue was the continued viability under Section 2 of a price squeeze claim where a monopolist sells a product or service to its wholesale customers at a price sufficiently high so that they cannot profitably resell against the monopolist's pricing to retail customers. Before *linkline*, the leading price squeeze case was *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945). In *linkline*, the Supreme Court held that there could be no price squeeze claim because the monopolist had no "antitrust duty" to deal with the plaintiff at the wholesale level, and because the plaintiff had not shown that the monopolist's retail prices were below any appropriate level of the monopolist's costs. The decision effectively eliminates cost squeeze claims from Section 2 jurisprudence by requiring such claims to become predatory pricing claims subject to the rules of *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U. S. 209, 222-224 (1993). The decision also disturbingly adopts the new concept of an "antitrust duty to deal," which is nothing more than circular reasoning finding no basis in prior

antitrust jurisprudence. That a monopolist has no “antitrust duty to deal” is the Court’s extrapolation of dictum in *Verizon v. Trinko, LLP* to create a new antitrust principle where none previously existed, without a reasoned consideration of what a monopolist’s duty to deal ought to be in a situation where the monopolist sells at both wholesale and retail. In such a situation, the rule might plausibly be that a monopolist electing to sell at retail and wholesale ought not set wholesale prices at a level the monopolist knows and intends will drive out retail competitors. In other words, the monopolist has no duty at all to sell at wholesale to its retail competitors, but if it chooses to do so, it cannot set prices at a level that it knows and intends will prevent them from competing at retail. Whether this rule or some other rule makes sense is not really the point. The point is that the Supreme Court never even considered the issue of what the rule ought to be, and instead swept everything under the rug of its new “antitrust duty to deal” label, which is simply another way of saying that the courts should find that monopolists have a duty to deal only in cases virtually indistinguishable from *Aspen Skiing Co. v. Aspen Highland Skiing Corp.* *linkline* continues a trend of making a dead letter of the Court’s definition of predatory conduct as “attempting to exclude rivals on some basis other than efficiency,” *Aspen Skiing*, 472 U.S. at 605, a standard intelligible to litigants, courts, and particularly juries, and therefore threatening to antitrust defendants and apparently anathema to the present Supreme Court.

When one looks back at these cases, one sees that *per se* rules now have a much narrower scope, applying only to horizontal price-fixing and divisions of markets and customers; the rule of reason covers everything else under Section 1, with its requirement of proving market power in a relevant market; the only pricing practices of antitrust concern, other than horizontal price-fixing, require proof of prices below cost and likely recoupment; pleading and procedure have become much more difficult for antitrust plaintiffs; and the overall reach of the antitrust laws is shrinking.

Nor does the Supreme Court appear to be done. In granting certiorari in *American Needle, Inc. v. National Football League*, 538 F.3d 736 (7th Cir., 2008), *certiorari granted*, No. 08-661 (U.S. 6/29/2009), the Court appears poised to extend the single entity defense not only to sports leagues, but to numerous other types of organizations and associations of competitors. In *American Needle*, the Seventh Circuit held that National Football League acted as a single entity in licensing team logos for merchandise, and therefore could not be liable under Section 1 for engaging in an unlawful combination or conspiracy. Both the plaintiff and the NFL asked for certiorari. The Court requested the views of the Solicitor General, which advised *against* granting certiorari. The Court nonetheless granted certiorari, to the mystification of most Supreme Court watchers. Two features of *American Needle* stand out as different from the other nine cases: first, the defendant won in the court of appeals, and the Supreme Court granted certiorari nonetheless; and, second, the Court granted certiorari contrary to the Solicitor General’s recommendation. What this seems to presage is that a significant faction on the Court sees an opportunity for a major disquisition on the single entity defense enunciated in *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984), and on the scope of joint venture liability implicated in *Texaco v. Dagher*. Furthermore, the Court’s opinion in *American Needle* is likely to give scant, if any, weight to whatever views the Obama Justice Department expresses. One quails at the prospect of what will emerge from the Court in its decision.

In predicting what a new administration will do with antitrust enforcement, one must bear in mind what this Supreme Court has done to antitrust in its last nine decisions, and will likely continue to do. In addition, the judicial appointments of the last eight years have placed on the bench a large number of judges who share the views of the conservative wing of the Supreme Court with regard to antitrust. These judges not only must follow the Supreme Court’s decisions in the last nine cases, but also are unlikely to be receptive to expansive and vigorous antitrust enforcement.

Thus, the legacy of the Bush Administration and this Supreme Court has been to restrict antitrust enforcement to such a degree that one must seriously question whether a revival of antitrust enforcement is possible or likely, even if the will is there to accomplish it.

B. The Enforcement (or Non-Enforcement) Agencies

In each of the nine antitrust cases discussed above, the plaintiff prevailed in the Court of Appeals, the Supreme Court granted certiorari, and the Supreme Court ruled for the defendant. Also,

in each of these cases, the Solicitor General, expressing the views of the Antitrust Division of the Department of Justice, the FTC, or both, weighed in on the side of the defendant in the Supreme Court. It is difficult to understand the interest of the Government in making antitrust enforcement more difficult and the reach of the antitrust laws narrower and more restrictive. Although each of the nine cases involved private litigants instead of the Government, the rules and limits imposed by the Supreme Court are equally applicable to most Government enforcement actions. Strangely, the Antitrust Division and the FTC appear to want to make their own enforcement actions more difficult. Apparently, this is a tradeoff the Bush Administration was willing to make in order to limit the access of private antitrust plaintiffs to the federal courts.

Besides routinely taking positions in opposition to private plaintiffs before the Supreme Court, the Antitrust Division and FTC also substantially curtailed the number of actions brought against mergers during the Bush years. See James Langenfeld & Daniel R. Shulman, "The Future of U.S. Federal Antitrust Enforcement: Learning from Past & Current Influences," *The Sedona Conference Journal* (Vol. 8) (Fall 2007), pp. 2-8. In those instances where the Antitrust Division or FTC challenged mergers, they have met with a singular and distressing lack of success. *United States v. Oracle Corp.*, 331 F. Supp. 2d 1098 (N.D. Cal. 2004); and *FTC v. Arch Coal Inc.*, 329 F. Supp. 2d 109 (D.D.C. 2004); *United States v. SunGard Data Sys.*, 172 F. Supp. 2d 172 (D.D.C. 2001).³

The upshot of the foregoing is a perfect storm of merger nonenforcement at the close of the Bush Administration. The Government brings fewer cases; those they bring come before a conservative bench and result in losses; and the effect of losing such apparently strong cases as *Oracle*, *Arch Coal*, and, until its reversal, *Whole Foods* is to demoralize and discourage the Government from bringing more merger cases. The possibility of the Government's challenging a merger from four to three firms in an industry appears nonexistent; the prospect for challenging a three-to-two merger is doubtful or remote.

There are, however, several bright spots. First, the Antitrust Division has consistently prosecuted price-fixing and output reduction cartels, most of which have been international. These have included, *inter alia*, vitamins, air cargo rates, marine hoses, and a succession of electronics components, among them SRAM and DRAM chips, LCD flat panels for computers and televisions, flash memory, and cathode ray tubes, all of which have led to grand jury investigations. See also Langenfeld & Shulman, *id.* at pp. 8-11. One reservation that might be expressed, however, is that the Government's enforcement activities do not seem to have had a deterrent effect, as new cartels continue regularly to come to light.

Another observation worth making is that the FTC has consistently appeared more vigorous in its enforcement activities than the Antitrust Division. Although it lost, the FTC brought *Arch Coal*. It also brought *Whole Foods*, where it prevailed on appeal after losing at trial. The FTC has also taken a position against Hatch-Waxman patent settlements as *per se* unlawful market divisions, although with mixed results. The FTC further prosecuted and prevailed in the *Three Tenors* case, and in doing so laid out a logical and principled approach to applying the quick look rule of reason. *Polygram Holding, Inc. v. FTC*, 416 F.3d 29 (D.C. Cir. 2005).⁴

A third heartening development is the Antitrust's Division's recent repudiation of *Competition and Monopoly: Single-Firm Conduct under Section 2 of the Sherman Act*, United States Department of Justice (2008), the last hurrah of the Bush Antitrust Division, which can best be compared to a defeated army's spiking its guns as it retreats vanquished from the field. In this report, the Bush DOJ attempted to establish new guidelines for Section 2 liability, which were ridiculously one-sided in favor of defendants and further demonstrated a disregard, if not disdain, not only for precedent, but also for the views of the FTC, which felt compelled to go on record in opposition to the new guidelines. President Obama's new head of the Antitrust Division, Christine Varney, explicitly disavowed her predecessor's report, in a speech of May 11, 2009, in which she said:

3 The original draft of this article included in this list *FTC v. Whole Foods Market, Inc.*, 502 F.Supp.2d 1, (D.D.C. 2007), *reversed*, ___F.3d___, 2008 WL 2890688 (D.C. Cir. July 29, 2008). The D.C. Circuit's reversal of *Whole Foods* is a heartening development, which may help to reinvigorate merger enforcement in the next administration.

4 Fairness also requires giving credit to the Antitrust Division for successfully litigating *United States v. Dentsply Int'l, Inc.*, 399 F.3d 181 (3d Cir. 2005).

For these reasons, I have withdrawn the Section 2 Report by the Department of Justice. Effective May 11, 2009, the Section 2 Report no longer represents the policy of the Department of Justice with regard to antitrust enforcement under Section 2 of the Sherman Act. The Report and its conclusions should not be used as guidance by courts, antitrust practitioners, and the business community.

Finally, the Obama administration has to date signalled an apparent willingness to make a much harder look and much firmer stand against mergers, as is apparent from its review of the proposed Ticketmaster-Live Nation and Pfizer-Wyeth combinations.

C. The Class Action Fairness Act of 2005

Another important antitrust legacy of the Bush Administration is 28 U.S.C. §§ 1332(d), 1453 and 1711-15, which bears the Orwellian title of the Class Action Fairness Act of 2005 (“CAFA”). The effect of CAFA is to put in federal court virtually all state law antitrust actions brought as class actions. The impetus for the legislation was the proclivity of state legislatures to pass statutes allowing for more vigorous private enforcement under state antitrust law than under federal law, such as various *Illinois Brick* repealer statutes permitting indirect purchasers to recover damages from price fixers. With the requirement that such actions be brought instead in federal courts, state law indirect purchaser antitrust cases now end up in MDL proceedings consolidated with direct purchaser cases. This creates for federal district courts a witches brew of procedural and substantive conundrums. For example, *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938), requires a federal court to decide how various state supreme courts throughout the United States would apply the antitrust law of their respective states. At the same time the federal courts must decide whether and to what extent to follow the procedural law of each state in which a state law antitrust class action is asserted. These issues bubble into a bewildering and noxious effluvium when the federal courts deal with issues of class certification and antitrust injury, as is apparent from recent decisions in the SRAM and graphics processing unit multidistrict proceedings.

Thus, not content with stifling federal antitrust enforcement, the Bush Administration and its cronies in Congress have reached out to cast a dead hand on state antitrust enforcement as well.

III. THE FUTURE

Prognostication is risky, but a few predictions can safely be made, while others of a more speculative nature will be advanced.

First, vigorous cartel enforcement can be expected to continue, both by the Government and by private plaintiffs. Where price-fixing is suspected or detected, the Department of Justice will continue to convene grand juries, and private plaintiffs will file cases, particularly consumer class actions. One change that is hoped for is that at least one or more of these proceedings will result in sufficiently serious penalties to deter future cartel activity, such as a trial in a civil class case resulting in a money judgment that actually approximates the damages sustained by the class, trebled, rather than a settlement that the defendants regard merely as a cost of doing business or tax for price-fixing. If cartel activity is effectively to be deterred by Government or private litigation, a doomsday scenario actually needs to eventuate in one of the cases, with top executives going to prison and the company paying the class’s real treble damages.

Second, merger enforcement is likely to become more vigorous, especially under a Democratic administration. Even if Senator McCain wins, however, some uptick in merger enforcement is likely, because one cannot imagine enforcement being this moribund forever. Indeed, now that Obama is President, the Department of Justice must deal with a number of drug company mega-mergers and the Ticketmaster-Live Nation merger, all of which involve financially healthy companies, which prophesy cost savings from their combinations as a result of substantial layoffs. This raises the question of whether such cost savings ought to be viewed as pro- or anti-competitive in a time of recession and rising unemployment, and whether this is a proper consideration for antitrust enforcers.

Third, there are lacunae and uncertainties in antitrust law that cry out for resolution and will need to be addressed. Chief among these is bundled pricing. The Third Circuit's decision in *3M v. LePage's, Inc.*, 324 F.3d 141 (3d Cir. 2004), cert. denied 542 U.S. 953 (2004), has been widely condemned, and specifically rejected by the report of the Antitrust Modernization Commission, and by the Ninth Circuit in *Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883 (9th Cir. 2008), *superseding and amending* 502 F.3d 895 (9th Cir. 2007). This is an area where the Supreme Court could provide welcome guidance.

The Supreme Court has also not reviewed a merger case in almost 40 years. As Judge Posner noted in *Hospital Corporation of America v. FTC*, 807 F.2d 1381, 1385 (7th Cir. 1986), with respect to the Supreme Court's merger decisions of the 1960s:

The other decisions in that decade—in particular *Brown Shoe Co. v. United States*, 370 U.S. 294, 82 S. Ct. 1502, 8 L. Ed. 2d 510 (1962); *United States v. Aluminum Co. of America*, 377 U.S. 271, 84 S. Ct. 1283, 12 L. Ed. 2d 314 (1964); *United States v. Von's Grocery Co.*, 284 U.S. 270, 86 S. Ct. 1478, 16 L. Ed. 2d 555 (1966), and *United States v. Pabst Brewing Co.*, 384 U.S. 546, 86 S. Ct. 1665, 16 L. Ed. 2d 765 (1966)—seemed, taken as a group, to establish the illegality of any nontrivial acquisition of a competitor, whether or not the acquisition was likely to bring about or shore up collusive or oligopoly pricing. The elimination of a significant rival was thought by itself to infringe the complex of social and economic values conceived by a majority of the Court to inform the statutory words “may . . . substantially . . . lessen competition.” None of these decisions has been overruled.

One would be hard pressed to find a lower court decision following any of these cases to enjoin or unwind a merger.

Similarly, alleged “efficiencies” in the form of cost savings are today the most frequently cited justifications for proposed mergers. Nonetheless, the Supreme Court has stated that claimed cost savings are not a sufficient justification for an otherwise unlawful combination. *FTC v. Procter & Gamble Co.*, 386 U.S. 568, 580 (1967). When lower courts have considered such an efficiency or cost-saving defense, they have generally required some showing that any claimed cost savings will ultimately be passed on to consumers. *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 720 (D.D.C. 2001); *FTC v. Univ. Health, Inc.*, 938 F.2d 1206, 1223 (11th Cir. 1991); *FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1088-89 (D.D.C. 1997); *FTC v. Butterworth Health Corp.*, 946 F. Supp. 1285, 1300-01 (W.D. Mich. 1996); *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 171-72 (D.D.C. 2000); *United States v. United Tote, Inc.*, 768 F. Supp. 1064, 1084-85 (D. Del. 1991); *California v. Am. Stores Co.*, 697 F. Supp. 1125, 1132-33 (C.D. Cal. 1988), *aff'd* in part and *rev'd* in part on other grounds, 872 F.2d 837 (9th Cir. 1989), *rev'd*, 495 U.S. 271 (1990); *United States v. Long Island Jewish Med. Ctr.*, 983 F. Supp. 121, 148-49 (E.D.N.Y. 1997) (“The second prong of the ‘efficiencies’ analysis is whether these savings would be passed on to the consumers.”). Here, again, guidance from the Supreme Court would be welcome and is long overdue.

The issue of Hatch-Waxman patent settlements also cries out for Supreme Court analysis and guidance. Because the trend of the decisions is strongly in favor of sustaining the validity of these settlements, contrary to the position of the FTC, however, this Supreme Court is unlikely to intervene, unless the FTC is able to prevail in one of its challenges.

Finally, it is anyone's guess what the future holds for enforcement directed at unilateral conduct. The Supreme Court appears, in *Trinko*, to have closed the door to challenges to a monopolist's refusal to deal. Likewise, there do not appear to be any prohibited pricing practices by a monopolist that do not require below-cost pricing and a reasonable likelihood of recoupment. This raises the interesting question of the future of exclusive dealing arrangements by a monopolist, when the inducement to obtain the exclusivity is based on some form of monetary consideration, like a market share discount, rebate, or some other form of payment for not doing business with competitors. One must ask whether, in such cases, the plaintiff must allocate the payment for

exclusivity to the price for the monopolist's product or products and show the products are being sold below cost in order to establish predation. If so, this raises the question of whether there is a principled basis for distinguishing these rebate or payment-based exclusive dealing cases from exclusive dealing arrangements procured by non-monetary inducements or threatened refusals to deal if the buyer deals with the monopolist's competitors. Because exclusive dealing arrangements are a staple of Section 2 cases, such as in *Microsoft*, these are interesting issues that courts are almost certain to wrestle with in the next four years.

IV. CONCLUSION

Unfortunately, analysis of the future of antitrust enforcement under the next administration must begin with a post-mortem, to determine whether there is anything of the patient that has survived the last eight years, and, if so, what. Equally unfortunately, the answer is not much. Even more unfortunately, the medical staff charged with ensuring the future health and viability of the patient consists of the present Supreme Court and sitting federal bench, which in many respects exhibits an attitude of "better off dead." That said, cartel enforcement appears to be alive and perhaps well, and should continue so under the next administration. Merger enforcement can only get better. The rest depends on who occupies the White House and Congress and whether there is any interest in beginning to disinter the centenarian now buried at least up to its neck and gasping for air. I refer to the antitrust laws. November 4 will tell us.

GLOBAL ENFORCEMENT OF ANTICOMPETITIVE CONDUCT

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Globalization of commerce has increased the economic interdependence of countries around the world.¹ The increasing integration of markets has brought with it an increase in the number and frequency of anticompetitive business practices, affecting economies worldwide. Recent statistical analysis found that the 283 international cartels discovered between 1990 and 2005 adversely affected more than one quarter of the world's business. In 2005 alone, sales affected by cartels were about \$2.1 trillion in real U.S. dollars.² Of the 283 discovered cartels, 16% were active only in North America, 47% were active only in Europe (compared to 16% in North America and 12% in other continents), and the remaining 25% operated globally.³

The increasingly globalized nature of anticompetitive practices has been accompanied by an increase in competition laws enacted by countries around the world.⁴ For example, Australia, Japan, Israel and Ireland have all worked to enhance their competition laws since 1990.⁵ In addition, several Latin American countries enacted or revised competition laws in the last twenty years, including Panama, Nicaragua, Venezuela, Chile and Argentina.⁶ China first introduced a comprehensive competition law in 2007,⁷ and its anti-monopoly law only became effective on August 1, 2008.⁸ In most cases, these new competition acts are patterned on those in the United States and Western Europe, and focus on the market and effects of the enacting country.⁹

One effect of the number of competition laws enacted worldwide is increased divergence in their application and enforcement. This leads to inconsistent detection and regulation of anticompetitive practices, which, in turn, allows such conduct to remain profitable. Because the enforcement of country-specific competition laws is necessarily limited in a globalized economy, only the cross-border cooperation of both criminal and private enforcement can effectively deter

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1 Alvin K Klevorick & Alan O. Sykes, *United States Courts and the Optimal Deterrence of International Cartels: A Welfareist Perspective on Empagran*, 3 J. COMPETITION L. & ECON. 309, 310 (2007).

2 *Id.*

3 John M. Connor & C. Gustav Helmes, *Statistics on Modern Private International Cartels 1990-2005*, (The American Antitrust Institute, AAI Working Paper No. #07-01, Jan. 2007) at Summary [hereinafter Connor Working Paper].

4 Countries with emerging market economies realize the benefits that competition laws can provide for the development process. Similarly, countries whose economies are in transition see competition policy as a vehicle for ensuring the operation of efficient markets and as a remedy for entrenched dominant position positions in specific industries. See John O. Haley, *Competition Law for the Asia-Pacific Economic Cooperation Community: Designing Shoes for Many Sizes*, 1 WASH. U. GLOBAL STUD. L. REV. 1, 2 (2002).

5 Scott D. Hammond, *Charting New Waters in International Cartel Prosecutions*, at the The Twentieth Annual National Institute on White Collar Crime (March 2, 2006), available at <http://www.usdoj.gov/atr/public/speeches/214861.htm>.

6 Ana Maria Alvarez & Pierre Horne, *Implementing Competition Law and Policy in Latin America: The Role of Technical Assistance*, 83 CHI.-KENT L. REV. 91, 98 (2008).

7 Richard Schwindt & Devin McDaniels, *Competition Policy, Capacity Building, and Selective Adaptation: Lessons from Japan's Experience*, 7 WASH U. GLOBAL STUD. L. REV. 35, 36 (2008). See Chinese Anti-monopoly law, available at http://www.lawinfochina.com/law/display.asp?db=1&cid=6351&keyword=anti_monopoly.

8 Stephen Harris, Jr. & Rodney Ganske, *The Monopolization and IP Abuse Provisions of China's Anti-Monopoly Law: Concerns and a Proposal*, 75 ANTITRUST L.J. 213 (2008).

9 As William Kovacic has noted, "A half-century ago, only one country, the United States, had antitrust statutes and active enforcement. Today over ninety jurisdictions have competition laws." William E. Kovacic, *Extraterritoriality, Institutions, and Convergence in International Competition Policy*, 97 AM. SOC'Y INT'L L. PROC. 309 (April 2-5, 2003).

anticompetitive conduct and compensate victims. While there have been significant strides in cooperation among government enforcement agencies, global mechanisms for private, civil enforcement must also keep pace to ensure that these goals are met.

I. THE PROBLEM OF SELECTIVE ENFORCEMENT

Inconsistent application of existing laws – and, indeed, the absence of competition legislation in many areas – has led to the problem of uneven regulation and enforcement of competition laws. This “selective enforcement” allows cartels, monopolists and other antitrust offenders to continue to be profitable operating on a global basis, despite facing stringent enforcement in certain jurisdictions. As Professor Eleanor Fox has described the problem:

In view of the fact that markets are global and law is national (or regional) only, there are obstacles to achieving consumers’ interest, efficiency, and innovation – all of which surpass borders. We are relegated to working out problems horizontally, nation to nation, or not working them out and letting the chips fall where they may. Often conflicts are observed, but only from a nation-centered perspective. Officials of one nation will notice an inconsistency within their own system, usually belatedly, often at the remedy stage, and these officials assume that if certain “thorns in the side” are removed (such as foreign injunctions against U.S. firms’ mergers, or mandatory injunctions compelling duties by a U.S. firm), the problem will be cured. This is an illusion. The particular compromises achieved are likely to be suboptimal, to reflect nationalism often masquerading in the name of competitiveness, and to feed the growing consolidation of industry.¹⁰

Deterring anticompetitive conduct thus requires a global cross-jurisdictional approach. It is now widely recognized that anticompetitive conduct can have a negative effect on a wide range of countries or regions, even if the conduct is targeted to only one, or a handful, of countries.¹¹ While this recognition has inspired efforts to converge competition rules toward international norms,¹² such uniformity for competition rules is still lacking.

Selective enforcement exists because the competition regimes of different countries or regions have different goals, informed by distinct societal and economic norms that impact policy considerations and, thus, levels of enforcement. Because different competition regimes have different goals, and each focuses on its own territory, it is not surprising that the intensity and scope of enforcement is widely divergent.

Exacerbating this problem are concerns about how one country’s competition policy can affect other countries, *i.e.*, “negative comity.”¹³ For example, under the Supreme Court’s comity analysis in *Empagran*, even where nations agree about primary conduct, such as price fixing, damages may be limited with respect to foreign nationals because United States trading partners may object to robust remedies allowed under U.S. law.¹⁴ This, in turn, encourages countries to refuse to hold U.S. entities liable in exchange for the U.S. not holding their companies liable for open market infringements. This negative comity then lessens the likelihood of effectively redressing or stopping international cartel activity.

¹⁰ Eleanor M. Fox, *Remedies and the Courage of Convictions in a Globalized World: How Globalization Corrupts Relief*, 80 *TUL. L. REV.* 571, 576-77 (Dec. 2005).

¹¹ According to Kovicic, “[t]he global expansion of competition law influences cross-border commerce. National or regional antitrust systems often endorse the comparatively broad view of extraterritoriality pioneered by the United States and the European Union (EU). This ensures that individual transactions or practices involving major suppliers of goods and services will be subject to scrutiny under the competition laws of more than one jurisdiction, and often many.” Kovicic, *supra* note 9.

¹² See *Id.*; *Foreign Law Year in Review: 2001*, 36 *INT’L LAW.* 879, 883 (2002).

¹³ See Fox, *supra* note 10, at 578.

¹⁴ See *Id.*

A. Global Price Fixing Cartels

1. Selective Enforcement Allows Cartels to Remain Profitable

One consequence of an increasingly interdependent marketplace is the rise of the international cartel,¹⁵ a problem made worse by the selective enforcement of cartel practices. While cartels are universally condemned,¹⁶ with enforcement in the European Union and other areas becoming increasingly more active,¹⁷ selective and inconsistent enforcement continues to make them profitable for the participants. For example, one need look no farther than the United States' antitrust enforcement scheme – one of the world's most comprehensive, featuring civil and criminal enforcement by federal, state, and private parties – to see the limitations national borders impose on international cartel enforcement. While the United States has enjoyed numerous recent successes against foreign and international cartels, enforcement by U.S. consumers alone, for the damage international cartels cause to them, may not sufficiently deter the cartels. If a cartel is made to pay damages solely for the harm it causes to a geographically limited group of consumers, it may still make enough wrongful profit worldwide to make violating competition laws economically attractive.¹⁸ As Circuit Judge Higginbotham noted, "Unless persons injured by the conspiracy's effects on foreign commerce could also bring antitrust suits against the conspiracy, the conspiracy could remain profitable and undeterred." *Den Norske Stats Oljeselskap As v. HeereMac Vof*, 241 F.3d 420, 435 (5th Cir. 2001) (Higginbotham, J., dissenting). Competition law enforcement must also become truly global to remove the overall profit from international cartels, and thus deter their formation. *See, e.g., Amicus Br. of Joseph E. Stiglitz and Peter R. Orszag, F. Hoffman-La Roche, Ltd. v. Empagran S.A.*, No. 03-724 (S. Ct. of the United States), at 3-5 ("If that aggregate expected punishment is smaller than the sum of the profits garnered in each nation, deterrence of the global cartel is inadequate and consumers everywhere will be harmed.").

National borders not only cause problems in the legal enforcement of cartels, but also create advantages that allow them to operate more effectively. Borders can prevent detection of a cartel by masking its geographical reach, thereby hindering discovery of illicit payments and international agreements on market allocations.¹⁹ In other words, globalization has allowed companies to operate and maneuver freely within the economy, but features inherent to national barriers also help provide protections for cartelists who operate internationally.

Despite the increased attention cartels have received from the international community, inconsistent under-enforcement on a worldwide basis makes the operation of a cartel worth the risk to the cartelist.²⁰ Current measures are not by themselves an adequate deterrence for cartelists, nor provide adequate compensation for consumers worldwide, and it is not surprising that recidivism "bedevils the international cartel scene."²¹

15 International-cartel discovery rates have been increasing since 1990, from four to six per year in the early 1990s to about 35 per year in 2003-2005. Connor Working Paper, *supra* note 3.

16 As the United States Supreme Court put it in *Verizon Commc'ns v. Trinko, LLP*, cartels are "the supreme evil of antitrust." 540 U.S. 398 (2004).

17 "The current message to large organisations emanating from both the EU and the UK Office of Fair Trading (OFT) about involvement in cartel activity is 'clean up your act or face both financial and criminal consequences.'" *Cracking Down on Cartels*, STRATEGIC RISK, Dec. 2007, available at <http://www.strategicrisk.co.uk/story.asp?storycode=368294>, (last visited July 28, 2008).

18 For example, in the case of the worldwide vitamins cartel, though defendants have paid criminal fines of approximately \$2.2 billion in the United States and overseas, and have settled civil lawsuits with domestic plaintiffs in the amount of approximately \$2.4 billion, those sanctions pale when compared to the profits of approximately \$18 billion, adjusted for inflation, which defendants reaped during the 1990s. *See Amicus Br. of Economics Profs. B. Douglas Bernheim, et al.*, at 9-11, *F. Hoffman-La Roche, Ltd. v. Empagran S.A.*, 542 U.S. 155 (2004) (No. 03-724). Thus, despite criminal and civil prosecutions more aggressive than those levied against any other cartel, defendants will still walk away with an estimated \$9 to \$13 billion in global profits by virtue of their cartel activity, more than double the fines and damages they have paid to date in all proceedings. *See Amicus Br. of Profs. Bush, et al., F. Hoffman-La Roche, Ltd.* 542 U.S. 155 at 4. As Professor Bush, *et al.*, noted, "These sanctions are much less than the amount needed to discourage future cartel formation." *Id.*

19 Jonathan T. Schmidt, *Keeping U.S. Courts Open to Foreign Antitrust Plaintiffs: A Hybrid Approach to the Effective Deterrence of International Cartels*, 31 YALE J. INT'L L. 211, 200 (2006) (internal citations omitted).

20 *See generally*, Connor Working Paper, *supra* note 3.

21 *Id.* For example, of the 11 companies with the worst record for repeat cartel offenses, each has been caught in at least 10 different cartels. As the authors note, however, "These 11 companies are simply the proverbial 'tip of the iceberg,' because we have found 174 documented instances of cartel recidivism; of these 86 companies recorded three or more cartel violations." *Id.*

2. Selective Enforcement Harms Regional And Global Economies

The lack of sufficient enforcement has grave consequences for the economic region the cartel affects, whether the cartel acts globally, regionally or locally. This is so because cartel activity necessary leads to a loss of competition, inefficient market outcomes,²² and therefore, an inefficient allocation of resources. Because national and regional economies are often intimately intertwined, a cartel in one country or region will in turn spread and affect other countries or regions.²³

The European Commission's White Paper on Damages Actions for Breach of the EC Antitrust Rules ("White Paper") finds, for example, that when looking at *domestic EU cartels*, the annual cost to consumers and other victims of hardcore cartels equals approximately €25 billion to €69 billion annually. Expressed as a proportion of the EU's gross domestic product, the negative welfare impact of all these hardcore cartels is estimated as ranging from 0.23% to 0.62% of EU's GDP in 2007 (and this only includes harm by cartels, not monopolies, etc.). Put even simpler, the potential benefits of enhanced private enforcement can be illustrated like this: if more effective competition mechanisms were to lead to a reduction of hardcore cartels by, for example, 5%, the negative consumer welfare impact would be reduced by €1.23 to €3.45 billion.²⁴

When looking at *global cartels*, the annual costs to EU consumers and other victims of hardcore cartels equals approximately €13 billion to €37 billion annually. This estimate comprises harm from consumers and other victims paying a high overcharge, and also economic benefits foregone by consumers, etc. who do not purchase due to the inflated price.²⁵

B. Abuse of Dominant Position

1. Reasons for Divergent Enforcement

Policy and enforcement issues are more complicated in cases involving an abuse of a dominant position than in cartel cases. In cases involving abuse of dominant position, the same behavior is often evaluated under different standards in different countries.²⁶ In fact, the difficulty that results from divergent standards of what constitutes improper unilateral conduct has been called the "the single most problematic [transnational antitrust issue] that exists . . ."²⁷ This problem arises primarily from the different policy, economic and legal considerations that shape competition enforcement across jurisdictions.

2. Policy Considerations

Underlying policy considerations often obscure enforcement because abuse of dominant position cases can involve other legal rights. Intellectual property rights – such as patents and copyright – effectively sanction a legal monopoly or claimant position, even if such a grant is only

22 "[T]here is near-universal agreement amongst economists that naked cartels result in inefficient outcomes." Richard Schwindt & Devin McDaniels, *Competition Policy, Capacity Building, and Selective Adaptation: Lessons from Japan's Experience*, 7 WASH U. GLOBAL STUD. L. REV. 35, 40 (2008).

23 See e.g., Margaret Levenstein & Valerie Y. Suslow, *Contemporary International Cartels and Developing Countries: Economic Effects and Implications for Competition Policy*, 71 ANTITRUST L. J. 801 (2004).

24 *Commission Staff Working Document accompanying document to the White Paper on Damages actions for breach of the EC antitrust rules*, Brussels, at 14-15, SEC (2008) 406 (Apr. 2, 2008) [hereinafter White Paper].

25 Several modern cartels provide similar examples. For example, in the electronics industry, several defendants have been investigated by authorities in both the U.S. and EU for their participation in multiple cartels affecting millions, if not billions, of dollars in sales across multiple continents. Manufacturers of DRAM, a variety of random access memory component that stores digital information and provides high-speed storage and retrieval of data used in personal computers, printers, digital cameras, wireless telephones, and other electronic devices, have been the subject of price-fixing investigations by both the United States Department of Justice ("DOJ") and the European Commission ("EC"). Several companies have already pled guilty in the United States and have paid hundreds of millions of dollars in fines.

Many of the same defendants were involved in a cartel in the SRAM market as well, which had an enormous impact on the European market. During the conspiracy period from 1999 through 2005, total European sales of SRAM are estimated to be €3.93 billion. SRAM Market Study Q4, 2004 (2005 sales are projected numbers). This represents approximately 20% of worldwide SRAM sales during this period. The impact of the conspiracy on SRAM prices was particularly dramatic in 2000, when average selling prices increased over 37% from \$3.93 per unit in 1999, to \$5.31 per unit in 2000. While prices later dropped in 2002, the SRAM manufacturers' cartel continued to maintain prices above what they otherwise would have been. The cartel in the polymethyl-methacrylate ("PMMA") market had a similarly massive impact. The number of EU purchasers of the PMMA affected by defendants' conspiracy is likely in the thousands. The EC, in its investigation, found that the PMMA cartel covered the whole of the European Economic Area ("EEA"), and that the 2000 EEA market value for the PMMA products involved was €665 million.

26 See Kovicic, *supra* note 9.

27 Diane P. Wood, *The U.S. Antitrust Laws in a Global Context*, 2004 COLUM. BUS. L. REV. 265, 272 (2004).

temporary. It can be a difficult policy determination to reconcile competitor enforcement with these IP protections. Similarly, the extent to which product bundling can be either a means to compete, or a means to suppress competition, has no simple answer. Different countries make different determinations when balancing such considerations against competition enforcement.

a. Economic Considerations and Legal Standards

National courts, regulators and legislatures take into account different economic considerations when determining what constitutes an abuse of dominant position. Each country or region that adopts a prohibition on abuse of dominant power adapts its interpretation of the law to its specific circumstances. For example, one of the stated goals of the new Chinese anti-monopoly law is to promote “the healthy development of the socialist market economy,”²⁸ which is not necessarily a goal adopted by many other competition regimes.

Different approaches to monopolization are not limited to those between transition economies, such as China, and more mature economies. Interpretative differences between ‘monopolization’ in the U.S. and ‘abuse of dominance’ in the EU, for instance, are now the areas of greatest difference between competition policies of the United States and Europe.²⁹ While both section 2 of the Sherman Act (the anti-monopolization statute in the United States) and Article 82 of the Treaty Establishing the European Community (the European statute prohibiting abuse of dominant market power) were “informed by a mixed set of socio-political-economic goals,”³⁰ those goals are actually quite different. Section 2 in the United States was created to combat the aggregation of power that undermines the ability of small market players to operate fairly within the market.³¹ Article 82 in the European Union, on the other hand, was adopted to help regulate dominant firms in an effort to protect powerless market actors such as buyers, suppliers, competitors, and consumers as part of the quest to achieve an integrated common market in Europe.³²

The differences in goals and standards between countries results in the uneven enforcement of unilateral anticompetitive conduct.³³ This different view of what constitutes abuse of dominant power, or monopolization, means that many companies – including IBM, Coca Cola, Microsoft, Intel and Apple – have come under scrutiny in one jurisdiction for conduct that is not investigated or regulated in other jurisdictions. For example, the European Union began an enforcement action against Intel for conduct that the United States initially refused to investigate.³⁴ Inconsistent application of the competition laws on a global scale can create unpredictable effects for the businesses involved, consumers, and overall legal enforcement.

2. Without Effective Enforcement, Abuse Of Dominance Harms Markets And Consumers

The difficulty countries have in determining what constitutes abuse of dominant position does not render its effect on markets any less pernicious.³⁵ With one entity abusing its dominant power in any given market, the economic efficiency of that market is greatly reduced. Horizontal competitors are restricted in their ability to enter the market, which interferes with their ability to

28 Anti-monopoly Law of the People's Republic of China, available at http://www.fdi.gov.cn/pub/FDI_EN/Laws/law_en_info.jsp?docid=85714.

29 Reza Dibadi, *Article 82 Gestalt, Myths, Questions*, 23 SANTA CLARA COMPUTER & HIGH TECH. L.J. 615, 617 (May 2007) (quoting William J. Kolasky, *What Is Competition? A Comparison of the U.S. and European Perspectives*, 49 ANTITRUST BULL. 29, 40 (2004)).

30 Eleanor M. Fox, *Monopolization, Abuse of Dominance, and the Indeterminacy of Economics: The U.S./E.U. Divide*, 2006 UTAH. L. REV. 725 (2006).

31 John J. Flynn, *Antitrust Jurisprudence: A Symposium on the Economic, Political and Social Goals of Antitrust Policy: Introduction*, 125 U. PA. L. REV. 1182, 1186-87 (1977); John J. Flynn, *The Reagan Administration's Antitrust Policy, "Original Intent" and the Legislative History of the Sherman Act*, 33 ANTITRUST BULL. 259, 290-300 (1988).

32 See Fox, *supra* note 30.

33 No less an authority than Herbert Hovenkamp has discussed the difficulties of defining what constitutes improper unilateral conduct. HERBERT HOVENKAMP, *THE ANTITRUST ENTERPRISE* 151 (2005) (“The very ubiquity and diversity of unilateral conduct render classification of offenses extremely difficult.”).

34 Only after a change in leadership at the FTC did it begin to investigate Intel, in June 2008. See Joel Hruska, *Intel Antitrust Woes Spread as FTC Launches Investigation*, ARS TECHNICA, June 6, 2008, available at <http://arstechnica.com/news/ars/post/20080606-intel-antitrust-woes-spread-as-ftc-launches-investigation.html>; Jeremy Reimer, *EU Slaps Intel with Formal Antitrust Charges*, ARS TECHNICA, July 26, 2007, available at <http://arstechnica.com/news/ars/post/20070726-eu-slaps-intel-with-formal-antitrust-charges.html>.

35 Remedies can only be effective if approached with a global view. “For every antitrust violation we need a remedy. Remedies are typically not satisfactory, leading to the angst of ‘Pyrrhic victories.’ Globalization is aggravating the problem.” Fox, *supra* note 10, at 572.

effectively compete within that market. With competition foreclosed in the market, consumers – much like consumers of a price-fixed product– pay higher prices than they otherwise would, and suffer from a reduction in quality as the incentive to innovate from the entity abusing its dominant market power is diminished.

With the continued globalization of economies over the last several decades, however, the effect caused by an entity abusing its dominant power will not be relegated merely to the area in which the abuser operates. Instead, the foreclosed market may initiate chain reactions that infect the market or closely similar markets in other countries or regions. When an entity abuses its dominant market power in one country or region, it may diminish consumer welfare in others.

II. GLOBAL PUBLIC REMEDIES FOR ANTICOMPETITIVE BEHAVIOR AS A SOLUTION TO SELECTIVE ENFORCEMENT

Resolution of the problem of selective enforcement must match the scope of enforcement to the scope of the violation. This increased public enforcement³⁶, and the corollary cross-border cooperation necessary to make the enforcement effective, must occur both in the criminal and civil arenas. Increased cooperation among enforcement agencies and an improved mechanism to resolve global private litigations are therefore necessary.

A. Cross-Border Cooperation in Public Investigations

Progress has already been achieved in the criminal enforcement of cartel behavior. In a recent and ongoing investigation into a bid-rigging cartel in the marine hose industry, for instance, governments from countries on three continents coordinated their regulatory enforcement activities to ensure that a global cartel was met with a unified, harmonized global criminal response.

In May 2007, eight executives from the United Kingdom, France, Italy and Japan were arrested in the United States and charged for their role in a conspiracy to rig bids and fix prices for marine hose.³⁷ The arrests in the United States were coordinated with raids in Europe and Japan. Assistant Attorney General Thomas O. Barnett emphasized the importance of cross-jurisdictional cooperation, stating that the arrests in combination with raids in the United States and abroad “demonstrate [the] ability to work effectively with foreign competition authorities to shut down international cartels.”³⁸

Nor did the cross-jurisdictional cooperation end with the raids. Immediately after pleading guilty in the United States to participating in the marine hose cartel, three executives were arrested in the United Kingdom for the same activity.³⁹ On June 11, 2008, the Southwick Crown Court in the United Kingdom handed down larger sentences for the three men than those to which they each had agreed under their American plea agreements.⁴⁰ As a result of cooperation between the United States and the United Kingdom, the defendants’ prison terms in the United States, the longest ever given to foreign nationals charged with antitrust offenses, were suspended in consideration for the time to be spent in prison in the United Kingdom – three years for two of the defendants and two and a half

36 There is no question, for example, that the European Commission is dedicated to the public enforcement of competition laws. Examples of industries that have most recently faced significant fines by the European Commission are those manufacturing elevators and switch gears. In the market for the installation and maintenance of lifts and escalators in Germany, Belgium, Luxembourg and the Netherlands, EU regulators imposed record fines totaling over €992 million on five manufacturers for their cartel participation. The largest fine of €479 million was imposed on ThyssenKrupp because the company was determined to be a price-fixing recidivist. In addition, Otis was fined €225, Schindler €144 million, Kone €142 million, and Mitsubishi’s Dutch subsidiary €1.8 million. See Press Release, Schindler, European Commission Drops Accusations of Pan-European Collusion (Feb. 21, 2007), http://www.schindler.com/group_news?news=88264. In the switch gears industry, Siemens was recently fined a total of €418 million, including €396 million in its Power Transmission and Distribution (PTD) division and €22 million against Siemens Austria. See *Siemens to Take EU Fine to European Court of Justice*, EU BUSINESS, Jan. 24, 2007, http://www.eubusiness.com/news_live/1169643624.79/.

37 Press Release, United States Department of Justice, Eight Executives Arrested on Charges of Conspiring to Rig Bids, Fix Prices and Allocate Markets for Sale of Marine Hose (May 2, 2007). Marine hose is a flexible rubber hose used to transport oil between tankers and storage facilities and buoys.

38 *Id.*

39 *U.S. Jail Time Suspended for British Cartel Members*, COMPETITION LAW 360 (June 27, 2008).

40 Hearing before His Honour Judge Geoffrey Rivlin QC, *Regina v. Whittle*, (June 11, 2008).

years for the third. Although the prison sentences in the United States were suspended, the three men still faced substantial fines ranging from \$75,000 to \$100,000 in the United States.⁴¹

Investigations such as the one into the marine hose cartel are not the only means through which governments have been working together to deter anticompetitive conduct. The United States also has entered agreements with several countries, including Japan, Brazil, Australia and the United Kingdom, to foster cooperation between governments for the investigation and prosecution of cartel activity.⁴² Through these agreements, and participation in inter-governmental groups such as the International Competition Network⁴³ and the ICN Workshop on Cartel Enforcement,⁴⁴ governments from around the globe have shown a keen interest in using coordinated criminal enforcement to stop cartels.

While cooperation in the criminal enforcement of anticompetitive conduct is helpful in deterring such conduct, cross border criminal enforcement has at least two flaws that inherently limit its effectiveness. First, government agencies, by their nature, are limited by political and practical considerations in terms of what cases they can and will pursue. Any enforcement agency has only a certain amount of resources at its disposal, which means that choices are made in terms of what conduct is or is not pursued. The problems with this type of selective enforcement can be magnified if a government has irrational, political or other incentives to discriminatorily protect one industry or company. The second major limitation of criminal enforcement is that the victims of the illicit conduct go uncompensated for the losses that result from the conduct. Civil enforcement, when used in conjunction with criminal enforcement efforts, is a necessary component of a complete structure of anti-cartel enforcement.

B. Expanding Private Enforcement of Anticompetitive Practices

Unlike criminal enforcement, private damage actions for cartel infringements have the advantage of being market-based rather than regulatory. They are directly related and proportionally correlated to the harm inflicted on the cartel's victims. Experience in the United States has shown how potent a weapon civil enforcement can be. There, the use of private damages actions accounts for approximately 90% of the means of ensuring compliance with the antitrust rules.⁴⁵ The current state of the law, in which there is no global mechanism to collectively address the victims harmed by anticompetitive conduct and limited extra-territorial jurisdiction for civil cases, is beginning to show signs of change, with select jurisdictions recognizing the value of collective redress.

1. First Steps in the European Union

On December 20, 2005, the European Commission published a Green Paper that addressed how to facilitate actions for damages caused by violations of the EC Treaty competition rules on restrictive business practices and abuse of dominant market positions (Articles 81 and 82 EC Treaty respectively). The Green Paper was part of an effort to learn from U.S. private damages actions and adapt similar, though not identical, approaches to the European setting.⁴⁶ As the European Commission noted:

Enhanced private enforcement will maximize the amount of enforcement as a means of enforcement additional to public enforcement. Increased levels of enforcement of the law will increase the incentives of companies to comply with

⁴¹ *U.S. Jail Time*, *supra* note 40.

⁴² Harvey I. Safenstein, *The Practical Aspects of Corporate Antitrust Compliance Programs*, 1426 PLI/CORP. 691, 859 (June 2004).

⁴³ See Hammond, *supra* note 5.

⁴⁴ R Hewitt Pate, of the United States Department of Justice, said at the 2004 ICN Cartel Workshop, "I can think of no better or more valuable substantive contribution to cartel enforcement than supporting this workshop." See, e.g., R. Hewitt Pate, *International Anti-Cartel Enforcement*, ICN Cartels Workshop (Nov. 21, 2004).

⁴⁵ W. Wils, *Should Private Antitrust Enforcement Be Encouraged in Europe?* (2003) 26(3) *WORLD COMPETITION* at 473.

⁴⁶ See, e.g., Commission of the European Communities, *Green Paper: Damages Actions for Breach of the EC Antitrust Rules*, COM (2005) 672 final (Dec. 19, 2005), available at http://eur-lex.europa.eu/LexUriServ/site/en/com/2005/com2005_0672en01.pdf; Commission Staff Working Paper, *Annex to the Green Paper*, SEC (2005) 1732 (Dec. 19, 2005), available at http://ec.europa.eu/comm/competition/antitrust/actionsdamages/sp_en.pdf.

the law, thus helping to ensure that markets remain open and competitive [F]acilitating private enforcement will add more frequently than before to the fines imposed by public competition authorities the possibility for the victim of the anti-competitive behaviour to recover his losses. Both damages awards and the imposition of fines contribute [to] the maintenance of effective competition and deter anticompetitive behaviour.⁴⁷

This initiative was driven by the recognition that, to date, there have been very few damages claims brought before courts of the Member States for breaches of the competition rules. For example, a study conducted on behalf of the European Commission found that private enforcement of European competition law through damages actions is relatively meager, and characterized the area as one of “total underdevelopment” and “astonishing diversity”⁴⁸. As England’s Office of Fair Trading recently reported:

It is notable that, so far, consumers appear to have obtained virtually no redress in private competition law actions. It is unclear how extensively businesses have obtained redress to date, given that few successful cases have been reported and that the details of any private settlements that have been reached are confidential.⁴⁹

Two and a half years later, on April 3, 2008, the Commission published the White Paper, discussed earlier, as a follow-up to the Green Paper, containing more detailed suggestions for new models to achieve compensation for consumers and businesses who are the victims of breaches of EC competition law. The White Paper includes suggestions for making damages claims by victims more viable and efficient, while ensuring respect for European legal systems and traditions. The model outlined by the Commission is based on compensation through single damages for the harm suffered.

The Commission’s move toward easing the way for civil litigations based on violations of competition law is based on the recognition that businesses and consumers harmed by anticompetitive activity are entitled to be compensated for their actual losses.⁵⁰ A more developed civil litigation mechanism will enhance the overall level of respect for the EC competition rules by discouraging companies from engaging in anticompetitive activity, which in turn will lead to the development of more fair and efficient markets and economies. Allowing for civil litigation also has the benefit of bringing the benefits of Community law closer to citizens.⁵¹

The Commission’s proposals effectively acknowledge that private enforcement of competition law, which compensates victims, discourages anticompetitive conduct and benefits the European Community at large, is underdeveloped at present in the European Union.⁵² The extent to which this situation is transformed by the Commission’s proposals remains to be seen. Even so, the Commission’s papers represent only the first steps needed to develop a comprehensive means of achieving legal redress for victims of anticompetitive behavior on a regional basis in Europe. Because of the fluidity of the current landscape, broader transnational solutions may be achieved through informal private settlement processes.

47 *Annex to the Green Paper*, *supra* note 47, at 6-7.

48 *See Study on the Conditions of Claims for Damages in Case of Infringement of EC Competition Rules*, Ashurst (Aug. 31, 2004), available at http://ec.europa.eu/comm/competition/antitrust/actionsdamages/economic_clean_en.pdf; *see also* Neelie Kroes, Member of European Commission in charge of Competition Policy, Opening Speech at European Parliament Workshop on Damages Actions for Breach of the EC Antitrust Rules: The Green Paper on Antitrust Damages Actions: Empowering European Citizens to Enforce Their Rights (June 6, 2006), available at http://ec.europa.eu/comm/competition/antitrust/actionsdamages/speech_06062006.pdf

49 Office of Fair Trading, *Private Actions in Competition Law: Effective Redress for Consumers and Business* at 8 (April 2007), http://www.offt.gov.uk/shared_offt/reports/comp_policy/oft916.pdf.

50 In its 2001 judgment, in *Covage v Crehan* (case C-453/99), the Court of Justice explicitly recognized a right to damages for breaches of EC competition law. The Court stated that:

the full effectiveness of Article [81] of the Treaty and, in particular, the practical effect of the prohibition laid down in Article [81](1) would be put at risk if it were not open to any individual to claim damages for loss caused to him by a contract or by conduct liable to restrict or distort competition. Indeed, the existence of such a right strengthens the working of the Community competition rules and discourages agreements or practices, which are frequently covert, which are liable to restrict or distort competition. From that point of view, actions for damages before the national courts can make a significant contribution to the maintenance of effective competition in the Community. *Id.*

51 *Competition: Commission launches consultations on facilitating damages claims for breaches of EU competition law*, IP/05/1634 (Dec. 20, 2005).

52 *See* Ashurst, *supra* note 49.

2. Private Actors are Seeking Solutions with Defendants

Recent experience in the United Kingdom reflects a greater opportunity for private settlement of competition law claims. Despite the relative lack of stand-alone or follow-on private actions for damages in the UK courts arising from breaches of competition law,⁵³ a number of private settlements of competition disputes have been concluded between 2000 and 2005.⁵⁴ These settlements primarily involved abuse of dominance cases, and almost half of the settlements consisted of a payment in lieu of damages or some form of agreement as to future conduct.

Cartel cases, however, have not seen quite the same success in terms of private settlement. From 2000 to 2005, approximately 50 infringement decisions were issued by the Commission and United Kingdom's Office of Fair Trading involving cartellists. There were nevertheless relatively few private cartel settlements, indicating that literally thousands of potential victims (including large, sophisticated companies) of the many cartels that have been uncovered have not yet taken action to recover their losses arising from the disclosed cartels. No formal, effective mechanism exists to ensure global peace for defendants while simultaneously providing collective redress. Victims of the illicit activity are left uncompensated, even though in many of these situations in which there is or has been a government investigation, there is little question as to the defendant's liability. Given the lack of a formal private mechanism for global settlement, private claimants have been forced to implement creative settlement structuring in an attempt to achieve global remedies.

From the perspective of the cartelist or the abuser of dominant power, however, a principal obstacle to reaching settlement with the victims of anticompetitive behavior is the difficulty illicit actors have in achieving global peace. Defendants have expressed a willingness to enter into private settlements, but only if they receive private peace for the entirety of the market impacted by the anticompetitive behavior. In other words, a private or alternative dispute resolution mechanism for achieving global settlements that provides finality and closure must be available to infringers. Without such a mechanism, settlement agreements that attempt to approximate a global resolution are the best agreements available to both claimant and defendant.

One recent groundbreaking case demonstrates how settlements affecting European businesses and consumers can be structured. In early 2008, a £73.5 million settlement was reached on behalf of UK air passengers in the price-fixing class action lawsuit brought against British Airways and Virgin Atlantic in the United States.⁵⁵ Under the terms of the settlement, passengers who purchased tickets from either airline for specified long-haul flights between August 11, 2004 and March 23, 2006 will be able to claim a partial refund. Passengers who purchased tickets from the airlines in the United Kingdom are entitled to a refund of 33.3% of the fuel surcharge they paid on each flight segment purchased. Passengers who purchased tickets in the United States will receive their partial refund (also 33.3% of the fuel surcharge paid on each flight segment) in dollars rather than pounds out of a separate \$59 million United States settlement fund. This unprecedented settlement represents the first instance in which multijurisdictional claims have been resolved simultaneously, providing equal compensation to both United States and United Kingdom classes of purchasers.

3. A Formal Mechanism is Still Needed for Civil Redress

The current approach that necessitates such creative settlement structures, however is not sufficient to guarantee a true global settlement. Rather, it represents the beginning of a more comprehensive compensation procedure. A formal mechanism to resolve global disputes is still needed, and any such mechanism should be collective in nature. Only a collective mechanism can provide adequate compensation for all victims and avoid the chilling effect that results from forcing

53 There have only been 15 final judgments in competition damages cases in the last 40 years in the UK, with only one 'fully' successful claim in any of the cases.

54 Rodger, *Private Enforcement of Competition Law, The Hidden Story* [2008] ECLR.

55 Danny Fortson, *UK businesses braced for class action suits after BA and Virgin pay out \$200m*, THE INDEPENDENT, Feb. 16, 2008, available at <http://www.independent.co.uk/news/business/news/uk-businesses-braced-for-class-action-suits-after-ba-and-virgin-pay-out-200m-783077.html>.

claimants to sue individually. Individual consumers alone have almost no chance of being able to bring cases against corporate players engaged in anticompetitive behavior. Potential plaintiffs, who often decide against litigation because the costs of bringing an antitrust claim greatly outweigh their damages, may be inclined to join a collective action because they can profit from the economies of scale. There is then a strong case for shifting the balance of litigation risk in favor of the “little” man and small business. Furthermore, because the decision to bring a suit to enforce private rights against illicit actors is market driven, rather than policy driven, a formal mechanism for collective redress avoids the flaws and deficiencies present with selective enforcement.

Any formal mechanism for collective redress will only work if there is some level of universal jurisdiction that allows for cases to be coordinated among civil litigants in different countries. One possibility would be to have a procedure similar to the Multidistrict Litigation Panel in the United States, through which related actions filed in different countries could be coordinated into one action.

In implementing this mechanism, it must be clear as a matter of policy that the dominance of the supply relationship cannot itself deter the enforcement of private rights. The biggest pragmatic obstacle to private enforcement is not procedural, it is the fear that pursuing their rights will interfere with a purchaser-claimants relationship with its supplier. Until this threat of supply retaliation is removed from the market, private enforcement will be inadvertently restrained, if not in whole, than at least in significant part.

In order to act as an effective means of collective relief, any formal mechanism also must address: (1) the need for an opt-out system, or its functional equivalent; (2) reducing the putative effect of so-called “loser pays” rules that are prominent in the European Union; (3) issues related to indirect purchaser compensation; and (4) the need for truly global settlements.

a. The Opt-out System

The U.S. currently employs an opt-out model for class actions, where one party litigates on behalf of a class of all similarly situated victims, with the exception of those who choose to exclude themselves. While the opt-out system may be unique to the United States, and potentially objectionable to many other jurisdictions, some procedure must be created that replicates its functionality. As an alternative to the opt-out system, the European Commission has suggested through the White Paper, for example, that there either be (1) representative actions; or (2) opt-in actions.

With respect to representative actions, the EC recommends that they be brought by qualified entities such as consumer associations, state bodies or trade associations, on behalf of identified or, in restricted cases, unidentified victims. Though this is a step in the right direction, it is imperative that such options ensure that these entities that will represent consumers not be defined too narrowly. If they are, the types of actions will be severely restricted. In order for any system with a representative action model to be truly representative, certain criteria are necessary to ensure that all parties are protected. First, representative entities should be independent from conflicts of interest from whom the entity seeks to represent and from those whom it may wish to engage to run the collective action on its behalf. Second, the entity should be able to show that they are able to pursue the litigation effectively (though not so tightly as to restrict consumer groups from sub-contracting litigation efforts to reputable lawyers). And third, entities should be able to show that they are reputable.⁵⁶

Similarly, an opt-in system will only be effective if those EU Member States that implement such systems publicize potential litigation to claimants. All bars to publication need to be lifted so as to allow claimants to know about, and choose to opt-in to an action. Moreover, the formalities for

⁵⁶ This would be consistent with the current UK's system for representative actions. John Pheasant and Anna Bicarregui, Hogan & Hartson, LLP, *Striking the right balance: towards a “competition culture” not a “litigation culture”?* Comment on the European Commission's White Paper on damages actions for breach of EC antitrust rules, at 8.

opting in must be minimal. There should not be extensive claim forms or payment of fees when opting in to an action. Without these provisions, opt-in actions will be unsuccessful – potential plaintiffs will have no notice of the action, and even if they do, they will be discouraged to join due to the administrative and financial burdens of opting in.

b. “Loser Pays” Rules

In contrast to the United States, many countries operate under loser pay cost structures that require losing litigants to pay for the legal costs of the winning party. This threat of having to pay substantial costs stifles claimants from bringing meritorious cases because the potential cost outweighs any potential gain a claimant may receive from a litigation. Any universal mechanism for collective redress must develop means of addressing this threat.

Some countries with loser pays rules have begun to realize the negative effect they have on private actions. The European Commission, for example, has recently encouraged national courts to exercise their discretion in assessing costs flexibly in order to protect claimants. This is not enough, however. Competition regimes should take additional steps to emphasize that individual consumers who are represented by an approved representative body should be protected for adverse costs completely (regardless of the outcome of the litigation).

c. Indirect Purchasers and the Passing-On Defense

Different countries hold different views on the viability of indirect purchaser claims against anticompetitive actors. Much discussion in the White Paper revolves around resolving how to allow both the direct and indirect buyers from a cartel to claim redress where the overcharge the cartel has caused has been extracted from a whole group of purchasers. The primary issue is how to address the passing-on of anticompetitive overcharges from direct purchasers to indirect purchasers. The White Paper, after weighing several options, suggests defendants should be entitled to rely on the passing-on defense against a claim for compensation of the overcharge, brought by a claimant who is not a final consumer.⁵⁷ It also suggests that an indirect purchaser should be able to rely on the rebuttable presumption that the illegal overcharge was passed on in its entirety down to his level.⁵⁸ In the United States, on the other hand, indirect purchasers can only recover for antitrust damages in select states, meaning that certain purchasers in the United States have no standing to sue for claims that are nearly identical to those for which their indirect counterparts would have standing.

d. Mechanisms for Global Settlements

With recent government activity, and increased inter-governmental cooperation to enforce competition laws, more private settlements related to anticompetitive behavior are needed. Such cases need not be based on illicit activity that occurs mostly in the United States. Claimants now are using new tools to seek redress from the cartel for their global anticompetitive activity. It is easy to imagine a worldwide cartel, for example, that engaged in anticompetitive activity with respect to a product sold throughout the world. (Such a cartel, may or may not, affect commerce in the United States.) Using a combination of private agreement between private litigants, implemented through the use of an independent evaluation, and the laws of the United States, the European Union and several Member States of the European Union, one settlement can be used to attempt to resolve a cartel's global liability. The current state of laws outside of the United States in general, and the use of an opt-in rather than an opt-out system in particular, does not guarantee global resolution, but it can eliminate most of a cartel's practical exposure and provide sufficient comfort to the cartel that it has been provided with a mechanism that effects collective redress.

For example, the parties can reach an agreement on general terms for an overall settlement prior to formally initiating litigation proceedings. The cartel can agree to pay, for instance, a set

⁵⁷ White Paper, *supra* note 24, at 65.

⁵⁸ White Paper, *supra* note 24, at 67.

percentage of its worldwide sales to its customers for the product affected by the anticompetitive conduct (an “overcharge percentage”), and agree to cooperate with claimants as they pursue non-settling cartelists. In exchange, the settling cartelist can receive a near-worldwide release from any potential liability (and concomitant damages) stemming from its anticompetitive activity. Notably, this can be achieved through a private contract that does not require court approval, although approval may be sought in certain cases. In order to achieve such a settlement’s desired goal of reimbursing all potential claimants for the harm suffered as a result of the conspiracy, the settlement may require multiple mechanisms for multiple jurisdictions.⁵⁹ One such mechanism can carve viable United States claims out of the worldwide settlement, which would allow such claims to move forward under the class action opt-out system in the United States.⁶⁰ (And just as with the air passenger case described above, claimants in different jurisdictions can receive refund payments in different monetary denominations.)

Other mechanisms can then be used to secure the release of and payment for claims not involving the United States through the use of a “claims made” system. For instance, the settling cartelist would deposit (or, in certain situations, guarantee) the settlement amount, excluding the amount related to claims that can be made in the United States (if any), in an account that will be made available to potential claimants until all applicable statutes of limitations have expired. Those victims who directly or indirectly purchased the product(s) affected by the anticompetitive behavior from the settling cartelist can then recoup a portion of the payments made for the product(s) (*i.e.*, the estimated overcharge) from the account. Such worldwide claims would require an extensive private or public notice program to inform potential claimants of their opportunities with settling cartelist. In order to allocate refunds to claimants, particularly in situations that are more complicated than the per-ticket purchased refund in the air passenger case, an expert can be appointed to effect proper allocation.⁶¹

As part of the settlement, the settling cartelist could also provide consideration other than reimbursement payments, such as an agreement to cooperate in the investigation of its co-cartelists and an agreement to participate in “funding.” By funding, the settling cartelist could agree to pay for the costs associated with losses in any litigation subsequently initiated outside the United States by settling claimants against the settling cartelist’s co-conspirators. Funding is necessary to avoid the risks associated with the “loser pays” rules in the United Kingdom and elsewhere. A financial arrangement can normally be established between the settling cartelist and a third party funder that allows the settling cartelist to offset some or all of the costs of funding. Moreover, cartelists who settle early can demand that their later-settling co-conspirators cover any funding costs for which the early settler (or settlers) was responsible and take over any future funding obligations. Thus, the funding requirement creates an incentive toward early settlement. Other incentives for settling early can include the application of a lower overcharge percentage compared with those who settle later, which would translate into a settlement discount and reduced interest payments for the early settler.

The air passenger settlement described above and the hypothetical description of a structure that allows for near-global settlement represent the beginning of what is possible, and necessary, to better redress anticompetitive activity around the globe. A universal settlement structure that allows for consistent civil enforcement of competition rules and a practical alternative to multiple universal jurisdiction highest certainty and formality with the least cost but virtually assured unacceptable option.

59 For instance, in the Netherlands, a mechanism exists for court approval of privately agreed settlements under the Dutch Act on Collective Settlement of Mass Damages (*Wet collectieve afwikkeling massaschade*). Under this mechanism, on April 11, 2007, Royal Dutch Shell plc announced that it had reached a settlement with a class of claimants in connection with the adjustments of its proven oil and gas reserves in 2004. Shell agreed to make a maximum payment of \$ 352.6 million, plus administrative costs, to the members of the class without admitting any wrongdoing.

60 The air passenger case demonstrates that United States claims do not have to be carved out. There, the court in the United States exercised jurisdiction over the foreign claims, but applied European Union law to the European claims. If the cartel is structured differently, however, it may be easier to treat the claims that are viable in the United States as completely separate from all other global claims. That allows for use of the class action mechanism already available in the United States without violating comity concerns.

61 Such a position is a normal feature of settlements in many areas of the economy in the United Kingdom. See generally JOHN KENDALL, *DISPUTE RESOLUTION: EXPERT DETERMINATION* (3rd Ed. 2001).

4. Access to Evidence Between Jurisdictions

Recent developments in both the United States and the European Union related to the ability of a party litigating in one country to get relevant discovery from a party in a different country demonstrate precisely how cross-jurisdictional cooperation can be both effective and efficient. The issue of “access to evidence” raises the question of how to strike a balance between (1) what are perceived as “excesses of the US system”, which supposedly lead to a party settling a case because of the expansive discovery requirements, and (2) the current rules in many countries, including several Member States of the European Union, where claimants do not bring actions because all the documentation and evidence is in the hands of the defendants.

In the United States, the Supreme Court has potentially expanded litigants’ ability to perform cross-jurisdictional discovery. See *Intel v. AMD*, 542 U.S. 241 (2004). *Intel* reaffirms that 28 U.S.C. Section 1782 allows for discovery of domestic entities by parties to foreign proceedings. In addition, the *Intel* decision opens the door for discovery of United States entities to be made at a very preliminary stage of litigation – potentially even before a foreign proceeding is actually filed.⁶² This enhances the ability of a litigant pursuing anticompetitive behavior on a global scale to conduct discovery of domestic parties where the lawsuit is intended to be, but has not yet been, filed in a foreign court.⁶³

Based on this Supreme Court decision, the Union Federal des Consommateurs – Que Choisir (the “QC”) recently sought cross-jurisdictional discovery in a motion filed with the *Intel* court earlier this year. The QC is a French organization that defends the rights of consumers in litigation against corporations, and pushes for public policies reinforcing the rights of consumers. The QC’s motion – currently *sub judice* – seeks permission to take discovery that will help it pursue cases against Intel in London, England and Lisbon, Portugal, which the QC intends to bring subsequent to an expected ruling adverse to Intel from the European Commission.⁶⁴ If granted, the QC motion will demonstrate that courts can, at the very least, coordinate their discovery efforts when a company’s anticompetitive conduct affects several countries.

Meanwhile, the EC, in an attempt to overcome the “information asymmetry” problem while “avoid[ing] the negative effects of overly broad and burdensome disclosure obligations”, suggests in the White Paper that across the EU, “a minimum level of disclosure *inter partes* for EC antitrust damages cases should be ensured.”⁶⁵ The White Paper states that national courts should have the power to order parties to disclose specific categories of relevant evidence, thus forming a judge-controlled disclosure of relevant evidence.

These recent developments in both the United States and the European Union only the beginning of what is needed for global civil enforcement. Cross-jurisdictional discovery is necessary to assist a case that may be progressing at different speeds in different countries, particularly where the activity at issue crosses borders.⁶⁶ Such cooperation should be used and expanded, but it is not a substitute for a true universal mechanism to achieve collective redress for victims of anticompetitive conduct.

62 In its broadest holding, the Court found that Section 1782 “does not limit the provision of judicial assistance to ‘pending’ adjudicative proceedings.” *Intel Corp. v. Advanced Micro Devices, Inc.*, 542 U.S. 241, 258 (2004). The Court instead held that a dispositive ruling by a tribunal – the European Commission in *Intel* – need only be “within reasonable contemplation.” *Id.* at 259.

63 According to the Supreme Court, Section 1782 does not contain a “foreign-discoverability” requirement that would necessitate a threshold showing by the party seeking discovery that the discovery sought must be discoverable in the foreign proceeding. Based on the language of Section 1782, “confirmed by its context,” the Court concluded that “the statute authorizes, but does not require, a federal district court to provide assistance to a complainant in a European Commission proceeding that leads to a dispositive ruling, *i.e.*, a final administrative action both responsive to the complaint and reviewable in court.” *Id.* at 255. Although the Court carved out privileged material from the statute’s aegis, it found nothing in either the text or the legislative history of Section 1782 that could be read to limit “a district court’s production-order authority to material that could be discovered in the foreign jurisdiction if the material were located there.” *Id.* at 260.

64 *Advanced Micro Devices, Inc. v. Intel, Corp.*, Civ Act. No. 05441-JJF, Reply Brief of Union Federal des Consommateurs – Que Choisir in Support of Its Motion to Intervene, 1-2 (July 16, 2008). The QC brought its brief seeking discovery under, *inter alia*, Section 1782.

65 White Paper, *supra* note 24, at 5.

66 *Ford v. F. Hoffman-LaRoche, Ltd.*, Sup. Ct. Justice File No. 771/99 (Ontario, Canada), Justice Cumming’s Reasons for Decision ¶ 45-49 at 13 (Jan. 26, 2001).

III. CONCLUSION

In an ever-changing world, principles of justice cannot change with borders. To provide justice, however, there must be meaningful access to achieve it. Justice must not only be equal for all, it must be equally available to all.

Modern globalized life, while increasing the integration of markets, has also brought with it an increase in the number and frequency of anticompetitive practices, affecting economies worldwide. Though some competition regimes have tradition of strict enforcement of competition laws, independent national enforcement of competition laws cannot alone deter global anticompetitive conduct. Without effective international cooperation and a global mechanism for private enforcement, anticompetitive behavior will not be deterred, and the grave effects on economies and citizens around the world will continue. So long as international selective enforcement of competition laws remains a problem, cartelists and monopolists will continue to distort entire markets, injuring *all* market players: large and small, companies and citizens.

RE-EXAMINING TRANS-ATLANTIC SIMILARITIES AND DIVERGENCES IN SUBSTANTIVE AND PROCEDURAL COMPETITION LAW

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I. INTRODUCTION

At first glance, there appear to be striking similarities between competition law in the US and in the EC, in particular as regards substance as opposed to procedure. The underlying legislative provisions, while different in wording, are roughly equivalent: they deal with restrictive agreements, exploitative unilateral behaviour and anticompetitive mergers. In more recent years both jurisdictions have apparently been pursuing common objectives, namely the maximisation of efficiency and consumer welfare. In relation to procedural law, some similarities can also be found: while criminal sanctions are not available at EC level for violations of the competition law, the European Commission ('the Commission') has not been afraid to impose severe financial penalties on those undertakings that have breached the competition law rules; and to this extent, then, they are not unlike their opposite number in America. Furthermore, there have been moves by the Commission to encourage the use of private actions within the EC Member States; such actions are regularly employed to enforce competition law in the United States. While comments in the US media concerning the interventionist, and perceived anti-business, aspect to EC antitrust and merger law are not uncommon – and in the context of the history of EC competition policy may not be completely unwarranted – there is more commonality between the competition laws of these jurisdictions than there is conflict.

That is not to say, however, that important differences do not exist. In fact, there are a number of differences concerning not only the substantive application of the competition law rules, but also the procedures employed. Cases involving such notable parties as Microsoft and GE/Honeywell, among others, have highlighted these differences. Substantive differences exist concerning bundling, predation, the licensing of intellectual property rights and the assessment of conglomerate mergers. Integrationist objectives, present in EC jurisprudence, are absent in the US. Furthermore, differences in attitudes and culture have also influenced European approaches to procedural issues. The reticence of the vast majority of the EC Member States to introduce class actions or treble damages for private plaintiffs who have been injured due to anticompetitive conduct is an obvious example. So too perhaps is the prevailing attitude in Europe concerning the use of criminal sanctions for the punishment of individuals who have engaged in the most egregious forms of anticompetitive behaviour, such as operating a hard-core cartel, or even concerning the offer of immunity for cartel whistle-blowers. That said, some other procedural differences may merely be superficial; the difference between the effects test and the implementation test in the context of the extra-territorial application of the competition law provisions may well fall into this category, although such a proposition has yet to be tested by the Community Courts.

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An important question that should be posed here is whether these substantive and procedural differences are a problem. That is, are they so significant that they amount to a problem that needs to be 'solved'? How do we solve it? Can cooperation help? Is convergence an answer? If so, what rules exactly should converge and to what standard: US, EU, or some other 'best practice'? And perhaps even more difficult, how does one achieve such convergence in practice? This paper will attempt to address these issues. Before doing so however, it will consider the current similarities and differences between US and EC competition law. The paper, then, is divided as follows: Part II compares the substantive competition laws; Part III compares the procedural competition laws; and Part IV considers the issue of future conflict between US and EC competition law. Finally, it is submitted that, while some further cooperation/convergence may be desirable, if it is to occur it must be done in a coherent, consistent and coordinated manner, all the while respecting the sovereignty of all jurisdictions involved.

II. COMPARING THE SUBSTANTIVE COMPETITION LAWS

This part of the paper compares the substantive aspects of both US and EC competition law. The comparative analysis provided deals with restrictive agreements, unilateral anticompetitive behaviour and merger control, respectively.

A. Restrictive Agreements

Restrictive agreements are prohibited under both US and EC competition law. According to the US Sherman Act of 1890 '[e]very contract, combination . . . or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations' is unlawful. In order to avoid an over-inclusive law, the US Supreme Court interpreted this provision as prohibiting only those agreements which impose an 'unreasonable' restraint of trade.¹ There are two broad categories of agreements, both with different methodologies for determining reasonableness. There are those agreements that are assumed to unreasonably restrain trade; such per se illegal agreements display a 'pernicious effect' on competition, do not possess redeeming features and do not warrant an elaborate investigation of the precise harm they engender.² They include agreements relating to hard-core cartels, that is, those cartels that aim to fix-prices, divide markets, restrict output or bid-rig.³ In order to be considered to be per se illegal, an agreement must be manifestly anti-competitive;⁴ it must not only be a 'naked restriction on trade' but must also lack a plausible efficiency justification.⁵ The second category of agreements is the default category;⁶ it concerns those that are considered under the 'rule of reason'. These types of agreements may be deemed to be largely pro-competitive, even if they also exhibit a certain restraining effect on competition in a given market.⁷ The rule-of-reason approach traditionally required a full analysis of the economic effects of an agreement, where the pro- and anti-competitive aspects of the agreement are weighed against one another.⁸ However, a 'quick look' approach to the rule-of-reason has also developed in recent years;⁹ accordingly, the analysis of economic effects is not as robust where a 'great likelihood of anticompetitive effects can easily be ascertained'.¹⁰

The wording of the EC provision on restrictive agreements, namely Article 81 EC, is quite different to that of Section 1 of the Sherman Act. Article 81(1) EC prohibits agreements between undertakings, decisions of associations of undertakings, and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market. This provision details a non-exhaustive list of agreements which may be prohibited. Article 81(2) EC provides that such agreements are to be void and unenforceable. Article 81(3) allows for a limited exemption from Article 81(1) if the agreement

1 *Standard Oil Co. v. United States* 221 U.S. 1(1911), at 56.

2 *Northern Pacific Railway v. United States* 356 US 1 (1958), at 5.

3 See, e.g. *United States v. Socony Vacuum Oil Co.* 310 US 150 (1940), at 210; *United States v. Addyston Pipe & Steel Co.*, 85 F. 271 (6th Cir. 1898), aff'd as modified, 175 U.S. 211 (1899).

4 *GTE Sylvania* 433 U.S. 36 (1977), at 49-50.

5 *Broadcast Music Inc. v. Columbia Broadcasting System, Inc.* 441 U.S. 1 (1979).

6 A. Abbott (2005a), 'A Brief Overview of American Antitrust Law', The University of Oxford, Centre for Competition Law and Policy, The Competition Law & Policy Guest Lecture Programme - Paper (L) 01/05, 2005, at 6.

7 *Board of Trade of City of Chicago v. United States* 246 US 231 (1918).

8 A. Abbott (2005a), *op. cit.*, at 9.

9 *Ibid.*, at 9. See *National Society of Professional Engineers v. United States* 435 U.S. 679 (1978); *National Collegiate Athletic Association v. Board of Regents of University of Oklahoma* 468 U.S. 85 (1984).

10 *California Dental Association v. FT* 526 U.S. 756 (1999).

(a) contributes to improving the production or distribution of goods or to promoting technical or economic progress, while (b) allowing consumers a fair share of the resulting benefit, and does not (c) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives, or (d) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

Community law employs a taxonomy of agreements that is very similar to that which exists under US federal law, particularly so following Modernisation.¹¹ Agreements which have as their 'object' the restriction of European competition do not warrant an effects-based analysis; they are the European equivalent of agreements that are considered to be per se illegal in the US. Cartel agreements (which in Europe, like in the US, are considered to be the 'supreme evil of antitrust'¹²) and agreements that compartmentalise the common market are included within this category. By contrast, agreements which under EC law have as their effect the restriction of competition in the common market can be compared to those agreements subject to the rule-of-reason under US law. While the EC approach here is not identical to the US rule of reason,¹³ its underlying philosophy – revealed by *inter alia* its understanding of competitive harm,¹⁴ as well as its requirement that efficiency benefits be real and verifiable,¹⁵ is 'very much in keeping with American antitrust analysis'.¹⁶ Above all, it is in the area of 'effects' where a number of recent reforms have, on the whole, brought about greater convergence with US law with its stronger focus on economic principles and consumer welfare maximisation.¹⁷ In particular, the Verticals Block Exemption Regulation¹⁸ that was adopted in December 1999 injected a significant degree of economic-based thinking into the analysis of the beneficial effects of certain types of vertical restraints; the Guidelines on Article 81(3) also played their part. Indeed, legislation on horizontal cooperation agreements, agreements of minor importance, and technology transfer have all helped to establish 'a European policy approach towards agreements between firms that is more economics-based in terms of its priorities, processes and substantive case analysis'.¹⁹

One area where EC law has *not* been aligned with American antitrust reflects the geographical and political differences between the American federal state and the supra-national entity that is the European Community: European competition law has been traditionally hostile to agreements that are perceived as having a negative impact on the objective of free market integration, irrespective of efficiency analyses.²⁰ Community Courts jurisprudence from cases such as *Consten and Grundig*,²¹ *Delimitis*,²² *Pronuptia de Paris*²³ and *Parker Pen*²⁴ support this assertion. Even after the adoption of a consumer welfare approach by the Commission, such hostility is still evident in the treatment of agreements that provide absolute territorial protection to undertakings.²⁵ This traditional hostility was recently tempered somewhat in *GlaxoSmithKline Services Unlimited v. Commission*.²⁶ Although the agreement in question in that case was found to have as its object the restriction of parallel trade, it was held that according to the particular operative facts the welfare of final consumers

- 11 See, e.g. European Commission, *Guidelines on the Application of Article 81(3) of the Treaty*, 2004/C. 101/08, 27 April 2004 ('Guidelines on the Application of Article 81(3)').
- 12 This quote is taken from the Supreme Court judgment in the case *Verizon Communications v. Law Offices of Curtis v. Trinko*, 540 US 398 (2004), at 408. Under EC law, price-fixing agreements are 'by their very nature the worst kind of violations of Article 81': *POI/Thread*, Case COMP/38.337, Summary of Commission Decision of 14 September 2005 relating to a proceeding under Article 81 of the EC Treaty and Article 53 of the EEA Agreement, at paragraph 18.
- 13 In fact, the Court of First Instance has recently dismissed the existence of the rule-of-reason in the context of Article 81(1) EC: Case T-328/03, *O2 (Germany) GmbH & Co. OHG v. Commission* [2006] ECR II-1231, at paragraphs 66 to 71.
- 14 See, e.g. *Guidelines on the Application of Article 81(3)*, at paragraph 24.
- 15 See, e.g. *ibid.*, at paragraph 56.
- 16 A. Abbott (2005b), 'A Brief Comparison of European and American Antitrust Law', The University of Oxford, Centre for Competition Law and Policy, The Competition Law & Policy Guest Lecture Programme - Paper (L) 02/05, 2005, at 6.
- 17 That said, a vigorous policy of anti-cartel enforcement has also played its part: M. Bloom, 'Substantial Antitrust Convergence: Developed Country Antitrust Enforcement is Converging on a Consumer Welfare Basis', Speech, ABA Antitrust Section Spring Meeting, Washington, DC, 30 March 2005, at 7.
- 18 European Commission, *Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices*, Official Journal, L 336/21, 29 December 1999 ('the Verticals Regulation').
- 19 J. Vickers, 'Abuse of Market Power', Speech to the 31st Conference of the European Association for Research in Industrial Economics, Berlin, 3 September 2004, at 2; www.ofc.gov.uk/shared_ofc/speeches/spe0304.pdf.
- 20 See P. Marsden and P. Whelan, 'The "Consumer Welfare" Standard as a Form of Substantive Protection for Consumers under European Competition Law', Chapter 16, *Own Labels, Branded Goods and Competition Policy: The Changing Landscape of Retail Competition*, Ezrachi & Bernitz (eds), Oxford University Press, Oxford, 2009. Nonetheless, restrictions on competition that have adverse effects across US state lines are subject to possible censure under the Commerce Clause of the US Constitution, which gives Congress plenary power to regulate interstate commerce: A. Abbott (2005b), *op. cit.*, at 18.
- 21 Cases 56 and 58/64, *Etablissements Consten SA and Grundig-Verkaufs-GmbH v. Commission* [1966] ECR 299.
- 22 Case C-234/89, *Delimitis v. Henninger Bräu* [1991] ECR I-935.
- 23 Case 161/84, *Pronuptia de Paris GmbH v. Pronuptia de Paris Irmgard Schillgallis* [1986] ECR 353.
- 24 Case T-77/92, *Parker Pen v. Commission* [1994] ECR II-549.
- 25 The Verticals Regulation, at Article 4(b).
- 26 Case T-168/01, *GlaxoSmithKline Services Unlimited v. Commission* [2006] ECR II-2969.

could not be assumed to be adversely affected; the agreement therefore could not be prohibited solely on the grounds of its 'object'. This case, then, on its face at least seems to be at odds with earlier rulings such as *Consten and Grundig*, where no economic analysis of the welfare effects of agreements restricting parallel trade was conducted or required. It may however merely constitute an 'exceptional' case, and one that is confined to the specific characteristics of the pharmaceutical market.²⁷ Whether that is the case or not remains, for the moment at least, uncertain.

What is clear, in any case, is that such integrationist concerns are nowhere near as strong under US antitrust law. Indeed, following *GTE Sylvania*²⁸ non-price vertical restraints, including those imposing exclusive territories, are dealt with in the US using a rule-of-reason approach; this is due to the influence of 'Chicago School' economics.²⁹ The treatment of such vertical non-price restraints in the courts since that case was decided is such that commentators have claimed that they are almost considered to be per se lawful.³⁰ By contrast, and like the situation prevailing in Europe, until very recently vertical price, as opposed to non-price, restraints were considered to be per se illegal in the US.³¹ However, following the decision of the US Supreme Court in *Leegin*, minimum resale price maintenance is now to be judged under the rule of reason.³² European competition law has not yet followed suit. To date these sorts of vertical price restraints have not been tolerated in Europe. The attitude of the European authorities to such restraints is evident in its Verticals Block Exemption Regulation, where although some types of vertical agreements were exempted from Article 81(1) in order to respect modern economic theory, vertical restraints imposing fixed and minimum prices were not, irrespective of the market shares of the undertakings involved.³³ This fact demonstrates that, despite the more economics-based approach taken in relation to, amongst other things, vertical agreements, as well as the apparent adoption of a consumer welfare standard,³⁴ the Commission has not completely rejected legal formalism.³⁵ The US, by contrast, feels no real attachment to such formality in the context of vertical restraints.

B. Unilateral Behaviour

Unilateral anticompetitive conduct is an area of competition law where significant differences exist between the EC and the US. Article 82 EC, the European counterpart to Section 2 of the US Sherman Act 1890, prohibits an abuse by one or more undertakings of a dominant position within the common market. The non-exhaustive list of examples in this article resembles almost word for word the examples set out in Article 81(1). The prohibition of exploitative abuses, something that on its face is provided for in Article 82(a), and which is notably absent in US law, can be understood as an example of where ordoliberal standards may be implied by the competition provisions: it reflects the ordoliberal principle of forcing dominant firms to act as if they were operating under complete competition.³⁶ Article 82 EC has not yet been interpreted by the Community Courts as having as its sole or primary object the maximisation of consumer welfare.³⁷ To date it has been consistently interpreted by these Courts as a measure that aims to protect the competitive structure of the market, the so-called 'institution of competition', and to thereby support the economic freedom of undertakings to enter and compete in a given market irrespective of their efficiency; this is apparent in early competition cases such as *Commercial Solvents*,³⁸

27 A. Jones and B. Sufrin, *EC Competition Law*, Oxford University Press, 2007, at 231.

28 *GTE Sylvania* 433 US 36 (1977).

29 On the Chicago school of economic thought, see R. Bork, *The Antitrust Paradox*, Basic Books, New York, 1978; R. Posner, 'The Chicago School of Antitrust Analysis' (1979) 127 *University of Pennsylvania Review* 925; and E. Fox, 'The Modernisation of Antitrust: A New Equilibrium' (1981) 66 *Cornell Law Review* 1140.

30 A. Abbott (2005b), *op. cit.*, at 6.

31 See, e.g., *Dr. Miles Medical Co. v. John D. Park & Sons Co.* 220 US 373 (1911), at 407-408.

32 *Leegin Creative Leather Products, Inc. v. PSKS, Inc.* 551 U.S. (2007).

33 The Verticals Regulation, at Article 4(a).

34 On this see P. Marsden and P. Whelan (2009), *op. cit.*; M. Hutchings and P. Whelan, 'Consumer Interest in Competition Law Cases' (2006) 16(5) *Consumer Policy Review* 182; and P. Marsden and P. Whelan, 'Consumer Detriment' and its Application in EC and UK Competition Law' (2006) 27(10) *European Competition Law Review* 569.

35 E. Buttigieg, 'Consumer Interests under the EC's Competition Rules on Collusive Practices' [2005] *European Business Law Review* 643, at 717. See also Case 322/81, *Nederlandsche Banden-Industrie Michelin NV v. Commission* [1983] 3461; and Case T-219/99, *British Airways v. Commission* [2003] ECR II-5917 (CFI); and Case C-95/04 P, *British Airways v. Commission* [2007] ECR I-2331 (ECJ).

36 C. Ahlborn and C. Grave, 'Walter Eucken and Ordoliberalism: An Introduction from a Consumer Welfare Perspective' (2006) 2(2) *Competition Policy International* 19.

37 P. Marsden and P. Whelan (2009), *op. cit.*

38 Case 6-7/73, *Istituto Chimioterapico Italiano Spa and Commercial Solvents Corporation v. Commission* [1974] ECR 223.

Hoffmann-La Roche,³⁹ *United Brands*,⁴⁰ and *Michelin I*.⁴¹ These cases represent a triumph for ordoliberal ideas⁴² in that they are primarily concerned with the restriction of the individual actions of competitors and not with the overall impact of unilateral conduct on economic welfare.⁴³ Consequently, they adopt very formalistic approaches to certain economic activities undertaken by a dominant undertaking, such as the granting of loyalty rebates for example. This remains the situation at present despite the fact that the Commission's preference for a consumer welfare approach in EC competition law started to take shape in the mid to late 1990s.⁴⁴ Cases such as *Michelin II*,⁴⁵ *IMS Health*,⁴⁶ *France Telecom*,⁴⁷ and *British Airways*,⁴⁸ for example, support this point. Even after the publication of DG-Competition's Discussion Paper on Article 82 in December 2005⁴⁹ - a document that purportedly advocates the maximisation of consumer welfare as the primary objective of Article 82 - the Court itself has had the opportunity to expressly adopt and mandate the employment of a consumer welfare approach in the context of abuse of dominance, but it refused to do so.⁵⁰

The US provision on unilateral conduct, by contrast, does not use the words 'abuse of a dominant position'. Rather it speaks of 'monopolization'. Section 2 of the Sherman Act makes it unlawful to '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, or with foreign nations'. The mere existence of monopoly does not violate the Sherman Act;⁵¹ only conduct that can be interpreted as 'monopolisation' or an 'attempt to monopolise' is caught by the prohibition.⁵² In other words, it is the nature of the conduct that is at issue and not merely the status of an operator on the market. The reasoning behind this approach concerns innovation: 'To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive conduct'.⁵³ As is obvious from the wording of Section 2, such conduct can consist of an attempt to monopolise. US law differs from EC law in this regard. Under the European competition law rules, an abuse can only be found once dominance is established; attempts to achieve dominance are not unlawful. In the US, by contrast, the anticompetitive conduct of a non-dominant firm can be subject to the prohibition in Section 2 of the Sherman Act, if such conduct would enable the firm to achieve a monopoly in a given market.⁵⁴ The European Commission cannot depend on Article 82 EC to prevent the creation of monopolies; its ex ante powers only exist in relation to the control of anticompetitive mergers, as provided by the European Community Merger Regulation.⁵⁵ For one legal commentator at least, this limitation goes some way to explaining European aggressiveness towards single firm conduct.⁵⁶

According to current authority, monopolisation contrary to Section 2 occurs where: (1) monopoly power is possessed in the relevant market; and (2) there has been 'willful acquisition or maintenance of that power, as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident'.⁵⁷ Unlawful conduct under the second element is confined to exclusionary conduct - there is no equivalent in US federal law to Article 82(a) EC. Exclusionary conduct is conduct that 'exclude[s] rivals on some basis other than efficiency';⁵⁸ in

39 Case 85/76, *Hoffmann La Roche v. Commission* [1979] ECR 461.

40 Case 27/76, *United Brands v. Commission* [1978] ECR 207.

41 Case 322/81, *Nederlandsche Banden-Industrie Michelin NV v. Commission* [1983] 3461.

42 The theory of ordoliberalism holds that it is incumbent upon the state to create a proper legal environment for the economy and to maintain a healthy level of competition through measures adhering to market principles: E. Megay, 'Anti-Pluralist Liberalism: The German Neoliberals' (1970) 85(3) *Political Science Quarterly* 422.

43 Cf. T. Eilmansberger, 'How to Distinguish Good from Bad Competition under Article 82: In Search of Clearer More Coherent Standards for Anticompetitive Abuses' (2005) 42 *Common Market Law Review* 129, at 138.

44 See, e.g., J. Kallaugher and B. Sher, 'Rebates Revisited: Anti-Competitive Effects and Exclusionary Abuse Under Article 82' (2004) 25(5) *European Competition Law Review* 263.

45 Case T-203/01, *Michelin v. Commission* [2003] ECR II-4071.

46 Case C-418/01, *IMS Health GmbH & Co OHG v. NHC Health GmbH & Co KG* [2004] ECR I-5039.

47 Case T-340/03, *France Télécom SA v. Commission* [2007] ECR II-107.

48 Case T-219/99, *British Airways v. Commission* [2003] ECR II-5917 (CFI); and Case C-95/04 P, *British Airways v. Commission* [2007] ECR I-2331 (ECJ).

49 European Commission, *DG Competition Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses*, Brussels, December 2005.

50 Case C-95/04 P, *British Airways v. Commission* [2007] ECR I-2331.

51 It is also true that dominance per se is not prohibited under EC law. Indeed, it is the abuse of a dominant position, and not the existence of that dominant position, that is unlawful.

52 *Standard Oil Co. v. United States* 221 U.S. 1 (1911), at 62.

53 *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko* 124 S.Ct. 872, (2004), at 879.

54 A. Abbott (2005b), *op. cit.*, at 13.

55 Council of Ministers, *European Community Merger Regulation*, OJ L 24, 29.01.2004, 1-22 (hereafter 'the ECMR').

56 A. Abbott (2005b), *op. cit.*, at 13.

57 *United States v. Grinnell Corp.* 384 U.S. 563 (1966), at 570-71. See also *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko* 124 S.Ct. 872, at 878-79.

58 *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.* 472 U.S. 585 (1985), at 605.

determining whether it is present the authorities usually employ the 'no economic sense' test: conduct is deemed to be exclusionary if it makes no economic sense for the firm to engage in it but for the tendency of that conduct to lessen competition.⁵⁹ By employing such a test the US authorities only sanction inefficient conduct; conduct that is efficient is outside of the scope of Section 2 irrespective of its impact on the economic freedom of other actual or potential operators in the market. Unlike EC law, then, the objective behind the US provision on unilateral conduct is the protection of efficiency and therefore the maximisation of welfare; concerns for equality and freedom do not form part of the analysis. The Chicago School of economics is the dominant influence; unlike in Europe, *ordo-liberalism* has no part to play in assessing the lawfulness of unilateral conduct.

As the respective EC and US provisions on unilateral conduct pursue different aims, it would be no surprise if a given conduct were treated differently depending on the applicable (EC/US) law. Indeed, differences concerning various practices can be detected in the jurisprudence, including in relation to bundling,⁶⁰ fidelity rebates,⁶¹ and essential facilities,⁶² to name a few. The concept of predation, however, provides a sufficient illustrative example for present purposes. Under US law, predation – that is, the selling of a product below a determined level of cost – is not unlawful unless there is a likelihood of recoupment.⁶³ In other words, the authorities must demonstrate that there is a reasonable prospect that the alleged predator would be able to recoup its investment in below-cost prices. This requirement reflects the Chicago School belief in the inherent self-correcting mechanism that is the market: if monopolists cannot recoup their losses later, then it must be due to the existence of (actual or potential) competitive restraints; if such competitive restraints exist in the market, the consumer will not be harmed by any increased prices of the monopolist. The EC authorities do not exhibit such faith in the market. They believe that when predation occurs it is based on a factual assumption that below cost pricing can be a rational strategy adopted by a dominant firm to eliminate competitors.⁶⁴ Therefore, under the EC competition law rules, a demonstration of the possibility of recoupment is not required.⁶⁵ Consequently, it is easier to establish a predation case in Europe than it is in the US.⁶⁶ In the US, the prohibition on predation is rarely, if ever, enforced: apparently there have been no successful prosecutions for predatory pricing in the US since the case of *Brooke Group Ltd.*⁶⁷ The concept of predation, as interpreted by the US authorities, therefore illustrates another feature of the Chicago School and US enforcement in general, particularly as regards unilateral conduct, *viz.*, an aversion to intervention.

C. Mergers

There has been considerable convergence between the EC and US merger control laws over the last number of years. In the US, Section 7 of the Clayton Act 1914 prohibits the acquisition of share capital or assets 'where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition'. Under the European Community Merger Regulation,⁶⁸ which was amended in 2004, concentrations (i.e. mergers, acquisitions and full-function joint ventures) that have a Community dimension⁶⁹ are prohibited by the Commission if they 'would significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position'.⁷⁰ The substantive tests of both jurisdictions have now converged: the

59 See *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko* 124 S.Ct. 872, at 878-79.

60 See, e.g. N. Economides and I. Lianos, 'The Elusive Antitrust Standard on Bundling in Europe and in the United States at the Aftermath of the Microsoft Cases', NET Institute Working Paper No. 07-47, January 2008; available online at: <<http://ssrn.com/abstract=1078932>>.

61 See, e.g. V. Auricchio, 'Discount Policies in US and EU Antitrust Enforcement Models: Protecting Competition, Competitors or Consumer welfare?' (2007) 3(2) *European Competition Journal* 373.

62 See, e.g. U. Muller and A. Rodenhuisen, 'The Rise and Fall of the Essential Facility Doctrine' (2008) 29(5) *European Competition Law Review* 310; and A. Capobianco, 'The Essential Facility Doctrine: Similarities and Differences Between the American and the European Approach' (2001) 26(6) *European Law Review* 548.

63 *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.* 509 U.S. 209 (1993). Recently, the Supreme Court confirmed that predatory buying also requires proof of recoupment: *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.* 127 S. Ct. 1069 (2007).

64 H. Schweitzer, 'Parallels and Differences in the Attitudes Towards Single-Firm Conduct: What Are The Reasons', EUI Working Paper, LAW No. 2007/32, 2007, at 31.

65 See Case C-62/86, *AKZO Chemie BV v. Commission* [1991] ECR I-03359; and Case C-333/94 P, *Tetra Pak v. Commission* [1996] ECR I5951.

The EC test for predation was recently restated by the CFI: Case T-340/03, *France Télécom SA v. Commission* [2007] ECR II-107.

66 See J. Temple Lang and R. O'Donoghue, 'Defining Legitimate Competition: How to Clarify Pricing Abuses under Article 82 EC' (2002) 26 *Fordham International Law Journal* 83, at 142.

67 D. Evans and J. Padilla, 'Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach' (2005) 72 *University of Chicago Law Review* 73, at 88.

68 Council of Ministers, *European Community Merger Regulation*, OJ L 24, 29.01.2004, 1-22 (hereafter 'the ECMR').

69 This is determined by turnover thresholds; *ibid.*, at Article 1.

70 ECMR, Article 2(3).

'significant impediment of effective competition' (SIEC) test is 'substantively identical' to the 'substantial lessening of competition' (SLC) test.⁷¹ The EC Horizontal Merger Guidelines⁷² are also similar in their structure and substance to the guidelines issued by the Department of Justice and the Federal Trade Commission.⁷³ This is manifest in relation to concentration levels, the determination of efficiencies, the interpretation of the relevant substantive tests and the distinction between coordinated/non-coordinated effects.

There has also been an increasing sophistication in the economic analyses undertaken by the Commission,⁷⁴ as evidenced by cases such as *Sony/BMG*⁷⁵ and *Oracle/PeopleSoft*.⁷⁶ This helps to bring EC merger law more in line with its US counterpart. Other factors that have led to convergence are the adoption of the Commission Notice on Market Definition⁷⁷ (which advocates the use of the SSNIP test) and the creation of the post of Chief Economist within DG-Comp in 2003. According to Abbott, while substantive convergence has undoubtedly occurred, it does not necessarily follow that we will eventually reach a point in time when no differences will exist between these laws;⁷⁸ for him, there are three important reasons why this is so:⁷⁹ (i) the EC takes far more consideration of the views of competitors than the American authorities when assessing mergers;⁸⁰ (ii) the EC enforcers have a tendency to employ economics in a different manner to their US counterparts; and (iii) the EC enforcement officials are receptive to non-standard theories and may as a result prohibit mergers that have no short term harm for consumers. For these reasons,⁸¹ then, substantive analyses may not be identical in practice between the US and the EC authorities, despite convergence on the theoretical frameworks.

It is hoped nonetheless that the convergence identified above will lead to less conflict when international or Trans-Atlantic mergers are contemplated. There is one particular area of merger control law, however, where potential still exists for serious conflict: non-horizontal (i.e. vertical and conglomerate) mergers. Indeed, the last occasion when major differences of opinion were aired across the Atlantic on merger control law concerned a transaction that required vertical and conglomerate effects analyses: *GE/Honeywell*.⁸² Following the outcome of that case, as well as *TetraLaval/Sidel*,⁸³ the European Commission adopted its Guidelines on Non-Horizontal Mergers.⁸⁴ These guidelines are a reminder from Brussels that non-horizontal mergers are on the radar of the Commission. By contrast, the US over the last two decades or more has adopted a rather cautious approach to non-horizontal mergers. The Department of Justice guidelines⁸⁵ on this area of merger control are widely believed to be outdated and provide very little guidance on what vertical mergers will be challenged.⁸⁶ Nonetheless, there is general agreement in the US that non-horizontal mergers pose far less competition problems than horizontal mergers. Indeed, it has been several decades since the agencies have challenged a conglomerate merger.⁸⁷ The US Antitrust Modernization Commission believed that such mergers 'generally do not raise antitrust issues'.⁸⁸ Given that the Commission is far more open to challenging such mergers than the US authorities, it is not difficult to foresee potential conflicts sometime in the future on this issue.

71 Wilmer Cutler Pickering Hale and Dorr LLP, *Guide to EC Merger Regulation*, Fourth Edition, at 41; and M. Bloom, *op. cit.*, at 14.

72 European Commission, *Horizontal Merger Guidelines*, Official Journal C 31, 05.02.2004, 5-18.

73 See the 1997 *Horizontal Merger Guidelines of the Department of Justice and the Federal Trade Commission*, available at www.usdoj.gov/atr/public/guidelines/horiz_book/hmg1.html.

74 See M. Bloom, *op. cit.*, at 14.

75 Case No COMP/M.3333, *Sony/BMG*, 2004.

76 Case No COMP/M.3216, *Oracle/PeopleSoft*, 2004.

77 European Commission, *Notice on the Definition of the Relevant Market for the Purposes of Community Competition Law*, OJ C372, 9/12/97, 5.

78 A. Abbott (2005b), *op. cit.*, at 14.

79 *Ibid.*, at 14-16.

80 On this problem, see P. Whelan, 'The Role of Third Parties in the Competition Enforcement Landscape: A Critical Review of Recent and Possible Future EC Developments' [2007] *Competition Law Journal* 41, at 50.

81 And others, such as when geographical markets are national or regional, or when effects are only felt in one jurisdiction; A. Abbott (2005b), *op. cit.*, at 17.

82 See Case COMP/M.220, *General Electric/Honeywell*, Commission Decision, 3 July 2001; and Case T-210/01, *General Electric v. Commission* [2005] ECR II-5575.

83 Case T-5/02, *Tetra Laval BV v. Commission* [2002] ECR II-4381.

84 European Commission, *Guidelines on the Assessment of Non-Horizontal Mergers under the Council Regulation on the Control of Concentrations between Undertakings*, 28 November 2007, Brussels, available at: <http://ec.europa.eu/comm/competition/mergers/legislation/nonhorizontalguidelines.pdf>.

85 United States Department of Justice, *Non-Horizontal Merger Guidelines*, 14 June 1984; available at: www.usdoj.gov/atr/public/guidelines/2614.htm.

86 See e.g. the comments of R. Pitofsky in Federal Trade Commission, *Federal Trade Commission 90th Anniversary Symposium, A Conversation with Tim Muris and Bob Pitofsky*, 2004, at 172; www.ftc.gov/ftc/history/transcripts/040922transcript003.pdf.

87 S. B. Volcker, H. Schneider and L. B. Greenfield, 'EU Commission Adopts Non-Horizontal Merger Guidelines', 3 December 2007; www.wilmerhale.com/publications/whPubsDetail.aspx?publication=8145.

88 Antitrust Modernization Commission, *Antitrust Modernization Commission: Report and Recommendations*, 2 April 2007, at 68;

http://govinfo.library.unt.edu/amc/report_recommendation/chapter1.pdf.

III. COMPARING THE PROCEDURAL COMPETITION LAWS

This part of the paper compares the procedural aspects of both US and EC competition law. The comparative analysis provided deals with a number of important issues such as notification requirements, sanctions, private enforcement, extra-territorial jurisdiction and merger control procedures.

A. Notification Requirements

Prior to the entry into force of Regulation 1/2003 on 1 May 2004,⁸⁹ there was a major procedural difference between EC and US law as regards the treatment of restrictive agreements: anticompetitive agreements that were in violation of Article 81(1) EC had to be notified to the Commission in order to benefit from an exemption under Article 81(3).⁹⁰ If the agreement merited an exemption, then the Commission may have decided to issue a decision in that regard. More likely, however, was the issuance of a non-binding comfort letter. National courts were prohibited from applying Article 81(3) EC and therefore if such an issue arose in a case before it - for example, if a defendant claimed that he should not have to perform a contract he previously agreed to as it was in violation of Article 81(1) and the plaintiff argued that the agreement should be exempt - the court was required to suspend its proceedings and request the Commission to rule on the particular issue. Quite obviously, this was a very inefficient manner of dealing with restrictive agreements. It also operated as an obstacle to the use of private enforcement actions within the Member States. By adopting Regulation 1/2003, the Council of Ministers abolished this notification regime, and with it the monopoly of the Commission as regards the application of Article 81(3).⁹¹ Consequently, from 1 May 2004 onwards courts in the Member States, like their counterparts in the US, have been able to rule on whether restrictive agreements are on the whole beneficial or detrimental as regards welfare levels, and therefore whether or not they should be void and unenforceable.

B. Sanctions

EC sanctions for anticompetitive agreements are also similar to those which are imposed in the US. Unlawful restrictive agreements are void and unenforceable. Fines are imposed by the authorities, and injunctions may be available. A major difference, however, is that the fines imposed in the US are not administrative in nature. In fact, the US authorities do not have the power to impose an administrative fine. Rather, if fines are imposed, they must be imposed by a court of law and they are criminal in nature. Both individuals and corporate bodies can be subject to such fines. Indeed, in the US individuals can be forced to serve a term of imprisonment of up to ten years for violating Section 1 of the Sherman Act.⁹² At EC level only administrative fines can be imposed;⁹³ they are not criminal in nature, at least not according to the traditional concept of 'criminality'.⁹⁴ The Commission has no power at present to impose fines on individuals, although some have argued that the EC Treaty does not need to be amended for such powers to be granted to this authority.⁹⁵

Criminal antitrust penalties, including imprisonment, exist in a number of Member States, such as Ireland, the UK, Estonia and Germany; they only apply to hard-core cartel type behaviour. In the US, in theory at least, unilateral anticompetitive behaviour, that is monopolisation, can also result in a criminal trial and the imposition of criminal punishment on both a corporate body and an individual. That said, it has been at least thirty years or more since a criminal fine has been imposed for violation of Section 2 of the Sherman Act.⁹⁶ Indeed, it is now current policy for the Antitrust

89 Council of Ministers, *Council Regulation (EC) No 1/2003 of 16 December 2002 on the Implementation of the Rules on Competition Laid Down in Articles 81 and 82 of the Treaty*, (2003) Official Journal L1/1 ('Regulation 1/2003').

90 See EEC Council, *Regulation No 17: First Regulation Implementing Articles 85 and 86 of the Treaty*, OJ 13, 21.2.1962, p. 204-211, at Article 4.

91 Regulation 1/2003, at Article 6.

92 Antitrust Criminal Penalty Enhancement and Reform Act of 2004, Pub. L. No. 108-237, 118 Stat. 661.

93 Regulation 1/2003, at Article 23(5).

94 The sanction may be criminal for the purposes of Article 6 of the European Convention on Human Rights. See Case C-199/92 P. *Hüls v. Commission* [1999] ECR I-4287, at paragraphs 149-150; and Case C-235/92 P. *Montecatini v. Commission* [1999] ECR I-4539, at paragraphs 175-176. See also P. Whelan, 'Protecting Human Rights in the Context of European Antitrust Criminalisation', in I. Lianos & I. Kokkoris (eds), *The Reform of EC Competition Law: Towards an Optimal Enforcement System*, Amsterdam, Kluwer International, 2009, forthcoming.

95 See, e.g., W. Wils, 'Is Criminalization of EU Competition Law the Answer?' (2005) 28(2) *World Competition* 117; and P. Whelan, 'Contemplating the Future: Personal Criminal Sanctions for Infringements of EC Competition Law' (2008) 19(2) *King's Law Journal* 364.

96 S. Weber Waller, 'Remedies for Monopolization and Abuse of Dominance: A Little History and Some Thoughts on Disclosure and Access', paper presented at 'Antitrust Marathon (Part II): The Long Plod to Greater Understanding on Section 2/Article 82', Competition Appeal Tribunal, London, 11 April 2008.

Division of the Department of Justice not to prosecute those who have violated Section 2.⁹⁷ Instead, other remedies such as injunctions, divestment, the licensing of IP rights, and other behavioural and structural measures are imposed in this context. The EC, by contrast, is capable of imposing fines on undertakings who have abused a dominant position; and indeed they have done so on a number of occasions including in the *Microsoft* case.

When the US authorities impose fines for violation of Section 1 of the Sherman Act, like the European Commission, they are restricted concerning the level of the fine. The latter authority must ensure that the fine imposed, whether for violation of Article 81(1) or of Article 82, does not exceed 10% of the gross global turnover of the undertaking for the last business year.⁹⁸ Furthermore, by establishing a set of guidelines on the fines to be imposed in antitrust cases, the Commission binds itself to a particular methodology due to the operation of the principle of legitimate expectations. Although US Federal Guidelines exist, they are merely a guide and do not have to be adhered to by the judiciary.⁹⁹ But no maximum figure in percentage terms exist as regards a US fine; only maximum dollar (and prison term) amounts are provided.¹⁰⁰ These dollar amounts are \$100 million for a company and \$1 million for an individual. The US authorities may exceed these limits when they impose a fine that is equal to twice the gain of the offender or twice the loss to the victim.¹⁰¹ The 10% cap in the EC has not prevented the Commission from imposing very large fines in appropriate cases, fines which are often in the hundreds of millions. Cartel cases, in particular, often result in heavy fines. To this extent, then, there is a definite degree of similarity between the practice of the US and of the EC.

C. Private Enforcement

A notable difference in antitrust procedure, however, concerns the use of private enforcement, more particularly the use of private damages actions, as a means of ensuring compliance with the antitrust rules. In the US, approximately 90% of enforcement is done by way of private damages actions.¹⁰² Opt-out class actions are allowed, and treble damages are paid out to victims who can establish a claim. Standing is not available to the so-called indirect purchaser,¹⁰³ but the 'passing-on defence' cannot be relied upon by an infringer and therefore does not reduce the amount that a direct purchaser may be able to claim.¹⁰⁴ As an exception to the usual asymmetric cost rules that exist in the US, successful plaintiffs may be able to recover their costs including a reasonable attorney's fee.¹⁰⁵ Liberal discovery rules are also a feature of the US regime. To avoid abuse of the mechanism of private enforcement, the US courts have developed the concept of 'antitrust injury': plaintiffs can only sue for the type of damage that the antitrust statutes were designed to prevent.¹⁰⁶

In Europe, by contrast, private enforcement is in a highly underdeveloped state.¹⁰⁷ Major obstacles to the use of private actions have been identified, including weak discovery rules, uncertainty over the passing-on defence and indirect purchaser standing, and the unavailability of collective actions. The extent to which these obstacles exist depends on the particulars of the different legal regimes in each of the Member States. The European Commission, after analysing the US approach to antitrust enforcement, has recently attempted to encourage private damages actions in Europe, although not all commentators have been receptive to this idea.¹⁰⁸ With its Green Paper¹⁰⁹ and White Paper¹¹⁰ on damages actions respectively, the Commission proposed options for consultation and

97 US Department of Justice, *US Department of Justice, Antitrust Division Manual*, 3d edition, 1998, at Chapter III, Section C.5; available at www.usdoj.gov/atr/foia/divisionmanual/ch3.htm#c5.

98 Regulation 1/2003, at Article 23(2).

99 *U.S. v. Booker*, 543 U.S. 220 (2005).

100 See Antitrust Criminal Penalty Enhancement and Reform Act of 2004, Pub. L. No. 108-237, 118 Stat. 661 (codified as amended in scattered sections of 15 USC).

101 Criminal Fines Improvement Act of 1987, Pub. L. 100-185, 100 Stat. 1280 (codified as amended in 18 USC Section 3571).

102 W. Wils, 'Should Private Antitrust Enforcement Be Encouraged in Europe?' (2003) 26(3) *World Competition* 473, at 476; and S. C. Salop and L. J. White, 'Economic Analysis of Private Antitrust Litigation' (1986) 74 *Georgetown Law Journal* 1001.

103 *Illinois Brick v. Illinois* 431 US 720 (1977).

104 *Hannover Shoe v. US Machinery* 392 U.S. 481 (1968).

105 Section 4(a) of the Clayton Act, 15 USC 15(a).

106 *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.* 429 U.S. 477 (1977).

107 Ashurst, *Study on the Conditions of Claims for Damages in Case of Infringement of EC Antitrust Rules*, 31 August 2004, http://europa.eu.int/comm/competition/antitrust/others/private_enforcement/index_en.htm.

108 See, e.g., Wils (2003), *op. cit.*

109 European Commission, *Green Paper – Damages Actions for Breach of the EC Antitrust Rules*, COM(2005) 672, Brussels, 19 December 2005.

110 European Commission, *White Paper – Damages Actions for Breach of the EC Antitrust Rules*, COM(2008) 165 Final, Brussels, 2 April 2008 (the 'White Paper').

advocated action concerning these options. Notably, however, the Commission did not believe that double damages should be imposed on infringers in order to compensate the victims of anticompetitive behaviour.¹¹¹ Unlike the US, however, the Commission was prepared to see pre-judgment interest paid on awards of damages,¹¹² which arguably reduces in any case the need for double, or indeed treble, multipliers.¹¹³ The Commission also failed to see the value of having US-style class actions operate in Europe; for it the appropriate approach in Europe would be the combination of two mechanisms: representative actions brought by qualified entities; and opt-in collective actions.¹¹⁴ It is believed that these mechanisms will avoid the excesses of the US system, such as those related to the principal-agent problem that may exist between the lawyers and the victims.¹¹⁵ As a result of the European Court of Justice's judgment in the *Manfredi* case,¹¹⁶ it is likely that the indirect purchaser should be granted standing in a private damages action. In order to maintain consistency with the primary objective of private enforcement, as understood by the Commission, the passing-on defence should be allowed,¹¹⁷ something that the Commission has advocated in its White Paper.¹¹⁸ Whether these proposals will eventually be adopted by the Member States, or indeed whether they will be mandated to adopt them through a Directive, remains for the moment an unanswered question. Likewise, whether further or indeed any convergence on this issue between the regimes in the Member States and the US regime will occur in future is also a topic subject to conjecture.

D. Extra-Territoriality

One area of procedural law where the US approach has perhaps been influential is in relation to extra-territorial jurisdiction, in particular its use of the 'effects' test. The European Court of Justice ('ECJ') has so far refused to expressly adopt an effects-based test of jurisdiction. Up to now it has always been possible in Article 81 and Article 82 cases to decide the jurisdictional question on other grounds. In both the *Dyestuffs*¹¹⁹ and *Wood Pulp*¹²⁰ cases the effects doctrine was argued at length before the Court, but the European Court of Justice essentially avoided the issue: the Court neither expressly adopted nor rejected the US test. In *Wood Pulp*, however, an 'implementation' test was adopted. The Court of First Instance ('CFI'), in relation to proceedings under the European Community Merger Regulation, also dodged the pertinent question and denied itself the opportunity to expressly rule on the validity and desirability of an effects-based test.¹²¹ Despite a reticence by both Courts to expressly adopt the effects test, it can be argued, especially after *Gencor*,¹²² that the 'implementation' doctrine is almost identical to the effects test. It is difficult to resist the conclusion that *direct sales* into the Community (by a foreign company engaged in concerted practices outside the EC) will be enough to establish the implementation requirement, especially when one remembers that the ECJ stated that an undertaking's presence in the EC (through subsidiaries etc.) is immaterial.¹²³ It is submitted that if direct sales into the Community equals implementation then implementation is almost identical to effects, as effects can be measured by reference to sales within the Community.¹²⁴ Some commentators are of the view that the ECJ has already adopted the effects test – albeit implicitly.¹²⁵ According to Van Gerven, the Court 'adopted the effects test without due justification and qualification', as it failed to establish a sufficient link between the alleged conduct and the Community.¹²⁶ It is submitted that, even if one is wrong about

111 *Ibid.*, at paragraph 2.5.

112 *Ibid.*

113 See R. H. Lande, 'Are Antitrust "Treble" Damages Really Single Damages' (1993) 54 *Ohio State Law Journal* 115, where he argues that, due to the absence of pre-judgment interest in the US, treble damages actually equate to single damages.

114 The White Paper, *op. cit.*, at paragraph 2.1.

115 On the difficulties that US class actions may engender, see Howrey's Antitrust Practice Group, 'Trends in Antitrust Litigation: The New Breed of Class Action'; www.howrey.org/docs/ARA2005USPrivate.pdf. Some have argued that the fear of Europeans in this regard is not warranted and that the debate on class actions needs to be more balanced; see e.g. G. Schnell, 'Class Action Madness in Europe - A Call for a More Balanced Debate' (2007) 28(11) *European Competition Law Review* 617.

116 Joined Cases C-295/04 to C-298/04, *Manfredi* [2006] ECR I-6619.

117 See P. Whelan, 'Defences That Are Appropriate in Follow-On Damages Actions', paper presented at the UKAEL Conference: 'Competition and Private Enforcement: The Next Steps', University College London, 4 July 2008, at 8.

118 The White Paper, *op. cit.*, at paragraph 2.6.

119 Case 48/69, *JCI v. Commission* [1972] ECR 619.

120 Cases 89/85, 104/85, 114/85, 116-17/85, and 125-29/85, *A. Ahlström Osakeyhtiö v. Commission* [1988] ECR 5193.

121 Case T-102/96, *Gencor v. Commission* [1999] ECR II-753.

122 *Ibid.*

123 Van Gerven believes that such a conclusion would be erroneous, as direct sales do not 'constitute a sufficiently close and relevant link with the regulating State that is compelling enough to justify jurisdiction on its part': W. Van Gerven, 'EC Jurisdiction in Antitrust Matters: The *Wood Pulp* Judgment' [1989] *Fordham Corporate Law Institute* 451, at 470.

124 Cf. E. Fox, 'The Merger Regulation and its Territorial Reach: *Gencor Ltd. v. Commission*' (1999) 20(b) *European Competition Law Review* 334, at 336.

125 R. Higgins, *Problems and Process: International Law and How We Use It*, New York: Oxford University Press, 1994, at 75 (The ECJ has 'adopted the effects test in all but name').

126 W. Van Gerven, *op. cit.*

the exact jurisdictional scope an implementation test allows, the courts would expressly adopt an effects test if it were required. Such a situation could possibly occur in the case of a foreign cartel that refuses to sell into the Community. If it did so, the artificial difference that currently exists between US and EC law on this point would disappear.

E. Merger Procedures

Finally, a note on merger procedures is warranted. Like in the EC under the ECMR, mergers that fulfill certain criteria (detailed in the Hart-Scott-Rodino Act) must be notified in the US before they can be completed. To that extent then there is similarity between both jurisdictions. Nonetheless, there are quite a number of different jurisdictional and procedural differences between the merger regimes established by these respective pieces of legislation. For example, in the EC, concentrations with a community dimension fall within the sole jurisdiction of the European Commission, while in the US the federated states share jurisdiction over mergers with the federal authorities. Also, the jurisdictional thresholds for pre-merger notification in the US are different than those that are detailed in the ECMR. For example, in the EU these thresholds are based solely on the size and location of an undertaking's turnover, while in the US, by contrast, the size and location of assets is also taken into account. The definition of the concept of 'control' under the US regime is also different than its European counterpart: in the US it exists with a 50% equity shareholding, whereas in the EC 'decisive influence' is what matters. Consequently, a concentration may be deemed to exist in the EC when less than 50% of the shares are held by one entity.

The mere filing of a merger under the Hart-Scott-Rodino Act must be kept confidential by the authorities, unlike in Europe. The filing requirements in each jurisdiction are also quite different. In particular, 'second requests' do not exist under the ECMR. Although the EC considered adopting a two-step approach, it ultimately decided to reject it.¹²⁷ For this reason, Form CO is far more taxing than the premerger notification form that is used to comply with the Hart-Scott-Rodino Act.¹²⁸

Importantly, mergers are prohibited in the US by a court of law; in the EC, by contrast, the Commission, an administrative body, decides on their compatibility with EC law.¹²⁹ A formal hearing may be conducted by the Commission roughly two weeks following the issuance of the Statement of Objections. At this hearing unsworn testimony is taken from the parties as well as other interested persons, which may include both customers and competitors. But it should be understood, however, that this process is not the equivalent to a trial in the United States: the testimony is not sworn and there is no cross-examination.¹³⁰ While a hearing officer exists to ensure that the proceedings are conducted in a fair manner, he/she has no authority to make a decision on the lawfulness of the concentration.¹³¹

Furthermore, there are differences in the time periods during which the authorities need to make their decisions. Article 10 ECMR imposes strict time periods which can only be tolled for a finite period; the consent of the parties is required. But under the Hart-Scott-Rodino Act, the deadline for the final decision may be tolled without limit provided the parties consent to this. Finally, the European Commission is required, in all cases, to take a decision on the merger. Indeed, unlike under the American legislation, a failure to issue a decision by the relevant deadline ensures that the concentration is cleared in the form originally notified. As stated above, then, significant procedural differences exist with regard to merger control.

IV. AVOIDING FUTURE TRANS-ATLANTIC CONFLICTS

This part considers the issue of possible future conflicts between the US and the EC concerning the enforcement of their respective competition laws. It is divided into three sections. Section A sets out the potential for concern in this area. Section B details the (limited) usefulness of

¹²⁷ European Commission, *20th Report on Competition Policy*, Brussels, 1990, at 36.

¹²⁸ See J. Parisi, 'A Simple Guide to the EC Merger Regulation of 2004' (January 2005) *The Antitrust Source*, at 5.

¹²⁹ The Commission's decision may be appealed to the Court of First Instance under Article 230 EC.

¹³⁰ See J. Parisi, *op. cit.*, at 7.

¹³¹ *Ibid.*

bilateral cooperation agreements in reducing these concerns. Finally, and in a similar vein, Section C considers the concept of multilateral convergence.

A. Potential for Concern

In recent years we have witnessed the rather speedy globalisation of the world, with firms that traditionally focused on national markets taking their operations 'global'. Indeed, it is clear that multi-jurisdictional business activity has expanded dramatically, particularly over the last decade. As a result of these international business strategies, a growing interdependence between national/regional markets has developed. Furthermore, profound changes in business activity, driven by improvements in technology, communications and transport, continue to occur, and markets continue to evolve. As stated by Friedman, the global market is increasingly composed of 'new players, on a new field, developing new processes and habits for horizontal collaboration'.¹³² Isolated and distinct economies are now a thing of the past; and the world can in fact be seen to be 'flat'.¹³³ The US and the EC, as two of the largest economies in the world, have inevitably been affected by this flattening effect of globalisation. Companies that operate in such an environment will have to comply with a number of different competition laws from different countries, and multinational companies that operate in Europe as well as in the US will have to stay within the respective antitrust and merger laws of both of these jurisdictions. Even where EC companies are not present in the US market, they may nonetheless be subject to US antitrust law if their business practices have effects on the US economy, i.e. due to the operation of the concept of extraterritoriality. This situation, then, provides the context for a possible conflict between the enforcement of the US and the EC competition laws.

As explained above, there are quite a number of similarities in the competition rules of both the US and the EC. These similarities exist in both substantive and procedural law. As for substantive law: cartels are not tolerated; restrictive agreements should lead to a reduction in welfare before they are deemed to be unlawful; and merger control is concerned with protecting competition on the merits and not with protecting competitors. With procedural law, similarities include: an effects-based jurisdictional test (in substance if not form); the use of a prohibition, as opposed to a notification, regime with restrictive agreements; severe financial sanctions; and an *ex ante* notification merger control regime. But even with such similarities, however, it is possible that different results will occur in any given case: different agencies may well come to different (reasonable) conclusions on the lawfulness of a given behaviour, particularly if they have their own unique manner of applying economics, as explained above in relation to merger control. It is also true, of course, that differences in the competition laws can be detected and that these differences are capable of leading to a Trans-Atlantic conflict. Conflict could occur, for example, where the US allows a particular practice but the EC prohibits it, and where the company/companies involved decide(s) to abandon on *both* the EC and US markets what the US authorities consider to be an efficiency-enhancing practice.

One particular area of concern that should be noted in this regard is the assessment of unilateral behaviour. As stated above, the US and EU competition rules on unilateral conduct appear to follow different objectives. The US rules are concerned solely with the maximisation of consumer welfare, while those in the EU protect the economic freedom of actors on a given market. Furthermore, the European model is arguably more interventionist. In contrast to the US authorities, who are concerned primarily with type-one errors (i.e. false positives), the European Commission is most anxious about type-two errors (i.e. false negatives); hence the more interventionist approach in the context of unilateral conduct.¹³⁴ Intervention may also be more likely in the EC as this jurisdiction has many more former state-owned monopolies that need to be 'dealt with' than the US.¹³⁵ It is here, then, that conflict is most likely, and that convergence is most desirable.

But should European competition law follow the American example here and pursue an enforcement standard based solely on consumer welfare maximisation? While opposition to such a

¹³² T. Friedman, *The World is Flat, A Brief History of the Twenty-First Century*, Farrar, Straus and Giroux, 2005, at 181.

¹³³ S. Scott, 'Opening Remarks', 7th Annual ICN Conference, Kyoto, Japan, 14 April 2008.

¹³⁴ M. Bloom, *op. cit.*, at 21.

¹³⁵ W. Kolasky, 'Global Competition: Prospects for Convergence and Cooperation', Speech, American Bar Association Fall Forum, Washington DC, 7 November 2002, at 8.

solution would no doubt have to be overcome in Europe, and particularly in Germany, it is submitted that the more economics-based standard that is the consumer welfare standard should be adopted in Europe and followed through in the European Commission's decisions. This would not only reduce the possibilities for Trans-Atlantic conflict but would also ensure that two important advantages can be secured: (i) the alignment of EC competition law with its economic purpose in an internally consistent manner; and (ii) the prevention of form triumphing over substance to the detriment of consumers.¹³⁶ In order to secure these advantages, Article 82 EC should become more reliant on economic principles; but such principles should be capable of being applied in practice by the competition authorities, legal practitioners and courts.¹³⁷ In this regard, the outcome of the Article 82 consultation is eagerly awaited.¹³⁸ Indeed, it is hoped that this consultation will lead to increased convergence between the US and EC. In any case, the support of the Community Courts concerning the pursuit of the objective of consumer welfare maximisation would nonetheless be required for such convergence to occur.¹³⁹

Notable differences also exist concerning procedures. Most of these differences do not really pose difficulties for the smooth (as opposed to the efficient) operation of both US and EC competition law. They do not prevent, for example, the concurrent enforcement of the US and EC competition law rules. The use of criminal sanctions in the US, coupled with their absence at European level, is an example of a benign procedural difference: both US criminal and EC administrative treatment of a given conduct by a given individual/undertaking is indeed possible, as evidenced by for example the vitamins cartel cases. This is not to say that criminalisation within Europe would not have beneficial effects such as providing for an increase in deterrence or for the use of extradition arrangements between the EC and the US. The point is simply that the existence of criminal sanctions in the US does not mandate the use of such sanctions in the EC so as to avoid the possibility of serious conflict in competition law enforcement. This is a welcome fact, as an appetite for criminalisation does not currently exist within Europe as it does within the US, where cartel behaviour is generally seen to be a sophisticated form of theft.

But the possibility of conflict between the respective enforcement regimes is not the only concern when contemplating Trans-Atlantic competition law differences/similarities. Efficiency is something that also needs to be considered. This economic concept is particularly important in the context of merger control where significant differences exist on the particulars of the procedures employed. Indeed, procedurally the merging parties confront:

different forms, different measures for turnover and asset calculation, different timetables, ... different sorts of Phase II/Second Request examinations and incredible translation requests to name just a few of the hurdles.¹⁴⁰

There is an increased risk of procedural conflicts when, like with many merger cases, transactions are reviewed by multiple jurisdictions. In this context, the international business community faces significant burdens, costs, and uncertainties that are associated with filing and dealing with a large number of reviewing authorities, and which may *inter alia* 'discourage, unduly delay, or at best, constitute a tax on efficient, consumer-friendly transactions'.¹⁴¹ Even in relation to just the EC and the US, these issues are complex and may not have easy solutions. It is likely that these issues cannot be resolved unilaterally or through bilateral efforts alone.¹⁴² Indeed, multilateral efforts at convergence may be particularly fruitful in the area of merger procedures. For this reason as well as others, then, both bilateral and multilateral efforts at cooperation and convergence are considered in the sections that follow.

¹³⁶ J. Vickers, *op. cit.*, at 23.

¹³⁷ *Ibid.*

¹³⁸ See DG Competition, 'Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses', Brussels, December 2005, <http://ec.europa.eu/comm/competition/antitrust/art82/discpaper2005.pdf>.

¹³⁹ See L. Loydahl Gormsen, 'The Conflict Between Economic Freedom and Consumer Welfare in the Modernisation of Article 82' [2007] 3 *European Competition Journal* 329.

¹⁴⁰ T. Calvani, 'Devolution and Convergence in Competition Enforcement' (2003) 24(9) *European Competition Law Review* 415, at 416.

¹⁴¹ C. James, 'International Antitrust in the 21st Century: Cooperation and Convergence', Speech, OECD Global Forum on Competition, Paris, France, 17 October 2001, at 8-9.

¹⁴² *Ibid.*

B. Bilateral Cooperation

Bilateral attempts to reduce the possibility of conflict in competition matters have by and large followed the Recommendation of the OECD.¹⁴³ Cooperation agreements¹⁴⁴ aimed at facilitating the smooth functioning of competition enforcement have been concluded between the US on the one hand and Germany, Australia, Canada, and the EC on the other. Other similar agreements have been concluded between *inter alia* France and Germany, and Canada, New Zealand and Australia. The EC-US agreements of 1991 and 1998¹⁴⁵ are the most progressive of the agreements, encompassing positive comity provisions for the first time. These cooperation agreements, although useful in reducing system friction and the avoidance of conflicts, cannot be used to resolve disagreements between national enforcement agencies, especially when significant differences exist between their relative substantive analyses of competition issues. Further, cooperation agreements are subject to confidentiality requirements and do not generally involve changes in the domestic laws of the countries involved. This fact may contribute to their failure and may empty the agreements of all substance. A binding international multilateral treaty may solve some of these problems, especially if adoption of such a treaty entails significant changes in the domestic laws of the co-signatories.

On 23 September 1991, the European Commission concluded an agreement with the US, aiming to solve problems of extraterritorial jurisdiction in competition matters by promoting cooperation and coordination between their antitrust enforcement agencies. This agreement was later annulled by the ECJ in an action brought by France, the Netherlands and Spain.¹⁴⁶ Its importance however was not forgotten and the Council of Ministers resolved the legality issue by issuing a joint declaration (with the Commission) reinstating the agreement.¹⁴⁷ The cooperation agreement implemented many of the OECD recommendations. In particular, it provided for: prior notification of investigation or enforcement activities if they will affect the 'important interests' of another state;¹⁴⁸ the institutionalisation of meetings between officials and the exchange of information between such officials;¹⁴⁹ coordination of activity in cases in which both parties have an interest;¹⁵⁰ and both positive comity and (traditional) negative comity.¹⁵¹

It is expedient at this juncture to distinguish between positive and negative comity. Negative comity is essentially a doctrine of politeness and good manners between states. It involves the consideration and balancing of numerous factors by one state before deciding to take enforcement or judicial action. Positive comity, by contrast, involves one state requesting another to take enforcement action to prohibit activity that is causing (anticompetitive) effects within the requesting state's territory. Positive comity aims to assist countries to prosecute conduct which both have an interest in but which only one has the appropriate enforcement tools to reach effectively. Under Article 5 of the 1991 agreement the request must be considered and replied to, but the requested enforcement agency is under no obligation to comply with the request. These positive comity provisions were elaborated on and strengthened in the EC-US agreement of 4 June 1998. These provisions for positive comity have only been resorted to on one occasion: the *Sabre/Amadeus* review in 1999, where the US Department of Justice requested the Commission to investigate allegations of discrimination between Amadeus and Sabre airline reservation systems.¹⁵²

It has been argued that the Commission had no authority to agree to these positive comity provisions.¹⁵³ Article 3(2) of Regulation 17 provides that only Member States or natural or legal

143 OECD, *Revised Recommendation Concerning Cooperation Between Member Countries on Restrictive Business Practices Affecting International Trade*, OECD Doc C(95) 130 (final), 27 July 1995. On this see below.

144 See J. Parisi, 'Enforcement Cooperation Among Antitrust Authorities' (1999) 20 *European Competition Law Review* 133.

145 Agreement between the Government of the USA and the Commission of the European Communities Regarding the Application of their Competition Laws, 23 Sept. 1991, [1991] 4 CMLR 823, 30 ILM 1487 (hereafter 'the 1991 Agreement'); EU-US Positive Comity Agreement, 4th June 1998, [1998] OJ L173/28, [1999] 4 CMLR 502.

146 Case C-327/91, *France v Commission* [1994] ECR I-3641.

147 April 1995, [1995] OJ L94/45.

148 The 1991 Agreement, at Article 2.

149 *Ibid.*, at Article 3.

150 *Ibid.*, at Article 4.

151 *Ibid.*, at Articles 5 and 6 respectively.

152 The case was settled in July 2000. See European Commission Report, COM (2000) 618, p. 6.

153 See J. Walker, 'Extraterritorial Application of US Antitrust Laws: The Effect of the EC-US Antitrust Agreement' (1992) 33 *Harvard International Law Journal*, 583-591, 590; P. Torremans, 'Extraterritorial Application of EC and US Competition Law' (1996) 21 *European Law Review* 280, 289-291.

persons with a legitimate interest can submit to the Commission a request for enforcement action.¹⁵⁴ Torremans submits that the US does not fit either of these requirements and thus the provisions on positive comity may give rise to a new challenge before the Court of Justice.¹⁵⁵ Attorney General Tesauro believes that the positive comity provisions clearly breach Article 3(2) of the Regulation.¹⁵⁶ These opinions lead one to conclude that this aspect of the agreement is in a vulnerable position.

The agreements are further weakened by confidentiality requirements and by the fact that neither agreement affects existing laws in any way. Article 8 of the 1991 agreement for example states that:

notwithstanding any other provision of [the] agreement, neither party is required to provide information to the other party if disclosure of that information to the requesting party is (a) prohibited by the law of the party possessing the information; or (b) would be incompatible with important interests of the party possessing the information.¹⁵⁷

This article also stipulates that the agencies involved will try as far as possible to ensure that the confidentiality of the information received is protected.¹⁵⁸ Article 9 provides that the domestic laws of the co-signatories are not affected by the agreement.¹⁵⁹ As these agreements are not treaties they cannot override any provisions of EC or US law that may be inconsistent with their principles.¹⁶⁰ For Advocate General Tesauro both these articles combine to ensure that the agreement has a very limited effect on EC or US antitrust law.¹⁶¹ Regulation 1/2003 imposes an obligation of secrecy in competition matters on the Commission.¹⁶² Due to Article 9 of the 1991 agreement, this Regulation will take precedence over Articles 2, 3, and 5 of the agreement, ensuring 'the non-application of the agreement so far as the major provisions are concerned, ultimately emptying it of the whole of its substance'.¹⁶³ It is thus submitted that cooperation agreements do not solve problems of conflict due to extraterritoriality when confidentiality requirements impose limits on the ability of the enforcement agencies to deal with anticompetitive behaviour, especially when those who possessed the information in the first place give no waiver.

The agreement then seems to be of 'uncertain value'¹⁶⁴ given the fact that the ECJ may yet annul its positive comity provisions and the confidentiality requirements may result in an agreement with no substance. The agreement also displays weaknesses in that no obligations are created under it.¹⁶⁵ Consultations, exercise of positive comity, coordination of efforts and the use of negative comity for example are left to the total discretion of each state. The potential advantages of the agreement therefore depend on the reciprocal trust of each state, their sensitivity to international conflicts and their ability to forego investigations and enforcement actions when they recognise the existence of other more powerful, legitimate interests of co-signatories. Further, the agreement is silent on the position of private suits,¹⁶⁶ an issue of great importance in the US, where the majority of cases involve actions taken by private plaintiffs as opposed to enforcement agencies. The drawbacks of these agreements can be summarised as follows:

- They impose strict confidentiality requirements on the enforcement agencies;
- They do not affect existing legislation, including confidentiality laws;
- They only create discretionary powers and not legally binding obligations;
- They are silent on the issue of private suits; and

¹⁵⁴ Article 3(2) of Regulation 17/62, [1967] JO No. 13/204. This has been replaced by Article 7(2) of Regulation 1/2003.

¹⁵⁵ P. Torremans, *op. cit.*

¹⁵⁶ Conclusion of AG Tesauro in Case C-327/91, *France v. Commission* [1994] ECR I-3641.

¹⁵⁷ The 1991 Agreement, Article 8.

¹⁵⁸ *Ibid.*

¹⁵⁹ *Ibid.*, Article 9.

¹⁶⁰ A. Riley, 'Nailing the Jellyfish: The Illegality of the EC-US Government Cooperation Agreement' [1992] 3 ECLR 101, 106.

¹⁶¹ See Case C-327/91, *France v. Commission* [1994] ECR I-3641.

¹⁶² See Regulation 1/2003, at Chapter VIII.

¹⁶³ See AG Tesauro, *op. cit.*, at 540.

¹⁶⁴ M. Shaw, *International Law*, Cambridge, Cambridge University Press, 1997, at 489.

¹⁶⁵ C. Cocuzza and M. Montini, 'International Antitrust Cooperation in a Global Economy' [1998] ECLR 156, at 158.

¹⁶⁶ See P. Torremans, *op. cit.*, at 292.

- They do not provide a mechanism for solving conflicts involving a significant divergence on substantive analysis.¹⁶⁷

Torremans argues that a multilateral treaty producing binding obligations, which may override domestic legislation, should be adopted.¹⁶⁸ For him this treaty should define the applicable (extraterritorial) jurisdiction test in antitrust cases *viz.* the implementation doctrine, and should list the comity considerations to be undertaken as a matter of course in administering such a test.¹⁶⁹ In short, he believes that the cooperation agreements operate on a different level to that which is required. It is submitted that the advantages of Torremans' approach are obvious, effectively combating the disadvantages associated with cooperation agreements. However, it is also submitted that in the present political climate such an approach might not be feasible, involving as it does imposition of obligations on states, undermining their sovereignty to a degree that may not be appreciated. A multilateral cooperation framework that involves discretionary initiatives agreed at international level, possibly within the WTO or the OECD, may be a less challenging, less controversial – albeit weaker – alternative. A treaty establishing such a framework would need to change existing confidentiality laws if it were to be of any substance. Such an approach may involve a small number of states at first, expanding in scope once confidence has been established. Provision must be made to ensure downstream confidentiality. Although such a treaty may involve changes in the substantive provisions of domestic confidentiality laws, its successful operation depends to high degree on whether or not the agencies involved can assure the business community that sensitive information remains within a closed loop of enforcement agencies. In other words, a relaxation of confidentiality rules between enforcement agencies should not entail the abandonment of confidentiality requirements between these enforcement agencies and third parties. It is submitted that in the absence of a political will to adopt binding global competition standards, such a treaty may prove to be the best way forward.

C. Multilateral Convergence

There have been various attempts to create a framework for multilateral cooperation and convergence at certain international organisations such as the United Nations ('UN'), the Organisation for Economic Cooperation and Development ('OECD') or the World Trade Organisation ('WTO'). In 1980, at the United Nations Conference on Trade and Development ('UNCTAD'), a voluntary, non-binding code was adopted. The UN's *Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices*, detailed a set of core principles to be adopted in competition law systems. The aim of the UNCTAD in producing such a code was to encourage international consensus on substantive provisions of competition law. The code however fails in its attempt: the principles are very vague and its implementation at national level is left to the discretion of the individual UN states.

The OECD has attempted to encourage cooperation in the enforcement of national competition laws. In 1969, the organisation adopted a 'Recommendation' detailing the manner in which cooperation could be achieved.¹⁷⁰ This Recommendation has been modified over the years but it essentially provides that member countries should: notify other members when their national interests are affected by enforcement action under national competition law; share information and consult with the various enforcement agencies of member countries; coordinate parallel investigations when circumstances deem it appropriate; assist in investigation of anticompetitive activities; and rely on the concept of positive comity.¹⁷¹

The Recommendation only presents suggestions – as opposed to obligations – on how to facilitate effective cooperation in enforcement activities. Despite its voluntary nature, the

167 See, e.g., the *Boeing/McDonnell Douglas* and *GE/Honeywell* cases. As Von Meibom and Geiger state: 'bilateral agreements are no guarantee of success [in international enforcement activities]. The *GE/Honeywell* case has shown only too well that competition authorities can reach different decisions despite having bilateral agreements. This demonstrates the limitations of what can be achieved with bilateral agreements as long as the law is not harmonized'; W. Von Meibom and A. Geiger, 'A World Competition Law as an *Ultima Ratio*' [2002] ECLR 445, at 450.

168 P. Torremans, *op. cit.*, at 292.

169 *Ibid.*

170 OECD, *Revised Recommendation Concerning Cooperation Between Member Countries on Restrictive Business Practices Affecting International Trade*, OECD Doc C(95) 130 (final), 27 July 1995.

171 Summary of the proposals in the Recommendation, *ibid.*

Recommendation has achieved a certain degree of success, evidenced by the conclusion of cooperation agreements between *inter alia* the US and Canada, the US and the EU, and the EU and Canada. Another important development at the OECD was the creation of the Global Forum on Competition in October 2001. This forum convenes on a regular basis, bringing together representatives of the thirty OECD members, the EU and twenty-one non-OECD members. The Global Forum is essentially intergovernmental in nature, concentrating on coordination of economic policy and exchange of information. It has no legal rule making functions.

According to Von Meibom and Geiger¹⁷² one of the most promising initiatives at the moment is the International Competition Network (ICN)¹⁷³, founded on 25 October 2001. The ICN is the direct result of the recommendations of the US Attorney General's International Competition Policy Advisory Committee.¹⁷⁴ It is a project-orientated, consensus-based, informal network of antitrust agencies from both developed and developing countries that examines enforcement and policy issues of common concern to Member States. The Network consists of a Steering Committee and five working groups.¹⁷⁵ Like the Global Forum on Competition, the ICN is an intergovernmental forum with no rule-making functions.¹⁷⁶ Those who prefer binding international rules would submit that the ICN, although useful in reducing friction between Member States, does not go to the root of the problem. It is not radical enough, does not create binding obligations on members, and does not take significant steps towards convergence on substantive provisions of antitrust law. Nevertheless, the ICN has made considerable strides towards developing trust among competition agencies and soft convergence of laws, which has had more practical benefits than all other international efforts to date.¹⁷⁷

That said, some commentators have noted that the WTO, with its existing dispute settlement procedure, may be an appropriate forum to develop an international competition law.¹⁷⁸ The WTO, the successor of the General Agreement on Tariffs and Trade (GATT), is an organisation that concentrates primarily on trade liberalisation and the globalisation of markets. It does not have any antitrust policies of its own: there are no WTO rules imposing obligations on countries expressly in relation to the enforcement of their competition laws (despite some early attempts at this in the telecoms sector).¹⁷⁹ In 1993, during the Uruguay round that led to the creation of the WTO, a Draft International Antitrust Code was drawn up by a group of experts at the Max Planck Institute.¹⁸⁰ This code envisaged the creation of an international antitrust regime involving common substantive provisions of competition law, and the creation of an International Antitrust Authority with competence to prohibit activities inconsistent with such provisions.¹⁸¹ This authority would have power to: bring actions against National Authorities when they refuse to take appropriate enforcement measures under its antitrust laws; sue private parties for an injunction to stop anticompetitive behaviour; have a duty to sue a party before the International Antitrust Panel envisaged in the code; and assist Member States in the enactment and enforcement of antitrust laws.¹⁸² This project was considered too ambitious and no competition agreement was annexed to the Plurilateral Treaties annexed to the WTO Charter. A minority of this working group proposed a less radical solution based on the adoption of fifteen core principles towards which gradual legislative convergence should be undertaken.¹⁸³ No international consensus on this issue ensured that the WTO members adopted not even this proposal.

172 W. Von Meibom and A. Geiger, *op. cit.*, at 452.

173 See www.internationalcompetitionnetwork.org.

174 See *Final Report of the International Competition Policy Advisory Committee to the US Attorney General and Assistant Attorney General for Antitrust*, February 2000.

175 *Ibid.* The Steering Committee identifies work projects for the working groups. These groups are: The Mergers Working Group; The Advocacy Working Group; The Funding Working Group; The Memberships Working Group; and the Non-Governmental Advisors Working Group. See also G. Murphy, 'Responding to Challenges of a Globalised Marketplace' [2002] ECLR 227.

176 *Ibid.*

177 P. Marsden, 'Tune in to the International Competition Network - Not the WTO - for Practical Advances in International Anti-trust', *In Competition*, Brussels (December 2001).

178 See, e.g., A. Jones and B. Sufrin, *EC Competition Law: Text, Cases and Materials*, Oxford, Oxford University Press, 2001, at 1073. On the development of a WTO competition policy, see generally P. Marsden, *A Competition Policy for the WTO*, London: Cameron May, 2003.

179 On this see P. Marsden, 'Innovative Trade Rules with Anti-competitive Effects?', *International Business Lawyer*, London, (March 2001).

180 *Draft International Antitrust Code, GATT-MTO Plurilateral Trade Agreement*, Munich, Max Planck Institute, 1993.

181 *Ibid.*

182 For a concise summary of the Draft Code see C. Cocuzza and M. Montini, 'International Antitrust Cooperation in a Global Economy' [1998] ECLR 156, 160-61.

183 *Ibid.*

In June 1996, the EC Commission proposed that the December WTO Ministerial Conference establish a working group to investigate core principles of competition law that could be made available for adoption by Member States of the WTO.¹⁸⁴ The US was hostile to such a proposal believing that a WTO led international competition regime could not accommodate the diversity of its Member States.¹⁸⁵ Even if core principles were adopted they would be minimalist in nature, consisting of lowest common denominator ideas, undermining the effectiveness of present more broad ranging principles. The US also expressed the fact that the business community would have concerns about handing over business sensitive information to WTO bureaucrats.¹⁸⁶ Finally, the US questioned the appropriateness of the WTO dispute settlement procedures in dealing with competition law matters, believing that such reviews of anticompetitive behaviour 'could interfere with national sovereignty concerning prosecutorial discretion and judicial decision making, and could also involve WTO panels in inappropriate reviews of case specific, highly confidential business information'.¹⁸⁷ Convergence for the US should only entail 'moving together, based on learning and experience, but not binding rules' promulgated by an international organisation such as the WTO.¹⁸⁸

The EC proposal was not adopted. However, the 1996 WTO Ministerial Conference in Singapore did set up a working group to study the interaction of trade and competition policy.¹⁸⁹ In 2001, in Doha, Qatar, it was agreed at the Ministerial Conference that talks on convergence of competition rules would take place.¹⁹⁰ By late 2003, however, the EU had dropped its request on competition policy in order to ensure that a more limited, but still liberalising, trade agreement. As a result competition was effectively removed from the WTO's agenda.¹⁹¹ This example, then, highlights the difficulties that one faces when attempting to achieve a consensus concerning the convergence of competition law rules in a multilateral setting, particularly when opposition to such a project is registered by powerful jurisdictions such as the United States. Given this context, it is submitted that, for the moment at least, convergence - if it is to occur - should be of the soft law variety and should find its source in best practices guidelines and/or non-binding recommendations. Indeed, according to the United States at least, if convergence in a multilateral setting is to take place, it should be focused on discrete issues of best practices, a form of multinational antitrust convergence by 'baby steps'.¹⁹² It appears that the ICN is an existing forum that is particularly suited to such important work.¹⁹³

V. CONCLUSION

As outlined above, there are obvious similarities between competition law in the US and its counterpart in the EC, in particular as regards substance as opposed to procedure. The underlying legislative provisions, while different in wording, are roughly equivalent and in more recent years both jurisdictions have apparently been pursuing common objectives, namely the maximisation of efficiency and consumer welfare. Procedures, although not identical, also display similarities e.g. in relation to sanctions, the absence of notification requirements for agreements, and the use of extraterritorial jurisdiction. Important differences are also present. Indeed, substantive differences exist concerning bundling, predation, the licensing of intellectual property rights and the assessment of conglomerate mergers. Agreements that frustrate the objective of free market integration are prohibited in Europe; the US, by contrast, does not exhibit a similar concern for agreements that compartmentalise their national market. Differences in attitudes and culture have also influenced European approaches to procedural issues, as seen, for example, in the rejection of treble damages for private plaintiffs and the absence of individual criminal sanctions at EC level and in the majority of Member States.

184 Communication submitted by Sir Leon Brittan and Karl Van Miert, 'Toward an International Framework of Competition Rules', 18 June 1996, reprinted in European Commission Press Release IP(96) 523, 18 June 1996.

185 Address by Acting Assistant Attorney General Joel I. Klein, 'A Note of Caution with Respect to a WTO Agenda on Competition Policy', 18 November 1996, at 14. For a comprehensive summary of these contentions see J. Griffin, 'Foreign Governmental Reactions to US Assertions of Extraterritorial Jurisdiction' [1998] ECLR 64, 66-67.

186 Klein, *op. cit.*, at 14.

187 *Ibid.*, at 15.

188 T. Calvani, 'Devolution and Convergence in Competition Enforcement' (2003) 24(9) *European Competition Law Review* 415, at 418.

189 WTO Ministerial Conference Singapore, Final Declaration, 13 December 1996, 36 ILM 218 (1997), at paragraph 20.

190 WTO, Doha Ministerial Declaration, (WT/MIN(01)/DEC/1).

191 P. Marsden, 'Trade and Competition: Competition After Cancun - A Personal View' (2003) 2(10) *Competition Law Insight* 22, at 23.

192 T. Calvani, *op. cit.*, at 418. See also R. Tritelli, 'International Antitrust Convergence: A Positive View' (Summer 2005) *Antitrust* 25.

193 See, e.g., S. Scott, 'Opening Remarks', *op. cit.*

The question that was posed here was whether these substantive and procedural differences are a problem. In a globalised world, it is likely that companies subject to EC competition law will also be subject to US law, and vice versa. Given that these laws are not identical to each other, it is obvious that possibilities for conflict exist. This is particularly the case with unilateral behaviour. The cooperation agreements concluded between the US and the EC may help to reduce the likelihood of conflict, but these agreements suffer from a number of serious disadvantages. In the absence of a viable harmonisation project – which itself is something that is very unlikely to be initiated at this point in time - it is convergence that should attempt to make up for the drawbacks of cooperation agreements. In particular, soft law convergence through the ICN should be pursued. Such soft law convergence can help not only reduce the possibilities of conflict, but also improve the efficiency of the US and EC competition law regimes, particularly in the area of merger procedures. It is submitted here, in any case, that if further cooperation/convergence is to occur it must be done in a coherent, consistent and coordinated manner, all the while respecting the sovereignty of all jurisdictions involved.

COORDINATION AMONG NATIONAL ANTITRUST AGENCIES

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This paper examines the manner in which national antitrust agencies within the European Union (“EU”) and within the United States (“US”) coordinate antitrust enforcement in their respective territories, and also how they interact with other antitrust organizations around the world. In looking at these issues, the hope is to add a new perspective to the ever important question of convergence of substantive antitrust laws in a global economy. An examination of how national antitrust agencies coordinate among themselves provides some insight into whether convergence should always be the goal, and whether it can realistically be achieved.

Part I focuses on coordination among national antitrust agencies within the EU. Part II focuses on coordination among the US enforcement agencies. Part III focuses on cooperation among the EU, the US and other non-EU countries and organizations. The paper concludes with some policy considerations for purposes of examining these issues.

PART I: COORDINATION AMONG NATIONAL ANTITRUST AGENCIES IN THE EU

A. Introduction - Antitrust Enforcement in the Pre-Modernization Era

Council Regulation (EC) No. 1/2003⁵ (“Regulation 1/2003”) entered into force on May 1, 2004. The main objective was to strengthen the enforcement of European Commission (“EC”) competition rules at a national level through increased involvement of national competition authorities (“NCAs”) and national judges. Until that date, the enforcement of competition rules in the EU lacked coordination, was not based on the same set of rules and principles, and had limited application by NCAs and national judges. While it is possible for the early decades of the development of EC competition policy to attribute such an effect to a divergence of opinion for a clear antitrust policy, consensus began to develop in the 1980s, with member states gradually setting

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⁵ Council Regulation (EC) No. 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty. OJ L 1 of 4 January 2003, p. 1.

up national competition authorities and introducing national competition laws that were often largely modeled on EC law. Nonetheless, at that time the EU did not have normative instruments suitable to ensuring coordination of antitrust policy and enforcement at the national level.⁶

In the pre-modernization era, the EC was to a large extent alone in applying Articles 81 and 82 of the EC Treaty for prosecuting antitrust infringements capable of affecting trade between member states. NCAs retained competence to apply national antitrust provisions to infringements in their national territory, including infringements capable of affecting trade between member states, and thus fell within the scope of application of Articles 81 and 82 EC. However, the “monopoly” in the application of Articles 81 and 82, together with the fact that agreements affecting trade could be notified and approved in Brussels, led to a sub-optimal enforcement situation. This sub-optimal situation was further compounded by the EC’s limited enforcement resources, the under-development of the NCAs’ involvement in the application of EC competition law, and redundancies leading to inefficiencies because of different sets of rules.⁷

Regulation 1/2003 impacted the EC’s enforcement prerogatives and investigative powers. It determined, on the one hand, the appropriate use of the available resources and on the other hand, a mechanism whereby the coherent application of antitrust principles was actively pursued.

For the first time, the national competition authorities of the member states and the national courts obtained the power to apply the competition provisions in the Treaty in full within their respective jurisdiction/sphere of competence.⁸ In addition, when applying national competition law to agreements or conduct in breach of those rules, NCAs and national courts were obliged to apply Articles 81 and 82 of the EC Treaty (provided that the conduct was capable of affecting trade between member states).⁹

B. The European Competition Network and Its Functioning

The fact that Regulation 1/2003 empowered NCAs and national courts to apply Articles 81 and 82 triggered the concern that Community competition law might be applied in vastly diverging ways by different authorities and/or courts. In this respect, the establishment of the European Competition Network (“ECN”) was the most appropriate solution to ensure cross-border cooperation between antitrust authorities, capillary enforcement, and coherent application of EU competition rules.

The ECN is not an autonomous body or organization in the EU institutional landscape. It is, rather, a forum for cooperation between the EC and the NCAs. The role of the ECN is to facilitate the exchange of information between competition authorities and the mutual assistance in antitrust investigations, with a view to shaping a common competition culture and enhancing the efficiency of the antitrust enforcement action across Europe.¹⁰ The function of the ECN is not limited to the “institutional” activities provided for in Regulation 1/2003. Outside of the scope of such provisions, cooperation has grown and developed. Within the ECN, informal exchanges as well as periodic meetings in a range of different fora have their place. While the *plenary meetings* and *working groups* address issues concerning horizontal cooperation between the Authorities, ECN *subgroups* bring together experts for specific sectors. Moreover, any topic of sufficient weight and mutual interest can be taken up at the periodic Meetings of Directors General.

⁶ It must be observed, as an example, that Regulation 17/62 contained little provision for exchange of information between the Commission and the NCAs and none at all for exchange of information between the NCAs.

⁷ See Recital 3 of Regulation 1/2003: “*The centralised scheme set up by Regulation No 17 [...] hampers application of the Community competition rules by the courts and competition authorities of the Member States, and the system of notification it involves prevents the Commission from concentrating its resources on curbing the most serious infringements. It also imposes considerable costs on undertakings.*”

⁸ See Articles 5 and 6 of Regulation 1/2003.

⁹ See Art. 3 of Regulation 1/2003.

¹⁰ See K. Dekeyser and M. Jaspers, *A New Era of ECN Cooperation*, World Competition, 2007, pp. 3-24.

1. An Integrated and Flexible Enforcement System

Regulation 1/2003 sets forth the provisions regulating the cooperation within the ECN. The resulting system is based on parallel competencies of the Commission and the NCAs in the application of EU competition rules and on flexible case allocation. Additional orientations on the functioning of the ECN are included in the Commission Notice on cooperation within the Network of Competition Authorities (the “Network Notice”).¹¹

As a consequence of the establishment of the ECN, additional resources (in terms of investigative tools and case-specific information) became available to European competition authorities, enhancing their ability to be effective enforcers including in cases that have certain cross-border implications. NCAs are able to draw on information exchanges and assistance from other authorities in the network under the mechanisms foreseen in the Regulation.

Moreover, work sharing in the network contributes to making effective and efficient use of the limited resources available for antitrust enforcement.

The parallel competence and the flexible case allocation principles, included in the Network Notice, allow any well-placed competition authority to take action on a case.¹² Cases can be handled by authorities that are well placed in terms of being close to (and consequently possess enhanced knowledge of) the markets affected. In addition, work sharing in the network can contribute to alleviating the persisting resource constraints for antitrust enforcement. At the same time, the Commission is enabled to play a leading role in the enforcement and is not prevented from handling cases raising important policy issues independent of their geographical scope.¹³

2. Exchange of Information

A key, value-adding element of the ECN is the possibility to exchange case-specific information. Such information can be relevant for case allocation purposes and/or for investigating and/or proving a case. Exchanged information can be used in evidence, if the conditions in the Regulation are fulfilled. There are specific safeguards for leniency-related information.

Article 12 of Regulation 1/2003 regulates the exchange of information within the ECN. It provides that, for the purpose of applying Articles 81 and 82 of the Treaty, the Commission and the competition authorities of the member states shall have the power to (i) provide one another with and (ii) use in evidence any matter of fact or of law, including confidential information.

With respect to the use in evidence of exchanged information, Art. 12(2) of Regulation 1/2003 clarifies that

Information exchanged shall only be used in evidence for the purpose of applying Article 81 or Article 82 of the Treaty and in respect of the subject-matter for which it was collected by the transmitting authority. However, where national competition law is applied in the same case and in parallel to Community competition law and does not lead to a different outcome, information exchanged under this Article may also be used for the application of national competition law.

Only in two specific cases the information exchanged can be used in evidence to impose sanctions on natural persons namely when (i) the law of the transmitting authority foresees sanctions of a similar kind in relation to an infringement of Article 81 or Article 82 of the Treaty or (ii) the information has been collected in a way which respects the same level of protection of the rights of

¹¹ OJ C 101 of 27 April 2004, p. 43.

¹² On work sharing in the network and the concept of *well-placed* authority, see the Network Notice, paras 55s.

¹³ See ECJ judgment in case C-344/98, *Masterfoods*, [2000] ECR I-11369.

defense of natural persons as provided for under the national rules of the receiving authority. However, in this case, the information exchanged cannot be used by the receiving authority to impose custodial sanctions.

In this respect, it is worth adding that, although Art. 12 empowers NCAs to exchange information, it does not compel them to do so when requested by another NCA.¹⁴ The exchange of information is discretionary. Whether such discretion is outweighed by a general duty to cooperate imposed on the NCAs by Art. 10 of the EC Treaty has been the subject of debate.¹⁵ Some argue that the rationale of Art. 10, i.e., the need that the Community institutions and the national authorities assist each other in the implementation of the Treaty, suggests that a duty to provide information does exist. However, there are opinions to the contrary.¹⁶ What can be emphasized at this point is that, even if the *option* set forth by Article 12 is indeed construed as an *obligation*, such an obligation should not be considered unlimited. Leniency information, for instance, is of pre-eminent importance for antitrust enforcement and, as such, must be handled with caution.

The reflections above lead to the conclusion that the principles regulating the exchange and use in evidence of information gathered within the network are a cornerstone of the functioning of the ECN system. Access to information obtained anywhere in the network countries allows to build more solid cases at a faster pace while avoiding any duplication of investigative efforts. However, one caveat exists: the leniency information is an invaluable enforcement resource for the authority that gathers it and accordingly will subject to a special regime.

3. Cooperation in the EU and Leniency: The ECN Model Leniency Program

In order to provide a greater degree of predictability for potential applicants and prevent them from being faced with contradictory demands when more than one ECN leniency program is applicable, ECN members launched the ECN Model Leniency Program. It is an important tool for the harmonization of all European leniency programs.

The principal aim of this program is to provide details on how the one-stop-shop options for the handling of leniency within the ECN should work, thus setting out the principal substantive rules that ECN members believe should be common to all the programs they operate.

4. Work Sharing

With the sole exception of Article 11(6), the system of Regulation 1/2003 is a system of parallel competences. The Network Notice envisages that work sharing should be flexible and a matter of dialogue between the enforcers in the ECN. This approach initially raised concerns and was also contested in court.

In legal terms, it is noteworthy that the Court of First Instance (“CFI”) has for the first time taken position on questions of work sharing between the Commission and national competition authorities in the ECN in its judgments of March 8, 2007¹⁷ in the France Télécom cases. In a nutshell, the applicants in the case had argued that – by carrying out an inspection in a case that had previously been dealt with by the French NCA and consensually been pursued further by the Commission – the Commission had violated an alleged ‘division of competences’ that, according to the applicant, could be derived from Regulation 1/2003, the Network Notice and/or general principles.

In its judgment in Case T-339/04, the CFI rejected the arguments of the applicant(s) in respect of work sharing in the ECN in their entirety. It held in particular that Regulation 1/2003 has, in conformity with the principle of subsidiarity, provided for a wider association of the national

¹⁴ It must be considered that NCAs are already subject to an obligation to comply with the Commission’s request for information pursuant to Art. 18(6) of Regulation 1/2003.

¹⁵ See J. Faull & A. Nikpay, *The EC Law of Competition*, 2nd ed., 2007, pp. 141-142.

¹⁶ It is argued, in particular that the provision of Art. 12 of Reg. 1/2003 is a specific provision and, as such, it would prevail over Art. 10 EC Treaty. The latter is a rule of general character, which is only applicable to the extent that Community legislation does not specifically provide on the matter. See J. Faull & A. Nikpay, *cit.*, pp. 141-142.

¹⁷ Judgments of the CFI of 8 March 2007 in Cases T-339/04 and 340/04, *France Telecom v. Commission*.

competition authorities with the application of the EC competition rules. However, the Regulation has not changed the general competence of the Commission recognized by the case law of the European Court of Justice (“ECJ”) (*Masterfoods*). Moreover, the Regulation has not established a division of competences that could preclude the Commission from carrying out an inspection where a national competition authority is already dealing with the same case. Neither the Network Notice – as evidenced by its contents and wording – nor the Joint Statement establish binding criteria that could lead to the conclusion that – in the case at hand – solely the French competition authority could deal with the case and that the Commission was prevented from doing so. Furthermore, the principle of subsidiarity does not put into question the competences conferred on the Commission by the EC Treaty, which include the enforcement of the EC competition rules.

From a practical perspective, work sharing is not a major issue of concern and discussion within the network. Based on the Network Notice, cases are in the vast majority of instances followed up and concluded by the authority that started them.¹⁸ When initiating an investigation, authorities naturally take into account that they have a close relationship with the market in which the infringement takes effect, access to the evidence (if necessary with assistance by one or more other authorities) and enforcement powers to address the case. At present, there is no indication that any cases at all have been initiated by an authority that could not be considered well placed within the meaning of the Network Notice. In addition, any issues arising in connection with a possible re-allocation have been addressed and solved through bilateral discussions taking place within the network and at the earliest possible stage. In sum, the practice of the ECN shows that very few cases have been transferred from one competition authority to another or have given rise to work sharing discussions between authorities in the network.

5. Coherent Application of Antitrust Rules

Regulation 1/2003 pursues as one major objective: the coherent application of the EC competition rules by all enforcers. It recognizes the fact that inconsistencies in the application of Articles 81/82 EC can be detrimental to companies doing business in the internal market. Against this background, it calls for a high level of coherence which in turn, entails a degree of coordination in the ECN.

In the above respect, Regulation 1/2003 sets forth three main mechanisms in order to ensure the coherent application of the antitrust rules: (i) obligation on NCAs to apply community law whenever there is an effect on trade between member states, in a manner that ensures convergence between national and community law (Art. 3); (ii) obligation on the NCAs to inform the Commission at the latest 30 calendar days before the adoption of an envisaged decision (Art. 11(4)); and (iii) possibility for the Commission to intervene if there is a serious risk of incoherence by relieving the NCA of its competence to act (Art. 11(6)).

Art. 3 of Regulation 1/2003 has so far ensured the desired convergence in the application of antitrust rules, with the result that, from this perspective, there is now a level playing field for undertakings doing business in the European Union.¹⁹

In addition, the information mechanism foreseen in Art. 11(4) of Regulation 1/2003 allows the Commission to review all the envisaged decisions from NCAs so as to exercise its task and particular responsibility towards ensuring a coherent application of the antitrust provisions. The possibility to submit observations on a case²⁰ has proven, in this respect, to be a pragmatic and balanced tool to foster the required convergence. The aim of such observations is to draw the national authority’s attention to certain issues or to raise certain points which might merit further reflection. They are usually undertaken in a very informal manner in phone contacts between the national case-team and the responsible unit within DG Competition. In certain cases, the oral

¹⁸ See K. Dekeyser and D. Dalheimer, *Cooperation within the European Competition Network – Taking Stock After 10 Months of Case Practice*, in P. Lowe & M. Reynolds (eds), *Antitrust Reform in Europe: a Year in Practice*, London, International Bar Association, 2005, pp. 105-123.

¹⁹ See K. Dekeyser and M. Jaspers, *cit.*

²⁰ See Network Notice, para. 46.

dialogues are followed by a letter, but the fact that the views are expressed in writing does not change the informal nature of the exercise.

It is useful to underline that coherent application should not be confounded with absolute uniformity in outcome. Ensuring an overall level playing field for European business is achieved when the same type of legal and economic considerations govern enforcement action by ECN members. Market or case-specific elements may result in a different outcome for cases that would initially appear to be the same. Different ECN members may also opt for different instruments – such as prohibition or commitment decisions – to address the identified concern.

At this stage of the ECN activities, the Commission has never used the possibility granted by Art. 11(6) to take action on a case and relieve an NCA of its competence to act to ensure coherent application of EC rules. Informal contacts and comments have proven to be very effective in drawing the national authority's attention on the most relevant aspects of a case and the willingness of the national authorities to engage in these dialogues and to take due account of the suggestions made has turned this more voluntarily cooperation instrument into a useful complementary tool to the formal powers given to the Commission. In this respect, the powers granted by Art. 11(6) remain as an *extrema ratio* in the array of Commission's enforcement tools.

6. Achievements of The ECN Network

At present, the allocation of cases, work sharing, and exchange of information in the ECN have resulted in an enhanced and coherent application of EC competition rules. The ECN has had policy effects beyond what is expressly required by the Modernization Package, such as the growing convergence of national procedural rules and the work in the leniency field being good examples.²¹ However, not all discrepancies in the centralized and decentralized application of the competition rules have been removed, as the different policies for fines of each NCAs demonstrate.

The ECN network has brought about substantial improvements in antitrust enforcement in the EU. While the Commission maintains a leading and propulsive role within the network, it must be noted that, since the adoption of Regulation 1/2003, the NCAs have also been very active in prosecuting cartels as well as in pursuing other antitrust infringements of all types. Between May 2004 and mid-November 2007, the ECN members have adopted some fifty decisions applying Art. 81 to cartels. Three out of five of these decisions were adopted by the NCAs.²²

Numerous NCAs are pro-active enforcers in the liberalizing markets and have in recent years exercised a strict control vis-à-vis foreclosing strategies by – still dominant – incumbent operators. NCAs are active in sectors that involve highly complex economic questions, e.g., financial services, and address areas that had for a long time not been the object of competition law scrutiny, e.g., liberal professions. Also, the role of the sectoral ECN subgroups has to be highlighted in this regard. These groups bring together experts from the authorities in a given area and serve as a forum for mutual information and joint learning. They also provide opportunities for coordination of enforcement action that is reflected in clusters of cases being moved forward by various enforcers.

Thus, the improvements to be credited to the ECN go far beyond dry numbers and remarkably consist of continuous efforts in exchanging intelligence information and actively cooperating in case work.

C. Conclusion

Before the ECN, the EC held a monopoly in the application of Art. 81 and 82 of the EC Treaty. The ECN has significantly improved the situation by decentralizing enforcement powers and responsibilities.

21 See K. Dekeyser and M. Jaspers, "A New Era of ECN Cooperation," in *World Competition*, 30(1), 2007, p. 22.

22 See presentation by W. Wils at the conference "Fifty Years of the Treaty: Assessment and Perspectives of Competition Policy in Europe," IESE, Barcelona, November 19-20, 2007.

The ECN is not a decision-making body, but rather a forum for discussion, cooperation, and information exchange. Far from invading and eroding the competences and the prerogatives of single NCAs, the ECN is an efficiency-enhancing structure (in terms of both resources and information available) facilitating an incisive antitrust enforcement. In this scenario, the EC maintains a crucial and leading role, in particular by ensuring a coherent application of antitrust principles and policy in all member states. The EC may also, thanks to the ECN, focus its attention on the most urgent priorities, such as pan-European infringements.

The positive effects of the ECN are further enhanced by the sharing, within the network, of a common leniency policy and culture. In this respect, it is a great achievement that NCAs throughout Europe have within a remarkably short time frame decided to endorse the Model Leniency Program and align their leniency policies (already existing or forthcoming) to it. The result is a consolidation of a system characterized by greater efficiency and legal certainty, where it is easier, on the one hand, to unveil cartels and, on the other hand, to prosecute them at a faster pace and with greater effectiveness.

PART II: ANTITRUST COOPERATION AMONG US ANTITRUST AUTHORITIES

A. Introduction

Antitrust enforcement in the United States can best be described as a patchwork of concurrent, and to some extent overlapping, authorities at both the federal and state levels. Foremost at the federal level, the Antitrust Division at the US Department of Justice (“DOJ”) and the Federal Trade Commission (“FTC”) oversee investigation, litigation, and transactional review of a broad range of antitrust-related matters. At the state level, attorneys general may bring suit on behalf of the state and in their *parens patriae* role under both state and federal law, and state and territorial antitrust agencies also engage in transactional reviews. Moreover, private plaintiffs may sue on behalf of individuals, groups, or a large class of millions of “clients” under both federal and state law. The role of private plaintiffs and their interaction with US antitrust authorities is important but outside the scope of this paper.

Cooperation between the federal agencies and between federal and state governments occurs frequently on both formal and informal bases. The two prominent federal agencies, DOJ and FTC, share enforcement authority under the Clayton Act and accordingly coordinate with each other, at times in a dysfunctional fashion, to allocate investigative resources. Also, with the adoption of the Protocol for Coordination of Merger Investigations and the Protocol for Increased State Prosecution of Criminal Antitrust Offenses, federal and state antitrust authorities have increased their formal coordination in the investigation and prosecution of anticompetitive conduct. Moreover, federal caselaw heavily influences state court litigation and decision-making, thereby creating one body of law shared by both.

The United States and other countries cooperate through formal mechanisms, including bilateral agreements, mutual legal assistance treaties, and other diplomatic instruments, and informal mechanisms, and informal relationships. In addition, consultation occurs through various multinational organizations.

Congress enacted the Sherman Act into law in 1890 and passed the Clayton Act in 1914.²³ While the DOJ had already been prosecuting anticompetitive conduct for more than 30 years, President Franklin D. Roosevelt formally created the Antitrust Division of the DOJ in 1933 with the appointment and confirmation of Harold M. Stevens, the first Assistant Attorney General for Antitrust.²⁴ Congress’s passage of the Federal Trade Commission Act – in the same year as the Clayton Act – established the FTC, in part to supplement the DOJ’s enforcement of the antitrust

23 See Department of Justice, Timeline of Antitrust Enforcement Highlights at the Department of Justice, available at <http://www.usdoj.gov/atr/timeline.pdf> (last visited June 17, 2008).

24 See Lauren Kearney Peay, Note, *The Cautionary Tale of the Failed 2002 FTC/DOJ Merger Clearance Accord*, 60 Vand. L. Rev. 1307, 1311-12 n.15 (2007).

laws²⁵ and to create an administrative agency for the administrative rulemaking and adjudication of antitrust matters.²⁶

B. Cooperation Between Federal Antitrust Authorities

1. Background

The DOJ and the FTC share government enforcement of the federal antitrust laws. While the DOJ holds exclusive federal power to prosecute criminal and civil claims under the Sherman Act²⁷ and the FTC routinely investigates violations of the Robinson-Patman Act, both agencies can bring civil enforcement actions under the Clayton Act.²⁸ In its Antitrust Division Manual, the DOJ describes the enforcement relationship with the FTC:

The Antitrust Division and the FTC have concurrent statutory authority to enforce Sections 2, 3, 7, and 8 of the Clayton Act. Judicial interpretation of Section 5 of the FTC Act permits the FTC to challenge conduct that also may constitute a Sherman Act violation, and thus, there is an overlap with the Division in this area as well. This overlapping antitrust enforcement authority necessitates coordination between the two agencies to ensure both efficient use of limited resources and fairness to subjects of antitrust investigations.²⁹

When both agencies hold concurrent jurisdiction and to ensure efficient use of resources, the “clearance procedure” is used to designate one agency to proceed with the investigation.³⁰ Usually, one agency will grant the other agency clearance quickly.³¹ Adopted in 1995 by the two agencies, the Hart-Scott-Rodino Premerger Program Improvements agreement provides internal procedures to decide which agency will investigate a specific merger.³² Notwithstanding these procedures, conflicts do arise between the DOJ and FTC, especially in merger review under Section 7 of the Clayton Act.³³

In addition to consultation and referral for both merger and non-merger matters, the DOJ and FTC regularly share information and evidence with one another to the extent permitted by law.³⁴ The two agencies also cooperate in studying and designing antitrust policy, such as their participation in joint hearings and joint drafting of reports on a variety of topics,³⁵ issuance of various guidelines,³⁶ and joint filing of amicus briefs.³⁷ Further, the DOJ and FTC create task forces to study particular areas of the law and present reports, including the State Action Task Force and the Noerr-Pennington Task Force.³⁸

²⁵ See D. Bruce Hoffman & M. Sean Royall, *Administrative Litigation at the FTC: Past, Present, and Future*, 71 *Antitrust L.J.* 319, 319–20 (2003).

²⁶ See David Balto, *Returning to the Elman Vision of the Federal Trade Commission: Reassessing the Approach to FTC Remedies*, 72 *ANTITRUST L.J.* 1113, 1113–14, 1117–18 (2005).

²⁷ While it holds no power pursuant to the Sherman Act, the FTC can bring suit under 15 U.S.C. Section 45, i.e., FTC Act Section 5, for conduct that might violate the Sherman Act. See ABA Section of Antitrust Law, *Antitrust Law Developments* 691 n.454 (6th ed. 2007) (hereinafter “Antitrust Law Developments”) (citing *FTC v. Cement Inst.*, 333 U.S. 683, 690 (1948)).

²⁸ Antitrust Law Developments at 691. Other federal agencies possess limited jurisdiction under the Clayton Act, including the Surface Transportation Board, Federal Communications Commission, Department of Transportation, and the Federal Reserve Board. *Id.* at n. 455.

²⁹ Antitrust Div., U.S. Dep’t of Justice, Antitrust Division Manual ch. VII (3d ed. 1998), available at <http://www.usdoj.gov/atr/foia/divisionmanual/ch7.htm> (hereinafter “Antitrust Division Manual”).

³⁰ Antitrust Law Developments at 693. The latest revision of the Clearance Procedures of Investigations was adopted in 1993. *Id.* at n.462.

³¹ *Id.* at 694.

³² *Id.*

³³ *Id.* at 693–94.

³⁴ Antitrust Division Manual, Chapter VII.

³⁵ Antitrust Law Developments at 694. Those topics include intellectual property, health-care, and single-firm conduct. See, e.g., Federal Trade Comm’n & U.S. Dep’t of Justice, Hearings on Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy (Feb. 6–Nov. 6, 2002), available at <http://www.ftc.gov/opp/intellect/index.htm>; News Release, FTC, FTC Issues Report on How to Promote Innovation Through Balancing Competition with Patent Law and Policy (Oct. 28, 2003), available at <http://www.ftc.gov/opa/2003/10/cpreport.htm>; FTC/DOJ Report and Hearings on Health Care and Competition Law and Policy (Feb. 2003–Sept. 2003), available at <http://www.ftc.gov/ogc/healthcarehearings/index.htm>; Department of Justice and FTC Issue Merger Challenges Data, Announce Upcoming Merger Enforcement Workshop (Dec. 18, 2003), available at <http://www.usdoj.gov/atr/public/pressreleases/2003/201899.htm>.

³⁶ See, e.g., U.S. Dep’t of Justice & Federal Trade Comm’n, Horizontal Merger Guidelines (1992, revised 1997), available at <http://www.ftc.gov/bc/docs/horizmer.htm>; U.S. Dep’t of Justice & Federal Trade Comm’n, Antitrust Guidelines for Collaborations Among Competitors (2000), available at <http://www.ftc.gov/os/2000/04/ficdojguidelines.pdf>; U.S. Dep’t of Justice & Federal Trade Comm’n, Antitrust Guidelines for Licensing of Intellectual Property (1995), available at <http://www.usdoj.gov/atr/public/guidelines/0558.htm>; U.S. Dep’t of Justice & Federal Trade Comm’n, Antitrust Enforcement Guidelines for International Operations (1995), available at <http://www.usdoj.gov/atr/public/guidelines/internat.htm>; U.S. Dep’t of Justice & Federal Trade Comm’n, Commentary on the Horizontal Merger Guidelines (2006), available at <http://www.ftc.gov/os/2006/03/CommentaryontheHorizontalMergerGuidelinesMarch2006.pdf>.

³⁷ Andrew Gavil, *Antitrust Bookends: The 2006 Supreme Court Term in Historical Context*, 22 *Antitrust* 21, 22–23 nn.48, 49 (Fall 2007) (citing numerous joint briefs for the United States as amicus).

³⁸ Report of the State Action Task Force: Recommendations to Clarify and Reaffirm the Original Purposes of the State Action Doctrine to Help Ensure Robust Competition Continues to Protect Consumers (Sept. 2003), available at <http://www.ftc.gov/os/2003/09/stateactionreport.pdf>; Noerr-Pennington Task Force, described at <http://www.ftc.gov/os/2003/07/antitrustoversight.htm>.

2. Jurisdictional Conflicts Between the DOJ and the FTC

Section 7 of the Clayton Act tasks both the DOJ and FTC to prevent the formation of monopolies.³⁹ In 1976, Congress's passage of the Hart-Scott-Rodino Antitrust Improvements Act ("H-S-R Act") established a premerger notification process and a statutorily-defined waiting period.⁴⁰ However, the H-S-R Act did not provide any procedures for the DOJ and the FTC to define which agency would investigate a merger.^{41,42} At the same time, because it required the review of all mergers of a specific size and set a time limit for review, the H-S-R Act, in effect, demanded that the DOJ and FTC work efficiently to decide which agency would review each merger.⁴³

To alleviate the rising tide of clearance disputes, the DOJ and FTC entered into two agreements, one in 1993 and the second in 1995, under which the agency with the most expertise in the industrial sector of the proposed merger would investigate.⁴⁴ Nevertheless, clearance disputes between the DOJ and FTC consumed much of the 30-day waiting period, leaving the "cleared" agency with little time to review the merger.⁴⁵

In 2002, the DOJ and FTC announced the creation of a Memorandum of Agreement ("Clearance Agreement") that delineated the industry sectors that were to fall under each agency's purview, and the divisions would be permanent.⁴⁶ Approximately two months before the announcement, Senator Ernest Hollings, Ranking Member of the Commerce, Justice and State Appropriations Subcommittee of the US Senate that has the power to approve or disapprove the DOJ's budget, vociferously objected to the Clearance Agreement on the grounds that it would shift antitrust oversight from the FTC, which does not sit directly in the Executive Branch, to political appointees in the DOJ.⁴⁷ Political support for the Clearance Agreement never recovered, and despite the March 2002 joint announcement, the DOJ and FTC abandoned the effort in May 2002.⁴⁸

3. Findings in the Antitrust Modernization Commission Report

The same year that the Memorandum of Agreement was nullified, the Congress enacted the Antitrust Modernization Commission Act, which created a committee to study the current state of all antitrust laws and enforcement and make recommendations for improvement.⁴⁹ In 2007, the Commission delivered its final report within which it recommended

The Federal Trade Commission and the Antitrust Division of the Department of Justice should develop and implement a new merger clearance agreement based on the principles in the 2002 Clearance Agreement between the agencies, with the goal of clearing all proposed transactions to one agency or the other within a short period of time. To this end, the appropriate congressional committees should encourage both antitrust agencies to reach a new agreement, and the agencies should consult with these committees in developing a new agreement.⁵⁰

³⁹ Antitrust Law Developments at 333.

⁴⁰ *Id.* at 334.

⁴¹ See *The Cautionary Tale of the Failed 2002 FTC/DOJ Merger Clearance Accord*, 60 Vand. L. Rev. at 1314-15.

⁴² Even though notification must be made to both the DOJ and FTC at the beginning, parties would pick which agency they preferred to deal with by contacting the one or the other immediately after filing. The agencies now discourage this practice.

⁴³ See *id.*

⁴⁴ See *id.* at 1315-16; see also *supra* n.12.

⁴⁵ *Id.* at 1316 (citing Federal Trade Commission, Clearance Delays, <http://www.ftc.gov/opa/2002/02/clearance/cleardailystats.htm>). The DOJ and FTC commissioned a study to evaluate the problem and found that 24 percent of all matters for which clearance was requested delayed the review process, on average, by three weeks each. *Id.* at 1317-18; News Release, FTC, DOJ Announce New Clearance Procedures for Antitrust Matters (Mar. 5, 2002), available at <http://www.ftc.gov/opa/2002/03/clearance.shtm>.

⁴⁶ *Id.* at 1318. (citing Memorandum of Agreement Between the Federal Trade Commission and the Antitrust Division of the United States Department of Justice Concerning Clearance Procedures for Investigations (Mar. 5, 2002), available at <http://www.ftc.gov/opa/2002/02/clearance/ftcdojagre.pdf>). The DOJ was to have jurisdiction over agricultural and associated biotechnology; avionics, aeronautics, and defense electronics; beer; computer software; cosmetic and hair care; financial services/insurance/stock and option, bond, and commodity markets; flat glass; health insurance and healthcare products and services; industrial equipment; media and entertainment; metals; mining and minerals; missiles, tanks, and armored vehicles; naval defense products; photography and film; pulp, paper, lumber, and timber; telecommunications services and equipment; travel and transportation; and waste. The FTC was to have jurisdiction over airframes; autos and trucks; building materials; chemicals; computer hardware; energy; healthcare; industrial gases; munitions; operation of grocery stores and grocery manufacturing; operation of retail stores; pharmaceuticals and biotechnology; professional services; satellite manufacturing and launch and launch vehicles; and textiles.

⁴⁷ *Id.* at 1334 (citing Philip Shenon, *Plan to Split Up Antitrust Oversight Stalls*, N.Y. Times, Jan. 18, 2002, at C2).

⁴⁸ *Id.* at 1335 (citing Charles A. James, Statement Regarding DOJ/FTC Clearance Agreement (May 20, 2002), available at http://www.usdoj.gov/opa/pr/2002/May/02_ag_302.htm).

⁴⁹ Antitrust Modernization Commission Act of 2002. The Commission was composed of twelve commissions with four each appointed by the President, Senate, and House of Representatives. Pursuant to its enabling statute, the Commission terminated 30 days after issuing its report.

⁵⁰ Antitrust Modernization Commission, Report and Recommendations at 134 (2007), available at http://govinfo.library.unt.edu/amc/report_recommendation/toc.htm (hereinafter "Antitrust Modernization Commission Report").

The Commission found that the clearance disputes occurred infrequently,⁵¹ but when they do, the conflicts, among other things, “create tension in the normally cooperative relationship between the two agencies and undermine public confidence in the US antitrust enforcement regime.”⁵² The Commission highlighted two components of the 2002 Clearance Agreement that it found especially important. First, the allocation of areas of primary responsibility should be retained in whatever new agreement might be created.⁵³ Second, any new agreement should include the 2002 Clearance Agreement’s “tie-breaker” process where an independent arbitrator would assign a merger to one agency within 10 days of the initial clearance request.⁵⁴

C. Cooperation Between Federal And State Antitrust Authorities

All 50 states, plus the District of Columbia, Puerto Rico, and the Virgin Islands, have passed antitrust laws that largely track the Sherman Act and the Clayton Act.⁵⁵ In fact, the 1890 enactment of the Sherman Act occurred after 26 states had already put in place some form of antitrust prohibition, and the principal author of the Sherman Act himself stated that the federal statute was to “supplement the enforcement” of state law.⁵⁶ During the Reagan administration, many states perceived federal antitrust efforts as lacking and accordingly became more active in enforcing both federal and state law.⁵⁷ Today, state antitrust authorities coordinate more closely with federal authorities in the investigation and prosecution of anticompetitive conduct.

1. Background

A majority of states have laws similar, many almost identical, to Sections 1 and 2 of the Sherman Act, and less frequently, laws similar to Sections 3 and 7 of the Clayton Act and the Robinson-Patman Act.⁵⁸ Many states’ competition laws specifically require deference of varying degree to federal precedent, *i.e.*, “harmonization statutes.”⁵⁹ In states where no harmonization statute exists, state courts generally follow federal caselaw.⁶⁰ While some state courts have extended their jurisdiction’s competition laws to interstate commerce,⁶¹ some states have used comity to curtail the extraterritorial reach of state law.⁶² The United States Supreme Court has held that state antitrust laws are not preempted by either the Commerce Clause or the Supremacy Clause of the US Constitution.⁶³

In addition to state laws, states can bring suit under federal antitrust statutes. The H-S-R Act included provisions that ordered the DOJ to provide investigative information to state attorneys general and allowed state attorneys general to sue under the Sherman Act with *parens patriae* actions in the name of state residents for treble damages.⁶⁴ In addition, a state may bring suit as an injured purchaser on its own behalf under Section 4 of the Clayton Act,⁶⁵ and a state can seek injunctive relief under Section 16 of the Clayton Act for harms to the state’s economy.⁶⁶

In 1983, the National Association of Attorneys General (“NAAG”) created the Multistate Antitrust Task Force.⁶⁷ In 1989, NAAG formed the Executive Working Group on Antitrust to coordinate federal and state enforcement efforts.⁶⁸ A majority of states have joined the

51 *Id.*

52 *Id.*

53 *Id.* at 136.

54 *Id.*

55 Antitrust Law Developments at 623 (citing ABA Section of Antitrust Law, *State Antitrust Practice and Statutes* (3d ed. 2004)). To read a comprehensive list of state antitrust laws, see *State Laws*, 6 Trade, Reg. Rep. (CCH) Paragraph 30,000. *Id.*

56 Antitrust Law Developments at 623 (citing 21 Cong. Rec. 2457 (1890)).

57 See Kevin J. O’Connor, *Federalist Lessons for International Antitrust Convergence*, 70 Antitrust L.J. 413, 421 (2002).

58 Antitrust Law Developments at 623-24.

59 *Id.* (collecting statutes).

60 *Id.* (collecting cases).

61 *Id.* at 625 (citing *Coca-Cola, Co. v. Harmar Bottling Co.*, 2006-2 Trade Cas. (CCH) Paragraph 75,464, at 106,234 (Tex. 2006) (“mere involvement of interstate commerce does not permit a defendant to escape suit”).

62 *Id.*

63 Antitrust Modernization Report at 185 (citing *Exxon Corp. v. Governor of Md.*, 437 U.S. 117, 130 (1978); *California v. ARC Am. Corp.*, 490 U.S. 93, 101 (1989) (holding state antitrust laws to be within “an area traditionally regulated by the States” for which there is a “presumption against finding pre-emption”).

64 15 U.S.C. Sections 15c, 15f (2000); see Susan Beth Farmer, *More Lessons from the Laboratories: Cy Pres Distributions in Parens Patriae Antitrust Actions Brought by State Attorneys General*, 68 Fordham L. Rev. 361, 376-91 (1999).

65 Antitrust Law Developments at 725 (stating that “the states allege pricing fixing and seek overcharged amounts as their damages”).

66 *Id.* at 726 (citing *In re K-Dur Antitrust Litig.*, 338 F.Supp.2d 517, 550 (D.N.J. 2004) (denying defendants’ motion to dismiss states’ claims for alleged conspiracy to delay entry of generic drugs)).

67 Stephen Calkins, *Perspectives on State and Federal Antitrust Enforcement*, 53 Duke L.J. 673, 679 (2003).

68 Antitrust Modernization Report at 188 (citing Michael DeBow, *State Antitrust Enforcement: Empirical Evidence and a Modest Reform Proposal*, in *Competition Laws In Conflict* 269 (Richard A. Epstein & Michael S. Greve eds., 2004)).

Voluntary Pre-Merger Disclosure Compact, which “encourages merging firms to submit pre-merger filings to the member states in return for an agreement by the states to forgo the issuance of individual state subpoenas and to obtain documents through the same process used by the relevant federal antitrust agency.”⁶⁹

Consultation, coordination, and cooperation between federal and state antitrust authorities can take on a variety of forms. For example, in criminal investigations, the DOJ and state antitrust authorities agreed to a cross-deputization program in which state attorneys general could be appointed to assist in the prosecution of federal criminal antitrust cases.⁷⁰ As another example, the NAAG Executive Working Group holds monthly teleconferences with federal authorities.⁷¹ In the past, the DOJ held Common Ground Conferences with state attorneys general to discuss coordination of state and federal antitrust enforcement.⁷²

2. Coordination Protocols

In 1998, the DOJ, FTC, and NAAG adopted the Protocol for Coordination in Merger Investigations Between the Federal Enforcement Agencies and State Attorneys General (“Merger Protocol”).⁷³ In 1996, the DOJ and NAAG adopted the Protocol for Increased State Prosecution of Criminal Antitrust Offenses (“State Prosecution Protocol”).⁷⁴ Together, the Merger Protocol and the State Prosecution Protocol represent the two most important examples of the formal coordination between federal and state antitrust enforcement authorities.

The Merger Protocol helps define the areas ripe for coordination in the merger review process. For example, to avoid subpoenas from multiple state enforcement agencies, the Merger Protocol specifies that the federal agency investigating the proposed merger will share H-S-R filing documents with the state authorities with the consent of the merging parties.⁷⁵ Further, the Merger Protocol encourages the reviewing authorities to hold a teleconference early in the process to coordinate the collection of evidence and the hiring of experts.⁷⁶ The Merger Protocol also urges federal and state authorities to work closely with each other during settlement negotiations, and if possible, hold joint settlement talks.⁷⁷

The State Prosecution Protocol provides a mechanism for the DOJ to hand off criminal investigations to a state attorney general when the alleged anticompetitive conduct, usually bid-rigging or price fixing, only affects local concerns.⁷⁸ The State Prosecution Protocol imposes two criteria: first, the state attorney general must have the legal and personnel resources to undertake the criminal prosecution, and second, the state attorney general is willing to undertake the criminal prosecution.⁷⁹ If the attorney general satisfies those requirements, the DOJ will transfer all evidence related to the investigation.⁸⁰

3. Conflicts Between Federal and State Laws and Jurisprudence

In *Illinois Brick Co. v. Illinois*, the Supreme Court closed the door on the recovery of damages for indirect purchasers harmed by Section 1 of the Sherman Act.⁸¹ Before and after the Court’s 1977 decision in *Illinois Brick*, more than 25 states enacted laws, sometimes called “*Illinois*

69 Antitrust Modernization Report at 188-89 (citing National Association of Attorneys General, Voluntary Pre-Merger Disclosure Compact (1987, revised 1994), available at <http://www.naag.org/assets/files/pdf/200612-antitrust-voluntary-premergerdisclosure-compact.pdf>).

70 Antitrust Law Developments at 798-99 (citing Antitrust Division Manual, ch. VII). The California Attorney General’s Office participated in a grand jury investigation of alleged anticompetitive conduct involving electrical signals with the Antitrust Division. See, e.g., *United States v. Roseandin Elec.*, 1989-2 Trade Cas. (CCH) paragraph 68,809, at 62,242-45 (N.D.Cal. 1987); FTC, News Release, State, Federal Law Enforcers Launch Sting on Business Opportunity, Work-at-Home Scams (June 20, 2002), available at <http://www.ftc.gov/opa/2002/06/bizopswe.shtm>.

71 American Bar Ass’n, Section on Antitrust Law, The State of Federal Antitrust Enforcement at 48 (2004), available at http://www.abanet.org/antitrust/at-comments/2005/02-05/federal_at_enforcement.html.

72 U.S. Dept of Justice, Cooperative Antitrust Enforcement (1995), available at <http://www.usdoj.gov/atr/public/speeches/0142.htm>.

73 U.S. Dept of Justice, Protocol for Coordination in Merger Investigations Between the Federal Enforcement Agencies and State Attorneys General (1998), available at <http://www.usdoj.gov/atr/public/guidelines/1773.htm> (hereinafter “Merger Protocol”).

74 U.S. Dept of Justice, Protocol for Increased State Prosecution of Criminal Antitrust Offenses (1996), available at <http://www.usdoj.gov/atr/public/guidelines/0618.htm> (hereinafter “State Prosecution Protocol”).

75 Robert L. Hubbard & Sondra Roberto, *State Merger Enforcement*, 6 Sedona Conf. J. at 3 (2005).

76 *Id.*

77 *Id.* at 4.

78 See Protocol for Increased State Prosecution of Criminal Antitrust Offenses.

79 *Id.*

80 *Id.*

81 431 U.S. 720 (1977).

Brick repealers,” that specifically permit recovery for indirect purchasers for violations of state antitrust laws.⁸² The Supreme Court ruled that these laws were not preempted by federal law in its seminal decision in *California v. ARC America Corp.*⁸³ In that case, the state attorneys general of Alabama, Arizona, California, and Minnesota brought suit against ARC America under Section 4 of the Clayton Act as indirect purchasers who fell victim to a price fixing conspiracy in violation of Section 1 of the Sherman Act.⁸⁴ The states also alleged violations of their state antitrust laws.⁸⁵ In approving a settlement agreement, the District Court denied relief of the states’ indirect purchaser statutes because it found that those laws were preempted by federal law, and the Ninth Circuit affirmed.⁸⁶ The Supreme Court, however, found that the state indirect purchaser statutes are not preempted:

[T]he Court of Appeals erred in holding that the state indirect purchaser statutes are pre-empted. There is no claim that the federal antitrust laws expressly pre-empt state laws permitting indirect purchaser recovery. [. . .] Congress intended the federal antitrust laws to supplement, not displace, state antitrust remedies.⁸⁷

Moreover, the Court found that state indirect purchaser laws do not obstruct the “purposes and objectives of Congress,” stating that “[s]tate laws to this effect are consistent with the broad purposes of the federal antitrust laws: deterring anticompetitive conduct and ensuring the compensation of victims of that conduct.”⁸⁸

Ninety-seven years ago, in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, the Supreme Court held that minimum vertical price fixing, also referred to as minimum resale price maintenance, was *per se* illegal.⁸⁸ In 2007, the Supreme Court, in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, overruled the *per se* rule of *Dr. Miles* and replaced it with a rule of reason analysis.⁹⁰ Currently, 13 states forbid resale price maintenance,⁹¹ and the adherence of another eight states to federal precedent remains an open question.⁹² Moreover, 37 states filed an amicus curiae brief with the Supreme Court to implore the court not to overturn the *per se* rule of *Dr. Miles*.⁹³ The Vertical Restraints Guidelines issued by NAAG, last revised in 1995, currently describe resale price maintenance as *per se* illegal.⁹⁴

Two years prior to the Supreme Court’s decision, NAAG adopted a resolution that included numerous principles of state enforcement that takes a somewhat strident position of the states’ independence from federal antitrust enforcement.⁹⁵ The principles proclaim that “the federal antitrust laws were enacted by Congress with the intent that those laws complement rather than supplant state antitrust laws.”⁹⁶ Also, the principles state that NAAG “[o]pposes federal preemption of any state antitrust statutes, including indirect purchaser statutes, or other limitation of state antitrust authority, as such preemption or limitation would impair enforcement of the antitrust laws, harm consumers, and harm free competition.”⁹⁷

82 Antitrust Law Developments at 639 n. 118 (collecting statutes). Those states (and District) include Alabama, Arkansas, California, Colorado, the District of Columbia, Hawaii, Idaho, Illinois, Kansas, Maine, Maryland, Michigan, Minnesota, Mississippi, Nebraska, Nevada, New Mexico, New York, North Dakota, Oregon, Rhode Island, South Dakota, Utah, Vermont, West Virginia, and Wisconsin.

83 490 U.S. 93 (1989).

84 *Id.* at 97-98.

85 *Id.*

86 *Id.* at 99.

87 *Id.* at 101-02 (citing 21 Cong.Rec. 2457 (1890) (remarks of Sen. Sherman)) (footnote and other citations omitted).

88 *Id.* at 102 (citing *Illinois Brick*, 431 U.S. at 746; *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 485-486 (1977)).

89 220 U.S. 373 (1911).

90 127 S.Ct. 2705 (2007).

91 Richard A. Duncan and Alison K. Guernsey, *Waiting for the Other Shoe to Drop: Will State Courts Follow Leegin?*, 27 Franchise L.J. 173, 174 (Winter 2008). Those states include California, Connecticut, Kansas, Mississippi, Montana, Nevada, New Hampshire, New Jersey, New York, Ohio, South Carolina, Tennessee, and West Virginia. Note that New York and New Jersey hold contractual provisions that implement resale price maintenance unenforceable.

92 *Id.* at 177. Those states include Arkansas, Georgia, Maine, North Dakota, Vermont, and Wyoming.

93 See Briefs for the States of New York, Alaska, Arkansas, Connecticut, Delaware, Florida, Hawaii, Idaho, Illinois, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nevada, New Hampshire, New Jersey, New Mexico, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, South Dakota, Utah, Vermont, Washington, West Virginia, and Wyoming as Amici Curiae Supporting Respondents, *Leegin Creative Leather Prods. Inc. v. PSKS, Inc.*, 127 S. Ct. 2705 (2007) (No. 06-480), available at <http://www.antitrustreview.com/files/2007/02/leegin.pdf>.

94 *Id.* (citing Nat’l Ass’n of Attorneys General, Vertical Restraints Guidelines (2d ed. 1995)).

95 Nat’l Ass’n of Attorneys General, Resolution, Principles of State Antitrust Enforcement (2005), available at <http://www.abanet.org/antitrust/at-committees/at-state/pdf/modernization/naag-sp2005-res.pdf>.

96 *Id.* at 1.

97 *Id.* at 2-3.

4. Findings in the US Antitrust Modernization Commission Report

In its evaluation of state enforcement of antitrust laws, the US Antitrust Modernization Commission analyzed state enforcement using the NAAG State Antitrust Litigation Database.⁹⁸ The Commission found that of the 343 antitrust actions recorded during 1990 to 2006, 59 percent of the actions were undertaken with federal antitrust authorities.⁹⁹ The Commission also found that 80 percent of the enforcement actions dealt with “local or regional conduct.”¹⁰⁰ Forty-seven percent of the cases recorded involved price fixing, bid rigging, or market allocation, and 34 percent involved merger review.¹⁰¹ The remaining 19 percent consist of various forms of anticompetitive conduct, such as boycotts, tying, and resale price maintenance.¹⁰²

The Commission concluded that, overall, “[t]he available evidence suggests that . . . state and federal non-merger antitrust enforcement over the past seventeen years has been broadly consistent and not in conflict.”¹⁰³ The Commission recommended that no statutory change was necessary for state non-merger enforcement.¹⁰⁴ In addition, the Commission recommended no statutory change to the states’ role in reviewing mergers.¹⁰⁵ Additional recommendations for merger review included the encouragement of federal and state authorities to coordinate their merger review activities, to harmonize the application of substantive antitrust law, and to make investigative information requests consistent across federal and state authorities.¹⁰⁶

PART III: COOPERATION AMONG THE EU, THE US AND OTHER NON-EU COUNTRIES

Given the globalization of the economy and the cross-border nature of infringements, international cooperation – both at the bilateral and multilateral level – has become essential for the effective enforcement of competition rules. For example, in 2003, the DOJ, the European Commission (“EC”) Directorate-General for Competition, the Canadian Competition Bureau, and the Japanese Fair Trade Commission conducted simultaneous searches and interviews regarding suspected interrelated global cartel activity.¹⁰⁷ With the rise of multinational corporations and the global scope of commerce, multinational antitrust investigations and prosecutions are increasingly becoming the norm.¹⁰⁸

On the one hand, this cooperation can take place informally at a bilateral or multilateral level, for example through the implementation of the 1995 OECD Recommendation on international cooperation that provides a legal basis for the cooperation between the European Commission and the competition authorities of other OECD member countries. Activities carried out under the framework of the WTO, the OECD, and the International Competition Network (“ICN”) brought about substantial progress in the development of common standards to address specific issues.

On the other hand, the expansion of international economic relations increasingly requires that the EU and other countries conclude international agreements with other states and regions.

In 1967 the OECD recommended that the issues regarding the international enforcement of national competition laws be addressed during the negotiation of bilateral agreements. At the time, discussions amongst OECD member states resulted in a body of recommendations which would later

98 Antitrust Modernization Report at 190.

99 *Id.* at 191. The Commission noted that the NAAG State Antitrust Litigation Database defines “federal participation” as “there was a federal case related to the state case.” *Id.* Further, the Commission stated that the “database does not explain whether federal participation was ‘joint, parallel, or independent.’” *Id.*

100 *Id.*

101 *Id.* Figure 1 indicates that 29% of the merger review cases recorded involved federal participation and five percent without federal participation.

102 *Id.* at 195. Table A shows that six cases involving resale price maintenance occurred from 1999 to 2006.

103 *Id.* at 194.

104 *Id.* at 192-98. The Commission also recommended that state “non-merger enforcement should focus primarily on matters involving localized conduct and competitive effects.” *Id.* at 196-97.

105 *Id.* at 198-200.

106 *Id.* at 200-03.

107 Scott D. Hammond, U.S. Dep’t of Justice, Antitrust Div., An Update of the Antitrust Division’s Criminal Enforcement Program, Address Before the A.B.A. Section of Antitrust Law Cartel Enforcement Roundtable 1 (Nov. 16, 2005), available at <http://www.usdoj.gov/atr/public/speeches/213247.htm> (last visited July 18, 2008).

108 *Id.* (stating 90 percent of nearly \$3 billion in criminal fines collected from FY1997 to FY2005 came from international cartel activity and approximately 50 percent of corporate defendants were foreign based).

form the basis for many bilateral agreements, including the timely notifications of cases of interest to the other country, the sharing of information, the coordination of parallel investigations and mutual assistance in collecting evidence, as well as positive comity principles.

A. Cooperation Among the EU And Non-EU Countries

Today the EU engages in bilateral relations with a large number of countries and particular importance is placed on the bilateral cooperation agreements between the EU and USA, Canada and Japan, which – particularly the US agreement – have been developing satisfactorily. Under these agreements, competition authorities on both sides exchange information and coordinate their enforcement activities. Each side may ask the other to take on enforcement actions (positive comity), and each side must take account of the other's interests when enforcing competition rules (traditional or negative comity).

1. Administrative Agreements on Cooperation in Competition Law Matters: The Bilateral Agreements

a. United States of America

On September 1991, the Commission entered into the first independent agreement with the US on the issue of cooperation between competition authorities in the application of their competition laws ("EC/US Agreement"). The 1991 agreement was the first bilateral agreement to include the concept of positive comity. Furthermore, in 1998 the parties supplemented the agreement with another agreement regarding the application of "positive comity principles" in order to enhance the enforcement of their competition laws. The EC/US Agreement was intended to avoid or settle possible conflicts and has developed into an intensive cooperation between the European Commission and the two American competition authorities.

The EC/US Agreement covers the Commission's proceedings regarding competition law arising under Articles 81, 82, 85 and 86 EC as well as under ECMR and, within the US, competition proceedings carried out by the Antitrust Division of the Department of Justice and the Federal Trade Commission under the Sherman Act, the Clayton Act, the Wilson Tariff Act and the FTC Act.

The scope of the EC/US Agreement is limited to cooperation between the competition authorities at a federal level in the US and at the EC level in the EU. It excludes certain regulated sectors within the US, and does not establish a right for private parties. Moreover, this agreement must be interpreted in a manner consistent with the parties' existing domestic regulation. The main obligations of the EC/US Agreement are: (i) the obligation to notify the other party whenever the competition authorities become aware that their enforcement activities may affect the other party's important interests; (ii) a general obligation to provide the other party with the requested information unless the information falls under one of the exceptions and (iii) an obligation to assist to the other party's competition authorities in their enforcement activities and coordinate enforcement activities.

Thanks to efforts made on both sides to find a convergent policy, both EC and US authorities have reached compatible results, in particular due to the so-called negative and positive comity rules.

The negative comity principles require that an authority restrain itself in the application of its laws and regulations where the advantage gained from their application would be smaller than the negative effect they would have on the interests of another country's authorities.

In practice, the American authorities seem to have only once formally called upon the Commission, in *Boeing/McDonnell Douglas*,¹⁰⁹ to consider the interests of the American defense

109 OJ L 336/16, 1997.

industry in the investigation of the aforementioned concentration. Ultimately, the Commission was able to respect that request in its final Decision, authorizing the concentration.¹¹⁰

The positive comity principles, on the other hand, provide the parties with a framework for the common prosecution of certain practices, when anti-competitive practices in the territory of one party are also capable of affecting another party's significant interests. Thus, if one party believes that antitrust infringements taking place on the other party's territory are adversely affecting its important interests, it can inform the other party and request that appropriate enforcement activities be carried out by the competent authorities. The notified party has the discretion to decide whether or not to undertake enforcement activities and the notifying party is not prevented from undertaking its own enforcement actions.

In particular, the purpose of the 1998 Positive Comity Agreement has been to improve the rules governing the division of cases between parties in the investigation of anticompetitive activities which adversely affect the interests of another party and which are impermissible under the domestic competition laws of the State in which they are taking place (Article I(1) of the Positive Comity Agreement). In this respect, the Court of First Instance has assumed that the main purpose of the agreement was to give one party the opportunity to benefit from the effects of a procedure initiated by the other party.¹¹¹

In any case, in addition to these measures used to enhance efficiency, the desire to avoid jurisdictional conflicts must also be emphasized.

The application of the 1998 Comity Agreement is subject to two important limitations: (i) the information provided by one party to the competition authorities of the other party to implement the agreement shall be used exclusively for that purpose unless the authority providing the information, as well as its source, consent to another use; and (ii) the applicable rule takes precedence over the Comity Agreement.

To date the positive comity mechanism has only been formally used in *Sabre/Amadeus*¹¹² where US agencies asked the Commission to investigate anti-competitive conduct by several European airlines for their failure to provide Sabre, a US-based computer reservation system, with the same comprehensive and timely flight information they provided the European based Amadeus system. The Commission initiated proceedings against one airline following a request by the Department of Justice.

However other cases have been dealt with the positive comity principle on an informal basis: in *Nielsen* a competitor complained in both Europe and the US about an alleged abuse of dominant position by a research company. Since the complaint concerned practices employed mostly in Europe, the US authorities entrusted the Commission to carry out the proceedings as soon as they were ensured that the Commission would take action. Nevertheless, the Commission got the US authorities involved in the investigation, and they were able to close their proceedings shortly after the Commission did.¹¹³

Similarly, the Commission was able to better assess the proposed *Halliburton/Dressler* merger because it had already been the subject of negotiations between the parties and the US competition authorities.¹¹⁴

Moreover, in March 1999 the EC and the US agreed upon allowing reciprocal attendance at determined procedural stages in individual cases. Even if attendances had informal precedents, since US officials were informally present at the Commission hearings in the *Boeing/MDD* merger

110 Conversely, the Commission was recommended to exercise restraint in applying the ECMR after the *Oracle/Peoplesoft* merger was authorised in the U.S.

111 CFI Judgement of June 15, 2005, *Speciality graphites*, Case T-71/03, Section 116.

112 IP/00/835.

113 EC Com. Report on Competition Policy 26, 1996, 347.

114 EC Com. Report on Competition Policy 28, 1998, 351.

investigation, the chance provided for in the administrative arrangements was first used in December 1999, when officials of the Federal Trade Commission attended the Commission's oral hearing in the *BOC/Air Liquide* merger case.

While EC and US competition authorities have learned to cooperate closely to their mutual advantage, there are still concerns that US rules on discovery may undermine EU procedures, especially in the context of leniency applications.

This issue arose in the *Vitamins* cartel case when US plaintiffs sought to obtain full copies of leniency applications that were filed with the Commission to be used as evidence in their action for damages.

The Commission filed an *amicus curiae* brief in the matter of *In Re Vitamin Antitrust Litigation* where it did not dispute the possibility of suing leniency applicants for damages, but argued that the EC leniency program “*should not be available as a shortcut for plaintiffs*” because the application of discovery rules to EU leniency applications might “*undermine the effectiveness of the EC leniency program at a very critical stage of investigation.*”¹¹⁵ However, according to the plaintiffs, the defendants should take into account the fact that providing written statements to any governmental body “*waives any privilege or protection that otherwise may have shielded those materials from discovery.*”

The issue is not settled and shows the difficult balance of interests between protecting leniency applicants, whom authorities depend on to disclose the existence of cartels, and the plaintiffs' right to access information in order to bring an action, especially since private actions are now strongly encouraged by the Commission. The Commission has since then decided to follow the practice of US competition authorities and allow companies to apply for leniency orally.¹¹⁶

Notwithstanding this intensive cooperation, the Commission and the US antitrust authorities have reached different conclusions in several important cases.

With respect to mergers, the *GE/Honeywell* proposed merger, among others, was treated differently by the US Department for Justice, which cleared the merger and the Commission, which blocked it, showing that besides the challenge to aligning their procedures, the substantive tests carried out by the antitrust authorities do not converge entirely.¹¹⁷

The divergence in the approach to antitrust enforcement taken by the EC and US antitrust authorities was reinforced by the *Microsoft* case, which highlighted that unilateral behaviour is one of the most controversial issues in this area.

In this regard, it has to be recalled that some months after the EC decision on Microsoft, Mr. R. Hewitt Pate, then assistant Attorney-General for the Antitrust Division of the US Department of Justice stated: “*...Unilateral conduct remains the area of greatest separation between the general approaches of the US and the EU. At the broadest level, we in the United States might be said-in words suggested by Judge Posner at a recent Antitrust Division event to have a more Darwinian view of the competitive process. Over here, as a DG Comp economist has put it during the same program, there is a great emphasis on requiring that dominant firms limit themselves to ‘gentlemanly’ competition.*”

And EC Commissioner Mario Monti replied: “*...I think we are aiming at safeguarding conditions of Darwinian competition just as our American friends, provided it is Darwinian competition on the merit. If competition is Darwinian but through means other than the merit, then I believe that the competition authorities should be draconian.*”

¹¹⁵ See A. Burnside, H. Crossley: “Co-operation in competition: a new era?”, in *E.L.Rev.*, Sweet and Maxwell, April 2005, p. 252.

¹¹⁶ *Ibid.*

¹¹⁷ In speeches on this case, Charles James, who at the time was Assistant Attorney General for Antitrust at U.S. Department for Justice, pointed out that “*the DoJ had considered the merger to be procompetitive and beneficial to consumers*” that U.S. laws “*protect competition, not competitors*” and that “*the European approach ‘reflects a significant point of divergence.’*” The EU's reply was that it is mostly concerned with consumer welfare and that, in the long term, consumer welfare relies on effective competition, consequently the long-term risk of seeing competitors exit from the market is seen as more harmful than any advantage gained from the short-term improvements to competition. See A. Burnside: “GE, Honey; I sunk the Merger,” in *ECLR*, 2002, p.109.

In *Microsoft*, although both the Commission and the US Department of Justice kept each other informed throughout the duration of their respective proceedings against the corporation, in the US the case was resolved via a settlement, reached in 2002, which imposed largely behavioural remedies on Microsoft, while the Commission's proceeding in 2004 concluded by requiring Microsoft to disclose certain source code information, supply a version of Windows which does not include the Media Player, as well as the levy of a massive fine.

b. Competition Law Agreement EC/Canada

In 1999 the EC concluded a cooperation agreement with Canada that, for the most part, follows the agreements between EC and US.

The most relevant difference between the two agreements is the scope, given that the EC/Canada Agreement does not cover Article 86 EC proceedings. Another difference is that the catalogue of situations requiring a notification contains an additional circumstance requiring notification, *i.e.*, "enforcement activities that involve one of the parties seeking information located in the territory of the other party."

Under this agreement, each party's competition authority must, when carrying out coordinated enforcement activity, try to ensure that the other party's enforcement objective is also reached. Mechanisms of negative and positive comity are provided.

c. EC/Japan Competition Law Agreement

In 2003 the EC entered into an agreement with Japan on cooperation on competition law activities. The agreement was entered into exclusively by the EU Council. All relevant sections of the agreement follow the parallel agreements with the United States and Canada. It should be noted that the purpose of the EC/Japan Competition Law Agreement is not only to facilitate the cooperation and coordination between competition authorities but that such cooperation should contribute to the effective enforcement of each party's domestic competition laws. The first occasion was the *Heat Stabilisers and Impact Modifiers* case.¹¹⁸

d. Bilateral Relations with Korea and China

The Commission signed a Memorandum of Understanding with the Korea Fair Trade Commission in October 2004. It establishes a bilateral competition "dialogue," through which these authorities may exchange opinions on issues of competition policy and work together in case-related applications of their competition laws when it is admissible under their existing domestic laws.

Furthermore, the Chinese Department of Commerce and the Commission agreed in May 2004 to establish a "structured dialogue." This provides a forum for consultations on issues of competition policy and for assistance in the introduction of a competition regime.

2. Multilateral Cooperation

Since the end of World War II, attempts have been made to solve the legal and practical concerns raised by the parallel application of national competition laws, subject to the principle of territoriality, in the framework of a globalizing economy.

The draft of the *Havana Charter* (1948), the *UNCTAD Model Law* (1980) and the *Draft International Antitrust Code* (1993) were different attempts to find effective structures for governance at a multilateral level and thus respond to globalization.

In this respect, it has been affirmed that any form of "global solution" raises serious concerns about the economic and institutional differences between States. Moreover, according to this

¹¹⁸ EC Commission Report on Competition Policy 33, 2003, Section 697.

point of view, there is a serious objection that harmonization of the principles of competition law at a global level, would not be flexible enough to adapt quickly to new problems: “top down” solutions would even lead to insufficient enforcement.¹¹⁹

Therefore, as harmonization of competition law at the international level seems neither realistic nor desirable, international organizations seek to reach a consensus on a minimum set of standards at the international level.

While the draft of the *Havana Charter* contained a chapter on competition policy, this chapter was cast aside after the rejection of the Charter by the American Congress and forgotten during the *Uruguay Round*, which led to the creation of the WTO (1994), demonstrating the minor importance of competition law.

However, many provisions of WTO law refer to competition law concepts. The precise content of those general indications has yet to be developed because the WTO system is generally directed at States and thus does not have direct effects on business practices.

For example in *Kodak/Fuji* the US tried to argue that an exclusive agreement between Japanese wholesale distributors and a national manufacturer was an infringement of WTO law because it restricted trade. The dispute settlement panel of the WTO concluded that the toleration of anti-competitive practice of private persons does not constitute a *state* restriction of trade.¹²⁰

The WTO members made an attempt to include issues of competition law in the WTO system during the Ministerial Conference of Singapore in 1996, and the so-called “Singapore Issues” were put on the agenda of the Ministerial Conference of Doha of 2001 where a working group was appointed to concentrate on the principles of transparency, non-discrimination and the protection of procedural fairness.

However, during the Ministerial Conference of Cancun in 2003, the majority of the WTO members opposed the initiation of formal deliberation on a possible WTO competition agreement that was strongly supported by the EU.

Thus the EU, in order to improve multilateral coordination efforts which have yet to become a common competition framework, participates in informal international bodies. This fosters dialogue between authorities and experts, creating movement towards a convergence in competition laws and procedures, and towards the development of a new competition regime.

The idea is to achieve a convergence of national cartel law through voluntary adoption and gradual evolution. The biggest advantage of this “bottom-up” approach is that it respects the principle of subsidiarity and takes account of the States’ sovereignty over antitrust enforcement.

On the other hand, this approach causes delays and imbalances in the implementation of the proposed recommendations. In conclusion, convergence is less harsh, but much slower to achieve.

a. The OECD

One of the more important bodies for multilateral cooperation is the OECD. It was established in 1961 and brings together 35 countries to provide statistics on economic and social data so it can analyze and forecast economic developments and social changes and thus help countries find solutions to common problems related to market economy.

In particular the OECD’s Competition Committee is a source of policy analysis and provides governments with advice on important competition policy issues and market-oriented reform

119 See G. Roebing in G. Hirsch, F. Montag, F. Jurgen Sacker, “Competition Law: European Community Practice and Procedures,” Thomson Sweet & Maxwell, 2008, p 121 and 127.

120 WTO, WT/DS44/R-“Kodak/Fuji.”

by actively encouraging and assisting government decision-makers in tackling anti-competitive practices and regulations. Members of the Committee include senior representatives from the competition authorities in OECD countries, plus observers from a number of non-OECD countries. A larger number of countries participate through the Global Forum on Competition. Business and consumer representatives also participate in some Committee and Global Forum activities.

The OECD Committee works out *Best Practice Roundtables* and *Studies*, which provide statements on fundamental and sector specific topics of competition policy. Moreover, the Competition Committee proposes recommendations to the OECD Council of Ministers. They do not create binding law, but they often influence the development of the law in the OECD member states. Among these recommendations, there are the OECD Recommendation 1995 on International Cooperation; the OECD Recommendation 1998 on Effective action against hard core cartels; the OECD Recommendation 2001 on Structural separation in regulated industries; the OECD Recommendation 2005 on the merger review, whose content is similar to the ICN recommendation on the same topic.

b. The International Competition Network

The ICN was created in 2001, as a global antitrust network that was launched to “*provide competition authorities with a specialised yet informal venue for maintaining regular contacts and addressing practical competition concerns.*” It should be noted that the ICN does not have any binding power, but seeks to propose and adopt recommendations and guidelines to address relevant issues in the area of antitrust enforcement: it is an informal network of competition authorities which discusses topics of competition law and policy with the aim of providing recommendations for a convergence of procedural and substantial law.

Nowadays a large majority of the existing competition authorities joined the ICN (89, coming from 79 jurisdictions), including competition authorities from developing countries, as well as non-governmental bodies such as international organizations (*e.g.*, OECD and WTO), industry and consumer associations, associations and practitioners of antitrust law and economics and members of academia. ICN appoints project-related working groups that compare the individual jurisdiction’s different approaches in reports and conferences. When there are sufficient common features, at the annual conferences ICN presents Guiding Principles or Recommended Practices that have been endorsed by all competition authorities.

At present, ICN practice is mainly focused on a multi-jurisdictional merger review as the number of multiple notifications of large proposed concentrations has strongly increased. The ICN recommendations seek to reconcile the tension between the national control over mergers on one hand, and the desired coherent and efficient global regulatory framework on the other hand. If the recommendations are implemented they foster the convergence and a greater compatibility of the different proceedings thus making cross-border cooperation between the authorities of the ICN more effective. Furthermore, the increased predictability of parallel proceedings reduces the regulatory barriers for the merging undertakings.

This is an example on how the “bottom-up” approach can, in the long term, bring to a gradual convergence of national antitrust rules and a development of a global competition culture, possibly leading to the codification at international level.

c. Legal Relationships with Candidate Countries

Nowadays, the European Union has accession relationships with Croatia, Turkey, Macedonia and Albania. The agreements contain several provisions on the development of competition policy and state aid rules in those countries. Moreover, the Association Agreement between the EC and Turkey differs from the competition rules of other agreements of the EC, by allowing for the possibility of sanctions for private persons (Articles 32-33 Decision of the Association Council No. 1/95).

d. Regional Association Processes

The European Union has association agreements with the Southern Mediterranean Region (“EuroMed”) and with the neighboring CIS States. These agreements contain an obligation of the partner countries to introduce competition and state aid discipline.

Moreover, the European Union has intensified its political and economic dialogue with the African, Caribbean and Pacific countries (“ACP countries”) with the Cotonou Agreement, entered into force on April 1, 2003 and replacing the so-called Lomé Agreements. It provides for the implementation of rules and policies on restrictive agreements or practices as well as assistance and co-operation in drafting an appropriate legal framework.

e. Free Trade Agreements

Legal relations between the EC and Switzerland are based on the bilateral Free Trade Agreement of 1972 and seven other bilateral agreements, which entered into force on June 1, 2002. The substantive rules on competition declare that restrictive agreements, abuses of a dominant position and any state aid are incompatible with the proper functioning of the agreements in so far as they may affect trade between the EC and Switzerland.

The EC and its member states entered into other free trade agreements, containing competition rules, with Mexico (entered into force on October 1, 2000), Chile (signed in 2002) and South Africa (entered into force on May 1, 2004).

B. Cooperation Among the US And Other Countries’ Antitrust Authorities

1. US Diplomatic Instruments Enabling Cooperation Between Nations

The United States and eight nations have put in place executive, bilateral agreements through which they coordinate antitrust enforcement and investigations.¹²¹ In general, these agreements provide notification of investigations, sharing of non-confidential information, coordination of investigations, and consultation to resolve problems and disputes.¹²² The International Competition Policy Advisory Committee, as appointed by former President Bill Clinton and former Attorney General Janet Reno, described the bilateral agreements as:

Each of these agreements reflects two themes: enforcement cooperation, on the one hand, and the avoidance or management of disputes, on the other. According to the US Department of Justice, the extent to which one or the other of these themes has predominated in a particular agreement has depended on the specific bilateral concerns and history from which the agreement emerged. In addition, the most recent bilateral agreement includes a third theme, that of technical cooperation.¹²³

Enacted in 1994, the International Antitrust Enforcement Assistance Act enables executive agreements, if negotiated with certain conditions, to include provisions for the exchange of confidential information between antitrust authorities but does not allow the disclosure of confidential information for multinational merger review.¹²⁴ However, so far, the United States has entered into only one such agreement.¹²⁵ Nonetheless, the degree of cooperation is still quite considerable.

¹²¹ Antitrust Law Developments at 1261. Those countries include Germany, Australia, the European Communities, Canada, Israel, Japan, Brazil, and Mexico. Because these instruments are executive agreements, they do not affect existing law, such as prohibitions on the disclosure of confidential information without consent.

¹²² *Id.* at 1262.

¹²³ See International Competition Policy Advisory Committee to the Attorney General and Assistant Attorney General for Antitrust, U.S. Dept of Justice, Final Report, Annex C-1, v (Feb. 28 2000), available at <http://www.usdoj.gov/atr/icpac/finalreport.htm> (last visited July 18, 2008) (hereinafter “ICPAC Report”).

¹²⁴ *Id.*, Annex C-1, at vii.

¹²⁵ Agreement Between the Government of the United States of America and the Government of Australia on Mutual Antitrust Enforcement Assistance (1999), available at <http://www.usdoj.gov/atr/public/international/docs/usaus7.htm> (last visited July 18, 2008).

The United States Executive Branch has also negotiated and the United States Senate has approved Mutual Legal Assistance Treaties (“MLATs”) with more than 30 countries.¹²⁶ These treaties facilitate cooperation between nations in criminal antitrust matters, including the compulsion of evidence and the obtainment of confidential investigation information.¹²⁷ The DOJ’s Office of International Affairs serves as a point of contact for MLAT-related matters.¹²⁸

2. Findings in the United States’ Antitrust Modernization Commission Report

The United States’ Antitrust Modernization Commission analyzed cooperation between the US antitrust authorities and the rest of the world and decided that, for the most part, the DOJ and FTC worked closely and efficiently with other nations on antitrust-related issues.¹²⁸ At the same time, the Commission made a number of recommendations and findings. First, the Commission notes that 70 jurisdictions require notification of a proposed merger, and the filing requirements for each nation remain heterogeneous, and in aggregate, quite expensive.¹³⁰ The Commission recommended that the DOJ and FTC conduct a feasibility study, in coordination with other nations, of “some kind of common premerger notification system across countries that would reduce the burden associated with multiple filings.”¹³¹

Second, the Commission recommended that principles of both negative and positive comity be inserted into most bilateral and multilateral agreements because it provides “a useful mechanism to avoid duplicative enforcement and to reduce instances of potentially conflicting decisions.”¹³² The Commission recommended that comity should promote the goals of deferral, harmonization, coordination mechanisms, and benchmarking reviews.¹³³ Regarding deferral, a country, if the transaction or conduct does not impact its jurisdiction to as great of an extent as another country, would not seek an enforcement action or to impose remedies and defer to the other jurisdiction.¹³⁴ The harmonization of remedies principle simply means that, rather than limiting other nations from imposing different remedies, nations would have confidence that the first country to act would be “competent and free from political influence.”¹³⁵ The coordination mechanism and benchmarking review principles allow for entities subject to conflicting remedies will have an avenue to request the nations to consult with one another, and the benchmarking review principle would encourage nations that impose disparate remedies to conduct a “retrospective evaluation as to why the usual cooperation mechanisms failed.”¹³⁶

Conclusion

There has been a lot of effort to improve coordination and cooperation among national antitrust enforcement agencies in the EU and the US. Is the level of coordination and cooperation sufficient? The answer to that question is debatable. There are still differences in approach and there is still lack of coordination in certain areas. For example, in certain circumstances, confidentiality requirements limit cooperation on parallel case development in different jurisdictions. There are also substantive law differences among different national competition authorities, especially in the US. For example, in the US, there are differences in the law enforcement approach at the DOJ and at the FTC in monopolization cases, especially as those matters relate to intellectual property and competition law interfaces.¹³⁷ Some also argue that there are differences in merger enforcement views

¹²⁶ *Id.* at 181 n.7.

¹²⁷ Antitrust Law Developments at 1262; U.S. Dept. of State, Mutual Legal Assistance (MLAT) and Other Agreements, http://travel.state.gov/law/info/judicial/judicial_690.html (last visited July 18, 2008) (showing MLATs currently in force or pending Senate approval).

¹²⁸ U.S. Dept. of State, Mutual Legal Assistance (MLAT) and Other Agreements (directing prosecutors to contact Office of International Affairs).

¹²⁹ Antitrust Modernization Report at 213-14, 216.

¹³⁰ *Id.* at 217 (citing PricewaterhouseCoopers survey that found mergers typically required eight complete filings and cost \$3.8 million to \$11.5 million). It remains doubtful that there more than a handful of mergers which have been reported to much more than a dozen jurisdictions that require notification. This is based on an informal survey of several experienced practitioners.

¹³¹ *Id.* (noting that Germany, France, and Britain attempted a joint filing system but its use was infrequent).

¹³² *Id.* at 221.

¹³³ *Id.* at 223.

¹³⁴ *Id.* at 223-24. The Commission divided deferral between complete deferral, where a “direct, substantial, and reasonably foreseeable” standard would apply, and presumptive deferral in which choice-of-law principles would determine the nation to which deference would be paid.

¹³⁵ *Id.* at 224.

¹³⁶ *Id.* at 224-25.

¹³⁷ See Willard K. Tom, “The DOJ/FTC Report on Antitrust Enforcement and Intellectual Property Rights,” *Antitrust*, Summer 2007, Vol. 21, number 3, at 36-37.

and aggressiveness between the DOJ and the FTC.¹³⁸ Finally, there are arguably ambiguities surrounding several recent US Supreme Court antitrust opinions, as to which some controversy has been generated.¹³⁹

What insight, if any, does this provide to the inevitable questions surrounding “convergence” of the substantive antitrust laws in a global economy? The authors do not express any opinion, but rather offer two different viewpoints for consideration. One view is that to the extent there are differences in substantive antitrust enforcement among the authorities within the US, over time competition between the authorities will result in a superior substantive approach, and the same should apply for competition among substantive antitrust laws around the globe.¹⁴⁰ Furthermore, convergence of antitrust laws on a global basis may be too difficult and an unrealistic goal due to the unique political, social, legal and economic background of every country.¹⁴¹ While comity and cooperation are a good thing, acceptance of some difference in substantive law may be necessary when cooperation inevitably breaks down. This is especially the case given the uncertainty of the state of economics and its important role in antitrust law. Arguably further efforts to achieve better coordination and cooperation, both within the US and the EU and among each other, are of greater importance than achievement of complete convergence.

On the other hand, in an integrated global economy a single set of rules would certainly be more predictable, efficient and result in decreased legal fees, which in turn can spur economic growth and create efficiencies (factors of tremendous importance). Although there may be some benefits to competition among antitrust agencies, it could be argued that the inconveniences and inefficiencies the competitive process imposes on businesses make the result in the end not worth it. Moreover, some could question whether superior substantive approaches result from the competitive process.

138 See, e.g., Jonathan B. Baker and Carl Shapiro, “Reinvigorating Horizontal Merger Enforcement,” October, 2007, Prepared for the Kirkpatrick Conference on Conservative Economic Influence on U.S. Antitrust Policy, Georgetown University Law School, April 2007, organized by Robert Pitofsky, available at <http://faculty.haas.berkeley.edu/shapiro/mergerpolicy.pdf>

139 See Commissioner J. Thomas Rosch, “A Modest Proposal For Modest Antitrust Decisions at the Supreme Court,” presented at the Antitrust Section Spring Meeting of the American Bar Association, March 27, 2008, available at <http://www.ftc.gov/speeches/rosch/080327modest.pdf>.

140 See William E. Kovacic, Chairman, U.S. Federal Trade Commission, “Competition Policy in the European Union and the United States: Convergence or Divergence?,” Bates White Fifth Annual Antitrust Conference, Washington, D.C., June 2, 2008, available at <http://www.ftc.gov/speeches/kovacic/080602bateswhite.pdf>.

141 J. Thomas Rosch, Commissioner, U.S. Federal Trade Commission, “Has The Pendulum Swung Too Far? Some Reflections on U.S. and EC Jurisprudence,” Bates White Fourth Annual Antitrust Conference, June 25, 2007, available at <http://www.ftc.gov/speeches/rosch/070625pendulum.pdf>.

INTELLECTUAL PROPERTY AND ANTITRUST: TWO SCORPIONS IN A BOTTLE

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*“No monopolies shall be granted amongst us,
but of such new inventions that are profitable to the countrie,
and that but for a shor time”*

- Massachusetts Body of Liberties, 1641



The Congress Shall Have The Power ...

*To promote the progress of science and useful arts,
by securing for limited times to authors and inventors
the exclusive right to their respective writings and discoveries*

- U.S. Constitution, Article 1, Section 8



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Introduction. While it seems true that antitrust and intellectual property law are often like two scorpions in a bottle, is not always clear whether they are fighting, flirting or mating. It seems to depend on the season, the decade or the continent.

Today, it is politically incorrect to say out loud that there is a great conflict between patent law and competition law. All of the modern commentators today regard the patent laws and the antitrust laws as serving complementary purposes. They say that the limited exclusivity of patent laws promotes innovation and the efficient sharing of ideas, which in turn promote consumer welfare – a key purpose of antitrust and competition law. At some level of abstraction, this is no doubt true. Yet on the ground, in the trenches, in the agencies, and in the federal district courts, there is tension and often a degree of confusion. Intellectual property law, or at least US patent law, bestows on the owners of intellectual property rights (“IPR”) the right to exclude others from making, using, or selling their patented invention. For a long time, as discussed below, most courts considered this right to exclude to be the grant of a “monopoly.” Indeed, the 1641 Massachusetts Body of Liberties was explicit in this regard. And until just two years ago, a patent was presumed by competition courts to give its owner “market power” over the subject covered by the patent.

So whatever balance may be in place today between patent and competition law, it is youthful, and perhaps even short-lived. The individual report by the Federal Trade Commission, published in October 2003¹, expressed the view that the patent system in the United States was in need of repair and was in some ways more of a hindrance to competitive markets than a help. The Commission thus focused on questionable patents being issued by an understaffed and overworked PTO, and made a variety of recommendations: to allow post-grant review of and opposition to patents; to enact legislation to specify that challenges to the validity of the patent should be determined based on a preponderance of the evidence (rather than by clear and convincing evidence); to tighten the legal standards used to evaluate whether a patent is “obvious”; to require the PTO to consider possible harm to competition before extending the scope of patentable subject matter; to enact legislation to make it more difficult for a patentee to establish willful infringement; and to provide more money to the PTO to help look into all these things. This was a worthy undertaking.

This paper has a limited purpose – to try to highlight issues of current interest on both sides of the Atlantic and to make those issues sufficiently clear that they can be intelligently and interestingly discussed by people, including me, who have no special training in patent law but who have been or will be exposed to competition law in an intellectual-property setting. This paper spends a disproportionate amount of time dealing with the US law and policy on the western side of the Atlantic for two reasons: first, there is much more of it than there is in Europe and, second, it is much easier to find. So we begin with an overview of the current state of things at the IP/AT intersection in United States, including a small amount of foundational history. Along the way in places, and even more in Part 5, it presents the European approach to the space commonly occupied by IP and antitrust, which points in a rather different direction than the U.S. approach.

A. Some Brief Background

1. 1641-1930

For nearly 300 years, from 1641 up until about 1930, patents were King, despite the admonition in the Massachusetts Body of Liberties against monopolies, which in any event carved out an exception for “... such new inventions that are profitable to the countrie...” Antitrust was a toothless serf. During this period, the Supreme Court and lower federal courts were generally receptive to patents and the enforcement of patent rights. Patents in those years frequently stemmed from the work of the great American inventors, such as Thomas Edison, George Westinghouse and Cyrus McCormick, and the patent litigation of the day usually involved a vindication of the rights of individual inventors or their start-up companies, which were trying to compete with their larger competitors of the day.

¹ The FTC's Report, “To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy,” can be found at <http://www.ftc.gov/os/2003/10/innovationrpt.pdf>. For a brilliant Hymarx outline version of the entire Report, see the prepared remarks of FTC Chairman Timothy J. Muris, Competition and Intellectual Property Policy: The Way Ahead, before the American Bar Association, Antitrust Section Fall Forum (November 15, 2001), available at <http://www.ftc.gov/speeches/muris/intellectual.shtml>.

By way of example, the very first case ever to address the intersection of the patent and antitrust laws, *E. Bement & Sons, Inc. v. National Harrow Co.*,² upheld price fixing provisions in a patent pool. Then, in 1926, the Supreme Court upheld licensing price restrictions against government challenge in the *General Electric* case.³ The passage of the Sherman Act in 1890 had no immediate impact, although the Great Depression did.

2. 1930-1988

In a reversal of fortune that began during the 1930 in the midst of the Great Depression, and extended through the 1970s and a bit beyond, courts and the general public became increasingly hostile to patents. This hostility was based on the general understanding that patents were “monopolies” and, as such, were contributing to the increasing concentration of economic power, which in turn was perceived to be a significant cause of the Great Depression.

Much of this hostility found its way into the federal bench through judicial appointments made by President Roosevelt. Many of these appointees came from the ranks of those who were generally opposed to the visible excesses of big business and who perceived patent owners, by then often large corporate enterprises, as operating not in the public interest, but rather to make large fortunes for the few at the expense of many.

So it was that, starting in the 1930s, the Supreme Court repeatedly reminded the lower federal courts that patents were “monopolies.” The national suspicion of “monopolists” resulted in many decisions with “anti-patent” results, including:

- Restrictive infringement constructions
- Dislike of the contributory infringement remedy
- Frequent invalidity findings
- Restrictive validity requirements.⁴

In an antitrust setting, deeming a patent a “monopoly” had consequences. The evil Section 2 seeks to prevent or remedy is the exercise of monopoly or market power - the monopolist’s ability to control price or output - in ways that injure competition. Once the courts deemed a patent to have created a monopoly, many of the commercial practices of patentees became inherently suspect under Section 2.

In consequence, patent licenses also became subject to heightened scrutiny under Section 1 of the Sherman Act, prohibiting agreements that unreasonably restrain trade. In analyzing agreements under Section 1, it is almost always important to consider the market power of the parties to the agreement. If it was concluded that a patent holder has monopoly power, patent licenses came under closer scrutiny. This indeed occurred, and a group of patent licensing practices came to be considered *per se* unlawful under Section 1 because they were perceived as tending to “expand” the scope of the patent monopoly.

In addition, patent misuse – inequitable conduct by patent holders that can render the patent unenforceable – has deep roots in and close ties to antitrust law. As a result of the hostility of antitrust law to patents, a group of patent licensing practices rapidly came to be recognized as patent misuse and, thus, became bases to render patents unenforceable.

As the Depression of the ‘30’s gave way to the post war boom, the situation for patent holders became no better; well into the ‘70’s and beyond, the legal landscape at the crossroads of

2 186 U.S. 70 (1902).

3 *United States v. General Electric Co.*, 272 U.S. 476 (1926).

4 See generally, ABA Section of Antitrust Law, *Antitrust Law Developments* 1081 (6th ed. 2007).

patent and antitrust law remained often inhospitable for patent holders. These forces produced, in 1971, the infamous “Nine No-No’s” issued by the Antitrust Division.⁵

- (1) It is unlawful to require a licensee to purchase unpatented materials from the licensor;
- (2) It is unlawful for a patentee to require a licensee to assign to the patentee any patent which may be issued to the licensee after the licensing arrangement is executed;
- (3) It is unlawful to attempt to restrict a purchaser of a patented product in the resale of that product;
- (4) A patentee may not restrict his licensee’s freedom to deal in the products or services not within the scope of the patent;
- (5) It is unlawful for a patentee to agree with his licensee that he will not, without the licensee’s consent, grant further licenses to any other person;
- (6) Mandatory package licensing is an unlawful extension of the patent grant;
- (7) It is unlawful for a patentee to insist, as a condition of the license, that his licensee pay royalties in an amount not reasonably related to the licensee’s sales of products covered by the patent — for example, royalties on the total sales of products of the general type covered by the licensed patent;
- (8) It is unlawful for the owner of a process patent to attempt to place restrictions on his licensee’s sales of products made by the use of the patented process; and
- (9) It is unlawful for a patentee to require a licensee to adhere to any specified or minimum price with respect to the licensee’s sale of the licensed products.

Additionally, even if a patent related restraint was not *per se* unlawful under one of the Nine No No’s, it could still be found unlawful depending on the answers to the following questions:

- (1) Is the particular provision justifiable as *necessary* to the patentee’s exploitation of his lawful monopoly?
- (2) Are there available to the patentee *less restrictive alternatives* that are more likely to foster competition?
- (3) “Where the answer to the first question is no, and to the second is yes, the Department will consider bringing a case to challenge the restrictions involved.”⁶

This was not all that long ago. Antitrust was King; intellectual property was now the serf, although that was, for antitrust, the high water mark.

During the latter part of the ‘70’s, and even more so during the early days of the Reagan/Baxter regime, the Nine No-No’s were subjected to withering criticism and were set aside as a statement of either enforcement policy or the law itself. Two premises animated this new government policy at the IP/antitrust interface. First, a young Deputy to William Baxter, in an influential speech, made the point that there was nothing inherently wrong or anticompetitive about the market power conferred by a patent grant or other intellectual property rights:

While it is possible to debate the wisdom of the congressional decision to reward invention through the grant of what might be “market power,” it is indisputable

⁵ Address by Bruce Wilson, Special Assistant to the Assistant Attorney General (1971).

⁶ *Id.*

that Congress has made the choice. Accordingly, antitrust analysis is bound to accept the legality of the patent holder's monopoly position.⁷

This was repudiation of the Nine No No's, or at least most of their undergirding principles.⁸

Second, it came to be the received wisdom of the enforcement agencies that the value of the patent monopoly arises from the patent holder's ability to exploit his patent-based market power. It is only where market power is unlawfully obtained or exploited – that is, by means other than individual inventive effort – that a true antitrust problem arises. Thus, the independent decisions of the patent holder/patentee regarding the means by which an invention is to be combined with other productive inputs ought to be regarded as having no inherent anticompetitive import.

As the 1980's wore on, it became increasingly clear that enforcement policy would condemn only those intellectual property licensing arrangements that (a) restricted competition among technologies that were economic substitutes, or (b) excluded new technologies from the market, or (c) involved sham conduct designed to coordinate the pricing of the products not directly related to the patent. The antitrust laws were suddenly *not* viewed as hostile to licensing that represented an effort by the licensor fully to appropriate the inherent value of the intellectual property at hand.

3. 1988 and Beyond

In 1988, the Antitrust Division released its “Enforcement Guidelines for International Operations.” Section 3.6 of that document dealt with intellectual property licensing arrangements. It was the first real effort by the DOJ to develop a framework for thinking about intellectual property law and antitrust. The 1988 guidelines described a four step analysis. The *first step* examined whether the license restrained independent competition between the licensor and its licensee(s) in a relevant market and, if so, whether the license likely would create, enhance or facilitate the exercise of market power. This step in general was designed to analyze the competitive effects of cross licenses and patent pools involving competing technologies.

The *second step* examined whether the license expressly or implicitly restrained competition in some other market in which the licensor and licensee competed or would compete in the absence of the license. This inquiry was aimed at “spillover” effects. The Department was concerned about the competition that could occur if the licensee had access to the licensor's technology.

The *third step* examined whether the license would (a) result in anticompetitive exclusion (*e.g.*, exclusion other than that inherent in the intellectual property rights themselves), or (b) facilitate collusion in some market. This step drew heavily on the Reagan-era view that vertical restraints were, in general, benign and became unlawful only in exceptional circumstances -- such as where they facilitate collusion in horizontal markets resulting in anticompetitive exclusion from some essential input.

The *fourth and final step* examined whether any anticompetitive features were offset by procompetitive efficiencies generated by the license restrictions. This, of course, roughly paralleled the merger guidelines, which had by then been in force for more than five years.

Since 1988, literally hundreds of speeches, articles, papers, updated guidelines, agency reports, and of course judicial opinions, have issued addressing the intersection of IP and antitrust law. An extraordinary amount of time has been spent (and ink spilled) on the topic. The 1988 guidelines were superseded by the 1995 Intellectual Property Guidelines. Then, during the early years of the 21st-century the FTC and the DOJ held extensive hearings on the proper balance of

7 Abbott B. Lipsky, Jr., Deputy Assistant Attorney General, Antitrust Division, Current Antitrust Division Views on Patent Licensing Practices (November 15, 1981), *reprinted in* 4 Trade Reg. Rep. (CCH) Paragraph 13,129.

8 The Nine No No's have become a sort of parody. Almost nobody today actually reads them; instead they make fun of them as a symbol of something silly. But many of them still reflect the general view of the law today (#1, 4, 7 and, until last year, 9), and as our colleague Doug Rosenthal reminded me, in commenting on the antepenultimate draft of this paper, Bruce Wilson was a Republican.

competition and patent law and policy. These hearings resulted, in October 2003, in a report of several hundred pages from the FTC itself, which recommended a variety of changes to the patent system as summarized in the introduction to this paper.⁹ This was, even if flawed,¹⁰ a thoughtful and important document that in the long run might prove influential. Nearly four years later, in the spring of 2007, the two agencies issued their 123-page report on “Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition.” Meanwhile, of course, just in the last decade or so we have had a great many high profile IP cases and IP based antitrust cases or investigations involving Microsoft,¹¹ Intel,¹² QUALCOMM,¹³ Rambus,¹⁴ Xerox,¹⁵ Quanta,¹⁶ eBay,¹⁷ Verizon,¹⁸ and various pharmaceutical companies,¹⁹ among others. These cases, many involving technologies that are themselves barely a decade old, have been at least partly responsible for unleashing a tsunami of writings about the proper balance between protecting innovation and prohibiting monopoly.

Before going further, it is useful to dwell for a moment on the 1995 Guidelines for the Licensing of Intellectual Property, as they are still in effect and they still represent the enforcement policy of United States, notwithstanding the several hundred other pages of materials mentioned above issued both by the FTC and the DOJ.

First of all, the Guidelines set forth the view – considered almost radical at the time they were issued — that IP and antitrust have the common purpose: “of promoting innovation and enhancing consumer welfare.” (Section 1.0). The Guidelines announced that they were embracing three bedrock principles, most of them widely accepted today (although not completely, and in some cases grudgingly). However, at the time, none of the principles were really as embraced by the courts as they are today.

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- 9 See *n.1 supra*. When viewed in the broader context of reform in the United States, it seems clear that some of the FTC’s proposed changes are similar in nature or intent to those being considered currently by the United States Congress for the purpose of increasing the overall quality of granted patents. See The Patent Reform Act of 2007, H.R. 1908, S. 1145, 100th Cong. (2007). The 2003 FTC Report ended up being substantially embraced The Antitrust Modernization Commission too, see the Report and recommendations of the AMC, available at www.amc.com. The AMC’s main concerns surrounded the quality of patents issued, a certain laxity in the application of the obviousness requirement, and the limitations of the PTO in dealing with these problems. This may suggest that the focus is shifting away from the idea that the patent laws and competition laws are inherently in conflict, and reflecting instead a strengthening consensus that patents are not antithetical to competition so long as they are not misused or improvidently granted.
- 10 A most thoughtful critique of the FTC report was offered by Robert P. Taylor, “Imbalance” is in the Eye of the Beholder: A Comment on the FTC Report on Competition and Patent Law and Policy.” (March 3, 2004) (This paper was published, although I cannot find out right now where; I have a manuscript copy and would be happy to provide it to anyone who asks).
- 11 *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001) (*en banc*); Case T-2-1/04, *Microsoft Corp. v. Commission* (Sep. 17, 2007), available at <http://eur-lex.europa.eu/LexUriServ.do?uri=CELEX:62004A0201:EN:HTML>. It is also available via Lexis, where it is cited as 2007 ECJ EUR-Lex LEXIS 2620. The case will be referred to here simply as “*Microsoft CFI*” and citations will be to the pertinent paragraph number(s).
- 12 Intel is the target of a private action brought under Section 2 of the Sherman Act by Advanced Micro-Devices, Inc. *AMD et al. v. Intel*, Civil Action No. 55-441 (D. Del., filed January 27, 2005). The European Commission issued a press release on July 27, 2007 describing its Statement of Objections to Intel, brought as a result of a complaint launched by AMD with the EC. According to the Commissions release:
First, Intel has provided substantial rebates to a leading European personal computer retailer conditional on its selling only Intel-based PCs. Secondly, Intel made payments in order to induce a leading Original Equipment Manufacturer to delay the planned launch of a product line incorporating an AMD-based CPU. Thirdly, in a subsequent period, Intel has provided substantial rebates to that same OEM conditional on it obtaining all of its laptop CPU requirements from Intel.
Almost a year later, on July 17, 2008, the Commission issued a further release confirming that it had sent a supplementary Statement of Objections to Intel. According to that release:
“Each of the conducts outlined in the 26 July 2007 Statement of Objections and the SSO is provisionally considered to constitute an abuse of a dominant position in its own right. However, the Commission also considers at this stage of its analysis that all the types of conduct reinforce each other and are part of a single overall anticompetitive strategy aimed at excluding AMD or limiting its access to the market.
In the end, Intel is probably “simply” an Article 82 case without any special connection to intellectual property.”
- 13 QUALCOMM is the target of litigation by Broadcom and Nokia [*Broadcom Corp. v. Qualcomm, Inc.*, 501 F.3d 297 (3d Cir. 2007), *Nokia v. QUALCOMM*, Civil Action No. 06-509 JJE, 2006 US Dist. LEXIS 61383 (D. Del. Aug. 29, 2006)] in the United States and is the subject of an investigation by the EC in Brussels. The EC issued a release on October 1, 2007, announcing the initiation of formal proceedings against QUALCOMM in connection with a potential abuse of a dominant market position. The proceedings were commenced based on complaints lodged with the commission by Erickson, Nokia, Texas Instruments, Broadcom, NEC and Panasonic- all manufacturers of either mobile phones or chipsets. QUALCOMM is a holder of IPR in the CDMA and WCDMA standards for mobile telephony. The WCDMA standard forms part of the 3G (third generation) standard for European mobile phone technology.
The Commission pointed out in its release that the initiation of proceedings does not imply that the Commission has proof of an infringement, but only signifies that the Commission will conduct an in-depth investigation as a matter of priority.
According to the release, the alleged conduct concerns the terms under which QUALCOMM licenses its patents essential to the WCDMA standard and the investigation is focusing on whether QUALCOMM is dominant and whether the licensing terms and royalties imposed by QUALCOMM are, as alleged by the complainants, not fair, reasonable and nondiscriminatory (FRAND). As to the conduct relating to standardization, a finding of exploitive practices by QUALCOMM in the WCDMA licensing market contrary to Article 82 may depend on whether the licensing terms imposed by QUALCOMM are in breach of its FRAND commitment.
- 14 *Rambus Inc. v. Federal Trade Comm’n*, 522 F.3d 456 (D.C. Cir. 2008).
- 15 *In re Indep. Serv. Orgs. Antitrust Litigation*, 203 F.3d 1322 (Fed. Cir. 2000), *cert. denied*, 531 U.S. 1143 (2001).
- 16 *Quanta Computer, Inc. v. LG Elec., Inc.*, ___ U.S. ___, 128 S. Ct. 2109 (2008).
- 17 *eBay v. MercExchange, LLC*, 547 U.S. 388 (2006).
- 18 *Verizon Commc’ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004).
- 19 *In Re: Tamoxifen Citrate Antitrust Litigation*, 429 F.3d 370 (2d Cir. 2005); *Schering-Plough Corp. v. FTC.*, 402 F.3d 1056 (11th Cir. 2005); *Imperial Chem. Indus., PLC v. Heumann Pharm. GmbH & Co.*, 991 F.2d 811 (Fed. Cir. 1993), discussed in part 6, below.

1. Intellectual property is considered to be essentially comparable to other forms of property. Recall that in the early years, court decisions embraced the notion that patent holders enjoyed “... absolute freedom in the use or sale of rights under the patent laws of the United States” because the “very object of these laws is monopoly.”²⁰ It was based on this principle that the Supreme Court permitted horizontal price-fixing²¹ and minimum resale price maintenance²² by holders of intellectual property that would have been *per se* illegal had it involved tangible property. While this first principle has been criticized as giving little guidance, and misleadingly suggesting an overly simplistic approach to complex issues,²³ it is nonetheless a helpful first step at demystification of the field. Intellectual property rights are just like other property rights, but they are often very complicated packages or bundles of rights. A lot of intellectual property rights certainly do begin to look more complicated when they are put in pools together, when they are assembled in “thickets,” and when one tries to ascertain what other packages or bundles of rights might be thought to be competing with, and hence in the same market as, a particular patent and its associated claims. And, of course, the rights associated with patents are often contestable, making them difficult to pin down or stabilize for the purpose of the analyses required by antitrust.

2. There is no presumption that intellectual property generates market power in a relevant market for antitrust purposes. Previously, courts had condemned various practices they viewed as falling outside the protection of the patent and copyright laws because they were not inherent in the patentee’s exploitation of its statutory “monopoly.” Thus, Courts considered these practices — including tying, grantbacks, exclusive dealing, and package licensing — unlawful under the antitrust laws.²⁴ While Congress had amended the Patent Act in 1988 to clarify that the grant of a patent should not be equated with market power for purposes of the patent misuse defense,²⁵ it was not until the Supreme Court’s recent decision in *Illinois Tool Works v. Independent Ink, Inc.*,²⁶ that the judiciary finally abandoned the presumption in antitrust cases that intellectual property conferred market power or monopoly power.

This does not, of course, mean that patents never confer market or monopoly power: they may indeed do so if there is no other substitute readily available. But the absence of the presumption leaves patent holders far more secure from attacks based on Section 1 of the Sherman Act.

3. Licensing is generally procompetitive inasmuch or insofar as it allows firms to combine complementary factors of production in an efficient manner. For most practical purposes, the important aspects of the Guidelines spring from this proposition. As the agency put it:

Licensing, cross-licensing, or otherwise transferring intellectual property can facilitate integration of the licensed property with complementary factors of production. This integration can lead to more efficient exploitation of the intellectual property, benefiting consumers through the reduction of costs and the introduction of new products. Such arrangements increase the value of intellectual property to consumers and to the developers of the technology. By potentially increasing the expected returns from intellectual property, licensing also can increase the incentive for its creation and thus promote greater investment in research and development.²⁷

Again, this does not mean that all licensing is good, but in most cases, the antitrust issues are likely to be of a more obvious sort. Generally, licensing schemes will not raise antitrust issues, except for cases where: licenses effectively divide markets; the licensing arrangement effectively amounts to a merger of close competitors and hence the elimination of competition; the arrangement might foreclose or limit competitors’ access to required inputs; or where the arrangement might facilitate coordination

20 *Bement, Inc., v. National Harrow Co.*, 186 U.S. 70, 91 (1902).

21 *Id.* at 91-92.

22 *United States v. GE, Co.* 272 U.S. 476, 490 (1926).

23 Biester, Reevaluating the 1995 Antitrust Guidelines for the Licensing of Intellectual Property, *Antitrust Magazine*, 9 (Summer 2002).

24 Cases on these collected in ABA Section of Antitrust Law, *Antitrust Law Developments* (6th ed. 2007), 1081.

25 35 U.S.C. (d) (5).

26 547 U.S. 28 (2006).

27 Guidelines, Section 2.3.

between or among competitors. In Europe, there is the additional and consequential issue of whether a refusal to grant a license, or particular terms contained within a license, might amount to of an abuse of a dominant position under Article 82 of the EC Treaty (or a violation of Article 81), all of which is addressed in Part 5 of this paper below.

Beyond these three guiding principles, the Guidelines address the mode of analysis (Section 3.4) (nearly always rule of reason); set forth some general principles (Section 4);²⁸ provide a safe harbor (Section 4.3);²⁹ and provide some guidance with respect to specific areas, these being: horizontal restraints (Section 5.1), Resale Price Maintenance (Section 5.2), Tying (Section 5.3), Exclusive Dealing (Sections 4.1.2 & 5.4), Cross-Licensing and Pooling Agreements (Section 5.5), Grantbacks (Section 5.6), Acquisition of Intellectual Property (Section 5.7) and Enforcement of Invalid IP (Section 6).

The Guidelines do not address, however, what has become one of the hottest topics in IP/antitrust—the issues arising out of the settlement of patent litigation between brand-name drug companies and generic companies in the context of litigation generated by the Hatch Waxman Act and they also do not address the entire area of the role of antitrust in policing the use and abuse of IP in standard setting, also a vital area today both in the United States and Europe. This paper now visits these areas serially in an effort to explicate the state of the law, the state of important or conflicting government policy where appropriate, and generally to highlight important or attention-grabbing issues. Along the way, and also separately, the paper attempts to provide an understanding of the state of law and policy on many of these issues in Europe, or at least the European Union.³⁰

B. Current Issues

Most of the action at the confluence of IP and antitrust falls into one of a handful of “buckets.” These buckets, some of which are big and some of which are small, are describable as follows:

1. Conduct by the patentee that involves an effort to enforce rights the patentee does not really have. It is useful to think of this area of the law as involving essentially three different scenarios, although there may be variations of each. First, there is the classic situation described in *Walker Process*³¹ involving the enforcement of a patent procured by fraud on the Patent Office. Efforts to enforce such a patent may give rise to liability under Section 2 of the Sherman Act “... provided the other elements necessary to a Section 2 case are present.” This has always been a somewhat murky, yet more or less straightforward area of the law, although that is changing (it is becoming both less murky and less straightforward). Over the years, the “enforcement” requirement became its own critical element in *Walker Process* litigation.³² This has now changed as a result of the decision of the Federal Circuit in *Hydril Co. LP v. Grant Prideco LP*.³³ The court there held that the threat of enforcement activity directed against a rival’s customer was enough to satisfy the “enforcement” requirement of a *Walker Process* claim. What the Court said was:

Threats of patent litigation against customers, based on a fraudulently-procured patent, with a reasonable likelihood that such threats will cause the customers to cease dealing with their supplier, is the kind of economic coercion that the antitrust laws are intended to prevent. A supplier may be equally injured if it

28 “When a licensing arrangement affects parties in a horizontal relationship, a restraint in that arrangement may increase the risk of coordinated pricing, output restrictions, or the acquisition or maintenance of market power. Harm to competition also may occur if the arrangement poses a significant risk of retarding or restricting the development of new or improved goods or processes.”

“When the licensor and licensees are in a vertical relationship, the Agencies will analyze whether the licensing arrangement may harm competition among entities in a horizontal relationship at either the level of the licensor or the licensees, or possibly in another relevant market. Harm to competition from a restraint may occur if it anticompetitively forecloses access to, or increases competitors’ costs of obtaining, important inputs, or facilitates coordination to raise price or restrict output.”

29 Absent extraordinary circumstances, the Agencies will not challenge a restraint in an intellectual property licensing arrangement if (1) the restraint is not facially anticompetitive and (2) the licensor and its licensees collectively account for no more than twenty percent of each relevant market significantly affected by the restraint. This “safety zone” does not apply to those transfers of intellectual property rights to which a merger analysis is applied. See section 5.7.

30 A main, new, and important source of guidance in Europe is the 2004 Commission Guidelines on the Application of the EC Treaty to Technology Transfer Agreements, see Comm’n Reg. No. 772/2004, [2004] O.J. 2004 L 123/11.

31 *Walker Process Equip., Inc. v. Food Mac. and Chem. Corp.*, 382 U.S. 172 (1965).

32 See, Christopher R. Leslie, New Possibilities for Asserting *Walker Process* Claims, *Antitrust Magazine* 48-49 and nn. 7-8 (Summer 2007).

33 474 F.3d 1344 (Fed. Cir. 2007).

loses its share of the market because its customers stop dealing with it than if its competitor directs its monopolistic endeavors against the supplier itself. Without customers, a supplier has no business.³⁴

What this means is that patentees who are vulnerable to a claim that they procured their patent through fraud no longer have the kind of safe harbor at the margin that they used to have.³⁵

Walker Process claims are often raised as counterclaims in patent infringement actions and hence, if appealed, end up before the Federal Circuit. This can be important as a matter of what substantive law applies.³⁶ The most important case in this area is *Nobelpharma AB v. Implant Innovations, Inc.*,³⁷ which found that *Walker Process* and the sham exception to *Noerr*³⁸ "...provide alternative legal grounds on which a patentee may be stripped of its immunity from the antitrust laws; both legal theories may be applied to the same conduct."³⁹ Second, there are the slightly similar situations where a patentee might either commence enforcement on a patent in good faith, but along the way come to learn that critical prior art was not disclosed to the PTO, or might institute litigation with knowledge that its patent is for some reason invalid. The leading case in this area is *Handgards, Inc. v. Ethicon, Inc.*,⁴⁰ but there are several others too. Unlike a *Walker Process* claim, which requires the plaintiff to prove that the defendant knew it was enforcing a patent obtained by fraud, this theory requires only that the plaintiff show the defendant learned sometime before suit was filed (or even during the pendency of suit) that the patent was not valid, enforceable, or infringed. Thus the continuation of ongoing litigation can become liability producing if, as and when the plaintiff comes to learn that he has no case.

Third, there is a developing variation on these two themes. Suppose a plaintiff has a patent that is valid and plainly not procured by fraud. But suppose that the plaintiff, either alone or in concert with others proceeds knowingly and serially to assert patent claims against defendants the patentee knows or should know do not in fact infringe the patent. In such circumstances, a party whose goods are claimed to infringe the patent(s), and who is threatened by this serial litigation, even against his customers, may have a claim under Section 1 of the Sherman Act for conspiracy (assuming concerted action) or under Section 2 of the Sherman Act for monopolization or attempted monopolization (or conspiracy to monopolize) where the subject matter of the patent itself may describe a pertinent relevant market, either a goods market or a technology market. See *Rockwell Automation, Inc. v. Schneider Automation, Inc. et al.*⁴¹ The case proceeded for years after the motion to dismiss was denied and eventually settled. While the case was decided prior to the Supreme Court's decision in *Twombly*,⁴² there is little reason to believe that *Twombly* would have made any difference.⁴³

2. Acquisition of patents that might violate the antitrust laws, whether Sections 1 or 2 of the Sherman Act, or Section 7 of the Clayton Act. Conceptually, this is a relatively straightforward area. Nearly all of the activity here is at the federal level in the context of merger or joint venture reviews of one sort or another. This does not mean that there are not opportunities for private enforcement in this area, but the opportunities are probably quite limited and a keen understanding of the problem, if there is one, is likely to be difficult for outsiders to the technology or industry.

³⁴ *Id.* at 1350.

³⁵ Somewhat of a piece with this development is the Supreme Court's decision in *MedImmune, Inc. v. Genentech, Inc.*, 127 S. Ct. 764 (2007), which repudiated the Federal Circuit's "reasonable apprehension of suit" test for obtaining a declaratory judgment. The Supreme Court found the Federal Circuit's test inconsistent with the Supreme Court's own declaratory judgment jurisdiction and the Court was critical of the Federal Circuit for making it too difficult for competitors to challenge the validity of a rival's patent.

³⁶ See generally, ABA Section of Antitrust Law, *Antitrust Law Developments* (6th ed. 2007) 1090-91.

³⁷ 141 F.3d 1059 (Fed Cir. 1998).

³⁸ *Eastern R.R. Presidents Conference v. Noerr Motor Freight*, 365 U.S. 127 (1961), providing First Amendment protection to petitioning activity, including the filing of good faith non-sham antitrust lawsuits.

³⁹ *Nobelpharma AB*, 141 F.3d at 1071.

⁴⁰ 601 F.2d 986 (9th Cir. 1979).

⁴¹ Case No. 02-C-1195 (E.D. WI, Sep. 30, 2003) (denying defendants' motions to dismiss for failure to state a claim).

⁴² *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955 (2007), is an extremely important US Supreme Court decision requiring antitrust plaintiffs, and indeed other plaintiffs in general, to plead facts sufficient to support the conclusions alleged and eviscerating several decades of cases generally holding that if a plaintiff could prove "any set of facts" in support of his claim, his case could proceed beyond a motion to dismiss.

⁴³ Generally, just because a patent owner loses its case does not mean it did not have probable cause when it filed suit. For a situation to constitute a sham litigation, it must be the case that the patent owner learns it has no case *before judgment* but nevertheless continues to pursue its case.

3. Conduct by the patentee that involves tying (or maybe a tie-out) or bundling. This discussion assumes a working knowledge of the law of tying and bundling generally, at least in the United States. It does not assume knowledge of bundling or “range effects” in Europe. More so than in other areas of antitrust, lawyers and economists tend to think of tying or bundling in an intellectual-property setting as involving either “contractual” or “technological” tying or bundling. Classic “contractual” patent tying occurs when the tying product (such as a mimeographed machine) is patented, the tied product is an unpatented commodity used as an input (such as ink or paper), and the sale of the patented product is conditioned on the purchase of the unpatented product.⁴⁴ The analysis in general is relatively straightforward, at least in theory. As in any other type of tying, coercion is the essential element, and hence to establish unlawful tying there must be evidence that licensees were in some way forced to take a product they did not want.

This often comes up in a patent misuse setting where the defendant seeks to eviscerate the plaintiff’s patent by asserting patent misuse as an affirmative defense. Incidentally, it is worth being aware that patent misuse is often a much more powerful weapon than an antitrust counterclaim. While attorneys’ fees and treble damages are not available, the threat to the plaintiff is that the patent becomes unenforceable until the misuse is purged. More importantly, perhaps, the assertion of an affirmative defense of patent misuse, unlike the assertion of an affirmative antitrust claim or counterclaim, is not freighted with issues of standing, antitrust injury, injury in fact, damages and so forth, all of which can make an antitrust plaintiff’s life unusually difficult and burdened.⁴⁵

A “technological tie” is one in which “the tying and tied products are bundled together physically or produced in such a way that they are compatible only with each other.”⁴⁶ An example would be a razor and razor blade cartridge. The U.S. Government’s tying claim against Microsoft involved both a contractual and a technological bundling of the Internet Explorer Web browser (the tied product) with Microsoft’s Windows operating system (the tying product).⁴⁷ In many cases different intellectual property rights may themselves be combined into bundles or packages. Mandatory package licensing occurs when a patent owner refuses to license a particular patent unless a licensee accepts an entire package (or where the patent owner’s royalty scale has this effect). The notion includes “block booking” of motion pictures or television shows.⁴⁸

The circuit courts and the lower courts in general have not taken a consistent analytical approach to tying and bundling cases involving intellectual property. Package licenses generally come under the same set of rules as tying and bundling. At one extreme, the Eleventh Circuit applied the *per se* rule to a package license for television programming since the package at issue could not be distinguished from the block booking that the Supreme Court declared to be illegal *per se* in *United States v. Loew’s, Inc.*⁴⁹ On the other hand, the D.C. Circuit in its *en banc* *Microsoft*⁵⁰ decision declined to apply the *per se* rule to “platform software,” thereby carving out what has been described as a “technology exception” to the *per se* rule. The Federal Circuit, reversing the International Trade Commission, has also rejected a *per se* approach in a package licensing case and applied traditional tying case law to find that a package license combining alleged “essential” with “nonessential” patents did not constitute patent misuse because there was no separate demand for the “nonessential” patents, and thus no separate product market in which competition could have been foreclosed.⁵¹ The court

44 See US Dep’t of Justice & Fed. Trade Comm’n, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* (2007) 107.

45 Although establishing patent misuse is simpler than establishing an antitrust violation, a recent line of cases from the Federal Circuit incorporated traditional relevant market/antitrust analyses into the analysis. For example, the Federal Circuit in *Philips Corp. v. Int’l Trade Comm’n.*, 424 F.3d 1179 (Fed. Cir. 2005), concluded that, in certain cases, the doctrine of patent misuse under 35 U.S.C. Section 271(d) may even be narrower than the corresponding antitrust laws. Because 35 U.S.C. Section 271(d) designates several forms of conduct, including certain types of patent license tying, as not constituting patent misuse unless the patent holder has market power for the patent on which the license is conditioned, the Federal Circuit has concluded that patent misuse cannot be found in cases where it cannot be demonstrated that the patentee does not have market power, and need not be found even in cases where market power can be demonstrated. Consequently, even though the patent misuse doctrine is theoretically broader than the antitrust laws, in practice their scope may be much the same. Still, though, the procedural hurdles attending a misuse claim are noticeably fewer than those accompanying an antitrust claim.

46 1 Hovenkamp *et al.*, *IP and Antitrust* Section 21.5b2, at 21-104-05.

47 *United States v. Microsoft Corp.*, 253 F.3d 34, 45 (D.C. Cir. 2001)(*en banc*).

48 US Dep’t of Justice & Fed. Trade Comm’n, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* (2007) 107.

49 371 U.S. 38 (1962).

50 *Microsoft*, 253 F.3d at 95.

51 *Philips Corp. v. Int’l Trade Comm’n.*, 424 F.3d 1179, 1193-97 (Fed. Cir. 2005).

rejected a *per se* approach “[i]n light of the efficiencies of package patent licensing and the important differences between product-to-patent tying arrangements and arrangements involving group licensing of patents. . . .”⁵²

The antitrust treatment of these types of licenses depends mainly on whether the licensee has been forced to accept the package as a condition for receiving one or more desired licenses. Consensual package licenses not involving some form of coercion are generally found lawful and also do not amount to patent misuse. Where the price of the package sought does not vary depending on the number of licenses in it, there should not be any issue, and where for activities under one patent and package could not be carried out without infringing all patents in the group, then even theoretical “coercion” does not create liability.⁵³

Slightly similarly, the Federal Circuit held that a contractual tie that prevented licensees of Monsanto’s patented herbicide tolerance trait from using a non-Monsanto herbicide was not misuse when only Monsanto’s herbicide had been approved by the EPA for use with the Monsanto trait.⁵⁴ While the court took note that the Supreme Court had not permitted justifications for anticompetitive conduct unrelated to the public interest in competition, it found that the tie should be analyzed under the rule of reason and did not have the anticompetitive effect required to constitute patent misuse because it was the government registration restriction, not Monsanto’s contract, that limited competition.⁵⁵

In short, tying still presents legal challenges to companies and their counsel, and, concomitantly, opportunities for the plaintiffs’ bar. But in most cases the analysis is not particularly complicated and competition lawyers should not be intimidated by the fact that the legal analysis takes place in some specie of high-tech environment. On the other hand, and the decision of the Third Circuit in *LePages* notwithstanding, nearly all situations involving ordinary commercial bundling of products or services at prices above average variable cost are probably unburdened by material risk.

4. Conduct by a holder of intellectual property rights (IPR) in a standard-setting context. The main legal issue in this area is whether, or to what extent, a company’s conduct before a standard-setting organization (“SSO”) may thereafter limit its ability to enforce patents covering that standard. The patent and competition law principles continue to be far from settled; the area has seen an enormous amount of activity; and writings on the topic are plentiful.⁵⁶ The activity in this area has been coming from three directions: FTC enforcement activity resulting in litigation or consent decree; Justice Department Business Review Letters; and private litigation.

a. FTC Activity. The lead FTC enforcement action, of course, is *Rambus*,⁵⁷ about which I wrote a great deal for this group two years ago, concluding that the FTC decision was deeply flawed.⁵⁸ In a decision of more than a hundred pages, the Commission found Rambus to have engaged in a Section 2 Sherman Act violation by deceiving the SSO (the Joint Electron Device Engineering Council, universally referred to as JEDEC) into adopting Rambus’ proprietary technology as part of a standard. The gravamen of the FTC’s case was that “Rambus’ alleged deception [of the SSO] enabled it *either* to acquire a monopoly through the standardization of its patented technologies rather than possible alternatives, *or* to avoid limits on its licensing fees that the SSO would have imposed as part of its normal process of standardizing patented technologies.”⁵⁹ The court held that this latter activity - deceit enabling a monopolist to charge higher prices than it otherwise could have charged - would not in itself constitute monopolization. And since the

52 *Id.* at 1193.

53 *International Mfg. Co. v. Landon, Inc.*, 336 F.2d 723 (9th Cir. 1964).

54 *Monsanto Co. v. Scruggs*, 459 F.3d 1328 (Fed. Cir. 2006).

55 *Id.* at 1341.

56 Cowie, Antitrust and Standard Setting: Recent Developments, Presentation to licensing Executives Society (May 7, 2008); Anne Layne Farrar, Antitrust and Intellectual Property Rights: Assessing the Link between Standards and Market Power, *Antitrust Magazine* 42 (Summer 2007); Michael G. Cowie and Joseph P. Lavelle, Patents covering industry standards: the risks to enforceability due to conduct before standard-setting organizations, *AIPLA Quarterly J.* 95 (Winter 2002); Taylor, *Standard Setting: A Growing Morass*, (May, 2002) (unpublished).

57 *Rambus, Inc. v. Federal Trade Comm’n*, 522 F.3d 456 (D.C. Cir. 2008).

58 John Briggs, *The Unsettled and Unsettling Nature of U.S. Competition Law Governing Single Firm Conduct*, Sedona Conference at 19-23 (Oct. 26-27, 2006).

59 *Rambus Inc.* 522 F.3d at 458 (emphasis in original).

Commission only found “A” or “B” without determining which was the violation, since either could be, the Court found that the Commission’s conclusion that Rambus’ conduct was exclusionary depended on the syllogism that Rambus avoided one of two outcomes by not disclosing its patent interests; the avoidance of either of those outcomes is anticompetitive; therefore Rambus’ nondisclosure was anticompetitive.⁶⁰ But “the Commission expressly left open the likelihood that JEDEC would have standardized Rambus’ technologies *even if Rambus had disclosed its intellectual property*.”⁶¹ Under this hypothesis, JEDEC lost only an opportunity to secure a RAND commitment from Rambus. But the loss of such a RAND commitment is not itself a harm to competition from alternative technologies in the relevant markets. For this proposition, the panel relied heavily on the Supreme Court’s decision in *NYNEX Corp. v. Discon, Inc.*⁶²

Discon had alleged that New York Telephone, through a corporate affiliate, had switched its purchases of removal services from Discon to a higher-priced independent firm. The New York Telephone affiliate would pass the higher fees on to New York Telephone, which in turn passed them on to customers through higher rates approved by regulators. According to Discon, the nub of the deception was that AT&T technologies would provide the New York Telephone affiliate with a special rebate at year’s end, which it would then share with NYNEX. By thus hoodwinking the regulators, the scam raised prices for consumers. Discon, because it refused to play the game, was driven out of business. It alleged that the arrangement was anticompetitive and constituted both an agreement in restraint of trade in violation of Section 1 of the Sherman Act and a conspiracy to monopolize the market for removal services in violation of Section 2 of the Sherman Act.

As to Discon’s Section 1 claim, the Court held that where a single buyer favors one supplier over another for an improper reason, the plaintiff must “allege and prove harm, not just to a single competitor, but to the competitive process.”⁶³ And while conceding injury to consumers, the Supreme Court found that the consumer injury naturally flowed not so much from a less competitive market for removal services as from the exercise of market power *lawfully* in the hands of a monopolist, New York Telephone. It was that, combined with the deception worked upon the regulatory agency, that prevented the agency from controlling New York Telephone’s exercise of its monopoly power.⁶⁴

Because Discon based its Section 2 claim on the very same allegations of fraud, the Supreme Court vacated the appellate court’s decision to uphold that claim because “[u]nless those agreements harmed the competitive process, they did not amount to a conspiracy to monopolize.”⁶⁵ The D.C. Circuit panel sharply criticized the Commission for failing to grapple with, or even mention, the *Discon* case. This broad reading of *Discon* by the Court of Appeals seems especially to have rankled the Commission.

The panel’s decision is not necessarily the last word, since the Commission last June filed a petition for rehearing *en banc*, arguing that the panel decision is: (1) inconsistent with the causation standard for monopolization articulated by the D.C. Circuits’ *en banc* decision in *United States v. Microsoft Corp.*,⁶⁶ requiring “but for” proof in an equitable enforcement action would impose on the Government a nearly insurmountable burden of reconstructing the hypothetical “but for” marketplace - a burden that “would only encourage monopolists to take more and earlier anticompetitive action,” and (2) improperly extends the Supreme Court’s holding in *Discon* to protect a firm’s use of deception to achieve monopoly power. The Commission in this area argues that:

The panel’s dismissal of the harm to JEDEC members as a mere “loss of an opportunity to seek favorable licensing terms”- and its consequent reliance on the analysis in ... *Discon* - reflects its failure to appreciate the fundamental differences between actions taken by a monopolist to exercise monopoly power already obtained, and actions that are central to its obtaining of such power.⁶⁷

60 *Id.* at 463.

61 *Id.* at 466 (emphasis in original).

62 525 U.S. 128 (1998).

63 *Id.* at 135.

64 *Id.* at 136.

65 *Id.* at 139.

66 253 F.3d 34 (D.C. Cir. 2001).

67 FTC Pet. for Rehearing *en banc* at 10, <http://www.ftc.gov/os/caselist/0110017/080606rambusrehearingpetition.pdf>.

Rambus continues to be an important case not just for the parties, but also for the development of the law more broadly, including more broadly even than the IP/antitrust interface.

Less visible and less dramatic, but nonetheless important, is the Commission's January 2008 Consent Order involving Negotiated Dated Solutions, LLC ("N-Data").⁶⁸ The pertinent SSO was the Institute of Electrical and Electronics Engineers ("IEEE"). The case had its roots in the working group that determined that it would be desirable for Fast Ethernet equipment to be compatible with existing LAN equipment and with future generations of equipment. In 1994 the patent holder advocated that NWay technology be adapted into the new IEEE Ethernet standard. In 1994, the patent holder provided public assurances that if NWay technology were chosen, it would license NWay to any requesting party to for a one-time fee of \$1000. The patent holder later assigned a number of the patents, who in turn assigned some of them to N-Data. N-Data was aware of the 1994 assurances, but rejected requests from companies to license NWay technology for a one-time fee of \$1000 and instead threatened to initiate legal actions against companies refusing to pay its more excessive royalty demands.

In a 3-2 decision, the FTC accepted a consent decree from N-Data. In its "Statement," the majority wrote that "... we find reason to believe that [N-Data's] conduct violated Section 5 of the FTC act ... [as] an unfair method of competition.... [and that] N-Data's conduct is also an unfair act or practice." The majority relied on the 1972 Supreme Court decision in *FTC v. Sperry & Hutchinson Co.*⁶⁹ The fundamental issue here was whether Section 5 of the FTC Act reaches beyond those acts or that conduct prohibited by Sections 1 and 2 of the Sherman Act. In its accompanying "Analysis of Proposed Consent Order to Aid Public Comment," at 5, n.8, the Commission goes out of its way to note that: "... because the proposed complaint alleges stand-alone violations of Section 5 rather than violations of Section 5 that are premised on violations of the Sherman Act, this action is not likely to lead to well-founded treble damage antitrust claims in Federal Court." The majority recognized Commissioner Kovacic's dissenting concern that FTC "unfair methods" cases may support private actions based on state law and the majority seemed to share this concern, or at least "join[ed] him in encouraging comment on that issue."

The dissenting opinions of Chairman Majoras and Commissioner Kovacic questioned whether there should be liability at all, and Commissioner Kovacic was especially concerned that N-Data, a small company without substantial resources, could become exposed to private treble damage actions under state law or otherwise. He was critical of the majority's assumption that there would be no spillover effects and expressed concern that many state consumer protection statutes embrace rulings of the Federal Trade Commission as part of their substantive law and that many states have authorized private parties to enforce their UMC and UAP statutes in suits that permit the court to impose treble damages for infringements.

A salient point is that the private treble damage action has fallen into considerable disrepute when all five FTC commissioners express concern or fear about whether their decision would trigger such actions, even as they rely upon a case from the early 1970s that expanded the boundary of the Commission's authority to its very outer limit (*Sc&H*).

b. DOJ Activity.⁷⁰ The only notable recent DOJ activity has been the issuance of two Business Review Letters to two separate SSO's – one last year to the IEEE, another in 2006 to the VMEBus International Trade Association (VITA).

⁶⁸ All of the pertinent papers, filed January 23, 2008, may be found at <http://www.ftc.gov/os/caselist/0510094/index.shtm>.

⁶⁹ 405 U.S. 233, 242 (1972).

⁷⁰ Both the DOJ and the FTC have their fingerprints on a few policy statements from the DOJ/FTC 2007 Joint Antitrust/IP Guidelines in respect of standard setting. What they say is by and large unremarkable:

1. An IP holder's voluntary and unilateral disclosure in its licensing term, including its royalty rate, is not a collective act subject to review under Section 1 of the Sherman Act.
2. Bilateral *ex ante* negotiations about licensing terms that take place between an individual SSO member and an individual IP holder...outside the auspices of the SS also are unlikely to require special antitrust scrutiny....
3. *Per se* condemnation is not warranted for joint SSO activities that mitigate "hold up" and that take place before deciding which technology to include in a standard.

VITA sought review of its patent policy under which each member of the working group had to: (i) identify all relevant patents or patent applications; (ii) declare the maximum royalty rates and most restrictive non-royalty they will request for any such patent claims; (iii) patent holders may submit subsequent declarations with less restrictive licensing terms (including lower royalties); and (iv) working group members could consider the various declared licensing terms when deciding which technology to support during the standard-setting process. The Department advised that, unless the standard-setting process was used as a sham to cloak naked price-fixing or bid-rigging, it would analyze the action taken during the standard-setting process under the rule of reason. No enforcement challenge was merited.

IEEE sought review of a proposed patent policy under which a patent holder had five options: (i) provide no assurance; (ii) state that it does not hold essential patents; (iii) commit not to assert its patents against implementers of the standard; (iv) commit to a license on RAND terms, or (v) commit to maximum price terms. The Department concluded that the IEEE's policy offered potential benefits comparable to those offered by the VITA policy and hence did not merit an enforcement challenge.

c. Private Litigation. There are two broad classes of litigation and recent cases illustrate each. First, there are cases that hinge on IP disclosure issues, and second, there are cases that deal more with what a RAND promise means as a practical or legal matter.

Rambus is responsible for much of the private litigation in the first category. Some eight years ago, Rambus sued Infineon for allegedly infringing four of its patents in implementing the JEDEC SDRAM standards. Infineon counterclaimed asserting fraud claims under state law. Initially, the District Court found that Infineon had not infringed Rambus's patents and the jury found that Rambus had committed fraud by failing to properly disclose patent information to the SSO.⁷¹ On appeal, the Federal Circuit vacated the noninfringement judgment and was skeptical of the anticompetitive implications of nondisclosure. In particular, the majority found that JEDEC's disclosure rules were too vague to create any enforceable commitment for Rambus.

Then there was *Broadcom Corp. v. QUALCOMM Inc.*⁷² The simple holding was that a patent holder's intentionally false promise to a standard-setting organization that it would license its technology on RAND terms, coupled with the SSO's reliance on that promise when including the technology in a standard, amounted to anticompetitive conduct since it increased "the likelihood that patent rights will confer monopoly power on the patent holder."⁷³ The case may not be as reliable on this point as could be otherwise thought for two reasons: first, it relied heavily on the now reversed Federal Trade Commission decision in *Rambus* that was criticized by the D.C. Circuit as being in conflict with *Discon*.⁷⁴ Second, the decision simply reversed an order granting a motion to dismiss so there was no factual record to speak of beyond the complaint.

There is also *Nokia v. QUALCOMM, Inc.*⁷⁵ Here, as in the *Broadcom* case, the plaintiff asserts that QUALCOMM made a RAND promise to the SSO but failed to keep it. At the core of both cases is the presumption that being included in a standard confers market power on patent holders. According to the complaints, they share a common concern over the aggregate royalty rate for the 3G standard for mobile telecommunications. Both Broadcom and Nokia allege that RAND entails not just a reasonable royalty rate from each licensor viewed in isolation, but a reasonable cumulative rate when all firms' rates are stacked up, as would be required for any downstream firm to implement the standard in as much as the elements of a standard are complementary and implementers must therefore license all of them. In the circumstances, the assertion by Broadcom and Nokia was that a given firm's rates can be deemed reasonable only in light of their relative place in the

⁷¹ Anne Lynn Farrar, *Antitrust and Intellectual Property Rights: Assessing the Link Between Standards and Market Power*, *Antitrust Magazine* 32 (Summer 2007). [Hereafter "Farrar"].

⁷² 501 F.3d 297 (3d Cir. 2007).

⁷³ *Id.* at 314.

⁷⁴ *Rambus v. Federal Trade Comm'n*, *supra* at 463.

⁷⁵ Civil Action No. 06-509 JJE, 2006 US Dist. LEXIS 61383 (D. Del. August 29, 2006). The District Court's two page opinion is limited to remanding the case to the Delaware Court of Chancery, finding removal to have been improvident. Interestingly, the case was brought in state court as a breach of contract case in a standard-setting context. The court found that resolution of the claim depended on interpretation of the terms of the licensing agreement, rather than an interpretation of the patents. Accordingly, the court concluded that there was no substantial question of patent law warranting federal jurisdiction. I find this to be one of the most interesting aspects of all of this.

cumulative total. Thus a key element in the complaints by Nokia and Broadcom against QUALCOMM is that its rates are “excessive” in relation to its contributions to the standard. In defense, QUALCOMM has argued that its IP contributions to the 3G standard are highly valuable and its rates are hence justified. Indeed, QUALCOMM maintains that, rather than there being any *ex post* “holdup” by it, it is the mobile handset manufacturers downstream who are exerting market power in an effort to lower their licensing costs below reasonable levels.⁷⁶

Multiple complainants, including both Broadcom and Nokia, have lodged charges against QUALCOMM before the European commission.⁷⁷ Based only on the public documents available, it appears that the Commission’s investigation springs not from some broken promise, but rather from conduct on the part of QUALCOMM alleged to be in the nature of a breach of contract, namely, an alleged failure to charge licensees fair, reasonable, and nondiscriminatory (FRAND) royalties, as QUALCOMM had allegedly contracted to do with the SSO. In this respect, it seems to be congruent with the private action brought against QUALCOMM by Nokia.

In this connection, it is now noticeable that the European Commission has taken an interest in the level of royalties that are charged by IP holders. The *Microsoft CFI* decision requiring FRAND licensing by Microsoft was one step, and its investigation of QUALCOMM is clearly another.⁷⁸ The EC has also sent a Statement of Objections to Rambus on the ground that it infringed Article 82 of the EC Treaty by claiming unreasonable royalties for the licensing of certain patents for DRAMS subsequent to a so-called “bait and switch.”⁷⁹

4. Issues arising out of licensing in general, including cross licensing, patent pooling and grantbacks.⁸⁰

There is one patent case of great interest that, on its face, does not appear to have anything to do with antitrust law but that below the surface seems to have the potential to implicate antitrust to an increasingly great degree in patent licensing issues. The case is *Quanta Computer, Inc., et al. v. LG Electronics, Inc.*⁸¹ The case was about the patent exhaustion doctrine, sometimes also referred to as the “first sale” doctrine. The doctrine limits the patent rights that survive the initial authorized sale of a patented item. The Federal Circuit had held that the doctrine did not apply to method patents at all and, in the alternative, that it did not apply against LG because the sales at issue were not authorized by the conditional license agreement between LG and its licensees. The Supreme Court disagreed with the Federal Circuit on both scores holding that because the exhaustion doctrine applies to method patents, and because the license authorized the sale of complements that substantially embody the patents in suit, the sale exhausted the patents.

There are several reasons why this is a very important case. First, conditional licenses have become ubiquitous throughout the United States. They are used in drug applications, transgenic crops, and elsewhere as a way of making IP rights available to some without the patentee completely losing control of the patented technology. The Supreme Court’s decision clearly throws the status of a number of such licenses into doubt.

Second, the rule applied by the Supreme Court was derived from one of the Court’s decisions from a much earlier era, *United States v. Univis Lens Co.*,⁸² which many people thought had been significantly mitigated over the years by the lower courts as a practical matter. For the US antitrust community, it is perhaps fair to compare the *Quanta* decision to the old *Schwinn* case,⁸³

⁷⁶ This discussion of *Nokia* and *Broadcom* is drawn from the excellent summary in Farrar, *supra*, at 44.

⁷⁷ Cases COMP/C-3/39,247-252 (Feb. 13, 2006).

⁷⁸ This entire subject is covered in considerable detail in a worthwhile paper by my partner Damien Geradin, Pricing abuses by essential patent holders in a standard-setting context: A view from Europe, Paper presented to a University of Virginia conference on “The Remedies before Dominant Firm Misconduct” (June 4-5, 2008)(unpublished; available on request).

⁷⁹ See Memo/07/330, “Commission confirms sending a Statement of Objections to Rambus,” Brussels, 23 August 2007.

⁸⁰ For the interested and the curious, these are covered in a useful although abstract way in Chapters 3 and 4 the DOJ/FTC Report, Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition (2007), found at <http://www.usdoj.gov/atrp/public/hearings/ip/222655.htm>. For a thoughtful, although perhaps excessively polite, critique of this Report, see Willard K. Tom, the DOJ/FTC Report on Antitrust Enforcement and Intellectual Property Rights, *Antitrust Magazine* 35 (Summer 2007)

⁸¹ ___ S. Ct. ___ (June 9, 2008). Citations to the case are to the slip opinion, available at <http://www.supremecourt.gov/opinions/07pdf/06-937.pdf>.

⁸² 316 U.S. 241 (1942).

⁸³ *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967).

which simply looked at whether title had passed to decide whether the original seller was restraining trade by controlling (through a bilateral agreement with the buyer) any downstream aspect of the selling of the product.

Third, and this is related to both of the first two points, in its final footnote in the case, note 7, the Court said that:

... the authorized nature of the sale to Quanta does not necessarily limit LGE's other contract rights. LGE's complaint does not include a breach-of-contract claim, and we express no opinion on whether contract damages might be available even though exhaustion operates to eliminate patent damages. See *Keeler v. Standard Folding Bed Co.*, 157 US 659, 666 (1895) ("Whether a patentee may protect himself and his assignees by special contracts brought home to the purchasers is not a question before us, and upon which we express no opinion. It is, however, obvious that such a question would arise as a question of contract, and not as one under the inherent meaning and effect of the patent laws").

This is probably more important that it looks at first glance.

The brief of the Solicitor General supported the Petitioners and advanced the position ultimately taken by the Supreme Court. The defendants in *Quanta* had asked the Court to hold that their purchase of patented microprocessors from Intel, a licensee of the plaintiff patent owner LGE, carried with it an absolute right to incorporate these microprocessors into computer systems also covered by LGE's patents, notwithstanding an express limitation to the contrary in the patent licensed to Intel and the defendants' knowledge of that limitation. The Solicitor General, while recognizing the contractual freedom of a patent owner to impose reasonable conditions on its licensees, embraced making the formal transfer of title to a licensed product an operative event to cut off any subsequent assertion of patent rights against that product or a larger product into which it might be incorporated. The Solicitor General suggested that antitrust concerns motivated its position.⁸⁴

And so here we are, with a *Schwinn*-like patent decision from the Supreme Court that limits patent rights, but leaves the door open for patentees to achieve similar goals by contract, but in a setting where there is or may be a higher than normal degree of confusion surrounding the antitrust rules by which the contracts (licenses) will be judged.

The discussion that follows is by and large as applicable to contractual issues as to patent issues, a point made more salient by the *Quanta* decision.

As a very basic first step, it is important to know whether the relationship between a licensor and a licensee is horizontal or vertical. If, but for the license relationship, the companies would be competitors, the relationship is horizontal. A licensing arrangement has a vertical component when it affects activities that are in a complementary relationship. Companies that might be in competition generally might still be in a vertical relationship as to particular IP. Where a manufacturer licenses IP to a direct manufacturing competitor, whether the relationship is horizontal or vertical will depend on what alternatives are available. If the licensee has viable alternatives to the licensed IP, then the relationship is almost certainly horizontal. If not, it is probably vertical.

As a basic second step, it is useful to think about things as being either "inside the patent" or "outside the patent." An owner of intellectual property need not create competition in its own technology "inside the patent." Antitrust issues begin to arise when a licensing arrangement diminishes rivalry among entities that would have been actual or likely potential competitors in a relevant market in the absence of the license. And as we shall see in a few pages, unilateral conduct

⁸⁴ The general view of the patent bar was that *Quanta* provided an opportunity for the Supreme Court to modernize and update patent law. A thoughtful article published late last year, before oral argument in the case, said that: "it is time for the Court to abandon the formulaic and dogmatic approach that has characterized the case law on patent exhaustion for over a century. The court should ground the analysis instead on fundamental, uncontroversial, and widely accepted principles of patent licensing, foremost among which is the freedom of knowledgeable entities to enter into a binding license that serves the needs of their particular technology and industry." Robert P. Taylor and Henry C. Su, Patent Exhaustion: A Simple Problem Made Hard, *The Antitrust Source* (December 2007) (www.antitrustsource.com).

taken by the patentee “inside the patent” is very likely to be found lawful in virtually all circumstances provided that the patent is valid. However, conduct having a competitive impact “outside the patent” does not enjoy the same level of near certain lawfulness, although the mode of analysis should not be thought of as unduly intimidating.

A third basic thing to note is that the rule of reason in patent settings is not much different from the rule of reason elsewhere. The main lines of questions have to do with: whether the restraint increases the risk of coordinated pricing or reduced output; whether it results in the acquisition or maintenance of market power; and whether the arrangement poses a significant risk of retarding or restricting the development of new or improved goods or processes. As in any kind of market, the potential for competitive harm depends in part on the degree of market concentration, the ease or difficulty of entry, and the responsiveness of supply and demand to price changes in the market. In purely vertical settings, competitive harm may occur if the licensing arrangement forecloses access to, or increases competitors’ costs of obtaining, important inputs, or if it facilitates coordination to raise price or restrict output. For example, licensees who are competitors may find it easier to coordinate their pricing if they are subject to common restraints and licenses for the common licensor or competing licensors.

Finally, efficiencies may play a role in patent licensing settings even where there is some noticeable anticompetitive impact. This is especially true as to portfolio cross licenses and industries, such as the semiconductor or computer industries, that are characterized by large numbers of overlapping patent rights. These kinds of cross licenses allow firms operating within a patent “thicket” to use each other’s patented technology without the risk of litigation, including the risk of an injunction that could shut down production.

There is at least one area where patent law provides for virtually *per se* legality as a matter of antitrust and patent misuse law: territorial restrictions. Under the patent statute, a patentee has the right to license its patent for use in “the whole or any specified part of the United States.”⁸⁵ However, where territorial restrictions are applied based both on patent rights and on trade secret rights, that territorial restriction may be scrutinized once the patent has expired. This was the situation in *United States v. Pilkington plc*⁸⁶, where Pilkington continued to enforce the inclusive territories based on the trade secret license upon the expiry of the patent. The DOJ argued that the trade secrets had no substantial value and were simply a device for maintaining a market division arrangement. A consent Decree ensued.⁸⁷

Field of use restrictions are common and are generally lawful (*e.g.*, a license to use a novel OLED only for cell phone screens). Where a field of use restriction is within the patent grant (“inside the patent”), that should end the inquiry. Field of use restrictions “outside the patent” require a determination of competitive effect using the normal analytical approaches.

Nonexclusive cross licenses are governed by the rule of reason. When the licensing of rights allows firms to combine complementary factors of production, such licensing is normally procompetitive;⁸⁸ this is also true to the extent they operate as mechanisms for using technologies that require access to a large number of patents. The Guidelines provide a safe harbor if the parties to a cross license “collectively account for no more than 20% of each relevant market significantly affected by the restraint,” and the restraint is not “facially anticompetitive.”⁸⁹ Where a cross licensing arrangement affects a technology market for which market share data may be unavailable or may not actually represent the parties’ competitive significance, the agencies consider whether “there are four or more independently controlled technologies in addition to the technologies controlled by the parties to the licensing agreement that may be substitutable for the licensed technology at a comparable cost to the user.”⁹⁰ In other words, five rivals is enough for the agencies.

85 35 U.S.C. Section 261.

86 No. 94-345, 1994-2 Trade Cas. (CCH) Paragraph 70,842 (D. Ariz. 1994).

87 Available at <http://www.usdoj.gov/atr/cases/t220800/220860.pdf>.

88 See 2007 FTC/DOJ Report at 62-62.

89 Guidelines Section 4.3.

90 *Id.*

Patent pools are generally governed by the law of tying, although other Section 1 Sherman Act issues may well exist from time to time. Relatively few antitrust cases have been sustained in recent years in connection with patent pools,⁹¹ and the one case that did result in a finding of patent misuse (by the International Trade Commission) was swiftly reversed by the Federal Circuit.⁹² Patent pools are formed when multiple patented technologies are needed to produce a standardized product and they are generally recognized as mitigating the “holdup” and “holdout” problems that can sometimes stymie industry efforts to make a product that conforms to an industry standard. In general, competitive concerns tend to arise when the pools are composed of pure substitute patents covering technologies that compete with each other, rather than complementary patents covering separate aspects of a given technology that do not compete with each other.⁹³

Patent pools are much more likely to be a governmental issue than a private litigation issue. Governmental concern focuses on horizontal coordination among pool licensors as well as on the more subtle problem of discouraging R&D, new product development, and innovation in general that results from the ability of members of a pool to share their successful R&D and to free ride on the accomplishments of each other. Notably, the agencies have supplemented the pooling analysis found in the Guidelines in several business review letters issued by the Department of Justice⁹⁴ and in the FTC’s 1999 enforcement action against a patent pool formed by Summit Technology and VISX.⁹⁵ By and large, though, pools tend to be thought of as procompetitive by virtue of integrating complementary technologies, reducing transaction costs, clearing blocking positions and promoting the dissemination of technology. They are unlikely to have anticompetitive effects unless (1) excluded firms cannot effectively compete in the relevant market for the good incorporating the licensed technologies and (2) the pool participants collectively possess market power.

5. A word about grantbacks. A grantback is generally an agreement by which a licensee extends back to the licensor the right to use the licensee’s improvements to the licensed technology. In some cases, the scope could be even broader and cover inventions that relate in any way to the subject of the licensed patent(s). Grantbacks may be exclusive or nonexclusive. The competitive issue is whether or not the grantback reduces significantly the incentives of the licensee to invest in improving the licensed technology. As a rule, the issues surrounding grantbacks tend to be of governmental and policy concern, rather than of pertinence in private litigation.

Finally, there are some miscellaneous but important points. It is not an antitrust violation to extend royalties beyond the term of the patent, but it could be found to be patent misuse by some courts, thus making the patent unenforceable until the misuse is purged. Relatedly, providing for a royalty based on the total sales of infringing and non-infringing goods can amount to patent misuse unless the arrangement was for the convenience of the licensee. Discriminatory royalties are generally neither a misuse nor any form of antitrust violation, although increasingly SSO’s are requiring RAND royalty commitments and so discriminatory royalties subject to such commitments can raise either contract liabilities, or potentially, antitrust liabilities in some circumstances.

6. EU Law and Policy in Respect of the Topics Mentioned Above. When I began this paper, I intended to spend more time on European law and policy. However, two forces in particular have conspired to prevent this. First, there are few policy pronouncements on these topics emanating from the European Commission beyond the 2004 Technology Transfer Block Exemption (TTBE) and

91 *But see United States v. Krasnov*, 143 F.Supp. 184 (ED Pa. 1956), *aff’d per curiam*, 355 U.S. 5 (1957)(Violation of Sections 1 and 2 of the Sherman Act found where companies who together had monopoly power formed a patent pool and agreed: to refrain from licensing others; to allocate customers, to maintain prices established by the licensor and to determine jointly institution and maintenance of infringement suits); *United States v. National Lead Co.*, 63 F.Supp. 513 (SDNY 1945), *aff’d*, 332 U.S. 319 1947(court found illegal an agreement between two largest titanium dioxide companies involved in exchange of nonexclusive licenses under all of their patents, present and future, with knowledge and intent that such arrangement would strengthen each to the exclusion of others).

92 *See Part 3 supra.*

93 2007 FTC/DOJ report at 66.

94 *See* 2007 Report at Chapter, n. 58 and pp. 68-71.

95 *Id.* at 73-74. This was a somewhat straightforward enforcement action. Summit and VISX both owned patents relating to the manufacture and use of lasers employed in performing certain eye surgeries. At the time they put their patents in pool, they were the only firms whose later equipment had received marketing approval from the US FDA. The FTC alleged that the pool eliminated all competition between Summit and VISX in the sale and leasing of the pertinent equipment and in the licensing of technology related to the procedure. In effect, the pool operated as a price-fixing agreement.

an accompanying set of *Technology Guidelines*,⁹⁶ and second, finding out about the status of pending matters is considerably harder than one might think. For example, it is well-known that the EC is pursuing in depth investigations of some interest against Intel and QUALCOMM, in each case at the behest of various rivals, but it is not possible to learn much authoritative about these investigations other than by perusing documents filed by the targets of the investigation with the US Securities and Exchange Commission. None of the filings made by the parties (or by third parties) is accessible or public other than to “interested parties” (e.g., complainants), and even then they are heavily redacted and mostly confidential. From the EC, all we see is a single press release normally.

It is helpful to begin with a brief discussion of the sources of competition law and policy at the intersection of intellectual property and competition law within the European Union.⁹⁷ Insofar as European law is concerned, and putting wholly to one side for most purposes of this paper the national law of the 25 Member States, Articles 81 and 82 of the EC Treaty provide the initial source of competition law. These articles of the EC Treaty are enforced on a European wide basis mainly by the European Commission,⁹⁸ but national competition authorities (“NCA’s”) of the Member States now have been authorized since January 1, 2004 (under the Modernisation Program) also to enforce these provisions. Also, to the extent permitted by the courts and procedures of the Member States, private parties can also bring private actions asserting rights under Articles 81 and 82, including sometimes collective actions, in the courts of the Member States. Few such actions have been brought outside of France, Germany and the United Kingdom, but that may change as time goes on and, of course, the Commission is encouraging this in various ways, as other papers will discuss in some detail.

Nearly all of the cases in Europe involving principles of both intellectual property and competition law require a working knowledge of Articles 81 and 82 of the EC Treaty. It is therefore useful to begin with basic information about each.

Article 81

Article 81(1) states that “all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market” shall be prohibited as incompatible with the common market. This article forbids agreements that “directly or indirectly fix purchase or selling prices or any other trading conditions,” that “limit or control production, markets, technical development, or investment” and that “share markets or sources of supply,” among other things.⁹⁹ Article 81(1) is broader than Section 1 of the Sherman Act, but nonetheless has much in common with it.

By and large, Art. 81 does not often come into play in connection with intellectual property/competition law issues, and therefore I will dwell on it no further.

96 I do not mean, though, to understate the importance of the Technology Transfer Block Exemption Regulation and the associated *Guidelines*. The *Guidelines* lay out a “general framework for analysis,” and then apply this analytical framework to a list of specific restrictions commonly found in IP licenses. The Regulation and the associated *Guidelines* are available at <http://ec.europa.eu/comm/competition/antitrust/legislation/transfer.html>.

European Commission treatment of competition and intellectual property, as in the US, involved three phases. Prior to 1966, before the *Grundig* case, [1966] ECR 299, the Commission accepted that exclusive patent licensing agreements, unlike exclusive distribution agreements, could be viewed as not restrictive of competition as long as the contents of the license remained within the scope of the patent. Practices that leveraged the patentee’s rights so as to restrict matters “outside the patent,” were viewed as a misuse of the patent and generally were found illegal. In *Grundig*, the ECJ (this was prior to the formation of the CFI) broadened Article 81 (1) by defining it to apply to market partitioning agreements. Thus it stated that the infringement of Article 81 consisted of the attempt by the licensor and licensee to isolate the French market for Grundig products and maintain artificially separate national markets within the community. There followed more than two decades of development of case law. A most excellent publication detailing all these developments is Stephen D. Anderman and John Kallaugher, *Technology Transfer and the New EU Competition Rules: Intellectual Property Licensing after Modernisation* (Oxford University Press 2006). So far as I can tell, this is the only book written on the subject and it is a most indispensable research tool for anyone wishing to delve into the topic.

The third phase really began in recent years, culminating in the adoption in 2004 of the TTBE and its associated *Guidelines*, development of which began in 1996. The Regulation and the *Guidelines* are available at <http://ec.europa.eu/comm/competition/antitrust/legislation/transfer.html>.

97 See ABA Section of Antitrust Law, *Antitrust Law Developments* 164 *et seq.* (6th ed. 2007), for a useful, but incomplete, discussion of this very topic.

98 EC Treaty, Art. 84. EC decisions are subject to judicial review by EU Courts: The Court of First Instance (CFI), and thereafter, the European Court of Justice (ECJ). EC Treaty, Art. 220.

99 Art. 81(1)(a)-(e).

Article 82

Article 82 states that “[a]ny abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between Member States.” By its terms, Article 82 specifies certain prohibited practices including: “directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions; limiting production, markets or technical development to the prejudice of consumers; applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;” and “making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial use should, have no connection with the subject of such contracts.”¹⁰⁰

Critical to many IP-antitrust issues is the meaning of the term “dominant position,” not defined in the Treaty. The ECJ has held that a “dominant position” is

a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave in an appreciable extent independently of its competitors, its customers and ultimately of the consumers.¹⁰¹

This is very close to the definition of a “monopolist” in the United States, although it has been interpreted quite differently when put in the context of market share. A brief digression on some key differences between Article 82 and Section 2 of the Sherman Act as they have been applied in practice is in order.

The best short source document on this topic is a brilliant address given by FTC Chairman William E. Kovacic a few weeks ago entitled *Competition Policy in the European Union and the United States: Convergence or Divergence?*¹⁰² As he there points out, the interpretations of Article 82 by the CFI and the ECJ have tended to create a wider zone of liability for dominant firms than the decisions of the US courts under Section 2 of the Sherman Act.

In their technical findings and in their attitude, modern US Supreme Court decisions in cases such as *Brooke Group*, *Trinko*, and *Weyerhaeuser* have demonstrated greater skepticism about abuse of dominance claims than judicial decisions in matters such as *France Telecom/Wanadoo*, *Michelin II*, and *British Airways*. EU decisions in *IMS Health* and *Microsoft* show a greater inclination to condemn refusals to deal than modern US rulings such as *Trinko*. Unlike *Brooke Group* and *Weyerhaeuser*, *France Telecom/Wanadoo* decision rejects the need to apply a recoupment test to resolve allegations of exclusionary pricing. A finding of dominance can occur in the EU at or somewhat below a 40 percent market share, while the US offense of attempted monopolization usually treats shares below 50 percent as being inadequate to establish substantial market power.¹⁰³

There is a degree of unclarity about how to resolve the tension between the EC rules of competition contained and Articles 81 and 82 and the intellectual property rights conferred by the national systems of law. Article 295 of the EC Treaty provides that “[t]his Treaty shall in no way prejudice the rules in Member States governing the system of property ownership.” According to the ABA Section of Antitrust Law, “[i]n cases where the exercise of intellectual property rights conflicts with EU antitrust law, the Commission has the authority to limit the exercise of those intellectual property rights in order to harmonize them with EU law.”¹⁰⁴

¹⁰⁰ Art. 82 (a)-(d).

¹⁰¹ Case 85/76, *Hoffmann-La Roche & Co. v. Comm'n*, [1979] ECR 461, Paragraph 38.

¹⁰² Bates White Fifth Annual Antitrust Conference, Washington, DC at 11-12 (June 2, 2008).
<http://www.ftc.gov/speeches/kovacic/080602bateswhite.pdf>.

¹⁰³ *Id.* (Internal footnotes omitted).

¹⁰⁴ Antitrust Law Developments 1165-66 (6th ed. 2007). For this proposition, the volume cites *Établissements Consten. S.à.R.L. & Grundig-Verkaufs-GmbH v. Comm'n*, Joined cases 56&58/64, [1966] ECR 299, 345-46.

The highly thoughtful opinion of the Vice Chancellor in *Intel Corporation and VIA Technologies Inc and VIA Technologies*¹⁰⁵ (*Intel/Via*) contrasts two Court of Justice decisions. The earliest was *Volvo v. Veng*,¹⁰⁶ in which the court stated this about the right of an owner of intellectual property:

It must also be emphasized that the right of the proprietor of a protected design to prevent third parties from manufacturing and selling or importing, without its consent, products incorporating the design constitutes the very subject-matter of his exclusive right. It follows that an obligation imposed upon the proprietor of a protected design to grant to third parties, even in return for a reasonable royalty, a license for the supply of products incorporating the design would lead to the proprietor thereof being deprived of the substance of his exclusive right, and that a refusal to grant such a license cannot in itself constitute an abuse of a dominant position.¹⁰⁷

A decade later, in *ITT Promedia NV v. European Commission*,¹⁰⁸ the Court of Justice seemed to state a notably different proposition:

It follows from the nature of the obligations imposed by Article [82] of the Treaty that, in specific circumstances, undertakings in a dominant position may be deprived of the right to adopt a course of conduct or take measures which are not in themselves abuses and which would even be unobjectionable if adopted or taken by non-dominant undertakings (see, to that effect, case 322/81 *Michelin v. Commission* [1983] ECR 3461, Paragraph 57). Thus, the conclusion of a contract or the acquisition of a right may amount to abuse for the purposes of Article [82] of the Treaty if the contract is concluded or that right is acquired by an undertaking in a dominant position (see, to that effect, Case T-51/89 *Tetra Pak v Commission* [1990] ECR 11-309, Paragraph 23).¹⁰⁹

In a nutshell, it appears that Article 295 of the EC Treaty does not mean quite what it seemed to say, and article 82 does indeed have the capacity to “trump” IPR acquired from Member States.¹¹⁰

Main EU Cases Applying Competition Law to Intellectual Property

I should mention at the outset here that the paramount question in Europe, at least as a matter of EC law, is whether, or under what circumstances, a holder of IPR might be required to license others. Most of the cases arise in the context of a refusal to deal, after which the unlicensed company complains to the authorities, who then take over the investigation of the matter and either bring a case or do not. The issue can also arise, or at least it once has, in the context of a patent enforcement action where the defendant claims that the patent should be declared unenforceable against it because the suit itself by the patentee amounts to an abuse of a dominant position. This sort of setting is quite analogous to the “patent misuse” defense common in the United States, but that is, so far as I can tell, highly uncommon in Europe.

In the beginning, which in this area of European law was about 20 years ago, there was just the case of *Volvo v Veng* mentioned above.¹¹¹ The question presented was whether Volvo’s refusal to license its protected design for car body panels constituted an abuse of dominance. The actual holding was that such a refusal, standing alone, could not be regarded as an abuse of a dominant position. But in what we would call *dicta*, the ECJ went on to say:

¹⁰⁵ 2002 E.W.C.A. Civ 1905 (December 20)(*Intel/Via*).

¹⁰⁶ [1988] ECR 6211.

¹⁰⁷ *Id.* at 6235, Paragraph 8.

¹⁰⁸ Case T-111/96 [1998] ECR II-2937.

¹⁰⁹ *ITT Promedia*, *supra* at 2987, Paragraph 139. See *Intel*, *supra* at Paragraph 36.

¹¹⁰ There is no meaningful Europe-wide patent system, a reality that provides a complex overlay to the applicability of competition law to patents issued by one or another member state. The UK *SanDisk* case mentioned at p. 38-39 *infra* provides a most useful discussion of how this issue comes into play, including in detaining whether a particular court even has jurisdiction to hear a claim of patent abuse.

¹¹¹ Case 238/87, *AB Volvo v. Erik Veng (UK) Ltd.*, [1988] ECR 6211.

It must however be noted that the exercise of an exclusive right by the proprietor of a registered design in respect of car body panels may be prohibited by Article [82] if it involves, on the part of an undertaking holding a dominant position, certain abusive conduct such as the arbitrary refusal to supply spare parts to independent repairers, the fixing of prices for spare parts at an unfair level or a decision no longer to produce spare parts for a particular model even though many cars of that model are still in circulation, provided that such conduct is liable to affect trade between Member States.¹¹²

Volvo was followed, in 1995, by *Magill*.¹¹³ *Magill* involved a company that was the only source of basic information on program scheduling, an indispensable raw material for those wishing to compile a weekly television guide in the UK. *Magill* sought to publish a comprehensive weekly television guide, but was refused a license to do so by the defendants, who reserved to themselves the secondary market for weekly television guides by denying access to the basic information needed by others. The Commission found that the defendants had violated Article 82 (actually its predecessor) and ordered them to supply “third parties on request and on a nondiscriminatory basis with their [copyrighted] individual advanced weekly programme listings” and to permit publication of these listings.¹¹⁴ The CFI affirmed the Commission and was in turn affirmed by the ECJ, which laid out a three part test to identify those “exceptional circumstances” where the exercise of an exclusive right might “involve abusive conduct”: (1) the refusal related to information that was “indispensable” to the appearance of a “new product... for which there was a potential consumer demand”; (2) there was no justification for the refusal; and (3) the refusal allowed the defendants to “reserve... for themselves the secondary market... by excluding all competition on that market.”¹¹⁵ *McGill* was really the first case cleanly holding a refusal to deal to amount to an abuse of a dominant position under Article 82, and providing an analytical framework. The touchstone was that the “circumstances” had to be “exceptional.” As we shall soon see, the next decade brought about a fair amount of “exceptional circumstance creep,” and all at the very time that on the western side of the Atlantic there was developing a broad and relatively deep consensus that unilateral refusals to deal were almost always lawful.

Enter *IMS Health*,¹¹⁶ which on a rather different set of facts re-articulated and embraced the three-part test of *McGill*, while also reiterating that a dominant firm’s refusal to grant a license cannot “by itself” constitute an abuse. The Court stated that:

[T]he refusal... to allow access to a product protected by [an intellectual property right], where that product is indispensable for operating on a secondary market, may be regarded as abusive only where the undertaking which requested the license does not intend to limit itself essentially to duplicating the goods or services already offered on the secondary market by the owner of the [intellectual property right], but intends to produce new goods or services not offered by the owner of the right and for which there is a potential consumer demand.¹¹⁷

In other words, if the would-be licensee is actually going to do something beyond what the dominant firm already does with the IPR, then the circumstances appear to be “exceptional.” And so the conduct, not quite “by itself” only by virtue of external circumstances, can indeed create liability.

Before getting to the CFI decision in *Microsoft*, I want to digress momentarily to the most excellent decision of the Vice-Chancellor in the *Intel/Via* case mentioned above. The case is interesting for at least three reasons. First, the case is interesting because it sets forth a highly informative and useful discussion of the origins of the principles being applied, both in respect of Article 81 and Article 82 principles.

¹¹² *Id.* Paragraph 9.

¹¹³ Joined Cases C- 241/91 P and C- 242/91 P are *RTE and ITV v. Commission (Magill)* [1995] ECR I-743.

¹¹⁴ *Id.*, Paragraph 9-10. See generally two recent and useful secondary sources of information about some of the cases discussed herein: Damien Geradin, Pricing abuses by essential parent holders in a standard-setting context: A view from Europe, Paper prepared for the “The Remedies for an Dominant Firm Misconduct” Conference, University of Virginia (June 4-5, 2008); Renata B. Hesse, Counseling Clients on Refusal to Supply Issues in the Wake of the EC *Microsoft* Case, antitrust Magazine 32 (Spring 2008) .

¹¹⁵ See Hesse, *supra* at 33; *Magill* at Paragraphs 50-56.

¹¹⁶ Case C- 418/01, *IMS Health GmbH & Co. v. NDC Health GmbH & Co. AG.* [2004] ECR I 5039.

¹¹⁷ *Id.* Paragraph 49.

Second, it is a case decided applying UK law (the Competition Act 1998), but heavily reliant on and informed by the law of Articles 81 and 82 of the EC Treaty. While the case was decided prior to the onset of “Modernisation” (January 1, 2004), it nonetheless provides a most interesting example of how Article 82 may well come into play in other national courts.

Third, the case is interesting because the competition issues arose as part of the defense to a patent enforcement action. Intel was seeking to enforce patents against Via both in respect of CPU’s and chipsets. In defense, Via asserted:

(a) as to the chipset patents: that the bringing of the infringement proceedings was itself an abuse by Intel of the exercise of intellectual property rights and that in consequence Intel should be estopped or otherwise precluded from seeking the relief sought in the infringement proceeding, and

(b) as to the CPU patents: (i) that the refusal of Intel to grant a license to Via either in whole or on lawful reasonable terms was an abuse of a dominant position and hence that, again, Intel, should not be entitled to the relief sought, and (ii) Intel’s refusal to license Via was abusive because it formed part of a plan to withdraw from the market certain products for which there was a continuing demand, and to force consumers and users to adopt a new and more expensive technology.

In a moderately lengthy opinion, the Vice Chancellor found that the case clearly established various of the propositions advanced by Via, including that a license term is incompatible with Article 81 if it seeks to regulate the commercial market by controlling not only what is made with the licensed technology but also the use made of it thereafter. The court also accepted that “the exclusivity conferred by a patent may not be used to license the invention on terms which restrict or distort competition in some respect going beyond what is strictly necessary to define the extent to which exclusivity is thereby surrendered.”¹¹⁸ This recognizes that anti-competitive harm collateral to licensing acts which would otherwise constitute an infringement must be justified, if at all, on its own merits and not because of its inclusion in a license of an intellectual property right.¹¹⁹

If I understand correctly, this Article 81 issue seems congruent with, perhaps even almost identical to, the analysis that will now be required in the wake of the Supreme Court’s decision last term in *Quanta*, discussed above.

Just before I concluded this paper, I came across another UK case of note dealing with abuse of patent issues, *SanDisk Corporation v Koninklijke Philips Electronics NV & Ors* [2007] EWHC 332 (Ch). SanDisk brought a claim alleging breach of the Chapter I and Chapter II prohibitions of the UK Competition Act and Articles 81 and 82 of the EC Treaty. The judge had to consider whether the aggressive enforcement of patent rights in multiple Member States constituted abusive conduct. While the Court found itself, in the end, without jurisdiction to hear the claim by SanDisk, the judgment does confirm, relying very much on *ITT ProMedia NV v. Comm’n, supra*, that the bringing of a legal action will only breach Article 82 where an undertaking in a dominant position brings an action which (i) cannot reasonably be considered as an attempt to establish its rights and can therefore only serve to harass the opposite party; and (ii) is conceived in the framework of a plan whose goal is to eliminate competition. *SanDisk*, Paragraphs 43-45. However the predicate for the action, apart from the important jurisdictional issues [which require a reading of the case to appreciate], seems to have much in common with *Walker Process* and its progeny. As the court stated (at Paragraph 46):

Where there is no dispute that the patents have been granted to the patentee, it seems to me that the enforcement action can be considered to be merely harassing in the sense explained above if the patent is obviously not infringed or if the patent is invalid and in either case the patentee either knows or believes that to be the case.

118 *Intel/Via* at Paragraph 72.-73.
119 *Id.* Paragraph 73.

These two cases are a good segue into the recent decision of the CFI in *Microsoft*, to which this paper now turns.¹²⁰

It is useful to remind ourselves what the *Microsoft* case in Europe was all about. It began with Sun Microsystems complaining that Microsoft would not supply it with interface information that was necessary to develop server software products fully compatible with Windows-based PCs.¹²¹ The Commission began an investigation and became aware of more widespread complaints by other developers of non-Microsoft server operating systems who also complained that their competitive positions in the market for workgroup server operating systems were being impaired by Microsoft's refusal to share its interoperability information.¹²² The investigation lasted for five years, after which the Commission concluded that Microsoft had violated Article 82 of the EC Treaty by refusing to supply its competitors with the interface information described and that Microsoft's refusal to supply the information could lead to the elimination of its competitors from the relevant market.¹²³ The Commission also found that:

- an increasing number of consumers were locked into Microsoft's Windows workgroup server operating system "[d]ue to the lack of interoperability that competing work group server operating system products can achieve with the Windows domain architecture;"¹²⁴
- Microsoft's proprietary interface information was "indispensable to carry on business in [the] market;"¹²⁵ and that
- Microsoft's refusal could not be objectively justified merely by the fact that it constituted a refusal to license intellectual property.¹²⁶

As a remedy, the Commission ordered Microsoft to share its interface information to enable competing workgroup server software developers to create products fully interoperable with Windows-based PCs.¹²⁷ The order also compelled Microsoft to disclose updated interface information whenever Microsoft released a new version of its own software.¹²⁸ Finally, the commission made the point that if any of Microsoft's interface information constituted intellectual property, Microsoft would be entitled to charge reasonable royalties for supplying that information to competitors.¹²⁹

Microsoft also involved tying – the tying of the Windows Media Player ("WMP") to the Windows operating system. PC manufacturers were required to license windows with WMP. If they wanted to install an alternative media player on Windows, they could do so only by installing something in addition to WMP. The Commission found that:

- streaming media players and PC operating systems were two separate products (rejecting Microsoft's argument that WMP was an integral part of Windows);
- there was and continues to be separate consumer demand for stand-alone media players and a number of vendors develop and supply media players on a stand-alone basis; and

120 Case T-2-1/04, *Microsoft Corp. v. Commission* (Sep. 17, 2007), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62004A0201:EN:HTML>. It is also available via Lexis, where it is cited as 2007 ECJ EUR-Lex LEXIS 2620. The case will be referred to here simply as "*Microsoft CFI*" and citations will be to the pertinent paragraph number(s).

121 Case COMP/C- 3/37.792 (Mar. 24, 2004), cited here as "Microsoft EC" and to the pertinent paragraph. The full decision is available at http://europa.eu.int/comm/competition/index_en.html A far shorter and more reader-friendly summary of the case is published in the Official Journal of the European Union, cited here as *Microsoft EC OJ Paragraph* ____.

122 See Hesse, *supra* at 32-33.

123 *Microsoft EC*, Paragraph 692.

124 *Id.* Paragraph 694.

125 *Id.* Paragraph 712.

126 *Id.*

127 *Id.* Paragraph 799.

128 *Id.* Paragraph 1022.

129 *Id.* Paragraph 1008.

- Microsoft itself developed and distributed versions of its WMP for other PC operating systems and promoted WMP in direct competition with third-party media players.¹³⁰

As a remedy, the Commission ordered Microsoft to offer end-users and OEMs within the European Union a full functioning version of the Windows operating system not incorporating WMP. Microsoft was thus required to provide so-called “Windows Lite.” Microsoft was also enjoined from using any means that would have the equivalent effect of tying WMP to Windows, for example by reserving privileged interoperability with Windows to WMP or by promoting WMP over competitors’ products through Windows.¹³¹

Lastly, a fine was imposed. The basic fine was €165,732,101, which was uplifted by doubling for the gravity of the offense to €331,464,203, and then uplifted by another 50% for the duration of the infringement for a total of €497,196,304. This was a very large fine!

Microsoft appealed to the CFI, which affirmed the EC in all material respects. Regarding the refusal to deal, the main area of the case of lasting interest, the CFI purported to apply, but also expanded upon, the principles of *McGill* and *IMS Health* discussed above. Indeed, Microsoft itself relied on the criteria laid down in *McGill* and *IMS Health* while the Commission argued that an “automatic” application of the criteria laid down in *IMS Health* would be “problematic,” and that in order to determine whether such a refusal was abusive, one must take into account all the particular circumstances surrounding the refusal, which need not necessarily be the same as those identified in *McGill* and *IMS Health*.¹³² After discussing these and other cases, the CFI reiterated that it would only be “in exceptional circumstances that the exercise of the exclusive right by the owner of [an] intellectual property rights may give rise to an abuse [of a dominant position]...” within the meaning of Article 82.¹³³ The court then stated that the following circumstances could be considered “exceptional” in this sense:

- a refusal relates to a product or service indispensable to the exercise of a particular activity on a neighbouring market;
- the refusal is of such a kind as to exclude any effective competition on that neighbouring market; and
- the refusal prevents the appearance of a new product for which there is potential consumer demand.¹³⁴

If the circumstances are thus “exceptional,” the refusal will infringe Article 82 “unless the refusal is objectively justified.”¹³⁵ It is completely unclear under what circumstances a refusal might be deemed “objectively justified,” although it is clear that “... the mere fact of holding intellectual property rights” will never “in itself constitute objective justification for the refusal to grant a license,” since if that were so “the exception established by the case-law could never apply.”¹³⁶

Notably, too, the CFI¹³⁷ observed that not all three of these circumstances need necessarily be present for Article 82 to become applicable and that in the absence of one or more of the circumstances described above, the Court could go on to consider other factors advanced by the Commission.¹³⁸

¹³⁰ *Microsoft EC OJ*, Paragraph 26.

¹³¹ *Id.* Paragraphs 33-34. Microsoft was also enjoined from giving OEMs or users a discount conditional on their obtaining windows together with WMP. The unbundled “Windows Lite” version had to be no less performing than the version of windows bundled with WMP.

¹³² *Microsoft CFI* Paragraph 315-16.

¹³³ *Id.* Paragraph 331.

¹³⁴ *Id.* Paragraph 332.

¹³⁵ *Id.* Paragraph 333.

¹³⁶ *Id.* Paragraph 690.

¹³⁷ See Paragraph 336 and other paragraphs therein referred to.

¹³⁸ The other factors advanced by the Commission were three: (1) the information Microsoft refused to disclose related to interoperability in the software industry, a matter to which the Community Legislature attached particular importance; (2) Microsoft used its extraordinary power on the client PC operating systems market to eliminate competition on the adjacent work group server operating systems market; and (3) the conduct in question involved in disruption of previous levels of supply. *Microsoft CFI* ¶ 317.

It is difficult to avoid the conclusion that the *Microsoft* CFI decision expands the space occupied by Article 82 and diminishes, somewhat, the space occupied by the protections of intellectual property law. Many observers have concluded from the decision that a dominant firm will have little room to establish that a refusal to supply is objectively justified once it has been determined that the information sought by the rival is “indispensable,”¹³⁹ a word with the potential to have an extremely elastic meaning. Microsoft had argued that “. . . a particular technology [could not] be characterized as indispensable if it is ‘economically viable’ for the competitors of the undertaking in a dominant position to develop and market their products without having access to that technology.”¹⁴⁰ In rejecting that argument, the Commissioner seems to have said that what I need from you is “indispensable” if without it I cannot become your equal in our competing commercial endeavors.¹⁴¹ Finally, where *McGill* and *IMS Health* had required the prevention of any competition in the neighboring market, *Microsoft* evolved that requirement to something less – the suppression of expansion by existing rivals in the neighboring market. Thus, the bars for proving prerequisites (“indispensability” and “exceptional circumstances”) seem to have been lowered. While this may be a Microsoft-specific elasticity, these things have a way of migrating elsewhere.

7. Antitrust issues arising out of the settlement of patent litigation, normally in a so-called “Hatch Waxman” setting.¹⁴² This is an area of pertinence only in the United States and hence comes last in this paper. It has limited relevance to international or transatlantic issues except insofar as it underscores the “inside the patent”/ “outside the patent” distinction I have mentioned at various points in this paper. In any case, and while a niche topic even in the US (but a large niche), it is an area of great interest on the west side of the Atlantic and not just because it is an area of fierce disagreement even between the FTC and the DOJ. There is roiling discontent at the Commission about its failure to get courts to listen to it in respect of reverse payments in patent settlement litigation; at least three circuits (Federal, Second, and Eleventh) have issued decisions broadly holding that, like Las Vegas, what happens within the patent grant stays within the patent grant. These holdings amount to a near-total exclusion of antitrust from conduct within the patent grant and hence gives patent holders a right, if they can find a way, to bring about anticompetitive outcomes within the patent grant. The presumption of validity that accompanies the patent grant adds to the mix in important ways too. In short, these are interesting cases and there is a great deal below the surface that is pertinent to the broader issues of IP and antitrust.

While there are a number of cases of interest, I am for now going to mention just four, which taken together illuminate the issues well enough. The first case is *In re Indep. Serv. Orgs. Antitrust Litig.*,¹⁴³ wherein the court held that a patentee or copyright owner generally has an absolute right to refuse unilaterally to license patents or copyrights (or refuse to sell patented or copyrighted products) for any reason. The plaintiffs, independent service operators (ISO’s in the parlance) were complaining about the refusal of Xerox to sell them parts they needed to service Xerox products in the aftermarket. In other words, the case was an offspring of the *Kodak* case.

The precise holding was this:

[I]n the absence of any indication of illegal tying, fraud in the Patent and Trademark Office, or sham litigation, the patent holder may enforce the statutory right to exclude others from making, using, or selling the claimed invention free from [antitrust] liability... [This is so] even if the refusal to deal impacts competition in more than one market.

This was a broad holding against the plaintiff/appellant (interestingly, represented by now Chief Justice Roberts). Other circuits have slightly different and less sweeping rules,¹⁴⁴ but the Federal

139 See, e.g., Hesse, *supra* at 33 and n. 22; *Id.* Paragraph 694.

140 *Id.* Paragraph 337.

141 See *Id.* Paragraph 412.

142 Part of this section is an edited version drawn from part of last year’s paper, “The Incredible Shrinking Scope and Scale of American Antitrust, 1976-2007.”

143 203 F.3d 1322, 1329 (Fed. Cir. 2000), *cert. denied*, 531 U.S. 1143 (2001).

144 In the First and Ninth Circuits, however, the refusal to license (or sell) only gives rise to a rebuttable presumption that the refusal is supported by a legitimate business reason and, in the Ninth Circuit, that presumption can be rebutted by *subjective intent* evidence. See *Image Tech. Serv., Inc. v. Eastman Kodak Co.*, 125 F. 3d 1195, 1218 (9th Cir. 1997); *Data Gen. Corp. v. Grumman Sys. Support Corp.*, 36 F.3d 1147, 1187 (1st Cir. 1994); see also *Microsoft*, 253 F.3d at 63 (“frivolous” to argue “absolute and unfettered right” to use one’s own intellectual property as one wishes). It remains to be seen whether the use of subjective intent evidence, without satisfying the factual predicate of *Aspen*, can stand after *Trinko*.

Circuit's opinion in the area is doubtless the most important as it comes from a court that hears a lot of these issues more often than others. The decision was, and remains, controversial, and it is the starting point in a way for thinking about the next two cases.

Second, there is *Schering-Plough, Corp. v. F.T.C.*¹⁴⁵ What happened is that Schering settled some patent litigation with some generic companies who had made a "Paragraph IV certification" under the now familiar Hatch-Waxman regime under which a company seeking approval from the Food and Drug Administration (FDA) to market a new drug must file a New Drug Application (NDA) demonstrating the safety and efficacy of its product. Once an NDA has been approved and a company starts marketing a "brand name" version of the drug, a company seeking to market a generic version of that drug may file an Abbreviated New Drug Application (ANDA) demonstrating that its product is the "bioequivalent" of its brand name counterpart.

If the brand name version of the drug is the subject of one or more patents, FDA may not make its approval of an ANDA effective before the expiration of any such patent, unless the applicant makes a "Paragraph IV certification" that such patent is either invalid or not infringed by the generic version. If the patent holder files an action for infringement within 45 days of receiving notification of that certification, FDA's approval is automatically stayed for 30 months (unless the patent expires or a court holds the patent invalid or not infringed).

The settlements Schering entered into in each case involved (a) setting a date earlier than the expiry of the relevant patent after which the generics could enter the market, and (b) some non-trivial consideration flowing from Schering to the generics. There were a variety of other things going on in the case as well, including: judicial involvement in the settlements; cross licenses flowing to Schering; and a mediation of one of the patent disputes that suggested an uncertain 50/50 sort of litigation outcome.

The Commission's theory was simply that the payments from Schering to the generics ("reverse payments" as they have universally become known) coupled with the delayed entry of the generic amounted, pretty much without more, to a violation of Section 1 of the Sherman Act.

The Commission was defeated by Schering and the ALJ at trial; declared itself the winner on appeal to itself; lost by a wide margin in the Eleventh Circuit; got mugged by the DOJ, which opposed the Commission's own petition for *certiorari*, and then was quietly humiliated by the Supreme Court's denial of *certiorari*. The Commission is still licking its wounds and bruising for a fight and has chosen to make it *Cephalon* (see discussion of that case below). The problem for the FTC is that the Eleventh Circuit's decision was very broad, to the effect that any competition lost was within the "exclusionary potential" of the patent claims, regardless of the purpose or effect of the agreements. That is, it was "inside the patent." Furthermore, the Commission took the position that no sort of mini or other trial on the merits of the patents was necessary or desirable and so the Commission's position about the presumed anticompetitive effect of the agreements was the same whether the patent was 99% likely to be enforced or 1% likely to be enforced. But the Commission's actual position makes the most sense only if the patent is presumed to be nearly worthless.

And so the Commission is receiving annual reports about patent settlements and many of these reports contain arrangements that the Commission finds offensive. Yet it seemed to be doing nothing, at least until it filed suit against Cephalon last January. This is, no doubt, partly because of the third case of this group of four — *In Re: Tamoxifen Citrate Antitrust Litigation*.¹⁴⁶ The case had some skeletal similarities with Schering but the facts were quite different as the patent at issue had already been declared invalid by the time of the challenged settlement agreement.

As in *Schering*, the settlement at issue in *Tamoxifen* arose against the statutory backdrop of the Hatch-Waxman Act, summarized ever so briefly above, which of course establishes procedures designed to facilitate the market entry of lower-priced generic drugs while maintaining incentives to

145 402 F.3d 1056 (11th Cir. 2005).

146 429 F.3d 370 (2d Cir. 2005).

invest in new drug development. Under the version of the Hatch-Waxman Act in effect at the time of the relevant events, the first company to file an ANDA with a Paragraph IV certification for a particular drug was granted the exclusive right to market the generic version until 180 days after the earlier of two dates: (1) when the company began commercial marketing of the generic version, or (2) when a court held the patent invalid or not infringed.

Barr filed an ANDA to market a generic version of Zeneca's tamoxifen. In 1987, Barr amended its ANDA to include a Paragraph IV certification; shortly thereafter, Zeneca sued Barr for patent infringement in the United States District Court for the Southern District of New York. In 1992, the district court held the pertinent patent (the '516 patent) invalid and unenforceable on the ground that, in a predecessor patent application, Zeneca had fraudulently withheld data regarding the hormonal effects of tamoxifen on mice.¹⁴⁷ Zeneca appealed to the Federal Circuit. While that appeal was pending, Zeneca and Barr entered into a settlement, conditioned on *vacatur* of the judgment invalidating the '516 patent. The settlement provided that Barr would receive a cash payment of \$21 million from Zeneca, withdraw its Paragraph IV certification and its challenge to the validity of the patent, and enter into a license with Zeneca for the duration of the patent term, under which Barr would be allowed to market Tamoxifen supplied by Zeneca. According to the complaint, Zeneca and Barr also agreed that Barr would not market its generic version of the drug until the patent expired. If another generic manufacturer successfully invalidated the patent, the parties allegedly understood that Barr would attempt to invoke the exclusivity period on the basis of its previous Paragraph IV certification (and argue that the exclusivity period would not begin to run until Barr began commercial marketing of the generic version of the drug). If it were successful, Barr would effectively discourage any other generic manufacturer from entering the market until the patent expired

As agreed, Zeneca dismissed its appeal, and Zeneca and Barr moved to vacate the district court's decision. Consistent with its practice at the time, the Federal Circuit granted the parties' motion.¹⁴⁸ Three other companies later filed ANDAs with Paragraph IV certifications for generic versions of tamoxifen. Zeneca sued all three for patent infringement and prevailed. While that patent infringement litigation was still pending, Barr attempted to invoke the 180-day exclusivity period, but the FDA (after litigation on the issue) ultimately refused to allow it to do so.

In 2002, various plaintiffs filed a class action against Zeneca and Barr in New York alleging that the settlement unlawfully restrained competition by preventing Barr (and others) from marketing generic versions of the drug, thereby enabling Zeneca to continue monopolizing the market for tamoxifen. The Second Circuit affirmed the District Court's dismissal of the complaint.

The court first concluded that the complaint could not state an antitrust claim based on the settlement alone "without alleging something more than the fact that Zeneca settled after it lost to Barr in the district court." The court reasoned that "courts are bound to encourage' the settlement of litigation," and that restrictions on patent settlements might frustrate "the goals of the patent laws because the increased number of continuing lawsuits that would result would heighten the uncertainty surrounding patents." Although the court of appeals acknowledged that a settlement could be invalid under the antitrust laws if the parties had entered into the settlement in bad faith, the court refused to consider the likelihood of success on the underlying patent infringement claim in assessing the validity of a settlement. The court reasoned that it was impossible to assess the likelihood of Zeneca's success on appeal "with any degree of assurance."

The court also concluded that the mere allegation that the patent holder made a "reverse payment" to the alleged infringer as part of the settlement did not suffice to make out an antitrust claim, reasoning that "reverse payments are particularly to be expected in the drug-patent context because the Hatch-Waxman Act created an environment that encourages them." The court explained that a prospective generic manufacturer "has relatively little to lose" in a patent infringement suit precipitated by a Paragraph IV certification, whereas "[t]he patent holder's risk if it loses ... is correspondingly large."

¹⁴⁷ *Imperial Chem. Indus., PLC v. Barr Labs.*, 795 F. Supp. 619, 621-622 (S.D.N.Y. 1992).

¹⁴⁸ *Imperial Chem. Indus., PLC v. Heumann Pharm. GmbH & Co.*, 991 F.2d 811 (1993).

The court rejected plaintiffs' argument that the settlement was invalid under the antitrust laws because the size of the reverse payment was excessive, although the court acknowledged that "[t]here is something on the face of it that does seem 'suspicious' about a patent holder settling patent litigation against a potential generic manufacturer by paying that manufacturer more than either party anticipates the manufacturer would earn by winning the lawsuit." According to the court, however, "so long as the patent litigation is neither a sham nor otherwise baseless, the patent holder is seeking to arrive at a settlement in order to protect that to which it is presumably entitled: a lawful monopoly over... the patented product." The court explained that "the law allows the settlement even of suits involving weak patents with the presumption that the patent is valid and that settlement is merely an extension of the valid patent monopoly."

The court ultimately held that, "absent an extension of the monopoly beyond the patent's scope ... and absent fraud ..., the question is whether the underlying infringement lawsuit was objectively baseless in the sense that no reasonable litigant could realistically expect success on the merits." Applying that standard, the court determined that the settlement in this case was valid under the antitrust laws.

The plaintiffs filed a petition for *certiorari* and the Court invited the Solicitor General to express his views. In its filing, the SG took the view that the court of appeals erred by focusing on whether the underlying patent infringement claim was "objectively baseless"—a standard typically used in determining whether a defendant is entitled to antitrust immunity under the *Noerr-Pennington* doctrine—rather than engaging in a broader inquiry concerning the patent holder's likelihood of success on that claim. According to the SG, the court of appeals correctly recognized that, in passing on the validity of a settlement, a reviewing court should view the settlement from the perspective of the parties at the time they entered into it. But, said the SG, the court nevertheless refused to inquire into the likelihood of success on the patent infringement claim on the ground that it was impossible to assess the likelihood of success (in this case, Zeneca's likelihood of prevailing on appeal) "with any degree of assurance."

The SG emphasized that a court would not need to conduct a full trial on the merits of the underlying claim to assess the patent holder's likelihood of success and that a limited examination of the merits of the claim is hardly impossible. Indeed, similar inquiries are commonplace, such as in deciding whether to grant a preliminary injunction ... or in reviewing the fairness of a proposed class-action settlement. The SG also opined that the atypical facts of the case illuminated the court of appeals' error in refusing to consider the strength of the infringement claim beyond a determination that the claim was not objectively baseless.

The SG put special emphasis on the fact that at the time the parties entered into the settlement at issue here, the district court had already held Zeneca's patent invalid in a decision on the merits. As a result, said the SG, the Federal Circuit "would have reviewed [the district court's] factual findings underlying [its] conclusion of invalidity with considerable deference, rather than engaging in a presumption of validity." Thus, the case was plainly one in which, at the time of settlement, there was reason to doubt the patent holder's likelihood of success, although pointing the other way was the fact that Zeneca had prevailed in all three of its other infringement suits presenting the identical issue. The SG's criticism was that the standard articulated by the court of appeals precluded any such assessment.

But despite all the criticism of the Second Circuit's decision, the SG recommended against the Court taking the case on the theory that it did not provide a suitable vehicle. The Second Circuit's decision is obviously at odds with some fundamentals of the Eleventh circuit's decision in *Schering* inasmuch as in *Schering* the Eleventh Circuit held that the "proper analysis" of an antitrust challenge to a patent settlement "requires an examination of: (1) the scope of the exclusionary potential of the patent; (2) the extent to which the agreements exceed that scope; and (3) the resulting anticompetitive effects."¹⁴⁹ On the other hand, both courts put their focus on whether the "exclusionary effects of the agreement [exceeded the] scope of the patent's protection." And finally the Eleventh Circuit, unlike

149 *Schering-Plough* at 1066 (citing *Valley Drug Co. v. Geneva Pharm., Inc.*, 344 F.3d 1294, 1312 (11th Cir. 2003), *cert. denied*, 543 U.S. 939 (2004)).

the court in *Tamoxifen*, did not purport to hold that proof of “sham” or “objectively baseless” litigation is a prerequisite to antitrust liability (in the absence of proof that the settlement extended the patent holder’s monopoly beyond the patent’s scope).

The SG’s *Tamoxifen* brief brings to mind a bit the SG’s filing in *LePages*. The government plainly thought both decisions wrong, but apparently feared that the record was too tangled to allow for a clean decision.

The most recent response of the FTC to all of this has been, in February of this year, to file a suit against Cephalon alleging monopolization by it of the market for Provigil a branded prescription drug approved by the FDA for the treatment of excessive daytime sleepiness associated with narcolepsy.¹⁵⁰ According to the FTC complaint, Cephalon’s CEO has conceded that Provigil faces “no competition.”¹⁵¹ According to the FTC, Cephalon “bought off” through reverse payments four separate generic companies, each of which had planned to sell a generic version of Provigil and each of which had made a so-called Paragraph IV certification to the effect that either (a) its generic version of Provigil does not infringe Cephalon’s patents or (b) the patents were invalid. The FTC action against Cephalon is different from prior enforcement actions in several respects. First, the Commission went straight to Federal District Court and chose the District of Columbia as its preferred jurisdiction, presumably wanting to generate a conflict in the circuits so as to get one or more of these sorts of cases before the Supreme Court. In this respect, the Commission was frustrated almost at the outset, since Cephalon moved successfully to transfer the case to the Eastern District of Pennsylvania.¹⁵² This inability of the Commission to choose its own jurisdiction presents, for the commission, a separate problem, wholly apart from its otherwise frustrating experience with respect to Hatch-Waxman.

Second, the Commission did not sue any of the four generic manufacturers (Barr, Teva, Ranbaxy, and Mylan) who had filed the Paragraph IV certifications and received the “reverse payments.” This creates a rather different negotiating dynamic as between branded companies and generics in negotiating these arrangements since the risk of illegality may not be shared as in the past.

Third, by using a theory grounded on Section 2 of the Sherman Act, the Commission further changes the negotiating dynamics as between branded and generic pharmaceutical companies. Indeed, by focusing on Section 2 the Commission exposes the branded companies to private treble damage actions to a greater extent than the generics, although the generics are not necessarily free of liability in private actions just because the Commission has chosen only to pursue the branded company.

Fourth, the Commission seems to some extent to have taken on the burden of showing that one or more of the generic companies’ invalidity arguments would have prevailed, and hence, entry would in fact have occurred but for the payments by Cephalon.¹⁵³ This is a material change from the Commission’s prior rhetoric about not needing to inquire into the strength or weakness of the patent.

Based just on a reading of the complaint, the Commission seems to have a strong case relying upon theories and an approach not previously used. Still and all, the Commission continues to lobby Congress to change the law, while at the same time changing its approach slightly to accommodate the reality that it has lost all the cases it has brought under existing law.

150 The complaint and all other papers associated with this case are available via the FTC website at <http://www.ftc.gov/os/caselist/0610182/index.shtml>.

151 Complaint at Paragraph 27.

152 The opinion by Judge Bates ran to 21 pages and is of independent interest to US antitrust lawyers in general for its discussion of the transfer considerations attending enforcement actions brought by the government in the District of Columbia.

153 Complaint, Paragraphs 41-52.

OBSERVATIONS FROM THE FIELD: ACPERA'S FIRST FIVE YEARS

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I. INTRODUCTION

While some areas of antitrust law may involve varying degrees of uncertainty, price-fixing cartels are almost universally condemned.¹ This is due to the unequivocal acknowledgement of “tremendous harm caused by hard core cartels to businesses and consumers.”² As the Deputy Assistant Attorney General for the United States Department of Justice’s Antitrust Division has said, price-fixing cartels constitute “a crime – no different than common fraud or theft,” akin to stealing money “just as if they had lifted cash right out of their [victims’] wallets.”³ Such cartels “cheat their customers out of honest competition, and they pad their pockets with the profits of their conspiracy.”⁴ They are “sophisticated, premeditated crimes committed by highly-educated individuals in absolute secrecy.”⁵ The extent and nature of the offense makes clear the “contempt and disregard that the members of the cartel typically have for antitrust laws and enforcement.”⁶ Price fixing cartelists are the equivalent of modern day pirates—enemies of the global economy.⁷ There are now even rewards for their capture and identity.⁸

It is not surprising, then, that Justice Scalia described price-fixing cartels as “the supreme evil of antitrust.”⁹ Hardly a new position, the U.S. Supreme Court has long held that enforcement of the antitrust laws is “as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal freedoms.”¹⁰ In addition

- 1 See *FTC v. Superior Court Trial Lawyers Ass’n*, 493 U.S. 411, 421–23 (1990); *Ariz. v. Maricopa Med. Soc’y*, 457 U.S. 332, 342 (1982); *U.S. v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 224 n.59 (1940); R. Hewitt Pate, Acting Assistant Attorney Gen., Antitrust Div., Speech Before the British Society of International and Comparative Law: Anti-Cartel Enforcement: The Core Antitrust Mission (May 16, 2003) (“Since 1890, the Sherman Act has reflected the United States’ abiding faith that the elimination of competition in business [is] morally and economically wrong.”) (internal quotes omitted), (transcript available at <http://www.usdoj.gov/atr/public/speeches/201199.htm>); *U.S. v. Alton Box Bd. Co.*, No. 76 CR 199, 1977 WL 1374, at *11 (N.D. Ill. March 4, 1977) (noting the Department of Justice view that the price-fixing violation before the court “represents immoral, antisocial, and calculated conduct which should be punished as such”).
- 2 See speeches by Scott D. Hammond, Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dept. of Justice, Caught in the Act – Inside an International Cartel, Presented at OECD Paris, France (October 18, 2005) at 1 (transcript available at <http://www.usdoj.gov/atr/public/speeches/212266.htm>) [hereinafter “Caught in the Act”]. See also Scott Hammond, Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dept. of Justice, An Update of the Antitrust Division’s Criminal Enforcement Program (Nov. 16, 2005 at 1) (transcript available at <http://www.usdoj.gov/atr/public/speeches/213247.htm>) [hereinafter 2005 Update] (the “detection, prosecution, and deterrence of cartel offenses continue to be the highest priority of the Antitrust Division”); and Scott Hammond, Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dept. of Justice, From Hollywood to Hong Kong: Criminal Antitrust Enforcement Is Coming To A City Near You (Nov. 9, 2001) at 5 (transcript available at <http://www.usdoj.gov/atr/public/speeches/9891.htm>) [hereinafter “Hollywood to Hong Kong”] (“[b]y using informers, tape recordings, and search warrants, the message to the business community was clearly communicated – we will not pull any punches. These are the bare knuckle tools that the Division will use to detect and crack antitrust crimes.”).
- 3 Caught in the Act, *supra* note 2, at 1. Even law firms known for antitrust defense work/docs that cartels are “now branded a sophisticated form of theft.” See HOWREY TRANSATLANTIC CARTEL EXPERIENCE, http://www.howrey.com/docs/TACT_Brochure_April2005.pdf (last visited August 27, 2007). See also Memorandum of Understanding Between the Antitrust Div. and The Immigration and Naturalization Serv. (May 15, 1996) (available at <http://www.usdoj.gov/atr/public/criminal/9951.htm> (last visited April 17, 2008)) (“Whereas, the INS considers criminal violations of the Sherman Antitrust Act, 15 U.S.C. Section 1, to be crimes involving moral turpitude, which may subject an alien to exclusion or deportation from the United States”).
- 4 Scott Hammond, Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dept. of Justice, Beating Cartels At Their Own Game—Sharing Information In The Fight Against Cartels (Nov. 20, 2003) at 7 (transcript available at <http://www.usdoj.gov/atr/public/speeches/201614.htm>) [hereinafter Beating Cartels].
- 5 Caught in the Act, *supra* note 2, at 8.
- 6 Caught in the Act, *supra* note 2, at 2.
- 7 See OECD, HARD CORE CARTELS at 5 (2000), available at <http://www.oecd.org/dataoecd/39/63/2752129.pdf>. This is an attitude shared by antitrust enforcers in other countries as well. For example, Neelie Kroes, European Commissioner for Competition Policy said in February of 2008, “[i]n terms of economic governance, ... we have to ask ourselves how best to keep a grip on global actors in a global economy, if their anti-competitive behaviour is damaging the interest of the Union, its businesses or its citizens. Ideally, faced with global problems we would design truly global solutions.” First Symposium in Innsbruck (Feb. 7, 2008), <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/08/61&format=HTML&aged=0&language=EN&guiLanguage=en>. These global solutions may be developing. Professor Richard Schmalensee of the MIT Sloan School of Management noted in November 2007 that “[f]or better or for worse, the rest of the world seems to be modeling their competition laws and competition authorities on those in the European Community. Over 100 countries have established competition laws, a number that has increased two-fold since 1990 as more developing countries move towards market economies. In addition, countries that have had antitrust laws on the books have started enforcing those laws more aggressively in recent years.” <http://www.globalcompetitionpolicy.org/index.php?id=592&action=907> (last visited March 24, 2008). And Sir Anthony Clark, Master of the Rolls, stated in a speech given at an American Bar Association conference in London on October 3, 2007 that “[i]n today’s global village we can no longer live as islands unto ourselves. The continued growth of our ever-increasing globalised economy, of multi-national corporations, of the free movement of capital and services, of financial markets, of private international law and ever more common standards of human rights has an important consequence for us all. We must all ensure in this increasingly complex and interconnected world that our national civil justice systems are able effectively to respond to disputes with cross national boundaries.” (available at http://www.judiciary.gov.uk/docs/speeches/mr_american_bar_assoc_031007.pdf). Most recently, on March 26, 2009, the European Parliament voted 498 to 11 (with 17 abstentions) to adopt a 2008 White Paper recommending private damage actions to enforce EC rules against cartel activity. Melisa Lipman, *EU Parliament Backs Antitrust Relief For Victims*, Law 360, Mar. 26, 2009, http://www.law360.com/print_article/93881.
- 8 The United Kingdom’s Office of Fair Trading (“OFT”) announced in February of 2008 that it will pay financial incentives of up to £100,000 in return for information which helps it to identify and take action against illegal cartels. <http://www.of.gov.uk/news/press/2008/31-08> (last visited March 24, 2008).
- 9 *Verizon Commc’ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 408 (2004).
- 10 *Cnty. Commc’ns Co. v. City of Boulder*, 455 U.S. 40, 56 n.19 (1982) (quoting *U. S. v. Topco Associates, Inc.*, 405 U.S. 596, 610 (1972)). The OFT has advocated this view strongly during the last few years. In April of 2007, it issued a discussion paper recommending expanded private enforcement of the U.K.’s antitrust laws. The paper stated: “[s]trong competition regimes are essential for open, dynamic markets. They drive productivity and innovation and ensure the efficient allocation of resources, and are good for consumers and businesses.” OFT, PRIVATE ACTIONS IN COMPETITION LAW: EFFECTIVE REDRESS FOR CONSUMERS AND BUSINESS, p. 3 (Apr. 2007) (available at http://www.of.gov.uk/shared_oftr/reports/comp_policy/of916.pdf (last visited March 24, 2008)). The same paper went on to note that: “[i]f, under a system in which an action may only be brought on behalf of named individuals, an action does not proceed at all (or proceeds on behalf of only a small minority of those harmed...), an infringing undertaking will not be held to account for compensation that reflects either the harm caused to all the consumers affected by its anti-competitive behaviour, or its ‘ill-gotten gain’ from the infringing conducts.” *Id.* at p. 21. Philip Collins, the OFT’s Chairman, said at the time of the promulgation of the discussion paper that “[a] more effective private actions system would promote a greater culture of compliance with competition law and ensure that public enforcement and private actions work together to the best effect for businesses and consumers.” <http://www.of.gov.uk/news/press/2007/63-07> (last visited March 24, 2008).

to government enforcement, “[i]t is well recognized that private enforcement of [antitrust] laws is a necessary supplement to government action.”¹¹ Such private enforcement—*e.g.*, civil litigation and in particular class action lawsuits—is a vital part of “the federal scheme for deterring anti-competitive behavior.”¹² It has “long been recognized that class actions play an important role in the private enforcement of antitrust actions.”¹³ Government and private antitrust enforcement have historically gone hand-in-hand.¹⁴ Thus, in the most recent amendment to the antitrust laws, the Antitrust Criminal Penalty Enhancement and Reform Act of 2004, P.L. 108-237 (“ACPERA”) provided significant benefits to enhance both arms of antitrust enforcement.

With the passage of ACPERA, an Applicant gets all previous benefits of government immunity, as well as significant private enforcement benefits. If an Amnesty Applicant agrees to cooperate with civil litigants, ACPERA de-trebles an Amnesty Applicant’s civil exposure to actual damages attributable to the commerce done by it in the goods or services affected by the violation. Therefore, an Amnesty Applicant can enter the United States Department of Justice’s (“DOJ” or “Department”) leniency program to blow the whistle on its co-cartelists but no longer has to weigh exposure to joint and several treble damages through resulting civil antitrust litigation by the private bar. Accordingly, an Amnesty Applicant now receives significant civil liability benefits as well as an additional incentive to seek criminal immunity from the DOJ. This article examines some of the practical issues and competing interests that have been raised since ACPERA’s enactment.

This article is structured in five sections. Section two briefly summarizes the DOJ’s antitrust leniency program prior to the effective date of ACPERA. It also provides a brief overview of the basic features of ACPERA. Section three addresses to whom ACPERA cooperation is owed. Section four offers an in-depth analysis of some key features of the statute relevant to private antitrust suits: when the duty of cooperation by the Amnesty Applicant under ACPERA is triggered and the scope of such cooperation. Section five addresses the implications of potential competing civil and criminal ACPERA obligations.

II. THE DOJ’S CORPORATE LENIENCY PROGRAM AND THE PROVISIONS OF ACPERA

A. The Pre-ACPERA DOJ Corporate Leniency Program

The DOJ has “a policy of according leniency to corporations reporting their illegal antitrust activity at an early stage, if they meet certain conditions.”¹⁵ In 1993, the Department substantially revised its corporate leniency or amnesty program.¹⁶ Under these revisions, a corporation that either brought to the DOJ’s attention a cartel of which DOJ had been unaware, or was the first to come forward to cooperate in an investigation that was already underway, would, subject to certain conditions¹⁷ set out in the amnesty policy, receive complete immunity from prosecution for itself and for all its executives who cooperated in the investigation.

The policy behind the DOJ’s program was “to destabilize cartels, and [cause] the members of the cartels to turn against one another in a race to the Government.”¹⁸ The success of this program is evident in its statistics: Under the pre-1993 program, the DOJ received roughly one amnesty application per month; and under the post-1993 program, the application rate jumped to roughly two a month.¹⁹ “[I]n fiscal years 2004 and 2005, and so far in 2006, the Antitrust Division of the

11 *Cumberland Farms, Inc. v. Browning-Ferris Indus.*, 120 F.R.D. 642, 645 (E.D. Pa. 1988) (citations omitted).

12 *In re Bulk Extruded Graphite Prods. Antitrust Litig.*, 2006 WL 891362, at *4 (D.N.J. April 4, 2006).

13 *In re Vitamins Antitrust Litig.*, 209 F.R.D. 251, 258 (D.D.C. 2002) [hereinafter *Vitamins*].

14 Needle Kroes, European Commissioner for Competition Policy, First Symposium in Innsbruck (February 7, 2008).

15 See Corporate Leniency Policy (Aug. 10, 1993), at 1, www.usdoj.gov/atr/public/guidelines/0091.htm [hereinafter Corporate Leniency Policy].

16 “‘Leniency’ means not charging such a firm criminally for the activity being reported.” *Id.*

17 See Corporate Leniency Policy, *supra* note 15.

18 The Corporate Leniency program automatically grants amnesty to any corporation that reports illegal pre-investigation antitrust activity provided six conditions are met: (1) DOJ has not received information about the illegal activity from any other source; (2) once discovered, it acted promptly and effectively to end its participation in the activity; (3) it is candid and complete in reporting and cooperates fully with the DOJ investigation; (4) its confession is truly a corporate act, not isolated confessions from individuals; (5) where possible, it makes restitution to injured parties; and (6) it did not coerce another party to participate in the illegal activity and was not the leader or originator of the activity.

19 See Cong. Rec. at S3614 (Apr. 2, 2004).

19 See 2005 Update at 9.

Department of Justice has obtained fines of \$360 million, \$338 million, and \$473 million, respectively, and has brought criminal cases against 69 firms.²⁰ Cooperation obtained by the program has “led to the detection and prosecution of massive international cartels that cost businesses and consumers billions of dollars and has led to the largest fines in the Antitrust Division’s history.”²¹ The Division’s cartel enforcement efforts for the 2007 fiscal year imposed almost 30,000 jail days for participating corporate executives; recovered over \$630 million in fines and succeeded in obtaining the longest jail sentence (14 months) for a foreign national charged with a violation of U.S. antitrust laws.²²

However, an Amnesty Defendant, once entering the DOJ amnesty program, was almost guaranteed to face private civil litigation usually in the form of class actions for damages and injunctive relief. An amnesty application is, in essence, the functional equivalent of an acknowledgement of the existence of an illegal cartel;²³ therefore, the acknowledgement, by itself, established a strong foundation for future civil exposure to often large amounts. Under the provisions of the 1993 Act, the government could waive its right to criminal fines, but the Amnesty Defendant still faced joint and several treble damages in civil litigation.²⁴ This threat to the Applicant was a major impediment to corporate confessions to the DOJ.²⁵

According to one antitrust defense firm, “part of the calculus of determining to seek amnesty [pre-ACPERA] has traditionally been that while doing so eliminates the risk of criminal sanctions, amnesty leaves the recipient exposed to federal and state private lawsuits seeking treble damages.”²⁶ “In other words, before voluntarily disclosing its criminal conduct, a potential Amnesty Applicant [had to] weigh the potential ruinous consequences of subjecting itself to liability for three times the damages that the entire conspiracy caused.”²⁷ Thus, prior to the 2003 amendments to ACPERA, DOJ amnesty came at a high price to corporations: “the threat of exposure to a possible treble damage lawsuit by the victims of the conspiracy.”²⁸

B. ACPERA Removes a Significant Disincentive to Reporting Antitrust Violations

ACPERA applies to corporate antitrust leniency applicants²⁹ and their cooperating individuals³⁰ who enter into either a conditional or final amnesty agreement³¹ with the DOJ.

- 20 Thomas O. Barnett, Assistant Attorney General, Antitrust Division, U.S. Department of Justice, Criminal Enforcement Of Antitrust Laws: The U.S. Model (September 14, 2006) at 1 (transcript available at <http://www.usdoj.gov/atr/public/speeches/218336.htm>) (hereinafter “Criminal Enforcement”). The European Commission (“EC”) issued its notice on immunity from fines in cartel cases in 2006, which replaced an earlier policy from 1996. See Commission Notice on Immunity from Fines And Reduction of Fines in Cartel Cases, 2006/C298/11, 2006 O.J. (C298)17. Between February of 2002 and the end of 2005, the EC received 167 applications for leniency, 87 for immunity and 80 for reductions in fines. Europa Press Release, Competition: Commission Leniency Notice Frequently Asked Questions (Dec. 7, 2006) (available at <http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/06/470&format=HTML&aged=1&language=EN&guiLanguage=en>). From February of 2002, through the end of 2006, the EC has taken formal decisions in six cartel cases in which companies co-operated with the investigations under its Leniency Notice. Since the entry into force of the current Leniency Notice on February 14, 2002 until the present, the Commission has taken formal decisions in 6 cartel cases in which companies co-operated with the investigations under the 2002 Leniency Notice.
- 21 See Cong. Rec. at S3614 (Apr. 2, 2004).
- 22 Prepared Remarks Of Thomas O. Barnett, Assistant Attorney Gen., Antitrust Div., At The Task Force On Antitrust And Competition Comm., On The Judiciary U.S. H.R. (Sept. 25, 2007). (“these accomplishments reflect great strides in the Division’s efforts to rid the marketplace of cartels and their harm to consumers.”) *But cf.* Nathan Miller, Strategic Leniency And Cartel Enforcement 25 (Sept. 2007) (available at http://www.econ.berkeley.edu/users/webfac/gilbert/221_F07/miller.pdf) (last visited March 24, 2008) (“[a]s shown there is no discernable increase in [cartel] discoveries immediately following the introduction of ACPERA. The results suggest that ACPERA may have little substantial impact on detection capabilities.”)
- 23 See fn. 17.
- 24 See 15 U.S.C. Section 15. As Neelie Kroes of the EC said in a November 2007 speech: “[g]iven the costs of bringing a damages action in the competition field and the uncertainty in the outcome, the balance of risk and reward is often unfavourable to consumers. So consumers rarely if ever go to court... Out-of-court settlements can only really work if they are coupled with a realistic chance of effective court action. And when court action can only be taken by each consumer individually, no consumer will ever make it to the court room: collective redress mechanisms are therefore an absolute must.” (Nov. 9, 2007) (transcript available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/07/698&format=HTML&aged=0&language=EN&guiLanguage=en>).
- 25 See Cong. Rec. at S3614 (Apr. 2, 2004).
- 26 See Antitrust Update, New Federal Antitrust Legislation Alters Risk Assessments (August 2004) at www.weil.com. (last visited March 24, 2008) (“Weil article”).
- 27 See Cong. Rec. at S3614 (Apr. 2, 2004).
- 28 *Id.*
- 29 Antitrust leniency applicant “means, with respect to an antitrust leniency agreement, the person that has entered into the agreement.” See ACPERA at Section 212(3).
- 30 Cooperating individual “means, with respect to an antitrust leniency agreement, a current or former director, officer, or employee of the antitrust leniency applicant who is covered by the agreement.” See ACPERA Section 212 (5) (emphasis added).
- 31 An amnesty agreement, or “antitrust leniency agreement” as it termed in ACPERA, “means a leniency letter agreement, whether conditional or final, between a person and the Antitrust Division pursuant to the Corporate Leniency Policy of the Antitrust Division in effect on the date of the execution of the agreement.” See ACPERA at Section 212(2). See also Gary R. Spratling, Dep. Asst Attorney Gen., Antitrust Div., U.S. Dept. of Justice, Making Companies An Offer They Shouldn’t Refuse,” The Bar Ass’n of D.C.’s 35th Annual Symposium on Associations and Antitrust (February 16, 1999) at Ex. 2 (transcript available at www.usdoj.gov/atr/public/speeches/2247.htm) [hereinafter Making An Offer] (“In cases in which the Division’s investigation ultimately reveals that the amnesty applicant has not engaged in any criminal conduct, the Division will not grant amnesty because it is unnecessary.”) Thus, a corporation that is investigated, but is ultimately not found to have violated the antitrust laws, owes no duty of cooperation to civil plaintiffs.

The passage of ACPERA³² in June of 2004 allowed “the Justice Department, in appropriate circumstances, to limit a cooperating company’s civil liability to actual, rather than treble, damages in return for the company’s cooperation in both the resulting criminal case as well as any subsequent civil suit based on the same conduct.”³³ Hewitt Pate, the Assistant Attorney General for the Antitrust Division, noted in June of 2004 that “the de-trebling provision of the Act removes a major disincentive for submitting amnesty applications,³⁴ aiming to increase the incentives “for participants in illegal cartels to blow the whistle on their co-conspirators and cooperate” with the DOJ and civil plaintiffs.^{35, 36} One of the primary goals of ACPERA’s de-trebling provision was to advance cartel detection by encouraging self-reporting among corporations by removing the threat of treble damage civil suits. This is particularly valuable since cartel activity can be particularly difficult to uncover and prove without cooperation from a co-conspirator.³⁷ As a result of ACPERA, the DOJ gets crucial³⁸ cooperation and can pursue and detect more cartels. “The central purpose of [ACPERA] is to bolster the leniency program already utilized by the Antitrust Division so that antitrust prosecutors can more effectively go after antitrust violators.... cognizant of the needs of victims.”³⁹

Because of the laudable benefit of increasing self-reporting of cartels, as well as the fact that “[t]he bottom line is [that] a business is far more likely to be the victim of a cartel than a member of one,”⁴⁰ ACPERA was met with little to no opposition and quickly passed into law less than one year after its introduction in committee. Its sponsor in the U.S. House of Representatives described it as “truly bipartisan and bicameral in nature.”⁴¹

1. ACPERA’s Single Damages Protection

Section 213(a) of ACPERA, entitled “Limitation on Recovery,” states that the “amount of damages recovered by or on behalf of a claimant from an antitrust leniency applicant . . . shall not exceed that portion of the actual damages sustained by such claimant which is attributable to the commerce done by the applicant in the goods or services affected by the violation.”⁴² Often referred to as the de-trebling provision, the Act effectively “amends the antitrust laws to modify the damage recovery from a corporation and its executives to actual damages.”⁴³ In other words, “the total liability of a successful leniency applicant would be limited to single damages without joint and several liability.”⁴⁴ An ACPERA Amnesty Applicant “would only be liable for the actual damages attributable

32 ACPERA consists of five numbered sections (Sections 211-215), as Title II of H.R. 1086. It was introduced on March 5, 2003 by sponsoring Congressman Sensenbrenner. There were 16 co-sponsors, which notably included both Republican and Democratic sponsors. Senator Hatch, on November 6, 2003, at the Committee on the Judiciary, reported the bill with an amendment in the nature of a substitute — which included the language of ACPERA — without a written committee report. Representative Sensenbrenner appended a committee report to his floor statement in June of 2004. A helpful overview of the legislative history of ACPERA is found in Harrison & Bell at 219-21, *infra* note 35.

33 See Cong. Rec. at S3613 (April 2, 2004).

34 See ACPERA Press Release. Legislators also noted that ACPERA was created to eliminate this same “disincentive to self-reporting.” See Cong. Rec. at S3614 (April 2, 2004).

35 See Cong. Rec. at S3613 (April 2, 2004). See Glenn Harrison & Matthew Bell, *Recent Enhancements In Antitrust Criminal Enforcement: Bigger Sticks and Sweeter Carrots*, 6 *Houston Bus. & Tax L.J.* 207, 226 (2006) [hereinafter Harrison & Bell].

36 The benefits of ACPERA were further described by Senator Hatch: “more companies will disclose antitrust crimes, which will have several benefits. First, I expect that the total compensation to victims of antitrust conspiracies will be increased because of the requirement that amnesty applicants cooperate. Second, the increased self-reporting incentive will serve to further de-stabilize and deter the formation of criminal antitrust conspiracies. In turn, these changes will lead to more open and competitive markets.” See Cong. Rec. S3614 (April 2, 2004). See also *Scouring Pad Maker Will Plead Guilty to Charges of Conspiring to Fix Prices*, BNA Antitrust & Trade Reg. Rep., Nov. 4, 1993, at 585. (“[J]ust and swift resolution of a matter that otherwise might be complex and difficult to investigate was made possible by early and complete cooperation by one of the participants.”)

37 See Makan Delrahim, Deputy Assistant Attorney General, U.S. Dep’t of Justice Perspectives on International Antitrust Enforcement: Recent Legal Developments and Policy Implications, address before the American Bar Association Section of Antitrust Law Fall Forum at 8-9 (Nov. 18, 2003) (available at <http://www.usdoj.gov/atr/public/speeches/201509.pdf>).

38 Cooperation by cartelists is increasingly valuable as detection becomes more difficult, and cartelists employ more sophisticated means to conceal their crime. “[C]artelists are criminals” and “adept at concealment.” See Thomas O. Barnett, Ass’t Attorney General, Antitrust Div., U.S. Dep’t of Justice, *Seven Steps to Better Cartel Enforcement*, 11th Annual Competition Law & Policy Workshop (June 2, 2006) at 8 [hereinafter *Seven Steps*]. See also *Caught in the Act*, *supra* note 2, at 2 (“[t]he conspirators have discussed the criminal nature of their agreements; they have discussed the need to avoid detection by antitrust enforcers in the United States and abroad; and they have gone to great lengths to cover-up their actions — such as using code names with one another, meeting in secret venues around the world, creating false ‘covers’ — i.e., facially legal justifications — for their meetings, using home phone numbers to contact one another, and giving explicit instructions to destroy any evidence of the conspiracy”); *Seven Steps* at 8 (“True to type, many [cartelists] react to an investigation by actively obstructing the investigations of antitrust prosecutors.”); Scott Hammond, Deputy Ass’t Attorney Gen., Antitrust Div., U.S. Dep’t of Justice, *Ten Strategies for Winning the Fight Against Hardcore Cartels*, (October 18, 2005) (“When No ‘Hot Documents’ Are Uncovered by Investigators — A Frequent Event As Increased Deterrence Will Cause Cartels to Become More Sophisticated — Individual Admissions Are Needed to Prove Existence of Cartels”).

39 See Cong. Rec. at H3660 (June 2, 2004).

40 See *Hollywood to Hong Kong*, *supra* note 2, at 7-8; see also *Beating Cartels*, *supra* note 4, at 12 (“[i]t just makes no sense that honest businesses operating in a free market economy would not favor strong cartel enforcement.”). A similar sentiment was expressed in a recent letter to the editor of the U.K. newspaper, *The Financial Times*: “[i]f there is a guiding principle that dictates the way we do business in the U.K. it is that it should be conducted fairly.... Those operating a cartel are engaging in theft and should face [sanctions] I will not defend the indefensible....” The author was none other than David Lennan, who serves as Director General of the British Chamber of Commerce. *Hollywood to Hong Kong*, *supra* note 2.

41 Cong. Rec. at H3657 (June 2, 2004).

42 ACPERA Section 213(a).

43 *Id.*

44 See Cong. Rec. at S3614 (Apr. 2, 2004).

to its own conduct, rather than being liable for three times the damages caused by the entire unlawful conspiracy.⁴⁵ This significant damages reduction comes with a price: an Amnesty Applicant must provide substantial, timely cooperation to the civil plaintiffs.⁴⁶

Importantly, ACPERA affects only the division of responsibility for damages, leaving the remaining non-Amnesty Applicants jointly and severally responsible for remaining market-wide trebled damages, including the Amnesty Applicant's sales. While the Amnesty Applicant's exposure is limited to single damages "caused by its own actions," "the rest of its non-cooperating co-conspirators ... remain jointly and severally liable."⁴⁷ Nothing in ACPERA "affect[s], in any way, the joint and several liability of any party to a civil action described in section 213(a), other than that of the antitrust leniency applicant and cooperating individuals as provided in section 213(a) of this title."⁴⁸

This "damages-preserving" provision was explained by Senator Hatch as being necessary and justified: "because all other conspirator firms would remain jointly and severally liable for three times the total damages caused by the conspiracy, the victims' potential total recovery would not be reduced."⁴⁹ The remaining defendants "will be fully, jointly and severally liable for the treble damages the conspiracy caused, minus only the amount actually paid by the leniency applicant."⁵⁰ Indeed, Congress anticipated that ACPERA would effectively increase the recovery by private plaintiffs.⁵¹ As a result, "the full scope of antitrust remedies against [non-ACPERA] parties will remain available to the government and private antitrust plaintiffs."⁵²

2. ACPERA's Duty of Cooperation

One of the most significant components of ACPERA, and key for its success in ensuring that those harmed by the cartel are justly compensated, is its mandate that Amnesty Applicants cooperate with the civil plaintiffs in private litigation in order to be entitled to single damages protection. Specifically, ACPERA provides broad outlines of three areas of cooperation:

1. the Amnesty Applicant must provide a "full account" of "all facts known to the applicant. . . that are potentially relevant to the civil action;"
2. the Amnesty Applicant must "furnish[] all documents or other items" that are "potentially relevant to the civil action" that are in the applicant's or cooperating individual's possession or control "wherever they are located;" and
3. the Amnesty Applicant must use its "best efforts to secure and facilitate" from cooperating individuals covered by an agreement.⁵³

Thus, an Amnesty Applicant is required to uncloak the full nature, scope, extent and impact of the conspiracy to civil plaintiffs timely and fully in order to provide "satisfactory cooperation to the claimant with respect to the civil action."⁵⁴ This includes revealing the participants, dates, times, meetings, amounts, products, pricing, and communications in any forum, directly or indirectly, relating to the conspiracy. In fact, it was expected that this cooperation be so complete and

⁴⁵ *Id.* This actual damages limitation, however, is applicable only to conduct covered by the amnesty agreement. An Amnesty Applicant remains jointly and severally liable for treble damages for conduct outside its amnesty agreement (*e.g.*, for periods or commerce not covered by the amnesty agreement).

⁴⁶ ACPERA Section 213(a)-(b).

⁴⁷ See Cong. Rec. at S3615 (Apr. 2, 2004). See also Cong. Rec. H3657 (June 2, 2004) ("while a cooperating party would be liable only damages attributable to that party's conduct, noncooperating conspirators will remain jointly and severally liable for treble damages") and Cong. Rec. H3659 (June 2, 2004) (only "the remaining [noncooperating] conspirators remain jointly and severally liable to treble damages").

⁴⁸ See ACPERA Section 214(3).

⁴⁹ See Cong. Rec. at S3614 (Apr. 2, 2004).

⁵⁰ See Cong. Rec. at H3658 (June 2, 2004). See also Cong. Rec. at S3615 (Apr. 2, 2004) ("and while a party that receives leniency would only be liable for the portion of the damages actually caused by its own actions, the rest of the non-cooperating co-conspirators would remain jointly and severally liable for the entire amount of damages, which would then be trebled, to ensure that no injured party will fail to enjoy financial redress.")

⁵¹ *Id.*

⁵² See Cong. Rec. at H3657 (June 2, 2004).

⁵³ See ACPERA Section 213(b)(1)-(3).

⁵⁴ See ACPERA Section 213(b).

useful⁵⁵ to civil plaintiffs in their litigation “...that the total compensation to victims of antitrust conspiracies will be increased because of the requirement that Amnesty Applicants cooperate.”⁵⁶

An individual Amnesty Applicant (*e.g.*, a corporate executive with amnesty protection) is similarly subject to ACPERA’s cooperation requirements by (i) “making himself or herself available for such interviews, depositions, or testimony in connection with the civil action as the claimant may reasonably require;” and (ii) by “responding completely and truthfully, without making any attempt either falsely to protect or falsely to implicate any person or entity, and without intentionally withholding any potentially relevant information, to all⁵⁷ questions asked by the claimant in interviews, depositions, trials, or any other court proceedings in connection with the civil action.”⁵⁸

Not surprisingly, Amnesty Applicants and civil plaintiffs may interpret ACPERA’s cooperation requirements differently. And given the statute’s relatively recent passage, the precise contours of the cooperation required by ACPERA still need to be defined by the courts. To date, only one court—the district court in the *Sulfuric Acid Antitrust Litigation*—has entered an order finding satisfactory cooperation and a limitation of damages pursuant to ACPERA, and did so with no supporting explanation.⁵⁹

3. ACPERA’s Requirement Of Judicial Determination Of Satisfactory Cooperation

In order to qualify for single damages, an Amnesty Applicant must seek certification from the court that its cooperation to civil plaintiffs has been satisfactory. “The court in which the civil action is brought is empowered to determine whether the necessary cooperation has occurred.”⁶⁰ Such a determination occurs “after considering any appropriate pleadings from the claimant.”⁶¹ Thus, the full scope of the cooperation required by ACPERA will ultimately be defined by the courts, after being informed by the claimants about the sufficiency of cooperation,⁶² at the conclusion of litigation – by settlement, trial and appeal.⁶³

4. ACPERA’s Expiration

By the statute’s own terms, Sections 211-14 of ACPERA shall cease to have effect five years from the date of its enactment, June 22, 2004.⁶⁴ The statute does provide an exception that protects Amnesty Applicants whose case is still pending upon ACPERA’s expiration: “[w]ith respect to an applicant who has entered into an antitrust leniency agreement on or before the date on which the provisions of sections 211 through 214 of this subtitle shall cease to have effect, the provisions of sections 211 through 214 of this subtitle shall continue in effect.”⁶⁵ Only Section 215 of ACPERA, which increased the maximums in criminal fines and penalties for antitrust violations, will be effective past June 2009.

55 ACPERA cooperation makes civil litigation much more efficient because it defines the contours of the cartel, rather than requiring deductions from discovery about cartels that “operate in secret, and [whose] members usually do not co-operate with investigations of their conduct.” See Organisation for Economic Co-operation and Development, Global Forum on Competition, “Prosecuting Cartels Without Direct Evidence of Agreement”, Sept. 11, 2006 at 18. Cartel “participants understand their conduct is unlawful, and that their customers would object to the conduct if they knew about it, and so they take pains to conceal it.” *Id.* at 20. They use “extreme measures to conceal the existence of a cartel, including everything from creating bogus trade associations, the use of code names, and sophisticated ruses to keep general counsel in the dark, to hiding incriminating evidence in the attic of a cartel member’s grandparent’s home, wholesale document destruction and witness tampering after an investigation begins.” Beating Cartels, *supra* note 4, at 6. Early ACPERA cooperation with civil plaintiffs can even indirectly benefit the remaining co-cartelists, relieving them from defending against an overly broad complaint.

56 See Cong. Rec. at S3614 (Apr. 2, 2004).

57 Civil plaintiffs who find themselves faced with recalcitrant Amnesty Applicants may want to consider naming individuals cooperating with DOJ as defendants. ACPERA’s testimony requirements appear to be more stringent for cooperating individuals than for corporations.

58 ACPERA Section 213(b)(3)(A)(i)-(ii).

59 Minute Order (July 7, 2005) *In re Sulfuric Acid Antitrust Litig.*, No. 03 C 4576 (N.D. Ill. July 7, 2005). See I ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS 758 (6th ed. 2007).

60 See Cong. Rec. at H3658 (“The power of the court is the same whether the court is a state or federal court and whether the antitrust claims have been brought under state or federal laws”).

61 ACPERA Section 213(b).

62 *Id.* (court will determine whether the Amnesty Defendant “has provided satisfactory cooperation to the claimant with respect to the civil action”).

63 See discussion at page 107, *infra*.

64 *Id.* at Section 211(a).

65 *Id.* at Section 211(b).

III. ACPERA COOPERATION: TO WHOM?

A threshold question about the Amnesty Applicant's duty to cooperate under ACPERA is: to whom does that duty extend?

The statute answers this question to some degree, stating that a corporate Amnesty Applicant must provide a full account of all potentially relevant facts of which it knows to the "claimant" and furnish all potentially relevant documents "to the civil action."⁶⁶ Cooperating individuals must also make themselves available for interviews, deposition or testimony to the "claimant."⁶⁷ "Claimant" is statutorily defined as "a person or class" that has brought an action under the Sherman Act or any similar state law (except for a state or its sub-divisions).⁶⁸ The Congressional history refers to cooperation being provided to "any subsequent private plaintiffs bringing a civil suit based on the covered criminal conduct."⁶⁹ Commentators have routinely viewed the statute's protections as applying to private plaintiffs generally who file such civil suits.

The Act itself raises several fundamental definitional issues, however.

Does the "claimant" include those who opt out of a class and pursue a separate action? No court has addressed the topic, but the statutory definition would seem to encompass such opt-out plaintiffs ("opt-out"), even if the opt-out does not identify itself until after proceedings have commenced. What if the civil actions are brought by classes of direct purchasers under federal law and indirect purchasers under state law? Again, although no court has addressed the topic, the statutory definition on its face seems to encompass suits raising state law claims as well.⁷⁰

Both of these definitional issues have practical management considerations. Does the Amnesty Applicant have to provide separate cooperation, for example, to a class of federal claimants, state claimants and multiple individual opt-outs? If one set of claims is filed significantly later than the other, does the obligation of cooperation require duplicate efforts on the part of the Applicant or does the court (or the parties) have the authority to fashion an approach which controls, consolidates and coordinates such cooperation? Such a coordinated approach would seem sensible, particularly if it did not operate to prejudice any of the claimants to whom the obligation is owed.

Another issue arises with respect to the meaning of the civil liability exposure only to "that portion of the actual damages sustained by such claimant that is attributable to the commerce done by the applicant in the good or services affected by the violation."⁷¹ Does this mean the duty of cooperation extends only to plaintiffs or class members who did business with or made purchases from the Amnesty Applicant? Again, the broad definition of "claimant" provided by ACPERA, as well as the inability to sever the effect of one member of a cartel on the entire market, militates against such a narrow construction.⁷² Certainly, no such distinctions were drawn by the Amnesty Applicants in cases such as *Sulfuric Acid* or *Air Cargo*. The better approach, and that supported by the limited case law to date, is that the Amnesty Applicant's cooperation inures to the benefit of all plaintiffs and all members of any class, all of whom have a collective and indivisible interest in receiving the benefits of such cooperation.⁷³

66 *Id.* at Section 213(a)(1)-(2).

67 *Id.* at Section 213(a)(3)(A)(i).

68 *Id.* at Section 212 (4).

69 Cong. Rec. at S3614 (Apr. 2, 2004).

70 *In re Air Cargo Shipping Servs. Antitrust Litig.*, No. 06-MD-1775(J6)(VVP) (E.D.N.Y. June 27, 2006). [hereinafter *Air Cargo*] the Amnesty Applicant has provided cooperation to both direct and indirect purchaser classes. The legislative history also refers to cooperation in state law actions. Cong. Rec. at H3658 (June 2, 2004).

71 ACPERA, Section 213 (a). The duty of cooperation differs substantively from the issue of whether the cooperation from the Applicant can be limited to its purchases. See footnote 44, *supra*.

72 See *Dolphin Tours, Inc. v. Pacifico Creative Servs., Inc.*, 773 F.2d 1506, 1511 (9th Cir.1985) ("Defendants whose illegal conduct operates to exclude others from the relevant market, should not benefit because their wrongdoing makes it more difficult for the plaintiff to establish the precise amount of its injury."); *In re Aluminum Phosphide*, 893 F.Supp. at 1499 ("[C]ausation of injury may be found as a matter of just and reasonable inference from proof of defendants' wrongful acts and their tendency to injure plaintiffs, and from evidence of change in prices not shown to be attributable to other causes."); *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 114 n. 9 (1969) ("It is enough that the illegality is shown to be a material cause of the injury; a plaintiff need not exhaust all possible alternative sources of injury in fulfilling his burden of proving compensable injury under § 4.")

73 Of course, the fact that an Amnesty Applicant owes a duty of cooperation to all claimants does not mean that it has an obligation to settle with all claimants. It may choose to litigate defenses to some claims while settling others.

Lastly, cooperation is owed to civil plaintiffs until the conclusion of their lawsuit, accomplished by settlement or trial. In the *Sulfuric Acid Litigation*, civil plaintiffs observed that prematurely joining in a defendant's motion to certify a finding of "satisfactory cooperation" under ACPERA may limit their ability to compel ACPERA cooperation after the court has entered an order certifying the cooperation as satisfactory.⁷⁴ Because ACPERA cooperation continues until completion of trial,⁷⁵ there should be no prior certification of satisfaction at least until the completion of the trial or until the last defendant has settled with civil plaintiffs and all settlements are final, including appeals.⁷⁶

IV. ACPERA COOPERATION: WHEN AND HOW MUCH?

Another critical question under ACPERA involves the timeliness and scope of the obligated cooperation.

One set of commentators has noted that "ACPERA contains little on operating mechanics and governing standards, leaving litigants uncertain about its application and impact on individual cases."⁷⁷

Two other commentators have noted:

Clearly, the supervising judge of the civil action has the key role in determining whether the amnesty candidate has qualified for the benefits of Section 213(a) of the Act, specifically de-trebling of damages and removal of joint and several liability; and the ultimate determination as to the effectiveness of Section 213(a) appears to depend on the court's willingness to undertake the role of arbitrating inevitable disputes over the extent of an applicant's "cooperation." Further, it appears that the civil litigation plaintiff ("claimant") has a role in determining whether the applicant has cooperated enough to be eligible for de-trebling and removal from joint and several liability. Additionally, to the extent a claimant desires to hold an additional defendant fully liable, the claimant may mendaciously oppose a finding of satisfactory cooperation. Obviously, the effectiveness of section 213 will depend on the results of actual cases.⁷⁸

Likewise, in *Air Cargo*, Judge Edward Infante, a retired judge, prepared a report in support of a motion for preliminary approval of an \$85 million settlement with Amnesty Applicant Lufthansa Airlines in which he opined that "ACPERA provides little guidance on the cooperation necessary to limit an Amnesty Applicant's liability under the statute," and noted that the settlement agreement with Lufthansa set forth "the scope of the parties' cooperation obligations with a level of definition that is absent from the ACPERA statute itself."⁷⁹ This is because ACPERA describes the tools through which cooperation is to be provided (interviews, depositions, documents, etc.) and the general obligation of such cooperation, but not its specific quantity, frequency or quality. Because the extent of cooperation needed for each antitrust case is necessarily case specific, the drafters of ACPERA wisely left such determinations about sufficiency to the trial court.

74 *In re Sulfuric Acid Antitrust Litig.*, 231 F.R.D. 320, 330 (N.D. Ill. 2005) ("[I]tigation who take one view of the facts and prevail are equitably estopped to assert the opposite later.") Thus, because they had already joined in defendant's motion to certify its ACPERA cooperation as satisfactory, civil plaintiffs were forestalled later from arguing that not producing a witness for deposition was a violation of ACPERA cooperation by the defendant. This is despite the fact that plaintiffs joined in the motion upon the condition of ongoing future cooperation. This forward-looking caveat provided them little protection, and cautious civil plaintiffs would be wise to only seek certification once the case concludes.

75 For instance, an Amnesty Applicant may have produced documents under ACPERA. Without proper authentication, however, the use of such documents may be severely limited at trial. Moreover, civil plaintiffs cannot anticipate what rebuttal witnesses may be necessary at trial. Delaying cooperation certification prevents civil plaintiffs to fully utilize an Amnesty Applicant's cooperation.

76 ACPERA expires by its own terms on June 22, 2009. As of May 28, 2009, no new legislation has been presented to replace it and the issue did not come up during the March 10, 2009 confirmation hearings for Christine Varney, President Barack Obama's nominee to be Assistant Attorney General for Antitrust. <http://web.omm.com/files/upload/ACPERA%20-%20Lasting%20Limits%20Or%20Fleeting%20Experiment.pdf>.

77 *Clery Gottlieb, Litigation & Arbitration Report*, at 10 (Sept. 2005), available at http://www.cgsh.com/files/tbl_s47Details%5CFileUpload265%5C504%5CCGSH_Cleary_Gottlieb_Litigation__Arbitration_Report_-_Sept._05.pdf (last visited March 24, 2008) [hereinafter CGSH Article].

78 Harrison & Bell, *supra* note 35, at 227, 230 (footnotes omitted). See also Michael Hausfeld, Steig Olson & Seth Gassman, *Antitrust Class Actions: Continued Vitality*, Antitrust Review of the Americas at 73 (2008) (available at http://www.globalcompetitionreview.com/ara/19_classactions.cfm) (last visited March 24, 2008). [hereinafter Hausfeld Article]; CGSH Article, *supra* note 76, at 14.

79 Declaration of Magistrate Judge Edward A. Infante (Ret.), at 9 (July 13, 2007) [hereinafter Infante Declaration], attached as Exhibit 1 to the Declaration of Andrea L. Hertzfeld (July 13, 2007) [hereinafter Hertzfeld Decl.], filed in *Air Cargo*, No. 06-MD-1775(J6)(VVP).

A. Timeliness of Cooperation

How timely should cooperation be under ACPERA?

An ACPERA Amnesty Applicant's cooperation must be provided in a "timely" fashion. The legislative history emphasizes the materiality of this element. Congressmen in both the House of Representatives and the Senate preconditioned single damages on the provision of such timely ACPERA cooperation to civil plaintiffs. On the Senate side, Senator Hatch stated that "[i]mportantly, the limitation on damages is *only* available to corporations... if they provide *adequate and timely cooperation* . . . to any subsequent private plaintiffs bringing a civil suit."⁸⁰ On the House side, Representative Scott stated that the DOJ "will *only* grant such leniency if the company provides *adequate and timely* cooperation to both the government and any subsequent private plaintiffs in civil suits."⁸¹ An Amnesty Applicant has an affirmative obligation under the Act to provide civil plaintiffs with full cooperation (as discussed below) early and continuously until their case is concluded (either through settlement(s) or trial).⁸²

However, there is no unanimity on the "triggering events" for the "timely" provision of ACPERA cooperation. For instance, the Act contains no requirement that the Applicant identify itself to the civil claimants. It would be consistent however with the letter and spirit of the Act for claimants to demand and the court to order that in those private antitrust matters which involve an Amnesty Applicant, the Applicant identify itself to the claimants and the court at the earliest practicable time if seeking ACPERA de-trebling of damages. In litigation involving multiple claims, such disclosure would be appropriate after the entry of a case management order and prior to scheduling the filing of a consolidated complaint. Congress clearly intended that an Amnesty Applicant seeking single damages protection owes civil plaintiffs its cooperation at the point in the case where it can be "adequate[ly] and timely"⁸³ used by civil plaintiffs. Cooperation in such circumstances, should be provided timely in order to help civil plaintiffs "prepare and pursue" their litigation. This should occur in time to assist civil plaintiffs survive motions to dismiss, file amended complaints, and inform their discovery requests, among other tasks. To hold otherwise would inequitably deprive civil plaintiffs of the intended benefits of cost and time savings of ACPERA cooperation, while permitting the cartelists to attempt to claim the savings of the single damage ceiling.

The obvious corollary of this principle is that cooperation under ACPERA should not necessarily be tied to settlement with civil plaintiffs. Often, the two do go hand in hand. But, as discussed below, that is not uniformly the case. The Amnesty Applicant has no right to insist that its timely cooperation under the statute be contingent upon execution of a successful settlement.

Yet there may be Amnesty Applicants who may not seek the civil damage protection afforded by the Act. In the *TFT-LCD Antitrust Litigation*, the class plaintiffs filed a motion to compel the Amnesty Applicant—believed to be Samsung Electronics Company, Ltd.—to identify itself as the Applicant and provide full cooperation recognized under ACPERA⁸⁴ during the pretrial phase of the litigation or forfeit its right to have its civil exposure limited to single damages. Samsung filed a response asserting that the motion was premature, saying it is the Amnesty Applicant who applies to the Court for a reduction of liability and the court should be asked to rule on such a request in light of the cooperation by the Amnesty Applicant over the course of the litigation as a whole and in light of the reasonableness of plaintiffs' demands.⁸⁵

⁸⁰ Cong. Rec. at S3614 (Apr. 2, 2004) (emphasis added).

⁸¹ Cong. Rec. at H3659 (June 2, 2004) (emphasis added). See also Remarks of Rep. Conyers, at Cong. Rec. at H3660 (June 2, 2004) (the DOJ "will *only* grant such leniency if the company provides *adequate and timely* cooperation to both the government and any subsequent private plaintiffs in civil suits") (emphasis added).

⁸² Most often, a DOJ or other governmental investigation is announced and subsequent private litigants have no way of knowing the identity of the Amnesty Applicant(s).

⁸³ Cong. Rec. at H3659 (June 4, 2004) (emphasis added).

⁸⁴ See "Direct Purchaser Plaintiffs' Notice of Motion And Motion To Compel The Amnesty Applicant Defendant To Comply With ACPERA Or Forfeit Any Right It May Have To Claim Reduced Civil Liability; Memorandum Of Points And Authorities In Support Thereof" (April 17, 2009), filed in *In re TFT-LCD (Flat Panel) Antitrust Litig.*, MDL No. 1826 (N.D. Cal.).

⁸⁵ See "Samsung Corporation's Memorandum of Points And Authorities In Opposition To Direct Purchaser Plaintiffs' Motion To Compel The Amnesty Applicant Defendant To Comply With ACPERA Or Forfeit Any Right It May Have To Claim Reduced Civil Liability" (May 1, 2009), filed in *In re TFT-LCD (Flat Panel) Antitrust Litig.*, MDL No. 1826 (N.D. Cal.).

Interestingly, the DOJ filed a submission in favor of Samsung's position.⁸⁶ It agreed that the plaintiffs' motion was premature because the decision to impose treble damages comes at the end of a case and because an Amnesty Applicant may not seek reduced civil damages in a private follow-on civil action. The DOJ also expressed the concern that compelled early disclosure of the identity of the Amnesty Applicant might impede the DOJ's enforcement efforts.

The district court denied the plaintiffs' motion.⁸⁷ The Court found no provision in the statute or any case law that would support the plaintiffs' position. It went on to state:

To the contrary, the language of ACPERA suggests that the Court's assessment of an applicant's cooperation occurs at the time of imposing judgment or otherwise determining liability and damages. Plaintiffs argue persuasively that the value of an applicant's cooperation diminishes with time, and they note that plaintiffs are about to embark on significant and costly discovery that, at least in part, could be obviated if the applicant cooperated with plaintiffs. While the Court is mindful of these concerns, and will certainly consider all of these factors if and when an amnesty applicant seeks to limit liability under ACPERA, the Court finds no authority under ACPERA to compel an amnesty applicant to identify itself and cooperate with plaintiffs.⁸⁸

While it is true that the text of the statute might give little guidance, the legislative history cited above, which the court did not discuss, does so. Nonetheless, the court did say it was sympathetic to plaintiffs' concerns and would weigh them in granting any reduction to single damages for the Amnesty Applicant.

The notion advanced in the briefing of this motion that an Amnesty Applicant might not seek reduction of civil liability under ACPERA seems far fetched. However, defense counsel have argued that such a scenario is possible. One defense counsel has remarked: "[t]he motion [by plaintiffs in TFT-LCDs] implies that an amnesty applicant...must acknowledge the violation and cooperate with plaintiffs immediately. That's not the real world....There are all sorts of reasons why an amnesty applicant might want to wait and see how things play out, and in particular to consider whether defending the case is less expensive than cooperating with civil plaintiffs."⁸⁹

Likewise, the argument that disclosure of the identity of the Amnesty Applicant might impede DOJ enforcement is a *non sequitur*. In 2007, the Bank of America promptly disclosed in press releases and SEC filings its amnesty application to the DOJ in connection with the government's investigation of bid-rigging in the municipal derivatives industry. Likewise, in 2009, Tecumseh Products Company disclosed in SEC filings its cooperation with the DOJ with respect to the latter's investigation into the worldwide hermetic compressors cartel. There has been no basis to conclude that these disclosures in any way impeded the government's investigations.

Indeed, the government's position in *LCDs* is at odds with the precepts underlying its own antitrust leniency program. With respect to Type B leniency—leniency sought even after the DOJ has received information about the illegal antitrust activity—the government requires that “‘[t]he corporation reports the wrongdoing with candor and completeness and provides full, continuing and complete cooperation that advances the Division in its investigation.’”⁹⁰ Why, if determined not to jeopardize an ongoing investigation, should the requirement be any less as to cooperation with civil plaintiffs under ACPERA?

86 See “United States’ Opposition to Direct Purchaser Plaintiffs’ Motion To Compel the Amnesty Applicant Defendant To Comply With ACPERA Or Forfeit Any Right It May Have To Claim Reduced Civil Liability” (May 1, 2009), filed in *In re TFT-LCD (Flat Panel) Antitrust Litig.*, MDL No. 1826 (N.D. Cal.).

87 “Order Denying Direct Purchaser Plaintiffs’ Motion To Compel Amnesty Application Defendant To Comply With ACPERA” (May 19, 2009), filed in *In re TFT-LCD (Flat Panel) Antitrust Litig.*, MDL No. 1826 (N.D. Cal.).

88 *Id.* at 3.

89 Evan Hill, “Samsung Cooperation: Now or Never?” *The Recorder* at p.1 (Apr. 22, 2009).

90 Scott D. Hammond & Belinda Barnett, “Frequently Asked Questions Regarding The Antitrust Division’s Leniency Program And Model Leniency Letters” (Nov. 18, 2008) available at <http://www.usdoj.gov/atr/public/criminal/239583.htm>.

Despite the obvious intention of ACPERA to extend a civil benefit as an element of a criminal immunity process, it is not axiomatic that every Amnesty Applicant may always seek that benefit. The Act was designed with the dual purpose of aiding both public enforcement and private restitution. Applicants should not be able to undermine this purpose by accepting the benefit of single damages but treating the obligation as an option which it can accept, reject or delay selecting at its discretion.

Specific consideration should be given to the timeliness of cooperation at different stages of litigation.

1. Cooperation and Settlement

Is cooperation dependent on settlement? Can an Applicant truly afford to cooperate before it finalizes its civil exposure even under its statutorily limited liability?

Amnesty Applicants negotiating a settlement face:

a chicken-and-egg problem. How can Amnesty Applicants cooperate with plaintiffs without the protection of a finalized settlement agreement in hand? But how can Amnesty Applicants achieve a settlement agreement based on the liability limitations of ACPERA until they first meet ACPERA's requirements by cooperating?

The seeming circularity will usually be resolved through the same give and take of many other civil antitrust settlement negotiations. Each side will signal its willingness to assent both to the cooperation and to the settlement agreement. For example, these same negotiations occur when cooperation is a part of a settlement agreement outside the ACPERA context: the defendant must assure plaintiffs that the cooperation will be sufficient, but the defendant will not want to fully disclose its cooperation until after the settlement agreement is signed, lest it prematurely give away its bargaining chip. In that same spirit, plaintiffs and Amnesty Applicants will likely be able to come to settlement agreements based on good faith negotiations, using the same mechanisms already present in settlement discussions.⁹¹

In the *Air Cargo* case, Lufthansa, the Amnesty Applicant, engaged in detailed and substantial cooperation⁹² with plaintiffs' counsel prior to the approval of any settlement agreement and prior to the onset of any discovery.⁹³ Thus, for example, the settlement agreement provided that documents given to investigating authorities had to be made available, and counsel had to provide descriptions of the conduct at issue, commencing ten business days after the execution of the agreement.⁹⁴ Likewise, in the *Hydrogen Peroxide Antitrust Litigation*,⁹⁵ the Amnesty Applicant, Degussa, provided substantial cooperation in order to assure its entitlement to single damage protection under the Act while simultaneously advancing its probabilities of settlement.

Both of these examples demonstrate that cooperation need not be coupled with nor conditioned on settlement.

2. Pre-Filing

Does "timely" mean once a civil suit is filed or even before? Or does it mean once a civil suit is filed and a leadership organization for the putative settlement class is selected? While

⁹¹ CGSH Article, *supra* note 76, at 14.

⁹² Cooperation under the Lufthansa agreement was provided 10 days after execution of the settlement agreement and over a year and a half prior to preliminary approval papers were entered by the court.

⁹³ Infante Declaration at 10.

⁹⁴ Hertzfeld Decl., Exh. 2 at Paragraphs 54(g), (j).

⁹⁵ *In re Hydrogen Peroxide Antitrust Litig.*, MDL No. 1682 (E.D. Pa., filed Feb. 11, 2005).

“timely” can certainly be defined differently by either the recipient or the provider of the cooperation, the legislative history sheds some light on its meaning. “[T]he legislation *requires* the Amnesty Applicant to provide *full cooperation* to the victims as they *prepare and pursue* their civil lawsuit.”⁹⁶ Senator Hatch’s use of the words “prepare and pursue” would seem to indicate that an Amnesty Applicant was obligated to cooperate early as the case is being prepared and continuously as the case is being litigated.⁹⁷ Two recent litigations provide practical illustrations of how and when timeliness may be triggered.

In a recently filed lawsuit involving bid rigging of municipal derivatives, Bank of America acknowledged that:⁹⁸

Plaintiffs and Defendant Bank of America have engaged in confidential discussions about some of the facts and circumstances detailed in this Complaint over the last eight months in the context of a settlement process, including a number of sessions overseen by the Honorable Daniel Weinstein (Ret.) of JAMS. Judge Weinstein is one of the nation’s preeminent mediators of complex civil disputes. These discussions have been conducted pursuant to, among other things, an agreement that requires full and timely cooperation by Defendant Bank of America, which has been received. The information contained in this Complaint comes in part from information obtained from Defendant Bank of America and in part from publicly-available information, including regulatory filings.⁹⁹

Even in this case, however, the cooperation that the Bank of America was able to provide was limited by what the DOJ allowed it to disclose, with the result that a consolidated amended complaint was dismissed with leave to replead, with the court saying that more defendants could be added back in, once the bank was able to provide discovery about their participation in the alleged conspiracy.¹⁰⁰

Similarly, after the filing of multiple suits, Lufthansa provided cooperation prior to the filing of a consolidated amended complaint. As noted earlier,¹⁰¹ this initial cooperation allowed “claimants” to assert their claims with greater specificity and clarity than they otherwise could have been able to do. It allowed the fashioning of a complaint that focused on the evidence for which Lufthansa received amnesty for its participation in a revealed conspiracy. In both of these instances, provision of early ACPERA cooperation accomplished one of ACPERA’s principal goals: to “reduce the cost for victims to recover the damages they suffer from criminal antitrust conspiracies.”¹⁰²

The timing of cooperation, even with a willing Applicant, can be effected by other factors unrelated to the actual parties to the civil litigation. Some cases have delayed ACPERA cooperation obligations due to stays sought by the DOJ or otherwise imposed by the presiding court.¹⁰³ Such delays may be inevitable due to the legitimate public enforcement needs.

⁹⁶ Cong. Rec. at §3614 (Apr. 2, 2004) (emphasis added).

⁹⁷ Statements on the floor by the committee member in charge of the bill [Senator Hatch; Representative Sensenbrenner] “are regarded as being in the nature of supplemental committee reports and are accorded the same weight as formal committee reports.” 2A SUTHERLAND ON STATUTORY CONSTRUCTION §48.14 at 220 (4th ed. 1973); Me. Pub. Utils. Comm’n v. FERC, 454 F.3d 278, 282 (D.C. Cir. 2006) (“the court applies the traditional tools of statutory interpretation in determining congressional intent, looking to the text, structure, purpose, and legislative history of a statute.”) *Disabled in Action of Metro. N.Y. v. Hammons*, 202 F.3d 110 (2d Cir. 2000) (noting the “sponsor/floor manager statement” as an “authoritative and reliable” source of legislative history); *See also Wis. Pub. Intervenor v. Mortier*, 501 U.S. 597, 611 n.4 (1991) (“[c]ommon sense suggests that inquiry benefits from reviewing additional information rather than from ignoring it”); *U.S. v. Am. Trucking Ass’n, Inc.*, 310 U.S. 534, 543-544 (1940) (“when aid to construction of the meaning of words, as used in the statute, is available, there certainly can be no ‘rule of law’ which forbids its use, however clear the words may appear on ‘superficial examination’” (footnote omitted)); *U.S. v. Fisher*, 2 Cranch 358, 386 (1805) (“where the mind labours to discover the design of the legislature, it seizes every thing from which aid can be derived”).

⁹⁸ It remains to be determined what percentage of members of the proposed class are actually owed ACPERA cooperation. See ACPERA, §212(4).

⁹⁹ Class Action Complaint at 2, *Fairfax County v. Bank of Am.*, No. 1:08-cv-0433 (D.D.C. March 12, 2008). *See In re Municipal Derivatives Antitrust Litigation*, 232 F.R.D. 184, 185-87 (S.D.N.Y. 2008) (court discussed benefits of obtaining cooperation with the Bank of America in deciding whom to appoint as interim class counsel). While Bank of America may not statutorily owe ACPERA cooperation to municipalities or states, it signed an agreement obligating itself to provide “ACPERA cooperation” to such municipalities and states.

¹⁰⁰ *See* “Decision And Order” (Apr. 30, 2009) in *In re Municipal Derivatives Antitrust Litig.*, MDL No. 1950 (S.D.N.Y.).

¹⁰¹ See note 82 and accompanying text, *supra*.

¹⁰² *See* An Overview of Recent Developments in the Antitrust Division’s Criminal Enforcement Program Scott Hammond, Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dept. of Justice, An Overview of Recent Developments in the Antitrust Division’s Criminal Enforcement Program (Jan. 10, 2005) (transcript available at <http://www.usdoj.gov/atr/public/speeches/207226.htm>).

¹⁰³ The recognition of legitimate governmental needs in private enforcement proceedings is examined *infra* at Section V.

However, if there is a showing that no prejudice results from a necessary coordination of public and private enforcement, completion of defined stages of public enforcement should not delay an earlier performance of cooperation to civil litigants.¹⁰⁴

3. Motion To Dismiss Prior to Commencement of Discovery

Ever since the Supreme Court's decision in *Twombly*, defendants in price fixing cartels have sought mechanical refuge in the decisions language of "plausibility." Seemingly without reflection, horizontal price fixing complaints are routinely met with motions to dismiss on the grounds of conspiratorial implausibility.¹⁰⁵ If the cartel includes an Amnesty Applicant, does ACPERA's obligation of cooperation require the Applicant to disclose the facts of the cartel as revealed to the DOJ so that the court is apprised of all information which must inform its decision on plausibility?

An Applicant's admission into the DOJ leniency program should alone be sufficient to establish that a similarly based complaint raises "enough fact to raise a reasonable expectation that discovery will reveal evidence of [a plausible] illegal agreement".

Unquestionably, an Applicant's obligation to provide must be triggered by the filing of a "*Twombly* motion." If not offered prior to such a filing, the Applicant should be required to provide the factual "context that raises a suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action" to civil plaintiffs to include in their response.¹⁰⁶ Such cooperation would remove most ambiguity that the challenged conspiracy was just as "much in line with a wide swath of rational and competitive business strategy unilaterally prompted by common perceptions of the market" would be the genesis of an expensive and protracted antitrust case.¹⁰⁷ In fact, in light of an amnesty application to the DOJ and its explicit and implicit admissions,¹⁰⁸ the Supreme Court's concerns that an "implausible" conspiracy claim could involve the judicial system and the defendants in an unjustifiably expensive and protracted antitrust litigation evaporates.¹⁰⁹ The existence of an Amnesty Applicant in a criminal investigation as to the same conspiracy alleged in civil proceedings should mandate the denial of the vast majority of *Twombly* motions.¹¹⁰

4. Class Certification

What cooperation obligations are owed by an Amnesty Applicant at the time of class certification?

The reality of routine class treatment of antitrust claims is specifically anticipated by the terms of ACPERA. First, the definition of a claimant under the act, to whom the duty of cooperation is owed, explicitly includes a "class," on "whose behalf [a civil action] has been brought."¹¹¹ Thus, the duty of cooperation, described in Section 213(b) as being owed to the "claimant," is, by its terms, extended to class members and the specifics of their civil action. Second, the satisfactory nature of cooperation, "with respect to the civil action" as a whole. Therefore, a duty of cooperation must be triggered by the time of class certification and in fact, is owed to the class of victims it injured.

104 An ACPERA Amnesty Applicant's answer to the complaint that denies facts that are the foundation of its leniency agreement represents a failure to provide a "full account" of all "potentially relevant facts" required by ACPERA. Certainly, such denials could be later submitted to the court as evidence of lack of cooperation with civil plaintiffs under Section 213(b), endangering single damages protection. Thus, an answer to a civil complaint would clearly appear to be a triggering event for the commencement of ACPERA cooperation.

105 Indeed, in an opinion issued just two weeks after *Twombly*, *Erickson v. Pardus*, 127 S. Ct. 2197 (2007), the Court, citing *Twombly*, reaffirmed "the liberal pleading standards set forth by Rule 8(a)(2)" and held that "[s]pecific facts are not necessary" at the pleading stage. See *Erickson v. Pardus*, 127 S. Ct. 2197, 2200 (2007) (holding "[s]pecific facts are not necessary" at the pleading stage, and citing *Twombly*). *Accord Twombly*, 127 S. Ct. at 1973 n.14 ("Here, our concern is not that the allegations in the complaint were insufficiently 'particular[ized]'; rather, the complaint warranted dismissal because it failed *in toto* to render plaintiffs' entitlement to relief plausible.") (internal citation omitted); *Arista Records, LLC v. Does 1-27*, 2008 U.S. Dist. LEXIS 6241 (D. Me. Jan. 25, 2008) (Kravchuk, M.J.) ("Nothing in *Twombly* forbids lower courts from drawing inferences or accepting conclusory recitations as true for purposes of a motion to dismiss so long as the factual content that is supplied in the complaint demonstrates the plausibility of any necessary inferences").

106 *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 127 S.Ct. 1955, 1966 (2007).

107 *Id.* at 1964.

108 See fn. 17.

109 *Rossi v. Standard Roofing, Inc.*, 156 F.3d 452, 466 (3d Cir.1998) (quoting *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1986)).

110 See *In re Vitamins Antitrust Litig.*, No. 99-197 (TFH) 2000 U.S. Dist. LEXIS 7397, at *77 (D.D.C. 2000) (denying defendants' motion to sever based on the terms of their negotiated criminal pleas because "criminal guilty please do not establish boundaries for this civil litigation").

111 ACPERA, Section 212(4).

B. Breadth & Adequacy of Cooperation

1. Breadth of cooperation.

How extensive is the obligation of cooperation under the Act?

Both the language of ACPERA and its legislative history emphasize that Congress anticipated that Amnesty Applicants must provide civil plaintiffs with cooperation that extends beyond that required under the current federal discovery rules.

First, ACPERA requires that an Amnesty Applicant provide comprehensive and fulsome facts and documents to civil plaintiffs regarding its conduct: a “full account” of “all facts” is required as well as the production of “all documents” that are “potentially relevant to the civil action.”¹¹² Congress did not limit the provision of such facts or documents to a subset of information or topics.¹¹³

Despite explicit language to the contrary, some defense counsel nonetheless attempt to limit or restrict ACPERA cooperation to “merits,” or “just what was proffered to the DOJ,” or “all non-jurisdictional facts,” or “only the facts contained within the leniency agreement.” However, the text of ACPERA is clear regarding the intended breadth of cooperation: an ACPERA Amnesty Applicant must disclose “all facts” and “all documents” that are “potentially relevant to the civil action.”¹¹⁴

Second, ACPERA focuses on “potentially relevant” facts and documents needed to be provided to civil plaintiffs.¹¹⁵ The inclusion of the modifier “potentially” creates a discovery requirement *broader* both in scope and in reach than that allowed by the Federal Rules of Civil Procedure, which reaches only “relevant” documents. The Committee Report explicitly states that ACPERA’s “use of the term ‘potentially relevant’ is intended to preclude a parsimonious view of the facts or documents to which a claimant is entitled.”¹¹⁶ Indeed, this comports with recent interpretations generally of discovery obligations in antitrust cases.^{117, 118}

Third, ACPERA requires that a corporate Amnesty Applicant use its “best efforts” to secure testimony of individuals “covered by the [leniency] agreement.”¹¹⁹ Although no court has as yet defined this provision, its language imposes a higher degree of cooperation than mere “reasonable

112 ACPERA Section 213(b)(1)-(2).

113 Occasionally, an Amnesty Applicant seeks to limit its cooperation under ACPERA by contending that a portion of its conduct was immunized or beyond the jurisdictional reach of U.S. courts. The propriety of such an attempted limitation has not yet been litigated.

114 *Id.*

115 *Id.*

116 See Cong. Rec. H3658 (June 2, 2004).

117 Courts presiding over antitrust cases generally take a liberal view of relevance in determining the scope of discovery. See *New Park Entertainment, LLC v. Elec. Factory Concerns, Inc.*, No. Civ. A. 98-775, 2000 WL 62315, at *3 (E.D.Pa. Jan. 13, 2000) (internal quotations omitted) *Accord In re Potash Antitrust Litig.*, No. 3-93-197, 1994 WL 1108312, at *14 n.20 (D.Minn. Dec. 5, 1994) (“[t]he Courts have traditionally allowed liberal discovery, particularly when there are allegations of conspiracy and where ‘broad discovery may be needed to uncover evidence of invidious design, pattern or intent.’”)

118 The DOJ has recognized that “[i]nternational borders can not serve as barriers to our ability to investigate. There can be no safe harbors from which cartel members can operate.” *Beating Cartels*, *supra* note 4, at 2. The Deputy Assistant Attorney General of Criminal Enforcement was even more specific when he stated: “[w]e must gain access to subjects, evidence and witnesses that are located outside our borders.” *Id.* “The fact that the United States is the relevant market in this case does not necessarily limit discovery to the United States...A general policy of allowing liberal discovery in antitrust cases” has been observed by this Court because “broad discovery may be needed to uncover evidence of invidious design, pattern, or intent.” (*U.S. v. Dentsply Int'l, Inc.*, No. Civ. A-99-5 MMS, 2000 WL 654286, at *5 (D. Del. May 10, 2000)). For this reason, the scope of document production in antitrust litigation is often quite expensive. See *In re Automotive Refinishing Paint Antitrust Litig.*, 229 F.R.D. 482, 494-96 (E.D. Pa. 2005) (subpoena allowed against Belgian trade association); *In re Plastics Additives Antitrust Litig.*, No. 03-2038, 2004 WL 2743591 at *13-14 (E.D. Pa. Nov. 29, 2004) (court allowed discovery of materials produced to foreign antitrust regulatory bodies); *In re Vitamins Antitrust Litig.*, 2000 U.S. Dist. LEXIS 7397 (D.D.C. 2000) (court considered the context of specific discovery requests in order to determine if jurisdictional discovery against foreign defendants proceeded under the Federal Rules of Civil Procedure, rather than the Hague Convention); *In re Vitamins Antitrust Litig.*, No. 99-197 TFH, 2001 WL 1049433, at *11-12 (D.D.C. June 20, 2001) (refusing to place geographic limitation on merits-based discovery in global price-fixing case because acts or communications outside the United States may be admissible to establish existence of conspiracy); *In re Fine Paper Antitrust Litig.*, 685 F.2d 810, 818 (3d Cir. 1982) (no abuse of discretion where trial court permitted taking of 270 depositions and production of nearly two million documents in complex, nationwide antitrust claim); *In re Brand Name Prescription Drugs Antitrust Litig.*, 123 F.3d 599, 614 (7th Cir. 1997) (pretrial discovery involved more than 1,000 depositions and over fifty million pages of documents); *In re Linerboard Antitrust Litig.*, 296 F.Supp.2d 568, 577 (E.D. Pa. 2003) (pretrial discovery required production of millions of pages of documents).

119 ACPERA Sections 213(b)(3)(B).

efforts.”¹²⁰ The best efforts called for in the context of ACPERA could reasonably include making every available effort to ensure that an Amnesty Applicant’s employees and officers provide cooperation to private plaintiffs.¹²¹ A cooperating Amnesty Applicant may, for example, be required to pay for individuals’ counsel or otherwise pay expenses of those individuals cooperating with civil plaintiffs if such payment would encourage their cooperation. If these individuals choose not to cooperate (either because they are retired, based abroad, or they take the Fifth Amendment), such non-participation should be weighed by the court in determining whether they have provided satisfactory cooperation to civil plaintiffs.

This is not a radical or unfair position. With regard to a corporation’s entry into the DOJ’s leniency program, for example, “the number and significance of the individuals who fail to cooperate, and the steps taken by the company to secure their cooperation, are relevant in the Division’s determination as to whether the corporation’s cooperation is truly ‘full, continuing and complete.’”¹²² Similarly, the number and significance of individuals who fail to cooperate should also be relevant to the court’s evaluation of an ACPERA Amnesty Applicant’s cooperation with civil plaintiffs.¹²³ If however, such a failure results despite the actual best efforts of the Amnesty Applicant, the failure of the individual cannot and should not be attributed to the corporation. Practical solutions are available to distinguish the consequences of such a situation and should provide for the corporate retention of Amnesty benefits while removing those benefits only as to the truly recalcitrant individual.¹²⁴

2. Substantial Nature of Cooperation

How material must the Amnesty Applicant’s cooperation be under ACPERA?

The cooperation owed by an Amnesty Applicant was designed to be “substantial.”¹²⁵ The quality of cooperative information was the price for protection from joint and several treble damages, which often constitutes hundreds of millions of dollars. Under ACPERA, “to qualify for amnesty, a party must provide substantial cooperation . . . in any civil case brought by private parties that is based on the same unlawful conduct.”¹²⁶ The enormous savings provided by detrebbling dwarfs any associated costs of providing cooperation by an Amnesty Defendant. Indeed, the legal expenses and costs to the corporation associated with providing such substantial cooperation, even if required through trial, would rarely approach a defendant’s damage exposure for joint and several treble damages.

At a minimum, such cooperation to civil plaintiffs would appear to include: (a) a detailed account of all known facts¹²⁷ relevant to the litigation through interviews with current and former

120 Unfortunately, it seems probable that courts will also have to grapple with the meaning of “best efforts.” Some counsel seem to think that merely extending the request to cooperate with civil plaintiffs – and no more – to former employees will satisfy this obligation. Cursory review of analogous case law shows that the standard for “best efforts” will not be that lightly interpreted. See, e.g., E. Allan Farnsworth, *On Trying to Keep One’s Promises: The Duty of Best Efforts In Contract Law*, 46 U. Pitt. L. Rev. 1, 8 (1984) (“courts sometimes confuse the standard of best efforts with that of good faith Good faith is a standard that has honesty and fairness at its core and that is imposed on every party to a contract. Best efforts is a standard that has diligence as its essence and is imposed only on those contracting parties that have undertaken such performance. The two standards are distinct and that of best efforts is the more exacting”).

121 *EEOC v. R.J. Gallagher Co.*, 181 F.3d 645, 652 (5th Cir.1999) (employment case; “Best efforts” means “such efforts as are reasonable in the light of that party’s ability and the means at its disposal and of the other party’s justifiable expectations”).

122 See *Making an Offer*, *supra* note 31, at 4.

123 Other international antitrust enforcement authorities have adopted similar approaches with respect to an Amnesty Applicant’s duty to cooperate with investigating authorities. Under the EC’s 2006 Notice on Immunity from Fines and Reductions of Fines in Cartel Cases (which replaced earlier policies from 1996 and 2002), the undertaking seeking leniency must cooperate “genuinely, fully and on a continuous basis”; the EC spells out the requirements of such full cooperation in great detail. See Europa Press Release, Commission Notice on Immunity from Fines and Reduction of Fines in Cartel Cases, 2006/C 298/11, 2006 O.J. (C298) 17, Paragraphs 9, 12 (available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2006:298:0017:0022:EN:PDF>). The U.K.’s Office of Fair Trading issued a leniency policy in 2000 OFT’s Guidance As to the Appropriate Amount of a Penalty, Office of Fair Trading (2004) (available at http://www.of.gov.uk/shared_of/business_leaflets/ca98_guidelines/of423.pdf) (last visited March 24, 2008), which it updated in 2005 and 2006 with a guidance note Leniency and No-Action, Office of Fair Trading (2006) (available at http://www.of.gov.uk/shared_of/reports/comp_policy/of803a.pdf) (last visited March 24, 2008). The latter refers to the applicant’s “continuous and complete duty of cooperation.”

124 For example, in the *Hydrogen Peroxide* litigation, counsel anticipated recalcitrant former employees and drafted the settlement agreement accordingly. Thus, individuals (whose right to assert the Fifth Amendment was preserved in the settlement agreement) were only able to “obtain the benefits of the Release contained in this Agreement if they cooperate with Plaintiffs....”

125 Cong. Rec., at S3615 (Apr. 2, 2004).

126 *Id.*

127 For a price-fixing case, such facts should at least include: a description of the specific product that was fixed, including the dynamics of the market for it; specific mechanism of how the prices were fixed, including frequency; the identity of the primary actors that effectuated the price fix, including those of its co-cartelists; the dates, times and methods of communication between the co-cartelists; the effect of the price fix; the time period of the price fix; and the geographical scope of the price fix.

employees;¹²⁸ and outside counsel; (b) production of all potentially relevant documents and data; (c) production and explanation of transactional data; (d) industry and merits witnesses for deposition; (e) discovery responses (*e.g.*, interrogatories or requests to admit);¹²⁹ (f) agreement to provide factual proffers as often as is reasonable and necessary to support plaintiffs' prosecution of the action;¹³⁰ (g) provision of means to authenticate an Amnesty Applicant's documents if needed at trial (via stipulation or testimony); and (h) access to and provision of witnesses if needed for trial.

ACPERA's substantial civil damage limitation must be achieved the "old fashioned way," by earning it.

3. Case Studies of Cooperation

The obligation of an Amnesty Applicant to cooperate under ACPERA has had differing results.

In *Sulfuric Acid*, the two Amnesty Applicants: (a) provided plaintiffs "with a detailed account of all known facts relevant to the litigation" through interviews with current employees, former employees and outside counsel; (b) furnished plaintiffs with 35,000 pages of documents; (c) furnished plaintiffs with interrogatory responses; (d) provided plaintiffs with "numerous documents and information" regarding the DOJ's investigation of the sulfuric acid industry; and (e) "used their best efforts to locate witnesses with knowledge of the factual underpinnings of this litigation."¹³¹ This cooperation commenced shortly after the defendants were named as parties.

Similarly, in *Air Cargo*, Lufthansa provided attorney proffers in advance of submission of any settlement for court approval. The settlement agreement required it to, *inter alia*: (a) provide current and former officers, directors and employees knowledgeable about the DOJ investigation into the airline industry and/or having knowledge of relevant facts for interviews, conferences, testimony, document authentication and declarations; (b) production of transactional and substantive documents, including documents produced to the DOJ; and (c) provide proffers relating to the conduct at issue and eventually to meet as often as is reasonable and necessary to support plaintiffs' prosecution of the actions.¹³² As Judge Infante noted in *Air Cargo*, "[c]lass members have already received some of the benefit of the information provided by Lufthansa. This is clearly reflected in the recently-filed First Amended Consolidated Complaint, which substantially expands on the inner workings of the antitrust law violations at issue. As a further result of the information provided by Lufthansa, new parties were added and unnecessary defendants were removed."¹³³

And in *Hydrogen Peroxide*, Degussa, the Amnesty Applicant met with plaintiffs' counsel prior to class certification, made multiple evidentiary proffers, and provided documents and interviews that were quite valuable in shaping the claims in the case.¹³⁴

There are contrary experiences, however. In the *Urethanes Antitrust Litigation*,¹³⁵ for example, defendant Chemtura Corporation unilaterally decided that its obligation of cooperation could be satisfied by: (a) providing a full account of the alleged conspiracy at the commencement of merits discovery, (b) producing documents given to the DOJ at the commencement of class certification discovery; and (c) making some effort to procure the cooperation of two former

128 Under ACPERA, an Amnesty Applicant is obligated to use its "best efforts to secure and facilitate" cooperation from individuals covered by the leniency agreement. ACPERA, Section 213(b)(3)(B).

129 See Cong. Rec. H3658 (June 2, 2004) ("[r]ecognizing that there are discovery tools that plaintiffs can use in discovery of entities, this section is intended to require cooperation of entities in such discovery").

130 ACPERA, Section 213(b)(1) (ACPERA requires "a full account to the claimant of all facts known to the applicant . . . that are potentially relevant to the civil action").

131 Marsulex Brief, p. 6.

132 Infante Declaration, *supra* note 78, at 5-6.

133 Infante Declaration, *supra* note 78, at 9.

134 Memorandum of Law in Support of Direct Purchaser Class Plaintiffs' Unopposed Motion for Final Approval of Proposed Settlement with Degussa Corp., *In re Hydrogen Peroxide Antitrust Litig.*, No. 05-666 (E.D. Pa. Nov. 2, 2007).

135 *In re Urethanes Antitrust Litig.*, MDL No. 1616, 2008 WL 696244 (D. Kan March 13, 2008).

employees. In mid-litigation, it sought a judicial determination that it had satisfied its ACPERA obligations even though the cooperation contemplated by the statute is an ongoing one that spans the entirety of the follow-on civil litigation.¹³⁶

In the *Publication Paper Antitrust Litigation*,¹³⁷ the Amnesty Applicant, UPM-Kymmere Corporation, delayed its cooperation substantially, asserting that it did not want to do anything that would cause it to run afoul of EC authorities, who were conducting a parallel investigation. A similar issue arose in the *Automotive Paint Refinishing Antitrust Litigation*,¹³⁸ when the Amnesty Applicant took the position that it would provide no cooperation under ACPERA until a parallel EC investigation was closed and any appeals were exhausted.¹³⁹

Finally, in matters involving global cartels, foreign investigations may impede domestic statutory obligations. Cooperation with private plaintiffs required under ACPERA is sometimes delayed based on the excuse of a parallel EC investigation.¹⁴⁰ The EC's involvement in U.S. private antitrust actions contradicts U.S. policy with respect to Amnesty Applicants. It appears that the EC is using the threat of revocation of amnesty if the Amnesty Applicant for example, discloses the EC's statement of objections to a cartel.¹⁴¹ The basis for the EC's authority to do so is unclear, since the policy reason behind protecting the investigatory process is to keep confidential that information that is not known to the other accused cartelists. The EC's Statement of Objections, however, is routinely made available to every named company. Arguably, there is a denial of due process to the civil plaintiffs who are precluded from obtaining that information while the defendants, including the Amnesty Applicant, are in possession of it.¹⁴²

V. ACPERA'S INTERSECTION WITH CIVIL AND CRIMINAL PROCEEDINGS

Delayed cooperation resulting from the pendency of public enforcement proceedings raises concerns about the integration of public and private antitrust enforcement.

A. DOJ Investigations

Compliance with the requirements of ACPERA may intersect with an Amnesty Applicant's obligations to the DOJ. For example, if the DOJ begins an investigation, when should an Amnesty Applicant begin cooperation with civil plaintiffs? What happens to cooperation under ACPERA if the government investigation leads to no prosecution? Courts, litigants, and the DOJ are still mapping out what to do in these circumstances. While civil plaintiffs have a right to cooperation as soon as possible, the DOJ may legitimately need to delay the start of such cooperation in order to protect its ongoing investigation.

Anticipating this intersection, Section 214(1) of ACPERA holds that nothing in ACPERA shall be construed to "affect the rights of the Antitrust Division to seek a stay or protective order in a civil action based on conduct covered by an antitrust leniency agreement to prevent the cooperation described in section 213(b) from impairing or impeding the investigation or prosecution by the Antitrust Division of conduct covered by the agreement."

¹³⁶ See Motion for Leave to File Under Seal Chemtura's Motion For a Finding of 'Satisfactory Cooperation' And Limitation of Damages Pursuant To The Antitrust Criminal Penalty Enhancement and Reform Act of 2004 (June 20, 2007); *In re Urethanes Antitrust Litig.*, 2008 WL 696244, No. 04-1616-JWL (D. Kan. March 13, 2008). The motion was not ruled on because Chemtura soon settled.

¹³⁷ *In re Publ'n Paper Antitrust Litig.*, 346 F. Supp. 2d 1370 (D. Conn. 2004).

¹³⁸ *Automotive Paint*, 229 F.R.D. 482.

¹³⁹ Foreign blocking statutes can also potentially impose an obstacle. See, e.g., *Westinghouse Elec. Corp. v. Rio Algom, Ltd.*, 480 F.Supp. 1138, 1148 (N.D. Ill. 1979).

¹⁴⁰ In a Notice of Correspondence from the European Commission (Dec. 11, 2006), filed *In re Methyl Methacrylate (MMA) Antitrust Litig.*, No. 06-md-1768 (E.D. Pa.), the Director of Anti-Cartel Enforcement at the EC's Directorate General for Competition took the positions that admissions of cartel activity to the EC should not be used to seek damages in other allegedly unaffected jurisdictions.

¹⁴¹ The statement of objections is a statement that is distributed to all potential targets of the investigation so that each accused cartel list knows that information proffered by the EC.

¹⁴² See generally *Schad v. Ariz.*, 501 U.S. 624, 637 (1991) (the concept of due process demands fundamental fairness and rationality that is an essential component of that fairness); *Quill Corp. v. N.D. Bay and Through Heitkamp*, 504 U.S. 298, 312 (1992) ("[d]ue process centrally concerns the fundamental fairness of governmental activity").

Courts have taken differing approaches on this issue, as reflected in several recent decisions from the federal district court in the Northern District of California. In the *SRAM Antitrust Litigation*, the court ordered immediate production of documents produced to the federal grand jury in the ongoing parallel criminal investigation.¹⁴³ In the *DRAM Antitrust Litigation*, the court, in response to the DOJ's request (and prior to ACPERA), stayed depositions on the merits, but allowed production of grand jury documents.¹⁴⁴ In the *TFT-LCD Antitrust Litigation*, however, the court, again at the DOJ's request, stayed all merits discovery, including documentary discovery.¹⁴⁵ Other cases have taken a similar approach.¹⁴⁶

However, civil plaintiffs could propose a hybrid cooperation – a form of cooperation less than required under ACPERA but more than would be permitted under a stay – until the DOJ concludes its investigation or prosecution, and then seek full ACPERA cooperation only after that juncture. Possible aspects of such a compromise could include: (a) proffers by and interviews of an Amnesty Applicant, which the DOJ would not oppose; (b) production of materials produced by the Amnesty Applicant to the DOJ under a suitable confidentiality agreement; (c) no stay of discovery being sought by the DOJ that would encompass matters relating to personal jurisdiction or maintenance of records; (d) no limitations on third-party discovery; and (e) the DOJ advising the relevant court that an Amnesty Applicant exists and has informed the agency of conspiratorial conduct consistent with plaintiffs' allegations. Such a compromise would permit civil plaintiffs to prepare and pursue their case¹⁴⁷ while preserving the ability of the DOJ to investigate and criminally prosecute the cartel.

B. Foreign Antitrust Enforcement

Likewise, due to the international nature of some cartels, some defendants may be faced with the competing aspects and requirements of the U.S. and European Union leniency programs. If an Amnesty Applicant is prohibited by the E.C. from disclosing potentially relevant facts or documents to the civil plaintiffs in the U.S., should that same Amnesty Applicant be permitted to qualify for ACPERA single damages protection? If a civil plaintiff files, prepares, and litigates its case without the benefit of such cooperation, it seems inequitable to permit an Amnesty Applicant to claim at the end of the litigation less than valuable cooperation (that a civil plaintiff has taken the time, expense and effort to already gather on its own) in exchange for single damages savings. Courts will need to determine similar scenarios whether delayed or partial cooperation by global cartelists qualifies under ACPERA.

In *Publication Paper* for example, parallel governmental investigations are ongoing, in both the U.S. and elsewhere (such as the EC), the Amnesty Applicant may feel that its cooperation should be deferred until the foreign investigation is completed or it may even be told by foreign regulators that it may not cooperate until the foreign investigation has run its course. This creates a clear conflict for an Applicant. In light of recent decisions unequivocally ordering the production of foreign documents, the Applicant is directed to provide information "wherever" it is located.¹⁴⁸ Yet if it does, it may be penalized for doing so in the parallel foreign proceedings. The legislative history of the Act makes clear that these "[d]ocuments or other items in the applicant's possession, custody or control

143 Supplemental Case Management Order No. 1 (June 21, 2007) in *In re Static Random Access Memory (SRAM) Antitrust Litig.*, No. C 07-1819 (N.D. Cal.).

144 Stipulation & Order Limiting the Scope of Discovery, (Apr. 16, 2003) *In re Dynamic Random Access (DRAM) Antitrust Litig.*, No. MDL C-02-1486 PJH (N.D. Cal.).

145 *In re TFT-LCD Antitrust Litig.*, No. M-07-1827 SI, 2007 WL 2782951 (N.D. Cal. Sept. 27, 2007). For the DOJ's viewpoint on this intersection, see Niall E. Lynch, *PARALLEL PROCEEDINGS: THE GOVERNMENT PERSPECTIVE*, ABA SECTION OF ANTITRUST LAW 51ST ANNUAL SPRING MEETING COURSE MATERIALS 455 (Apr. 3, 2003).

146 See, e.g., "Stipulation And Order for Limited Discovery Stay" (Sept. 12, 2008), filed in *In re Cathode Ray Tubes (CRT) Antitrust Litig.*, MDL No. 1917 (N.D. Ca.); Order of April 20, 2009 in *In re Aftermarket Automotive Lighting Antitrust Litig.*, No. 09-MJ-2007 (C.D. Cal.); "Order Granting Motion of United States To Intervene And Stay Discovery" (Oct. 24, 2008) in *Albee v. Korean Air Lines Co., Ltd.*, MDL No. 1891 (C.D. Cal.). See also "Order No. 4" (Feb. 18, 2009) in *In re Hawaiian & Guamanian Cabotage Antitrust Litig.*, No. 08-md-1972 TSZ (W.D. Wash.).

147 See, e.g., *Sterling Nat'l Bank v. A-1 Hotels Intl, Inc.*, 175 F.Supp.2d 573, 575 (S.D.N.Y. 2000) (concluding that "it would be perverse if plaintiffs who claim to be the victims of criminal activity were to receive slower justice than other plaintiffs because the behavior they allege is sufficiently egregious to have attracted the attention of the criminal authorities"). It is "only through the discovery procedure that a plaintiff can determine the merit (or lack of merit) in his [or her] case and develop the strategy which will guide him [or her] throughout the litigation." *Golden Quality Ice Cream Co. v. Deerfield Specialty Papers, Inc.*, 87 F.R.D. 53, 56 (E.D. Pa. 1980). See also *In re Residential Doors Antitrust Litig.*, 900 F.Supp. 749, 756 (E.D. Pa. 1995) (rejecting argument that discovery can be stayed without prejudice to plaintiffs until completion of government's criminal investigation of unspecified others at unknown future date).

148 ACPERA, Section 213.

[are to] be produced even if they are arguably located outside the jurisdiction of the U.S. courts.¹⁴⁹ No courts, however, have as yet resolved this issue.¹⁵⁰

Foreign corporate Amnesty Applicants (or foreign parents of U.S. Amnesty Applicants) may present additional complexities. For instance, a foreign Amnesty Applicant may move to dismiss a civil case for lack of personal jurisdiction. This may be a first signal of non-cooperation under ACPERA. Since the Applicant has presumably already consented to the jurisdiction of the U.S. Department of Justice, in the criminal context if it resists a U.S. court's civil jurisdiction, a foreign Amnesty Applicant is arguably not satisfying its duty under the Leniency Program to make restitution to injured parties. Similarly, civil plaintiffs could request that a cooperating foreign Amnesty Applicant not resist service or insist on service of discovery under the cumbersome Hague Convention procedures.¹⁵¹

VI. CONCLUSION

Leniency programs have dramatically altered the landscape of criminal antitrust enforcement, both in and outside the United States. The program implemented by the DOJ not only pioneered the field in the context of criminal accountability, it is the only system in place currently that provides civil incentives to enhance its effectiveness. Within the DOJ system, an Applicant can achieve criminal peace and unprecedented civil damage limitation. That benefit however has a price – timely and full cooperation with civil claimants in order to restore market integrity and promptly retribute damages caused by its conduct.

ACPERA is a powerful tool in reshaping both public and private cartel enforcement. Its obligations are equally powerful and should be imposed accordingly. Application of the obligation should not be without exception. But exceptions should be extended only for reasons and on terms or conditions which do not diminish, detract or defeat the letter and/or spirit of the Act.

¹⁴⁹ Cong. Rec. at H3658 (June 2, 2004).

¹⁵⁰ U.S. courts have faced issues of blocking disclosure of leniency materials submitted to foreign antitrust regulatory authorities and the results have been mixed. Compare *In re Rubber Chem. Antitrust Litig.*, 484 F.Supp.2d 1078, 1080-84 (N.D. Cal. 2007) (denying access to leniency materials provided to EC) with Memorandum Opinion Re Bioproducts' Rule 53 Objection (Dec. 18, 2002) in *In re Vitamins Antitrust Litig.*, 2000 U.S. Dist. LEXIS 7397 (permitting discovery of EC submission and communications with Canadian enforcement authorities).

¹⁵¹ The Hague Convention on the Taking of Evidence Abroad in Civil and Commercial Matters: 23 UST 2555; TIAS 7444; 847 UNTS 231; 28 USCA 1782 (1975 Cum. Supp.); 28 USCA 1781 (Supp. 1979); 81 LM 37 (1969).

REEXAMINATION PRACTICE WITH CONCURRENT DISTRICT COURT LITIGATION OR SECTION 337 USITC INVESTIGATIONS

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AUTHORS' NOTE

Patent reexamination was first selected as a topic for presentation at The Sedona Conference® on Patent Litigation in 2006. Over the past three years, this paper has gone through at least eight revisions as the authors address current procedure, process and cutting edge topics in reexamination practice. For those not familiar with The Sedona Conference®, its mission is to “engage in true dialogue, not debate, all in an effort to move the law forward in a reasoned and just way.”² The paper therefore subscribes to a neutral “Swiss” approach of presenting all sides of an issue and not taking sides so that the Sedona-like dialogue on the topic can ensue. Many people have provided comments and information for this article, including judges, senior officials from the PTO, patent litigators, patent prosecutors, academics, bloggers, and interested members of the public. Moreover, the authors devote substantial portions of their practices to reexaminations on behalf of both patent owners and third party requesters. However, the views expressed herein are for purposes of deep dialogue and do not necessarily reflect those of any author or contributor to The Sedona Conferences® on-going effort in legal analysis, scholarship, and improvement of U.S. patent law.

1 Copyright 2009 The Sedona Conference® and Sterne, Kessler, Goldstein & Fox P.L.L.C., (SKGF). All Rights Reserved. The authors thank Michael Messinger, Michael Specht, Jason Eisenberg and Pauline Pelletier of Sterne Kessler for the reexamination stay research and data gathering and analysis presented in this article. The authors note with sadness the passing of their colleague and friend Kenneth C. Bass, III after a two year fight with cancer. Ken was a leading appellate specialist and contributed greatly to previous versions of this paper. His insight and friendship will be sorely missed.

2 http://www.thosedonaconference.org/content/tsc_mission/show_page_html. The Sedona Conference® is truly unique in its approach in providing what many consider to be the most sophisticated and advanced legal dialogue on U.S. patent law.

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I. INTRODUCTION

This paper addresses the interplay between patent litigation before the Federal Courts or the United States International Trade Commission (“ITC”) (“the courts”) and co-pending reexamination proceedings involving the patent-in-suit before the United States Patent and Trademark Office (“PTO”). As independent arbiters of patent validity, each forum poses a distinct set of challenges and risks for those disputing or defending patent validity. These so-called “parallel universes” work with separate rules, standards, procedures, time lines, and results in cases involving the same patent. High-profile cases involving high-profile reexaminations and co-pending litigation include *NTP, Inc. v. Research in Motion, Ltd.*³ (patents found to cover the Blackberry), *TiVo v. Echostar*,⁴ (TiVo’s TimeWarp Patents), *Proctor & Gamble v. Kraft Foods Global, Inc.*⁵ (patents for packing fresh coffee), and the numerous reexaminations⁶ and litigations⁷ surrounding U.S. Patent No. 5,253,341 for a “Remote Query Communication System.” These high-profile cases, some involving highly profitable products, have highlighted the critical interplay between the parallel universes of the Article III and Article I courts on the one hand and the PTO on the other.

Two primary factors have contributed to the increased use of reexamination as an alternate venue to challenge patent validity where district court litigation has been initiated. First, the PTO made a commitment in 2005 to make reexamination a more streamlined and viable venue for post-grant validity challenges by creating the Central Reexamination Unit (“CRU”). The CRU’s sole responsibility is handling reexaminations. The CRU’s organization and initiatives are described more fully below. But if the continued growth in the number of reexaminations filed is any indication, its formation has certainly put real teeth into a process previously perceived as pro-patent owner and plagued by delay and uncertainty.

Second, the legal landscape surrounding patent validity and reexamination has been in great flux. The Supreme Court’s 2007 decision in *KSR Int’l Co. v. Teleflex, Inc.*⁸ dramatically changed the calculus for determining whether an invention was “obvious” and that decision alone appears to have cast serious doubt on the validity of many hundreds of thousands of issued patents. Further, Federal Circuit cases such as *In re Translogic Tech.*,⁹ and *In re Swanson*,¹⁰ dramatically impacted and illuminated the legal landscape and brought the interplay between the courts and the PTO into sharper focus.

Patent infringement defendants and patent owners alike now recognize that defending patent validity before the CRU is a serious challenge. For this reason, reexamination filings have continued their rapid growth with no sign of slowing in 2009. The impact of a potential reexamination is now commonly considered by both parties in nearly every patent litigation and ITC investigation.¹¹ For that reason, patent owners contemplating a lawsuit should have a strategy in place in case the asserted patent is put into reexamination by the accused infringer. Similarly, every patent infringement defendant should consider the benefits of reexamination as an additional, and perhaps more favorable venue to challenge patent validity. Finally, district court judges and ITC administrative law judges should be aware of how reexamination can impact their respective proceedings. For these reasons The Sedona Conference® on Patent Litigation 2009 has incorporated reexamination into its highly acclaimed patent litigation program for the fourth year in a row.

In this paper, the authors expand and reinforce many of the topics covered in past Sedona Conferences® on Patent Litigation. The authors have also updated the reexamination statistics

3 *NTP, Inc. v. Research in Motion, Ltd.*, 418 F.3d 1282, 1326 (Fed. Cir. 2005).

4 *TiVo Inc. v. Echostar, et al.*, 2-04cv-01 (EDTX).

5 *Proctor & Gamble v. Kraft Foods Global, Inc.*, 3:08-cv-00930 and 3:07-cv-04413 (NDCA).

6 90/005,742; 90/008,972 and 90/009,381.

7 *Global Patent Holdings, LLC v. Pambers BRHC LLC*, No. 9-08CV80013 (S.D.Fla. Jan 08, 2008); *Zappos.com, Inc. v. Global Patent Holdings, LLC*, No. 2:07CV01726 (D.Nev. Dec. 26, 2007); *Global Patent Holdings, LLC v. CDW Corp.*, et al., No. 1:07CV04476 (N.D.Ill. Aug. 08, 2007).

8 *KSR Int’l Co. v. Teleflex, Inc.*, 127 S.Ct. 1727 (2007).

9 *In re Translogic Tech., Inc.*, 504 F.3d 1249 (Fed. Cir. 2008) (The Federal Circuit was presented with simultaneous appeal from BPAI and District Court on same patent. The Court decided the BPAI appeal first, upheld BPAI’s ruling that the patent was invalid, and vacated Translogic’s \$85 million damages award from the district court.)

10 *In re Swanson*, 540 F.3d. 1368 (Fed. Cir. 2008) (The Federal Circuit clarified when it is appropriate to base an SNQ on art previously considered by the Office.)

11 Failure to advise a client of the benefits of filing a request for reexamination of patents involved in a litigation was raised in a recent legal malpractice complaint as an instance where the conduct of a law firm “fell below the applicable standard of care.” *East Inc. v. Morrison & Foerster LLP*, CGC-09-487063.

distributed by the CRU, performed additional data collection, and have addressed how the *KSR* decision and many other recent significant legal developments are impacting reexamination practice.

This paper is organized differently from a typical journal article. In the spirit of The Sedona Conference®, **Section I** starts with hot topics and cutting edge recent legal developments in reexamination law and practice. For this version of the paper, each hot topic was selected based on those likely to be of greatest interest to judges. After all, it is the judges who largely manage the parallel universe between the courts and the PTO. This first section presumes the reader is at least somewhat familiar with the use of reexamination as a viable post-grant venue for challenging patent validity. In **Section II**, we describe in more detail the “parallel universes” of the courts and the PTO. These two tribunals are substantively different in both scope and standard of review. Understanding the differences is vital to any strategic reexamination decision making. In **Section III** we present advanced reexamination strategy considerations where federal court or ITC litigation is threatened or pending. Again, this section presumes some basic knowledge of reexamination practice. We discuss timing of reexamination requests, the risk versus reward calculus, general reexamination tenets, and other, often overlooked considerations. **Section IV** is a concise discussion of certain important aspects of basic reexamination practice. Therein, we discuss what is required to institute a reexamination, common pitfalls, the differences between *ex parte* and *inter partes* reexaminations, and other concerns. Readers not familiar with basic reexamination practice should review this section first. **Section V** provides a brief overview of the PTO’s Central Reexamination Unit, the current issues it faces, and recent initiatives to improve its core processes. We end with **Section VI**, which is a presentation and discussion of the most recent reexamination statistics, from both the CRU and our own independent data collection and analysis.

II. HOT TOPICS AND NEW DEVELOPMENTS

The marked increase in the use of reexamination has naturally caused more frequent and closer evaluation of its unique procedures by involved parties and the courts. In short, reexamination and its satellite issues (such as litigation stays) remain among the faster developing areas of intellectual property law. Indeed, in the words of top PTO officials, it is still a “work in progress.” We have identified a number of hot topics that are currently confronting parties finding themselves in a “parallel universe.” These hot topics, were selected and are discussed with special attention to the perspective of the judges who are tasked with managing the interfaces between the parallel universes. Our hot topics include:

- (A) Reexamination Pendency,
- (B) Litigation Stays,
- (C) Protective Orders,
- (D) Substantial New Questions of Patentability,
- (E) Real Party in Interest,
- (F) Impact of *KSR*,
- (G) Possible Defenses Other Than Patents and Printed Publications,
- (H) Multiple PTO Proceedings,
- (I) Appeals of *Inter Partes* Reexaminations to the BPAI and the Federal Circuit,
- (J) Impact of PTO and Court Decisions on Stock Price,
- (K) Effect of Settlement Agreements on *Inter Partes* Reexamination, and
- (L) Reexaminations and Willfulness.

Some of these hot topics are further discussed throughout this paper.

A. Reexamination Pendency

Reexamination pendency is a perennial hot topic for a number of reasons. First, for reexamination to be an effective post-grant venue for challenging patent validity, it must be concluded in a timely and efficient manner—*i.e.*, with the “special dispatch” required by statute. To avoid prejudice, however, the PTO must nonetheless act in a deliberate and fair manner by giving the patent owner a full opportunity to defend the patentability of its claims. Second, reexamination pendency is

an important factor weighed by the courts when deciding whether to stay concurrent litigation. Third, predictable reexamination timetables are enormously helpful to both third-party requesters and patent owners when they work reexamination strategies into dynamic district court litigation and ITC investigation timetables. In short, uncertainty in pendency of a reexamination proceeding diminishes the fairness and effectiveness of reexamination and litigation for all involved parties.

By statutory mandate, all reexaminations are to be handled with “special dispatch.”¹² Nonetheless, the CRU does prioritize pending reexaminations. For instance, higher priority is afforded to reexaminations of patents involved in litigation. Even higher priority is afforded when trial proceedings have been stayed pending the outcome of reexamination. Further, if there is a concurrent litigation and the reexamination proceeding has been pending for more than one year, the PTO may further expedite a reexamination proceeding by setting a one-month or thirty day period for responses to Office Actions.¹³ Litigation notwithstanding, the highest priority is assigned reexaminations that have been pending for two or more years.

The rules require patent owners to notify the PTO of prior or concurrent proceedings¹⁴ and the CRU has dedicated paralegals that search litigation databases for case status periodically during the pendency of the reexamination proceeding. The CRU thus assigns priority based on its own statistics and research, and based on patent owner notifications. However, it is still critical for the parties to keep the PTO informed of the existence and status of related co-pending district court or ITC proceedings.

Pendency at the CRU has been the subject of much previous analysis and discussion. Overall, the CRU has established an internal goal to issue a final office action or an Action Closing Prosecution within two years of the filing date of a request for reexamination. As the CRU works through its backlog, this goal is becoming more and more realistic. We provide in Section IV.A. some additional insight into internal PTO and CRU procedures to help decision makers identify potential bottlenecks and determining realistic reexamination timelines.

The issue currently gaining the most attention with respect to reexamination pendency is the rapidly growing backlog at the Board of Patent Appeals and Interferences (“BPAI” or “Board”), which takes appeals from the CRU in much the same way it does for regular prosecution. The recently released numbers for May 2009 are sobering. For all appealed cases (including those from the CRU), there were 9809 pending appeals at the beginning of May 2009.¹⁵ By the end of May 2009 that number had grown to 10,927 with over 1600 new appeals filed. Over that same time period, the Board disposed of only 523 cases. Assuming the Board can dispose of about 520 appeals a month, it would take the Board 22 months just to work through its pending cases, assuming no further requests are filed. But if the activity in May is any indication of the future, the Board is facing a nearly insurmountable hurdle. Other commentators have noted a nearly exponential increase since mid-2005.¹⁶

One possible reason for the increase may be additional appeals due to increased obviousness rejections in view of the *KSR* decision. Looking to the future, if the proposed PTO rules limiting continuations and requests for continued examinations are allowed to go into effect, appeals to the BPAI will likely increase far beyond the current numbers. If enacted, proposed legislation including additional post-grant patent review options will further exacerbate the BPAI backlog.

From the most recent statistics, it appears that the BPAI bottleneck is growing with little relief in sight. It is unclear, however, how or whether the statutory mandate for “special dispatch” will factor into the BPAI’s prioritization of cases. Will reexaminations be shunted to the head of the line

¹² 35 U.S.C. Sections 305 and 314.

¹³ MPEP Sections 2263 and 2663(L).

¹⁴ 37 C.F.R. Sections 1.565 and 1.985.

¹⁵ See <http://www.uspto.gov/web/offices/dcom/bpai/docs/receipts/fy2009.htm>.

¹⁶ See Dennis Crouch’s chart on the PatentlyO blog at: <http://www.patentlyo.com/patent/2009/06/timeline-of-the-bpai-backlog.html>.

over cases from regular prosecution? Will the Board establish a separate team of ALJs to expeditiously handle cases from the CRU? These issues are coming to a head and the authors are hopeful that the new PTO leadership will address these serious issues.

B. Litigation Stays

Litigation stays and reexamination pendency are closely linked. Pendency is, or at least should be, a factor in practically every stay decision. If a district court judge can have reasonable confidence in a reexamination timeline, it can simplify the stay calculus. For instance, if reexamination pendency is completely uncertain, or if the time to final decision extends years past an expected trial date, then stays become less likely as they severely prejudice the patent owner. Conversely, if the reexamination is certain to conclude shortly, substantial resources may be saved by issuing a stay.

Once a district court judge is reasonably comfortable with the reexamination timeline, then a number of other factors come into play. Judge Selna in the Central District of California has authored a number of nuanced stay decisions, including *Allergan Inc. v. Cayman Chem. Co.*¹⁷ Noting that “the totality of the circumstances governs,” Judge Selna listed the following positive factors supporting the grant of a stay:

1. Prior art presented to the Court will have been considered by the PTO, with its particular expertise.
2. Discovery problems relating to prior art can be alleviated by the PTO examination.
3. If the PTO invalidates the patent-in-suit, the case will likely be dismissed.
4. The outcome of reexamination may encourage settlement.
5. The record of reexamination will likely be entered at trial, thereby reducing the complexity and length of the litigation.
6. Issues, defenses, and evidence will be more easily limited in pre-trial conferences after a reexamination.
7. The cost will likely be reduced for both the parties and the court.

Judge Selna also noted the following negative factors that would support denial of a stay:¹⁸

1. Delay and changing market conditions over time may dramatically lower the value of injunctive relief.
2. Substantial expense and time invested may be wasted when litigating issues also under reexamination.
3. A delay may grant a tactical advantage to the moving party.
4. The reexamination outcome might not affect the civil litigation.

¹⁷ *Allergan Inc. v. Cayman Chem. Co.*, SACV 07-01316-JVS (Order dated April 9, 2009).

¹⁸ *Id.*

In *Allergan*, Judge Selna denied the stay primarily because the parties were competitors, and “the PTO might not conclude its reexamination for several years, and that this delay would prejudice Allergan’s rights to exclusive use of its patented technology and would cause it irreparable harm.”¹⁹

In a recent development, execution of judgment may be stayed based at least in part on reexamination proceedings. For example, the Federal Circuit recently granted an emergency request to stay enforcement of ITC cease-and-desist and exclusion orders. In this case, on November 15, 2007, the ITC had instituted an investigation based on a complaint by Funai Electric Co., Ltd. that several respondents were infringing its digital television patents.²⁰ Within weeks, an *ex parte* request for reexamination was filed. In late 2008, the ALJ issued an Initial Determination finding infringement of one of the patents. The ITC then issued a Final Determination finding infringement and issued exclusion and cease and desist orders on April 10, 2009.

On March 11, 2009 the CRU issued a Final Office Action rejecting all of the claims in the patent at issue.²¹ Based in part on that final action, the respondents asked the ITC to stay enforcement of its orders. At the same time, the respondents also filed a request that the Federal Circuit stay the ITC’s order pending appeal. According to a recent press release on one of the respondents’ websites, the Federal Circuit has granted the emergency request.²²

While not the final word on the issue of a stay, the Federal Circuit’s order is nevertheless significant. It suggests that a Final Office Action in a reexamination may be used as a basis for staying an ITC exclusion order even though the patent owner has not exhausted the right to appeal through the Board and much less the Federal Circuit.

The cynical view is that there are a sufficient number of factors involved to support either granting or denying at least a temporary stay in any given case. Because stay decisions are reviewed under an abuse of discretion standard, district court judges have almost unfettered authority. Nonetheless, more nuanced stay decisions are becoming the norm as ever more authority is developed on this issue. Practitioners and judges alike should be aware of all the nuanced factors that are in play. Reexamination stays are discussed more fully below in section IV.C.

C. Protective Orders

The interplay between the duty of disclosure in a reexamination proceeding and a protective order in a concurrent litigation is a critical issue facing not just the patent owner, but also the third party requester (who is often the defendant in the concurrent litigation), the PTO and the courts. How should parties craft a Protective Order in a concurrent district court litigation or ITC investigation to prepare for a possible reexamination proceeding at the PTO? Is it possible for a patent owner to satisfy its duty of disclosure while adhering to the guidelines of a protective order? What limitations does a protective order place on the resources available to a patent owner to prosecute the reexamination proceeding?

1. Duty of Disclosure in a Reexamination Proceeding

In a reexamination proceeding, each individual associated with the patent owner has a duty of candor and good faith in dealing with the PTO. The duty of candor includes a duty to disclose to the PTO all information known to that individual to be material to patentability in a reexamination proceeding.²³ Individuals who have a duty to disclose to the PTO all information known to be material to patentability in a reexamination proceeding. “[T]he patent owner, each attorney or agent who represents the patent owner, and every other individual who is substantively involved in a reexamination proceeding” is bound by the duty of candor.²⁴

¹⁹ *Id.*

²⁰ In the Matter of CERTAIN DIGITAL TELEVISION PRODUCTS AND CERTAIN PRODUCES CONTAINING SAME AND METHODS OF USING SAME, ITC Investigation No. 337-TA-617.

²¹ See Reexamination Control Nos. 90/010,075 and 90/008,828.

²² See <http://www.vizio.com/about.aspx?cid=3496&cid=1318>.

²³ 37 C.F.R. Sections 1.555(a) and 1.933(a).

²⁴ 37 C.F.R. Sections 1.555(a) and 1.933(b).

Some practitioners argue that the scope of the duty of disclosure in 37 C.F.R. Section 1.555 is ambiguous. Are all employees of the patent owner as well as every attorney or agent that represent the patent owner subject to the duty of disclosure regardless of their involvement in prosecution activities? For example, are litigation counsel covered by the duty of disclosure? Are retained experts?

Several district courts have limited the scope of the duty of disclosure to only those attorneys or agents substantively involved in preparation or prosecution. In *Intelli-Check v. Tricom Card Techs., Inc.*²⁵ the district court for District of New Jersey subscribed a duty of candor on each named inventor, prosecuting attorney, and other individual who is substantively involved in the preparation or prosecution of the patent application. Similarly, Judge Spencer in the Eastern District of Virginia found that a “party is only bound by the duty of candor, and therefore can only be penalized for failure to disclose material information, **if they are substantively involved in the preparation and prosecution of the patent application.**”²⁶

Therefore, a key question facing a patent owner is who can be called upon to prosecute and/or consult on strategy for the reexamination proceeding or the prosecution of other pending applications. To what extent may the patent owner’s trial team participate in prosecution of its pending patent applications, reexaminations, reissues, or interferences using information derived from the litigation? To what extent may the accused infringer’s trial team participate in prosecution of their own patent applications in the same subject matter as the patents in suit, in reexaminations of the patent owner’s patents, or in interferences involving the patent owner? Many litigation attorneys take a conservative approach to this issue and strictly avoid any involvement or discussions related to the prosecution of pending applications or reexaminations. Other litigation attorneys take a less conservative approach and participate in consultation on specific reexamination issues.

Additionally, a patent owner also must consider to what extent their reexamination expert may be considered to be “substantively involved in the preparation or prosecution of the patent application.” This consideration may influence whether a patent owner utilizes that same expert for the litigation as in the reexamination proceeding.

2. Considerations for Crafting a Protective Order

When crafting a protective order for district court litigation or ITC investigations, the parties must consider the possibility of a reexamination being filed when crafting the protective order for the litigation. For example, the parties may establish procedures to allow the filing of materials obtained during discovery that are subject to a protective order in the PTO reexamination proceeding. Absent sufficient procedures, a patent owner may be barred by the protective order from presenting materials to support patentability (*e.g.*, evidence of secondary considerations of nonobviousness) to the PTO. Similarly, the third party requester may be barred from submitting evidence supporting its obviousness position to the PTO.

Another important consideration is a prosecution bar. As a general matter, no party having access to another party’s highly confidential technical information under a protective order should be allowed to amend or supervise the amendment of pending claims in applications or claims under reexamination in the same technical space, nor should they be allowed to draft new claims.²⁷ In-depth knowledge of a competitor’s highly confidential technical information, combined with the ability to amend or draft claims, may convey a dangerously unfair advantage to the claim drafter. This applies equally to patent infringement plaintiffs and defendants, and applies equally whether the highly confidential information is received from an adversary or a party with temporarily aligned interests such as a co-defendant.

²⁵ 2005 U.S. Dist. LEXIS 38794 at *14 (D. N.J. Nov. 10, 2005).

²⁶ Memorandum Order, March 31, 2009, in *TeleCommunication Systems, Inc. v. Mobile 365, Inc.*, C.A. No. 3:06CV485, p. 8 (emphasis added).

²⁷ The protective order should explicitly and separately address applications and reexaminations. A reexamination is not an “application” and if the order simply addresses “applications,” then reexaminations would not expressly be covered.

Unresolved questions remain regarding the interplay between non-prosecution clauses in a protective order and a patent owner's duty of disclosure under 37 C.F.R. Sections 1.555 and 1.933. We expect significant developments in this area in the next year as the Office of Patent and Legal Administration ("OPLA") and the courts wrestle with this issue.

3. Handling Conflicting Duties

In a concurrent litigation, a patent owner may be faced with the circumstance in which it has the duty to disclose materials to the PTO under the duty of disclosure but has a conflicting duty to maintain the confidentiality of these materials under the protective order. How does a patent owner handle these conflicting duties?

Several practitioners have argued that the duty of disclosure to the PTO takes precedence over a protective order of a district court. Judge Spencer of the Eastern District of Virginia addressed the issue of whether the PTO's duty of disclosure over-rides the protective order of a district court such that the party does not have to obtain authorization to file materials subject to the protective order in the PTO.²⁸ Judge Spencer found that there was "no evidence – legal or logical – to support" the patent owner's (plaintiff's) contention that the Protective Order is overridden in its entirety by the PTO's disclosure requirements. A patent owner must therefore carefully consider the provisions of the district court's protective order before submitting materials covered by the protective order to the PTO.

In sum, both parties must consider the possibility of concurrent reexamination and must pay close attention to the protective order. Patent owners must understand their disclosure obligations under the reexamination rules. Patent owners should also consider carefully the duties and restrictions imposed upon them by receipt of such confidential or classified information. Accused infringers likewise need to be concerned about the impact of disclosing highly confidential technical information to other parties capable of drafting and amending patent claims.

D. Substantial New Questions of Patentability

Fundamental to every reexamination request is the substantial new question of patentability or the SNQ. The SNQ is the touchstone of patent reexamination and every reexamination request—both *inter partes* and *ex parte*—must include at least one SNQ. The purpose of the SNQ requirement is to create a threshold for reexamination to prevent serial reexamination proceedings on the same references, and to prevent harassment of the patent owner.²⁹ The SNQ requirement was included in the original 1980 *ex parte* reexamination statute as "a balance between curing allegedly defective patents [via reexamination] and preventing harassment of patentees."³⁰ While it may sound relatively simple, presentation of an SNQ is more subtle than many practitioners realize. This section presents an overview of the SNQ. It then discusses the impact of two recent court decisions on the SNQ. This section remains a "Hot Topic" because it is an often misunderstood area of reexamination practice that is ripe for litigation—*e.g.*, where the parties challenge the existence of an SNQ in a reexamination request through the Administrative Procedures Act or through appeal to the Federal Circuit.

1. The substantial new question ("SNQ") generally

Both the *ex parte* and *inter partes* statute require that a request for reexamination include at least one new substantial new question of patentability ("SNQ")³¹. The legislative history of the *ex parte* reexamination statute describes the SNQ as new, non-cumulative information about preexisting technology that may have escaped review at the time of the original examination of the patent

²⁸ Memorandum Order, March 31, 2009, *Telecommunication Systems, Inc. v. Mobile 365, Inc.*, C.A. No. 3:06CV485, p. 9.

²⁹ H.R. Rep. No. 96-1307 (1980).

³⁰ H.R. Rep. No. 107-120, at 1; see also *In re Recreative Technologies*, 83 F.3d 1394, 1397 (Fed. Cir. 1996).

³¹ 35 U.S.C. Sections 303 and 312.

application and in subsequent reexaminations of the patent, if they have been any. The SNQ could therefore be more aptly named a “substantial new technical teaching.” The establishment of an SNQ has tripped up many practitioners. It is not enough for a reference to be “new,” the reference must also be non-cumulative to the technological teachings previously considered by the PTO during prosecution. Therefore, even a newly discovered reference may not raise a SNQ if the reference merely is cumulative to similar prior art already fully considered by the PTO in a previous examination (and previous reexaminations).³² This is an important point when determining whether to file a reexamination request or what references to use.

The CRU rejects many reexamination requests on first filing for failure to clearly point out an SNQ. Specifically, the authors note a perceived increase in the number of reexamination requests that are receiving Notice of Incomplete Reexamination Request or requests being denied because the requester has failed to establish the reference used as a basis for an SNQ is “non-cumulative.”

Further, there is a common but fundamental misunderstanding by many as to the difference between an SNQ and a proposed ground of rejection. A reexamination request must include both at least one SNQ in addition to a detailed explanation of the pertinency and manner of applying the cited prior art to every claim for which reexamination is requested (the ground of rejection).³³ An SNQ is therefore separate and distinct from the proposed ground of rejection (a “*prima facie*” case of unpatentability).

Additionally, not all previously considered references (“old art”) are ineligible to support an SNQ. Old art previously considered in original or prior prosecution may be used to support an SNQ if shown in a new light. Second, previously unconsidered art may not provide *de facto* support for an SNQ if it is merely cumulative to art already considered by the Office. We discuss new light for old art in the following section.

2. In re Swanson and the SNQ

The Federal Circuit in *In re Swanson*³⁴ recently clarified what it takes to support an SNQ where a reference was previously used to reject the claims in original prosecution. The *ex parte* reexamination statute sets forth the universe of references that can be used to raise a SNQ.³⁵ In addition to a newly discovered reference, a previously applied reference can raise a SNQ if the previously applied reference is presented in a “new light”. Section 303(a) makes this explicit — “[t]he existence of a substantial new question of patentability is not precluded by the fact that a patent or printed publication was previously cited by or to the PTO or considered by the PTO.”³⁶ *In re Swanson* provides some guidance on what constitutes a “new light” for old art. For example, an SNQ based on previously applied art could arise because the examiner in the original examination misunderstood the actual technical teaching, because the examiner failed to consider a portion of the reference that contained the now cited teaching, or because the examiner applied the reference to a different limitation or claim than the reference is currently being applied.

But a reference does not raise an SNQ if the examiner in the original examination understood the actual technical teaching, but got it “wrong” in the rejection. This is a subtle but critical distinction.

32 MPEP Section 2242.

33 37 C.E.R. Sections 1.510(b) and 1.915(b).

34 *In re Swanson*, 540 F.3d 1368 (Fed. Cir. 2008).

35 35 U.S.C. Section 303(a) (patents and printed publications).

36 This sentence was added in the 2002 amendment to 35 U.S.C. Section 303 to specifically address *In re Portola Packaging, Inc.*, 110 F.3d 786 (Fed. Cir. 1997). In *Portola*, the Federal Circuit “interpreted the statutory intent [of the *ex parte* reexamination statutes] as precluding reexamination based on ‘prior art previously considered by the PTO in relation to the same or broader claims.’” *In re Swanson*, p. 11 (citing *Portola*, 110 F.3d at 791). Congress explained that the amendment to 35 U.S.C. Section 303(a) “overturns the holding of *In re Portola Packaging, Inc.*, a 1997 Federal court decision imposing an overly strict limit that reaches beyond the text of the Patent Act.” H.R. Rep. No. 107-120, at 2.

3. KSR and the SNQ

A further unsettled issue for many practitioners is the impact of *KSR* on reexamination practice. Did *KSR* open the door to reexamination challenges based on prior art overcome during original prosecution by arguing lack of teaching, suggestion, or motivation to combine?³⁷ The PTO pondered this critical issue for over sixteen months and then addressed this question explicitly in Rev. 7 of the M.P.E.P. (Manual of Patent Examining Procedure or MPEP), which became publicly available in August 2008. The MPEP now states:

The clarification of the legal standard for determining obviousness under 35 U.S.C. Section 103 in *KSR International Co. v. Teleflex Inc.* (KSR), 550 U.S. 550, 82 USPQ2d 1385 (2007) does not alter the legal standard for determining whether a substantial new question of patentability exists. The requirement for a substantial new question of patentability remains in place even if it is clear from the record of a patent for which reexamination is requested that the patent was granted because the Office did not show “motivation” to combine, or otherwise satisfy the teaching, suggestion, or motivation (TSM) test. Thus, a reexamination request relying on previously applied prior art that asks the Office to look at the art again based solely on the Supreme Court’s clarification of the legal standard for determining obviousness under 35 U.S.C. Section 103 in *KSR*, without presenting the art in new light or different way, will not raise a substantial new question of patentability as to the patent claims, and reexamination will not be ordered.³⁸

Following that amendment to the MPEP, the Federal Circuit issued its decision in *In re Swanson* on September 4, 2008. The *In re Swanson* decision did not address the impact of *KSR* on the determination of whether references raise an SNQ. The issue therefore remains unsettled.

KSR states that patent examiners, as well as the courts, can review the factual predicates underlying the obviousness calculus and reach the ultimate legal conclusion whether the subject matter is obvious.³⁹ Thus, it makes logical sense that it would be of great interest to the reexamination examiners to know what a person of ordinary skill in the art would have known at the time of filing of the original application for which reexamination is requested. The third party requester is advised to consider providing a description of what the POSITA would have known preferably in the reexamination request (or less preferably in a later response to an office action). This POSITA technical description can be presented in a separate section of the reexamination request, but regardless of how it is provided, it is necessary that the SNQ basis be set forth for each technical reference referred to in this technical description and that each of these SNQs be used in a least one proposed rejection. What is believed to be the first reexamination request that employed such a POSITA technical description is found in *Inter Partes* Reexamination Control No. 95/000,353 (“the ‘353 request”).

37 When *KSR* was decided at the end of April 2007, the PTO feared an avalanche of reexaminations based solely on an argument that the obviousness standard applied in the original prosecution had been relaxed. This argument was advanced by the Third Party Requester in *Ex Parte* Reexamination Control No. 90/008,949. In this request, the Third Party Requester argued that the Supreme Court’s decision in *KSR* provided a “new light” in which to view the references under the doctrine of obviousness. See Order Denying Request for *Ex Parte* Reexamination in Reexamination Control No. 90/008,949, p. 4. The *Ex Parte* Reexamination request was denied by the PTO. *Id.*, p. 5. In the denial, the PTO clarified the standard for determination of whether an SNQ exists based on “old art”:

Reexamination is limited to review of new information about preexisting technology, which may have escaped review at the time of initial examination of the patent application. It was not designed for harassment of a patent owner by review of old information about preexisting technology, even if a third party feels the Office’s conclusion based on that old information was erroneous. The reexamination legislative history nowhere provides for review of such old information, each time a court clarifies or re-interprets a standard or point of law that effects the patentability determination. If it did, the reexamination process would be unwieldy, because case law is constantly evolving.

... The *KSR* decision does not *per se* create new information about preexisting technology that may have escaped review at the time of the initial examination of the patent application. And, in this instance, the *KSR* decision does not present or view the “old art” in a different way, or in a “new light,” as compared to what was already considered in the ‘7628 reexamination proceeding.”

Id., pp. 6-9. (emphasis in original). The feared avalanche did not materialize but there is no doubt that *KSR* spawned more reexaminations than would have occurred otherwise.

38 MPEP Section 2216, Rev. 7, July 2008.

39 *KSR*, 540 U.S. at 413 (“While the sequence of [the Graham factors] might be reordered in any particular case, the factors continue to define the inquiry that controls. If a court, or patent examiner, conducts this analysis and concludes the claimed subject matter was obvious, the claim is invalid under Section 103”).

The '353 request provided an extensive discussion of the various factors, articulated by the Federal Circuit and discussed in the Examination Guidelines, which may be considered in determining the level of ordinary skill in the art.⁴⁰ The specific factors addressed in the '353 request included the types of problems encountered in the art, prior art solutions to those problems, rapidity with which innovations are made, the sophistication of the technology, and the educational level of active workers in the field.

E. Real Party in Interest

While *ex parte* reexamination requests may be filed anonymously by any party, at any time,⁴¹ *inter partes* reexamination requests must identify the real party in interest filing the request. The real party in interest requirement is closely tied to the *inter partes* reexamination estoppel provisions.⁴² The estoppel provisions of 35 U.S.C. Section 317(b) apply to the "third party requester" and "its privies." The real party in interest disclosure therefore must be "to the extent necessary for a subsequent person filing an *inter partes* reexamination request to determine whether that person is a privy."⁴³

The PTO currently is struggling with the "real party in interest" rule where there is concurrent district court litigation with multiple defendants. Typically, in a multi-defendant litigation, the group of defendants will create a joint defense group ("JDG"). Issues occur when one or more defendants, but not all, file an *inter partes* reexamination request. For instance, the filing defendant (or defendants) may have minimal infringement exposure but is alleged or believed to be acting as a surrogate for the other defendants who are not officially part of the *inter partes* reexamination and thus not bound by the estoppel provisions.⁴⁴ An alternative scenario is that the defendant filing the *inter partes* reexamination request is doing so on its own initiative, and perhaps against the wishes of one or more co-defendants.

In such situations, who is the real party in interest? Just the third party requester or the entire JDG? Just those JDG members who have concurred with the reexamination strategy? Just those JDG members who have provided prior art, research, review, analysis, drafts, staffing support, financial backing, concurrence on actual filings, approval of filings, etc.? The authors are aware of several cases involving various flavors of this scenario where the patent owner has filed a petition to vacate the reexamination order, or suspend the reexamination, on the grounds that the "real party in interest" has not been identified and the PTO therefore lacks jurisdiction to continue reexamination proceedings.⁴⁵ Where the parties disagree on the facts, the PTO takes the position that it has not been vested with the tools, such as a subpoena power, statutory authority, or a discovery process in reexamination proceedings, necessary to make a proper factual determination. Nor is there clear guidance in the *inter partes* reexamination statute, its legislative history, the PTO rules, or from the courts as to how to resolve such "real party in interest" issues which are real but now often effectively ignored.

Perhaps most importantly, petitions for challenging the real party in interest are not handled by the CRU but are referred to the Office of Patent Legal Administration ("OPLA"). These petitions take time and often significant resources to resolve and are perceived by some as being directly contrary to the statutory requirement that the PTO act with "special dispatch." As one OPLA official has stated, such petitions act as an "anchor" on reexamination proceedings that bring it to a standstill or even prevent the reexamination from getting underway.

40 See e.g., *In re GPAC*, 57 F.3d 1573, 1579 (Fed. Cir. 1995); *Customer Accessories, Inc. v. Jeffrey-Allan Indus., Inc.*, 807 F.2d 955, 962 (Fed. Cir. 1986); *Envtl. Designs, Ltd. v. Union Oil Co.*, 713 F.2d 693, 696 (Fed. Cir. 1983).

41 See 37 C.F.R. Section 1.510(b) (setting forth information required for an *ex parte* reexamination request and not including the identity of that requester); see also 37 C.F.R. Section 1.510(f) (requiring attorney or agent to have power of attorney if "a request is filed by an attorney or agent identifying another party on whose behalf the request is filed").

42 See M.P.E.P. Section 2612 ("note that it is the real party in interest that is subject to the estoppel provisions and not the party who actually filed the request").

43 37 C.F.R. Section 1.915(b)(8).

44 35 U.S.C. Sections 315(b) and 316(b).

45 The real party in interest issue arises in *inter partes* Reexamination Control Nos. 95/000,227 and 95/000,229.

There is at least one case where the PTO has dismissed an *inter partes* reexamination where the real party in interest was not identified to its satisfaction.⁴⁶ The request was filed by an entity calling itself “Troll Busters.” The requester’s website describes its service as completely anonymous: “Troll Busters takes aim and fires in our own name. The Patent Troll will never know who or how many are behind the ‘hit.’”⁴⁷ In practice, the PTO generally will not look beyond the required statement identifying the real party in interest unless it is not facially accurate or is ambiguous. In the Troll Busters case, based on the information posted on the Troll Busters webpages, the PTO issued a show cause order to establish the identity of the real party in interest. The PTO was not persuaded by the response, and terminated the reexamination stating that “Troll Busters cannot act as a ‘shill’ in an *inter partes* reexamination request to shield the identity of the real party or parties in interest.”⁴⁸ This is the only case of which the authors are aware where the PTO has terminated an *inter partes* reexamination request based on a finding of a violation of the real party in interest requirement.

The Troll Busters case establishes several important considerations for challenging the real party in interest. First, “extrinsic evidence may be submitted by the patent owner to support a petition to vacate the filing date or the Office may use extrinsic evidence to, *sua sponte*, order the requester/real party in interest to show cause.”⁴⁹ Second, the PTO stated that “[a]n entity named as the sole real party in interest may not receive a suggestion from another party that a particular patent should be the subject of a request for *inter partes* reexamination and be compensated by that party for the filing of the request . . . without naming the party who suggested and compensated the entity for the filing of a request.”⁵⁰ Finally, the PTO explicitly noted that *ex parte* reexamination was still an option for Troll Busters.

In sum, the PTO has a limited ability and appetite to resolve real party in interest disputes in the context of *inter partes* reexamination proceedings because the PTO does not have the discovery mechanisms in reexamination proceedings and resources to mediate or decide such a dispute. However, the “Troll Busters” case shows that an insufficient response to a show cause order may result in dismissal of the *inter partes* reexamination.

When a final decision in an *inter partes* reexamination is favorable to patentability, the estoppel provisions of 35 U.S.C. Section 315(c) attaches to the civil action. Although the PTO has limited ability to investigate and resolve real party in interest issues for PTO proceedings, some practitioners argue that a district court should investigate the true interested prior to instituting the estoppels in the litigation, particularly in multi-party litigation. This is a hot area of dispute, and the authors expect to see more developments over the next year.

F. Impact of KSR on Reexamination Practice

The Supreme Court’s decision in *KSR v. Teleflex* altered the obviousness calculus in fundamental way by making the obviousness determination more subjective. The full scope of KSR’s impact on patent reexamination remains to be seen, but initial reports indicate that the results may be dire for patent owners, particularly in the “predictable” arts. Extensive research about the impact of *KSR* has been done by many groups. That research demonstrates the impact is significant in original prosecution. For instance, perhaps the most extensive publicly available sample and analysis is by Microsoft’s Corporate Vice President for IP Policy and Strategy, Marshal Phelps *et al.*. His research was presented at Sedona Patent Litigation 2008.⁵¹ As his analysis shows, the most effective way to challenge an obviousness rejection in predictable arts is to persuasively argue, with factual support, that a claim feature is not taught by the references. If the references in fact show each element, either explicitly or inherently, then it seems to be very difficult to overcome an obviousness rejection.⁵²

⁴⁶ See Reexamination Control No. 95/001,045.

⁴⁷ See <http://www.troll-busters.com/>.

⁴⁸ See Control No. 95/001,045, “Decision Vacating Filing Date,” p. 7 (mailed Aug 25, 2008).

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ See Microsoft Obviousness Data Research Slide Deck in Obviousness Panel tab of course notebook of Sedona PL08.

⁵² Many argue that the mere existence of all of the claim elements in the prior art as the basis for a finding of obviousness turns this test of patentability on its head since most inventions are “combination of old elements.” This applies to some of the most important inventions of all time.

It is clear from recent Federal Circuit and BPAI of Patent Appeals and Interferences (BPAI) decisions that mere attorney argument is not sufficient in many cases to prove non-obviousness.⁵³ The attorney is typically not an expert in the technology of the claimed invention and is not a person of ordinary skill in the art.⁵⁴ To prove non-obviousness it seems the best tack is for the story of the invention to be told in its full glory so that the factual predicates are found in the record to support the desired legal conclusion of non-obviousness. While *KSR* makes many statements about what is or is not obvious, it is clear from Supreme Court law that what the decision-maker requires is all of the relevant facts about the invention and its predecessor technology. Thus it behooves the patent owner to put all of the necessary factual predicates in the reexamination record to support the desired legal conclusion of non-obviousness. Failure to do so could result in the CRU finding the claims not patentable and the BPAI and Federal Circuit on appeal being limited to a record that will not permit a reversal.

KSR is seen by some judges as providing examples of what might constitute good factual predicates to support non-obviousness, but not as a definitive guide on how best to set forth the full story of the invention. These factual predicates include the so-called “secondary considerations” or “objective evidence” of non-obviousness, such as unexpected results, long-felt need, failure by others and commercial success. But this list is not definitive and counsel for the patent owner should be vigilant and creative in ferreting out and presenting all factual evidence that supports patentability.

One crucial consideration is how to get factual evidence into the record during reexamination. Factual evidence can be in the form of trial evidence or testimony, publication, award, sales information, product reviews, *etc.* Should it be from an expert or at least from a witness considered to be a POSITA? The answer often is yes, although it is a tactical decision just to have POSITA qualification since a qualified technical expert can typically also opine as a POSITA. Reexamination counsel for the patent owner is ill advised to assume either role explicitly or through attorney argument unless she can be qualified as if she is testifying as such in court.⁵⁵

How should this factual evidence from the expert or POSITA be provided to the CRU? Probably it is best if it is in the form of an affidavit or declaration. But such a submission raises several concerns.

First is the specter of inequitable conduct. Reexamination counsel for patent owner is particularly vulnerable because the law is somewhat confused in this area of what constitutes sufficient disclosure of pecuniary benefit between affiant/declarant and the patent owner. Future versions of this paper will address this more fully. However, it behooves the drafter to err on the side of comprehensive disclosure, but such approach increases the size of the administrative record, something the PTO has indicated it would like to avoid, all things being equal.⁵⁶

The second concern is that the reexamination examiners have no mechanism and little experience at best in assessing the competency and veracity of the information and analysis presented in written submissions.⁵⁷

The third concern is the strict page limits imposed on responses to office actions. The page limit issue is sufficiently important that it is addressed separately below as a “hot topic.” We note however, that if the submission is denominated as “factual” as opposed to “argument” it is NOT counted in the page limit.

⁵³ See *Sundance, Inc. v. Demonte Fabricating LTD.*, No. 2008-1068, -1115 Slip op. at 4-7 (Fed. Cir. Dec. 24, 2008).

⁵⁴ *Id.* (disallowing a patent expert's testimony stating that “[d]espite the absence of any suggestion of relevant technical expertise, [the patent expert] offered expert testimony on several issues which are exclusively determined from the perspective of ordinary skill in the art”).

⁵⁵ *Id.*

⁵⁶ Since the duty of disclosure does not apply to reexamination counsel for third party requester, can “reverse” inequitable conduct be found by the PTO, BPAI or the courts for requester submissions clearly hiding the ball from the reexamination examiners? Or is the only possible violation that of 37 C.F.R. Section 11.18? And if the latter is the case, how would such a violation be raised? Would it be done by OPLA based on a Petition from the patent owner that would be referred to The Office of Enrollment and Discipline (OED)? We know the PTO is thinking about these issues but we do not know of any public information from OED showing such a violation has been successfully prosecuted. This different standard of care between reexamination counsel for patent owner and reexamination counsel for third party requester troubles many people and we expect it to be addressed by some tribunal soon.

⁵⁷ This is a broader problem than the mechanisms available to and experience possessed by reexamination examiners in that in *ex parte* prosecution there traditionally has been little use of affidavits and declarations. But post-*KSR*, this could change dramatically especially in light of recent BPAI and Federal Circuit decisions on obviousness.

We expect that the obviousness area of patent practice will experience extensive attention in the next year as applicants, patent owners, and challengers grapple with the practical implications of *KSR* in PTO examinations, in the CRU, at the BPAI, and in the federal courts and at the ITC.

G. Possible Validity Challenges Other Than Patents and Printed Publications

Original patent claims in both *ex parte* and *inter partes* reexamination proceedings are only examined on the basis of patents and printed publications.⁵⁸ The full suite of defenses available in patent litigations including statutory subject matter (35 U.S.C. Section 101), written description and enablement (35 U.S.C. Section 112), public use, prior sale, and inequitable conduct are NOT available in reexamination proceedings. This disparity between invalidity challenges available in a district court and the invalidity challenges in reexamination has spawned efforts to expand the available bases for requesting reexamination to create more equivalence between the two forums. The PTO takes the position that the reexamination statute does not permit such an expansion.⁵⁹ The CRU has therefore strictly enforced the narrow basis for reexamination of original claims to rejections based on patents and printed publication. Under this regime, collateral prior art defenses—for example commercialization activities surrounding a printed publication—cannot be considered in reexamination even though such defenses can be considered in any parallel court litigation under prior art categories such as “on sale” or “public use.”

The efforts to achieve identity between the invalidity challenges available in district court and those available in reexamination have centered primarily on changes to the underlying statute and the introduction of a new post grant review process. This post-grant review (“PGR”) process has been proposed in several prior versions of Patent Reform legislation; and as of the publication of this paper Senate Bill S515 contains language for a “first window” post-grant review. Under the current version, the “window” concept refers to the time period from when the patent issues to when the period for filing a PGR would close—12 months in the current draft. The PGR would supplement, not replace reexamination. As part of the legislation, *inter partes* reexamination would be made available for all unexpired patents.⁶⁰ The PGR would be an adversarial two-party process in the PTO with expanded grounds for challenging validity of a patent beyond the limited patents and printed publication available in reexamination. Limited discovery would be available and oral testimony before administrative law judges (“ALJs”) would be allowed. Under the current view, the ALJ would rule in a summary judgment style. The goal of the PGR would be a faster, better, and cheaper alternative to the courts for decision on the validity of issued patent claims. The PGR concept as currently envisioned has generated considerable controversy from many stakeholder groups who question whether the professed goals are attainable and whether the PGR would actually improve the patent system and protect legitimate patent rights.

Other efforts focus on expanding the examination performed by the CRU, after a request is granted. As discussed above, the PTO does not address rejections of original patent claims beyond those based on patents or printed publications. The premise for not addressing these grounds for invalidity, particularly statutory subject matter or 35 U.S.C. Section 112 written description and enablement challenges, is that the original patent claims were found patentable under these statutory provisions during prosecution and therefore the claim status under these provisions has not changed. However, some practitioners argue that decisions by the Federal Circuit and Supreme Court occurring after allowance of the original patent claims undermine this reasoning. As an example, the Supreme Court has granted *cert* in the recent case address statutory subject matter, *In re Bilski*. Most watchers of this case expect the Supreme Court to formulate a new test for determining the existence of statutory subject matter. Such a decision will have a ripple effect, calling into question the patentability of a significant number of issued patents, particularly in the electrical arts, methods of doing business, and diagnostic and testing methods.

⁵⁸ 35 U.S.C. Sections 302, 311; 37 C.F.R. Sections 1.510(a), 1.915(b).

⁵⁹ See 37 C.F.R. Sections 1.552, 1.906; M.P.E.P. Sections 2258, 2658.

⁶⁰ Currently, *inter partes* reexamination can only be filed for a patent issued from an original application filed on or after November 29, 1999. See 37 C.F.R. Section 1.913; See also M.P.E.P. Section 2611.

As a result of these cases, the authors predict increased pressure on the PTO and Congress to introduce statutory subject matter challenges, at a minimum, into reexamination proceedings. Although statutorily barred from being included in the reexamination request, some practitioners argue that the PTO could, on its own, raise these issues during reexamination, in the same manner that is done during original prosecution. Although potentially allowable under the current statute, this approach would require a change to the PTO rules and procedures. Under current PTO procedures, amendments to the original patent claims open the door to these additional invalidity challenges—but only against the amendments.

H. Multiple PTO Proceedings Involving the Same Patent - Reexamination with Other Reexamination, Reissue, or Interference Proceeding

If the parallel universe of having the same patent subject to review in reexamination and court litigation seems complicated enough, the picture can become even more multi-dimensional if the patent is also subject to additional reexamination, reissue, or interference proceedings. There are several scenarios possible under current practice. Another *ex parte* or *inter partes* reexamination can be filed on the same patent.⁶¹ A reissue application, whether broadening or narrowing, can also be filed. Additionally, the patent in reexamination can be involved in an interference proceeding with another patent application. Under present practice, it is conceivable that a single patent could be involved in all of these proceedings concurrently.

Such multiple proceedings will likely have a significant impact on pendency, cost, and complexity of the reexamination.⁶² Such multiple PTO proceedings involving the same patent are not rare. In fact, multiple reexaminations of the same patent and/or a reexamination with a parallel reissue application are seen frequently, especially if the patent is perceived as being very valuable or is part of a hard-fought litigation. In Section V.F. below, the practice issues involving these parallel proceedings are examined.

Should a patent owner or third party requester initiate an additional concurrent proceeding? There are several important political and strategic perspectives to consider before initiating another concurrent proceeding. First, certain types of proceedings may be merged by the PTO. For example, multiple reexaminations of the same patent are typically merged into one proceeding. Because of the nearly certain merger, some practitioners have adopted the practice of first filing an *ex parte* reexamination and then following soon after with an *inter partes* reexamination. The *ex parte* reexam typically involves fewer claims and fewer SNQs than the later filed *inter partes* reexam. Some argue that this strategy allows the requester to obtain a quick filing date (to enhance the possibility of a stay from the court), and prevents a stay of the *inter partes* reexamination after merger due to the presence of the *ex parte* issues. Additionally, *ex parte* interview rights are typically extinguished after merger of the proceedings.

Other practitioners file multiple *ex parte* reexaminations (alone or in combination with an *inter partes* reexamination) on the same patent. With regard to the *ex parte* scenario, this “rolling reexams” approach is not prohibited by statute or by the rules. Because the multiple reexaminations are typically merged, patent owners argue that rolling reexaminations delay conclusion the reexamination proceeding, undermining their statutory right to a reexamination proceeding handled with “special dispatch,” waste valuable patent term, can effectively turn an *ex parte* proceeding into an *inter partes* proceeding, and could be perceived as harassment of the patent owner.

Reissue applications may also be merged with a copending reexamination proceeding. The merged reissue/reexamination proceedings are often transferred to the technology center for handling, rather than the CRU. Some practitioners argue that this strategy creates an unfair advantage by allowing the patent owner to prosecute the reexamination in a technology center that may be more

61 If an *inter partes* reexamination has already been filed, the estoppel provisions of 35 U.S.C. Section 317 prevent the third party requester or its privies from filing a subsequent reexamination request.

62 Current legislation contained in S515 in the U.S. Senate could expand this complexity with the creation of a “first window” post-grant review process and expansion of *inter partes* reexamination to cover all unexpired patents.

friendly to the patent owner and that operates under different performance metrics for examiners. Practitioners also argue that this technique is used to introduce delay into the PTO proceedings. Authors have been told that the PTO is constantly reviewing its merger procedures for reissues and reexamination to remove the potential for “gaming the system.”

A patent being reexamined may also be involved in an interference proceeding with at least one application.⁶³ The general policy of the PTO is that the reexamination proceeding will not be delayed, or stayed, because of an interference or the possibility of an interference.⁶⁴ In a concurrent reexamination and interference, the PTO follows the practice of making the required and necessary decisions in the reexamination proceeding and, at the same time, going forward with the interference to the extent desirable.⁶⁵ Any party to the interference may make a miscellaneous motion under 37 C.F.R. Section 41.121(a)(3) to suspend an interference pending the outcome of a reexamination proceeding.⁶⁶ Similarly, a party to the reexamination proceeding may file a petition to stay the reexamination proceeding because of the interference.⁶⁷

I. Appeals of Inter Partes Reexaminations to BPAI and Federal Circuit

Not a single *inter partes* reexamination has been appealed from the BPAI to the Federal Circuit. While a small percentage of *inter partes* reexamination certificates have issued from the CRU,⁶⁸ a search of the BPAI’s decisions reveals that the BPAI has decided less than five *inter partes* reexaminations.⁶⁹ Significantly, at least three of these decisions resulted in a non-final, non-appealable decision, and were therefore remanded to the examiner for further prosecution.⁷⁰

One reason for BPAI’s inability to issue final decisions seems to be a lack of clarity in both the rules and statutes for the role of the BPAI in reviewing CRU decisions. More specifically, it is not clear whether the BPAI should act as a judge between patent owner and the third party requester, or whether it should sit as a “super examiner,” the role it often takes in appeals.

The Chart entitled “Procedure Following Board Decision for Reexaminations Commenced On or After November 2, 2002” in MPEP Section 2601.01 graphically shows at least one remand problem that currently exists. In this example, the remand from the BPAI to the CRU occurs where a proposed ground of rejection in the reexamination request is not adopted by the CRU examiners in the first Office Action. On appeal to the BPAI the third party requester raises this as a “new ground of rejection” that should have been made by CRU. The BPAI agrees but does not have the factual and argument record to decide the rejection and thus remands the reexamination back to the CRU to address with the parties. This remand may occur for other reasons or may occur a second time. It is the specter of multiple remands that has created the concern that *inter partes* reexamination may be fundamentally flawed.⁷¹

Another possible reason for absence of cases making it to the Federal Circuit, is that, for a certain small subset of *inter partes* reexaminations, the process is effective without need to appeal to either the BPAI or the Federal Circuit. According to a recent PTO statistics, 44 *inter partes*

63 See M.P.E.P. Sections 2284, 2686.02.

64 See M.P.E.P. Sections 2284, 2686.02.

65 See M.P.E.P. Sections 2284, 2686.02.

66 See M.P.E.P. Sections 2284.II, 2686.02II.

67 See M.P.E.P. Sections 2284.V, 2686.02IV.

68 A Reexamination Certificate is issued at the completion of the reexamination process, regardless of the outcome, which often is cancellation or disclaimer of all of the claims.

69 See, e.g., Reexamination Control No. 95/000,006 (USPN 6,357,595); Reexamination Control No. 95/000,009 (USPN 6,399,670); Reexamination Control No. 95/000,030 (USPN 6,508,393).

70 It has been posed to the authors that the reason for no *inter partes* case making it from the BPAI to the Federal Circuit is due (1) to the very small number of *inter partes* reexaminations filed in the early years of the statute; and (2) to the practical reality that the *inter partes* reexamination process is a “work in progress” and like all such endeavors, it takes time to work out the kinks and “get it right.” Both of these observations appear correct but belie the practical consequence that the goals of *inter partes* reexamination of being faster, better and cheaper than the district courts in assessing patentability based on patents and printed publications have failed so far in practice.

71 At Sedona PL08 this possibility of multiple remands (dubbed the “infinite do loop” from computer programming parlance) was raised and seriously discussed. Senior PTO officials and others were concerned about its existence. Since then the authors have conferred with these senior officials and others to assess whether this problem is global or whether it is limited to two possible remands or to certain situations (e.g., the unadopted proposed ground of rejection example discussed). It seems that it is too early in the deployment of the current *inter partes* reexamination process to know whether the problem is global. Moreover, it may be that the BPAI will go more in the direction of acting as a judge who makes a final decision and sets case for appeal to Federal Circuit, and less as a “super examiner” who remands for another round of prosecution in its review of *inter partes* reexaminations.

reexamination certificates have issued as of December 31, 2008, out of 544 total requests filed through December 31, 2008.⁷² While this represents only ten percent of total *inter partes* reexaminations granted, the statistics indicates that [t]hird party requesters succeeded in having all claims cancelled or disclaimed in 70% (31) of the first 44 completed *inter partes* proceedings in which a certificate issued.⁷³ The high success rate is skewed by the significant non-response rate by the patent owner either after a first Office Action or after actions later in prosecution. Thus, the data might simply show that the *inter partes* process works well for a very weak patent in which the patent owner has little incentive to defend the patent's validity.

The practical effect of this uncertainty appears to be that the BPAI remands at least some reexaminations, especially *inter partes*, back to the CRU.⁷⁴ Based on the authors' interviews with senior BPAI and CRU personnel, we know the PTO is aware of this issue and is working to assess the issue and perhaps to devise changes that take into consideration the policy goals behind *inter partes* reexamination. Specifically, the PTO is seeking an approach that recognizes that *inter partes* reexamination should not be a tool used to harass patent owners, but rather functions as post-grant validity check on issued patents that is faster, cheaper, and better than federal the court challenges. Those objectives formed Congress's basis for creating the *inter partes* reexamination process.

J. Impact of PTO and Court Decisions on Stock Price

The CRU, the courts and the parties should all be aware of how their decisions involving reexaminations can impact the world outside the tribunal. In certain high profile situations in the past two years, the stock price (and company valuation) of a publicly traded patent owner has dropped precipitously due to a significant decision in a patent suit⁷⁵ or in a concurrent reexamination of the patent in suit such as the issuance of a non-final office action rejecting some or all of the claims of the patent in reexamination.⁷⁶ This precipitous drop is in large part due to "short selling" in the capital markets of the stock of the patent owner, which is driven down by the shorts as a way to make a big profit. Putting aside whether such practices are proper, it seems fair that the PTO should indicate on its website that rejections in non-final office actions do not necessarily reflect the final disposition of such claims in reexaminations. This information may stem the lack of knowledge of the full implications of a non-final office action and thus may allow the capital markets to more accurately and appropriately react to these reexamination developments.

Coupled to these precipitous stock drops due to non-final office action rejections, litigation and reexamination counsel for the requester have issued press releases touting the significance of the development. While the First Amendment encourages full disclosure of public information, critics contend that these press releases are so slanted that they cross the line of what is proper conduct for attorneys when "litigating in the press."

The authors have interviewed corporate executives and securities litigators regarding what legal rights and responsibilities patent owners have with and against short sellers using non-final reexamination and other patent enforcement developments to make quick big profits. In addition, they have interviewed experts in media relations and have received excellent feedback on how best to

⁷² *Inter Partes* Reexamination Filing Data - December 31, 2008, United States Patent and Trademark Office (December 2008). Authors note that 193 *inter partes* reexamination were filed through 2006.

⁷³ *Id.*

⁷⁴ The question has been raised by several as to why this multiple remand ("infinite do loop") problem does not exist with *ex parte* reexamination. One answer may be the structural difference of the third party requester not having standing once the *ex parte* request is instituted. A patent owner has no incentive to raise the "new ground of rejection" argument at the BPAI that the CRU should have adopted a proposed ground of rejection not used from the reexamination request.

⁷⁵ In January 2009, shares of Rambus fell nearly 40% when the U.S. District Court for the District of Delaware ruled in a patent infringement suit that the "company cannot enforce 12 of its semiconductor patents in a suit against Micron Technology Inc. because Rambus destroyed documents about them." See IPLaw360, Document Shredding Voided Rambus Patents (January 9, 2009).

⁷⁶ Tessera Technologies shares dropped nearly 40% following a non-final office action in a patent reexamination. Tessera's stock recovered somewhat, but only after its general counsel contacted investors and assured them non-final actions were not unusual and that "[c]laims of a patent can not be invalidated in reexamination until the process is fully complete, including all appeals." (See http://www.forbes.com/markets/2008/03/04/tessera-chip-patent-market-equity-cx_md_0304markets37.html). In another reported case, 01 Communique's stock fell more than 61% following an announcement that its patent infringement case against Citrix had been stayed pending reexamination of the patents underlying the claims. (See <http://network.nationalpost.com/np/blogs/tradingdesk/archive/2008/03/13/hot-stock-01-communique-down-60-on-patent-re-examination.aspx>) Finally, Avistar Communications blamed Microsoft initiated reexaminations for its need to cut its U.S. and European workforce by 25%. (See <http://www.siliconbeat.com/2008/03/26/local-firm-blames-25-job-cut-on-microsoft-action/>).

deal with court and PTO decisions in the parallel universe. In these days of instant corporate “news”—created by mass communications and the Internet, bloggers and message boards, mainstream press and self proclaimed anonymous pundits, investors and manipulators—perception is often more powerful than the “truth” and it behooves senior executives, their counsel and advisors to be current on best practices on how best to deal with this ever present challenge.

The authors commend the book *STOP THE PRESSES*⁷⁷ by Richard S. Levick, Esq. and Larry Smith as an excellent source of best practices for meeting this challenge. The following eight suggestions were provided by Melissa Arnoff of Levick Communications on how best to control and frame instant corporate “news.”

(1) Be positive: Don't repeat negative language or focus on negative verdicts. Instead, find a way to position the news in a positive, or at least neutral, light.

(2) Embrace the media: Instead of hiding from reporters, get to them early to tell your story and put decisions in context so they can tell balanced, accurate stories. If you avoid commenting, your opponent will control the entire story. This is the era of transparency; you cannot hide.

(3) Be an educator, not an enemy: Patent law is complicated. Help inform reporters and investors so that they better understand the re-exam process and don't over react to small decisions that are part of a long process. At first, this practice may seem awkward, but it will pay great dividends in better and fairer media coverage.

(4) Stay in front of the news: Prepare statements and news releases for each possible court decision before the verdict so that you can deliver your position immediately and not be delayed by the approval process and wordsmithing.

(5) Tell your story: Know what story you want to tell beyond the litigation. What company image do you want to project? Use that image in all your interviews so that you have something to talk about beside the legal process. Every public utterance is ultimately a marketing opportunity.

(6) Repeat. Repeat. Repeat: Don't be afraid to tell your story to as many audiences as possible as many times as possible. You don't have to use the same words every time, but keep the message consistent.

(7) Use your friends: Enlist third-parties to help tell your story and validate the strength of your company, or the details of patent law. It adds credibility and gives you more ways to tell your story.

(8) Apply the “Power of Three”: Why spend so much time preparing a speech or writing a paper only to use it once? Maximize your effort by finding at least three uses for each product you create. If you deliver a presentation before a group, re-package the talk as an article for a legal or IP publication, edit it for use as a blog post, and pitch it to the news media as the core of a feature story.

Compounding the issue of adverse impacts on stock is the delay by the PTO in posting documents on its publicly searchable database (“PAIR”). The PTO has improved the delay between filing and posting documents on PAIR. According to a PTO official, the goal is to have documents posted within two business days (48 hours).

K. Effect of Settlement Agreements on Inter Partes Reexamination

What is the effect on *inter partes* reexamination proceedings where a settlement agreement is reached in a concurrent litigation and one of the parties to the reexamination concedes or stipulates

⁷⁷ Richard S. Levick & Larry Smith, *STOP THE PRESSES: THE CRISIS AND LITIGATION PR DESK REFERENCE* (Watershed Press, 2007 2ND Ed).

either to the validity or invalidity of the patent? It is well settled that, during litigation, patent owners may make admissions to which they may be bound to during reexamination proceedings. For instance, a patent owner may make a binding admission as to whether a particular reference is prior art. If a third party requester concedes patent validity in a settlement agreement, is the PTO then obligated to decide the reexamination on such an admission? Would a settlement be considered a final decision such that the estoppel provisions now apply in the reexamination? Does a third party requester lose standing to participate in an *inter partes* reexamination automatically upon settlement or should removal from the reexamination proceeding be a condition of settlement? If a third party requester agrees to step out of the reexamination, would the *inter partes* reexamination continue or does the PTO convert the *inter partes* proceeding to an *ex parte* reexamination?

A settlement agreement will not operate to terminate a co-pending *inter partes* reexamination, even when an identity of claims and issues exists between the two proceedings. The estoppel provisions of 35 U.S.C. Section 317(b) states that the estoppels arise “[o]nce a final decision has been entered against a party in a civil action ... that the party has not sustained its burden of proving the invalidity of any patent claim in suit.” A settlement agreement is not a final decision that a party has not sustained its burden of proving invalidity of a patent claim. PTO takes this position and will not terminate an *inter partes* reexamination based solely on a settlement agreement between parties.

The PTO also will not automatically remove standing of the third party requester when the co-pending litigation settles. Therefore, any settlement agreement must address the ability of the third party to continue participation in the *inter partes* reexamination request. A third party can waive its ability to participate further in the reexamination. When the third party steps out of the reexamination, the *inter partes* reexamination is effectively turned *ex parte* in nature (*i.e.*, only the patent owner remains). Other interested entities are not permitted by the PTO to step into the shoes of the settling requester.⁷⁸ But whether a reexamination can upset a prior settlement agreement is another story, as noted in *In re Swanson*.⁷⁹

L. Reexaminations and Willfulness

Another extremely hot topic in concurrent reexamination and litigation is the use of reexaminations as a defense against willful infringement. In *In re Seagate Technology, LLC*⁸⁰ the Federal Circuit overturned the then existing standard for willful infringement. Under the new standard, “to establish willful infringement, a patentee must show by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent.”⁸¹ If this threshold objective standard is satisfied, the patentee must also demonstrate that this objectively defined risk was either known or so obvious that it should have been known to the accused infringer.⁸²

Under the new standard, some practitioners argue that the granting of a reexamination request by the PTO therefore defeats a claim of willful infringement. To date, district courts have declined to establish a *per se* rule regarding the impact of reexamination on a claim of willfulness. Instead, the district courts have viewed the granting of a reexamination request as one factor, among a totality of the circumstances, to consider in examining whether a party can meet the requirements of *In re Seagate*.⁸³ At least one court found that “[i]t does appear that a reexamination order may be taken as dispositive with respect to post-filing conduct.”⁸⁴

78 In litigations involving multiple accused infringers, the accused infringers that are not requesters to an *inter partes* reexamination run the risk that the requester will settle and use this prospect as settlement leverage with the patent owner who benefits from having the reexamination effectively converted to *ex parte*. However, these same accused infringers benefit because they are not subject to the estoppels of the *inter partes* statute.

79 *In re Swanson*, 540 F.3d 1168, at n.5 (Fed. Cir. 2008) (noting that “an attempt to reopen a final federal court judgment of infringement on the basis of a reexamination finding of invalidity might raise constitutional problems”).

80 *In re Seagate Technology, LLC*, 497 F.3d 1360 (Fed. Cir. 2006).

81 *Id.* at 1371.

82 *Id.*

83 See *Lucent Technologies v. Gateway, Inc.*, 2007 U.S. Dist. LEXIS 95934 (S.D. Cal. 2007); See also *St. Clair Intellectual Property Consultants, Inc. v. Matsushita Electronic Industrial Co., Ltd.*, 2009 U.S. Dist. LEXIS 49882 (D. Del 2009).

84 2007 U.S. Dist. LEXIS 95934 at *19.

Decisions on the impact of reexamination on the willfulness inquiry have focused on the status of the claims at the time of the willfulness determination. For example, if a reexamination certificate issued without amendments to the claims or claims in suit, a court may be hesitant to assign much weight to the reexamination request in the willfulness inquiry. However, before the reexamination certificate issues, the validity of a patent remains questionable and allegations of deliberate or reckless actions by a defendant may lack sufficient factual or legal grounds.⁸⁵

III. THE “PARALLEL UNIVERSE” EXAMINED

The term “parallel universe” has been used to describe the situation where patent validity is considered simultaneously by both a district court or the ITC and the PTO. It should be noted that the proceedings are “parallel” only in the temporal sense. To the extent that the term connotes any other identity of procedure, the term is a misnomer. In actuality, the proceedings are quite different in both scope and procedure. Understanding those differences are critical to any informed decision making on parallel reexamination proceedings. Before tackling reexamination strategy considerations in Section III, we first explore some basic differences in the two proceedings.

A. Scope of Proceedings

The scope of available validity challenges is far broader in district court litigation than it is in patent reexamination proceedings. In district court litigation, patent validity may be challenged under any statutory provision, including provisions set forth at 35 U.S.C. Sections 101, 102, 103 and 112. Further, patent challengers also may argue that the asserted patent is unenforceable due to either inequitable conduct or laches. Patent reexamination, on the other hand, is far more limited in scope. By statute, reexaminations may only be initiated when the PTO is presented with a “substantial new question of patentability” or (“SNQ.”)⁸⁶ An SNQ only may be predicated on prior art printed publications and may not be cumulative to information already considered by the PTO in original prosecution or in prior reexaminations. An SNQ may not be predicated on any other statutory provisions, including whether the claims contain statutory subject matter under section 101 or whether there exists an “on-sale-bar” or “public use” under section 102(b). Any party considering a parallel reexamination should be aware of the limited scope available to challenge the patentability during a patent reexamination.

B. Standard of Review

The standard of review for patent validity is different in district court litigation than it is before the CRU in patent reexamination proceedings. In district court, patent claims enjoy a presumption of validity, which may be overcome only by clear and convincing evidence. In contrast, no such evidentiary presumption exists during reexamination before the PTO. The PTO and the CRU use a “preponderance of the evidence” standard for adjudicating patentability.⁸⁷ For this reason, challenging a patent’s validity⁸⁸ should be easier before the PTO than in the district court. Nevertheless, a patent owner faces many practical limitations in its ability to amend claims during reexamination.⁸⁹ As noted herein, if claims are amended substantively, liability for past damages is put at serious risk.

⁸⁵ See March 3, 2009 ORDER, *Ultratech Int'l, Inc. v. Swimways Corp.*, 3:05-cv-134-J-25MCR (M.D. Fla.).

⁸⁶ 35 U.S.C. Sections 303, 304, 312, 313.

⁸⁷ MPEP Section 706.1. (“The standard to be applied in all cases is the ‘preponderance of the evidence’ test. In other words, an examiner should reject a claim if, in view of the prior art and evidence of record, it is more likely than not that the claim is unpatentable.”).

⁸⁸ The district courts determine “validity,” while the PTO reexamines “patentability.” The authors use these terms interchangeably, but they are technically different.

⁸⁹ No proposed amended or new claim enlarging the scope of claims of a patent is permitted in a reexamination proceeding, 35 U.S.C. Section 305. The test for when an amended or new claim enlarges the scope of an original claim is the same as that under the two-year limitation for reissue applications that add enlarging claims under 35 U.S.C. Section 251, last paragraph. MPEP Section 2250 (citing *In re Freeman*, 30 F.3d 1459, 1464 (Fed. Cir. 1994)). After expiration of a patent undergoing reexamination, no amendments may be proposed for entry, 37 CFR Section 1.121(j). Further, any amendments and all claims added during the proceeding are withdrawn if a patent expires during pendency of a reexamination proceeding. MPEP Section 2250.

C. Claim Construction

The standards for claim construction are very different in district court litigation as compared to patent reexamination proceedings. During reexamination proceedings, claims are construed with their broadest reasonable interpretation, consistent with the specification.⁹⁰ For this reason, a *Markman* order in district court has no preclusive effect on the PTO and is not binding thereon.⁹¹ A broad claim construction draws in more potential prior art.⁹²

In U.S. district courts, on the other hand, claims are often construed so that they remain valid in view of prior art. The court looks to get the “correct” claim construction after reviewing the parties’ respective positions. Such a construction will typically be narrower than used by the PTO and may thus limit the world of available prior art.

This is not a merely academic distinction—the difference in claim construction can have real world effects in the parallel universe. Consider a situation where a court issues a claim construction order in a litigation and the patent owner is ultimately successful in defending its intellectual property right against an invalidity challenge based on this claim construction. The defendant (or another third party) may subsequently challenge the patentability of the same patent in the PTO. In this situation, the PTO, using a broader construction, creates a different scope for the claims, and arguably a different intellectual property right. In such cases, the patent owner is not permitted to adopt the claim construction of the court. Due to these different claim construction standards, a patent owner may be forced into the difficult circumstance of having to amend claims to incorporate the court’s construction and potentially lose past damages, or continue to argue the issue in the reexamination proceeding and potentially extinguish all intellectual property rights in the patent. To be sure, more than a few patent owners have faced this exact situation.

It is technically true that patent owners have the ability to amend claims during reexamination, provided the amendments do not enlarge the scope of the claims. In the parallel universe situations, however, this ability is severely circumscribed. First, substantive amendment of asserted claims could literally wipe out a district court or ITC *Markman* ruling. If the litigation or ITC investigation has progressed to trial, substantive amendment of asserted claims could result in an enormous waste of judicial and party resources—sometimes to the tune tens of millions of dollars. Second, if a patent owner is forced to amend claims to preserve patentability, it risks the loss of any claim to past damages under the intervening rights doctrine, which is fully applicable to reexamination proceedings.⁹³ In many instances, this not an insignificant prospect. Third, in *inter partes* proceedings, the patent owner is not allowed to interview the examiner. If the patent owner decides to first argue around the prior art, and then is faced with a final office action, there is little room for the type of negotiation necessary to arrive claim amendments likely to be successful in overcoming pending final rejections. Thus, in reality, patent owners have an extremely limited ability to amend claims. This is one area of law that deserves careful attention.

D. Decision Makers

The ultimate arbiter of patent validity is different in the district court than it is in patent reexamination proceedings. This may be stating the obvious, but this fact has very real consequences. Patent validity challenges in district court are determined by a judge or jury that more often than not has absolutely no technical background in the relevant art. Before the CRU, on the other hand, patentability is determined by technically trained, experienced patent examiners. Moreover, the CRU assigns a 3 examiner team to each reexamination.

90 *In re Yamamoto*, 740 F.2d 1596, 1571 (Fed. Cir. 1984).

91 *In re Trans Texas Holdings Corp.*, 498 F.3d 1290, 1297 (Fed. Cir. 2007).

92 When a patent owner loses their ability to amend the claims (e.g., when a patent term expires during the reexamination proceeding), the standard for claim construction moves from the broadest reasonable interpretation standard to a standard “pursuant to the principle set forth by the court in *Phillips v. AWH Corp.*, 415 F.3d 1303, 1316, 75 USPQ2d 1321, 1329 (Fed. Cir. 2005)(words of a claim ‘are generally given their ordinary and customary meaning as understood by a person of ordinary skill in the art in question at the time of the invention).” MPEP Section 2258.I.G.

93 35 U.S.C. Sections 307(b) and 316(b).

E. District Court v. Central Reexamination Unit

“Courts do not find patents ‘valid,’ only that the patent challenger did not carry the ‘burden of establishing invalidity in the particular case before the court”⁹⁴ A prior holding of validity by a district court is therefore not inconsistent with a subsequent holding of invalidity by the PTO.⁹⁵ While the PTO may accord deference to factual findings made by the court, the determination of whether an SNQ exists will be made independently of the court’s decision on validity, since the decision is not controlling on the PTO.⁹⁶ A non-final holding of claim invalidity or unenforceability also will not be controlling on the question of whether an SNQ is present. Only a final holding of claim invalidity or unenforceability (after all appeals) is controlling on the PTO. In such cases, an SNQ would not be present as to the claims held invalid or unenforceable.⁹⁷ In other words, the PTO will not reexamine patent claims that previously were invalidated by a district court. In sum, only a final, non-appealable, ruling on invalidity is binding on the PTO.

F. Cumulative Effect

The cumulative effect of the “non-parallel” aspects of district court and reexamination proceedings is profound. It is the authors’ perception that broader claim construction used by the PTO, combined with the lack of any presumption of validity and skilled decision makers, results in far easier prior art validity challenges. Moreover, the CRU often rejects all of the claims in the first OA and puts the burden on the patent owner to prove the patentability of the claims even if the claims have been subject to extensive prior art attack in prior court actions.

With a high level understanding of the fundamental differences between validity challenges before the district court and the CRU, we now can explore various reexamination strategy considerations when district court litigation is threatened or pending.

IV. REEXAMINATION STRATEGY CONSIDERATIONS WHEN LITIGATION IS THREATENED OR PENDING

A comprehensive strategy should be in place before filing a reexamination request. The requester should have a clear objective and should be fully aware of the consequences of filing a reexamination request. Once filed, the requester cannot “unfile” the reexamination as part of a settlement with the patent owner.⁹⁸ After the reexamination is instituted, it will take on a life of its own. Many pitfalls await the unwary requester who has not fully thought out the consequences of filing a reexamination request. The following sections are presented roughly in chronological order.

A. Reexamination Pendency

Reexamination pendency continues to be a “Hot Topic.” As noted above in the Hot Topics section, a realistic timetable for a reexamination is a crucial datapoint for third party requesters, patent owners and judges as they navigate the parallel universe. For these reasons, we provide below some insight into external and internal PTO and CRU procedures, as well as the latest information regarding reexamination pendency.

Upon filing, reexamination requests first undergo review by the CRU staff to ensure compliance with the rules. For instance, the staff will ensure that each reference cited by requester is

⁹⁴ *In re Swanson*, 540 F.3d 1368, 1377 (Fed. Cir. 2008).

⁹⁵ In an *inter partes* reexamination brought by a party to the litigation, a final holding of validity in the civil action triggers the estoppel provisions of 37 C.F.R. Section 317(b) in the reexamination proceeding. All issues that were raised or could have been raised by the party in the civil action will not be maintained in the *inter partes* reexamination proceeding.

⁹⁶ *Ethicon, Inc. v. Quigg*, 849 F.2d 1422, 1428-29 (Fed. Cir. 1988); *In re Swanson*, No. 2007-1534 at pp. 12-18 (citing *Ethicon*, 849 F.2d at n. 3 and *Stevenson v. Sears Roebuck & Co.*, 713 F.2d 705, 710 (Fed. Cir. 1983)) (emphasis in original).

⁹⁷ See MPEP Section 2686.04.

⁹⁸ In a recent example, we are told that a third party requester attempted to halt a reexamination proceeding by stopping payment of a check for the reexamination fee. The PTO indicated that such actions could result in OED imposing a suspension of the attorney from PTO practice for taking the action.

used to support at least one SNQ. Further, the staff recently began ensuring that the requester properly and affirmatively demonstrated that each SNQ is non-cumulative of the art previously considered during original prosecution or previous reexaminations. If the reexamination request passes muster under the CRU staff, a notice of the request is made public in the Official Gazette. When a request is deemed to satisfy all the requirements of the *ex parte* or *inter partes* rules,⁹⁹ the filing date becomes the reexamination filing date. Just because the notice of request is published in the Official Gazette does not necessarily mean that the reexamination request was satisfactory. Roughly 10% of requests are later vacated by the examining panel for informalities. While this number has fallen from roughly 15% in previous years, the authors have noted a recent uptick in denial rates based on the requester's failure to adequately prove that the proposed SNQ is not cumulative to the art considered during original prosecution.

Once a satisfactory request has been made, the CRU has a three-month deadline to issue a decision on the request based on whether a substantial new question of patentability ("SNQ") has been raised in the request.¹⁰⁰ For *ex parte* requests, the grant starts a two month window in which the patent owner may respond to the request. In that response, the patent owner may amend claims or argue that the claims under reexamination are patentable. If the patent owner elects to file a statement, then the third party requester may reply. This is the only opportunity a third party requester gets to participate in an *ex parte* reexamination proceeding. Most reexamination practitioners advise against filing a patent owner's response for this reason. For *inter partes* requests, CRU procedures suggest that a first office action on the merits accompany the grant, but that is not required. Overall, the CRU has established an internal goal to issue a final office action or an Action Closing Prosecution ("ACP") within two years of the filing date of a request for reexamination. As the CRU works through its backlog, this goal is becoming more and more realistic.

All reexaminations are required by statute to be handled with "special dispatch."¹⁰¹ Nonetheless, higher priority is afforded to reexaminations of patents involved in litigation. Even higher priority is afforded when trial proceedings have been stayed pending the outcome of reexamination. The highest priority is assigned to reexaminations that have been pending for at least two years. The rules require patent owners to notify the Office of prior or concurrent proceedings,¹⁰² and the CRU has dedicated paralegals that search litigation databases for the status of pending litigation during the pendency of the reexamination proceeding. The CRU thus assigns priority based on its own statistics and research, and based on patent owner notifications. Therefore, it is critical for the Patent Owner to keep the PTO informed of the existence and status of related co-pending district court or ITC proceedings.

Currently, approximately 40% of the pending reexamination requests lay in the electrical/software/business method arts. In addition, the mechanical arts make up around 35% and this number is growing. While there may be a perception that reexamination is disfavored in the chemical/biological arts, we note that over 20% of reexamination filings were in these arts. The lower number of requests in the chemical/biological arts is likely a mirror of current trends in the technology centers and the fewer issued patents in the chemical/biological fields. Current pendency rates reflect the large number of reexaminations in the electrical arts. Using the two-year-to-final-action metric, the chemical/biological group has no backlog, while nearly 90% of the mechanical reexaminations achieved this goal. However, only 70% of the electrical/software/business method reexaminations resulted in a final action by the two-year point.

Once prosecution closes, an appeal to the BPAI is available to the patent owner in *ex parte* reexamination and to both the patent owner and the third party requester in *inter partes* reexamination. After hearing an appeal, the BPAI has a stated goal of then rendering a reexamination decision in six months. However, one serious issue currently impacting overall reexamination pendency is the growing backlog of cases awaiting disposition by the Board. As

99 35 U.S.C. Sections 510 (*ex parte* reexaminations) and 919 (*inter partes* reexaminations).

100 The substantial new question of patentability (SNQ) is discussed in more detail in subsequent sections of this paper.

101 35 U.S.C. Sections 305 and 314.

102 37 C.F.R. Sections 1.565 and 1.985.

noted above in the Hot Topics, the current BPAI statistics look grim, and without serious attention, the Board will soon face a nearly insurmountable backlog cases. If the Board does not implement procedures to deal separately with reexaminations and appeals from the CRU merely are added to the end of the line, then the growing BPAI bottleneck may run afoul of the statutory mandate for “special dispatch.” Moreover, the backlog and threatens to remove reexamination as a timely and efficient post-grant challenge.

The apparent BPAI bottleneck notwithstanding, as yet there are no reliable statistics on the pendency of reexaminations appealed to the BPAI. In an April 2008 briefing on *inter partes* reexaminations, the Institute for Progress estimated the average pendency for an unappealed *inter partes* reexamination as more than 3.5 years, and the expected pendency for appealed *inter partes* reexamination as at least 6.5 years.¹⁰³ Our survey of the *inter partes* reexaminations filed between 1/1/2000 and 5/31/2003 supports this expected pendency data for appealed *inter partes* reexaminations. Only four of the reexaminations filed during this period reached the stage where the BPAI has issued a decision. In each of those cases, the time period between the issuance of the right of appeal notice by the CRU and the issuance of the BPAI’s decision has been greater than three years.¹⁰⁴

Reexamination pendency has attracted high-level scrutiny. For example, Chief Judge Paul R. Michel commented on the ability of the PTO to handle post-grant proceedings in an Address at the *Federal Trade Commission Hearing on the Evolving IP Marketplace*, held on December 5, 2008:

To me, the proposed alternative for weeding out bad patents is convincing. Can we really get a faster, better, and cheaper review of challenged patents at the PTO than in the courts? Experience with the existing PTO reexamination procedures raises doubts.

And the PTO is already overwhelmed by *ex parte* examination with average pendencies over three years, in some arts, far longer. Is it realistic to expect the PTO to be able to conduct a new form of *inter partes* reexamination faster and cheaper than the courts? And more accurately? Unless its new procedures, competencies, and powers can be clearly defined, how will we know what consequences would follow? How will we know this is not a mirage in the desert that looks like an oasis, but has no water?

At present, the apparent BPAI bottleneck threatens to dwarf any pendency driven by the CRU or even briefing before the Board. However, some practitioners note that at least seven months can pass between the filing of a notice of appeal, the patent owner’s brief, the third party requester response (if *inter partes*), and the examiner’s answer. In the *inter partes* reexaminations we analyzed, this time period is often longer due to the period of time between Respondent’s Brief and the Examiner’s Answer.¹⁰⁵ The authors note that these early filed cases may not be representative because each of these reexaminations was filed prior to the institution of the CRU. At this time, there is no way to determine whether the CRU will increase the speed of the appeal briefing process.

B. Settlement

Reexamination could help force an early settlement. For example, some practitioners suggest presenting a reexamination request to the opposing party patent owner prior to submitting the request to the PTO (*i.e.*, a “pocket reexamination request”). The idea is to encourage early settlement of pending litigation on favorable terms. The patent owner may need to be educated on the risks that reexamination poses to its patent-in-suit. Further, the patent owner will be put on notice of invalidity risks its patent-in-suit faces at trial. Even if a pocket reexamination does not immediately drive settlement, a grant of reexamination, or an Office Action that is adverse to the patent claims,

¹⁰³ *Reexamining Inter Partes Reexamination*, Institute for Progress (April 2008).

¹⁰⁴ See Reexamination Control Nos. 95/000,006, 95/000,009, 95/000,015, and 95/000,017.

¹⁰⁵ See, e.g., 95/000,006 and 95/000,017 (5 months between Respondent’s Brief and Examiner’s Answer); and 95/000,018 (18 months between Respondent’s Brief and Examiner’s Answer).

especially a final rejection, may improve the accused infringer's settlement negotiating position. Potential requesters should keep in mind, however, that once launched the reexamination bell cannot be unrung.

C. *Litigation Stays*

Because the issue of patent validity is running concurrently in two separate proceedings, judicial economy would seem to counsel a stay of one or the other proceeding in all instances. In reality, this is far from true because each venue is bound by different rules and standards for assessing patent validity. Further, each venue is bound by very different rules and standards for determining whether a stay is appropriate, and each stay decision is highly fact specific. Some general patterns may be discerned, however, and these are described more fully below.

District court judges have inherent and almost unfettered control over their own dockets. A decision to stay a case is reviewed for abuse of discretion—a very difficult standard to overcome on appeal. Further, district court judges have great flexibility in the types of stays they issue. For instance, in one Eastern District of Texas case, Judge Everingham granted a motion to stay the litigation based on the accused infringer's *ex parte* reexamination request. In the order granting the stay, the court crafted a stipulation that the accused infringer must agree not to challenge the validity at trial of the patents-in-suit based on prior art patents or printed publications that were considered in the reexamination proceedings. Ordinarily, these estoppels only apply to *inter partes* reexams, and only after the proceeding has concluded. Further, the accused infringer was barred from directly or indirectly instituting any further reexamination proceedings, despite being statutorily allowed to do so.

Despite this nearly unfettered discretion, however, courts will generally consider at least the following high level factors in making stay determinations: (1) whether a stay will unduly prejudice or present a clear tactical disadvantage to the nonmoving party; (2) whether a stay will simplify the issues at trial; and (3) whether discovery is complete and whether (or when) a trial date has been set. These broad factors are discussed more fully below.¹⁰⁶

First, a court looks at the extent to which the non-moving party would be prejudiced in delaying the litigation. Inherent in this factor is consideration of reexamination pendency. Further, as noted above in the Hot Topics, the extent to which the parties are competitors should be considered carefully. In certain instances, the district court will mitigate any potential prejudice to the patentee by requiring a stipulation that the accused infringer will not challenge the patent on grounds considered during reexamination. By doing so, the court reasons, the patentee “is afforded both the advantage of *ex parte* proceeding and an estoppel effect.”

Second, courts take into account the possibility of simplifying issues with a stay. Under this factor, the status of the reexamination is often considered. The further along the reexamination, the more likely a stay will be granted. Typically, stays are rarely granted on the basis of the reexamination grant and at least a first office action rejection is required. Of course, potential invalidation of the only patent-in-suit would simplify many issues, but cases are often more complicated. For example, an accused infringer may have a strong case for patent invalidity based on statutory subject matter or an on-sale bar. Reexaminations may not be instituted on this basis and the court may still, therefore, have to determine patent invalidity on these grounds if the patent survives reexamination on the prior art. As the PTO develops more information about the reexamination process, in particular the statistics of *inter partes* reexamination, courts will be better able to make an informed decision as to whether a stay will simplify a subsequent trial.

Finally, the court asks if discovery is complete and whether trial dates have been set. Judicial economy naturally favors requests made early in the litigation. Therefore, in view of (1) and (2)

¹⁰⁶ For a thorough and nuanced stay analysis, see Judge Selna's decision denying a motion to stay *Allergan Inc. v. Cayman Chemical Co.*, SACV 07-01316-JVS (CDCA April 9, 2009).

above, any patent challenger hoping to stay the more costly district court litigation should strive to get its reexamination filed as soon as possible and to request a stay of a co-pending litigation as soon as feasible. Denials due to premature requests are usually without prejudice and stay requests can be renewed based on developments during reexamination.

Of course, reexamination pendency remains a big factor. Consider this extreme example of a litigation stayed pending an *inter partes* reexamination: In July 2002, Harry Shannon filed an *inter partes* reexamination request (Control No. 95/000,005) challenging the validity of patent asserted in a patent infringement litigation in the Middle District of Florida (*Enpat, Inc. v. Shannon, et al*, 6:02-cv-00769). In September 2002, the District Court stayed the litigation pending a final decision on the validity of the claims by the PTO. In the reexamination proceeding, the right of appeal notice was issued by the CRU in August 2005, following an action closing prosecution. The appeal has yet to be decided by the BPAI. In May 2004, the district court directed administrative closure of the case pending final decision by the PTO. In that order, the parties were required to provide periodic status reports on the reexamination proceeding to the district court. In February 2005, the plaintiff Enpat filed an unopposed motion to dismiss the case without prejudice due to the pending reexamination request.

Judges deciding a motion to stay, or presiding over a concurrent litigation stayed pending a reexamination, may consider contacting the CRU.¹⁰⁷ The authors have been informed that calls from judicial clerks to the PTO have occurred. Some commentators argue that this ability to contact the CRU when deciding a motion to stay is a valuable tool to a judge deciding whether to grant a stay motion. What restrictions, if any, should be placed on communications between federal judges and CRU officials? Should these communications be limited strictly to procedural details or as fellow government officials should judges be provided less restrictive communication? These questions remain open.

If a party is successful in obtaining a stay in the district court litigation pending resolution of a reexamination, that fact immediately should be brought to the attention of the CRU. The CRU has set forth procedures to increase the pace at which reexaminations involved in concurrent litigations are handled. For example, in situations where a stay is granted in a concurrent litigation, the PTO will take up a reexamination request within six weeks of filing and “all aspects of the proceeding will be expedited to the extent possible.”¹⁰⁸ It is therefore critical for parties to keep the CRU informed of the status of the concurrent litigation.

Stays are also technically available in reexaminations. Unlike the district courts, however, the PTO does not have an unfettered ability to control its docket. The rules provide the ability for the patent owner to request a stay.¹⁰⁹ Generally, the PTO has been unwilling to grant such stay requests due to the statutory mandate to handle reexaminations with special dispatch. However, in an *inter partes* reexamination, the PTO may be amenable to a stay where the reexamination proceeding is at its beginning stages, the litigation is near a final resolution, and estoppel would render all issues in the reexamination moot when the litigation becomes final. To avoid a possible stay of the reexamination proceeding, the requester should file a reexamination request as early as practical in a concurrent litigation.

Finally, the Federal Circuit will not likely issue a stay of any case before it. If an appeal arrives from the BPAI, the Federal Circuit will rule and any decision adversely affecting the validity of any patent claim would trump any district court decision to the contrary. If an appeal from the district court arrives first, the Federal Circuit will likewise rule on the district court case. The PTO would be bound by any ruling invalidating a claim, but the reverse is not true. An unsuccessful validity challenge in the district court is not binding on the PTO as it reviews patent validity under different standards. To the extent that the cases arrive simultaneously at the Federal Circuit, the court

¹⁰⁷ The Office of Patent Legal Administration has a hotline for questions dealing with “Reexamination and Reissue legal and policy guidance.” The number is (540) 772-7703. The authors have found the staff to very helpful and responsive to all manner of requests.

¹⁰⁸ MPEP Section 2686.04.

¹⁰⁹ See 37 C.F.R. Sections 1.565(b) and 1.987.

may review the BPAI decision first. For instance, the Federal Circuit was presented in an appeal from a district court decision and from the BPAI on the same patent.¹¹⁰ In the district court decision, a jury awarded over \$85 million for Hitachi's infringement of its patent. In a parallel decision, the BPAI found the patent to be invalid as obvious. Both appealed to the Federal Circuit. The Federal Circuit first heard the appeal from the BPAI and affirmed the patent's invalidity in a precedential decision. The Court then vacated the district court's decision and remanded for dismissal.

In the end, the best source for how a particular district court judge will deal with a motion to stay is local counsel. Local counsel should have their finger on the pulse of the court and its judges at any moment in time. For the PTO, stays are highly unlikely given the statutorily imposed mandate to deal with reexaminations with special dispatch. Finally, the Federal Circuit likely will deal with appealed cases as they are presented to it, without issuing any stay. This is especially true where the BPAI decision arrives prior to, or simultaneously with, a district court decision.

D. Impact on Trial¹¹¹

Can the existence of or developments in the reexamination proceeding, such as a final rejection of the claim(s) in suit, be brought to the attention of the jury, or is this inadmissible because it is too prejudicial? One patent litigator shared with the authors that her mock jury research indicated that the mere knowledge by the jury of the existence of the reexamination reduced the likelihood that the jury would find invalidity because it assumed that the PTO, the administrative agency expert in deciding validity, now had assumed responsibility for this issue. In effect, the jury would "punt" on the invalidity issue. Assuming this jury research is reproducible, it further argues that the judge should be concerned about the prejudicial impact on the jury of any information about the existence of or developments in the reexamination. Indeed, the possibility that unexpected developments in the reexamination could be admissible at trial has been the basis for some trial counsel choosing not to seek reexamination even when there is strong prior art.¹¹²

However, at least one district court decision deemed non-final reexamination proceedings to be too prejudicial to present to a jury.¹¹³ In that case, the court ruled that "without any [final] conclusions of the PTO to rely upon, evidence that the PTO is currently reexamining the patent may work to unduly alleviate Defendants' 'clear and convincing' burden for both invalidity and willfulness in front of the jury." Similarly, the Federal Circuit recently recognized that "a requester's burden to show that a reexamination order should issue from the PTO is unrelated to a defendant's burden to prove invalidity by clear and convincing evidence at trial."¹¹⁴ If the trend of these recent decisions continue, it may be difficult to get any evidence at all related to reexamination proceedings before a jury.

Finally, some trial counsel take the view that, if the prior art is not successful before the CRU, it will be even less successful before the court. This is based on the use of *KSR* at the PTO, the broader claim construction rules at the PTO, and the lower burden of proof of invalidity at the CRU. To put it in sound bite terms – "If you can't win it at the CRU, then you have even less chance to win it in court." Such counsel take this view particularly in jurisdictions having a reputation for upholding the validity of patents.¹¹⁵

¹¹⁰ *In re Translogic Tech., Inc.*, 504 F.3d 1249 (Fed. Cir. 2008).

¹¹¹ This is a "hot topic" based on discussions with many top trial counsel. While it is still anecdotal, it appears that the more "trial experienced" the counsel is, the less she is concerned that the existence of or developments in a concurrent reexamination will be allowed by the judge to be brought to the attention of the jury. We solicit feedback on this topic.

¹¹² This concern seems to be intertwined with several factors. The first is that many judges have little practical knowledge about reexaminations and what really happens at the CRU or the BPAI. They could be "easily swayed" by initial developments from the CRU, whether it is rejection of all of the claims or allowance of some of the claims in suit in the first office action. The second is that some judges would like to defer to the PTO the validity issue. The third is the possibility of a litigation stay, which if granted initially and then lifted later could present a dilemma in explaining to the jury why there has been a time delay in the suit.

¹¹³ *Microsoft Corporation et al. v. Commonwealth Scientific & Industrial Research Organisation*, 6-06-cv-00549 (April 9, 2009 EDTX) (Judge Davis).

¹¹⁴ *Procter & Gamble Co. v. Kraft Foods Global, Inc.*, 549 F.3d 842, 848 (Fed. Cir. 2008).

¹¹⁵ The court of particular interest is the USDCT EDTX. The perception is that most of the judges in this "pro-patent" court resent the intrusion of the reexamination process into their judicial proceeding. Thus, the concern is that if there is a "favorable" development in the CRU for the patent owner, the judge would be more inclined to let the jury know of this development than if there has been an "unfavorable" development. Trial counsel who have faced this issue with these judges observe that there is a low likelihood that the judge will allow any developments in the reexamination to be brought to the attention of the jury because they need to be balanced on such admissibility determinations. As one trial counsel put it in opining that all developments in reexaminations will be excluded from the jury, is that the balanced approach of exclusion will be based on the adage of "what is good for the goose [patent owner], is good for the gander [third party requester]."

E. Damages

Official PTO statistics (provided below) indicate that approximately two-thirds of patents that emerge from reexamination result in some change to their claims—ten percent of claims are canceled outright.¹¹⁶ Where claims are substantively amended, the accused infringers may not be liable for past damages under intervening rights law. This can be crucial where the patent term is short or the accused infringers have clear and inexpensive design-around options.

More specifically, substantive amendments made during reexamination may defeat damages for past infringement under the statutory doctrine of intervening rights.¹¹⁷ A patent owner cannot seek damages for claims that are not substantially identical to the original claims.¹¹⁸ There is no *per se* rule for determining whether a claim is not “substantially identical.”¹¹⁹ The analysis includes examining “the claims of the original and the reexamined patents in light of the particular facts, including prior art, the prosecution history, other claims, and any other pertinent information.”¹²⁰ The determination is a legal one, and a claim is changed if its scope is changed.¹²¹

If a claim is not substantially identical, then a patentee may not seek damages for product sales prior to issuance of the reexamination certificate. If damages have already been awarded, a defendant may seek to have damages vacated since the claims were void *ab initio*. Again, because of the potential impact on damages, reexamination requests should be filed on all patents-in-suit, if possible, and on all the asserted claims.

Accused infringers should consider the following CRU statistics as of March 31, 2009:

- 73% of *ex parte* reexaminations initiated by a third party, reaching the issuance of Reexamination Certificate, resulted in some or all of the claims being canceled or amended. Only 27% survived with all claims being confirmed.¹²²
- 73% of *inter partes* reexaminations completed resulted in all claims being canceled, while 93% resulted in some change to the claims. Only 7% survived with all claims being confirmed.¹²³

A full set of current CRU statistics is included at the end of this paper.¹²⁴

F. Potential Risks for Accused Infringers

The clearest risk for an accused infringer is that at least one asserted patent claim survives the reexamination process unamended and without any adverse prosecution history estoppels. The reexamination may allow the patent owner to have the CRU consider all of the prior art in the litigation and to present arguments and declarations that support patentability of the claims over this prior art. This could include, for instance, possible secondary (objective) considerations of non-obviousness that were not present when the claims were originally prosecuted.

An *ex parte* reexamination may also give the patent owner a significant advantage in dealing with the prior art because, once begun, the third party requester is excluded from the process, while the patent owner can interview the examiner. Although the court can find a patent invalid even if it

116 Some critics assert that there is insufficient granularity in these PTO statistics to reflect situations where some, but not all, asserted claims are either found to be invalid or are substantially amended.

117 35 U.S.C. Sections 252, 307(b), 316(b).

118 *Bloom Eng'g Co. v. N. Am. Mfg. Co.*, 129 F.3d 1247, 1250 (Fed. Cir. 1997).

119 *Laitram Corp. v. NEC Corp.*, 952 F.2d 1357, 1358 (Fed. Cir. 1991).

120 *Id.* at 1362-63.

121 *Tennant Co. v. Hako Minuteman, Inc.*, 878 F.2d 1413, 1417 (Fed. Cir. 1989).

122 As of March 31, 2009, 6743 *ex parte* reexamination certificates have been issued by the PTO. This represents approximately 70% of all *ex parte* reexaminations granted. Recall that *ex parte* reexaminations may also be initiated by request of the patent owner or the PTO Director.

123 As of March 31, 2009, only 55 *inter partes* reexamination certificates have been issued. This represents approximately 10% of all reexamination requests granted by the PTO.

124 The PTO updates these statistics quarterly. See <http://www.uspto.gov/web/patents/cru.html>.

survives reexamination, most judges likely will defer to the presumed administrative expertise of the PTO, CRU, and BPAI.

Further, putting an asserted patent into reexamination could allow the patent owner to correct other defects in the patent, such as potentially ambiguous claim language, antecedent basis problems, or other perceived issues with the claims. This is especially true with newly issued patents where the potential for damages lies in the future, rather than with past damages. In the same vein, patent owners can also add claims during reexamination, provided that the added claims are not broader in scope than the original claims. The added claims could strategically cover aspects of the accused infringing products not included in the issued claim set, although prohibitions against broadening amendments may bar such activity.

Finally, a reexamination request filed early on in the litigation could impact trial. This is especially true where the PTO decisions are favorable to patentability. However, as noted above, there are questions and concerns as to the admissibility of any non-final PTO action at trial.

G. Timing of Reexamination Requests – When to File?

Once a decision is made to proceed with a reexamination strategy, one of the most important considerations is deciding when to file. The timing of a reexamination request ultimately will be determined by the requester's overall goals.

Early filing should be considered where the goal is to stay a more costly district court litigation until the validity of the asserted patent is adjudged by the PTO. Most courts will not consider staying the litigation until at least a first office action rejection is received. Statistics indicate that the issuance of the first office action could be one year or more after the request is granted and a filing date is accorded in an *ex parte* reexamination request. In an *inter partes* reexamination, the rules state that “[t]he order for *inter partes* reexamination will usually be accompanied by the initial Office action on the merits of the reexamination.”¹²⁵ In the authors' experience, however, this is not always the case, particularly with the increased popularity of *inter partes* reexaminations in the past two years.

Early filing is also highly recommended where the reexamination is launched as an insurance policy against an adverse district court decision. Overall, at least two years are typically necessary for a final decision from the CRU¹²⁶—waiting too long to file a request could reduce the effectiveness of such a strategy. For such strategy, keeping tabs on the trial date is a must.

Sometimes, seeking a litigation stay is not feasible. Further, there is always a chance that an adverse decision by the CRU could have a negative impact on trial. In such cases, it may be desirable to delay reexamination filing to a point somewhat less than one year prior to trial. This mitigates the chance of an adverse CRU decision impacting trial, but may still be early enough for the reexamination to have a positive impact.

In some cases, parties have waited until after an adverse trial decision to file a reexamination request. Appeals to the Federal Circuit are notoriously uncertain, and a remand on an issue of claim construction or damages, for example, could result in a new trial on those issues. In this case, a reexamination may have time to run its course prior to a subsequent final decision or appeal.

Finally, reexaminations should also be considered as a settlement tool. Early preparation of a “pocket reexamination” to show to the patent owner could help drive negotiations in favor of an accused infringer. Even if the reexamination is not immediately filed, the efforts in preparing the pocket reexamination are directly applicable to an accused infringer's invalidity case and would likely not be wasted.

¹²⁵ 37 C.F.R. Section 1.935.

¹²⁶ The CRU has indicated an internal goal of 24 months from instituting the *inter partes* reexamination request to final office action.

Given the above timing considerations, the authors recommend considering the following factors:

1. What overall goals should a reexamination strategy accomplish?
2. When is the trial scheduled and how firm is the trial date?
3. How has the court reacted to reexaminations in the past?
4. How strong is the prior art and are there one or more SNQs to support one or more proposed grounds of rejection?
5. Are *all* of the asserted claims subject to an SNQ?
6. How complicated is the invalidity case and what are realistic chances of success before a jury or judge?
7. Are there pertinent dates on the discovery docket that might counsel delay in filing—*e.g.*, after close of discovery to ensure all discovered prior art is included or after inventor depositions?

One additional consideration was raised in a recent Federal Circuit decision where a party attempted to obtain relief from a final judgment under FRCP 60(b)(6) based on alleged disclaimers made during post-trial reexamination.¹²⁷ In this case, the accused infringer waited until the district court's entry of judgment to file its reexamination request. The reexamination had progressed to a point where the patent owner had to respond to an office action rejection. In that response, the patent owner allegedly made "representations to the [PTO]" the "limited the scope" of one of the accused claims.¹²⁸ The district court denied the Rule 60(b)(6) motion stating that the accused infringer "waited until after judgment in this case to file its Petition for Reexamination, while simultaneously failing to appeal the jury's finding of validity."¹²⁹ Because Rule 60 motions are reviewed under an abuse of discretion standard and typically require "extraordinary circumstances," the Federal Circuit affirmed the decision.

Nonetheless, the authors can envision circumstances where a motion under Rule 60 might be granted. For instance, if the reexamination is timely filed and the patent owner voluntarily amends the asserted claims, or the asserted claims are finally declared invalid, after a final judgment is reached in the district court on the original claims, it seems relief from such a final judgment would be warranted. We are not aware of such a case, but relief under Rule 60 opens another potential window of time where a positive reexamination result could be useful.

H. Multiple Ex Parte Reexamination Requests

Where a party has a choice in filing an *ex parte* or *inter partes* reexamination request, what considerations go into the choice? One factor to consider is that there is no legal limit on the number of *ex parte* reexamination requests that can be filed. However, the bar for establishing a valid SNQ may become higher with each reexamination request. Because the Examiner makes a determination whether a reference raising an SNQ is cumulative to earlier considered art, the more references already considered raises the bar for references in subsequent reexamination requests.

In what situations should multiple *ex parte* reexamination requests be considered? The ability to file more than one request can be a valuable tool where the patent owner is seen to

¹²⁷ *Amado v. Microsoft Corp.*, 517 F.3d 1353 (Fed. Cir. 2008).

¹²⁸ *Id.* at 1363.

¹²⁹ *Id.*

mischaracterize the prior art, to make inconsistent statements between the reexamination and the parallel court proceeding, or where there is newly discovered prior art that surfaces after the previous reexamination request has been filed.

Another factor to consider is the impact that multiple or “rolling” reexamination requests may have on a district court judge. Could multiple reexamination requests impact an already granted litigation stay? At least one district court precluded an accused infringer from filing further *ex parte* reexamination requests as a condition of granting its motion to stay a litigation on the eve of trial.¹³⁰ The ability to file subsequent reexamination requests may be an important tool in an overall *ex parte* reexamination strategy and relinquishing that ability should be carefully considered.

On March 1, 2005, the PTO issued the “Notice of Changes in Requirement for a Substantial New Question of Patentability for Second or Subsequent Request for Reexamination While an Earlier Filed Reexamination is Pending.” In the Notice, the PTO set forth a new policy:

Under the new policy, the second or subsequent request for reexamination will be ordered only if that old prior art raises a substantial new question of patentability that is different than that raised in the pending reexamination proceeding. If the old prior art cited (in the second or subsequent request) raises only the same issues that were raised to initiate the pending reexamination proceeding, the second or subsequent request will be denied.

. . . Further, 35 U.S.C. 303(a) states “[w]ithin three months following the filing of this title, the Director will determine whether a substantial new question of patentability affecting any claim of the patent concerned is raised by the request.” It is reasonable to interpret this provision as requiring each request for reexamination to raise its own substantial new question of patentability as compared not only to the original prosecution (in the application for the patent) and any earlier, concluded reexamination proceedings, but to pending reexamination proceedings as well.

Id.

When faced with the specter of multiple reexamination requests, a patent owner may consider filing a petition with the PTO arguing that subsequent reexamination requests are being filed for the purposes of harassment or to delay prosecution of a pending request.¹³¹ If the prior art provided in the subsequent request unquestionably presents a new SNQ, the petition may not have a high likelihood of success. However, when coupled with an argument that the SNQs in the subsequent reexamination requests are cumulative, these petitions may be successful. This should also be a consideration when determining whether to file multiple reexamination requests.

I. Additional Strategic Questions to Consider

1. Withholding of prior art

Should an accused infringer withhold prior art from a reexamination request? If the reexamination request was an *ex parte* request, such art could become the basis for subsequent reexamination requests, if necessary and non-cumulative. If the reexamination request was an *inter partes* request, the withheld art may still be available for use at trial. Estoppel does not attach to the withheld [or applied] art until a final decision is reached in the *inter partes* reexamination proceeding.¹³² Therefore, in litigation with concurrent *inter partes* reexamination proceedings, the

¹³⁰ See *Visto Corp. v. Research in Motion Ltd.*, No. 2-06CV-181 (E.D. Tex. complaint filed Apr. 28, 2006).

¹³¹ See MPEP Section 2240.

¹³² 35 U.S.C. Section 317(b).

withheld [or applied] art could be “ripped” from the litigation if the reexamination finishes before the litigation, and *vice versa*.

The authors are aware of some district court judges who have crafted stays to preclude the third party requester from using art that could or should have been brought during the reexamination proceeding. Also note that there are express limitations regarding subsequent submissions of prior art in *inter partes* reexaminations.

Further, the trial team may be subject to the PTO’s duty of disclosure requirements, as discussed above.¹³³ If the withheld art was disclosed during the litigation, for example as part of the accused infringer’s invalidity contentions, then the patent owner or the patent owner’s reexamination team may have the ability, or indeed the duty, to submit that withheld art and have it considered during the reexamination. One question to consider is whether the litigation team’s knowledge of material prior art could be imputed to a patent owner. In short, many traps exist for the unwary, and patent owners must take care to avoid conduct that could result in inequitable conduct charges.

2. Experts’ independence

Should technical or legal experts have access to reexamination requests not yet filed prior to preparing reports? Also, do experts have a role in preparing a reexamination request? It is becoming increasingly clear that post-*KSR* obviousness battles will likely require expert testimony in the form of affidavits or declarations. Care must be taken by both parties to a litigation that expert testimony in the form of affidavits in the reexamination before the PTO is consistent with any expert testimony or reports to be used at trial, and *vice versa*. A potential impeachment or inequitable conduct minefield awaits the uninformed.

Another question to consider is whether an expert is an “individual associated with the patent owner” in the context of the Rule 56 duty of disclosure. Put differently, does a patent owner have the duty to inquire of their experts if they know any references that should be cited?

3. Privilege issues

Is there a waiver of privilege when a PTO submission, prosecution event, or meeting uses litigation work product or reveals trial strategy? The patent owner has an obligation to inform the PTO of any concurrent district court litigation in *ex parte* and *inter partes* reexaminations. While the CRU monitors the concurrent litigation, it is prudent for the patent owner to view this as an ongoing duty. For *inter partes* reexamination, any person can file a paper notifying the PTO of a concurrent proceeding.

If a party thinks information must be disclosed, the protective order should specify procedure for the parties to “meet and confer” to resolve any disclosure issues. If parties cannot agree, then the issue may need to be raised to the presiding judge. One way to protect information that a party feels must be disclosed, but is designated under the protective order, is filing the information under seal at the PTO with a petition to expunge at the conclusion of the proceeding.¹³⁴ The PTO specifies detailed procedures for filing information under seal in pending applications. The information to be protected is submitted in a labeled, sealed envelope. A petition to expunge the information accompanies the sealed documents. If the examiner does not believe the sealed information is material to patentability, the petition is granted and the information is expunged from the file. If the information is deemed material to patentability, the petition is denied, the information will become part of the application record, and the information will be available to the public.

¹³³ See 37 C.F.R. Sections 1.555, 1.933; see also Section II.A.3., *supra*.

¹³⁴ See MPEP Sections 724.04 - 724.06.

It is important to note, however, that the information filed under seal may be made public at the conclusion of the reexamination process. Therefore, the court and the party owning the confidential information should be involved in the decision to disclose and how the disclosure is made to the PTO.

4. *Fast courts versus slow courts*

How might the perceived speed of a court affect a decision to file a request for reexamination? Since the average pendency of a reexamination through the CRU, the BPAI, and the Federal Circuit is 48 to 96 months, is the vehicle of reexamination more suitable for a slow court? As noted herein, the timing of a reexamination request depends on the requester's overall goals. If the purpose of a threatened reexamination is to drive settlement, then the speed of the court is irrelevant. If the goal of the reexamination request is to stay the litigation, then speed of request is paramount.

ITC patent actions are notoriously fast and bear some special attention. As most readers are aware, ITC investigations proceed more quickly than district court actions. Some reports indicate that an ITC investigation is generally completed within 15 months, whereas the average patent litigation in district court takes approximately 22 months.¹³⁵ In the past, the speed with which the ITC had to proceed was strictly mandated by statute. Since the statute was amended in 1994, the ITC now must "conclude any such investigation and make its determination under this section at the *earliest practicable time* after the date of publication of notice of such investigation."¹³⁶

Due to this statutory mandate for a swift investigation, it should not be surprising that the ITC is hesitant to stay its investigations. One recent ITC case confirms the ITC's reluctance. In this case, the presiding administrative law judge ("ALJ") granted a stay pending reexamination of the patents-in-suit.¹³⁷ On appeal to the Commission, the stay was rejected, and proceedings were reinstated. The defendant petitioned the Federal Circuit for a *writ of mandamus* that the stay be reinstated. The Federal Circuit refused to reinstate the stay, finding that the Commission had justified its action and that hardship, inconvenience, and avoidance of a particularly complex trial are not sufficient reasons to grant *mandamus*.

At the same time, however, the ITC has not adopted any *per se* rule regarding staying an investigation in light of a concurrent reexamination at the PTO. Rather, the ALJ will weigh several factors, including: (1) the stage of discovery and the hearing date; (2) the issues in question and trial of the case; (3) the undue prejudice or clear tactical disadvantage of any party; (4) the stage of the reexamination at the PTO; (5) the efficient use of ITC resources; and (6) the availability of alternative remedies in federal court.¹³⁸ In certain instances, the ALJ will extend the target date for completion of the investigation in view of a concurrent reexamination proceeding.

Because of the speed with which the ITC conducts its investigations, litigants should expect an ITC investigation to proceed on its normally rapid pace with a low likelihood that the ALJ will stay the investigation.

5. *Cases with multiple defendants*

In cases with multiple accused infringers, how should a patent owner deal with reexamination threats by a single defendant, or a plurality of defendants? For the multiple defendants contemplating a reexamination strategy, what if the defendants are not of a single mind when it

¹³⁵ See Vivek Koppikar, *Evaluating the International Trade Commission's Section 337 Investigation*, 86 J. PAT. & TRADEMARK OFF. SOC'Y 432, 433 (2004).

¹³⁶ 19 U.S.C. Section 1337(b)(1) (emphasis added); see also 19 C.F.R. Section 210.2 ("It is the policy of the Commission that, to the extent practicable and consistent with requirements of law, all investigations and related proceedings under this part shall be conducted expeditiously. The parties, their attorneys or other representatives, and the presiding administrative law judge shall make every effort at each stage of the investigation or related proceeding to avoid delay.")

¹³⁷ *In re Freescale Semiconductor, Inc.*, Misc. No. 875, 2008 WL 2951399 (Fed. Cir. June 25, 2008) (non-precedential) (order denying "petition for a writ of mandamus to direct the [ITC] to vacate its opinion denying petitioner's motion for stay pending reexamination of the patents at issue" in Investigation No. 337-TA-605).

¹³⁸ *In re Certain Personal Computer/Consumer Electronic Convergent Devices, Components Thereof and Products Containing Same*, Inv. No. 337-YA-558, ALJ Order No. 6, 2006 ITC Lexis 52, at *12-*22 (U.S.I.T.C. Feb. 7, 2006) (order granting temporary stay).

comes to reexamination strategy? Should reexamination be explicitly dealt with in any joint defense agreement? Again, any reexamination request can be timed so that it will not likely affect any trial proceedings. A requester could further allay fears by committing to the other non-participating defendants not to request a litigation stay should the claims be rejected by the PTO. Of course, a consensus strategy is most desirable, but nothing is likely to bar a single defendant from launching a reexamination request if it believes its interests are best served by doing so.

One final consideration is how the “real party in interest” rule is addressed in multiple-defendant cases, as discussed above. Do the requester’s non-participating co-defendants fall under the estoppel provisions? If not, could the same art be “litigated” at the PTO and at the district court by these non-participating defendants?

6. The judge’s perception of reexamination requests

Might a judge view a reexamination request as usurping the judge’s authority? Does it help if the reexamination request is submitted by counsel not associated with trial counsel? Keep in mind that *ex parte* reexamination requests may be filed anonymously. Could it be in the requester’s interest, where there is co-pending litigation, to anonymously file the reexamination request? Patent owners should consider interrogatory and/or production requests directed to whether the accused infringers have filed a reexamination request or caused a reexamination request to be filed.

Historically, many district court judges viewed reexaminations, particularly *ex parte* reexaminations, with disbelief and have been reluctant to grant stays especially if their court operates on a “fast track.” More recently at Sedona discussions, some judges have expressed the view that they may rethink their approach in the future now that the CRU has been created and the PTO statistics seem to indicate prompt processing of reexaminations and a high probability of the reexamination resulting in some or all of the claims being found unpatentable. However, other judges are troubled by the time delay of reexaminations.¹³⁹ Litigants thus should pay special attention in the court filings relating to stays to explain the current reexamination environment.

7. Impact on laches

Do reexamination proceedings or the issuance of a reexamination certificate have any impact on the six-year statutory laches provisions of 35 U.S.C. Section 286. A recent decision by the Federal Circuit seems to indicate that a reexamination certificate will not restart or impact the six-year laches presumption for enforcing an issued patent.¹⁴⁰

8. Duty of disclosure

It is clear that the patent owner remains under a duty of disclosure while the patent is in reexamination proceedings under 37 C.F.R. Sections 1.555 and 1.933. Further, a third party requester participating in an *inter partes* reexamination owes a duty of candor and good faith to the PTO under 37 C.F.R. Section 11.18. The ongoing duty of disclosure for the patent owner raises some interesting strategic questions that we consider below.

For instance, who should handle the reexamination? Options include using patent attorneys from the trial team, or prosecution attorneys from the litigating law firm. Alternatively, outside patent attorneys or patent attorneys inside the patent owner’s company could be used. Critical issues to consider include efficiencies, maintenance of privilege, and perhaps most importantly, compliance with protective orders. Best practices may warrant use of outside patent attorneys for the prosecution of the reexamination who are walled off from the litigation team, especially where the protective order includes a non-prosecution clause.

¹³⁹ See Order Denying Sun Microsystems, Inc.’s Renewed Motion For Partial Stay in *Network Appliance Inc. v. Sun Microsystems, Inc.*, United States District Court for Northern District of California (C-07-06053), issued November 4, 2008, (citing Sedona PL08 version of this paper).

¹⁴⁰ See *Serdarevic v. Advanced Med. Optics, Inc.*, 87 U.S.P.Q.2d 1481, 1484-85 (Fed. Cir. 2008) (holding that the presumption of laches applied against inventorship claim despite intervening reexamination proceeding).

Another strategic question is determining what to cite to the CRU. The MPEP requires citation of “patents or printed publications which (A) are material to patentability in a reexamination proceeding, and (B) which have not previously been made of record in the patent file.”¹⁴¹ Validity decisions in reexamination may not be made on the basis of fraud on the Office, or on the basis of prior use or sale. Therefore, the patent owner arguably has fewer categories of potentially relevant material to cite to the PTO. However, it appears as if the obligation remains to disclose the same broad scope of prior art printed publications as would be the case in the original prosecution.¹⁴²

However, because the prevalence of inequitable conduct charges in patent litigation remains unabated,¹⁴³ many reexam practitioners reasonably err on the side of caution in preparing information disclosure statements. For instance, in the recent case of *Larson Mfg. Co. v. Aluminart Prods. LTD.*,¹⁴⁴ the district court found a reexamined patent to be unenforceable for failure to cite information from a related copending application. Specifically, the patent owner failed to cite a number of references applied in the copending application, as well as two office actions where the application examiner had considered the same art as the CRU examiner. The Federal Circuit overturned the inequitable conduct charge finding that the uncited references were cumulative. But in doing so, the Court also determined that the office actions *were* material. The case was remanded to consider whether the requisite intent was present as to the uncited office actions. There was no mention by the Court of the fact that the MPEP does not appear to require citation of material “previously ... made of record in the patent file.”

Arguably the patent owner is required in the reexamination to disclose the same broad scope of prior art as would be the case in the original prosecution. The result of cases such as *Larson Mfg.* is that the filing of an IDS of voluminous length citing all types of prior art uncovered in the course of a concurrent patent litigation are regularly filed in reexamination proceedings—filings that include re-citation of all the art previously filed in any parent or otherwise related applications, during regular prosecution. Where a patent owner feels compelled to cite material that may not be strictly required by the MPEP, it may simplify matters for the CRU. There are many examples of IDS filings in reexaminations where hundreds and hundreds of possible prior art items disclosed during a concurrent litigation are dumped on the CRU by using separate IDS pleadings for different categories of information. For instance, one pleading may clearly cite to art previously cited during original prosecution of related applications, while a second pleading may cite to art newly discovered during the concurrent litigation or ITC investigation. The CRU examiner can then more easily discern what she may consider relevant to a particular case.

Yet another strategic question revolves around what information to cite from a co-pending district court litigation or ITC investigation. The MPEP states that the duty of disclosure under Rule 555 “is consistent with the duty placed on patent applicants” by Rule 56. In that regard, Rule 56 requires citation of “[i]nformation from related litigation.”¹⁴⁵ Such information includes “pleadings, admissions, discovery including interrogatories, depositions, and other documents and testimony.”¹⁴⁶ Such categories of information may include assertions that are contradictory to assertions made to the examiner. Where there are concurrent litigation or ITC investigation proceedings, these classes of information must be continually monitored and cited to the office where relevant. Again, because of the prevalence of inequitable conduct charges, many practitioners err on the side of caution and are reasonably over-inclusive in this regard. If information is cited that is beyond the scope of the reexamination proceedings—e.g., information related to allegations of prior sale or use—the CRU will simply note the issue as unresolved.¹⁴⁷

141 MPEP Section 2280.

142 See MPEP Section 2280 and 2684.

143 *Larson Mfg. Co. v. Aluminart Prods. LTD.*, 559 F.3d 1317 (Fed. Cir. 2009) (“The ease with which inequitable conduct can be pled, but not dismissed, is a problem of our own making.”) (Concurring Opinion) (J. Linn).

144 *Id.*

145 MPEP Section 2001.06(c).

146 *Id.*

147 MPEP Section 2280.

However, the reexamination proceeding is strictly limited to considering prior art in the categories of patents, printed publications and admissions, and cannot address other forms of prior art such as public use, offer for sale, public knowledge, etc. Considerable CRU resources are wasted by Examiners considering art that cannot form the basis of a rejection of the original issued claims in a reexamination.¹⁴⁸ However, only submitting patents and printed publications in an IDS does not relieve the patent owner and its reexamination attorneys of the risks of violation of the duty of disclosure and possibly committing inequitable conduct.

Further, 37 C.F.R. Section 11.18 requires the patent owner's reexamination attorneys to conduct a reasonable inquiry of submissions to the PTO, which means that some level of review of each prior art submission should be done prior to filing. Currently, it seems that due to the risk of inequitable conduct, patent owners are erring of the side of voluminous IDS filings and are not culling out possible prior art that does not fit into the categories of patents, printed publications, and admissions.

Throughout the *inter partes* reexamination proceeding, the patent owner also has an obligation to "call the attention of the Office to any prior or concurrent proceedings in which the patent is or was involved, including but not limited to interferences, reissue, reexamination, or litigation and the results of such proceedings."¹⁴⁹ Additionally, any party may file a paper in an *inter partes* reexamination proceeding notifying the Office of the same. How much information is a party required to submit from a concurrent litigation? Is bare notice of a concurrent proceeding sufficient to meet the obligation imposed by Rule 985? Many patent owners are submitting voluminous court documents from concurrent litigation. Many of these documents would not qualify as prior art during original prosecution or reexamination prosecution.

One unresolved issue in this regard is the extent to which the duty of disclosure under Rules 555 and 933 would apply to a patent owner's trial team. What if the trial team is completely barred by the protective order from participating in the prosecution of a concurrent reexamination? How high and impervious must the wall be between the trial team and the reexamination team to avoid implicating the duty of disclosure rules? What if one or more members of the trial team are registered patent attorneys? What disclosure obligations does a patent owner have, and can these obligations be avoided by remaining intentionally ignorant of prior art or other potentially relevant information that is confidentially disclosed over the course of the litigation?

These are very important questions as the trial team is likely to become aware of material prior art or other material information either through its own investigation or simply through the accused infringer's disclosure of its invalidity contentions. At least one recent district court decision suggests that the duty of disclosure does NOT trump a trial attorney's obligations under the protective order to maintain the confidentiality of protected information.¹⁵⁰ As a final matter, while possibly not under the same duty of disclosure as a patent owner, the requester nonetheless has the duty of candor during the PTO proceeding, as that Rule 11.18¹⁵¹ applies equally to both reexaminations and all other proceedings before the PTO.¹⁵²

V. BASIC REEXAMINATION PRACTICE

A. Generally

As noted above, reexamination can be *ex parte* or *inter partes*. In *ex parte* reexamination, a third party requester will receive copies of office actions and patent owner replies, but cannot

¹⁴⁸ If a Patent Owner chooses to add new claims or amend claims during a reexamination proceeding, the added language is subjected to a broader examination, similar to that of an examination of an original application. For example, the new claim or new limitation is considered for compliance under 35 U.S.C. Section 112. See MPEP Section 2258.II. Furthermore, some practitioners argue that non-patent, non-publication prior art (e.g., prior use, prior offer for sale) is material to new claims and/or new limitations added during reexaminations.

¹⁴⁹ 37 C.F.R. Section 1.985; see also Section 1.565 for similar *ex parte* rule.

¹⁵⁰ See Hot Topics Section C.

¹⁵¹ 37 C.F.R. Section 11.18.

¹⁵² The uncertainty between the required and also preferable bounds of the duty of disclosure in reexaminations and the ever present specter of a violation of the duty of disclosure, where even many at the PTO will say they do not know where the real lines are, is argued by some as just another example of why significant change in the law of inequitable conduct (or the duty of disclosure) needs to occur, whether by court decision or legislative change.

otherwise participate in the reexamination proceeding, and cannot appeal PTO decisions. In *inter partes* reexamination, when the patent owner submits a reply to an office action, the third party requester is entitled to file comments in response thereto. The third party's comments must, however, be limited to issues raised by the office action or in the patent owner's response. The third party requester is entitled to certain appeals, but is also subject to certain estoppels. Both *ex parte* and *inter partes* reexaminations are discussed below.¹⁵³

In order to assure timely delivery of papers, both the third party requester and patent owner should provide the PTO with current correspondence address information. In the past, both the patent owner and third party requester utilized the same form when changing correspondence address. The use of the same form resulted in situations where the patent owner correspondence address was used by the PTO as the third party requester correspondence address. The PTO has recently introduced a "Patent Owner Change of Correspondence Address" form, and a separate "Third Party Requester Change of Correspondence Address" to address these concerns.

B. The Request and the SNQ

Rule 1.510(b) sets forth the mandatory elements of an *ex parte* reexamination request, and Rule 1.915(b) sets forth the mandatory elements of an *inter partes* reexamination. Both *ex parte* and *inter partes* reexamination requests require: (1) a statement pointing out each SNQ, and (2) a detailed explanation of the pertinence and manner of applying cited patents and printed publications to every claim for which reexamination is requested.

The SNQ must be based on prior patents and/or printed publications.¹⁵⁴ Other patentability issues, such as prior public use or insufficiency of the disclosure, will not be considered for instituting a reexamination.

The PTO will only reexamine those claims for which a SNQ is alleged and found. The PTO will consider an undated document if it is accompanied by reliable evidence, such as an affidavit or deposition transcripts, supporting an asserted publication date. Where a reference originated with the patent owner, the CRU might consider issuing a request to the patent owner for additional information under 37 C.F.R. Section 1.105. For reexaminations ordered on or after November 2, 2002, a finding of an SNQ, and claim rejections, can be based solely on previously cited/considered "old" prior art, or in combination with other prior art.¹⁵⁵

The request must also include an identification of every claim for which reexamination is requested, and a detailed explanation of the pertinence and manner of applying each of the cited prior art to every claim for which reexamination is requested.¹⁵⁶ Failure to address each submitted reference in the detailed request will result in a denial of a filing date.

It is not uncommon for reexamination requests, particularly *inter partes* reexamination requests, to have hundreds of pages. Some commentators note that such lengthy requests are unduly long and amount to an abuse of the reexamination process. However, other commentators note that, particularly in *inter partes* reexamination where the requester is faced with "use it or lose it" estoppel provision for known references, a third party requester is forced into lengthy requests in order to fully develop all SNQs available when the reexamination request is filed.

The filing date of the reexamination request starts the two-year period in which the PTO strives to issue a final office action or otherwise conclude the reexamination proceeding. The CRU and its staff are known to be hyper-technical in reviewing reexamination requests. Any procedural

¹⁵³ Other practitioners and commentators have provided summaries of the mechanics of reexamination practice. See, e.g., J. Steven Baughman, *Reexamining Reexaminations: A Fresh Look at the Ex Parte and Inter Partes Mechanisms for Reviewing Issued Patents*, 89 J. PAT. & TRADEMARK OFF. SOC'Y 349, 360 (2007); Roger Shang & Yar Chaikovskiy, *Inter Partes Reexamination of Patents: An Empirical Evaluation*, 15 *Tex. Intell. Prop. L.J.* 1 (2006); Sherry M. Knowles, et al., *Inter Partes Patent Reexamination in the United States*, 86 J. PAT. & TRADEMARK OFF. SOC'Y 611 (2004).

¹⁵⁴ 37 C.F.R. Sections 1.510(b)(1), 1.915(b)(3).

¹⁵⁵ MPEP Sections 2242(II)(A), 2258.01(A).

¹⁵⁶ *Id.* Sections 1.510(b)(2), 1.915(b)(3).

defects will cause the reexamination request to be rejected. We recommend close adherence to the guidelines outlined in the MPEP, and to the rules in the C.F.R. We also recommend obtaining publicly available recent requests (*i.e.*, after the latest amendments to 37 C.F.R. Section 1.915 and Section 1.510) that have been successful to use as a template.

C. Ex Parte Reexamination

Ex parte reexamination can be requested by a patent owner or any third party requester at any time during the enforceability of a patent.¹⁵⁷ Subsequent requests for *ex parte* reexamination by a third party requester are permitted, provided the prior art raising the new SNQ is not cumulative to prior art previously considered. Co-pending reexamination proceedings may be merged.¹⁵⁸ The patent owner is not permitted to broaden the scope of claims during *ex parte* reexamination.¹⁵⁹ A third party requester can petition the PTO Director to review a determination refusing *ex parte* reexamination.¹⁶⁰ The Director's decision on the petition is non-appealable, but can be challenged via a district court action.

In response to a grant of *ex parte* reexamination, the patent owner is entitled to file a statement on the new question of patentability, including any proposed amendments the patent owner wishes to make.¹⁶¹ Where the *ex parte* reexamination was requested by a third party, the third party is entitled to respond to the patent owner's statement.¹⁶² This may be one reason why patent owners rarely submit a statement prior to receipt of an office action.

The patent owner is entitled to appeal to the BPAI and to the Federal Circuit with respect to any decision adverse to the patentability of any original, proposed amended, or new claim of the patent.¹⁶³

D. Director-Initiated Ex Parte Reexamination

The PTO Director can institute *ex parte* reexaminations *sua sponte*.¹⁶⁴ Under current PTO practice, the Director can institute a reexamination only upon a finding that a patent brings dispute on the PTO or that a significant procedural error occurred during examination. For example, where a patent examiner failed to consider references submitted in an information disclosure statement during the examination process, despite numerous requests from the applicant, the PTO may independently determine whether the references raise a SNQ. Some argue that since the creation of the CRU, however, the use of Director-initiated *ex parte* reexaminations has ceased based on the belief that the affected public can assume the burden of policing patents that are adverse to them. However, others argue that the lack of Director-initiated *ex parte* reexaminations since creation of the CRU is simply a coincidence.

E. Inter Partes Reexamination

1. Generally

Inter partes reexamination can be requested by any party other than the patent owner and its privies, at any time during the period of enforceability of a patent.¹⁶⁵ *Inter partes* reexamination is only available for patents that issued from an original application filed in the United States on or after November 29, 1999.¹⁶⁶ Until recently, the meaning of "an original application" was not fully settled. The issue was whether an *inter partes* reexamination can be filed on a patent from a continuation

¹⁵⁷ 35 U.S.C. Section 302; 37 C.F.R. Section 1.510.

¹⁵⁸ 37 C.F.R. Section 1.565.

¹⁵⁹ *Id.* Section 1.552(b).

¹⁶⁰ *Id.* Section 1.515(c).

¹⁶¹ *Id.* Section 1.530.

¹⁶² *Id.* Section 1.535.

¹⁶³ 35 U.S.C. Section 306.

¹⁶⁴ 35 U.S.C. Section 303; 37 C.F.R. Section 1.520.

¹⁶⁵ 37 C.F.R. Section 1.913.

¹⁶⁶ *Id.*

application having a filing date on or after November 29, 1999, but which claims priority to a filing before November 29, 1999. The PTO's position was that "an original application" includes any application with an actual filing date on or after November 29, 1999, regardless of whether that application claimed priority to an application filed before that date. The PTO's interpretation was upheld in district court¹⁶⁷ and was subsequently affirmed by the Federal Circuit in *Cooper Techs. Co. v. Dudas*.¹⁶⁸ The practical effect is that only patents whose actual filing date is on or after November 29, 1999, are eligible for *inter partes* reexamination, irrespective of whether the patent's effective filing date is earlier.

As with *ex parte* reexaminations, a third party requester can petition the Director to review a determination refusing *inter partes* reexamination. The Director's decision of the petition is non-appealable.¹⁶⁹

A patent owner is entitled to appeal to the BPAI and to the Federal Circuit with respect to any decision adverse to the patentability of any original or proposed amended or new claim of the patent.¹⁷⁰ A third party requester is entitled to appeal to the BPAI and to the Federal Circuit with respect to any *final* decision favorable to the patentability of any original or proposed amended or new claim of the patent.¹⁷¹

2. Estoppels in *inter partes* reexamination

Estoppels in an *inter partes* reexamination flow two ways—from the *inter partes* reexamination to the civil action, and from the civil action to the *inter partes* reexamination. In a subsequent civil action, a party cannot argue invalidity of a claim finally determined to be valid or patentable on any ground which that party raised or could have raised during the *inter partes* reexamination.¹⁷² The third party is not, however, precluded from asserting invalidity based on newly discovered art that was unavailable to the third party requester and the PTO at the time of the *inter partes* reexamination.¹⁷³ Similarly, once a final decision has been entered against a party in a civil action that the party has not sustained its burden of proving the invalidity of any patent claim in suit, the party and its privies cannot request *inter partes* reexamination on the basis of issues that the third party raised or could have raised in the civil action.¹⁷⁴ It appears from the statute that these estoppels in *inter partes* cases apply only to civil actions brought in the district court under 28 U.S.C. Section 1338 and not to Section 337 ITC investigations. Whether this was an oversight is unknown, but the authors are not aware of any cases for which estoppel has been applied in an ITC investigation.

Once a request for *inter partes* reexamination has been granted, the third party requester cannot file a subsequent request for *inter partes* reexamination while the prior *inter partes* reexamination is pending.¹⁷⁵ Further, once a final decision is granted favorable to patentability of any original, proposed amended, or new claim, the third party requester cannot thereafter request *inter partes* reexamination of such claim on the basis of issues that the third party raised or could have raised in the prior *inter partes* reexamination.¹⁷⁶

Finally, after an *inter partes* reexamination has been instituted, the third party requester is precluded from citing any additional prior art unless it rebuts a finding of the examiner or a response by the patent owner, or if it became known or available after filing the request.¹⁷⁷ There are no estoppels, however, that prevent the third party requester from filing subsequent *ex parte* reexaminations. But the CRU closely examines such subsequent requests with a close eye to whether there is, in fact, a true SNQ.

167 *Cooper Techs. Co. v. Dudas*, 85 U.S.P.Q.2d 1465 (E.D. Va. 2007) (Brinkema, J.).

168 *See Cooper Techs. Co. v. Dudas*, No. 2008-1130, slip op. at 2-7 (Fed. Cir. Aug. 19, 2008).

169 37 C.F.R. Section 1.927.

170 35 U.S.C. Section 315(a).

171 *Id.* Section 315(b).

172 35 U.S.C. Section 315(c).

173 *Id.* Section 315(c).

174 35 U.S.C. Section 317(b).

175 *Id.* Section 317(a).

176 *Id.* Section 317(b).

177 *Id.* Section 1.948.

F. Mergers of Concurrent Proceedings

1. Merger of co-pending reexaminations

Multiple *ex parte* reexaminations on the same patent will generally be merged.¹⁷⁸ However, the decision is at the sole discretion of the Office, which will take into account its statutory mandate of “special dispatch.”¹⁷⁹

If one of the multiple co-pending reexamination requests is *inter partes*, then the merger decision proceeds under the *inter partes* rules.¹⁸⁰ According to the MPEP, merger decisions are made by the Office of Patent Legal Administration (“OPLA”). After multiple reexaminations have been ordered, the CRU will deliver the multiple orders to the OPLA, and OPLA will determine whether and how the reexamination should be merged. OPLA will thereafter issue a merger order that will govern the merged proceedings. The merged proceedings will then proceed under the *inter partes* rules, except that the third party requester will maintain its rights under the *ex parte* rules—e.g., the third party requester would maintain its right to respond to any patent owner’s statement.¹⁸¹ No *ex parte* rights appear to remain with the patent owner, and the right to interview any *ex parte* issues appears to be foreclosed as a general rule. If a party feels its *ex parte* rights have been unfairly terminated by a merger, then it may consider a Rule 181 petition to preserve *ex parte* rights.

2. Merger of co-pending reissue applications and reexaminations

The authors are aware of multiple situations where a patent owner has, upon being subjected to a reexamination request, proceeded to file a reissue application.¹⁸² It is also not unusual for a patent owner to file a reissue application in advance of a lawsuit to clear up any errors or to put a claim set in better condition for litigation. If the reissue application is filed within the two years of the issue date of the patent, a broadening reissue is available.¹⁸³ While a patent owner may not broaden claims during reexamination, a broadening reissue application may preserve that right.

Where a reissue application and a reexamination are co-pending, the PTO may merge the proceedings or suspend one of the two proceedings.¹⁸⁴ It is the general policy of the PTO that the two proceedings will not be allowed to proceed simultaneously without merger or suspension of one or the other.¹⁸⁵ The reason for the policy is to permit timely resolution of both the reissue and the reexamination, and to prevent inconsistent and possibly conflicting amendments. Therefore, even if the parties do not make a specific petition for merger or suspension, the PTO will take action *sua sponte* to prevent parallel proceedings.¹⁸⁶ Because of the statutory mandate to treat reexaminations with “special dispatch,”¹⁸⁷ the PTO should not suspend the reexamination unless there are exceptional circumstances. This is especially true due to the potential for extending prosecution of reissue applications through continuation applications or requests for continued examination.

As with the merger of multiple reexamination requests, the determination to merge or suspend is made by the OPLA, and the decision is made on a case-by-case basis.¹⁸⁸ Factors include: (1) timing (whether reissue was filed first); (2) the statutory mandate to treat reexaminations with “special dispatch”; (3) the fact that the reissue could continue indefinitely via continuation applications; and (4) whether the patent owner consented to a stay of the reissue application. A merger order will typically lay out the ground rules for the merged proceeding to proceed

¹⁷⁸ 37 C.F.R. Section 1.565.

¹⁷⁹ MPEP Section 2283.

¹⁸⁰ 37 C.F.R. Section 1.989.

¹⁸¹ *Id.*

¹⁸² See, e.g., Reissue application no. 11/513,425 and *inter partes* reexamination control no. 95/000,155.

¹⁸³ See 35 U.S.C. Section 251.

¹⁸⁴ See 37 C.F.R. Section 1.565(d) for reissue merger with *ex parte* reexamination and 37 C.F.R. Section 1.991 for reissue merger with *inter partes* reexamination.

¹⁸⁵ MPEP Section 2686.03.

¹⁸⁶ See e.g., merger decision for *inter partes* reexamination control number 95/000,270, which was merged (*sua sponte*) with broadening reissue application serial number 11/703,606; and merger decision for *inter partes* reexamination control number 95/000,269, which was merged (*sua sponte*) with reissue application serial number 11/636,350. Both of these cases involved concurrent district court litigation.

¹⁸⁷ 35 U.S.C. Sections 305, 314(c).

¹⁸⁸ *In re Allain*, 71 U.S.P.Q.2d 1751 (Com’r Pat. & Trademarks Apr. 26, 2004) (non-precedential).

simultaneously. Importantly, jurisdiction of a merged proceeding stays with the CRU, not with the Technology Center reissue examiner.

Where the merger is with an *inter partes* reexamination, the OPLA's merger order strictly limits the third party requester's participation to those issues unique to the reexamination. For example, third party requesters will be strictly prohibited from commenting on the reissue claims or other issues unique to reissue, such as recapture. Further, the merged proceeding will not allow for interviews or extensions of time (except for good cause). Finally, in merged proceedings, the reexamination is terminated upon the issuance of a reexamination certificate.

G. Extensions of Time

Reexaminations must be carried out with "special dispatch."¹⁸⁹ For this reason, patent owners are uniformly given shortened periods of time to respond to office actions on the merits—typically two months, instead of the usual three allowed during original prosecution. Further, because reexaminations are not "applications," the ability to obtain extensions of time under 37 C.F.R. Section 1.136 is foreclosed. Instead, patent owners seeking an extension of time are bound by reexamination Rules 1.560 and 1.956. Under those rules, extensions of time are only given if sufficient cause is demonstrated. Even then, extensions are typically available for only one month barring a showing of extraordinary circumstances.¹⁹⁰

That said, well supported requests are often granted. Factors that appear to warrant extensions of time include, for example, ongoing parallel discovery in a co-pending district court or ITC action. Discovery such as expert reports or inventor depositions that are due during the two month window for responding to the office action may necessitate added time for review and consideration.¹⁹¹ Other factors include the availability of declarants, the need to obtain evidence in support of patentability arguments, and whether reexamination is new to the proceedings. For instance, extensions of time have been granted when reexamination counsel needs to investigate a possible swear behind under Rule 131, or needs to obtain declaratory evidence under Rule 132. The same is true when the need arises to obtain evidence of secondary considerations in rebutting an obviousness rejection.

Another important aspect of any request to extend time is an affirmative showing of what steps the patent owner has taken in responding to the office action. *See* MPEP Section 2265. A detailed showing is required. Only with this showing may the CRU properly balance the need to proceed with special dispatch with the ability of the patent owner to fully respond to the rejections in the office action, and to adequately defend its patent right.

It should also be noted that filing a request for an extension of time does NOT toll the time to respond. Therefore, any requests should be made well in advance of the deadline. The CRU responds to requests in a fairly prompt manner. One recent evaluation shows a mean decision time of 14 days, with a median time of 11 days. The authors have seen the CRU act in as little five days from the request.

If an extension of time is secured for responding to a particular action, any subsequent request to extend for the same action will only be granted if there are extraordinary circumstances, such as incapacitation of reexamination counsel.¹⁹² For responses to subsequent actions, the standard reverts to sufficient cause. Put differently, the term "second or subsequent requests" refers to a second or subsequent request in the context of the particular deadline for which an extension is sought, and not to second or subsequent requests over the course of the entire reexamination. This is important because "second or subsequent" requests are only granted under "extraordinary circumstances."

189 35 U.S.C. Sections 305 and 314(c).

190 *See* MPEP Sections 2265 and 2665.

191 *See* Control Nos. 95/000,285, 95/000,310, and 95/001,018.

192 *See* MPEP Sections 2265 and 2665.

However, based on conversations with two CRU SPEs, if the PTO perceives a pattern of delay, such as where an applicant requests an EOT for every deadline, subsequent requests over the course of an entire reexamination receive closer and closer attention. While not reviewed under the “extraordinary circumstances” standard, these subsequent EOT requests will get closer inspection and may require additional proof than would have been required for a first request.

H. Page Limits For Inter Partes Reexamination Papers

The *inter partes* reexamination rules impose a 50-page limit on Office Action responses filed by the patent owner and written comments filed by the third party requester.¹⁹³ However, there is no corresponding limit set on the size of the reexamination request or the Office Action issued by the Examiner.¹⁹⁴

On one hand, page limits force the prosecuting attorneys to economize their arguments and reduce the number of pages that an Examiner must review in each Office Action cycle. On the other hand, in cases having lengthy and complex Office Actions, these page limits may not afford the patent owner the ability to adequately argue all the issues raised in the reexamination request and/or Office Action.

How can the PTO balance the need for economy while protecting the right of the patent owner to protect its property right? Can the PTO *sua sponte* waive the page limit rule when an Office Action exceeding a specific length is issued?

This issue is exacerbated by the need to create a full and complete factual record of the story of the invention and the relevant prior art to overcome obviousness rejections. In the patent interference context there is the Evidence Appendix that is used to create the factual record and is not counted as part of the page limits for attorney argument. The PTO in the interference context takes a liberal view of what is allowed into the Appendix that often runs thousands of pages in length. Many argue that the CRU should adopt a corresponding approach to the page limit in reexaminations.

VI. CENTRAL REEXAMINATION UNIT (CRU) IMPROVES QUALITY AND REDUCES PENDENCY

A. Dedicated Examiners

In 2005, the PTO created a dedicated Central Reexamination Unit (CRU) to ensure quality and consistency of reexamination proceedings, and to reduce pendency. The CRU handles all reexaminations regardless of technology, and all legacy reexaminations have been transferred to the CRU from their respective technology centers. The CRU is currently headed by a new CRU Director, Mr. Greg Morse, who assumed his new duties on June 23, 2008.

In 2006, the CRU included 31 patent examiners, three supervisory patent examiners, and 10 support staff. When Mr. Morse took over in June 2008, the CRU ranks had grown to a total of 53 patent examiners with 10 in the biological/chemical group, 12 in the mechanical arts, and 31 in the electrical arts. There are now four supervisors, while the clerical staff remains at 10. An announcement has been made that the CRU is looking for seven additional examiners, mostly in the electrical arts. In short, the CRU continues to grow in response to increased use of reexaminations as a viable post-grant vehicle to challenge patent validity.

The examiners in the CRU are selected from the ranks of the PTO examiner corps and have an average of approximately 17 years of examining experience. Many of the CRU examiners also

¹⁹³ 37 C.F.R. Section 1.943(b).

¹⁹⁴ The trend in *inter partes* reexamination appears to be the filing of lengthy reexamination requests. In many cases, the reexamination request exceeds 500 pages. It is not uncommon for the request to exceed 250 pages.

have advanced technical degrees and/or law degrees. The CRU examiners are evaluated on work quality and workflow, not on production quotas, as is the case with the regular examiner corps. Assignment to the CRU is recognized throughout the PTO as professional advancement; morale throughout the CRU is high, and turnover is low.

By statutory mandate, reexaminations are handled with “special dispatch.”¹⁹⁵ Preparation of each office action involves two patent examiners and one supervisory patent examiner. One of the patent examiners prepares the office action. The second patent examiner and the supervisory patent examiner review the office action before the office action is mailed. The three examiners confer to resolve any disagreements.

B. Interaction Between CRU and OPLA

As noted above, the CRU works closely with the OPLA to resolve petitions to the director, disputes involving the “real party in interest,” petitions to merge proceedings, and the like. The CRU also works closely with the OPLA in examining the practical effects of its own rules, and in examining ways to streamline reexamination proceedings to reflect today’s realities.

At least one OPLA official has acknowledged that, while the present rules worked well in the past when there were relatively few reexaminations, they are “clunky” in view of today’s realities. The CRU and OPLA are therefore currently looking to “streamline” some of the rules.

C. Practice Suggestions

Under its new practice, the CRU will only reexamine claims for which a SNQ is alleged and found. In the past, a SNQ for even a single claim would typically trigger the reexamination of all claims.

Under the new rules, every submitted reference must be applied to at least one claim. Many requests are being denied a filing date for failing to apply every cited reference. The filing date is important because, as mentioned above, the PTO strives to issue a final office within two years of the filing date.

Litigation docket numbers are not to be cited in PTO disclosure forms (*i.e.*, PTO Form 1449, PTO/SB/08A, or PTO/SB/08B). Affidavits and/or testimony transcripts can be cited in PTO disclosure forms.

Extensions of time in reexamination proceedings must be obtained in advance and will not be granted without a substantial reason. A request for an extension of time must include a description of relevant activities to date, reasons necessitating an extension of time, and relevant actions that will be taken during the requested extension period. Potentially valid reasons include the death or unavailability of an inventor, or a need for trial testimony or exhibits. Extensions of time will generally not be granted for holidays or vacations.

If a practitioner has a concern about a reexamination, he or she should contact the Office of the CRU Director before petitioning the Patent Commissioner. A petition to the Commissioner triggers the transfer of the reexamination file from the CRU to the Commissioner, which may delay the reexamination proceeding.

D. Recommendations That Are Circulating

Substantial discussion exists among reexamination experts about ways the current reexamination process can be improved. While the topics discussed below are not meant to be exhaustive, the ones presented are “hot button” issues and deserve immediate and special attention.

1. Extensions of time

In reexamination proceedings, deadlines for filing responses or third party papers are generally extremely short, particularly in cases involving a concurrent litigation. However, the PTO is cognizant that a patent owner must be provided with a fair opportunity to present an argument against any attack on the patent¹⁹⁶ and has granted requests for extension of time in a number of cases. If a patent owner is faced with an action presenting extensive and complex rejections or an action requiring development of factual affidavits, the patent owner should consider filing a request for an extension of time. Such a request should be detailed and provide sufficient cause to justify the extension. When deciding such requests, the PTO must balance the interest of the parties against the statutory mandate that reexaminations be conducted with special dispatch.

The *inter partes* reexamination rules allow for the patent owner to request an extension of time to reply to an Office Action (or any action) for sufficient cause.¹⁹⁷ However, the rules explicitly prohibit the third party from receiving an extension of time for submitting written comments to the patent owner's Office Action response.¹⁹⁸ Many practitioners argue that this rule is unfair to the third party requester, particularly in cases where the patent owner has received an increase in the page limit for reply or submits voluminous factual evidence. One recommendation being circulated is to remove the prohibition against the third party requester and allow the third party requester to request extensions of time using the same standards applied to the patent owner.

2. Page limit waivers

As discussed above, the *inter partes* reexamination rules impose a 50-page limit on Office Action responses filed by the patent owner and written comments filed by the third party requester. One recommendation circulating is that the PTO remove the 50-page limit. Opponents argue that removal of any page limit would invite spurious and unfocused arguments, increasing the burden on the Examiners. Another recommendation circulating is that the PTO *sua sponte* waive or increase the 50-page limit when issuing extensive Office Actions.

Another factor that directly impacts page limits is whether the responder is presenting facts or argument. A simple presentation of facts does not count against the page limit, while attorney (or applicant) argument does. For this reason, the authors recommend that practitioners take a lesson from district court litigation and clearly separate the facts from the argument. This can be done in the body of the response by delineating factual sections from arguments, much the same way a summary judgment motion or opinion will have separate sections for “findings of fact” and “conclusions of law.” Alternatively, practitioners should consider a separate Evidence Appendix. Both of these devices will assist the responder in separating facts surrounding the story of the invention and the prior technology, from the arguments in favor (or against) patentability.

One complicating factor worth noting is that the line between “facts” and “argument” may be a blurry one. Discussion of teachings of a reference is factual. The ultimate conclusion of obviousness is legal. In between, however, could exist gray areas. Nonetheless, practitioners can only help themselves if clear distinctions are made in the body of any response.

196 See MPEP Sections 2265 and 2665.

197 37 C.F.R. Section 1.956.

198 37 C.F.R. Section 1.947.

3. Adopt an “interference-type” approach

Given the concern regarding pendencies of reexamination proceedings, particularly *inter partes* proceedings, some experts have argued that the reexamination process should be modeled after the interference process currently instituted by the PTO. The authors intend to further develop this idea in future versions of this paper.

E. CRU Criticisms

Some practitioners have nicknamed the CRU as the “Central Rejection Unit.” Is there any practical truth to this moniker?¹⁹⁹ With the much greater resources devoted to the reexamination process by the CRU, coupled with the impact of *KSR* in terms of how printed publications and patents will be treated by the CRU, and in *inter partes* reexaminations the presence of the third party requester throughout the process, speculation abounds that the chance of a claim surviving the reexamination process is becoming less and less as time goes on. Is this speculation correct in practice?

Some critics argue that the CRU is unfairly inclined to find claims invalid in reexaminations especially where these claims have been subjected to extensive prior litigation and have survived significant validity challenges in the courts. They contend that, because the CRU essentially does no searching but instead relies on the parties to do this task, the examiners do not appreciate the innovation captured by the claimed invention because they are “spoon fed” the prior art by the requester.

Moreover, critics contend that the CRU tends to “rubber stamp” the reexamination request filed by the requester in *inter partes* proceedings and that the first office action almost always rejects all of the claims. Some contend that this improperly shifts the presumption to the patent owner that the claims are *prima facie* invalid. They also contend that the patent owner essentially only has the response to the first office action to put forth evidence of non-obviousness and that trying “to prove a negative” is daunting at best, and a practical impossibility at worst. Critics argue that this approach subverts the constitutional basis for patents.

Finally, some critics contend that the PTO is pressuring the CRU to be very negative towards claims in reexamination to mollify powerful political forces at work. Those political forces seek to weaken valuable patent rights owned by non-practicing entities, which happen to encompass entities such as universities and R&D innovation companies. Some perceive that these entities are being ganged up on and attacked unfairly in the courts. The employees of the PTO interviewed by the authors believe that this criticism is unfounded. These employees counter that any pressures from the PTO are limited to meeting deadlines and timelines.

F. Practitioner Criticisms

Some critics argue that practitioners are abusing the reexamination process by filing papers for intentional delay or by turning the petition process into a form of motion practice in front the Office of Patent Legal Administration.

The authors interviewed high level OPLA, CRU and BPAI officials, as well as several judges. These individuals provided extensive criticisms and suggestions on how practitioners could improve in terms of dealing with the PTO and the courts in reexaminations. The authors have provided these criticisms and suggestions in the applicable sections of this paper, rather than providing

¹⁹⁹ Some people argue that the reexamination decisions issued by the PTO support this nickname. For example, as of September 30, 2008, the PTO has granted 8467 *ex parte* reexamination requests. Of the granted requests, only 1264 *ex parte* reexaminations have resulted in confirmation of all claims. As of December 31, 2008, the PTO has granted 439 *inter partes* reexamination requests. Of the granted requests, only four *inter partes* reexaminations have resulted in confirmation of all claims. Assuming that Office Actions have not issued in a percentage of the recently filed reexaminations, these statistics lead to the conclusion that the PTO has issued rejections in approximately 80% or more of the *ex parte* reexaminations and in approximately 95% or more of the *inter partes* reexaminations. Additionally, approximately 70% of *inter partes* reexaminations receive a first Office Action on the same day that the reexamination is ordered. See Reexamining Inter Partes Reexam, *Institute for Progress* (April 2008).

a long laundry list here. Suffice it to say, the bar needs to improve its practices and procedures in a manner commensurate with what the PTO and the courts need to do.

VII. REEXAMINATION STATISTICS

We conclude this paper with a discussion of reexamination statistics. The authors have done their own independent data gathering and analysis of reexaminations and offer the following summary. To provide further insight into reexamination practice, the authors have conducted a thorough review of all reexamination requests that have been published in the Official Gazette January 1, 2008, through September 23, 2008. A sampling of that review is provided herewith.

The review of the requests shows that 128 *inter partes* reexamination requests were made involving 94 unique patent owners. There were 531 *ex parte* reexamination requests involving 351 unique patent owners. For *inter partes* reexaminations, the unique patent owners included 106 U.S.-based companies and seven Japanese companies, with the remainder of the patent owners based in 11 other countries. For *ex parte* reexaminations, the unique patent owners included 431 U.S.-based companies and 34 Japanese companies, with the remainder of the patent owners based in 21 other countries.

The technologies involved were similarly diverse. The *inter partes* reexamination requests involved 67 different technology classes, with the top ten technology classes representing nearly 44% of the total number of classes within *inter partes* reexamination requests. The technology classes with the most *inter partes* reexamination requests were: "Data processing: database and file management or data structures," "Data Processing: financial, business practice, management, or cost/price determination," and "Surgery." Each of these classes had eight *inter partes* reexamination requests. The *ex parte* reexamination requests involved 165 different technology classes, with the top ten technology classes representing 35% of the total number of classes. The three technology classes with the most *ex parte* reexamination requests were "Surgery" (38), "Electrical computers and digital processing systems: multicomputer data transferring" (34), and "Chemistry: molecular biology and microbiology" (19).

Attached are the most recent reexamination statistics from the PTO (dated March 31, 2009).

2009 CRU REEXAMINATION STATISTICS

UNITED STATES PATENT AND TRADEMARK OFFICE

Commissioner for Patents
United States Patent and Trademark Office
P.O. Box Box 1450
Alexandria, VA 22315-1450
www.uspto.gov

Inter Partes Reexamination Filing Data - March 31, 2009

- 1. Total requests filed since start of inter partes reexam on 11/29/99 .6091
2. Number of filings by discipline
a. Chemical Operation 139 23%
b. Electrical Operation 242 39%
c. Mechanical Operation 217 36%
d. Design Patents 11 2%
3. Annual Reexam Filings
Fiscal Yr. No. Fiscal Yr. No. Fiscal Yr. No. Fiscal Yr. No.
2000 0 2003 21 2006 70 2009 133 YTD
2001 1 2004 27 2007 126
2002 4 2005 59 2008 168
4. Number known to be in litigation 382 63%
5. Decisions on requests 532
a. No. granted 503 95%
(1) By examiner 502
(2) By Director (on petition) 1
b. No. denied 29 5%
(1) By examiner 25
(2) Reexam vacated 4
6. Overall reexamination pendency (Filing date to certificate issue date)
a. Average pendency 33.7 (mos.)
b. Median pendency 30.8 (mos.)
7. Total inter partes reexamination certificates issued (1999 - present) 55
a. Certificates with all claims confirmed 4 7%
b. Certificates with all claims canceled 40 73%
c. Certificates with claims changes 11 20%

1 Of the requests received in FY 2009, 20 requests have not yet been accorded a filing date, and seven requests have had preprocessing terminated, for failure to comply with the requirements of 37 CFR 1.915. See Clarification of Filing Date Requirements for Ex Parte and Inter Partes Reexamination Proceedings, Final Rule, 71 Fed. Reg. 44219 (August 4, 2006).

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Ex Parte Reexamination Filing Data - March 31, 2009

1.	Total requests filed since start of <i>ex parte</i> reexam on 07/01/81	9893 ¹	
	a. By patent owner	3603	36%
	b. By other member of public	6125	62%
	c. By order of Commissioner	165	2%
2.	Number of filings by discipline		
	a. Chemical Operation	2873	29%
	b. Electrical Operation	3404	34%
	c. Mechanical Operation	3456	35%
	d. Design Patents	160	2%
3.	Annual Ex Parte Reexam Filings		
	Fiscal Yr. No. Fiscal Yr. No. Fiscal Yr. No. Fiscal Yr. No.		
	1981 78 (3 mos.) 1989 243 1997 376 2005 524		
	1982 187 1990 297 1998 350 2006 511		
	1983 186 1991 307 1999 385 2007 643		
	1984 189 1992 392 2000 318 2008 680		
	1985 230 1993 359 2001 296 2009 308 YTD		
	1986 232 1994 379 2002 272		
	1987 240 1995 392 2003 392		
	1988 268 1996 418 2004 441		
4.	Number known to be in litigation	2992	30%
5.	Decisions on requests	9525	
	a. No. granted	8754	92%
	(1) By examiner	8641	
	(2) By Director (on petition)	113	
	b. No. denied	771	8
	(1) By examiner	736	
	(2) Reexam vacated	35	
6.	Total examiner denials (includes denials reserved by Director)	849	
	a. Patent owner requester	444	52%
	b. Third party requester	405	48%
7.	Overall reexamination pendency (Filing date to certificate issue date)		
	a. Average pendency	24.8 (mos.)	
	b. Median pendency	19.3 (mos.)	

1 Of the requests received in FY 2009, 26 requests have not yet been accorded a filing date, and preprocessing of 12 requests was terminated for failure to comply with the requirements of 37 CFR 1.510. See Clarification of Filing Date Requirements for *Ex Parte* and *Inter Partes* Reexamination Proceedings, Final Rule, 71 Fed. Reg. 44219 (August 4, 2006).

8. Reexam certificate claim analysis:	Owner <u>Requester</u>	3rd Party <u>Requester</u>	Comm'r <u>Initiated</u>	<u>Overall</u>
a. All claims confirmed	22%	27%	12%	25%
b. All claims cancelled	8%	13%	21%	11%
c. Claims changes	70%	60%	67%	64%
9. Total ex parte reexamination certificates issued (1981 - present)				6743
a. Certificates with all claims confirmed			1681	25%
b. Certificates with all claims canceled			756	11%
c. Certificates with claims changes			4306	64%
10. Reexam claim analysis - requester is patent owner or 3rd party; or Comm'r initiated.				
a. Certificates - PATENT OWNER REQUESTER				2790
(1) All claims confirmed			619	22%
(2) All claims canceled			228	8%
(3) Claim changes			1943	70%
b. Certificates - 3rd PARTY REQUESTER				3806
(1) All claims confirmed			1044	27%
(2) All claims canceled			497	13%
(3) Claim changes			2265	60%
c. Certificates - COMM'R INITIATED REEXAM				147
(1) All claims confirmed			18	12%
(2) All claims canceled			31	21%
(3) Claim changes			98	67%

THE PARALLEL UNIVERSES OF THE USITC & THE DISTRICT COURTS

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I. INTRODUCTION

Intellectual property has taken a leading role in the U.S. economy, generating 18 percent of the U.S. gross domestic product on average.² Moreover, the industries that principally rely on intellectual property protection and enforcement, including semiconductors, computers, electronics, pharmaceuticals, automotive, entertainment, and others have been an engine of growth in the economy, accounting for 26 percent of the annual real gross domestic product growth over a recent five-year period.³ These industries rank among the highest paying employers across the U.S., employing an estimated 18 million workers or about 13 percent of the workforce.⁴

The availability of multi-pronged enforcement strategies is essential to the vitality and continued success of these industries. These enforcement strategies necessarily include a careful examination of the risks and rewards of enforcing valuable intellectual property rights in the district courts as well as the U.S. International Trade Commission (“ITC” or “Commission”).

The ITC is an independent, nonpartisan, quasi-judicial federal agency.⁵ Its mission is to provide international trade expertise to the legislative and executive branches of government and to resolve claims of unfair import trade that harm domestic industries in the United States.⁶ Chief among its responsibilities is the adjudication of claims of infringement of IP rights pursuant to Section 337 of the Tariff Act of 1930, as amended.⁷

The ITC has seen remarkable growth in its caseload, increasing by nearly 80 percent from 2003 through fiscal year 2007.⁸ In fiscal year 2008, the ITC has hit a high water mark for newly filed complaints.⁹ By all accounts, Section 337 case filings are expected to increase, particularly in the wake of the U.S. Supreme Court’s recent decision in *eBay, Inc. v. MercExchange, LLC*,¹⁰ which has had the effect of curtailing the availability of injunctions from U.S. district courts in patent cases. The ITC has rejected the view that *eBay* has a similar constraining effect on its authority or discretion to issue its own injunctive relief pursuant to Section 337.¹¹ Thus, the attractiveness of the ITC’s injunctive remedies has garnered increased interest of IP owners who view the ITC as an important forum for the enforcement of their valuable IP rights, especially in the post-*eBay* litigation environment.

1 Ms. Gonzalez and Ms. Cofrancesco are partners of Howrey LLP and Ms. Salata is an associate of Howrey LLP. The views expressed in this article are of the authors and do not necessarily reflect the views of their law firm or any of the firm’s clients.

2 See General Accounting Office, INTELLECTUAL PROPERTY, GAO-08-157, Report to the Ranking Member, Senate Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, Committee on Homeland Security and Government Affairs (March 2008).

3 *Id.*

4 *Id.*

5 19 U.S.C. Section 1330. The Commission is comprised of six Commissioners equally split between Democrats and Republicans who have been nominated by the President and confirmed by the U.S. Senate for nine-year terms. *Id.*

6 19 U.S.C. Sections 1330, 1332, 1337, 1671 et seq., 1673 et seq.; 19 C.F.R. 201.7; 19 C.F.R. Subpart B.

7 19 U.S.C. Section 1337. Implementing regulations promulgated pursuant to the authority of Section 337 are published at 19 C.F.R. Part 210.

8 U.S. INTERNATIONAL TRADE COMMISSION, PERFORMANCE AND ACCOUNTABILITY REPORT FOR FISCAL YEAR 2007 at 67, available at http://www.usitc.gov/ext_relations/about_itc/USITC_PAR_2007.pdf (last visited September 26, 2008).

9 See Trade Remedy Investigations: Section 337 Investigational History, available at http://usitc.gov/trade_remedy/int_prop/inv_his.htm (last visited September 25, 2008).

10 126 S.Ct. 1837 (2006).

11 See *Certain Baseband Processor Chips and Chipsets, Transmitter and Receiver (Radio) Chips, Power Control Chips, and Products Containing Same, Including Cellular Telephone Handsets*, Inv. No. 337-TA-543, Comm’n Op. at 62-63 n.230 (June 7, 2007) (“The Commission, in interpreting its organic statute, takes the position that the Tariff Act of 1930, as amended, represents a legislative modification of the traditional test in equity [applied by the Supreme Court in *eBay*]....”).

II. OVERVIEW OF THE ITC'S AUTHORITY TO ENFORCE IP RIGHTS UNDER SECTION 337

Section 337 of the Tariff Act of 1930, as amended, confers upon the ITC broad authority to issue remedial orders to eliminate unfair methods of competition and unfair acts in connection with the importation of merchandise into the United States.¹² Section 337 enumerates five categories of unfair acts in connection with importation of accused products for which injury to the domestic industry is presumed: (1) infringement of a valid and enforceable U.S. patent;¹³ (2) infringement of a valid and enforceable registered trademark;¹⁴ (3) infringement of a valid and enforceable registered copyright under Title 17 of the U.S. Code;¹⁵ (4) infringement of a registered semiconductor mask work;¹⁶ and (5) infringement of exclusive rights in a protected vessel hull design under Chapter 13 of Title 17 of the U.S. Code.¹⁷ The authority to remediate these unfair acts can only be invoked where the complainant has demonstrated that a domestic industry exploiting the involved IP rights exists or is in the process of being established.¹⁸

The ITC's remedial authority also extends to any other unfair methods of competition and unfair acts in connection with imported merchandise that have the effect of injuring a domestic industry in the United States, preventing the establishment of such a domestic industry, or restraining or monopolizing trade and commerce in the United States.¹⁹ The statute imposes no limitations on the types of unfair acts and methods of competition that are remediable under this provision of Section 337; and claims under this provision have included antitrust claims,²⁰ trade dress misappropriation,²¹ infringement of common law trademarks,²² trademark dilution;²³ misappropriation of trade secrets,²⁴ passing off,²⁵ false designation of origin or source,²⁶ unfair competition,²⁷ and false advertising,²⁸ among other forms of unfair acts and methods of competition. Section 337 investigations most frequently involve claims of patent or trademark infringement. In recent years, nearly 90 percent of Section 337 cases involve at least one patent infringement claim.²⁹

Section 337 investigations are initiated by the filing of a complaint by one or more complainants containing detailed factual allegations establishing both an unfair act, typically infringement of one or more patent claims or infringement of other IP rights by named respondents, as well as establishing the domestic industry requirement.³⁰ Upon institution, the investigation is assigned to an Administrative Law Judge ("ALJ") who presides over the investigation.³¹ An investigative attorney from the ITC's Office of Unfair Import Investigations ("OUII") is assigned to participate in each investigation as a party.³² *Markman* hearings and technical tutorials are optional depending on the ALJ's discretion in particular matters.

12 19 U.S.C. Section 1337.

13 *Id.* Section 1337(a)(1)(B).

14 *Id.* Section 1337(a)(1)(C).

15 *Id.* Section 1337(a)(1)(B)(i).

16 *Id.* Section 1337(a)(1)(D).

17 *Id.* Section 1337(a)(1)(E).

18 *Id.* Section 1337(a)(2).

19 *Id.* Section 1337(a)(1)(A).

20 See generally Kao, T., *Reexamining Antitrust Claims Under Section 337*, ITC TRIAL LAWYERS ASS'N SECTION 337 REPORTER, Vol. XXIII, at 1 (Summer 2007).

21 See, e.g., *Certain Ink Markers and Packaging Thereof*, Inv. No. 337-TA-522, USITC Pub. 3971 (Dec. 2007).

22 See, e.g., *Certain Bearings and Packaging Thereof*, Inv. No. 337-TA-469, Comm'n Op. at 2 (Dec. 2007).

23 See, e.g., *Bearings*, Inv. No. 337-TA-469, Comm'n Op. at 2.

24 See, e.g., *Certain Processes for the Manufacture of Skinless Sausage Casings and Resulting Product*, Inv. No. 337-TA-148/169, USITC Pub. 1624 (Dec. 1984).

25 See, e.g., *Bearings*, Inv. No. 337-TA-469, Comm'n Op. at 2; *Certain Nut Jewelry and Parts Thereof*, Inv. No. 337-TA-229, USITC Pub. 1929 (Nov. 1986).

26 See, e.g., *Bearings*, Inv. No. 337-TA-469, Comm'n Op. at 2; *Nut Jewelry*, Inv. No. 337-TA-229.

27 See *Nut Jewelry*, Inv. No. 337-TA-229.

28 See, e.g., *Bearings*, Inv. No. 337-TA-469, Comm'n Op. at 2; *Certain Food Storage Containers*, Inv. No. 337-TA-152, USITC Pub. 1563 (August 1984).

29 See, e.g., U.S. INTERNATIONAL TRADE COMMISSION, YEAR IN REVIEW, FISCAL YEAR 2006 at 14 (indicating 66 out of 70 active investigations during fiscal year 2006 included patent infringement allegations), available at

http://hotdocs.usitc.gov/docs/pubs/year_in_review/pub3915.pdf (last visited September 26, 2008).

30 19 C.F.R. Sections 210.8 through 210.10.

31 Proceedings conducted by the ALJ are in accordance with the Administrative Procedure Act (5 U.S.C. Sections 551 *et seq.*) and the Commission's Rules of Practice and Procedure, 19 C.F.R. Part 210. The conduct of the Commission's investigation is generally consistent with the Federal Rules of Evidence and the Federal Rules of Civil Procedure. In addition, each ALJ issues his own set of Ground Rules governing the conduct of the investigation over which he presides.

32 19 C.F.R. Section 210.3.

Following discovery and pre-trial briefing, the ALJ conducts a hearing, akin to a district court trial, on all disputed issues.³³ The hearing enables the parties to present live witness testimony and documentary, demonstrative and physical evidence to support their positions.³⁴ Respondents are accorded the statutory right to present all legal and equitable defenses.³⁵ After consideration of post-hearing submissions, the ALJ issues a final Initial Determination (“ID”) disposing of all issues concerning whether a violation of Section 337 exists, together with a Recommended Determination as to appropriate remedies to address the violation.³⁶ Parties may petition the Commission to review one or more issues decided in the ID.³⁷ An initial determination becomes the determination of the Commission unless the Commission determines to review the ID within the timeframes set forth in the regulations.³⁸ Thereupon the ITC issues its final determination in the investigation and solicits written comments on the appropriate remedy, bonding and the public interest.³⁹ Based on the record of the investigation and the comments of the parties, the ITC renders its determination on violation issues, and issues one or more remedial orders designed to provide complete relief for the violation found.⁴⁰ The ITC’s final determination is subject to Presidential review for policy reasons and its determination and orders are appealable to the U.S. Court of Appeals for the Federal Circuit.⁴¹

III. COMPARATIVE ADVANTAGES OF ENFORCING IP RIGHTS IN THE ITC VERSUS DISTRICT COURTS

IP litigators frequently tout a number of distinct features and advantages that inure to the benefit of complainants who choose to enforce their IP rights in the ITC as compared to filing an action solely in a U.S. district court. The most significant differences between a Section 337 proceeding in the ITC and a patent infringement action in a federal district court include: (1) relatively speedy adjudication of infringement claims in the ITC as compared to district courts; (2) the potential for adjudicating claims before specialized intellectual property judges; and (3) the potent remedies available in the ITC including general and limited exclusions orders and cease and desist orders.

There are additional pertinent considerations that may enter into the calculus as to whether a Section 337 action should be filed in addition to or in lieu of a district court action. These other factors are discussed in Parts IV and V below. IP owners are well advised to carefully evaluate all aspects of both ITC and district court litigation for the enforcement of their IP rights consistent with their goals and budget.

A. The Speedy Discovery and Resolution of Disputes

The ITC is internationally recognized as a forum that affords expeditious adjudication of matters. In fact, this is a Commission policy, a Congressional mandate and is reflected in both Section 337 and the ITC’s Rules of Practice and Procedure (19 C.F.R. Part 210).

The statute mandates prompt completion of investigations by requiring that cases be decided with due haste:

The Commission shall conclude any such investigation and make its determination at the earliest practicable time after the date of publication of notice of such investigation.⁴²

The implementing regulations further emphasize this Congressional mandate, particularly Rules 210.2, 210.42 and 210.51. Rule 210.2 states that “all investigations and related proceedings

³³ 19 U.S.C. Section 1337(c); 19 C.F.R. Section 210.36.

³⁴ 19 C.F.R. Section 210.36.

³⁵ 19 U.S.C. Section 1337(c).

³⁶ 19 C.F.R. Section 210.42.

³⁷ *Id.* Section 210.43.

³⁸ *Id.* Section 210.42. The ALJ may also dispose of issues concerning violation of Section 337 by summary determination, akin to summary judgment in the district courts. *See* 19 C.F.R. Section 210.18.

³⁹ 19 C.F.R. Section 210.50.

⁴⁰ 19 U.S.C. Sections 1337(d), (e), (f).

⁴¹ *Id.* Sections 1337(c), (j).

⁴² *Id.* Section 1337(b)(l).

under this part shall be conducted expeditiously.”⁴³ From the language of the rule, it is clear to all parties, including the ALJ, that the Commission shall make an effort “at each stage of the investigation” to “avoid delay.”⁴⁴ Rule 210.51 deals with the period for concluding the investigation and reflects the statutory mandate of establishing a target date early in the case. To promote such expeditious adjudication, the Commission must, within 45 days after institution of an investigation, establish a target date for completion of the investigation.⁴⁵ Additionally, Rule 210.42 states that the ALJ “shall certify the record to the Commission and shall file an initial determination on whether there is a violation of section 337” no more than “four (4) months before the target date set pursuant to Section 210.51(a).”⁴⁶

With its emphasis on expeditious adjudications, it is often quipped that ITC proceedings are not for the faint of heart as they progress quickly from the moment a case is instituted straight through to completion. Discovery commences immediately with response times of ten days or less. The period for discovery often is five to six months. Discovery is broad-ranging in scope with few limitations on interrogatories, document requests, depositions, and foreign discovery. Time to trial has been on the order of seven to nine months. Historically, the length of time for completion of investigations has ranged from 12 to 15 months since Congress repealed the mandatory statutory deadline.⁴⁷

When Congress eliminated the fixed statutory deadlines in permanent relief cases in 1994, the legislative history made clear that the ITC was expected “to complete its [Section 337] investigation in approximately the same amount of time as is currently the practice.”⁴⁸ At that time, most Section 337 cases (except those designated “more complicated”) were completed within 12 months.

More recently, however, investigation target dates and procedural schedules have been slipping as investigations are regularly set at 15 months and extended for longer durations. The Commission has acknowledged this issue attributing the lengthening of investigations to “stays pending other proceedings and reassignment of cases due to the retirement of an administrative law judge, as well as the resource constraints relative to the recent surge in caseload.”⁴⁹ To accommodate the present crush of cases and the temporary shortage of judges and staff, the ITC amended its Rules of Practice and Procedure, effective August 6, 2008, to permit the ALJ to set a maximum 16-month target date, rather than the 15-month target date, without seeking approval from the Commission.⁵⁰ In addition, newly amended Rule 210.42 requires that the ALJ “shall certify the record to the Commission and shall file an initial determination (“ID”) on whether there is a violation of section 337” no more than “four (4) months before the target date set pursuant to Section 210.51(a).”⁵¹

Critics have expressed concern that these regulatory changes would effectively establish a *de facto* 16-month target date for investigations and may inadvertently start the ITC down a “slippery slope” of extending target dates that may erode the ITC’s reputation as a forum which provides a quick resolution.⁵² Additionally, critics are concerned that there will now be longer investigations at the ITC as a result of the rule change and that this change will open the door to further expansions of time limits in the future. The ITC counters that the amendment will give its judges more flexibility to set target dates where the facts dictate the necessity to do so.⁵³ Moreover, the Commission noted that it would revisit the target date issue after hiring more judges and staff and obtaining additional resources.⁵⁴ Thus, although critics are concerned that this change may somewhat

43 19 C.F.R. Section 210.2.

44 *Id.*

45 See 19 U.S.C. Section 1337(b); 19 C.F.R. Section 210.51(a).

46 See Notice of Final Rules of General Application and Adjudication and Enforcement, 73 Fed. Reg. 38316, 38324 (July 7, 2008) (to be codified at 19 C.F.R. Section 210.42(a)(1)(i)).

47 See SECTION 337 INVESTIGATIONS AT THE U.S. INTERNATIONAL TRADE COMMISSION: ANSWERS TO FREQUENTLY ASKED QUESTIONS, USITC Pub. 3708 at 21 (July 2004), available at http://www.usitc.gov/trade_remedy/int_prop/pub3708.pdf (last visited September 26, 2008).

48 S. Rep. No. 103-412, at 188 (1994).

49 Notice of Final Rules of General Application and Adjudication and Enforcement, 73 Fed. Reg. 38316, 38318 (July 7, 2008) (to be codified at 19 C.F.R. Part 210).

50 *Id.*

51 *Id.* at 38324 (to be codified at 19 C.F.R. Section 210.42(a)(1)(i)).

52 See 73 Fed. Reg. at 38318 (noting comments of the ITC Trial Lawyers Association and the Intellectual Property Owners Association criticizing the ITC’s proposed rule regarding target dates). See Also Sheri Qualters, *New ITC Patent Rules Criticized*, THE NATIONAL LAW JOURNAL (July 29, 2008), available at <http://www.law.com/jsp/article.jsp?id=1202423346828> (last visited September 26, 2008).

53 73 Fed. Reg. at 38318.

54 *Id.*

dampen the attractiveness of pursuing IP enforcement before the ITC, the Commission believes, as do many practitioners that this rule change reflects the actual practice of the ITC in recent years.

While it may be too early to gauge whether the rule changes portend sustained increases in case completion timeframes, based on a review of ITC practice since the publication of the new rules on July 7, 2008, the facts do not appear to bear out critics' concerns. Since July 7, 2008, six Section 337 investigations have been instituted; and target dates have been set for three of the six cases.⁵⁵ A target date of 15 months was set in two of those investigations, while the third investigation established a 16-month target date.⁵⁶ Thus, even under the new amendments to the ITC's Rules of Practice and Procedure, target dates of 15 and 16 months experienced thus far still result in faster completion of cases than patent litigation in most district courts.

B. Specialized Judges

Another frequently cited advantage of litigation before the ITC is its specialized intellectual property judges. ALJs at the ITC have authority to adjudicate IP complaints under the Administrative Procedure Act.⁵⁷ They function like federal district court judges in civil cases without a jury. The ALJs are very specialized in that nearly 90 percent of the cases litigated before them involve patents, thus enabling them to develop considerable expertise in this area of law. Additionally, the ALJs often schedule tutorials in these cases, allowing experts and attorneys to educate them on the technology involved in the investigation. By contrast, district court judges hear numerous types of criminal and civil cases, with the exception of a handful of courts which experience a relatively higher concentration of patent cases such as the Eastern District of Texas, the Eastern District of Virginia, the Northern District of California, and the District of Delaware.

C. Injunctive Remedies are Available to Provide Complete Relief to Complainants for Violation of Section 337

The principal remedies meted out by the ITC for a Section 337 violation are injunctive in nature.⁵⁸ The most powerful among these injunctive remedies are exclusion orders which prevent the adjudicated infringing merchandise from being imported into the United States.⁵⁹ An exclusion order issued by the ITC directs U.S. Customs and Border Protection ("CBP") to exclude articles from entry into the United States that have been found to violate Section 337.⁶⁰ There are two types of exclusion orders – a general exclusion order and a limited exclusion order. A general exclusion order is available in very limited circumstances.⁶¹ Such an order directs CBP to exclude all infringing articles, without regard to source. Thus, all infringing articles will be excluded from entry into the United States – even infringing articles that do not originate from a named respondent in the investigation. Limited exclusion orders, on the other hand, apply only to infringing articles that originate from a named respondent in the investigation. Thus, CBP is directed to exclude only infringing articles that originate from a specified party that was a respondent in the Commission investigation.

Also within the ITC's arsenal is the power to issue cease and desist orders that prohibit specified unfair acts from being undertaken in the United States.⁶² Cease and desist orders can be ordered in addition to general or limited exclusion orders. A cease and desist order directs a respondent in a Section 337 investigation to cease its unfair acts; including selling infringing imported articles out of U.S. inventory. Cease and desist orders are enforced by the Commission and

55 The cases are *Base Stations and Wireless Microphones*, Inv. No. 337-TA-653 (15 month target date); *Peripheral Devices and Components Thereof and Products Containing Same*, Inv. No. 337-TA-654 (16 month target date); *Cast Steel Railway Wheels, Certain Processes for Manufacturing or Relating to Same and Certain Products Containing Same*, Inv. No. 337-TA-655 (target date to be determined); *Integrated Circuits and Products Containing Same*, Inv. No. 337-TA-656 (15 month target date); *Automotive Multimedia Display and Navigation Systems, Components Thereof, and Products Containing Same*, Inv. No. 337-TA-657 (target date to be determined); *Video Game Machines and Related Three Dimensional Pointing Devices*, Inv. No. 337-TA-658 (target date to be determined).

56 *Base Stations and Wireless Microphones*, Inv. No. 337-TA-653 (15 month target date); *Peripheral Devices*, Inv. No. 337-TA-654 (16 month target date); *Integrated Circuits*, Inv. No. 337-TA-656 (15 month target date).

57 5 U.S.C. Sections 551 *et seq.*

58 See generally Juliana M. Cofrancesco, *ITC Remedial Orders: What Are They And How Far Do They Reach?* 2008 AIPLA Annual Meeting Conference Paper (October 2008).

59 19 U.S.C. Section 1337(d).

60 See *id.*

61 See *Laser Bar Code Scanners*, Inv. No. 337-TA-551, Comm. Op. at 22 (June 14, 2007).

62 19 U.S.C. Section 1337(f).

not CBP. Consent orders likewise restrict specified acts in the United States with the consent of the named respondent.⁶³

Each of these remedial orders provides the jurisdictional basis for the ITC's continued monitoring and enforcement of its orders in the event a violation of these orders occurs. For example, where an attempt has been made to import excluded merchandise, the ITC may issue a seizure and forfeiture order against the offending importer to ensure that any future shipments by that importer are seized and forfeited to the United States.⁶⁴ Violations of ITC cease and desist orders and consent orders are subject to severe monetary penalties.⁶⁵ Given these potent additional remedial powers, the scope and breadth of ITC remedial orders have profound implications for further actions that may be taken by the Commission in a later enforcement proceeding.

The ITC's orders may potentially apply to companies that were never parties to the case and may apply to downstream products that were never adjudicated to be infringing. Moreover, the ITC's remedies have the potential to ensnare redesigned products that were never adjudicated in the investigation. While Section 337 is designed to protect domestic industries from infringement of intellectual property rights and other unfair competition from imported products, U.S. companies are not immune from Section 337 actions when their activities have the requisite nexus to importation. Even electronic transmissions that violate Section 337 may be reached by ITC remedial orders.

Preliminary relief is also available under Section 337 on a highly expedited schedule. Specifically, the ITC may issue temporary exclusion orders and temporary cease and desist orders within 90 days after the case is instituted.⁶⁶

Once the Commission has found a violation of Section 337, it must determine which remedy or remedies are appropriate to address the violation found to exist. Although the Commission receives a recommendation from the administrative law judge as to an appropriate remedy, the Commission makes its own judgment based on the evidence presented to the judge below as well as facts presented directly to the Commission on the subject of an appropriate remedy in written comments or at a public hearing on rare occasion.⁶⁷

The Commission's authority to issue any remedy is conditioned upon consideration of the public interest.⁶⁸ The ITC first identifies the remedy appropriate to address the violation and then determines whether the public interest factors set forth in the statute would preclude the issuance of that remedy.⁶⁹ The statutory public interest factors against which an exclusion order or a cease and desist order are weighed are: "the public health and welfare, competitive conditions in the United States economy, the production of like or directly competitive articles in the United States, and United States consumers."⁷⁰

The permissible scope of an ITC remedial order is established in the notice of investigation that is published in the Federal Register.⁷¹ A remedial order may not cover products that are not within the Commission's notice of investigation.⁷²

The Commission has broad discretion to fashion an appropriate remedy for a Section 337 violation.⁷³ Notwithstanding that conceptually the Commission's remedial authority is broad, it has applied its authority "in a measured fashion and has issued only such relief as is adequate to redress

63 *Id.* Section 1337(c).

64 *Id.* Section 1337(i).

65 *Id.* Section 1337(f)(2).

66 *Id.* Sections 1337(e), (f).

67 See *Certain Agricultural Tractors Under 50 Power Take-Off Horsepower*, Inv. No. 337-TA-380, USITC Pub 3026, Comm'n Op. at 15 (March 1997); *Baseband Processor Chips*, Inv. No. 337-TA-543, Comm'n Op. (June 7, 2007).

68 19 U.S.C. Sections 1337(d)(1), (e)(1), (f)(1).

69 *Baseband Processor Chips*, Inv. No. 337-TA-543, Comm'n Op. at 17.

70 19 U.S.C. Sections 1337(d)(1), (e)(1), (f)(1).

71 19 C.F.R. Section 210.10(b). See also *Certain Systems for Detecting and Removing Viruses or Worms, Components Thereof, and Products Containing Same*, Inv. No. 337-TA-510, USITC Pub. 3936, Comm'n Op. at 4 (August 2007) (citing *Certain Insect Traps*, Inv. No. 337-TA-498, Order No. 7 (April 2004)).

72 See *Certain Automated Mechanical Transmission Systems for Medium-Duty and Heavy-Duty Trucks and Components Thereof*, Inv. No. 337-TA-503, USITC Pub. 3934, Comm'n Op. at 4 (August 2007) (declining to include transmissions for vehicles other than those covered by the notice of investigation).

73 See *Hyundai Elec. Indus. Co. Ltd. v. United States*, 899 F.2d 1204, 1209 (Fed. Cir. 1990).

the harm caused by the prohibited imports.⁷⁴ The guiding principle often cited by the Commission is to tailor relief consistent with the central purpose of ITC remedial orders: “to ensure complete relief to the domestic industry.”⁷⁵

IV. ENFORCING IP RIGHTS IN BOTH THE ITC AND DISTRICT COURT

Many cases brought before the ITC have parallel complaints filed in a district court. The advantage to filing in both fora allows the complainant to choose its forum in both arenas (as opposed to being hailed into court in a jurisdiction that was not its choosing in a declaratory judgment action). Additionally, by filing a parallel action in a district court, a complainant may potentially recover monetary damages – a remedy not available in Section 337 investigations. When parallel actions are pending, a number of issues are presented, including whether and under what circumstances a stay of the ITC and/or district court proceeding may be available and whether the ITC investigation may otherwise be terminated by respondents without a finding of a violation.

A. Automatic Stay of the District Court Action (28 U.S.C. Section 1659)

Companies that are sued in both district court and in the ITC may, as a matter of right, obtain a stay of the district court action. Pursuant to 28 U.S.C. Section 1659(a), a district court must stay the action at the request of a defendant who is also a respondent in the ITC investigation with respect to any claim that involves the same issues before both forums.⁷⁶ Such stays are granted as a matter of right as long as the respondent requests the stay within 30 days of the later of (i) being named as a respondent in the Section 337 investigation or (ii) the filing of the district court action.⁷⁷ The stay remains in place until the ITC’s determination becomes final, including conclusion of all appeals.⁷⁸

Upon conclusion of the Section 337 investigation, or the lifting of the stay, the record from the proceeding at the ITC may be transmitted to the district court for use in the district court action.⁷⁹

B. Stay of the ITC Proceeding In Case of PTO Re-examination

Stays are rarely granted at the ITC. Although in theory, a stay is available for good cause shown, two recent cases, *Personal Computers* and *Semiconductor Chips* provides incremental insight into particular circumstances that the Commission might find appropriate for the issuance of a stay of ITC proceedings in the context of a PTO reexamination under its multi-factor analysis applied by the Commission.⁸⁰ In determining whether to stay an investigation when PTO reexamination proceedings are ongoing, the Commission has weighed the following factors: (1) the state of discovery and the hearing date; (2) whether a stay will simplify the issues and hearing of the case; (3) the undue prejudice or clear tactical disadvantage to any party; (4) the stage of the PTO proceedings; and (5) the efficient use of Commission resources.⁸¹ A sixth factor, *i.e.*, whether alternative remedies are available in federal court, was previously part of the Commission’s analysis, but has now been rejected by five of six currently sitting ITC Commissioners.⁸² Each request for a stay is evaluated by the presiding ALJ and sitting Commission based on the specific facts of the case.

In both *Personal Computers* and *Semiconductor Chips*, the ITC held fast to its policy of “expeditiously adjudicating” Section 337 matters.⁸³ Timing was among the most important factors that drove the result of whether a stay was granted, and in particular, the procedural posture of both

74 *Certain Devices for Connecting Computers Via Telephone Lines*, Inv. No. 337-TA-360, USITC Pub. 2843, Comm’n Op. at 9 (Dec. 12, 1994). See also *Certain Curable Fluoroelastomer Compositions and Precursors Thereof*, Inv. No. 337-TA-364, USITC Pub. 2890, Comm’n Op. at 4-5 (May 1995).

75 *Certain Hardware Logic Emulation Systems and Components Thereof*, Inv. No. 337-TA-383, Comm’n Op. at 16 (March 31, 1998).

76 See 28 U.S.C. Section 1659(a).

77 See *id.*

78 *In re Princo Corp.*, 478 F.3d 1345, 1348 (Fed. Cir. 2007).

79 28 U.S.C. Section 1659(b).

80 See *Certain Semiconductor Chips With Minimized Chip Package Size and Products Containing Same*, Inv. No. 337-TA-605, Comm’n Op. (April 29, 2008); *Certain Personal Computer/Consumer Electronic Convergent Devices, Components Thereof, and Products Containing Same*, Inv. No. 337-TA-558, Order No. 6 (February 7, 2006).

81 See *Semiconductor Chips*, Inv. No. 337-TA-605, Comm’n Op. at 3; *Personal Computers*, Inv. No. 337-TA-558, Order No. 6, at 11-12.

82 *Compare Semiconductor Chips*, Inv. No. 337-TA-605, Comm’n Op. at 3 n.2 (majority view rejecting 6th factor of availability of alternative remedies in federal court) with Comm’n Op. at 4 n.2 (Commissioner Pinkert’s view that 6th factor should not be eliminated for purposes of considering whether to stay an investigation).

83 See 19 C.F.R. Sections 210.2, 210.51 and 210.42.

the PTO reexam and the ITC investigation in these two cases. The Commission's analysis suggests that a movant will have a higher likelihood of success if the reexamination process at the PTO is in its final stages and the ITC investigation is in its initial stages. The other factors likewise may affect the outcome of the Commission's balancing test.

In the *Personal Computers* investigation, the need for a stay pending reexamination at the PTO was evaluated very early in the ITC proceeding. In fact, discovery had not been conducted and no trial date had been set.⁸⁴ Additionally, as opposed to one of the parties moving for a stay, the Commission itself ordered the ALJ to address the issue in its Notice of Investigation.⁸⁵ After requesting and reviewing submissions from the parties on this issue of a stay, the ALJ issued an ID ordering a temporary stay.⁸⁶

The stay was based on the ALJs weighing of the six factors and concluding that each factor weighed in favor of a stay.⁸⁷ With regard to factor one, the ALJ emphasized that the ITC investigation was just beginning.⁸⁸ With regard to factor two, the ALJ stated that the results of the PTO reexamination would be helpful to the disposition of the investigation.⁸⁹ With regard to factor three, the ALJ stressed that it is the respondents that would be unduly prejudiced because they did not file for the reexam and did not decide when to file the complaint.⁹⁰ With regard to factor four, the ALJ considered the fact that the PTO proceeding was in an advanced state and the ITC proceeding was in an initial stage.⁹¹ With regard to factor five, the ALJ held that at this early stage in the 337 proceeding, a limited amount of Commission resources had been dedicated, thus a stay of the proceeding would be timely.⁹² With regard to factor six, the ALJ found this factor favored a stay because the complainant could be compensated monetarily for the period of the stay through the parallel district court action.⁹³ Lastly, reasoning that ITC investigations are under statutory mandate to be completed at the "earliest practicable time," the ALJ ordered a temporary stay that could be reevaluated and lifted at any time for good cause shown.⁹⁴

The Commission, agreeing with the ALJ's order, determined not to review the ID and it became the Commission's final determination.⁹⁵ In fact, the ALJ issued two subsequent IDs extending the stay and each time the Commission determined not to review, thus approving the ALJ's determinations.⁹⁶ It is interesting to note that the target date was eventually extended as a result of the stay orders. The effect of extending target dates may indicate one reason why stays are used so sparingly in the ITC.

In *Semiconductor Chips*, respondents filed a joint motion to stay the investigation on the eve of trial and although their motion was granted by the ALJ, it was reversed by the Commission upon review. In granting the motion for stay pending reexamination, the ALJ weighed the same factors above and found that "granting a stay would be the most appropriate course of action."⁹⁷ The ALJ ordered the investigation stayed pending completion of the reexamination of the two patents at issue in the investigation.⁹⁸

However, approximately one month later, the Commission reviewed and reversed the ID.⁹⁹ In its opinion, the Commission, contrary to the ALJ, found that the above factors weighed *against* granting a stay.¹⁰⁰ The Commission stated that this was particularly true in this case because a stay

84 See *Personal Computers*, Inv. No. 337-TA-558, Order No. 6 at 10.

85 71 Fed. Reg. 363-364 (January 4, 2006).

86 See *Personal Computers*, Inv. No. 337-TA-558, Order No. 6.

87 See *id.*

88 See *id.* at 10.

89 See *id.* at 11.

90 See *id.* at 11-12.

91 See *id.* at 12-13.

92 *Id.* at 13.

93 *Id.* at 14.

94 *Id.* (citing 19 U.S.C. Section 1337(b)(1)).

95 See *Personal Computers*, Notice of Decision Not to Review an Initial Determination Ordering a Temporary Stay (March 10, 2006).

96 See *Personal Computer*, Order Nos. 11, Initial Determination Granting a Three Month Stay (April 21, 2006) and 13, Initial Determination Extending Temporary Stay (July 10, 2006) and Notice of Decision Not to Review an ID Granting an Additional Three Month Stay (May 12, 2006) and Notice of Decision Not to Review an ID Extending the Temporary Stay (July 31, 2006).

97 See *Semiconductor Chips*, Inv. No. 337-TA-605, Order No. 52, at 10 (February 26, 2008).

98 See *id.*

99 See *Semiconductor Chips*, Inv. No. 337-TA-605, Notice of Commission Decision to Review and Reverse ALJ Order No. 52 (March 27, 2008) and Commission Opinion (April 29, 2008).

100 See *Semiconductor Chips*, Inv. No. 337-TA-605, Comm. Op. at 4.

would effectively terminate the investigation, “in light of the fact that the patents at issue are virtually certain to expire before the PTO’s reexamination is completed.”¹⁰¹ Further the Commission distinguished this matter from the facts in *Personal Computer* by pointing out that this Section 337 investigation was in an advanced stage (days before trial) and the PTO reexamination was in an initial stage.

In *Semiconductor Chips*, the Commission weighed the factors as follows: with regard to the first factor, the Commission found it weighed against a stay because significant expenses had already been incurred in this investigation (by the eve of trial). Additionally, the Commission pointed out that a stay at this point was contrary to Congress’ mandate and the Commission policy that Section 337 investigations be expeditiously adjudicated.¹⁰² The Commission held that the second factor, weighed in favor of a stay, but was not determinative.¹⁰³ With regard to the third factor, the Commission held that it weighed “heavily” against a stay. In fact, the Commission cautioned that respondent’s motion could be a manipulative tactic to deprive the patent holder of its rights to enforce presumably valid patents.¹⁰⁴ With regard to the fourth factor, the Commission held that it weighed against a stay because the reexamination was at an initial stage (as opposed to an advanced stage as the ALJ believed) and thus further distinguished the instant case from the circumstances present in *Personal Computer*.¹⁰⁵

Lastly, with regard to the fifth factor, the Commission found that it weighed in favor of a stay. However, in finding this, the Commission stated that this factor alone did not overcome the other factors.¹⁰⁶ In fact, the Commission noted again that the proceeding before the ALJ had reached a relatively advanced stage, which diminishes the extent of Commission resources needed to complete the investigation. Thus, the Commission dismissed the fifth factor as non-determinative.¹⁰⁷

The Commission gave the sixth factor no weight.¹⁰⁸ The Commission reasoned that since section 337 remedies are in addition to and “not instead of, other remedies at law,” remedies potentially available in the district courts are “irrelevant” to their analysis of whether to stay the proceeding.¹⁰⁹ Further, the Commission stated that it is the right of the aggrieved party to select the forum in which to pursue relief.¹¹⁰

C. Termination of An ITC Investigation At Respondents’ Request

An ITC case is frequently terminated at the request of a respondent in three circumstances pursuant to the authority of Section 337(c): settlement agreements, arbitration agreements, and license agreements.¹¹¹ The Commission Rules provide that “[a]ny party may move at any time for an order to terminate an investigation in whole or in part as to any or all respondents on the basis of a settlement agreement, a licensing or other agreement, including an agreement to present the matter for arbitration”¹¹² Termination of the investigation on these grounds need not constitute a determination that a Section 337 violation has occurred.¹¹³

In any initial determination terminating an investigation by settlement agreement, the ALJ is required to consider and make appropriate findings regarding the effect of the proposed settlement on the public health and welfare, competitive conditions in the United States economy, the production of like or directly competitive articles in the United States, and United States

101 *See id.*

102 *See id.* at 6.

103 *See id.* at 8.

104 *See id.* at 8-10.

105 *See id.* at 11-12.

106 *See id.* at 12.

107 *See id.* at 13.

108 *See id.* at 3 n. 2.

109 *Id.*

110 *Id.*

111 19 U.S.C. Section 1337(c). An investigation may also be terminated upon a respondent’s motion for termination on the basis of a consent order as stipulated to by the respondent. *Id.*

112 19 C.F.R. Section 210.21(a)(2); *see Certain Nitrile Gloves*, Inv. No. 337-TA-608 and *Certain Nitrile Rubber Gloves*, Inv. No. 337-TA-612, Order No. 91, Unreviewed Initial Determination Granting Motion To Terminate Respondent Dynarex Corporation Based on a Settlement Agreement at 2 (July 23, 2007).

113 *See* 19 C.F.R. Sections 210.21(b)(2), (d).

consumers.¹¹⁴ Thus, an ITC case can be terminated by a respondent if that respondent enters into a settlement agreement, with or without a license agreement from the complainant and moves to terminate the investigation on that basis.

Another situation where an ITC case can be terminated by a respondent is when an arbitration clause implicates the patent-in-suit. According to the explicit language of 19 U.S.C. Section 1337(c) and Commission Rule 210.21(d), the relevant inquiry in deciding whether to terminate an investigation based on an arbitration agreement is simply whether the parties agreed to “present the matter for arbitration.”¹¹⁵ So long as a party’s contentions that an issue in the investigation is arbitratable are not “wholly groundless,” the investigation should be terminated as to that issue.¹¹⁶

In *Wireless Communication Chips*, the ALJ granted respondent’s motion to terminate the investigation due to pending arbitration based on this language in the statute.¹¹⁷ In so ruling, the ALJ noted that respondents’ contentions concerning an arbitration agreement were not “wholly groundless” and that the complaint was “grossly inadequate” and not properly pled.¹¹⁸ The Commission decided not to review the ALJ’s Initial Determination making it the final determination of the Commission.¹¹⁹

Lastly, a respondent can move to terminate an ITC investigation based on a license agreement. In certain situations, a respondent can request a district court to enjoin the complainant from pursuing an ITC investigation. For example, in *Texas Instruments, Inc. v. Tessera, Inc.*, the Federal Circuit construed the scope and effect of a venue selection provision in a license agreement between Tessera and Texas Instruments (“TI”).¹²⁰ The Federal Circuit held that any disputes by and between the parties had to be resolved under mandates of that venue provision – meaning, effectively, that Tessera could only sue TI in accordance with the venue provision in the license agreement and that an action could only be brought in California and not in the ITC.¹²¹

While Tessera had a case against TI pending in a federal district court, Tessera also filed a complaint in the ITC against TI and its customer, Nokia. Following the Federal Circuit’s decision and once the matter was back before the district court judge, TI successfully moved for a preliminary injunction against Tessera. The district court judge enjoined Tessera from going forward against both TI and Nokia in the ITC and concluded that the venue provision (as interpreted by the Federal Circuit) required that any litigation against TI occur in California. Thus, as is evident from the Tessera/Texas Instruments example, a respondent can effectively stop an ITC investigation based on a license agreement.

V. STRATEGIC CONSIDERATIONS AS TO WHETHER THE ITC AND/OR DISTRICT COURT MAY BE SELECTED TO PURSUE A PATENT INFRINGEMENT CASE

A patent infringement case can be filed in any district in the United States that has personal jurisdiction over the defendant. Thus, a case may be filed in those states or districts where the defendant’s products are sold but where the defendant does not maintain offices. The venue chosen for a district court patent litigation may reflect the patent owner’s perceptions concerning the likelihood of one party or the other prevailing in the litigation, how likely it may be that the case is transferred to the defendant’s home district, how quickly a dispute is resolved, how quickly a matter may go to trial, the jury composition at trial, and other factors.

114 See 19 C.F.R. Section 210.50(b)(2); see *Certain Nitrile Gloves*, Inv. No. 337-TA-608 and *Certain Nitrile Rubber Gloves*, Inv. No. 337-TA-612, Order No. 91, Unreviewed Initial Determination Granting Motion To Terminate Respondent Dynarex Corporation Based on a Settlement Agreement (July 23, 2007) at p. 2.

115 19 U.S.C. Section 1337(c); 19 C.F.R. Section 210.21(d). See also *Certain Wireless Communication Chips and Chipsets, and Products Containing Same, Including Wireless Handsets and Network Interface Cards*, Inv. No. 337-TA-614, Order No. 5, Unreviewed Initial Determination Granting QUALCOMM’s Motion to Terminate the Investigation Due to Pending Arbitration at 17 (October 18 2007).

116 See *id.* at 14.

117 See *id.* at 17, 22-26.

118 See *id.*

119 See *Wireless Communication Chips*, Inv. No. 337-TA-614, Notice of Commission Determination Not to Review an Initial Determination Granting Respondent’s Motion to Terminate The Investigation Due to a Pending Arbitration (November 21, 2007).

120 *Texas Instruments, Inc. v. Tessera, Inc.*, 231 F.3d 1325, 1331 (Fed. Cir. 2000).

121 *Id.*

Similarly, a number of considerations may be at play in the complainant's decision to file its patent infringement complaint in the ITC. Some of these issues and considerations are discussed following a general overview of the requirements for filing a Section 337 complaint in the ITC.

A. Requirements for Filing a 337 ITC Case

The requirements for the contents of a Section 337 complaint are set forth at 19 C.F.R. Section 210.12. Before filing a complaint, the potential complainant is advised to consult the Office of Unfair Import Investigations ("OUII") to discuss procedural requirements and to submit a draft complaint for OUII's review in order to avoid issues with its complaint. Additionally, this process allows OUII to verify that the complaint is not frivolous and is properly pled.

1. The Domestic Industry Requirement

A distinct requirement of Section 337 is that complainant must satisfy the domestic industry requirement of the statute. Under Section 337, an industry in the United States "relating to the articles protected by" that intellectual property right must exist or be "in the process of being established" in order for the owner of the intellectual property right to be entitled to pursue its case at the ITC.¹²² The ITC complaint must include a description of the domestic industry affected by the alleged infringing articles.¹²³ The date for the determination of the existence and sufficiency of a domestic industry is the date of filing of the complaint.¹²⁴ If no domestic industry exists at the time of complaint, the ITC has jurisdiction to investigate if the complainant is in the process of establishing a domestic industry.¹²⁵

The domestic industry requirement entails a two-fold inquiry. First, a complainant must establish that the domestic article of commerce is actually protected by the intellectual property right asserted. In the case of a patent right, the complainant must show that the domestic article practices at least one claim of each patent asserted. This is known as the technical prong of the domestic industry requirement. Second, the complainant must demonstrate that it has made a significant economic investment in the United States related to the domestic article. This is known as the economic prong of the domestic industry requirement. Information relevant to the economic prong, including relevant operations of any licensees, encompasses but is not limited to: (i) significant investment in plant and equipment; (ii) significant employment of labor or capital; and (iii) substantial investment in the exploitation of the subject patent, copyright, trademark, or mask work, including engineering, research and development and licensing.¹²⁶

The complaint must also include a description of complainant's business and its interests in the relevant domestic industry or in the trade and commerce allegedly affected.¹²⁷ Every intellectual property based complaint should show that complainant is the owner or exclusive licensee of the subject intellectual property.¹²⁸ Additionally, the complaint should state the nature and extent of the complainant's domestic activities relating to its patented product, including production and distribution facilities, employees, and the percentage of volume added to the product resulting from these activities. When the complainant alleges an unfair act other than infringement of a patent or a registered copyright, trademark, or mask work (for example a trade dress), the complaint must state a specific theory underlying the allegations in the complaint regarding the existence of a threat or effect to destroy or substantially injure a domestic industry, to prevent the establishment of a domestic industry, or to restrain or monopolize trade and commerce in the United States.¹²⁹

Although complainants must show a domestic industry exploiting the patent or other intellectual property right in the United States, whereas no such requirement exists for enforcement of

122 19 U.S.C. Section 1337(b).

123 See 19 C.F.R. Section 210.12(a)(6)(i).

124 See *Data Storage Systems, Inv. No. 337-TA-471*, Order No. 17 (November 8, 2002) (citing *Concealed Cabinet Hinges, Inv. No. 337-TA-289*, ID at 116-117 (September 28, 1990)).

125 19 U.S.C. 1337(a)(2). See also *Scanning Multiple-Beam Equalization Systems for Chest Radiography, Inv. No. 337-TA-326*, Order No. 27 (September 16, 1991).

126 19 U.S.C. Sections 1337(a)(2), (a)(3).

127 See 19 C.F.R. Section 210.12(a)(7).

128 *Id.*

129 See 19 C.F.R. Section 210.12(a)(8).

these rights in district court, this requirement has not proved to be a significant impediment to U.S. or foreign-based companies with U.S. operations.¹³⁰ In fact, many foreign-based companies have met with success in enforcing their IP rights at the ITC.¹³¹

2. Allegation of A Section 337 Violation, Including Infringement Allegations Supported by Claim Charts (Under the New Rules)

The complaint must also set forth the basis for complainant's claim of a Section 337 violation. Accordingly, for cases alleging patent infringement as the basis for a Section 337 violation, the complaint must include: (i) an identification (and a certified copy) of each involved patent; (ii) an identification of the ownership of each involved patent (and certified copies of each assignment); (iii) identification of each licensee; (iv) identification of foreign counterpart patents and patent applications; (v) a non-technical description of the claimed invention of each involved patent; (vi) identification of the patent claims being asserted against each named respondent; (vii) a showing that each person named as violating Section 337 is importing or selling the articles alleged to violate Section 337; and (viii) drawings, photographs or other representations of both the involved imported articles alleged to infringe the patent claims and the domestic articles protected by the involved patents.¹³²

In addition, until the final rules were promulgated on July 7, 2008, complainants filing a complaint in the ITC based on allegations of patent infringement were required to provide a claim chart "that applies an exemplary claim" of each involved patent to a representative domestic article and to an allegedly infringing article of the named respondents.¹³³ However, as a result of the new amendments to the ITC Rules of Practice and Procedure, complainant's potential burdens regarding its pre-filing preparations may well have increased. Under amended Rule 210.12(a)(9)(viii), effective August 6, 2008, a complainant must include a claim chart "that applies *each asserted independent claim* of each involved U.S. patent to a representative involved article of each person named as violating section 337 . . ." ¹³⁴ The effect of this change is yet to be seen.

Some critics have argued that requiring the extra work of a claim chart for each and every independent claim at the beginning of the case, puts an additional burden on patentees and will create more work and costs at the start of the case.¹³⁵ Other practitioners feel that this work is already being completed by potential complainants in order to ensure a well-pled complaint.¹³⁶ In the comments to the published rules, the Commission stated that the patent infringement claim chart would encourage early resolution of disputes and wouldn't increase the burden a complainant already bears in preparing and filing a non-frivolous complaint.¹³⁷

Since these new rules have only been in effect for a little over two months, no real data is available to assess the impact that this rule change may have on the Section 337 caseload or otherwise to affect the Section 337 practice at the ITC.

3. Importation

Reflecting the fact that Section 337 is at bottom a trade statute, Section 337 requires that the accused violation occurs in connection with the importation, sale for importation, or sale in the United States after importation of the accused article.¹³⁸ Accordingly, Rule 210.12(a)(3) requires that each

¹³⁰ 19 U.S.C. Section 1337(a)(2).

¹³¹ See, e.g., *Certain Laminated Floor Panels*, Inv. No. 337-TA-545 (general exclusion order, cease and desist order); *Certain DVD/CD Players and Recorders, Color Television Receivers and Monitors, and Components Thereof*, Inv. No. 337-TA-542 (settlement); *Certain Semiconductor Devices and Products Containing Same*, Inv. No. 337-TA-525 (settlement); *Certain Optical Disk Controller Chips and Chipsets and Products Containing the Same, Including DVD Players and PC Optical Storage Devices II*, Inv. No. 337-TA-523 (settlement); *Certain Light-Emitting Diodes and Products Containing Same*, Inv. No. 337-TA-512 (limited exclusion order).

¹³² See *id.* Section 210.12(a)(9).

¹³³ See *id.* Section 210.12(a)(9)(viii).

¹³⁴ See 73 Fed. Reg. at 38321-22 (to be codified at 19 C.F.R. Section 210.12(a)(9)(viii)) (emphasis added). The amended rules retain the requirement of a claim chart that applies "an exemplary claim" of the patent to a representative domestic involved article. See 73 Fed. Reg. at 38322 (to be codified at 19 C.F.R. Section 210.12(a)(9)(ix)).

¹³⁵ See Sheri Qualters, *New ITC Patent Rules Criticized*, THE NATIONAL LAW JOURNAL (July 29, 2008), available at <http://www.law.com/jsp/article.jsp?id=1202423346828> (last visited September 26, 2008).

¹³⁶ See *id.*

¹³⁷ 73 Fed. Reg. at 38317.

¹³⁸ 19 U.S.C. Section 1337(a)(1)(B).

complaint before the ITC “[d]escribe specific instances of alleged unlawful importations or sales . . .”¹³⁹ Importation can be shown in many ways. For example, in the *Digital Multimeters* investigation, which resulted in the issuance of a general exclusion order and cease and desist orders against domestic respondents, specific instances of importation were described for each of 18 respondents’ products.¹⁴⁰

The *Digital Multimeters* complaint specifically alleged importation and/or sale in the United States after importation for each respondent. As proof, the complainant attached, as exhibits to the complaint, photographs of the respondents’ infringing products purchased in the United States. Additionally, the complaint included, as exhibits, purchase orders proving that the products had in fact been delivered to addresses in the United States.

Further, the complaint indicated why the product was alleged to have been manufactured overseas. For each product at issue, the complaint described whether the product was alleged to have been manufactured overseas because it was stamped with its place of origin (e.g., “Made in China”) or whether this information was provided elsewhere (i.e., respondent’s web site). The complaint included this detailed description for each respondent as well as submitting to the Commission (as exhibits to a Motion for Summary Determination) physical exemplars of these products for review. In the end, the Commission found importation, held that complainant had established a violation of Section 337, and issued a general exclusion order.¹⁴¹

B. Strategic Considerations Regarding the Timing of Filing an ITC Complaint

Although the decision as to the timing of a Section 337 complaint depends in each instance on the facts and circumstances presented, a number of strategic issues relating to timing may be considered regarding an ITC case and a parallel district court case.

Filing an ITC action concurrently with a district court action is one option that allows a complainant to preserve its choice of forum in the district court and to prevent respondents from filing a declaratory judgment action in the district court of their choice. When the cases are filed concurrently in the two fora, a respondent may choose to avail itself of the automatic stay provision of 28 U.S.C. Section 1659.

Some practitioners may choose to file an ITC investigation after they have filed a district court case. This option allows the complainant an opportunity to get a complaint filed quickly and preserve its choice of forum. As mentioned above, an ITC complaint usually requires more work than a complaint in a district court. Thus, this options allows the complainant to get a case filed (in a district court) while continuing to prepare its ITC action. Additionally, a respondent may file an ITC case as a means of putting pressure on a plaintiff in a pending district court case.

For some ITC complainants, the assignment of a particular judge to its case may have a perceived impact on the likely speed of resolution of infringement claims and procedural and substantive motions, certain procedural practices such as settlement conferences, *Markman* hearings, the availability of the judge to address promptly discovery disputes, the judge’s likely positions as to discovery practices and disputes, and other such factors. Up until the mid-1990s, new cases were assigned to the sitting ALJs by the Chief Judge. Following Chief Judge Saxon’s resignation in August 1995, cases were assigned by the Secretary’s office on a rotating basis. Although there were exceptions to this general practice, each new case was assigned to the ALJ next in line. This “rotation method” provided some predictability as to the likely assignment of a particular judge for each complaint. With the recent elevation of Judge Luckern to the Chief Judge post, the methodology for judicial assignment is not evident.

C. Protective Orders for Confidential Information

Administrative Protective Orders (“APOs”) are routinely issued by the ALJ in every Section 337 investigation in order to protect confidential business information (“CBI”). In fact, one of the

¹³⁹ 19 C.F.R. Section 210.12(a)(3).

¹⁴⁰ See *Certain Digital Multimeters and Products with Multimeter Functionality*, Inv. No. 337-TA-588, Comm’n Op. (June 3, 2008).

¹⁴¹ See *id.*

first orders issued by the ALJ is the protective order prescribing the procedure for the protection of CBI which the parties produce during discovery and as evidence in the record. This protective order is issued without consultation of the parties and is issued early to ensure that discovery proceeds without delay.

Each counsel for the parties must agree in writing to be bound by the APO at the outset of the investigation in order to obtain any information in connection with the investigation which is classified as business confidential.

Although the language in the APO may vary for each judge, there are fundamental provisions that appear in each APO. Typically APOs exclude in-house corporate counsel and business persons from having access to CBI. In effect, the APO is a one-tier order allowing only outside counsel and the OUII investigative attorney to have access to CBI information produced in the investigation. While parties may seek to modify the protective order to allow in-house counsel to have access, unless all parties agree, such a motion will almost certainly be denied. Even if allowed, in-house counsel is not permitted to see any third-party confidential information.

Although this is standard and a matter of course in ITC investigations, this differs from district court protective order practice. This distinction needs to be carefully monitored and addressed by practitioners when there is a parallel district court litigation involving a protective order that allows in-house counsel access to information deemed restricted and confidential in the ITC.

In addition to seeking modification of the ALJ's standard protective order issued as a matter of course at the outset of the investigation, parties may also seek additional protective provisions in the APO, such as particular provisions relating to experts or attorneys who are actively prosecuting patents or serving as consultants in a particular technology.

D. The One Week Trial

Some practitioners have been baffled recently by the ITC's new trend of setting a "one week trial" for certain complex ITC investigations. In fact, certain ALJs at the ITC have started trying cases in one week regardless of the number of parties and the number of patents. For example, in *Semiconductor Integrated Circuits*, the ALJ set hearing dates involving eighteen respondents and one patent to commence after a pre-hearing conference on Monday, March 9, 2008 and to conclude no later than Friday, March 13, 2008, allowing only five days to present evidence on all issues in dispute in the matter.¹⁴² In *Semiconductor Chips*, an investigation involving seven respondents and two patents, the ALJ allotted one week for the hearing. The hearing was ordered to commence on Monday, February 25, 2008 (following the conclusion of a prehearing conference) and to conclude no later than Friday, February 29, 2008 (also allowing only 5 days).¹⁴³

Faced with these difficult circumstances, respondents have attempted to negotiate additional trial time. In *Semiconductor Chips*, for example, all seven respondents filed a joint motion requesting an additional four hearing days due to (1) the number of asserted claims, (2) the number of accused products, (3) outstanding key depositions, (4) the large number of expert witnesses, and (5) the sheer complexity of the case. The OUII investigative attorney did not take a position regarding the motion. However, the ALJ found respondents' arguments unpersuasive and denied their motion to extend the hearing dates. The ALJ reasoned that the investigation involved patents that had been heavily litigated and "the requirement that Respondents are expected to coordinate their efforts to avoid duplication (Ground Rule 10.1)"¹⁴⁴

E. Available Remedies at the ITC

As noted above, the ITC is authorized to issue injunctive remedies only; monetary relief is not available at the ITC under Section 337. These remedies include limited exclusion orders, general

142 See *Certain Semiconductor Integrated Circuits Using Tungsten Metallization And Products Containing Same*, Inv. No. 337-TA-648, Order No. 10: Setting Procedural Schedule (July 1, 2008) ("*Semiconductor Integrated Circuits*").

143 See *Certain Semiconductor Chips with Minimized Chip Package Size and Products Containing Same*, Inv. No. 337-TA-605, Order No. 7, at 3 (September 19, 2007) ("*Semiconductor Chips*").

144 See *Semiconductor Chips*, Inv. No. 337-TA-605, Order No. 21, at 3 (December 28, 2007).

exclusion orders, and cease and desist orders that are designed to address the violation of Section 337 found to exist. Among the considerations that factor into the calculus of whether to pursue a claim in the ITC relates to the specifics of these remedies,

1. Enforcement of Exclusion Orders by U.S. Customs and Border Protection

Once the exclusion order issues, both respondents and complainants are well advised to meet with U.S. Customs and Border Protection's Intellectual Property Branch. This meeting provides an opportunity to discuss with CBP the specifics of the case and the involved products, any tests for infringement, any known importers, and any aliases under which known importers may import. Respondents will call particular aspects of the Commission's analysis or the scope of the order to CBP's attention in order that respondent's products may continue to lawfully enter the United States without undue complications. Additionally, this meeting is an opportunity to discuss certification of non-infringing products and the specifics of that certification. Lastly, complainants are advised to stay in regular contact with CBP to ensure that any breaches in enforcement are brought to CBP's attention.

2. Exclusion Orders and Downstream Products

The issue whether downstream products of third parties may properly be included within the scope of a limited exclusion order is a hotly debated topic in the ITC bar. This issue was recently presented in the *Baseband Processor Chips* case.¹⁴⁵ In *Baseband Processor Chips*, Broadcom filed a complaint naming only one respondent, Qualcomm.¹⁴⁶ In that complaint, Broadcom alleged that Qualcomm's chips infringe Broadcom's patents. During the liability phase of the investigation, the ALJ found that Qualcomm's chips did in fact infringe one of Broadcom's patents. With respect to remedy, Broadcom sought exclusion of not only Qualcomm chips, but also cellular handsets and other handheld devices containing Qualcomm chips imported by non-parties. The ALJ, however, recommended that the ITC exclude only the chips imported by Qualcomm and not handsets manufactured and imported by non-parties.¹⁴⁷

The Commission affirmed the ALJ's finding that Qualcomm violated section 337, however, the Commission did not adopt the ALJ's recommended remedy. Instead, the Commission issued a limited exclusion order excluding from entry not only chips imported by Qualcomm, but also handheld wireless communication devices, including cellular telephone handsets and PDAs, containing Qualcomm baseband processor chips or chipsets. In doing so, the Commission carved out from the limited exclusion order certain handsets imported on or before June 7, 2007 (the date of issuance of order), allowing such models to continue to be imported.¹⁴⁸

Following issuance of this limited exclusion order, various third parties moved the Court of Appeals for the Federal Circuit for a stay, pending appeal, of the limited exclusion order issued by the Commission on June 7, 2007.¹⁴⁹ In granting the stay, the court stated that in order to obtain a stay pending appeal, movants must establish a substantial case on the merits and that the balance of harms weigh in their favor. Finding this, the court stayed the Commission's limited exclusion order pending appeal in order to address movants' question regarding whether the Commission has the authority to issue a limited exclusion order excluding products of persons other than the named respondent found in violation under 1337(d)(1) and (d)(2).¹⁵⁰ Movants argue that under these statutory provisions, the ITC cannot exclude products of an entity unless it first determines that the entity has violated Section 337 and the movants had never been found in violation of Section 337. The appeal of the Commission's determination in that matter is pending before the Federal Circuit at this time.

¹⁴⁵ See *Certain Baseband Processor Chips and Chipsets, Transmitter and Receiver (Radio) Chips, Power Control Chips, and Products Containing Same, Including Cellular Telephone Handsets*, Inv. No. 337-TA-543, Comm'n Op. on Remedy, the Public Interest, and Bonding (June 7, 2007) ("*Baseband Processor Chips*").

¹⁴⁶ *Id.*

¹⁴⁷ *Id.* at 17.

¹⁴⁸ *Id.* at 28.

¹⁴⁹ See *Broadcom v. USITC*, No. 2007-1164, Order (Fed. Cir. November 16, 2007).

¹⁵⁰ *Id.* at 6-7.

3. General Exclusion Orders

General exclusion orders are the most potent remedy available from the ITC. This remedy distinguishes the ITC from any other forum for patent litigation. General exclusion orders are difficult to obtain and issued in limited situations, but they can provide complete relief against all infringing imports. One advantage of a general exclusion order is it eliminates the complainant's need to continue to bring cases against multiple and dispersed infringing products from numerous sources. A general exclusion order can mean relief against all infringing products, regardless of whether they originate from a named respondent in the investigation.

A permanent general exclusion order is issued under the authority of Section 337(d)(2).¹⁵¹ Such relief is appropriate where a general exclusion order “is necessary to prevent circumvention of an exclusion order limited to products of named persons,” or “there is a pattern of violation of [Section 337] and it is difficult to identify the source of infringing products.”¹⁵²

In applying these standards, the Commission evaluates the evidence presented during an investigation using the factors set forth in *Certain Airless Paint Spray Pumps & Components Thereof*, Inv. No. 337-TA-90, USITC Pub. 1199, Comm'n Op. (Nov. 1981) (*Spray Pumps*). In *Spray Pumps*, the Commission determined that to issue a general exclusion order there must be (1) “a widespread pattern of unauthorized use,” and (2) “business conditions from which one might reasonably infer that foreign manufacturers other than the respondents to the investigation may attempt to enter the United States market with infringing articles.”¹⁵³ For the purposes of obtaining a general exclusion order, a widespread pattern of unauthorized use may be established by proving as least one of the following:

- (1) a Commission determination of unauthorized importation of the infringing article into the United States by numerous foreign manufacturers; [or]
- (2) the pendency of foreign infringement suits based on foreign counterparts to the U.S. intellectual property right at issue; [or]
- (3) other evidence that demonstrates a history of unauthorized foreign use of the intellectual property right.¹⁵⁴

In addition to proving a widespread pattern of unauthorized use, the complainant must also demonstrate that business conditions exist from which one could reasonably infer that foreign manufacturers other than the respondents in the investigation may attempt to enter the United States market with infringing articles.¹⁵⁵ The Commission has held that the following factors are relevant to such an inquiry:

- (1) the existence of an established demand for the article in the U.S. market and conditions for the world market;
- (2) the availability to foreign manufacturers of U.S. marketing and distribution networks;
- (3) the cost for foreign entrepreneurs whose facilities could be converted to manufacture articles protected by the intellectual property right at issue;
- (4) the number of foreign manufacturers whose facilities could be converted to manufacture the protected article at issue; and

¹⁵¹ If the circumstances involve a named respondent found to be in default, the statute authorizes issuance of a general exclusion order under Section 337(g)(2). 19 U.S.C. Section 1337(g)(2).

¹⁵² 19 U.S.C. Section 1337(d)(2); see also *Certain Ink Markers*, Inv. No. 337-TA-522, Order No. 30 at 62.

¹⁵³ *Spray Pumps*, Inv. No. 337-TA-90, Comm'n Op. at 17-18; see *Certain Agricultural Tractors Under 50 Power Take-Off Horsepower*, Inv. 337-TA-380, USITC Pub. 3026, Comm'n Op. at 19-20 (March 1997) (*Tractors*).

¹⁵⁴ *Spray Pumps*, Inv. No. 337-TA-90, Comm'n Op. at 18-19; *Certain Two-Handle Centerset Faucets and Escutcheons and Components Thereof*, Inv. 337-TA-422, USITC Pub. 3332, Comm'n Op. at 7-8 (July 2000).

¹⁵⁵ *Spray Pumps*, Inv. No. 337-TA-90, Comm'n Op. at 18-19.

(5) the foreign manufacturers' ability to convert a facility to produce the protected articles.¹⁵⁶

F. Additional Considerations

While the ITC offers expeditious adjudication and potent remedies, other considerations also may be pertinent to the choice of forum for IP disputes. First, monetary relief is not available in the ITC, whereas district courts offer the possibility of damages for patent infringement in addition to potential injunctive relief.¹⁵⁷ Thus, a complainant whose goals include recovering damages for past infringement would of necessity have to file a case in district court.

Second, the ITC's decisions on patent issues are not subject to *res judicata* or collateral estoppel principles in subsequent district court litigation.¹⁵⁸ There is no statutory requirement that the district court in the parallel action accord the ITC's prior determination any particular deference or weight. In practice, district courts give varying weight to prior ITC determinations.

Third, in contrast to district courts, the ITC's remedial decisions are subject to statutory public interest considerations, and may potentially be disapproved by the President of the United States for policy reasons, which rarely has occurred in the history of the statute. In practice, however, rejection of remedial orders on public interest grounds by the ITC or on policy grounds by the President have been rare.

G. Additional New Rules and Their Anticipated Impact on 337 Procedures

As mentioned above, the amendments to the Commission's Rules of Practice and Procedure for Section 337 investigations became effective August 6, 2008.¹⁵⁹ The most significant of these changes has been discussed in the preceding sections above. The final regulations also contain two changes from those proposed in the Commission's Notice of Proposed Rulemaking (NPR) proposing to amend the Commission's Rules of Practice and Procedure.¹⁶⁰ None of the changes are expected to have any significant impact on Section 337 practice.

First, with regard to Rule 210.11(b), relating to the service of the complaint, the existing substantive rule is unchanged which describes the ability of the complainant with leave of the presiding ALJ to effect personal service of the complaint and notice of investigation upon a respondent where the Secretary's efforts to serve the respondent have been unsuccessful. The amendment concerns substitution of the word "complainant" for "party" in order to avoid any possible confusion.¹⁶¹

Second, with regard to Rule 210.39, the Commission adopted the commentators' suggestion to require the parties to notify the Commission of the issuance or dissolution of a stay of a parallel district court proceeding only if the issuance or dissolution actually occurs, and to provide ten days for the parties to notify the Commission.¹⁶²

EPILOGUE¹⁶³

Since the presentation of this paper at the Ninth Annual Sedona Conference in 2008, there has been a sea change in the practice of Section 337, specifically with respect to the Commission's authority to issue an exclusion order that encompasses downstream products containing an

156 *Spray Pumps*, Inv. No. 337-TA-90, Comm'n Op. at 18-19; *Faucets*, Inv. No. 337-TA-422, Comm'n Op. at 3-7; see *Tractors*, Inv. No. 337-TA-380, Comm'n Op. at 20-21.

157 See 19 U.S.C. Sections 1337(d), (e), (f).

158 The Federal Circuit has held that ITC decisions in patent matters have no preclusive effect in subsequent district court litigation under the doctrines of claim preclusion/*res judicata* and issue preclusion/collateral estoppel. See *Bio-Technology General Corp. v. Genentech*, 80 F.3d 1553, 1564 (Fed. Cir. 1996); *Texas Instruments Inc. v. Cypress Semiconductor Corp.*, 90 F.3d 1558, 1569 (Fed. Cir. 1996); *Tandon Corp. v. USITC*, 831 F.2d 1017, 1019 (Fed. Cir. 1987); *Texas Instruments Inc. v. USITC*, 851 F.2d 342, 344 (Fed. Cir. 1988); *Corning Glass Works v. USITC*, 799 F.2d 1559, 1570 n.12 (Fed. Cir. 1986).

159 73 Fed. Reg. 38316.

160 72 Fed. Reg. 72280 (Dec. 20, 2007).

161 73 Fed. Reg. at 38317.

162 *Id.* at 38318.

163 On May 5, 2009, Cecilia H. Gonzalez, the co-author of this article, passed away. Ms. Gonzalez was one of the most widely recognized and accomplished leaders in the Section 337 bar. Her loss is mourned by her colleagues at Howrey, and indeed by Section 337 and IP practitioners world-wide. This Epilogue was prepared by the co-author of this article, Juliana M. Cofrancesco, a partner at Howrey.

adjudicated infringing component. On October 14, 2008, the U.S. Court of Appeals for the Federal Circuit issued its decision *Kyocera Wireless Corp. v. International Trade Commission*,¹⁶⁴ that affects the scope of injunctive remedies available to IP rights holders in infringement actions under Section 337 before the Commission.

For the past twenty years, in Section 337 investigations involving accused components, a complainant would often name only the component producer as the respondent, but would seek exclusionary relief against downstream products containing such components. Based on this complaint and the evidence presented at the hearing, the Commission has issued limited exclusion orders directing U.S. Customs and Border Protection to stop imports of infringing articles, as well as downstream products of third parties containing those articles. However, in *Kyocera*, the Federal Circuit overruled long-standing Commission precedent on this remedial issue. The *Kyocera* decision clarified that the scope of the ITC's statutory authority to issue limited exclusion orders does not reach the downstream products of third parties. The Court held that in order to reach downstream products, either the complainant must request a general exclusion order and sustain the heightened evidentiary burden associated with this request or the downstream product manufacturers must be named as respondents in the investigation. The *Kyocera* decision, and changes to Section 337 practice in the wake of that decision, are discussed below.

A. Factual Background of the *Kyocera* Decision

Based upon a complaint filed by Broadcom Corp. on May 19, 2005, the ITC initiated an investigation, *Certain Baseband Processor Chips and Chipsets, Transmitter and Receiver (Radio) Chips, Power Control Chips, and Products Containing Same, Including Cellular Telephone Handsets*, Inv. No. 337-TA-543. Broadcom's complaint sought a limited exclusion order directed to the accused baseband processor chips as well as downstream products incorporating the chips including cell phones, PDAs, and smart phones. After conducting an investigation, the ITC found a violation of Section 337. Due to the intense public interest issues raised in the case, the Commission convened a rare public hearing on remedy and public interest issues. On June 7, 2007, the Commission issued a limited exclusion order barring entry of the accused chips and downstream products containing those chips. Exempted from the exclusion order were imports of downstream product models that had previously been imported on or before June 7, 2007. In reaching its remedy determination, the ITC applied the multi-factor analysis originated in the 1989 *EPROMs* case.¹⁶⁵

The respondent, third party handset manufacturers, and third party cellular network providers appealed the ITC's determination to the Federal Circuit. These companies also moved for a stay of the exclusion order pending appeal, which was granted by the Federal Circuit in a rare decision in Section 337 cases.

B. The Court's Holdings in *Kyocera*

On appeal, the Federal Circuit vacated and remanded the ITC's remedy determination, holding that Section 337 provides no authority to the ITC to issue a limited exclusion order barring entry of the merchandise of non-parties. Specifically, the Court noted that because the third parties were not "persons determined to be violating Section 337," as required for a limited exclusion order under Section 337(d)(1),¹⁶⁶ it was impermissible for the ITC to issue an order barring the products of these third parties that were not named in the investigation.¹⁶⁷

The Federal Circuit noted that the statute authorizes general exclusion of infringing products, regardless of source, where a complainant satisfies the heightened burdens of Section 337(d)(2).¹⁶⁸ Those factors are: (1) when it is necessary to prevent circumvention of an LEO directed to goods of named parties; or (2) when there is a pattern of violation and it is difficult to identify the source of the infringing goods.¹⁶⁹

¹⁶⁴ 545 F.3d 1340 (Fed. Cir. 2008).

¹⁶⁵ See *Certain Erasable Programmable Read Only Memories*, Inv. No. 337-TA-276, Comm'n Op. (April 28, 1989).

¹⁶⁶ 19 U.S.C. Section 1337(d)(1).

¹⁶⁷ *Kyocera*, 545 F.3d at 1357-58.

¹⁶⁸ *Id.*

¹⁶⁹ 19 U.S.C. Section 1337(d)(2).

The *Kyocera* Court's adherence to the plain meaning of the statute brought to an end the ITC's practice of extending the scope of a limited exclusion order to include not only the respondent's adjudicated components, but also the downstream products of non-parties that incorporate such components.

C. Section 337 Developments in the Aftermath of *Kyocera*

The *Kyocera* decision has led to dramatic shifts in the ITC's remedial actions not only with respect to limited exclusion orders, but also with respect to general exclusion orders. The ITC has abandoned the multi-factor *EPROMs* test previously applied in limited exclusion order cases involving downstream products. In cases where general exclusion orders are requested, it has sidelined its long-standing multi-factor analysis under 1981 *Spray Pumps* decision¹⁷⁰ in favor of applying the statutory language of the general exclusion order provision, Section 337(d)(2). There has also been an increase in the number of respondents named in Section 337 complainants, particularly downstream product manufacturers in the wake of the *Kyocera* decision. While it is too early to make predictions about future trends based on the *Kyocera* decision, it appears that the Commission's Section 337 caseload may not be significantly impacted as a result of this decision. Finally, there are currently efforts underway to seek legislative changes to the Section 337 statute to provide the Commission explicit statutory authority to reach downstream products containing accused infringing components.

170 See also *Certain Airless Paint Spray Pumps and Components Thereof*, Inv. No. 337-TA-90, USITC Pub. 1199, Comm'n Op. (Nov. 1981).

PROVING WILLFUL INFRINGEMENT POST-*SEAGATE*: DON'T DIVORCE THE WILLFULNESS ANALYSIS FROM ITS TORT FOUNDATIONS AS AN INTENT INQUIRY

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Does the new standard for willful infringement laid out by the Federal Circuit in *Seagate*¹ really signal a sea change in how willfulness will be proven? In *Seagate*, the Federal Circuit overruled the “duty of due care” standard for willful infringement set out in *Underwater Devices*² because it set too low a threshold for willful infringement, a threshold akin to mere negligence.³ Instead, the Federal Circuit held that willful infringement “requires at least a showing of objective recklessness.”⁴ The *Seagate* opinion discussed how this objective recklessness standard comports with the general understanding of willfulness in the civil context.⁵

The Court then went on to provide a two-part test:

[1] [T]o establish willful infringement, a patentee must show by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent. . . . The state of mind of the accused infringer is not relevant to this objective inquiry.

[2] If [the] threshold objective standard [of [1]] is satisfied, the patentee must also demonstrate that this objectively-defined risk (determined by the record developed in the infringement proceeding) was either known or so obvious that it should have been known to the accused infringer.⁶

The Court did not elaborate on this new standard or two-part test, instead stating “[w]e leave it to future cases to further develop the application of this standard.”⁷

Looking at the well-established meaning in the civil context of “willful” and “objective recklessness,” helps to shed light on this new test and perhaps answers, or at least raises, some questions regarding its interpretation. First, is the “state of mind of the accused infringer” really “not relevant” to the willfulness inquiry, or just not directly relevant to the first prong of an “objective recklessness” analysis? *Seagate*’s holding that “at least” a showing of objective recklessness is required, as well as basic tort law and common sense, indicates that state of mind should not be completely irrelevant to a willfulness inquiry as nothing prevents a plaintiff from trying to prove an even *higher* standard of culpability, such as “knowing” or “subjectively reckless” infringement. Second, although

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1 *In re Seagate Tech., LLC*, 497 F.3d 1360 (Fed. Cir. 2007) (en banc).

2 *Underwater Devices Inc. v. Morrison-Knudsen Co.*, 717 F.2d 1380 (1983).

3 *Seagate*, 497 F.3d at 1371.

4 *Id.*

5 *Id.* at 1370-71.

6 *Id.* at 1371.

7 *Id.*

the Court stated the objectively defined risk is “determined by the record developed in the infringement proceeding” are defenses raised only in litigation sufficient to show a defendant did not act recklessly? The history of tort and patent law indicates that because the willfulness inquiry is to determine if the accused infringer had a sufficiently culpable state of mind, defenses prepared for trial should typically not be the focus of the analysis. What is important to look at in the record of the infringement proceeding is what facts were available to the defendant as he started or continued with infringing activity and had knowledge of the patent(s), which in most circumstances will be prior to the start of litigation.

With these two considerations in mind, in practice the evidence presented to prove willful infringement may in most instances look very similar to the evidence traditionally presented in the past. Moreover, even though *Seagate* stated “state of mind” is not relevant to the first prong of the test recited, evidence regarding what the defendant knew about the patent and the reasons it had for believing it did not infringe or that the patents were invalid prior to starting, or continuing, infringing activity—the same evidence that could evidence actual state of mind—seems relevant. The only difference is the trier of fact gets to do its own analysis of those facts and determine whether the defendant’s analysis (or lack thereof) and actions were reasonable or reckless, instead of relying on the defendant’s conclusion or actual state of mind. Of course, if there is actually evidence that the defendant in fact thought it was proceeding to infringe a valid patent, it seems an even higher standard of “subjective recklessness” or “knowing” infringement would be met. At the least, this evidence of “state of mind” of the defendant would seem to be substantial evidence that the defendant acted despite an objectively high risk. In other words, if a defendant subjectively thought it was infringing, it should be easy for a jury to conclude the defendant acted unjustifiably since proceeding to do what one thinks is illegal seems clearly or objectively risky. Only when a defendant puts forth a reason or reasons why it thought at the relevant time it was not infringing or the patent is invalid, should the jury need to grapple with whether, when those reasons are objectively assessed, the risk of infringement was in fact high. Or when a defendant does not offer any reasons for why it proceeded with infringing activity, the jury will need to grapple with whether the defendant’s lack of analysis was reasonable or rather posed an unjustifiable risk, and whether the risk was really known or should have been known by the defendant.

If *Seagate* is interpreted consistently with its tort foundations, and the willfulness inquiry kept focused on its origins as a measure of culpability, a proxy for intent, *Seagate* might not represent a great sea change. On the other hand, if *Seagate* is interpreted to completely divorce state of mind from the analysis, then *Seagate* signals the Federal Circuit’s desire to practically eliminate willful infringement from patent litigations.

A. “Objective Recklessness” in the Tort Context: A State of Mind

Infringement is a strict-liability tort, and the enhancement of damages allowed upon a finding of willful infringement comports with the traditional allowance of enhanced or punitive damages for intentional torts or torts committed with a sufficient degree of culpability.⁸ For most torts actual intent does not need to be proven to merit punitive damages. Rather, tort law recognizes that torts can be committed with a state of mind falling anywhere along a broad spectrum, for example, from unknowing, to accidental, to negligently, to recklessly, to deliberately. “Willfulness” in infringement, as in other torts, is supposed to be a measure of a sufficiently culpable state of mind.⁹ Thus, willful infringement is often characterized as a question of the infringer’s intent.¹⁰

8 See, e.g., *Vulcan Eng'g Co. v. Fata Aluminium, Inc.*, 278 F.3d 1366, 1378 (Fed. Cir. 2002) (“The tort of willful infringement arises upon deliberate disregard for the property rights of the patentee.”); *SRI Int'l, Inc. v. Adv. Tech. Labs., Inc.*, 137 F.3d 1462, 1464 (Fed. Cir. 1997) (35 U.S.C. Section 284 “recognizes the tortious nature of patent infringement and the public interest in a stable patent right, for enhanced damages are not compensatory but punitive.”).

9 See, e.g., *Smith v. Wade*, 461 U.S. 30, 46-48 (1983) (“The Restatement (Second) of Torts (1977), for example, states: ‘Punitive damages may be awarded for conduct that is outrageous, because of the defendant’s evil motive or his reckless indifference to the rights of others.’ ... Most cases ... have adopted more or less the same rule, recognizing that punitive damages in tort cases may be awarded not only for actual intent to injure or evil motive, but also for recklessness, serious indifference to or disregard for the rights of others, or even gross negligence.”); *Rite-Hite Corp. v. Kelley Co.*, 819 F.2d 1120, 1125-26 (Fed. Cir. 1987) (“‘Willfulness’ in infringement as in life, is not an all-or-nothing trait, but one of degree. It recognizes that infringement may range from unknowing, or accidental, to deliberate, or reckless, disregard of a patentee’s legal rights. ... The term ‘willfulness’ thus reflects a threshold of culpability in the act of infringement that, alone or with other considerations of the particular case, contributes to the court’s assessment of the consequences of patent infringement.”).

10 E.g., *Ortho Pharm. Corp. v. Smith*, 959 F.2d 936, 944 (Fed. Cir. 1992) (“Whether infringement is ‘willful’ is by definition a question of the infringer’s intent.”); *Gustafson, Inc. v. Intervest Systems Indus. Prods.*, 897 F.2d 508, 510-11 (Fed. Cir. 1990) (“Whether an act is ‘willful’ is by definition a question of the actor’s intent, the answer to which must be inferred from all the circumstances.”).

The distinction between various categories of conduct such as “negligent” conduct, “reckless” conduct, or “intentional” conduct can be very elusive, and vary dramatically based on the tort or crime to which the conduct is supposed to be related.¹¹ According to general tort principles, the central distinction among the various categories of conduct is supposed to relate to

the actor’s degree of certainty that negative consequences will result from his act or omission. If a person acts either with the desire to cause the harm or with the belief that the harm is certain to result, the action is labeled “intentional.” If the actor has no such desire of belief, but acts unreasonably in light of the risks, his behavior is labeled “negligent.” Between the poles of “intent” and “negligence” lies the gray area of “reckless indifference.”¹²

One way to look at the distinction between an intentional violation of a right and a reckless violation of a right is to think of recklessness as a lesser form of intent. While an intentional violation of a right requires a desire to cause the violation or a belief that a violation is certain to result from one’s conduct, a reckless violation, in contrast, occurs when one believes or reasonably should believe that his conduct is *very likely*, but not certain, to result in a violation.¹³

It should be remembered that objective recklessness is a lower standard of intent than subjective recklessness or of an even higher actual intent standard. Traditionally, criminal law has permitted a finding of recklessness only when a person disregards a risk of harm of which he is aware, a “subjective” standard that requires proving what a defendant knew. On the other hand, civil law has traditionally applied a lower “objective” standard for recklessness that does not necessarily require proving what the defendant actually thought. The civil standard does not limit liability to only intentional or knowing bad faith actions, but rather permits looking at what facts were available to a defendant and then determining if under the circumstances the defendant acted (or failed to act if he had a duty to act) in the face of an unjustifiably high risk of harm that is either known or so obvious it should have been known.¹⁴

Given this role of “willfulness”, “recklessness” and “objective recklessness” in tort law as measures of culpability or surrogates for sufficient evidence of intent, it seems to defy common sense for the “state of mind” of the accuser infringer not to be relevant to an overall willfulness inquiry. A reading of *Seagate* in line with the well-established meaning in the civil context of these terms suggests that the Court merely meant that “state of mind” is not directly relevant to one prong of an “objective recklessness” analysis, but that state of mind is of course key to an overall inquiry of willfulness.¹⁵

B. *Seagate* Does Not Preclude Proving Willfulness through a Higher Standard of Intent than “Objective Recklessness”

Seagate’s primary holding that willful infringement requires “at least a showing of objective recklessness” merely defines what the *minimally* culpable state of mind needs to be, or the minimally sufficient evidence of intent that need be shown to prove willful infringement. In civil law, willfulness traditionally includes reckless violations of a standard, as well as violations that violate a higher “knowing” standard.¹⁶ Thus, while willful infringement requires *at least* a showing of objective

11 For example, *In re Albarran*, 347 B.R. 369 (9th Cir. 2006) demonstrates how in the copyright infringement context just evidence of knowledge of another’s right and proceeding with infringing activity in disregard of the right is sufficient evidence to meet even the higher “subjective” intent standard, leaving one hard-pressed to determine what evidence would meet the even lower standard of recklessness but not meet the higher standard. In *Albarran*, Chapter 7 debtors had previously been found liable for willful copyright infringement and were trying to discharge the debt in bankruptcy. The judgment creditor opposed discharge of the debt on the ground that it was nondischargeable because it was a debt for a “willful and malicious” injury. Willful copyright infringement (like willful patent infringement according to the new *Seagate* standard) can be proved by showing “knowing” infringement or “reckless” infringement. However, “reckless disregard” is insufficient to establish the nondischargeability of a debt due to “willful” injury under 11 U.S.C. Section 523(a)(6). *See id.* at 376, 385. Therefore, the bankruptcy trial court and the bankruptcy appellate panel of the Ninth Circuit in *Albarran* had to analyze whether the evidence from the copyright infringement trial was sufficient to satisfy the higher subjective intent standard or merely a lower objective recklessness standard. The court held that evidence that the infringer was aware of the plaintiff’s copyright when they took infringing duplicative actions was sufficient evidence to infer the necessary subjective intent. *See id.* at 385-86.

12 *Germany v. Vance*, 868 F.2d 9, 18 n.10 (1st Cir. 1989) (citing W.P. Keeton, D. Dobbs, R. Keeton, & D. Owen, Prosser and Keeton on the Law of Torts Section 31, pp. 169-70 (5th ed. 1984)).

13 *See id.*; Restatement (Second) of Torts Section 500, comment f (1977).

14 *See Farmer v. Brennan*, 511 U.S. 825, 836 (1994); *Safeco Ins. Co. of Am. v. Burr*, 127 S.Ct. 2201, 2208-09 & n.9, 2215 (2007); *see also Seagate*, 497 F.3d at 1371 (The “civil law generally calls a person reckless who acts ... in the face of an unjustifiably high risk of harm that is either known or so obvious that it should be known.”) (quoting *Farmer*, 511 U.S. at 836) (alteration in original).

15 *Seagate* ostensibly relied on the “well-established meaning in the civil context” of the “term willful” and its “standard” inclusion of “reckless behavior” in setting its new standard for willful infringement. 497 F.3d at 1370-71.

16 *See, e.g., Safeco*, 127 S.Ct. at 2208.

recklessness, it is consistent with traditional tort law and common sense that willfulness can be shown either through objectively reckless actions *or* by proving a higher standard of intent such as “subjective recklessness” or “knowing” infringement. The state of mind of the accused infringer must be relevant to the willful infringement inquiry because state of mind evidence is necessary to show knowing infringement or subjective recklessness. However, since *Seagate* also permits the lower “objective recklessness” standard, proving the actual state of mind of the accused infringer by clear and convincing evidence is not necessary.

The Federal Circuit has previously recognized that considerations of intent and belief—considerations most relevant to the higher “knowing” or “subjective recklessness” standards—as well as considerations of reasonableness and prudence—considerations most relevant to the “objective recklessness” standard—are all questions to be considered in assessing willfulness. In *SRI International*, the Federal Circuit wrote because all the foregoing questions must be considered by the jury and because they also relate to the credibility of the witnesses, appellate review of the willfulness issue should be particularly deferential to the trier of fact.¹⁷

C. Timing Is Everything: Evidence of Willfulness Should Typically Focus on Facts Known to Accused Infringer and His Actions Pre-Litigation

The statements in *Seagate* that the “objectively defined risk” should be “determined by the record developed in the infringement proceeding” and that the “state of mind of the accused infringer is not relevant”¹⁸ could be interpreted as indicating reasonable defenses presented at trial regarding non-infringement or invalidity necessarily preclude a finding of willfulness.¹⁹ However, such an interpretation flies in the face of the traditional meaning of willfulness in the tort context, as well as several previous Federal Circuit precedents and *Seagate*’s own reasoning for not extending waiver of privilege to trial counsel based on disclosure of an opinion of counsel by non-trial counsel. A better interpretation is that even under an “objective recklessness” analysis where the state of mind of the accused infringer is not directly relevant and which is determined by the record developed in the infringement proceeding, the key focus still must be on the facts known to the accused infringer and the accused’s actions *at the time* when the accused infringer had notice of the patents and proceeded with actions relevant to infringement. Only by looking at such evidence can the trier of fact decide whether the accused infringer acted despite an unjustifiably high risk when the facts are objectively viewed. If so, the infringer had sufficient culpability, even though the infringer may have subjectively viewed the same facts differently and thus had a different irrelevant actual state of mind regarding the likelihood of infringement or validity, or have later learned additional facts to better justify its actions.

In *Crystal Semiconductor*,²⁰ the defendant argued the jury’s verdict of willful infringement should be vacated because the defendant presented non-frivolous defenses of invalidity and non-infringement at trial. The Federal Circuit rejected this argument, stating “defenses prepared for a trial are not equivalent to the competent legal opinion of non-infringement of invalidity which qualify as ‘due care’ *before* undertaking any potentially infringing activity.”²¹

17 *SRI Int’l*, 127 F.3d at 1465 (“Since the issue of willfulness not only raises issues of reasonableness and prudence, but is often accompanied by questions of intent, belief, and credibility, appellate review requires appropriate deference to the special role of the trial court in making such determinations. ... Thus a finding of willful infringement will be sustained unless the reviewing court has a definite and firm conviction that the trier of fact erred.”) (citations omitted).

18 497 F.3d at 1371.

19 In fact, at least a couple district courts appear to have interpreted *Seagate* in such a manner as evidenced by undue reliance on litigation defenses in analyzing willful infringement issues. See *ResQNet.com, Inc. v. Lansa, Inc.*, 533 F.Supp.2d 397, 420 (S.D.N.Y. 2008) (entering judgment of no willful infringement after bench trial because “[w]hile Lansa was ultimately unsuccessful in defending against infringement or proving invalidity with regard to the ‘075 Patent, its arguments in these areas were substantial, reasonable, and far from the sort of easily-dismissed claims that an objectively reckless infringer would be forced to rely upon”); *Franklin Elec. Co. v. Dover Corp.*, No. 05-C-598-S, 2007 U.S. Dist. LEXIS 84588, at *22 (W.D. Wis. Nov. 15, 2007) (holding a prior summary judgment grant of non-infringement, even though it was reversed by appellate court, sufficient to preclude finding of willful infringement and finding all evidence regarding the defendant’s knowledge and state of mind prior to the litigation was irrelevant, and therefore granting defendant summary judgment of no willful infringement). In a post-*Seagate* opinion, the Federal Circuit wrote in *dicta* that “[a]s we stated in *Seagate*, the patentee must prove the ‘infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent.’ *Id.* at 1371. Under this objective standard, both legitimate defenses to infringement claims and credible invalidity arguments demonstrate the lack of an objectively high likelihood that a party took actions constituting infringement of a valid patent.” *Black & Decker, Inc. v. Robert Bosch Tool Corp.*, 260 F. App’x 284, 291 (Fed. Cir. 2008). While this statement could be argued as supporting an interpretation that reasonable trial defenses can prevent a finding of willful infringement, the statement is also not inconsistent with the interpretation of *Seagate* outlined in this article. Legitimate defenses can demonstrate objective reasonableness, if the defenses reflect the defendant’s thinking in starting or continuing with infringing activity upon notice of the patents. Such a connection should not automatically be assumed, though, particularly if the record contains evidence to the contrary.

20 *Crystal Semiconductor Corp. v. Tritech Microelectronics Int’l, Inc.*, 246 F.3d 1336 (Fed. Cir. 2001).

21 *Id.* at 1352 (emphasis added).

Crystal Semiconductor is not the only case in which the Federal Circuit has rejected such an argument. In *Hoechst Celanese*²² the court rejected arguments that the verdict of willful infringement could not be affirmed because the trial judge had commented that the case was “a close one” or because the Patent and Trademark Office had granted a re-examination request which also demonstrated the closeness of the case. Rather, the Court noted that in determining the issue of willfulness, the jury should “measure” the infringing behavior by assessing

the circumstances in which the infringer acted, against an objective standard of reasonable commercial behavior in the same circumstances. Willful infringement is thus a measure of reasonable commercial behavior in the context of the tort of patent infringement. The extent to which the infringer disregarded the property rights of the patentee, the deliberateness of the tortious acts, or other manifestations of unethical or injurious commercial conduct, may provide grounds for a finding of willful infringement and the enhancement of damages.²³

In *Johns Hopkins University*,²⁴ the Federal Circuit held the district court did not err in excluding evidence that the defendant CellPro had been wholly successful in an original jury trial, in a subsequent trial on willfulness and damages. After the original jury trial, the district court had granted various post-trial motions that changed certain claim constructions, found infringement of one patent as a matter of law, and granted summary judgment motions regarding infringement of another patent and validity of the patents. In the subsequent trial, the jury found CellPro had willfully infringed and granted damages to Johns Hopkins. The Federal Circuit held that the “1995 jury verdict had no bearing upon the willfulness of CellPro’s infringement on the dates it received notice of Hopkins’ patent rights.”²⁵ CellPro had notice of the patents-in-suit several years before the infringement lawsuit was filed and before they started infringing activity. The appellate court noted that the dates when CellPro had notice of the patents were “the proper times for assessing CellPro’s willfulness” and thus CellPro’s temporary victory in the 1995 trial was not “significantly probative of CellPro’s lack of culpability during the early stages of its infringing activity.”²⁶

Similarly, in *Datascope*,²⁷ in reversing a district court’s finding of no willful infringement, the Federal Circuit noted that the lower court’s reference to the fact that the Federal Circuit’s earlier decision in the case on liability issues (infringement and validity) was a 2-1 decision was improper. The dissent’s reasoning regarding non-infringement in the earlier appeal could not be attributed to the defendant nor related back to their thinking at the “critical period” when infringement began, several years prior to the first appellate decision.²⁸ In *Critikon*,²⁹ the appellate court held that the district court erred in relying on four opinions of counsel received by defendant *after* it began marketing its infringing product. The Federal Circuit reversed the district court’s finding of no willful infringement. The defendant had received four different opinions *prior* to marketing its infringing product but those opinions did not even consider that the defendant made a significant design change prior to putting the product on the market that made the product much more like the patented design and the opinions were superficial and conclusory.³⁰

Seagate does not appear to overrule the *Crystal Semiconductor* holding (or similar holdings in other cases) that non-frivolous defenses at trial cannot necessarily prevent a finding of willful infringement. In fact, *Seagate* actually quotes the same language quoted above from *Crystal Semiconductor*, and relies on its distinction between trial defenses and legal opinions prepared prior to the start of infringing activity and the filing of a lawsuit in holding that privilege waiver resulting from disclosing an opinion of counsel should not extend to trial counsel.³¹ *Seagate* notes that “in ordinary circumstances, willfulness will depend on an infringer’s prelitigation conduct.”³² It is precisely

22 *Hoechst Celanese Corp. v. BP Chems. Ltd.*, 78 F.3d 1575 (Fed. Cir. 1996).

23 *Id.* at 1583.

24 *Johns Hopkins Univ. v. Cellpro, Inc.*, 152 F.3d 1342 (Fed. Cir. 1998).

25 *Id.* at 1362-63.

26 *Id.* at 1362, 1365.

27 *Datascope Corp. v. SMEC, Inc.*, 879 F.2d 820 (Fed. Cir. 1989).

28 *Id.* at 828-29.

29 *Critikon, Inc. v. Becton Dickinson Vascular Access, Inc.*, 120 F.3d 1253 (Fed. Cir. 1997).

30 *Id.* at 1259-60.

31 *Seagate*, 497 F.3d at 1373.

32 *Id.* at 1374.

because willful infringement usually “must find its basis in prelitigation conduct,” that opinions of counsel obtained after litigation has commenced “will likely be of little significance” and why communications with trial counsel have little relevance and thus weigh against extending waiver to trial counsel.³³

Thus, if an infringer acted in bad faith and took actions intending to infringe a valid patent, or at least acted recklessly by taking actions considered commercially unreasonable in the face of the facts apparent to the infringer at the time he had notice of the patent, the fact that the infringer or its trial counsel later came up with some at least plausible defenses to infringement or validity, should not negate the infringer’s earlier bad faith or reckless actions. Infringers should “not be permitted to be saved from their flagrant disregard for the patents laws by the fortuity that when the patent in issue was closely scrutinized in [a] lawsuit, a close question of obviousness was presented.”³⁴

If the focus of a willfulness inquiry is trial defenses, and not necessarily what the accused infringer was thinking at the time he decided to engage in infringing activity with knowledge of the patent, then the deterrence purpose that underlies willful infringement will not be served.³⁵ The concept of willful infringement “is a statement that patent infringement, like other civil wrongs, is disfavored, and intentional disregard of legal rights warrants deterrence.”³⁶ In addition, the Federal Circuit has made enhancement of damages dependent on a finding of willfulness.³⁷ Thus, both the deterrence purpose, and any desire to be able to make fully economically whole one who has been wronged—the two roles that willful infringement is supposed to serve³⁸—will be disserved if *Seagate* is interpreted to ignore the true intent or culpability of the infringer so long as the bad faith infringer can later come up with at least some plausible defense at trial.

D. Proving Sufficient Culpability for Willful Infringement

In light of the considerations discussed above, the evidence a patentee should get into the record at trial and focus on in attempting to prove a defendant’s infringement was willful, either because it was knowing, subjectively reckless or objectively reckless, is evidence regarding when the defendant had knowledge of the patent or patents in suit, and actions taken (or not taken) and any statements made at that time that reflect the defendant’s state of mind as to respect for patent rights or thinking as to why respect for the patent(s) was not necessary in proceeding with infringing activity. If the accused infringer had notice of a patent prior to the start of infringing activity, their actions and thinking from the time of notice to the commencement of infringing activities would seem to be most relevant. However, their thinking and actions in continuing to infringe for a significant period of time would also be pertinent, as would be the case for accused infringers who receive notice of a patent after having already engaged in infringing activity but decide to continue with the activity. Of course, the length of time over which a defendant continues infringing activity is a factor that weighs in enhancement of damages.³⁹

Any contemporaneous statements made by the defendant or its agents that actually reflect their thinking regarding infringement or validity or the reasons why they started or proceeded with infringing activity after they had notice of the patent should be key, as such evidence could help to meet even the higher “knowing” or “subjectively reckless” standards of willfulness. For example, memorandums or emails by defendants that reflect knowledge of a patent and a belief that their action is infringing should be key evidence of willfulness. Of course, an opinion of counsel that reflects likely infringement of a valid patent would also be key, but in practice will likely never be seen since there is no reason for a defendant to disclose a negative opinion of counsel. After-the-fact

³³ *Id.*

³⁴ *Datascope*, 879 F.2d at 829 n.8 (quoting *Dickey-John Corp. v. Int’l Tapetronics Corp.*, 710 F.2d 329, 348 (7th Cir. 1983)).

³⁵ Of course, trial defenses could reflect what an infringer’s reasons were for proceeding with infringing activity at the relevant time. But such a relationship should not necessarily be presumed, especially when the record reflects contradictory facts from the relevant time frame.

³⁶ *Knorr-Bremse Systeme Fuer Nutzfahrzeuge GmbH v. Dana Corp.*, 383 F.3d 1337, 1342 (Fed. Cir. 2004) (en banc).

³⁷ *Seagate*, 497 F.3d at 1368 (“Absent a statutory guide, we have held that an award of enhanced damages requires a showing of willful infringement.”) (citing *Beatrice Foods Co. v. New England Printing & Lithographing Co.*, 923 F.2d 1576, 1578 (Fed. Cir. 1991)). In their concurrence in *Seagate*, Judges Gajarsa and Newman criticize the court for grafting willfulness onto 35 U.S.C. Section 284 and making enhancement of damages dependent on willfulness. 497 F.3d at 1376-84.

³⁸ *Rite-Hite*, 819 F.2d at 1126 (“The role of a finding of ‘willfulness’ in the law of infringement is partly as a deterrent—an economic deterrent to the tort of infringement—and partly as a basis for making economically whole one who has been wronged....”).

³⁹ *Read Corp. v. Portec, Inc.*, 970 F.2d 816, 828 (Fed. Cir. 1992).

statements made by defendants at trial regarding the reasons for why they proceeded with infringing activity should be given much less weight than pre-litigation statements (e.g. as reflected in emails or memoranda), as defendants are motivated to make self-serving statements during litigation. Although, of course, statements *against interest* elicited from a defendant or their agents or former agents during litigation can be powerful. Therefore, depositions of employees or former employees are important in looking for evidence of willful infringement.

When strong evidence of a defendant's actual state of mind exists that shows the defendant believed it would infringe the patent but proceeded to do so anyway, then the new *Seagate* test for objective recklessness has less importance because a higher knowing or subjective recklessness standard should be able to be proved. The objective recklessness analysis becomes important when the defendant offers a reason or reasons for why at the time that they had notice of the patent they believed it was, or would, not be infringed by their product or actions, or believed it was invalid. The objective recklessness analysis also has application when a defendant offers no explanation for proceeding with infringing activity with knowledge of the patent. In the first case, the trier of fact will need to do its own analysis of the explanation offered and determine whether defendant's conclusion to proceed with infringing activity was objectively reasonable in light of all the facts and circumstances at the time. If the defendant offers no explanation—i.e. the evidence shows he had notice of the patent, but no opinion of counsel or even lay analysis is presented of why the patent was viewed as not infringed or invalid—then the trier of fact will have to decide whether proceeding with infringing activity in such circumstances is objectively reasonable or unreasonable.

The question of whether or not the “no explanation” situation⁴⁰ is sufficient evidence of willful infringement is theoretically an open question since *Seagate* changed the previous “duty of care” standard. Previous case law supports that such conduct is willful or at least can be viewed by objective jurors as objectively reckless. For example, in *Crystal Semiconductor*, the record showed that the defendant had known of one of the patents-in-suit for at least a couple of years prior to the filing of suit and had looked at the patent to attempt to “design around” the patent, but never sought any advice of counsel regarding infringement before proceeding to sell accused products.⁴¹ The Court found this to be substantial evidence of willful infringement, as it found no reason to vacate the jury verdict.⁴² In *SRI International*, the Court even wrote that “[p]rudent behavior generally requires that competent legal advice was obtained before the commencement of the infringing activity.”⁴³ The Court also noted that whether willful infringement could “ever be purged by subsequent legal advice” was an open question.⁴⁴ Thus, while it appears subsequent legal advice, or subsequently developed trial defenses, *may* perhaps play a role in the analysis and may even, along with other factors, help to negate a finding of willfulness, it certainly seems reasonable for a jury to conclude that having knowledge of a patent but proceeding ahead with potentially infringing activity without properly analyzing infringement and validity issues is simply objectively unreasonable or reckless behavior that merits a finding of willful infringement. In other words, there is a strong position that the infringe-now, come-up-with-valid-defenses-later approach is objectively reckless.

Therefore, if a defendant knows that a plaintiff will be able to show at trial that the defendant had notice of the patent prior to the filing of suit (and notice that they make a product or conduct activity in the relevant field and thus may infringe) and yet the defendant chose to proceed with infringing activity, the defendant might very well want to consider disclosing an opinion of counsel or thinking how to otherwise introduce evidence of why they thought they would not infringe or that the patent was invalid. Otherwise, the defendants will risk having what the record will reflect as a stick-your-head-in-the-sand approach (simply ignoring a presumptively valid patent) be viewed as commercially unreasonable and objectively reckless. Although the Federal Circuit has made very clear that a defendant certainly *need* not present an opinion of counsel and no “adverse inference”

40 Whether a defendant never seeks advice of counsel in the first place, or does seek advice but chooses to maintain privilege and not disclose the opinion, the result should be the same; the trial record should be devoid of any reference of the defendant seeking advice of counsel. If somehow reference to the fact that advice of counsel was sought does make it into the record even though that advice is not disclosed, the trier of fact should fully discount such “evidence” as without disclosure of the actual content of the advice one has no basis to believe it was competent.

41 246 F.3d at 1352.

42 *Id.*; see also *id.* at 1346 (“willful infringement is question of fact and is reviewed by this court for substantial evidence”).

43 127 F.3d at 1468 (citing *Minnesota Mining and Mfg. Co. v. Johnson & Johnson Orthopaedics, Inc.*, 976 F.2d 1559, 1580 (Fed. Cir. 1992); *Spindelfabrik Suesen-Schurr, Stahlblecker & Grill GmbH v. Schubert & Salzer Maschinenfabrik Aktiengesellschaft*, 829 F.2d 1075, 1084 (Fed. Cir. 1987)).

44 *Id.* at 1468.

will be drawn from failure to present advice of counsel,⁴⁵ disclosing a competent, favorable opinion of counsel from prior to the start of infringing activity or shortly after receiving notice of the patent, still seems the best way for a defendant to avoid a finding of willful infringement. The Federal Circuit recently held in a post-*Seagate* case that a competent counsel opinion concluding either that the defendant did not infringe or that the patent was invalid provides a sufficient basis for the defendant to proceed with its disputed activity without engaging in “objectively reckless” behavior.⁴⁶ Of course, the patentee can always argue that a disclosed opinion of counsel was not “competent” and that it was objectively reckless for the accused infringer to have relied on it. Thus, the production of a timely opinion of counsel does not end the willful infringement inquiry.

If a defendant obtained no timely opinion of counsel upon having notice of a patent or does not wish to disclose it, then the defendant could offer testimony as to the defendant’s reasons for believing it would not infringe or that the patent is invalid. However, if the testimony has no support in documents contemporaneous to the time at which the reasons were supposedly relied on, the testimony should be subject to attack as being self-serving testimony manufactured for trial and subject to the trier of fact’s credibility determinations. And, of course, just as the competence of an opinion of counsel can be attacked so can the competence of any non-attorney reasoning presented by various fact witnesses. Reliance on non-attorney conclusions, especially if they were not written out and documented at the time and thus shown not to be conclusory, seems particularly prone to a finding of objective recklessness.

Seagate does imply that obtaining or relying on opinions of counsel may be unnecessary when the defendant has no knowledge of the patent until the filing of suit. The *Seagate* opinion states that a “substantial question about invalidity or infringement is likely sufficient not only to avoid a preliminary injunction, but also a charge of willfulness based on post-filing conduct.”⁴⁷ However, this statement does not say questions raised about infringement or validity during litigation (*i.e.* during the preliminary injunction phase or otherwise) can negate willfulness based on *pre-filing* conduct, the ordinary focus of willfulness charges. A post-filing opinion of counsel does seem unwarranted, though, if the defendant had no notice of the patents-in-suit prior to filing of the lawsuit, since defendant’s good faith belief of non-infringement or invalidity, and thus an objectively reasonable basis for choosing to continue with any allegedly infringing activity, can be evidenced by defenses fairly contemporaneously presented in the litigation. Thus, a reasonable trial defense as to non-infringement or invalidity of the patent-in-suit may be the end of a willful infringement claim when it is clear the defendant had no notice of the patent prior to the lawsuit. This should be a small fraction of cases, however, as *Seagate* noted “in ordinary circumstances, willfulness will depend on an infringer’s prelitigation conduct.”⁴⁸

What seems most likely in practice is that a trial record will reflect various competing pieces of evidence that could be argued as showing actual intent or that could be argued as evidencing objective reasonableness or recklessness. For example, the plaintiff could present a pre-litigation memorandum by an agent of a defendant that indicates a belief that the defendant is proceeding with infringing activity and that the patent is valid. The defendant could present an opinion of counsel that presents a basis for a belief of non-infringement of the patent. There could also be evidence that the company felt it completely unnecessary to do any official analysis of validity of the patent. The trier of fact must assess the credibility of the various pieces of evidence and its proponents, and weigh all the competing pieces of evidence against each other. One can imagine very different outcomes coming from the jury room, all potentially supportable. The opinion of counsel could be viewed as superficial, conclusory or biased and be given little weight, while the employee memorandum is viewed as very credible and sufficient evidence of the defendant’s true state of mind such that a knowing or subjective recklessness standard of willfulness is met. On the other hand, the memorandum could be given little weight, while the opinion of counsel is viewed as very sound and the jury concludes the company relied on its conclusion and to do so was objectively reasonable. Or,

45 *Knorr-Bremse*, 383 F.3d at 1344-46; *Seagate*, 497 F.3d at 1371 (“[W]e also reemphasize that there is no affirmative obligation to obtain opinion of counsel.”).

46 *Finsisar Corp. v. DirecTV Group, Inc.*, 523 F.3d 1323, 1339 (Fed. Cir. 2008).

47 497 F.3d at 1374.

48 *Id.*

the jury could conclude that the employee memorandum and opinion of counsel each offered sound reasoning for believing in either infringement or non-infringement and that since there seemed to be competing views within the company as to whether they were infringing, in such circumstances it was unjustifiably risky or reflective of lack of respect for the patentee's rights to proceed with the infringing activity without even analyzing the validity of the patent or further investigating infringement issues.

The possible combinations of evidence as well as the possible interpretations based on all the evidence of record and the credibility of the witnesses are endless. Even under the new "objective" standard, there appears to be plenty of space for subjective jury determinations as to what actions or inactions by a defendant constitute reckless versus reasonable behavior in light of the circumstances at the time when a defendant chose to proceed with, or continue, infringing activity with knowledge of a relevant patent, as well as many credibility determinations to make in evaluating the inevitable two sides of the story as to what the circumstances exactly were at the relevant times, and whether reliance on certain "circumstances" was objectively reasonable or reckless. There seems to still be plenty of reason to heed the earlier direction from the Federal Circuit to give appropriate deference to the trier of fact given the many questions of credibility, intent, belief, reasonableness and prudence involving in deciding the issue of willfulness.⁴⁹

CONCLUSION

An interpretation of *Seagate* that continues to focus the willful infringement analysis on the state of mind of the accused infringer, or at least the evidence regarding the facts known or available to the accused infringer and reasoning and actions taken after the time they had notice of a patent so that the jury can objectively assess whether they undertook infringing action with a sufficiently culpable "reckless" state of mind, is consistent with the tort underpinnings of willful infringement. This article offers such an interpretation and discusses some support for it. The evidence sufficient to support a finding of willful infringement based on a standard as interpreted herein might not be all that different from evidence seen in many pre-*Seagate* cases. Of course, the Federal Circuit really may intend to completely remove all "state of mind" considerations from any willful infringement analysis, and make the test completely dependent on whether a defendant can present any plausible infringement or validity defense in litigation. One, however, must question whether such a test serves the principle behind willful infringement of breeding respect for patents to protect innovation, or why enhanced damages—which are traditionally awarded for intentional torts or those engaged in with a sufficiently culpable state of mind—are dependent on a finding of willfulness. Since it seems no case would ever even proceed through litigation if there is not any plausible defense as to infringement or validity, willful infringement may become a relic of the past if such a test is the Federal Circuit's true intent, and Congress or the Supreme Court does not intervene. Only time, and perhaps some clarification from the Federal Circuit, will resolve the questions raised by *Seagate* as to the future of willful infringement.

Epilogue:

From the time when this article was originally written for and presented at last year's Sedona Conference® on Patent Litigation, district courts have continued to grapple with interpreting *Seagate* in further developing the application of the standard it articulated. At least of few of these opinions have touched on issues discussed here. For example, in *Power Integrations v. Fairchild Semiconductor*, 585 F.Supp.2d 583 (D. Del. 2008), the plaintiff argued that the strength of the defendant's defenses at trial should be irrelevant to willfulness, because the willfulness inquiry should focus on an infringer's prelitigation conduct. *Id.* at 588. The court found a tension in the case law regarding this based on *Seagate's* emphasis of prelitigation compared with the dicta in *Black & Decker* regarding defenses. *Id.*; cf. note 19 *supra*. In an effort to reconcile this perceived conflict in the law, the court concluded that the retrial on willfulness it ordered "must focus on the prelitigation conduct of the accused infringer in the first instance but must also taken [sic] into account whether the accused infringer maintained plausible or credible defenses to noninfringement and invalidity." 585

⁴⁹ See note 17 *supra*.

F.Supp.2d at 588; *see also Eastman Kodak Co. v. Agfa-Gevaert N.V.*, 560 F.Supp.2d 227, 302-305 (W.D. N.Y. 2008) (finding no infringement but nonetheless addressing evidence of defendant's pre-trial design-around efforts in stating plaintiff also failed to sustain burden of proof on willfulness and noting "[w]illfulness is assessed at the time the infringer received notice of the existence of the patent," but also noting substantial questions as to validity and infringement were raised at trial). One court has taken the approach of analyzing willfulness at different periods of time, and found the defendant liable for willful infringement for several years prior to and during the early part of litigation before the period in which defendant discovered and presented prior art that the court indicated at least provided some justification for defendant's infringing conduct. *See Krippelz v. Ford Motor Co.*, 2009 WL 799493 (N.D. Ill. Mar. 25, 2009).

Some courts appear to be more willing to analyze the evidence and grant summary judgment of no willfulness given the new *Seagate* standard. *See, e.g., Honeywell Int'l v. Universal Avionics Sys. Corp.*, 585 F.Supp.2d 636 (D. Del. 2008). Whereas many courts continue to defer to jury resolution of issues of intent, belief and reasonableness versus recklessness given the complexity of these issues and the variety of facts and evidence that can bear on them and be viewed in different ways. *See, e.g., Mass Engineered Design, Inc. v. Ergotron, Inc.*, 2009 WL 1035205, at *11-12 (E.D. Tex. Apr. 17, 2009) (rejecting defendant's argument that its trial defenses of invalidity and non-infringement should lead to JMOL of no willfulness as the "hindsight technical arguments of counsel and testimony by Defendants' expert were undoubtedly considered by the jury and given their appropriate weight" and noting there was evidence in the record jury may have relied on in finding willfulness); *Church & Dwight Co. v. Abbott Labs.*, 2008 WL 2565349, at *10 (D.N.J. June 24, 2008) (refusing to overturn jury verdict of willfulness as, viewing the evidence in the light most favorable to the non-movant, there was sufficient evidence defendant willfully infringed); *Arlington Indus., Inc. v. BridgePort Fittings, Inc.*, 2009 WL 260981, at *13 (M.D. Pa. Feb. 4, 2009) (denying defendant summary judgment of no willful infringement: "Proper adjudication of the willful infringement issue requires the factfinder to examine the totality of the circumstances. ... Much of this evidence requires judgments of credibility and the reasonableness of various business decisions.").

While courts have noted the Federal Circuit's admonishments that no adverse inferences can be drawn from failure to offer an opinion of counsel, failure to offer an opinion of counsel or some other evidence of formal analysis of infringement has been key in some findings of willfulness. *See, e.g., Kowalski v. Mommy Gina Tuna Res.*, 2009 WL 856331, at *2 (D. Haw. Mar. 30, 2009) (holding defendant's belief the patent was invalid did not negate finding of willfulness since there was substantial evidence the belief was recklessly formed: no opinion of counsel was obtained and defendant never even thoroughly read patent but rather relied largely on advice of a non-attorney friend in forming belief of invalidity); *Wordtech Sys. Inc. v. Integrated Network Solutions, Inc.*, 2009 WL 113771, at *2 (E.D. Cal. Jan. 15, 2009) (awarding treble damages after jury finding of willfulness and noting "Defendants made no effort to determine whether the patents were invalid or not infringed" despite being given notice of the patents). As before *Seagate*, evidence of copying also continues to be a strong basis for a finding of willfulness. *See, e.g., GSI Group, Inc. v. Sukup Mfg. Co.*, 591 F.Supp.2d 977, 982 (C.D. Ill. 2008) ("copying a patented device shows an objectively high likelihood that such an act would constitute infringement").

In summary, many courts appear to recognize that even after *Seagate*, the question of willful infringement can involve a complex assessment of facts known or available to the accused infringers and their actions after they had notice of a patent, that is often best suited for jury evaluation given credibility determinations and weighing of evidence that may be involved. Most courts have not ended the inquiry at whether a non-infringement or invalidity defense is presented at trial. The best way to apply the *Seagate* standard, and in what particular factual circumstances willfulness should or need not be addressed by a jury, however, is likely to continue to be an issue for the trial courts to grapple with for some time. Remembering the tort foundations of willfulness and its relationship to the inquiry of intent can be useful in thinking about the standard articulated in *Seagate* and how it should be applied to particular facts and cases.

THE “ELEVATED EVIDENTIARY BURDEN” TO PROVE INEQUITABLE CONDUCT

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I. INTRODUCTION

Inequitable conduct is a defense to patent infringement that carries a very big stick: a finding that an entire patent—or even numerous related patents—are unenforceable because of the patentee’s improper conduct before the PTO. This paper discusses the state of the law as reflected in a group of Federal Circuit opinions from approximately the last year.

If the August 2008 case of *Star Scientific*² were the latest word from the Federal Circuit, we would have little difficulty concluding that the most recent trend appears to be in the direction of strictly holding the defendant to its “elevated evidentiary burden”³ of proof for inequitable conduct and limiting the application of the doctrine to only the most culpable behavior. Indeed, *Star Scientific* teaches not only that the inference of deceptive intent cannot be inferred from materiality, but that the clear and convincing standard requires that deceptive intent must be “the single most reasonable inference” from the evidence as a whole.⁴

The problem is that *Star Scientific* is “book-ended” by conflicting cases. *Praxair*,⁵ which just issued on Sept. 29, 2008, sustained a finding of intent which was inferred simply from the high materiality of a withheld prior art reference. In the *Aventis* case decided in May 2008, the Federal Circuit denied a petition for rehearing and rehearing en banc on Sept. 25, 2008 that squarely raised the disparities between different panels in the Federal Circuit on the legal standard for intent.⁶ There appears to be an ongoing intracircuit conflict that may only be resolved in an en banc proceeding, perhaps the vehicle being an en banc petition in the *Praxis* case.

The policy implications should be further explored. The Federal Circuit has long been concerned about the frequency with which inequitable conduct is alleged in patent cases and the harm to the patent litigation system (and individual attorneys) that results.⁷ There is good reason for the Federal Circuit to focus on the problem of rampant inequitable conduct claims in litigation. Like willful infringement which the Federal Circuit addressed en banc in *In re Seagate*⁸ last year, inequitable conduct threatens to be the tail wagging the dog in patent litigation.

But if the Federal Circuit signals that the unenforceability penalty will only be applied in cases that are exceptionally “egregious” or “extreme,” some patent applicants may decide that they can game the system. As the Federal Circuit pointed out in the recent *Aristocrat* case, inequitable conduct plays an important role in the system of remedies in patent litigation as the mechanism whereby

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2 *Star Sci., Inc. v. R.J. Reynolds Tobacco Co.*, 537 F.3d 1357 (Fed. Cir. Aug. 25, 2008) (Michel, C.J.).

3 *Id.* at 1365.

4 *See id.* at 1366; *see also Scanner Techs. Corp. v. ICOS Vision Sys. Corp.*, 538 F.3d 1365, 1366-67 (Fed. Cir. June 19, 2008) (Clevenger, J.).

5 *Praxair, Inc. v. ATMI, Inc.*, 543 F.3d 1306 (Fed. Cir. Sept. 29, 2008) (Dyk, J.; Lourie, J., dissenting from the affirmance of inequitable conduct).

6 *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, No. 2007-1280, September 25, 2008, Denial of Petition for Rehearing and Rehearing En Banc.

7 *See Kingsdown Med. Consultants, Ltd. v. Hollister Inc.*, 863 F.2d 867 (Fed. Cir. 1988); *Burlington Indus. v. Dayco Corp.*, 849 F.2d 1418 (Fed. Cir. 1988).

8 *In re Seagate Tech. LLC*, 497 F.3d 1360 (Fed. Cir. 2007) (en banc).

procedural irregularities during prosecution may be redressed in the courts.⁹ Some applicants may conclude that the benefits of failing to fully meet the prescribed standards of conduct before the PTO outweigh the small risk that a finding of inequitable conduct will be affirmed on appeal.

For the inequitable conduct penalty to protect the ex parte system of patent examination, the Federal Circuit must continue to make clear that findings of inequitable conduct will be affirmed in cases where the applicant has intentionally engaged in conduct that falls short of the PTO’s standards for disclosure of material information during patent prosecution.

II. LEGAL STANDARDS FOR INEQUITABLE CONDUCT

A. *Kingsdown* and the Inequitable Conduct “Plague”

Any discussion of the Federal Circuit’s current inequitable conduct jurisprudence must begin with *Kingsdown*.¹⁰ Twenty years ago, the Federal Circuit concluded that “the habit of charging inequitable conduct in almost every major patent case had become an absolute plague.”¹¹ Later that same year, the Federal Circuit issued an en banc opinion in the case of *Kingsdown Medical Consultants, Ltd.*¹² The *Kingdown* opinion is widely understood to reflect the Federal Circuit’s desire to curtail the use of inequitable conduct claims as a litigation tactic.

Kingsdown involved a continuation application which mistakenly carried forward certain broad claims that had been rejected in the original application. The broad claims had been found allowable only after *Kingsdown* amended them to overcome an indefiniteness rejection. When *Kingdown*’s attorney carried forward the claims into the new application, the attorney inadvertently copied the rejected, broad, unamended claims. The examiner did not notice the mistake and issued the claims in a patent. The district court deemed the mistake to be “gross negligence” by the patent attorney which rose to the level of intent to deceive the PTO.¹³

The Federal Circuit reversed the district court and found no inequitable conduct. The Federal Circuit held that the district court clearly erred because there was no evidence that *Kingsdown*’s attorney intended to act inequitably.¹⁴ The Federal Circuit further held that gross negligence alone cannot justify an inference of intent to deceive the PTO.¹⁵ Importantly, in *Kingsdown*, the Federal Circuit affirmed that proof of inequitable conduct requires clear and convincing evidence of *both* materiality and intent.¹⁶

B. *Star Scientific* and the Current Law

Written by Chief Judge Michel, the August 2008 *Star Scientific* opinion includes a comprehensive review of the law of inequitable conduct.¹⁷ In his review, Chief Judge Michel sets forth what he refers to as the “elevated evidentiary burden” that the defendant must meet to prove inequitable conduct.¹⁸ As Chief Judge Michel explained:

The need to strictly enforce the burden of proof and elevated standard of proof in the inequitable conduct context is paramount because the penalty for inequitable conduct is so severe, the loss of the entire patent even where every claim clearly meets every requirement of patentability. This penalty was

⁹ *Aristocrat Techs. Australia Pty Ltd. v. Int’l Game Tech.*, 543 F.3d 657, 659 (Fed. Cir. Sept. 22, 2008) (holding there is no defense of “improper revival” of a patent application by the PTO) *cert. den.*, 129 S. Ct. 2719 (June 15, 2009).

¹⁰ *Kingsdown Med. Consultants, Ltd. v. Hollister Inc.*, 863 F.2d 867 (Fed. Cir. 1988) (en banc to overrule precedent that stated “gross negligence” mandates a finding of intent to deceive).

¹¹ *Burlington Indus. v. Dayco Corp.*, 849 F.2d 1418, 1422 (Fed. Cir. 1988).

¹² *Kingsdown*, 863 F.2d at 876-77.

¹³ *See id.* at 872.

¹⁴ *See id.* at 876.

¹⁵ *See id.*

¹⁶ *See id.* at 872.

¹⁷ *Star Sci., Inc. v. R.J. Reynolds Tobacco Co.*, 537 F.3d 1357, 1365-66 (Fed. Cir. Aug. 25, 2008) (Michel, C.J.).

¹⁸ *See id.* at 1365.

originally applied only in cases of “fraud on the Patent Office.” Subsequent case law has broadened the doctrine to encompass misconduct less egregious than fraud, but the severity of the penalty has not changed, and thus courts must be vigilant in not permitting the defense to be applied too lightly. Just as it is inequitable to permit a patentee who obtained his patent through deliberate misrepresentations or omissions of material information to enforce the patent against others, it is also inequitable to strike down an entire patent where the patentee only committed minor missteps or acted with minimal culpability or in good faith. As a result, courts must ensure that an accused infringer asserting inequitable conduct has met his burden on materiality and deceptive intent with clear and convincing evidence before exercising its discretion on whether to render a patent unenforceable.¹⁹

1. The Applicability of the Inequitable Conduct Defense

The defense of inequitable conduct usually involves allegations that a patent-in-suit was procured through improper conduct before the PTO. Patent applicants “have a duty to prosecute patent applications in the Patent Office with candor, good faith, and honesty.”²⁰ That duty requires that persons involved in the prosecution of a patent disclose all known information material to patentability to the PTO.²¹ A breach of this duty constitutes inequitable conduct and renders the entire patent (and, in appropriate cases, related patents) unenforceable.²²

Although the defense is usually predicated on misrepresentations during patent prosecution, the defense is not so limited. One example is the incorrect payment of a small entity fee.²³ In *Ulead*, the Federal Circuit stated:

[W]e no reason why the doctrine should not extend into other contexts, like the present one, where the allegation is that inequitable conduct has occurred after the patent has issued and during the course of establishing and paying the appropriate maintenance fee. In this context, it is equally important that the PTO receive accurate information from those who practice before it.²⁴

Thus, the inequitable conduct defense is not confined to instances of misrepresentation that bear on the patentability of claims in an application but may involve other types of misrepresentation to the PTO.

2. Framework of the Inequitable Conduct Analysis

The burden of proof lies with the accused infringer.²⁵ To prevail on the defense, the accused infringer must prove two factual elements: 1) materiality, and 2) intent to deceive the PTO.²⁶ Both elements are questions of fact that must be proven by clear and convincing evidence.²⁷ The defendant must make a threshold showing of *both* elements by clear and convincing evidence.²⁸ However, even after the threshold showing of both materiality and intent has been made, “[t]he district court must still balance the equities to determine whether the applicant’s conduct before the PTO was *egregious* enough to warrant holding the entire patent unenforceable.”²⁹ “Thus, even if a threshold level of both materiality and intent to deceive are proven by clear and convincing evidence, the court may still decline to render the patent unenforceable.”³⁰

19 *Id.* at 1365-66 (citations omitted).

20 *Honeywell Int’l Inc. v. Universal Avionics Sys. Corp.*, 488 F.3d 982, 999 (Fed. Cir. 2007).

21 *See* 37 C.F.R. § 1.56(a).

22 *See id.*

23 *See, e.g., Nilsen v. Oram Sylwania, Inc.*, 504 F.3d 1223 (Fed. Cir. Oct. 10, 2007) (Lourie, J.).

24 *Ulead Sys., Inc. v. Lex Computer & Mgmt. Corp.*, 351 F.3d 1139, 1144 (Fed. Cir. 2003) (internal citations omitted).

25 *See Star Sci.*, 537 F.3d at 1365.

26 *See id.*

27 *Young v. Lumenis, Inc.*, 492 F.3d 1359, 1363 (Fed. Cir. 2007).

28 *See Star Sci.*, 537 F.3d at 1365.

29 *See id.* (emphasis added).

30 *Id.*

3. Materiality

The Federal Circuit has held that “information is material to patentability when a reasonable examiner would consider it important in deciding whether to allow the application to issue as a patent.”³¹ The materiality element may be established by clear and convincing evidence that the patent applicant “made an affirmative misrepresentation of material fact, failed to disclose material information, or submitted false material information” to the PTO.³² Information is not material when it is cumulative of information previously disclosed to the PTO.³³

In evaluating materiality, the Federal Circuit has often looked to the PTO standard set forth in Rule 56.³⁴ Rule 56 imposes on “each individual associated with the filing and prosecution of a patent application ... a duty of candor and good faith in dealing with the Office, which includes a duty to disclose to the Office all information known to that individual to be material to patentability as defined in this section.”³⁵ The current version of Rule 56 makes information material to patentability if it

is not cumulative to information already of record or being made of record in the application, and

- (1) It establishes, by itself or in combination with other information, a prima facie case of unpatentability of a claim; or
- (2) It refutes, or is inconsistent with, a position the applicant takes in:
 - (i) Opposing an argument of unpatentability relied on by the Office, or
 - (ii) Asserting an argument of patentability.

A prima facie case of unpatentability is established when the information compels a conclusion that a claim is unpatentable under the preponderance of evidence, burden-of-proof standard, giving each term in the claim its broadest reasonable construction consistent with the specification, and before any consideration is given to evidence which may be submitted in an attempt to establish a contrary conclusion of patentability.³⁶

A misstatement or omission that is material under the Rule 56 standard is considered material for the purposes of the inequitable conduct inquiry, but the converse is not true. A statement can be material for the purposes of showing inequitable conduct “even if it does not meet the standard for Rule 56 if, in the totality of the circumstances, a reasonable examiner would have considered such information important in deciding whether to allow the patent application.”³⁷ It is well settled that information may be material even if that information would not by itself invalidate the claims.³⁸

4. Intent to Deceive the PTO

The showing required is *specific intent* to deceive the Patent Office. For example, where nondisclosure of prior art is alleged, “clear and convincing evidence must show that the applicant *made a deliberate decision* to withhold a known material reference.”³⁹

31 *Id.* at 1367 (referencing *Symantec Corp. v. Computer Assocs. Int'l, Inc.*, 522 F.3d 1279, 1297 (Fed. Cir. 2008); *Digital Control, Inc. v. Charles Mach. Works*, 437 F.3d 1309, 1314 (Fed. Cir. 2006)).

32 *See id.* at 1365 (referencing *Cargill, Inc. v. Canbra Foods, Ltd.*, 476 F.3d 1359, 1363 (Fed. Cir. 2007)).

33 *See id.* at 1367 (referencing *Honeywell Int'l Inc. v. Universal Avionics Sys. Corp.*, 488 F.3d 982, 1000 (Fed. Cir. 2007)).

34 *Purdue Pharma L.P. v. Endo Pharms., Inc.*, 438 F.3d 1123, 1129 (Fed. Cir. 2006).

35 37 C.F.R. Section 1.56(a).

36 37 C.F.R. Section 1.56(b).

37 *Monsanto Co. v. Bayer Biosci. N.V.*, 514 F.3d 1229, 1238 n.11 (Fed. Cir. 2008).

38 *McKesson Info. Solutions, Inc. v. Bridge Med., Inc.*, 487 F.3d 897, 913 (Fed. Cir. 2007).

39 *Star Sci.*, 537 F.3d at 1366 (quoting *Molins PLC v. Textron, Inc.*, 48 F.3d 1171, 1181 (Fed. Cir. 1995)) (emphasis supplied by Federal Circuit); *see also Kingsdown Med. Consultants, Ltd. v. Hollister Inc.*, 863 F.2d 867, 876 (Fed. Cir. 1988) (en banc) (showing of gross negligence does not meet requirement to prove intent).

Proof of intent does not require direct evidence; intent can be inferred from indirect and circumstantial evidence.⁴⁰ The indirect or circumstantial evidence must still be clear and convincing, however.⁴¹ “[T]he involved conduct, viewed in light of all the evidence, including evidence indicative of good faith, must indicate sufficient culpability to require a finding of intent to deceive.”⁴² “Further, the inference must not only be based on sufficient evidence and be reasonable in light of that evidence, but it must also be *the single most reasonable inference* able to be drawn from the evidence to meet the clear and convincing standard.”⁴³

“Materiality does not presume intent, which is a separate and essential component of inequitable conduct.”⁴⁴ The fact that information that is later determined to be material was not disclosed does not, standing alone, establish deceptive intent.⁴⁵ However, this principle has not always been strictly adhered to. As Judge Rader stated in his dissent in *Aventis*: “More recently, however, the judicial process has too often emphasized materiality almost to the exclusion of any analysis of the lofty intent requirement for inequitable conduct. Merging intent and materiality at levels far below the *Kingsdown* rule has revived the inequitable conduct tactic.”⁴⁶ This general issue—under what circumstances may deceptive intent be inferred—remains a source of uncertainty in the law and, apparently, conflict between different panels in the Federal Circuit.

5. Balancing by the Court

If, and only if, materiality and intent have both been shown by clear and convincing evidence, the court will engage in a balancing analysis to determine whether to exercise its discretion to hold the patent unenforceable.⁴⁷ “[T]he district court must balance the *substance* of those now-proven facts and all the equities of the case to determine whether the severe penalty of unenforceability should be imposed.”⁴⁸ However, even after the threshold showing of both materiality and intent has been made, “[t]he district court must still balance the equities to determine whether the applicant’s conduct before the PTO was *egregious* enough to warrant holding the entire patent unenforceable.”⁴⁹ “Thus, even if a threshold level of both materiality and intent to deceive are proven by clear and convincing evidence, the court may still decline to render the patent unenforceable.”⁵⁰ “The more material the omission or the misrepresentation, the lower the level of intent is required to establish inequitable conduct, and vice versa.”⁵¹

6. Standard of Review by the Appellate Court

Most findings of inequitable conduct are appealed to the Federal Circuit after a bench trial. Accordingly, the usual standard of review is two-tier.⁵² The Federal Circuit reviews the district court’s underlying factual determinations for clear error.⁵³ The Federal Circuit then reviews the district court’s ultimate decision as to inequitable conduct for abuse of discretion.⁵⁴ If the district court’s determination was based on a clearly erroneous finding of materiality or intent, a misapplication of law, or a clear error of judgment, the Federal Circuit will find that the district court abused its discretion and reverse.⁵⁵

40 See *Star Sci.*, 537 F.3d at 1366 (referencing *Cargill*, 476 F.3d at 1364).

41 See *id.* (referencing *Ferring B.V. v. Barr Laboratories, Inc.*, 437 F.3d 1181, 1186 (Fed. Cir. 2006)).

42 *Impax Labs, Inc. v. Aventis Pharms, Inc.*, 468 F.3d 1366, 1374-75 (Fed. Cir. 2006) (quoting *Kingsdown*, 863 F.2d at 876).

43 *Star Sci.*, 537 F.3d at 1366-67 (referencing *Scanner Techs. Corp. v. ICOS Vision Sys. Corp.*, 538 F.3d 1365, 1376 (Fed. Cir. 2008)) (emphasis added).

44 *Id.* at 1366 (quoting *GFI, Inc. v. Franklin Corp.*, 265 F.3d 1268, 1274 (Fed. Cir. 2001)).

45 See *id.*

46 *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, 525 F.3d 1334, 1350 (Fed. Cir. May 14, 2008) (Rader, J., dissenting).

47 *Star Sci.*, 537 F.3d at 1367.

48 *Id.* (quoting *Molins*, 48 F.3d at 1178) (emphasis supplied by Federal Circuit).

49 See *id.* at 1365 (emphasis added).

50 *Id.*

51 *Id.* at 1367 (referencing *Critikon, Inc. v. Becton Dickinson Vascular Access, Inc.*, 120 F.3d 1253, 1256 (Fed. Cir. 1997)).

52 See *id.* at 1365.

53 See *id.*

54 See *id.*

55 See *id.*; see also *Larson Mfg. Co. v. Aluminar Prods, Ltd.*, 559 F.3d, 1317, 1327 (Fed. Cir. Mar. 18, 2009) (“An abuse of discretion occurs when (1) the trial court’s decision is clearly unreasonable, arbitrary, or fanciful, (2) the court’s decision is based on an erroneous construction of the law, (3) the court’s factual findings are clearly erroneous, or (4) the record contains no evidence upon which the court rationally could have based its decision. See *W. Elec. Co. v. Piezo Tech., Inc.*, 860 F.2d 428, 430-31 (Fed. Cir. 1988).”).

Alternatively, if the appeal is from a grant of summary judgment by the district court, the Federal Circuit’s review is *de novo* and nondeferential.⁵⁶

III. RECENT CASES

In this section, we summarize recent Federal Circuit cases in chronological order. The following section discusses the trends in the cases and some additional issues.

A. *McKesson*⁵⁷

In *McKesson*, the Federal Circuit affirmed a finding of inequitable conduct after a bench trial. Judge Newman dissented.

The alleged conduct involved the failure of a patent attorney to submit three pieces of material information during prosecution.⁵⁸ The case involved three applications pending in the PTO before two different examiners.⁵⁹ The attorney failed to disclose to the second examiner in the second case (1) a prior art patent found by the first examiner in the first case; (2) the initial rejection of broad claims by the first examiner in the first case; and (3) the allowance of claims in the third case by the second examiner (*i.e.*, failure to disclose to the same, second examiner).

The trial court held a bench trial limited to the inequitable conduct defense, which resulted in the judgment of unenforceability of the patent-in-suit. The district court found the three items of information to be individually and collectively material.⁶⁰ The district court also found that circumstantial evidence and the lack of a credible explanation warranted a finding of deceptive intent.⁶¹ The intent finding was apparently buttressed by the patent attorney’s testimony that he would make the same decisions not to disclose if given the chance to prosecute the same applications again.⁶²

Regarding the first allegation, the district court concluded that the second examiner would have found the new prior art patent highly material and not cumulative.⁶³ Among other reasons, before the first examiner found the new prior art patent, the same relevant prior art had been submitted in both the first and second cases.⁶⁴ Further, the first examiner found the new prior art patent was not cumulative. Intent to deceive was established, in part, because the new prior art patent rendered untrue a statement by the patent attorney to the second examiner just seventeen days before and the attorney “could not have (or certainly should not have) missed [the patent’s] significance.”⁶⁵

The Federal Circuit held that the district court did not err in concluding that the new prior art patent was material and not cumulative.⁶⁶ Based on the circumstances of the attorney’s discussions with the two examiners, the Federal Circuit concluded that the attorney knew or should have known of the high materiality of the art, and that the district court did not err in finding that deceptive intent was established in light of the circumstantial evidence and the lack of a credible explanation.⁶⁷

As to the second allegation concerning nondisclosure of rejections in the first case, the Federal Circuit found the rejections material because of the similarities between the claims in the two cases such that the rejections should have been disclosed to the second examiner.⁶⁸ Moreover, the

⁵⁶ See *Eisai Co. Ltd. v. Dr. Reddy’s Labs, Inc.*, 533 F.3d 1353, 1359 (Fed. Cir. July 21, 2008) (Rader, J.).

⁵⁷ *McKesson Info. Solutions, Inc. v. Bridge Med., Inc.*, 487 F.3d 897 (Fed. Cir. May 18, 2007) (Clevenger, J.; Newman, J., dissenting).

⁵⁸ See *id.* at 901.

⁵⁹ See *id.* at 904.

⁶⁰ See *id.* at 901.

⁶¹ See *id.*

⁶² See *id.*

⁶³ See *id.* at 909.

⁶⁴ See *id.* at 908.

⁶⁵ See *id.*

⁶⁶ See *id.* at 913-17.

⁶⁷ See *id.* at 917-20.

⁶⁸ See *id.* at 919-23 (relying on Manual of Patent Examining Procedure Sections 2001.04, 2001.06).

Federal Circuit affirmed the finding of intent by clear and convincing evidence notwithstanding that the existence of the first case was disclosed to the second examiner.⁶⁹

The third and last inequitable conduct allegation was based on the attorney's failure to inform the second examiner that the same, second examiner had granted a related case—the third case—a few months before. The existence of the third case had been disclosed to the second examiner, but not the fact that he granted the case. Although the Federal Circuit recognized that the information could have been cumulative and not material if the second examiner remembered that he granted the third case, the court said that there was no evidence on that point. The withholding of this information was deemed material and done with deceptive intent. The Federal Circuit found no clear error in the findings of materiality and intent to deceive and no abuse of discretion in the district court's finding of inequitable conduct.

Judge Newman's dissent⁷⁰ was focused on the failure to require clear and convincing evidence of deceptive intent. Judge Newman stated that the failure to require such evidence of intent to deceive would do nothing but encourage a return to the "plague" of inequitable conduct claims and opportunistic litigation that the Federal Circuit has tried to discourage.

B. *Nilssen*⁷¹

In *Nilssen*, the Federal Circuit affirmed a holding of inequitable conduct after a bench trial that resulted in the unenforceability of fifteen patents.⁷² *Nilssen* involved an inventor who represented himself in the prosecution of his patents.⁷³ There were numerous allegations of inequitable conduct, including failure to disclose that a person who submitted declarations to the PTO had a financial interest in Nilssen's patents; incorrect payment of small entity maintenance fees; intentionally misclaiming a priority date; failure to disclose ongoing litigation to the examiner; and failure to identify prior art in patent prosecution.⁷⁴ The Federal Circuit affirmed findings of inequitable conduct based on each of these allegations. The Federal Circuit concluded its opinion by commenting that it was the collection of the problems, not the allegations considered individually, that indicated "repeated attempts to avoid playing fair and square with the patent system" and that the outcome of the case indicates that Mr. Nilsson erred in his belief that he had no need of professional assistance in dealing with the complicated patent process.⁷⁵

C. *Innogenetics*⁷⁶

In *Innogenetics*, the Federal Circuit affirmed a grant of summary judgment of no inequitable conduct on the grounds that alleged misrepresentations regarding a prior art reference were "mere attorney argument" and thus not material.⁷⁷

In an EPO proceeding, the prosecuting attorney identified the Cha PCT application as the "closest prior art," under a "problem solution" framework that is used in European practice.⁷⁸ The attorney argued, however, that none of the submitted references taught or disclosed the claimed method.⁷⁹ The EPO found that certain claims were not novel in light of the Cha PCT application. Claims were therefore amended with a disclaimer that they were "amended to disclaim the teaching of the Cha PCT application."⁸⁰

69 See *id.* at 922.

70 See *id.* at 926 (Newman, J., dissenting). Judge Newman filed an extensive dissent along the same lines in *Ferring B.V. v. Barr Laboratories, Inc.*, 437 F.3d 1181, 1203 (Fed. Cir. 2006) (Newman, J., dissenting) ("The panel majority's holding that deceptive intent is established as a matter of law if the applicant 'should have known' that information might be material to patentability, further revives the 'plague' of the past, with burdens that far outweigh any conceivable benefits."). In *Ferring*, the Federal Circuit found inequitable conduct based on declarations submitted to the PTO where *Ferring* failed to disclose that the declarants had previously been paid consultants.

71 *Nilssen v. Ovrarn Sylvaria, Inc.*, 504 F.3d 1223 (Fed. Cir. Oct. 10, 2007) (Lourie, J.).

72 See *id.* at 1226.

73 See *id.* at 1226-27.

74 See *id.* at 1227-29.

75 See *id.* at 1235.

76 *Innogenetics, N.V. v. Abbott Labs.*, 512 F.3d 1363 (Fed. Cir. Jan. 17, 2008) (Moore, J.).

77 See *id.* at 1379.

78 See *id.* at 1378-79.

79 See *id.* at 1379.

80 See *id.*

In the prosecution of the patent-in-suit, the Cha PCT application was submitted with an international search report that noted the application as problematic.⁸¹ The attorney that prosecuted the U.S. application submitted an accompanying prior art statement that “the references do not relate to the invention and, therefore, further discussion of the same is not necessary.”⁸² The attorney later admitted, however, that he did not actually examine the prior art references and his statement was boilerplate that he used on other occasions.⁸³

The Federal Circuit agreed with the district court that the materiality prong was not met. The statements regarding the Cha PCT application were “mere attorney argument.”⁸⁴ Moreover, because the Cha PCT application itself was submitted to the PTO examiner, he or she was free to examine it herself and accept or reject Innogenetics’ arguments.⁸⁵

D. *Monsanto*⁸⁶

In *Monsanto*, the Federal Circuit affirmed a holding of inequitable conduct after a bench trial.⁸⁷ The inequitable conduct was based on Bayer’s failure to submit a scientist’s notes from a scientific meeting that were inconsistent with arguments regarding patentability that Bayer was making.

The Barnes Abstract was submitted as prior art in the prosecution of the patent-in-suit.⁸⁸ The Barnes Abstract was published in conjunction with a scientific conference. In a poster presented at the meeting, Dr. Barnes presented additional data that confirmed additional accomplishments not mentioned in the Abstract. A Bayer scientist attended the meeting and took notes, which were later provided to others at Bayer, but were not disclosed to the PTO.⁸⁹

The description of the additional accomplishments in the attendee’s notes were inconsistent with arguments made by Bayer to the PTO.⁹⁰ The district court found it “very obvious” that the content of the notes were in “sharp contradiction” to Bayer’s arguments to the examiner.⁹¹ The district court found not credible testimony from Bayer that its scientists did not appreciate the content of the notes or that the notes were not submitted because they were illegible.⁹²

The Federal Circuit affirmed. The Federal Circuit held that the notes were highly material because they directly contradicted arguments made to the PTO in support of patentability.⁹³ As to intent, the Federal Circuit stated that “absent a credible reason for withholding the information, intent may be inferred where a patent applicant knew, or should have known, that withheld information would be material to the PTO’s consideration of the patent application.”⁹⁴ The Federal Circuit held that the district court did not clearly err in finding intent on the grounds that the explanations offered by Bayer were not credible.

E. *Pfizer*⁹⁵

In *Pfizer*, the Federal Circuit affirmed a finding of no inequitable conduct after a bench trial because, even if the two nondisclosed prior art references were material, there was insufficient proof of intent to deceive.⁹⁶

81 *See id.*

82 *See id.*

83 *See id.*

84 *See id.*

85 *See id.*

86 *Monsanto Co. v. Bayer Biosci. N.V.*, 514 F.3d 1229 (Fed. Cir. Jan. 28, 2008) (Gajarsa, J.).

87 *See id.* at 1233, 1242.

88 *See id.* at 1234.

89 *See id.* at 1235-36.

90 *See id.* at 1238-39.

91 *See id.* at 1239.

92 *See id.* at 1241.

93 *See id.* at 1240.

94 *See id.* at 1241.

95 *Pfizer, Inc. v. Teva Pharms. USA, Inc.*, 518 F.3d 1353 (Fed. Cir. Mar. 7, 2008) (Dyk, J.).

96 *See id.* at 1366.

The defendant argued on appeal that the materiality of the references, standing alone, was sufficient to establish intent, if the patent holder offered no credible explanation for withholding them.⁹⁷ But the district court found that Pfizer did offer a good faith explanation. One of the named inventors testified that Pfizer concluded that the prior art references were significantly distinct from the compounds in the application and did not meet the usual criteria for disclosing similar compounds to the PTO. The district court found the testimony credible and recognized Pfizer's "highly consistent pattern" when determining which compounds should be disclosed as supporting good faith. The Federal Circuit agreed that there was no basis for finding inequitable conduct, because the materiality of a reference is insufficient to establish intent where the applicant has provided a credible explanation for the withholding of a reference.⁹⁸

F. *Ortho-McNeil*⁹⁹

In *Ortho-McNeil*, the Federal Circuit affirmed summary judgment of no inequitable conduct. The inequitable conduct allegation involved tests by the applicant on prior art compounds.¹⁰⁰ The defendant contended that the applicant's own tests yielded data that were inconsistent with arguments that the applicant made during prosecution about the teachings of the prior art but the applicant did not disclose those test data to the PTO.¹⁰¹ The Federal Circuit agreed with the district court that the applicant did not misrepresent the teachings in the references, and only repeated what the references themselves said.¹⁰² Furthermore, the applicant never made any affirmative representations that contradicted its own test results regarding the properties of the prior art compounds.¹⁰³ The Federal Circuit thus affirmed the district court's dismissal of the inequitable conduct claims.¹⁰⁴

G. *Symantec*¹⁰⁵

In *Symantec*, the Federal Circuit affirmed a grant of summary judgment of no inequitable conduct.¹⁰⁶ *Symantec* involved three alleged material misrepresentations in declarations filed with the PTO.

The first inequitable conduct claim involved inventor-of-record Gray's alleged misrepresentation that he was an inventor in a declaration filed with the application.¹⁰⁷ At trial, the inventor was unable to identify with specificity what his contribution was. The Federal Circuit agreed with the district court that, particularly in light of a co-inventor's testimony that Gray came up with the idea for the invention, Gray's testimony only showed that his memory had lapsed and did not create a genuine issue of material fact that Gray was not an inventor.

The second inequitable conduct claim was based on Gray's statements in a second declaration responding to an office action.¹⁰⁸ Gray stated that he was familiar with the state of the art relating to computer viruses and computer virus prevention. Gray also stated that he set out to develop an algorithm to check a computer file for virus infections. These statements were allegedly false because Gray was a marketing and not a technical person, and someone else actually developed the algorithm itself. The Federal Circuit agreed with the district court that Gary's statements did not establish any genuine issue whether the declaration was false or misleading.

97 See *id.* at 1366-67.

98 See *id.* at 1367 (relying on *Ferring B.V. v. Barr Labs., Inc.*, 437 F.3d 1181, 1191 (Fed. Cir. 2006) (three conditions must be met where a party relies solely on the materiality of the references to prove intent: "(1) the applicant knew of the information; (2) the applicant knew or should have known of the materiality of the information; and (3) the applicant has not provided a credible explanation for the withholding").

99 *Ortho-McNeil Pharm., Inc. v. Mylan Labs., Inc.*, 520 F.3d 1358 (Fed. Cir. Mar. 31, 2008) (Rader, J.).

100 See *id.* at 1363.

101 See *id.*

102 See *id.*

103 See *id.*

104 See *id.*

105 *Symantec Corp. v. Computer Assocs. Int'l, Inc.*, 522 F.3d 1279 (Fed. Cir. Apr. 11, 2008) (Dyk, J.).

106 See *id.* at 1296.

107 See *id.* at 1297.

108 See *id.*

The third inequitable conduct allegation was based on the statement in a declaration by another co-inventor Wakelin that he had reviewed and understood the contents of the application and the claims.¹⁰⁹ Wakelin later testified that he only understood the claims in general terms. The district court found that materiality was not established even if Wakelin did not fully understand the claim language, and the Federal Circuit agreed.

H. *Aventis*¹¹⁰

In *Aventis*, the Federal Circuit affirmed a finding of inequitable conduct after a bench trial. In an previous appeal, the Federal Circuit affirmed that the information at issue was material to patentability but reversed the grant of summary judgment of inequitable conduct because there were genuine issues of material fact as to intent.¹¹¹ In this appeal, the Federal Circuit affirmed the district court’s finding of an intent to deceive the PTO. Judge Rader dissented.

The inequitable conduct involved the failure of a noninventor scientist to disclose that two sets of data that he compared in submissions to the PTO were obtained at different dosages.¹¹² The patented drug consists of heparins that are used medically to prevent abnormal blood clotting. The comparison was between the half-lives of the claimed drug and a prior art drug. The scientist did not disclose that the two sets of data that he compared were obtained using different dosages.

In an earlier 2006 opinion, the Federal Circuit held that the withheld information was material to patentability in view of *Aventis*’ repeated arguments to the examiner that the half-life differences were highly significant.¹¹³ On remand, the district court held a bench trial limited to the issue of intent. The district court rejected various explanations from the scientist, including that the clinically relevant dosages were different for the two compounds and the half-life data were appropriately compared at those relevant dosages. The Federal Circuit found that the district court did not clearly err in rejecting the proffered explanation of mere inadvertence and finding intent to deceive the PTO.¹¹⁴

Judge Rader dissented.¹¹⁵ In introductory discussion, Judge Rader stated that “my reading of our case law restricts a finding of inequitable conduct to only the most extreme cases of fraud and deception.”¹¹⁶ Judge Rader further stated that “equitable conduct has taken on a new life as a litigation tactic” and that “this court ought to revisit occasionally its *Kingsdown* opinion”¹¹⁷ which “properly made inequitable conduct a rare occurrence.”¹¹⁸ Judge Rader blamed a “judicial process [that] has too often emphasize materiality almost to the exclusion of any analysis of the lofty intent requirement for inequitable conduct. Merging intent and materiality at levels far below the *Kingsdown* rule has revived the inequitable conduct tactic.”¹¹⁹ Judge Rader went on to note that “[t]his court has even observed a number of cases, such as this one, that arrive on appeal solely on the basis of inequitable conduct where the trial court has apparently elected to try this issue in advance of the issues of infringement and validity.”¹²⁰

Judge Rader’s view was that the record did not show clear and convincing evidence of intent to deceive the PTO.¹²¹ He noted that while the clear-error standard of review is high, “it is not insurmountable.”¹²² Judge Rader observed that the failure to disclose the information was consistent with oversight and the evidence did not indicate active attempts to conceal information. Judge Rader

109 See *id.* at 1298.

110 *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, 525 F.3d 1334 (Fed. Cir. May 14, 2008) (Prost, J.; Rader, J., dissenting).

111 *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, No. 05-1513, 2006 U.S. App. LEXIS 14778, at *19 (Fed. Cir. June 7, 2006) (Prost, J.) (nonprecedential).

112 See *Aventis*, 525 F.3d at 1341.

113 See *id.*

114 See *id.* at 1349.

115 See *id.* at 1349 (Rader, J., dissenting).

116 See *id.* (Rader, J., dissenting).

117 See *id.* (Rader, J., dissenting).

118 See *id.* at 1350 (Rader, J., dissenting).

119 See *id.* (Rader, J., dissenting).

120 See *id.* (Rader, J., dissenting) (citing cases); see also *Research Corp. Techs., Inc. v. Microsoft Corp.*, 536 F.3d 1247 (Fed. Cir. Aug. 1, 2008) (Rader, J.) (discussed *infra*).

121 See *Aventis*, 525 F.3d at 1349 (Rader, J., dissenting).

122 See *id.* at 1351 (Rader, J., dissenting).

stated that he found “it difficult to fathom” that a scientist of such stature would risk tarnishing his stellar professional reputation with a false submission to the PTO for an invention in which that scientist was not even involved. Judge Rader also pointed out that two individuals, the prosecuting attorney and the scientist, had apparently made the same mistake. Moreover, the scientist himself subsequently disclosed and corrected the error with a second declaration to the PTO.

The Federal Circuit recently denied rehearing and rehearing en banc in *Aventis*.¹²³ *Aventis*’s petition argued that the *Aventis* decision “effectively dispens[ed] with the separate element of ‘intent’ in inequitable conduct cases involving a material omission.”¹²⁴ *Aventis* further argued that courts applied this erroneous view of the law “regularly hold[ing] patents unenforceable for mere negligence.”

Aventis’s petition for en banc review was supported by numerous amici curiae, including the Biotechnology Industry Organization, the Pharmaceutical Research & Mfrs. of America, Johnson & Johnson, Eli Lilly & Co., Caterpillar Inc., 3M Co., and a group of law professors. Among other things, the amici stressed the inefficiencies and burden that result from forced overdisclosure of marginally relevant information during prosecution and “the potential under-explanation of what is salient to the examination process.”¹²⁵

I. *Scanner Technologies*¹²⁶

In *Scanner Technologies*, the Federal Circuit reversed a finding of inequitable conduct after a bench trial because the district court clearly erred in its finding of materiality.¹²⁷

Scanner Technologies involved a petition to make special.¹²⁸ The patent holder learned that the accused infringer had launched a competing product that allegedly infringed claims of its patent applications.¹²⁹ The applicant filed a petition to make special to seek accelerated review of its patent applications because of actual infringement.¹³⁰ A declaration in support of the petition allegedly contained false statements, including statements regarding the accused infringer’s conduct at trade shows where the patent holder’s invention had been displayed.¹³¹ The petition to make special was granted.¹³² The district court concluded that the allegedly false statements were intended to mislead the PTO into believing that the accused infringer had actually copied the patent holder’s invention after viewing it at trade shows.¹³³ The district court found to the contrary, that the alleged infringer had developed the accused product from an earlier product of its own.¹³⁴

The Federal Circuit first held that the materiality prong could be met by false statements that did not relate to patentability: “When the setting involves a petition to make special, as is the case here, we reaffirm that a false statement that succeeds in expediting the application is, as a matter of law, material for purposes of assessing the issue of inequitable conduct.”¹³⁵

However, the finding of materiality was overturned because the district court’s interpretation of those statements was rejected by the Federal Circuit.¹³⁶ The Federal Circuit stated that, in assessing the evidence, all reasonable inferences must be considered by the court: “Whenever evidence proffered to show either materiality or intent is susceptible of multiple reasonable inferences, a district court clearly errs in overlooking one inference in favor of another equally

¹²³ *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, No. 2007-1280, September 25, 2008, Denial of Petition for Rehearing and Rehearing En Banc.

¹²⁴ See Combined Petition for Panel Rehearing and Rehearing En Banc of *Aventis* at 1-2, available at 2008 WL 2761591.

¹²⁵ Brief for Multiple Companies as *Amici Curiae* in Support of Panel Rehearing or Rehearing En Banc at 3; see also, e.g., *Amicus* Brief of Biotechnology Industry Organization in Support of Plaintiff-Appellant *Aventis*’s Petition for Rehearing or Rehearing En Banc, available at 2008 WL 2952312; Brief for Johnson & Johnson as *Amicus Curiae* in Support of Panel Rehearing or Rehearing En Banc, available at 2008 WL 2952313.

¹²⁶ *Scanner Techs. Corp. v. ICOS Vision Sys. Corp.*, N.V., 538 F.3d 1365 (Fed. Cir. June 19, 2008) (Clevenger, J.).

¹²⁷ See *id.* at 1379.

¹²⁸ See *id.* at 1370.

¹²⁹ See *id.*

¹³⁰ See *id.*

¹³¹ See *id.* at 1372 & n.2.

¹³² See *id.* at 1370.

¹³³ See *id.* at 1372.

¹³⁴ See *id.*

¹³⁵ *Id.* at 1375.

¹³⁶ See *id.* at 1379.

reasonable inference.”¹³⁷ The opinion further explained that “[i]n light of the requirement that inequitable conduct be found by clear and convincing evidence, the district court erred when it adopted an unfavorable inference regarding [one of the statements at issue] over an equally reasonable favorable inference.”¹³⁸

According to the Federal Circuit, all the allegedly false statements relied on by the district court were subject to reasonable interpretations that were different from the ones that the district court reached.¹³⁹ The evidence was not clear and convincing that the patent holder falsely told the PTO that the accused infringer copied the invention.¹⁴⁰ The evidence showed that the patent holder simply told the PTO in the declaration that it believed there was infringement.¹⁴¹

J. *Eisai*¹⁴²

In *Eisai*, the Federal Circuit affirmed findings of no inequitable conduct after a bench trial and on summary judgment.¹⁴³ There were five separate bases for the alleged inequitable conduct.¹⁴⁴ All the inequitable conduct allegations were rejected by the district court and the Federal Circuit affirmed.

The first four allegations were the subject of bench trial. The first allegation was that *Eisai* failed to disclose a co-pending application to the examiner of the patent-in-suit.¹⁴⁵ The Federal Circuit determined that the disclosure would have been prudent.¹⁴⁶ The Federal Circuit held, however, that the district court had ample evidence that the materiality of the other application was low based on testimony and evidence that the compounds in the two applications were believed to be separately patentable and were not viewed “primarily in relation to one another” by the *Eisai* scientists.¹⁴⁷ The Federal Circuit held, moreover, that the record was “devoid of any real suggestion of intent” to deceive the patent office.¹⁴⁸

The second allegation was that *Eisai* failed to disclose rejections from the co-pending application.¹⁴⁹ The district court did not reach the issue of materiality, because it found insufficient evidence of intent to deceive the PTO. The Federal Circuit found that the facts alleged did not rise to the level of “culpability” required to establish intent under *Kingsdown*.¹⁵⁰

The third allegation was *Eisai*’s failure to disclose a piece of prior art in the prosecution of the patent-in-suit.¹⁵¹ The Federal Circuit was persuaded that the prior art patent offered “nothing new to the record” before the PTO.¹⁵² Furthermore, the record lacked clear and convincing evidence of intent to deceive.

The fourth allegation was that *Eisai* submitted misleading data in a declaration to overcome an obviousness rejection during the prosecution of the patent-in-suit.¹⁵³ The data were allegedly misleading because they did not include the compound that was the subject of the co-pending application.¹⁵⁴ The district court found that the declaration itself was highly material, but *Eisai* had no obligation to provide the additional data.¹⁵⁵ The Federal Circuit affirmed the district court’s finding of no inequitable conduct, and noted that the record again lacked evidence of deceptive intent.¹⁵⁶

137 *Id.* at 1376.

138 *Id.* at 1377.

139 *See id.* at 1376-79.

140 *See id.*

141 *See id.* 1378-79.

142 *Eisai Co. Ltd. v. Dr. Reddy’s Labs., Inc.*, 533 F.3d 1353 (Fed. Cir. July 21, 2008) (Rader, J.).

143 *See id.* at 1355.

144 *See id.* at 1360.

145 *See id.*

146 *See id.*

147 *See id.* at 1360-61.

148 *See id.*

149 *See id.*

150 *See id.*

151 *See id.* at 1361.

152 *See id.*

153 *See id.* at 1361-62.

154 *See id.*

155 *See id.*

156 *See id.*

The final allegation was disposed of by the district court on summary judgment.¹⁵⁷ The allegation was that Eisai concealed another pharmaceutical compound from the examiner. The district court found insufficient evidence of both materiality and intent. The Federal Circuit affirmed. The appeals court noted that the strongest evidence was that one Eisai “insider” made a “passing comment” that the similar of the claimed compound to another compound “bothers me.”¹⁵⁸ The Federal Circuit found this vague, subjective statement to be insufficient to establish a genuine issue regarding materiality or intent.¹⁵⁹

K. *RCT*¹⁶⁰

In *RCT*, the Federal Circuit reversed a finding of inequitable conduct after a bench trial because the district court failed to conduct a proper analysis and the Federal Circuit remanded for a proper consideration on the merits.¹⁶¹

The district court canceled a scheduled jury trial and held a bench trial limited to the issue of inequitable conduct.¹⁶² The trial court further limited the testimony from RCT to inventor testimony on candor and good faith. The trial court specifically barred RCT from presenting expert evidence regarding materiality. The trial court thereafter ruled that RCT’s patents were unenforceable for inequitable conduct.¹⁶³

The Federal Circuit reversed because the district court clearly erred by considering only one prong of the analysis, intent to deceive the PTO, and ignoring materiality.¹⁶⁴ The nondisclosed information consisted of data obtained after the filing of the patent applications. The Federal Circuit explained that this data was not material to the patentability of the claimed invention.¹⁶⁵ Furthermore, the Federal Circuit noted that the data was published, which is inconsistent with an intent to conceal data from the PTO.¹⁶⁶ Indeed, the Federal Circuit found that the intent analysis was clearly erroneous, since the district court relied on statements by the inventor that did not evidence that any of the submissions to the PTO were untrue.¹⁶⁷

L. *Star Scientific*¹⁶⁸

In *Star Scientific*, the Federal Circuit reversed a finding of inequitable conduct after a bench trial because it found the district court’s factual findings to be clearly erroneous. As to the first patent-in-suit, the finding of intent was clearly erroneous. For the second patent, the finding of materiality was held to be clearly erroneous.

The inequitable conduct involved an alleged conspiracy between the inventor and Star Scientific to prevent disclosure to the PTO of a letter from one of Star Scientific’s outside consultants (the “Burton letter”).¹⁶⁹ The technology-in-suit was for curing tobacco by a process that resulted in reduced levels of particular carcinogens.¹⁷⁰ The Burton letter discussed Dr. Burton’s new observation that reduced levels of the carcinogens had been achieved in Chinese tobacco products.¹⁷¹ The Burton letter thus showed that the prior art had achieved low levels of the carcinogens.

¹⁵⁷ See *id.* at 1362.

¹⁵⁸ See *id.*

¹⁵⁹ See *id.*

¹⁶⁰ *Research Corp. Techs., Inc. v. Microsoft Corp.*, 536 F.3d 1247 (Fed. Cir. Aug. 1, 2008) (Rader, J.).

¹⁶¹ See *id.* at 1250, 1254-55.

¹⁶² See *id.*

¹⁶³ See *id.*

¹⁶⁴ See *id.* at 1252.

¹⁶⁵ See *id.* at 1252-53.

¹⁶⁶ See *id.* at 1252.

¹⁶⁷ See *id.* at 1253-54.

¹⁶⁸ *Star Sci., Inc., v. R.J. Reynolds Tobacco Co.*, 537 F.3d 1357 (Fed. Cir. Aug. 25, 2008) (Michel, C.J.).

¹⁶⁹ See *id.* at 1361-62.

¹⁷⁰ See *id.* at 1361.

¹⁷¹ See *id.* at 1361-62.

Star Scientific switched prosecution firms during the prosecution of the first patent-in-suit.¹⁷² The key allegation was that when Star Scientific changed firms, Star Scientific prevented the attorneys at the old firm, Sughrue, from disclosing the Burton letter to the attorneys at the new firm, Banner.¹⁷³ The Burton letter had been analyzed by an attorney at the Sughrue firm.¹⁷⁴ The attorney was initially concerned but, after investigation and further analysis, decided the letter and its content were not material.

The Federal Circuit concluded that with respect to the first patent-in-suit, there was no evidence of intent to deceive the PTO.¹⁷⁵ The district court clearly erred in concluding that Star Scientific deliberately prevented the Banner lawyers from learning of the letter. There was no evidence that the letter was a reason for changing firms. The defendant, furthermore presented no evidence that the either the inventor or the decision makers at Star Scientific were aware of the Burton letter or the information in it before the Sughrue firm was replaced. In short, the Federal Circuit found a “major gap” in the defendant’s evidence regarding intent.¹⁷⁶ The Federal Circuit noted that, even if Star Scientific’s explanations were not credible, as the district court found, Star Scientific was not required to offer a good faith explanation because the defendant did not first meet its burden to prove a threshold level of intent to deceive by clear and convincing evidence.¹⁷⁷

With respect to the second patent-in-suit, the Federal Circuit held that the district court clearly erred in finding the Burton letter material.¹⁷⁸ To the contrary, the Burton letter was clearly cumulative to other information disclosed to the PTO, which included an interrogatory response from the litigation that stated the prior art had achieved low or insignificant levels of the carcinogens. The Federal Circuit made no determination whether the finding of deceptive intent as to the second patent was clearly erroneous.¹⁷⁹

M. *Praxair*¹⁸⁰

In *Praxair*, the Federal Circuit affirmed a finding of inequitable conduct as to one patent-in-suit and reversed a finding of inequitable conduct as to another patent-in-suit. The allegations of inequitable conduct were based on prior art that was allegedly withheld from the PTO.

As to the first patent-in-suit, the Federal Circuit affirmed the finding of inequitable conduct.¹⁸¹ The appeals court agreed that the prior art was material. On the intent prong, the district court inferred intent to deceive from the high materiality of the prior art in the context of statements made during the prosecution. The Federal Circuit sustained the district court’s finding. The Federal Circuit found that there was no question that the prosecuting attorney and one of the inventors knew of the prior art, and that the attorney was aware of its obvious materiality.¹⁸² The Federal Circuit also agreed that the applicants failed to present any good faith explanation for withholding the art.¹⁸³

As to the second patent-in-suit, the Federal Circuit reversed. The district court relied on the statements during prosecution referred to above to establish a high degree of materiality. That was error, the Federal Circuit determined, because those statements were made only in the prosecution of the first patent and could not be used to establish materiality as to the second patent.

Judge Lourie dissented as to the affirmance of inequitable conduct for the first patent.¹⁸⁴ Judge Lourie stated that Federal Circuit law requires more than materiality for a finding of intent to

172 See *id.* at 1363.

173 See *id.* at 1367.

174 See *id.* at 1362.

175 See *id.* at 1367-68.

176 See *id.* at 1368.

177 See *id.*

178 See *id.* at 1371.

179 See *id.* at 1370.

180 *Praxair, Inc. v. ATMI, Inc.*, 543 F.3d 1306 (Fed. Cir. Sept. 29, 2008) (Dyk, J.; Lourie, J., dissenting from the affirmance of inequitable conduct).

181 See *id.* at *9.

182 See *id.* at *8.

183 See *id.* at *8-9.

184 See *id.* *19 (Lourie, J., dissenting-in-part).

deceive.¹⁸⁵ Judge Lourie also stated that the district court erred in failing to conduct a balancing of materiality and intent before determining whether inequitable conduct had occurred.¹⁸⁶ In addition, Judge Lourie criticized the majority for failing to properly analyze whether the attorney and the inventor “knew, or should have known,” of the materiality of the withheld art.¹⁸⁷

IV. DISCUSSION AND QUESTIONS

A. Trends in the Cases

Star Scientific's strict application of legal standards for inequitable conduct is “book-ended” by *Praxair* and *Aventis*, which use a lower standard to find deceptive intent.

The Federal Circuit appears to be applying a strict legal standard for deceptive, if the cases of *Scanner Technologies*, *RCT*, *Eisai*, and *Star Scientific* are an accurate indication. These four recent cases suggest that the standard for proving the factual elements of materiality and intent is high and may be getting higher. Indeed, *Star Scientific* (August 2008) and *Scanner Technologies* (June 2008) suggest that the clear and convincing standard requires that the district court reject unfavorable inferences whenever there are competing favorable inferences that are equally reasonable. This latter standard seems to go further than simply strictly holding the accused infringer to his burden of proof.

Other cases apply lower standards for intent. Some cases explicitly apply a “knew or should have known” standard, which encompasses mistake or negligence. The latest example is *Praxair*, decided on September 29, which reaffirms that intent may be inferred from materiality in some circumstances.¹⁸⁸ *Aventis*, decided in May 2008, affirmed a finding of intent to deceive where the record was apparently ambiguous. In *Aventis*, Judge Rader argued in a strongly worded dissent that the noninventor scientist who was accused of wrongdoing had little incentive to risk his professional standing and that the scientist’s later actions in disclosing the problem to the PTO were inconsistent with an intent to deceive.

A showdown appears inevitable. Cases like *Praxair* and *Aventis* conflict with the cases imposing a strict requirement for proof of intent to deceive, including *Kingsdown*, which is en banc precedent. Will it be necessary for the Federal Circuit to undertake another en banc review to resolve this persistent uncertainty in the law?

B. Policy Issues

In *Star Scientific*, Chief Judge Michel described the fine line that the courts must walk to ensure that the severe penalty of unenforceability is applied appropriately.¹⁸⁹ His discussion and that of Judge Rader in his *Aventis* dissent appear to reflect a view that inequitable conduct should be limited only to the most egregious and extreme cases.¹⁹⁰ In a similar vein, Judge Lourie suggested in his *Praxair* dissent that the rule that intent may be inferred from materiality was never meant to apply except in a context with such egregious facts that the omission could not have been inadvertent.¹⁹¹ As Judge Rader explained:

In *Kingsdown*, this court clearly conveyed that the inequitable conduct was not a remedy for every mistake, blunder, or fault in the patent procurement process. Even mistakes that struck at the heart and integrity of the process—

¹⁸⁵ See *id.* at *20 (Lourie, J., dissenting-in-part).

¹⁸⁶ See *id.* (Lourie, J., dissenting-in-part).

¹⁸⁷ See *id.* (Lourie, J., dissenting-in-part).

¹⁸⁸ See *Praxair, Inc. v. ATMI, Inc.*, 543 F.3d 1306, 1313-14 (Fed. Cir. Sept. 29, 2008) (“An inference of intent to deceive is generally appropriate, however, when (1) highly material information is withheld; (2) the applicant knew of the information [and] ... knew or should have known of the materiality of the information; and (3) the applicant has not provided a credible explanation for the withholding.”) (citation and internal quotation marks omitted).

¹⁸⁹ *Star Sci.*, 537 F.3d at 1365-66 (citations omitted).

¹⁹⁰ See *id.* at 1365 (referencing *Monsanto Co. v. Bayer BioSci. B.V.*, 363 F.3d 1235, 1239 (Fed. Cir. 2004)); *Aventis*, 525 F.3d at 1349.

¹⁹¹ *Praxair*, 543 F.3d at 1329 (Lourie, J., dissenting-in-part) (referencing *Bruno Independent Living Aids, Inc. v. Acorn Mobility Servs., Ltd.*, 394 F.3d 1348 (Fed. Cir. 2005)).

like repeatedly copying and acquiring rights to a rejected claim—did not amount to inequitable conduct. Instead this court required “culpable” conduct supported by clear and convincing evidence of intent to deceive the USPTO.¹⁹²

Judge Rader concluded: “*Kingsdown* properly made inequitable conduct a rare occurrence.”¹⁹³

But is the standard in danger of being set too high and failing to act as a brake on the actions of applicants who prosecute patents under the ex parte examination system? The applicant’s incentives in ex parte prosecution run somewhat counter to the interests of the patent system and the public. If the Federal Circuit makes known that only the most extreme and rare cases of inequitable conduct will trigger the remedy of unenforceability, it would not be surprising if some applicants will see an opportunity and take advantage. What will be the effect of making it more difficult to prove inequitable conduct? Who will benefit the most?

C. Inequitable Conduct Issues in the Reexamination Content

We conclude by raising a few questions about reexamination and inequitable conduct:

- If the PTO finds a substantial new question of patentability based on a prior art reference that was not before the PTO during the original prosecution, may an inequitable conduct charge be brought on the grounds that the applicant, at a minimum, should have known of the reference?
- If a reexamined patent is a member of a family of patents, can reexamination of the one patent “cure” inequitable conduct problems for the whole family?
- Does the existence of a protective order in litigation trump the duty to disclose material information to the PTO?

V. EPILOGUE

As this article is being prepared for publication, seven months later, the proper standard for inferring deceptive intent remains unsettled. Rehearing was not sought in the *Praxair* case. En banc rehearing and certiorari review were denied in *Star Scientific*¹⁹⁴ and certiorari was denied in *Aventis*.¹⁹⁵

In March 2009, the Federal Circuit issued an opinion in *Larson Manufacturing Co. v. Aluminart Products Ltd.*, which again underscored the inconsistency in the case law.¹⁹⁶ The panel reversed a finding of inequitable conduct and remanded for determination of whether deceptive intent was present in the withholding of two office actions in a copending prosecution from a panel of PTO examiners who were reexamining the patent-in-suit. The Federal Circuit provided specific guidance to the district court on remand. Among other things, the panel stated that “just as merely withholding a reference cannot support an inference of deceptive intent, so too an accused infringer cannot carry its threshold burden simply by pointing to the absence of a credible good faith explanation.”¹⁹⁷ Moreover, the court must weigh any evidence of good faith against the evidence favoring a finding of deceptive intent.¹⁹⁸

Judge Linn filed a concurring opinion in *Larson* urging the Federal Circuit to undertake en banc review to clarify the test for inferring deceptive intent. As Judge Linn noted, the sole issue at trial

¹⁹² *Aventis*, 525 F.3d at 1350.

¹⁹³ *Id.*

¹⁹⁴ *Star Sci., Inc. v. R.J. Reynolds Tobacco Co.*, 537 F.3d 1357 (Fed. Cir. Aug. 25, 2008), *reh’g & reh’g en banc den.*, (Fed. Cir. Oct. 22, 2008), *cert. den.*, 129 S. Ct. 1595 (Mar. 9, 2009).

¹⁹⁵ *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, 525 F.3d 1334, 1350 (Fed. Cir. May 14, 2008), *reh’g & reh’g en banc den.*, (Fed. Cir. Sept. 25, 2008), *cert. den.*, 129 S. Ct. 2053 (Apr. 27, 2009).

¹⁹⁶ 559 F.3d 1317 (Fed. Cir. Mar. 18, 2009).

¹⁹⁷ *Id.* at 1340-41 (citations omitted).

¹⁹⁸ *See id.* at 1341.

was the inequitable conduct and, after this remand, the case would continue to focus on the inequitable conduct—again, the tail wagging the dog.¹⁹⁹ He further noted that the current case law permits an inference of deceptive intent whenever “(1) highly material information is withheld; (2) the applicant knew of the information [and] . . . knew or should have known of the materiality of the information; and (3) the applicant has not provided a credible explanation for the withholding.”²⁰⁰ This, Judge Linn argued, allows a finding of deceptive intent based on evidence of simple negligence, which is inconsistent with Supreme Court precedent and with the intent of the Federal Circuit to do away with the “plague” of alleging inequitable conduct in almost every patent case.²⁰¹ In addition, the obligation to produce a “credible explanation” improperly shifts the burden to the patentee to prove that the patentee did *not* intend to deceive the PTO.²⁰² Finally, the test conflicts with the directive in *Star Scientific* that deceptive intent must be the “single most reasonable inference.”²⁰³ Despite Judge Linn’s concurrence, the Federal Circuit denied a petition for rehearing in *Larson* on April 13, 2009. Perhaps the persistent uncertainty in the legal standard will have the salutary effect of deterring withholding of material art during patent prosecution that might otherwise occur under the very high standard of *Star Scientific*.

199 *See id.* at 1343 (Linn, J., concurring).

200 *Id.* (Linn, J., concurring) (internal quotation marks omitted).

201 *See id.* at 1344 (Linn, J., concurring).

202 *See id.* (Linn, J., concurring).

203 *See id.* (Linn, J., concurring).

CONDUCTING E-DISCOVERY AFTER THE AMENDMENTS: THE SECOND WAVE

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I. TRENDS

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IV. CONCLUSION

This paper focuses on the remarkable “second” wave of decisions rendered in 2008 - 2009 regarding the discovery of electronically stored information (“ESI”) in the Federal Courts.

¹ Thomas Y. Allman is one of the Editors of *The Sedona Principles – Second Edition* (2007). An earlier version of this paper was presented at the Sedona Conference Mid-Year Meeting, Denver, Colorado (May 14-15, 2009).

I. TRENDS

At least three major themes dominate this second generation of post-2006 Amendment decisions.² First, the scope of discovery clearly extends to ephemeral information. Second, cooperation among parties in discovery has emerged as a decisive mandate and, third, counsel, both inside and retained, must accept responsibility, along with and apart from their clients, for discovery compliance.

We briefly discuss each of these trends before turning to the recent decisions regarding discovery of ESI.

A. Expanded Scope

Rule 34(a), as amended by the 2006 Amendments to the Federal Rules, clarifies that electronically stored information is discoverable when “stored in any medium” from which it can be obtained, “translated, if necessary” into a “reasonably usable form.”

Thus, even transitory or ephemeral manifestations of electronic information are discoverable. In *Columbia Pictures v. Bunnell*,³ a party was required to “begin preserving and subsequently produce a particular subset of the data in RAM under [its] control.”⁴ The District Court emphasized the relevance of the information, the lack of other available means to obtain it – and the ease with which it could be logged and retained.

Thus, relevant information in operating systems, dynamic databases, websites and voicemail (“digital audio files”),⁵ for example, can be discoverable whether found on individual or networked hard drives or on personal devices such as cell phones and PDAs.⁶

B. Cooperation

The 2006 Amendments mandate an earlier and meaningful discussion among opposing counsel on key e-discovery issues. As noted in *SEC v. Collins & Aikman*,⁷ there is now a real “mandate for counsel to act cooperatively. Rule 37(e) requires “good faith” dealings among counsel⁸ and there is a “perceptible trend” for “counsel [to] genuinely attempt to resolve discovery disputes.”⁹

The Sedona Conference[®] has proposed, through its Cooperation Proclamation initiative, that all parties focus on increased cooperation in discovery with advocacy reserved for articulating and pressing the merits of a litigating position.¹⁰

To facilitate this process of cooperation, Rule 26(f) provides that parties must meet and confer “as soon as practicable” to develop a discovery plan designed to encourage reasonable and balanced approaches to discovery.

A key topic identified for discussion in Rule 26(f) is the steps - if any - a party intends to take to preserve potentially relevant information for purposes of discovery.¹¹ This is especially important as to information stored in inaccessible sources, since, absent agreement, it is something of a “catch-22” to predict, in advance, whether “good cause” under Rule 26(b)(2)(B) can later be shown for production.

2 For useful analysis of the initial decisions rendered immediately after the 2006 Amendments, see Douglas L. Rogers, *A Search for Balance in the Discovery of ESI Since December 1, 2006*, 14 Rich. J. L. & Tech. 8 (2008) and Emily Burns, et al, *E-Discovery: One Year of the Amended Rules of Civil Procedure*, 64 N.Y.U. Law Rev. 201 (2008).

3 245 F.R.D. 443 (C.D. Cal. 2007), denying motion to reverse Magistrate Order, 2007 WL 2080419 (C.D. Cal. 2007).

4 245 F.R.D. 443 at 448.

5 Alan F. Blakley, *Digital Audio Files in Litigation*, 2 J. Legal Tech. Risk Mgmt. 1 (2007).

6 See, e.g., *McClain v. Norfolk Southern*, 2009 WL 701001 (N.D. Ohio March 16, 2009)(cell phone photographs); *Arteria Property v. Universal Funding*, 2008 WL 4513696 (D. N.J. 2008)(websites); *Flagg v. City of Detroit*, 252 F.R.D. 346 (E.D. Mich. 2008)(text messaging devices).

7 2009 WL 94311 (S.D. N.Y. Jan. 13, 2009).

8 See, e.g., *Arista Records v. Usenet.com, Inc.*, 2009 WL 185992, at *16, n.31 (S.D. N.Y. Jan. 26, 2009)(parties should “negotiate in good faith [about] preservation difficulties).

9 *Neuman v. Borders*, 2009 WL 931545, at *3, n. 3 (D.D.C. April 6, 2009).

10 The Sedona Conference[®] Cooperation Proclamation (2008)(“The costs associated with adversarial conduct in pre-trial discovery have become a serious burden to the American judicial system.”), downloadable at <http://www.thosedonacommunity.org>.

11 Thomas Y. Allman, *The Impact of the Proposed Federal E-Discovery Rules*, 12 Rich. J. L. & Tech. 13, at Paragraph 14 (2006)(“[T]he paradigm of a producing party acting independently, and somewhat cavalierly, in determining its preservation obligations is modified by the [Amendments]”).

Another key issue for discussion is whether “metadata” will be sought in a case. As noted in *Kentucky Speedway, LLC v. NASCAR*,¹² “whether metadata is relevant or should be produced is [an issue] which ordinarily should be addressed by the parties in a Rule 26(f) conference.”¹³

Similarly, discussion should be initiated as early as feasible about methods to limit or cull the information to be produced in discovery. Courts expect parties to reach practical agreement on search terms, date ranges, key players and the like.¹⁴

Finally, it is advisable to discuss the terms of any confidentiality or non-waiver agreements that may be developed to handle the production – inadvertent or otherwise – of privileged or work-product materials or confidential or trade secret materials. Rule 26(b)(5)(B) and Evid. Rule 502 now provide ample authority, with court approval, to design court orders to manage both procedural and substantive aspects of the issue.

A failure to meet with opposing counsel to resolve discovery problems will have consequences. In *May v. Fed Ex Freight*,¹⁵ a court refused to rule on a motion to compel e-mail filed prematurely where the plaintiff did not meet and confer with defendant and its IT representatives.

C. Counsel Responsibility

Another trend is the increased likelihood that counsel may be held individually or jointly responsible with their client for failures to preserve and produce discoverable ESI.¹⁶ ABA Model Rule 3.4 obligates counsel to make a “reasonably diligent effort to comply with a legally proper discovery request.” In *Zubulake v. UBS Warburg (“Zubulake V”)*,¹⁷ the court suggested that both inside and outside counsel bear responsibility for client compliance with discovery obligations.

In the case of *In re Rosenthal*,¹⁸ counsel was sanctioned for having omitted to act or to advise his client about duties to preserve information.¹⁹ In *Phoenix Four, Inc. v. Strategic Resources Corp.*,²⁰ counsel was sanctioned because of her duty to locate and preserve relevant electronic information.

Rule 26(g) is increasingly cited for the obligation of counsel to conduct a “reasonable inquiry” before signing discovery filings. The Rule mandates an award of sanctions, where violations exist, against counsel, client or both of them.

In *Adele S.R.L. v. Filene’s Basement, Inc.*,²¹ *Cache La Poudre Feeds, LLC v. Land O’Lakes, Inc.*,²² and *Board of Regents of University of Nebraska v. BASF Corp.*,²³ clients were sanctioned for failures of counsel and their client.

In *R & R Sails Inc. v. Insurance Co. of Pennsylvania*,²⁴ however, both counsel and client were sanctioned for the Rule 26(g) discovery failures.

Discovery sanctions against counsel have also been assessed under Rule 37 as an incident to counsel “advising” clients regarding discovery matters or under the inherent power of courts to manage their affairs. In *Ajaxo v. Bank of America*,²⁵ a court sanctioned counsel under Rule 37 for causing “needless discovery motions.”

12 2006 WL 5097354 (E.D. Ky. 2006).

13 Id. at *8 (failure to notify of demand for metadata until seven months after production of electronic and hard copy of documents).

14 *Siemens v. Jutai*, 2009 WL 800143 (S.D. Fla. March 25, 2009)(restricting search and agreeing on list of search terms).

15 2009 WL 1605211 (M.D. La. June 8, 2009)(ordering meeting to “discuss the burden and expense” before assertion of a motion to compel).

16 See also *Bray & Gillespie Management LLC v. Lexington Insurance*, 2009 WL 546429, at *21 (M.D. Fla. March 4, 2009)(clients have a duty to supervise the discovery conduct of their lawyers).

17 *Zubulake v. UBS Warburg*, 229 F.R.D. 422, 431(S.D.N.Y. July 20, 2004)(“the central question” is “whether UBS and its counsel took all necessary steps to guarantee that relevant data was both preserved and produced.”).

18 2008 WL 983702 (S.D. N.Y. March 28, 2008).

19 Id. at *10 - 11 (counsel failed to advise client to preserve documents and warn against deleting email).

20 2006 WL 1409413 (S.D.N.Y. May 23, 2006).

21 2009 WL 855955 (S.D. N.Y. March 24, 2009).

22 244 F.R.D. 614 (D. Colo. 2007).

23 2007 WL 3342423 (D. Neb. 2007).

24 251 F.R.D. 520 (S.D. Cal. 2008).

25 2008 WL 5101451, at *2 (E.D. Cal. 2008)(ordering reimbursement of fees paid for “needless discovery motion” but not sanctioning client “at this time.”).

A mild presumption exists that clients are in the best position to control their counsel and, absent egregious counsel conduct, should bear the discovery sanctions.²⁶ If needed, “client and counsel can apportion the sanctions amongst themselves, consistent with their respective degrees of culpability.”²⁷

In *Qualcomm v. Broadcom*²⁸ in addition to sanctioning the client, the court referred counsel to the California Bar for investigation of possible ethical violations and also ordered inside and outside counsel to participate in a “Case Review and Enforcement of Discovery Obligations (“CREDO”)” Program to “identify the failures in the case management and discovery protocol.”²⁹

The debate as to how counsel can best adapt to this new emphasis on counsel responsibility for client compliance has been spirited.³⁰

II. PRESERVATION

The duty to preserve potentially discoverable information in the form of hard copy or electronically stored information is not spelled out in the Federal Rules and is largely governed by the common law.³¹

The duty arises when a party has notice that evidence is or may become relevant to current or future litigation,³² a determination which can be highly fact-dependent.³³ The duty to preserve transitory or ephemeral data not routinely retained as a business matter may require a specific demand for preservation.³⁴

In *Columbia Pictures v. Bunnell*, *supra*,³⁵ sanctions for failure to preserve temporary information in RAM were refused because of the failure of the requesting party to make it clear that information would be sought in discovery.³⁶

There is no requirement that preservation be accomplished in any particular format, provided that the relevant information can be retrieved and produced at the appropriate time.³⁷

A. Litigation Holds

Once a preservation obligation is acknowledged, a potential producing party must undertake some form of affirmative action, a process which has come to be called a “litigation hold.”³⁸

A “litigation hold” should inform persons with the power to affect the continued existence of electronic information of the need to retain it. A typical approach focuses on key individuals who are likely to have access to information relevant to the claims or defenses.

26 See Thomas Y. Allman, *Achieving an Appropriate Balance: The Use of Counsel Sanctions in Connection with the Resolution of E-Discovery Misconduct*, 15 Rich. J.L. & Tech. 9, at Paragraphs 34-40 (2009).

27 *Alden v. Mid-Mesabi Associates*, 2008 WL 2828892, at *18 (D. Minn. July 21, 2008) (noting that it is “far too facile to presume” that counsel should be blamed for failure to allow discovery).

28 2008 WL 66932 (S.D. Cal. 2008), *vacated and remanded*, 2008 WL 638108 (S.D. Cal. 2008). See also *Qualcomm v. Broadcom*, 548 F.3d 1005 (Fed. Cir. C.A. December 1, 2008) (affirming in part underlying remedy ordered by District Court).

29 *Id.* at *18-20 (to establish “baseline: for other cases and to “establish a turning point: in “decline in and deterioration of civility, professionalism and ethical conduct in the litigation arena.”).

30 See Kristine L. Roberts, *Qualcomm Fined for “Monumental” E-Discovery Violations—Possible Sanctions Against Counsel Remain Pending*, LITIG. NEWS ONLINE (2008).

31 See *Silvestri v. GM*, 271 F.3d 583 (4th Cir. 2001).

32 *Zubulake v. UBS Warburg LLC (“Zubulake IV”)*, 220 F.R.D. 212, 216 (S.D.N.Y. 2003).

33 Compare *Miron v. Rambus*, 2009 WL 54887 (D.Del. Jan. 9, 2009) with *Hynix v. Rambus*, 2009 (N.D. Cal. Feb. 3, 2009) (conflicting conclusions as “reasonable foreseeability” of litigation based on same internal memo).

34 Kenneth J. Withers, “Ephemeral Data” and the Duty to Preserve Discoverable Electronically Stored Information, 37 U. Balt. L. Rev. 349, 373-377 (Spring 2008).

35 2007 WL 2080419 (C.D. Cal. 2007), *affirmed sub nom.* 245 F.R.D. 443 (C.D. Cal. 2007).

36 See also *Arista Records v. Usenet.com, Inc.*, 2009 WL 185992, at *15 (S.D. N.Y. Jan. 26, 2009); *Phillips v. Netblue*, 2007 WL 174459 (N.D. Cal. 2007) (no duty to retain hyperlinks).

37 *Quinby v. WestLG AG (“Quinby II”)*, 245 F.R.D. 94 (S.D. N.Y. Sept. 5, 2006) (should not punish routine business practices that do not destroy documents or alter them in any material sense”); *but see* DCBAR Op. 341 (Sept. 2007) at B(1) (removal of metadata in litigation context may be prohibited depending upon the type of metadata involved).

38 *Kinnally v. Rogers Corporation*, 2008 WL 4850116 (D. Ariz. 2008).

Courts continue to rely upon *Zubulake v. UBS Warburg* (“*Zubulake IV*”)³⁹ for the proposition that “as a general rule, inaccessible backup tapes need not be preserved unless they are known to contain documents “of ‘key players’ to the existing or threatened litigation.” For some courts, this remains a viable articulation⁴⁰ to determine if the duty had been violated.⁴¹

However, “[p]reserving all backup tapes is rarely necessary or cost effective.”⁴² There must be a reason to believe the information on the source would be relevant to the issues.⁴³

Meeting preservation obligations should be seen as part of a corporate commitment to an effective compliance program. Increasingly, entities that can afford to do so are dedicating IT personnel and counsel to the task of coordinating and managing the process.

B. Limitations

The “duty to preserve” is not absolute. The outer limits are governed by relevance as mitigated by the “proportionality” principle.⁴⁴ When the burdens and expenses involved in a preservation effort are “disproportionate to the potential value” of the information source, the duty does not arise.⁴⁵

Courts are also reluctant to speculate on relevance.⁴⁶ Thus, in *Best Buy Stores, L.P. v. Developers Diversified Realty*,⁴⁷ a District Judge held that there was no duty to maintain a database in a particularly accessible form “absent specific discovery requests or additional facts suggesting that the database was of particular relevance to this litigation.”⁴⁸

Most courts are also reluctant to impose burdensome storage requirements not routinely provided by the party. In *Malletier v. Dooney & Bourke*,⁴⁹ for example, a court held there was no duty to install a system to monitor and record chat room conversations.

Moreover, when a duty to preserve ephemeral information is not obvious, a requesting party may not “sandbag” the opposing party by remaining silent and later filing a motion for sanctions.

C. Preservation Orders

Pre-discovery preservation orders do not issue in the absence of evidence that a producing party does not intend to comply with its duty to preserve.⁵⁰ In *Ellington Credit Fund v. Select Portfolio Services*,⁵¹ the court refused to issue a blanket preservation order where the court was satisfied that the producing party was aware of its obligations.

In *Texas v. City of Frisco*,⁵² the court refused to entertain an action seeking declaration of preservation responsibilities based solely on receipt of a pre-suit preservation demand letter.

Moreover, courts no long honor requests for open-ended *ex parte* or blanket preservation orders absent exceptional circumstances.⁵³

39 220 F.R.D. 212, 217-218 (S.D. N.Y. 2003)(there is no general duty to preserve backup media used for disaster recovery, subject to an exception for those tapes known to contain discoverable information of key players).

40 *Forest v. Caraco*, 2009 WL 998402 (E.D. Mich. April 14, 2009)(applying the “Zubulake exception”).

41 The Committee Note to Rule 37(e) notes that “good faith” may require suspension of automatic recycling when a litigation hold is established.

42 See Mary Mack, Dennis Kiker and Tom Mighell, *Effective Management of Litigation Holds and E-Discovery*, 27 NO.4 ACC DOCKET 36, at 44 (May 2009).

43 See *Toussie v. Count of Suffolk*, 2007 WL 465160 (E.D. N.Y. Dec. 21, 2007)(no duty to preserve without showing of prejudice).

44 Hon. Paul Grimm, Michael Berman, Conor Crowley and Leslie Wharton, *Proportionality in the Post-Hoc Analysis of Pre-Litigation Preservation Decisions*, 37 U. Balt. L. Rev. 381, 404 (Spring 2008)(“limitations should be engrained by analogy”).

45 The Sedona Conference “*Commentary on Preservation, Management, and Identification of Sources of Information that are not Reasonably Accessible*” (July, 2008), at 14 (“Step Five Analysis – The Proportionality Principle”).

46 *Sampson v. City of Cambridge*, 2008 WL 2717757 at *10 (D. Md. 2008)(it is “completely speculative” to assume that email lost constituted relevant evidence).

47 2007 WL 333987 (D. Minn. 2007).

48 *Id.* at *3. The court also held that there was no “good cause” to order restoration of the database since it was not shown that the materials sought were “uniquely available” from the database.

49 2006 WL 3851151 (S.D. N.Y. 2006).

50 *Gregg v. Local 305 IBEW*, 2008 WL 5171085 (N.D. Ind. 2008).

51 2009 WL 274483 (S.D. N.Y. Feb. 3, 2009).

52 2008 WL 828055 (E.D. Tex. 2008).

53 See Committee Note to Rule 26(f) (“[a] preservation order issued over objection should be narrowly tailored [and] [*ex parte*] preservation orders should issue only in exceptional circumstances.”).

D. Spoliation Sanctions

The failure to preserve ESI can lead to allegations of “spoliation” of evidence. As one Circuit Court of Appeals has affirmed,⁵⁴ however, “sanctions should be considered only if the court finds a clear duty to preserve, a culpable failure to preserve and produce relevant ESI, and a reasonable probability of prejudice to the adverse party.”

Sanctions can involve harsh remedies such as dismissals or default judgments⁵⁵ or lesser sanctions such as adverse inference instructions or monetary sanctions, depending on the circumstances.⁵⁶ In *Asher Associates v. Baker Hughes*,⁵⁷ the court imposed a “non-dispositive” sanction for failure to preserve the components of a drilling tool and in *Innis Arden Golf Club v. Pitney Bowles*⁵⁸ the court did the same in regard to contaminated soil samples.

Prior to the 2006 Amendments, concern was expressed about the fairness of sanctioning the inadvertent or negligent loss of electronically stored information caused by routine business practices.⁵⁹

In partial response, the Advisory Committee added Rule 37(e)⁶⁰ which limits, absent “exceptional circumstances,” the imposition of rule-based sanctions for losses due to the “routine, good faith” operation of electronic information systems. The clear intent was to separate out the unintentional, even careless or negligent, conduct from intentional misuse of the system features.⁶¹

In *Doe v. Norwalk Community College*,⁶² the rule was not applied because there was no “consistent, ‘routine’ system in place.”

Some courts seem to assume that once a duty to preserve attaches something akin to strict liability follows for any losses.⁶³ This is particularly true in cases involving automatic deletion of information for business reasons. Despite the widespread adoption of that approach, as documented by a Sedona Conference⁶⁴ Commentary,⁶⁴ courts are often suspicious of such policies.⁶⁵

Where spoliation *is* deliberate courts do not - and should not - hesitate to issue sanctions⁶⁶ However, cases like *Phillip M. Adams & Associates v. Dell*⁶⁷ are surely wrong in criticizing automatic deletion because of the remote possibility that third parties - unidentified but vaguely anticipated - might someday seek them in discovery.

In contrast, in *Escobar v. City of Houston*,⁶⁸ the court correctly applied Rule 37(e) in refusing to sanction the failure to interrupt the routine practice of overwriting audio tapes absent any showing that the producing party acted in bad faith. A similar result was reached in *Phillips v. Potter*,⁶⁹ where there was no proof of bad faith or malicious intent in employing automatic deletion of email.⁷⁰

54 *John B. v. M.D. Goetz*, 532 F. 3d 448, 459 (6th Cir. 2008)(referencing Sedona Principle 14 [2nd Ed. 2007]).

55 *Atlantic Recording v. Howell*, 2008 WL 4080008 (D. Ariz. 2008)(“brazen destruction” of evidence).

56 *See Kauneis v. Sherrer*, 529 F. Supp. 2d 503 (D. N.J. 2008)(citing degree of fault and degree of prejudice as key factors).

57 2009 WL 1328483 (D. Colo. May 12, 2009).

58 2009 WL 1416169 (D. Conn. May 21, 2009)(landowner disposed of samples of contaminated property after duty attached).

59 *See Martin Redish, Electronic Discovery and the Discovery Matrix*, 51 Duke L.J. 561, 625(2001) (“if done routinely in the ordinary course of business, [destruction of ESI] does not automatically give rise to an inference of knowledge of specific documents’ destruction, much less intent to destroy those documents for litigation-related reasons.”).

60 Enacted as Rule 37(f) but renumbered as Rule 37(e) in the 2007 “style” amendments.

61 Thomas Y. Allman, *Inadvertent Spoliation of ESI After the 2006 Amendments: The Impact of Rule 37(e)*, 2009 Fed. Cts. L. Rev. 2 (2009)(quoting Advisory Committee member to the effect that “good faith” assumes that the party “did not deliberately” permit a system to destroy information).

62 248 F.R.D. 372 (D. Conn. July 16, 2007).

63 *See Burns et al, E-Discovery, supra*, 64 NYU Law Rev. 201 at 217(questioning authority which implies strict liability).

64 *See The Sedona Conference Commentary on Email Management Guidelines for the Selection of Retention Policy* (August 2007), 8 The Sedona Conf. J. 239 (2007)(describing variety of acceptable auto-deletion policies).

65 *See, e.g., Connor v. Sun Trust Bank*, 546 F. Supp. 1360 (N.D. Ga. 2008)(concluding that loss of email not archived before automatic deletion must have been intentional since “doubtful” that the witness was not aware of need to preserve).

66 *Kvitka v. Puffin Company*, 2009 WL 385582 (M.D. Pa. Feb. 13, 2009)(intentional deletion of email from laptop).

67 2009 WL 910801, at *14 (D. Utah March 30, 2009)(criticizing email practices which allow individual employees to determine which emails to retain).

68 2007 WL 2900581 at *18 (S.D. Tex. 2007).

69 2009 WL 1362049 at *5 (W.D. Pa. May 14, 2009).

70 *Accord, Petcou v. C.H. Robinson Worldwide*, 2008 WL 542684 (N.D. Ga. 2008).

Other courts ignore Rule 37(e) by relying upon their inherent, not rule-based, sanctioning power.⁷¹ However, this approach is disingenuous, since there is no principled reason to distinguish among the reasons for sanctions based on the source of the sanctioning power.⁷²

Not all courts have adopted the unreasonably strict standards alluded to above. As one court put it, “[m]ere negligence in losing or destroying records [after a duty applies] is not enough [to justify sanctions] because it does not support an inference of consciousness of a weak case.”⁷³ In *Adorno v. Port Authority*,⁷⁴ the court denied a motion for sanctions because “I am simply not persuaded on this record that a reasonable jury could find that the evidence was harmful to the [party’s] defense of the case.”

III. PRODUCTION

Courts increasingly exercise significant oversight of the mechanics of e-discovery compliance.⁷⁵

A. Proportionality

All discovery is limited by the “proportionality” principle, currently found in Rule 26(b)(2)(C). This principle provides that a party need not provide discovery when the potential benefits are outweighed by the burdens or costs involved.

Thus, in *Dilley v. Metropolitan Life*,⁷⁶ a court refused to require a producing party to access a database in order to respond to an interrogatory where “the significance of the discovery to the issues in the present case is substantially outweighed by the burden.”

In *Mancia v. Mayflower Textile Servs. Co.*,⁷⁷ the court criticized “kneejerk discovery requests served without consideration of cost or burden to the responding party” and “boilerplate objections” which do not disclose the burdens involved.⁷⁸ The court ordered that the parties meet and cooperate with a goal of “attempt[ing] to quantify a workable ‘discovery budget’ that is proportional to what is at issue in the case.”⁷⁹

In *Oxford House v. City of Topeka*,⁸⁰ a court denied access to deleted email because “the likelihood of retrieving these electronic communications is low and the cost high.” A similar result was reached in *Palgut v. City of Colorado Springs*,⁸¹ where the costs of restoration of backup tapes outweighed the “possible yield of relevant and probative information.”

A reviewing court is empowered to deny discovery sought, condition it on payment of some or all of the costs involved⁸² or order sampling to provide information on the necessity for further discovery. In *Kay Beer Distributing v. Energy Brands*,⁸³ the court refused to compel production of ESI collected as part of preliminary search where the costs of a further review for privilege, confidential and relevant information were deemed to be excessive.⁸⁴

71 Rule 37(e) speaks of sanctions “under these rules.” See *Technical Sales v. Ohio Star Forge*, 2009 WL 728520 (E.D. Mich. March 19, 2009)(Rule 37(e) does not limit spoliation sanctions based on inherent power of courts).

72 See Moore’s Federal Practice §37A.57 (2008)(“a court [should not] sanction a party under its inherent authority unless the sanction would be appropriate under [Rule 37(e)].”).

73 *Salvatore v. Pingel*, 2009 WL 943713, at *10 (D. Colorado, April 6, 2009)(refusing to impose sanction for “negligent destruction of Maintenance Log”).

74 2009 WL 8574965 (S.D. N.Y. March 31, 2009).

75 See Frank Vecell, Thomas Fasone, III, and Cathy Clark, *Litigation Management: And You May Find Yourself In a Large Document Review*, 27 No.4 ACC Docket 82, at *83 (May 2009).

76 2009 WL 756967 (N.D. Cal. March 19, 2009); see also *Nelson v. Farm, Inc.*, 2009 WL 939123 (D. Kan. April 6, 2009)(cautioning that it is not enough to argue requires use of “unreasonable” expenditure of resources).

77 253 F.R.D. (D. Md. 2008).

78 *Id.* at 359.

79 *Id.* at 364.

80 2007 WL 1246200 (D. Kan. 2007).

81 2007 WL 4277564 (D. Colo. 2007).

82 *CBT Flint Partners v. Return Path, Inc.*, 2008 WL 4441920 (N.D. Ga. Aug. 7, 2008)(“relevance and importance are [not] proportional” to the costs involved).

83 2009 WL 1649592 (E.D. Wis. June 10, 2009).

84 *Id.* at *5; compare *Spieker v. Quest Cherokee, LLC* 2008 WL 4758604 (D. Kan. 2008)(ducking impact of disproportionate review costs by ordering parties to confer about impact of Rule 502 on reducing privilege costs).

B. Two-Tiered Approach

The 2006 Amendments placed a presumptive limit on production of ESI by enacting Rule 26(b)(2)(B), also known as the “two-tiered” approach, which provides that discovery from inaccessible sources can only be ordered upon “good cause,” “subject to the limitations” of Rule 26(b)(2)(C). A party need not initially resort to such sources if they are “identified” to opposing counsel.⁸⁵

Accessibility often turns on the nature of storage media involved.⁸⁶ Information stored on local hard drives, networked servers, distributed devices or offline archival sources are immediately accessible without restoration or reconstruction.⁸⁷ The Sedona Conference[®] has suggested additional “data complexity factors” for use in the assessment, however, since even active data can be deemed to be burdensome to utilize and review.⁸⁸

It can be argued that the “two-tiered” approach is cumbersome and that its addition was unnecessary. Although “good cause” is dutifully (and mechanically) referenced in many of the cases, the courts are, in fact, primarily focused on proportionality.⁸⁹

On balance, however, the “accessibility” distinction provides a useful vocabulary for discussion of unnecessary burdens and costs and has apparently been successful in reducing disputes over inaccessible sources.⁹⁰

C. Form or Forms of Production

The amended Federal Rules are silent on the form or forms in which ESI should be produced. The Advisory Committee left the matter for individual case adjudication while making it clear that it was taking no position on the need for metadata in a particular case.⁹¹

Rule 34(b) thus provides, in the absence of agreement of the parties or a court order, that electronic information should be produced as “ordinarily maintained” (often referred to as “native” format) or in a “reasonably usable” format, which carries with it an obligation to assist the requesting party and not to degrade any existing capability to perform electronic searches.⁹²

As noted in *Aquilar v. ICE*,⁹³ the relevance of and need for metadata (substantive, system or embedded metadata) may vary as between memoranda, email, spreadsheets and hierarchical databases, with different results for each. It is often sufficient to produce memoranda, emails and electronic records in PDF or TIFF format accompanied by a load file containing searchable text and selected metadata.⁹⁴

Spreadsheets and databases may require a different approach.⁹⁵ In the case of *In re ClassicStar Mare Lease Litigation*,⁹⁶ the court ordered production of information from a complex financial database in native format, not TIFF with load files, because of difficulties in utilizing the latter.

85 David K. Isom, *The Burden of Discovering Inaccessible Electronically Stored Information: Rules 26(b)(2)(B) & 45(d)(1)(D)*, 2009 Fed. Cts. L. Rev. 1, 7-10 (2009)(describing the role of “identification” of inaccessible sources of ESI).

86 *Zubulake v. UBS Warburg (“Zubulake I”)*, 217 F.R.D. 309, 318-320 (S.D. N.Y. 2003)(a distinction that corresponds closely to the expense of production).

87 *The Sedona Conference Glossary: E-Discovery & Digital Information Management 2* (2d ed. Dec. 2007).

88 The Sedona Conference[®] *Commentary on Preservation, Management and Identification of Sources of Information that Are Not Reasonably Accessible*, at 11 (with chart)(July 2008).

89 See *Panel Discussion, Managing Electronic Discovery: Views from the Judges*, 76 Fordham L. Rev. 1, at *23 (2007)(Courts “pass by” the “almost mechanical burden-shifting procedure” when the value is so outweighed by the burden that the court will not require production).

90 See Thomas Y. Allman, *The Two-Tiered Approach to E-discovery: Has Rule 26(b)(2)(B) Fulfilled Its Promise?*, 14 Rich. J. L. & Tech. 7, ¶67 (2008)(“Parties are increasingly tempering their demands and reaching practical and effective accommodations under circumstances which did not exist before.”).

91 Comment, 93 Cornell L. Rev. 221, 224 (2007)(rule makers were silent because electronic discovery was such a new and changing area of law that the Committee was not confident in setting down a firm and inflexible rule).

92 Committee Note, Rule 34, subdivision (b) (2006).

93 255 F.R.D. 350 (S.D. N.Y. 2008)(containing a comprehensive analysis of the discoverability of metadata from the perspective of existing case law, the Rules and the *Sedona Principles*).

94 *Id.*, at 356 (quoting from *Sedona Principle* 12, Cmt. 12b, Illus. I [imaged production with load files satisfies the goals of Principle 12 since in a usable form, i.e., electronically searchable and paired with essential metadata]); See also *P&G v. S.C. Johnson & Son, Inc.*, 2009 WL 440543 (E.D. Tex. Feb. 19, 2009)(production made in “searchable TIFF”).

95 *Id.*, at 362-363 (targeted queries and live demonstration of system operation).

96 2009 WL 260954 (E.D. Ky. Feb. 2, 2009).

The advantage to an imaged format is that it can be easily bates numbered and redacted and does not contain associated metadata or embedded data requiring additional review for privilege.⁹⁷

Meaningful consultation on the most appropriate form or forms of production should take place as early as feasible.⁹⁸ In *D'Onofrio v. SFX Sports Group, Inc.*,⁹⁹ the failure to clearly request information in its original format with metadata was fatal to a motion to compel.¹⁰⁰

When the need for production in native format is litigated, the “proportionality principle” applies in assessing the need for metadata. Thus, in *Michigan First Credit Union v. Cumis Insurance Society*,¹⁰¹ the court sustained an objection to production “along with intact metadata” because “production of this metadata would be overly burdensome with no corresponding evidentiary value.”

D. Search & Retrieval

Parties must conduct a diligent search for relevant information using reasonable search criteria when responding to discovery. In *Keithley v. Homestore.Com.*,¹⁰² the court criticized the “lackadaisical attitude” employed and the “egregious failure to diligently search for responsive documents in alternative locations until well after the eleventh hour.”

The court in *Ford Motor v. Edgewood*,¹⁰³ however, noted that the producing party is often in the best position to design an “appropriate method of searching and culling data.”

Search or “culling” of ESI to reduce the amount of information requiring manual review is an important part of the process. Typical best practices include “elimination of system files, de-duplication, culling by date ranges, keyword search, and identification of target subsets.”¹⁰⁴

The use of key words has been endorsed as a search method for reducing the need for human review of large volumes of ESI. As noted in the case of *In re Seroquel Products Liability*,¹⁰⁵ however, it must be “a cooperative and informed process [which includes] sampling and other quality assurance techniques.”

Some courts have authorized cost-shifting where a party failed to take the opportunity to participate in formulating search terms.¹⁰⁶

The failure to use appropriate search technology has been criticized. In *Wingnut Films, Ltd. v. Katja Motion Pictures Corp.*,¹⁰⁷ sanctions were imposed for a failure to “conduct or arrange for a server-wide search for documents containing the phrase “Lord of the Rings” or any other keywords.”

Courts are prepared to critically examine the methods used. In *United States v. O'Keefe*,¹⁰⁸ the Court opined that the determination of whether search terms will yield information is a complex question “clearly beyond the ken of a layman” and requires evidence that “meets the criteria of [FRE] 702.” In *Victor Stanley v. Creative Pipe*,¹⁰⁹ keyword searching was not deemed to be “reasonable” when the proponent failed to adequately explain the process.

97 See also Burns et al., *E-Discovery*, supra, 64 NYU Law Rev. 201 at 216 (alluding to the variety of competing ethical conclusions about the propriety of “metadata mining”).

98 Sedona Principle 12 has now favors production in native format where it is needed in light of the nature of the case. See Aguilar, supra, 255 F.R.D. at 356.

99 247 F.R.D. 43 (D.D.C. 2008).

100 Id. at 48 (approving observation that “in order to obtain metadata . . . you should specifically ask for it to begin with”).

101 2007 WL 4098213 (E.D. Mich. 2007).

102 2008 WL 3833384, at *5 (N.D. Cal. 2008).

103 2009 WL 1416223, at *9 (D. N.J. 2009) (relying on Sedona Principle 6 in absence of showing that the party was “purposefully (or even negligently) withholding documents”).

104 The Sedona Conference “Best Practices for the Selection of Electronic Discovery Vendors: Navigating the Vendor Proposal Process (June 2007 Version), D-3.

105 244 F.R.D. 650, 662 (M.D. Fla. Aug. 21, 2007) (criticizing failure to identify or validate process).

106 Surplus Source v. Mid America Engine, 2009 WL 961207 (E.D. Tex. April 8, 2009) (cost of additional run of search terms).

107 2007 WL 2758571 (C.D. Cal. 2007).

108 2008 WL 449729 (D.D.C. 2008).

109 250 F.R.D. 251 (D. Md. May 29, 2008).

In *Disability Rights Council v. WMTA*,¹¹⁰ the court noted the “recent scholarship” indicating the efficiencies of “concept searching.”¹¹¹ The Sedona Conference® has covered these and related topics in several publications.¹¹²

E. Shifting Costs

The Supreme Court held in *Oppenheimer Fund, Inc. v. Sanders*¹¹³ that while a presumption exists that producing parties pay the costs of production, a court may mitigate undue burden by requiring “payment of the costs of discovery.”¹¹⁴

In making its decision, a court is not bound to apply any particular formula or multi-factor test. In *Guy Chemical Company v. Romaco*,¹¹⁵ the court rejected the need for rigid formulae in favor of the exercise of sound discretion. In contrast, *Zubulake I*,¹¹⁶ suggests the employment of a hierarchy of factors.

In *Zubulake III*,¹¹⁷ the court asserted that “only the costs of restoration and searching should be shifted” and that “the responding party should always bear the cost of reviewing and producing electronic data.”¹¹⁸

However, the 2006 Amendments do not limit the power of a court to remedy undue burdens. While Rule 26(b)(2)(B) affirmatively notes the power of courts to condition discovery from inaccessible sources on the payment of costs, “[t]he amended rule does not say that judges may only consider cost allocation if the subject of the discovery . . . is not reasonably accessible.”¹¹⁹

Parties must discuss the issue early enough that meaningful evaluation of the need for cost-shifting, if any, can occur *before* any costs are incurred and courts can carefully monitor the nature and extent of the cost-shifting process.¹²⁰

In *CBT Flint Partners v. Return Path, Inc.*,¹²¹ the court required a requesting party to pay for the costs of a privilege review as a condition of compliance with the “extraordinary demands made [for] document production.” This was consistent with *Principle 13* of the Sedona Principles (Second Edition), which recommends that the “costs of retrieving and reviewing” electronic information can be shifted in appropriate cases.¹²²

In *Chemie v. PPG Industries, Inc.*,¹²³ the court held that because privilege review in that case was such a “daunting task,” the costs of searching for documents and preparing a privilege log would be “open to further discussion [and] [i]t may be that some cost sharing is warranted.”

Some courts see the cost of privilege review or culling of information prior to production as a burden which should be assumed by a producing party as a matter of course.¹²⁴ In *Brookdale University Hospital v. Health Insurance Plan*,¹²⁵ for example, a court rejected a request for fees and vendor costs associated with locating privileged information under the facts of the case.

110 242 F.R.D. 139 (D.D.C. June 1, 2007).

111 See also Committee Note to Fed. R. Evid. 502(b) (references to use of advanced technology).

112 The Sedona Conference® *Commentary on Search and Information Retrieval Methods* (2007), 8 The Sedona Conf. J. 189 (2008); The Sedona Conference® *Commentary on Achieving Quality* (2009).

113 437 U.S. 340, 358 (1978).

114 *Id.* (a party “may invoke the district court’s discretion under Rule 26(c) to grant orders protecting him from ‘undue burden or expense.’”).

115 243 F.R.D. 310 at *2 (N.D. Ind. 2007) (“This Court has discretion [to act] and finds [it] unnecessary to engage in such an analysis.”).

116 See *Zubulake v. UBS Warburg LLC*, 217 F.R.D. 309, 320-324 (2003) (announcing a seven factor test).

117 216 F.R.D. 280 (S.D. N.Y. 2003).

118 *Id.*, at 290.

119 The Hon. Lee H. Rosenthal, *A Few Thoughts on Electronic Discovery after December 1, 2006*, 116 Yale L. J. Pocket Part 167 at 180 (2006).

120 *Cason-Merenda v. Detroit Med. Ctr.*, 2008 WL 2714239 (E.D. Mich. 2008).

121 2008 WL 4441920 (N.D. Ga. Aug. 7, 2008) (payment of \$300,000 for “costs of the review” because of the failure to demonstrate that the “relevance and importance are proportional” to the costs involved).

122 *Sedona Principle 13* provides, in relevant part, that “[i]f the information sought is not reasonably available to the responding party in the ordinary course of business, then, absent special circumstances, the costs of retrieving and reviewing such electronic information may be shared by or shifted to the requesting party.”

123 218 F.R.D. 416, 422 (D. Del. 2003).

124 See *Covad Communications v. Revonet*, 254 F.R.D. 147, 150 (D.D.C. 2008) (presumption exists that cost of privilege review is assumed by producing party as a matter of course, citing to *Peskoff v. Faber*, 251 F.R.D. 59, 61 (D.D.C., 2008) (refusing to shift costs of forensic examination).

125 2009 WL 393644 (E.D. N.Y. Feb. 13, 2009).

While some courts have permitted parties to “purchase” discovery,¹²⁶ other cases have cogently cautioned against such a practice.¹²⁷ A willingness to pay costs should not automatically entitle a party to discovery.

F. Direct Access and Sampling

Rule 34(a), as amended, explicitly provides that a party may seek to “test or sample” designated documents or electronically stored information.

A typical example occurs when a requesting party seeks direct access because of its concerns over compliance with discovery obligations. Courts typically require proof that the producing party has been unwilling or unable to produce the information sought or that the information is about to be lost. As pointed out in *Butler v. Kmart Corporation*,¹²⁸ Rule 34(a) “does not generally give the requesting party [the] right to search the responding party’s records,” citing the Eleventh Circuit opinion in the seminal case of *In re Ford Motor Co.*¹²⁹

Another example is when a producing party is faced with production from complex databases. In *Zurich American v. ACE*,¹³⁰ a Magistrate Judge ordered that a “protocol for sampling” be prepared to secure examples of the information sought. Similarly, in *Aguilar v. ICE*,¹³¹ the court ordered a demonstration of a database operation to help decide whether targeted inquiries would be sufficient.

Courts seem to find ways, however, to routinely permit forensic examinations of laptops, servers and distributed devices where credible allegations of breach of non-compete or unfair competition are involved.¹³² In *Bank of Mongolia v. M&P Global*,¹³³ the court ordered access based merely on inadequacies of production, not any showing of unwillingness to perform or misconduct.

However, a higher standard is often applied when third parties are involved. In *Daimler Truck v. Younessi*,¹³⁴ the recipient of a subpoena was permitted to make its own search and was not required to produce its computer for copying.

G. Privileged Information

The sheer volume of electronic information available in the typical case makes it more difficult to conduct a meaningful pre-production review for privileged and confidential information. This has serious cost implications since costly manual review by counsel is often involved.¹³⁵

The Advisory Committee recommended that parties consider appropriate “claw-back” arrangements as well “quick peek” arrangements whereby pre-production privilege review would be limited or eliminated.¹³⁶ Rule 26(b)(5)(B) was added by the 2006 Amendments to provide a backup “claw-back” procedure in the absence of an agreement or court order.

Subsequently, Congress passed and the President signed Evidence Rule 502 into law, thereby creating a basis for substantive court action.¹³⁷

126 See *National Union Fire Insurance v. Clearwater Insurance*, 2007 WL 2106098 at *3, n. 10 (S.D. N.Y. 2007) (“[I]f Clearwater wishes to pay to restore the data of the back-up tapes, it may do so.”).

127 *Cognex Corporation v. Electro Scientific Industries*, 2002 WL 32309413 (D. Mass. 2002) (“At some point, [we] need to say ‘enough is enough’”).

128 2007 WL 2406982 (N.D. Miss. 2007).

129 345 F.3d 1315, 1317 (11th Cir. 2003).

130 2006 WL 3771090 (S.D. N.Y. 2006).

131 255 F.R.D. 350, 363 (S.D. N.Y. 2008).

132 See, e.g., *Andrew v. Cassinelli*, 2009 WL 736669 (N.D. Ill. March 18, 2009) (appointing special master to oversee discovery because search by defendant was “deficient”); compare *Mintel v. Neerghen*, 2009 WL 1033357 (N.D. Ill. April 17, 2009) (“mere speculation” not enough to justify forensic examination of third party’s computers).

133 2009 WL 1117312 (S.D. Fla. April 24, 2009) (arguing that this does not allow “unfettered access” to computer since expert was officer of the court).

134 2008 WL 2519845 (W.D. Wash. 2008).

135 Jack E. Pace III and John D. Rue, *Early Reflections on E-Discovery in Antitrust Litigation: Ten Months Into the New Regime*, 22-FALL Antitrust 67, 69 (Fall, 2007) (costs of privilege review necessary for production of ESI (including metadata) can be staggering).

136 Committee Note, Rule 26(f) (2006).

137 Act of Sept. 19, 2008, PL 110-322, 122 Stat. 3537.

Thus, Rule 502(d)¹³⁸ clarifies that non-waiver orders permitting production without any review (the “quick peek” approach) are binding on parties and non-parties alike. While such non-waiver orders have been issued before, they typically have been confined to idiosyncratic cases.¹³⁹ In the case of *In re Fannie Mae Securities Litigation*,¹⁴⁰ for example, the D.C. Court of Appeals, mandated the production of privileged materials to opposing counsel as a sanction for delays in producing a privilege log in order to facilitate “faster” resolution of outstanding privilege disputes.

As a practical matter, however, it is virtually impossible to “unring the bell” when privileged or confidential information is disclosed to opposing parties and their counsel.¹⁴¹ Routine consensual use of “quick-peeks” is therefore quite unlikely.

Courts should resist the temptation to compel parties to forgo pre-production review.¹⁴² The federal rules do not “supersede the lawyer’s duty of confidentiality under Model Rule 1.6.”¹⁴³ Courts should tread lightly when dealing with ethical obligations not to disclose privileged information.¹⁴⁴

In addition, Rule 502(b)¹⁴⁵ provides a uniform national standard for adjudicating claims of waiver through inadvertent production. In *Rboads Industries v. Building Materials Corp.*¹⁴⁶ and *Heriot v. Byrne*,¹⁴⁷ production of privileged information did not constitute a waiver since reasonable steps were undertaken to prevent disclosure. The opposite conclusion was reached in *Victor Stanley v. Creative Pipe*.¹⁴⁸

The preparation of privilege logs, as required by Rule 26(b)(5)(A), is increasingly at the center of concerns over costs and privilege waiver. When both privileged and non-privileged communications are present, only the privileged communications which are adequately identified may be withheld from a chain of emails.¹⁴⁹

Thus, consensual arrangements designed to reduce the burdens of privilege logs are worthy of serious consideration.¹⁵⁰

Counsel has the responsibility, under Rule 26(g), to make a “reasonable inquiry” about any search methodology employed prior to signing a response or objection based on the search.¹⁵¹

H. Discovery Sanctions

Courts are increasingly prepared to sanction inadequate compliance with discovery obligations involving ESI.¹⁵² Unlike the case of pre-discovery spoliation sanctions,¹⁵³ discussed *supra*, specific Federal Rules often provide the rule of decision and Rule 37(e), the so-called “safe harbor” rule, is largely inapplicable.

138 Rule 502(d) provides that a federal court may order “that the privilege or protection is not waived by disclosure” and it “is also not a waiver in any other Federal or State proceeding”.

139 *Whitaker Chalk Sundeal & Sawyer, LLP v. Dart Oil & Gas Corporation*, 2009 WL 464989 (N.D.Tex. Feb. 23, 2009)(compelling initial disclosures of privileged and confidential information despite risks of waiver in state proceedings).

140 552 F.3d 814 (D.C. Cir. Jan. 6, 2009)(involving “deliberative process privilege” without mention of Rule 502).

141 *D’Onofrio v. SFX*, 2009 WL 859293, at *3 (D.D.C. April 1, 2009)(“it is difficult to unlearn something once it is learned”).

142 See Testimony of Thomas Y. Allman, Advisory Committee on Evidence Rules, Hearings, Phoenix, Arizona (Jan. 12, 2007) at pps 7-9 (expressing guarded support for limited use of “quick peek” agreements but cautioning against compelling parties to do so without their agreement), available at http://www.uscourts.gov/rules/EV_Hearing_Transcript_011207.pdf

143 Mark L. Tuf, *Techno Ethics: Ethical Challenges in Emerging Technology*, ABA GP Solo Magazine (June 2007).

144 *Compare Koch Foods of Alabama LLC v. General Electric Capital Corporation*, 2008 WL 152723 (M.D. Ala., 2008) with *Mass Engineered Design v. Ergotran*, 2008 WL 4873421, at *3-4 (E.D. Tex. 2008)(attorney notes compelled as sanction where ethical rules are violated).

145 Rule 502(b) requires proof of (1) inadvertent disclosure (2) reasonable steps to prevent it and (3) prompt and reasonable steps to rectify the error.

146 254 F.R.D. 216 (E.D. Pa. Nov. 14, 2008)(pre-production reviews largely conducted by automated means).

147 2009 WL 742769 (N.D. Ill. March 20, 2009)(vendor production not monitored nor quality assurance checking conducted).

148 250 F.R.D. 251, 262 (D. Md. May 29, 2008)(finding that keyword searching was not “reasonable” given the failure to explain what had been done and why it was sufficient).

149 See *Muro v. Target Corporation* 243 F.R.D. 301 (N.D. Ill. 2007).

150 See Jeanne A. Thomas, David D. Cross and Courtney Ingrassia Barton, *Reducing the Costs of Privilege Reviews and Logs*, Nat. L. J., March 23, 2009 (cost savings can come from not logging privileged documents which would not be harmful if disclosed).

151 See *Nelson v. Farm, Inc.*, 2009 WL 939123 (D. Kan. April 6, 2009)(requiring affirmative statement of search methods used).

152 See Sheri Qualters, *25 Percent of Reported E-Discovery Opinions in 2008 Involved Sanctions Issues*, NAT’L L.J., Dec. 17, 2008, (sanctions for the mishandling of electronic discovery).

153 *Alden v. Mid-Mesabi Associates*, 2008 WL 2828892, at *16 (D. Minn. 2008)(failure to produce ESI “bears a close relationship to the ‘spoliation of evidence’ and is sanctioned accordingly”); but see *Stamphill v. Health Care*, 2008 WL 2359730 (W.D. Okla. 2008)(a sanction under Rule 37 where documents are not destroyed is not a spoliation claim).

Generally speaking, “mere imperfection” in discovery compliance is not sufficient grounds for sanctions, especially where the deficiencies are not timely called to the courts attention.¹⁵⁴

Rule 37 requires that the sanctions be “appropriate” and “just” and there is “no bad faith requirement.”¹⁵⁵ In *Keithley v. Homestore.Com*¹⁵⁶ and *Adele S.R.L. v. Filene’s Basement, Inc.*,¹⁵⁷ for example, the court issued monetary sanctions for late production of information. Courts also cite Rule 26(g) when counsel has failed to make a reasonable inquiry about the scope or diligence of discovery.

However, an entry of dismissal or default is not authorized under either rule without a showing of “willfulness, bad faith or fault.”¹⁵⁸

Courts frequently utilize their inherent power to sanction egregious discovery abuse.¹⁵⁹ In *Qualcomm Inc. v. Broadcom*,¹⁶⁰ the intentionally ignoring of warning signs that a client search was inadequate led to severe sanctions on client and counsel. Other recent cases involving similar misconduct include *Southern New England Telephone Co. v. Global NAPs, Inc.*,¹⁶¹ *Micron Technology, Inc. v. Rambus Inc.*¹⁶² and *Kipperman v. Onex Corporation*.¹⁶³

In some cases, courts impose sanctions on both counsel and client, although the more typical response is to sanction the party,¹⁶⁴ especially where there is a failure to commit adequate resources to the discovery effort.¹⁶⁵

However, “where the infraction is the fault of the party’s attorney, the appropriate remedy is to shift the costs to the party’s counsel.”¹⁶⁶ In *Bray & Gillespie Management LLC v. Lexington Insurance Co.*,¹⁶⁷ the court sanctioned lead counsel and his law firm while exonerating the client.

IV. CONCLUSION

The 2006 Amendments were designed, as noted in *Board of Regents v. BASF Corp.*,¹⁶⁸ to promote open and forthright sharing of information to expedite case progress, minimize burden and expense and remove contentiousness as much as possible.

Nonetheless, the costs of e-discovery continue to rise, which carries grave risks and threatens to undermine confidence in the judicial system. In its 2007 decision in *Bell Atlantic Corporation v. Twombly*,¹⁶⁹ the Supreme Court noted that “the threat of discovery expense will push cost-conscious defendants to settle even anemic cases before reaching those proceedings.”¹⁷⁰

It has been argued that the 2006 Amendments are not sufficient to adequately address the rising cost of e-discovery. If this proves to be the case, there may be a need for further amendments to the Civil Rules of Procedure.¹⁷¹

154 *Swofford v. Eslinger*, 2009 WL 1025223, at *1 (M.D. Fla. April 14, 2009)(“The purpose of the discovery rules is to facilitate resolution of cases on their merits . . . [c]reation of satellite litigations or opportunities for seeking sanctions is not a goal of the process.”).

155 *Stanphill v. Health Care*, 2008 WL 2359730 (W.D. Okla. June 3, 2008).

156 2008 WL 4830752 (N.D. Cal. 2008).

157 2009 WL 855955 (S.D. N.Y. March 24, 2009)(criticizing “slothfulness” and “discovery passivity”).

158 *GSI Group v. Sukup*, 2008 WL 3849695 at *5 (C.D. Ill. Aug. 18, 2008).

159 See *Chambers v. NASCO, Inc.*, 501 U.S. 32, 44-45 (1991). In addition, courts can seek, at least as to counsel, to impose sanctions under the authority of 28 U.S.C. § 1927, which applies when an attorney has multiplied proceedings “unreasonably and vexatiously.”

160 2008 WL 66932, at *13 (S.D. Cal. 2008).

161 251 F.R.D. 82, 96 (D. Conn. 2008)(repeated violations of discovery orders).

162 255 F.R.D. 135, 150 (D. Del. 2007)(destruction of documents that party “knew or should have known” would become material).

163 2009 WL 1473708 (N.D. Ga. May 27, 2009).

164 See Allman, *The Use of Counsel Sanctions*, *supra*, 15 Rich. J.L. & Tech. 9 at Paragraphs 51-55 (most courts apply a mild de facto presumption against sanctioning counsel for discovery misconduct, even when the client is relatively blameless).

165 See, e.g., *L.H. v. Schwarzenegger*, 2008 WL 2073958 (E.D. Cal. 2008)(criticizing reliance on one employee to respond to discovery in statewide class action); *accord Rhoads v. Building Materials*, 254 F.R.D. 216, 227 (E.D. Pa. Nov. 14, 2008)(desire to “minimize costs of litigation and to be frugal” no excuse for “failed screening of privileged documents”).

166 *Ogler Homes v. Chicago Regional Council of Carpenters*, 2008 WL 5082979 (N.D. Ill. Nov. 24, 2008)(costs of changes in expert report due to late submission of information).

167 2009 WL 546429, at *21 (M.D. Fla. Mar. 4, 2009).

168 2007 WL 3342423 at 5(D. Neb. Nov. 5, 2007).

169 550 U.S. 544, 127 Sup.Ct. 1955 (2007)

170 127 Sup. Ct. at 1967.

171 See Final Report of the American College of Trial Lawyers and the Institute for the Advancement of the American Legal System, March 2009, at p. 17.

FEDERAL RULE OF EVIDENCE 502(d) AND COMPELLED QUICK PEEK PRODUCTIONS

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INTRODUCTION

In 2006, the e-discovery amendments to the Federal Rules of Civil Procedure went into effect. These amendments provided a formal introduction of “quick peek” productions to the legal community. While quick peek productions lack a specific definition, the fundamental concept involves a party responding to document requests or a subpoena by producing its documents and data without performing a privilege or responsiveness review. The production itself, however, does not constitute a waiver of privilege. The producing party can later assert privilege over documents that the receiving party intends to use.

Despite this introduction and litigants’ constant complaint about the costs of privilege review, quick peek productions are rarely undertaken. One reason litigants have avoided quick peek agreements is because they were not assured they could enforce the non-waiver agreement against non-parties in separate matters. The recent introduction of Federal Rule of Evidence 502, particularly subdivision (d), protects against this danger. According to Rule 502(d), a court may enter an order that holds any disclosure of privileged material made during that litigation does not constitute a waiver in that proceeding or a subsequent proceeding. The first part of this paper explains in more detail how Rule 502(d) covers quick peek productions, and how it relates to other subdivisions in Rule 502. In light of the viability of quick peek productions, the second part of the paper examines whether a court can compel quick peek productions on non-consenting parties.

I. THE HEART OF FEDERAL RULE OF EVIDENCE 502.

Unbeknownst to the casual reader, subdivision (d) is the most important provision of Rule 502. Most lawyers read Rule 502 and surmise that the critical provision is subdivision (b), which establishes a uniform standard to determine what constitutes an inadvertent disclosure. While this provision is unquestionably important, subdivision (d) permits parties to essentially do away with privilege review without waiving privilege over any protected communications. That would be a major sea change from the status quo.

Before Rule 502(d), parties could not effectively enter into quick peek agreements because the parties had no protection from a non-party that later contended in a separate proceeding that the quick peek production constituted a waiver of privilege.¹ And Rule 502(b) only protects privilege for inadvertent disclosures made with reasonable care to prevent disclosure. Under Rule 502(d), however, parties may opt out of the default standard in subdivision (b) and disclose documents under any standard of care if that standard is memorialized by a court order. Specifically, Rule 502(d) provides:

¹ See, e.g., *Genentech, Inc. v. U.S. Int’l Trade Comm’n*, 122 F.3d 1409, 1418 (Fed. Cir. 1997) (finding waiver after production of documents in a separate matter even though the production was pursuant to a protective order). See also FED. R. EVID. 502, Advisory Committee Notes (2007) (“Parties are unlikely to be able to reduce the costs of pre-production review for privilege and work product if the consequence of disclosure is that the communications or information could be used by non-parties to the litigation.”).

(d) Controlling effect of a court order. A federal court may order that the privilege or protection is not waived by disclosure connected with the litigation pending before the court – in which event the disclosure is also not a waiver in any other federal or state proceeding.

Thus, through a court order under Rule 502(d), parties may engage in quick peek productions without threat of any party later arguing—in a state or federal proceeding—that that production waived privileged.² Indeed, the Advisory Committee specifically envisioned quick peek agreements pursuant to Rule 502(d). “[T]he court order may provide for return of documents without waiver irrespective of the care taken by the disclosing party; the rule contemplates enforcement of ‘claw-back’ and ‘quick peek’ arrangements as a way to avoid the excessive costs of pre-production review for privilege and work product.”³

Subdivisions (e) and (f) reinforce the general principle in subdivision (d). Rule 502(e) underscores the need for a court order, and not just an agreement between parties. Like some courts under the common law,⁴ Rule 502(e) provides that a confidentiality agreement between parties is only binding on those parties. Thus, even if the parties agreed by themselves to quick peek productions, a non-party could later challenge disclosures made through those productions as waivers. A Rule 502(d) order, in contrast, applies to the world. Similarly, Rule 502(f) explicitly establishes that a court order under subdivision (d) applies to subsequent state proceedings.⁵ If Rule 502(d) orders did not apply to subsequent state actions, “the holders of protected communications and information, and their lawyers, could not rely on the protections provided by the Rule, and the goal of limiting costs in discovery would be substantially undermined.”⁶

In sum, Rule 502(d) clearly and effectively allows parties to engage in whatever form of document production they want without fear of waiving privilege, as long as a court incorporates that process into an order. In fact, courts may even issue a Rule 502(d) order *sua sponte* and without party agreement.⁷ And one court has already required parties in a discovery dispute to address Rule 502 for future production and cost issues.⁸ This line of reasoning raises the more provocative question of whether courts can compel parties to engage in a quick peek production without the parties consent.

II. CAN A COURT FORCE A QUICK PEEK DOCUMENT PRODUCTION ON NON-CONSENTING PARTIES?

One question that has arisen since Rule 502 took effect is whether a court may require parties to produce documents according to a court-ordered quick peek. In a strict sense, this issue is one of first impression. The analysis is two-fold. The first issue is whether the courts have the authority to compel quick peek productions on non-consenting litigants. If they do, the second issue is whether and when courts should invoke that authority. The following discussion addresses each issue.

A. Courts Can Likely Achieve at Least the Result of Forcing Quick Peek Productions on Non-Consenting Parties.

The question over whether a United States district court judge can require a quick peek production pits two longstanding principles against each other: the power of a district court to manage its cases versus the sanctity of the confidential relationship between attorney and client. Both proponents and opponents of forced quick peek productions have a basis for their position. Ultimately, however, a court may likely succeed in at least issuing such a short schedule for document production that it leaves no other choice on the parties but to adopt a quick peek format.

² See, e.g., Gregory P. Joseph, *The Impact of Rule 502(d) on Protective Orders*, Minnesota State Bar Association CLE, Pressure on the Privilege, at 4 (2008).

³ FED. R. EVID. 502, Advisory Committee Notes (2007).

⁴ See *Hopson v. City of Baltimore*, 232 F.R.D. 228, 234-36 (D. Md. 2005) (discussing split in case law regarding whether non-waiver agreements were enforceable).

⁵ Some question the constitutionality of this provision. See generally Henry S. Noyes, *Federal Rule of Evidence 502: Stirring the State Law of Privilege and Professional Responsibility with a Federal Stick*, 66 WASH. & LEE L. REV. 673 (2009).

⁶ FED. R. EVID. 502, Advisory Committee Notes (2007).

⁷ FED. R. EVID. 502, Advisory Committee Notes (2007) (“Party Agreement should not be a condition of enforceability of a federal court’s order”).

⁸ *Spieker v. Quest Cherokee, LLC*, No. 07-1225-EFM, 2008 WL 4758604, at *4 (D. Kan. Oct. 30, 2008).

1. A Proposed Basis of Authority to Require Quick Peek Productions.

The confidential nature of the attorney-client privilege has never absolutely trumped a district court's authority to review the privileged communication. The most obvious example, of course, is the *in camera* review procedure. Courts historically and routinely have required parties to disclose allegedly privileged communications for a court-only review to determine if the communication is properly privileged.⁹ Despite the disclosure, the privilege is maintained if the court concludes that the communication is privileged.¹⁰ The *in camera* review procedure underscores that the privilege is not absolutely confidential between attorney and client. But the issue of forcing a party to disclose its privileged communications—not just to the court—but to its adversary is a substantial step further, and requires a review of a court's authority to issue that order.

Rule 502 does not provide that authority. While Rule 502(d) permits a court to enter an order allowing parties to engage in a quick peek productions, Rule 502 provides no explicit grant of power to district courts authorizing them to force parties to produce documents in such a format. Rule 502 does not offer an independent basis for a court to force parties to do away with privilege review.

A court's authority to control the manner in which parties produce documents would likely come from its inherent authority over case management. "Courts are invested with inherent powers that are 'governed not by rule or statute but by the control necessarily vested in courts to manage their own affairs so as to achieve the orderly and expeditious disposition of cases.'" Within this context of a court's authority to manage discovery in its cases lies support for proponents who will argue that a court can require quick peek productions.

The leading case in this regard is *Transamerica Computer Company, Inc. v. International Business Machines, Corp.*¹² The Ninth Circuit decided the *Transamerica* case on interlocutory appeal. It involved an underlying antitrust action in the Northern District of California, which was the subject of multi-district litigation centered in the District of Minnesota.¹³ The District of Minnesota managed discovery for the cases, and issued an order that required IBM, the defendant, to produce documents within three months.¹⁴ This required extraordinary effort because IBM had seventeen million documents to prepare for inspection.¹⁵ In order to relieve the burden placed on IBM, the district court ruled that inadvertently produced privileged documents did not constitute waiver.¹⁶

In a decision ahead of its time, the Ninth Circuit addressed a party's contention that the documents produced in litigation in the District of Minnesota waived attorney-client privilege in regards to separate litigation in another jurisdiction. Essentially, the issue was whether the court's order requiring accelerated document review and production while preventing waiver was valid.¹⁷ Through its analysis, the Ninth Circuit concluded that the court had "in a very practical way, 'compelled' [IBM] to produce privileged documents" under the court's pretrial discovery order.¹⁸ The Ninth Circuit, nonetheless, approved of the pretrial order because it preserved the attorney-client privilege.¹⁹ In upholding the finding of non-waiver, the Ninth Circuit indicated that "[o]ne reasonable method of accelerating the discovery proceedings without impinging upon the parties' right to prepare their cases properly was to do precisely what Judge Neville did, that is, to issue an order preserving claims of privilege."²⁰

9 See, e.g., *United States v. Zolin*, 491 U.S. 554, 568 (1989) ("Indeed, this Court has approved the practice of requiring parties who seek to avoid disclosure of documents to make the documents available for *in camera* inspection, and the practice is well established in the federal courts.").

10 *Id.* (explaining that "disclosure of allegedly privileged materials to the district court for purposes of determining the merits of a claim of privilege does not have the legal effect of terminating the privilege").

11 See, e.g., *Unigard Sec. Ins. Co. v. Lakewood Engineering & Mfg. Corp.*, 982 F.2d 363, 368 (9th Cir. 1992) (quoting *Chambers v. NASCO, Inc.*, 501 U.S. 32, 43 (1991)); *Naartex Consulting Corp. v. Watt*, 722 F.2d 779, 783, (D.C. Cir. 1983), *cert. denied*, 467 U.S. 1210 (1983) (explaining that "a district court has broad discretion in its resolution of discovery problems that arise in cases pending before it").

12 573 F.2d 646 (9th Cir. 1978).

13 See *id.* at 648.

14 See *id.*

15 See *id.*

16 See *id.* at 649-50.

17 See *id.* at 647.

18 See *id.* at 651-52. Other courts view the underlying facts as "compelled disclosure." See, e.g., *In re Sealed Cases*, 877 F.2d 976, 980 (D.C. Cir. 1989) (classifying *Transamerica* as "court-compelled disclosure").

19 Importantly, the Ninth Circuit indicated that had the district failed to preserve the privilege, the pretrial order would have exceeded the trial court's discretion. See *id.* at 652.

20 *Id.* at 653.

The teaching point in *Transamerica*, therefore, is that a district court's discovery order will be upheld even if it effectively requires a party to produce privileged documents to its adversary, as long as the privilege is not lost. Proponents of allowing courts to force quick peek production format on parties will use this reasoning as their basis for authority and precedent.

2. An Opposition to Forced Quick Peek Productions.

Parties unwilling to agree to a quick peek production, however, will unlikely accept a court's authority to impose a quick peek production upon them. Opponents of compelled disclosure will likely assert that compelled disclosure violates a party's fundamental Due Process rights. Even though the attorney-client privilege is not a constitutional right,²¹ courts have found the Due Process clause implicated when privileged communications are required to be disclosed.²² More generally, in fact, case law addressing whether a crime or fraud has vitiated the attorney-client privilege establishes that parties have rights to prevent disclosure of privileged communications—even to the court *in camera*.

The United States Supreme Court held in *United States v. Zolin* that a court cannot compel a party to disclose privileged communications for *in camera* inspection without the requesting party making a showing of a factual basis adequate to support a good faith belief that a reasonable person would conclude a review of the privileged communications may reveal evidence of a crime or fraud.²³ The Court reached this conclusion because a blanket rule allowing *in camera* review “would place the policy of protecting open and legitimate disclosure between attorneys and clients at undue risk.”²⁴

The *Zolin* Court also held that a more stringent test than the “reasonable party” test would be required if a party sought outright disclosure of the privileged communication, and not just *in camera* review.²⁵ To justify invading the privilege, courts require that the requesting party make a *prima facie* showing of a crime or fraud.²⁶ The Ninth Circuit recently held that this *prima facie* showing must be made by a preponderance of the evidence standard.²⁷ In addition to the required *prima facie* showing by the requesting party, moreover, courts hold that the party invoking the privilege has an absolute right to offer evidence supporting the privilege.²⁸ “The importance of the privilege [] as well as fundamental concepts of due process require that a party defending the privilege be given the opportunity to be heard, by evidence and argument, at the hearing seeking an exception to the privilege.”²⁹

The solid precedent that articulates the burden of proof and procedure for vitiating an attorney-client communication due to the commission of a crime or fraud is a powerful obstacle to a court forcing a quick peek production format on non-consenting parties. If a court cannot require disclosure of a privileged communication *in camera* unless the “reasonable person” standard has been met showing that a crime or fraud took place, then, *a fortiori*, a court will not be able to compel parties to produce their files—including privileged communications—upon no showing. Quite simply, this case law establishes that the attorney-client privilege cannot be broken in a cavalier manner. As a result, it provides a strong basis to maintain that a quick peek production cannot be forced upon a non-consenting party.

21 See, e.g., *Clutchette v. Rushen*, 770 F.2d 1469, 1471 (9th Cir.1985), cert. denied, 475 U.S. 1088 (1986).

22 See, e.g., *In re John Doe Corp.*, 675 F.2d 482, 489-90 (2d Cir. 1982) (explaining that routine *in camera* proceedings would violate due process). See also *In re Grand Jury Proceedings (Doe)*, No. 91-56139, 1993 WL 6598, at *3 (9th Cir. Jan. 15, 1993).

23 491 U.S. 554, 572 (1989).

24 *Id.* at 571.

25 *Id.* at 572.

26 *In re Feldberg*, 862 F.2d 622, 625-26 (7th Cir. 1988).

27 *In re Napster, Inc. Copyright Litig.*, 479 F.3d 1078, 1094-95 (9th Cir. 2007) (explaining that “judicious use of *in camera* review, combined with a preponderance burden for terminating privilege, strikes a better balance between the importance of the attorney-client privilege and deterrence of its abuse than a low threshold for outright disclosure.”).

28 See *Haines v. Liggett Group, Inc.*, 975 F.2d 81, 97 (3d Cir. 1992). See also *Napster*, 479 F.3d at 1093 (“We hold that in civil cases where outright disclosure is requested the party seeking to preserve the privilege has the right to introduce countervailing evidence.”); *In re General Motors Corp.*, 153 F.3d 714, 716 (8th Cir. 1998) (“This being a civil case, the district court may not, however, compel production without permitting the party asserting the privilege, to present evidence and argument.”).

29 *Haines*, 975 F.2d at 96-97.

3. A Court May Indirectly Require Parties to Produce Documents in a Quick Peek Format.

Even if a litigant succeeds in avoiding a direct order to produce documents in a quick peek format, that litigant can probably not avoid a *de facto* order that results in a quick peek production. As discussed above, courts enjoy broad discretion to “manage their own affairs so as to achieve the orderly and expeditious disposition of cases.”³⁰ A court very well could order document production to be completed within one or two months, along with a Rule 502(d) order stating that if the parties agree to a quick peek format that no waiver will result. Such a timeframe in a massive and complex litigation may indirectly force the parties to forgo a privilege review and produce their documents in a quick peek format.

B. Forced Quick Peek Productions Unfairly Prejudice and Harm Litigants.

Forced quick peek productions raise a number of concerns for litigants. Quick peek productions jeopardize the sanctity of the attorney-client privilege and undermine the policy justifying the privilege, may prejudice the privilege holder in litigation, are at odds with litigants’ business considerations, and improperly and ineffectively shift the burden of document production to the receiving party. These concerns are all compounded when the quick peek production is involuntary.

1. Quick Peek Productions Are Inimical to the Attorney-Client Privilege.

The attorney-client privilege is the oldest privilege known to the common law.³¹ The existence of the privilege dates back to Roman law through “[t]he notion that the loyalty owed by the lawyer to his client’s case disables him from being a witness in his client’s case.”³² Similarly, the first trace of the privilege in the English common law dated back to Queen Elizabeth’s time, in which “the oath and honor of the barrister and the attorney protect them from being required to disclose, upon examination in court, the secrets of the client.”³³ This code of honor justification later shifted to the current basis: a client cannot be expected to put forth all necessary facts without the assurance that the lawyer will not be compelled to reveal those confidences over the client’s objection.³⁴ The United States adopted the privilege and this justification from the common law,³⁵ and the United States Supreme Court lucidly defined the policy behind the privilege in *Upjohn Co. v. United States* as encouraging “full and frank communications between attorneys and their clients and thereby promot[ing] broader public interests in the observance of law and administration of justice.”³⁶ The sanctity of the privilege is a bedrock principle of our system of justice.

The fundamental element of the privilege is that communications are confidential. In light of this confidentiality, clients tell their lawyer the most intimate and personal things in their lives. For that reason, attorneys are ethically bound to keep client communications in confidence, save specific exceptions.³⁷ The very notion of quick peek productions, therefore, is fundamentally foreign to attorneys, even if the approach is approved of by a federal court. And despite a court’s approval, the long-term consequences to the privilege must be assessed before quick peek productions are regularly undertaken.

In order to be effective, the United States Supreme Court explained that “if the purpose of the attorney-client privilege is to be served, the attorney and client must be able to predict with some degree of certainty whether particular discussions will be protected. An uncertain privilege, or one which purports to be certain but results in widely varying applications by the courts, is little better than no privilege at all.”³⁸ A quick peek production is at odds with this aspiration. In the long-run,

30 *Unigard Security Ins., Co. v. Lakewood Eng’r & Manuf., Corp.*, 982 F.2d 363, 368 (9th Cir. 1992).

31 *See Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981).

32 John W. Strong, MCCORMICK ON EVIDENCE, Section 87 at pg. 134 (5th Ed. 1999).

33 *Id.*

34 *See id.*

35 In 1776, Delaware was the first colony to codify the attorney-client privilege in its Constitution.

36 *Upjohn*, 449 U.S. at 389.

37 ABA Model Rule of Professional Conduct Section 1.6. An attorney does not violate his ethical obligations by disclosing confidential information pursuant to a court order. *See id.* Section 1.6(6).

38 *Upjohn*, 449 U.S. at 393.

then, it seems likely that clients will be reluctant to either turn over all their documents to their attorneys out of concern that their attorneys will not protect privileged information, or the clients will withhold relevant information while consulting with their attorneys, or both. These possibilities are diametrically opposed to the policy of encouraging “full and frank” communications between client and attorney.

Quick peek productions not only threaten the theory for the privilege, but the productions also raise practical concerns for attorneys and clients. The first concern is the inability to “unring the bell.”

2. Litigants Suffer Unfair Prejudice Through Disclosure of Privileged Communication to Their Adversaries.

Even though a party may be able to preserve privilege over a document produced in a quick peek format sanctioned by court order, the producing party may still bear unfair prejudice through the disclosure of the privileged communication alone, which cannot be undone. This refers to the proverbial bell that cannot be un-rung. Indeed, this was the basis for the strict approach to inadvertent disclosures. No matter what precautions were taken, the damage associated with the disclosure cannot be cured. One court explained, for instance, that “regardless of how painstaking the precautions, there is no order I can enter which erases from defendant’s counsel’s knowledge what has been disclosed. There is no remedy which can remedy what has occurred, regardless of whether or not the precautions were sufficient.”³⁹

While the law on inadvertent disclosure has changed, the peril identified by the court remains true today. There is nothing that a court or a party can do to prevent a receiving party from utilizing privileged information later in the litigation, even if the party does not use the privileged document. A party may, for instance, submit a request for admission that is based on review of a privileged document. Or a party may adjust its settlement position in light of its privileged review of information. The possibilities of prejudice are endless, and the stakes are often too high in complex litigation to gamble with these possibilities.

3. Litigants Will Also Oppose Open-file Productions.

Litigants will also oppose quick peek productions because clients do not want to produce non-responsive business-sensitive documents. Clients are concerned about producing documents to their competitors that disclose trade secrets and competitive information, as well as documents that may lead to additional causes of actions, like antitrust or employment class action suits. A protective order alone, moreover, will not assuage this concern. Courts, for example, will deny proposed experts access to an opposing party’s confidential information if there is a risk that the expert will misuse the confidential information, even if the proposed expert agrees to be bound by the protective order. Both conscious and subconscious abuse of the opponent’s confidential information can be real concerns that justify denying a party its expert of choice.⁴⁰ Likewise, even subconscious abuse by those privy to produced privileged documents is a real danger. This danger is compounded in quick peek productions where entire files of data are disclosed without any pre-production screening. Similarly, while many protective orders are meant to protect against use of the documents in a separate proceeding, including the commencement of a new proceeding,⁴¹ the fact remains that the more documents that are produced, the higher the possibility that they will become public or abused.

Litigants also risk violating privacy laws and confidentiality agreements through quick peek productions.

³⁹ *Genentech, Inc. v. U.S. Int’l Trade Comm.*, 120 F.R.D. 445, 449 (D. Mass. 1988).

⁴⁰ See, e.g., *Safe Flight Instrument, Corp. v. Sundstrand Data Control, Inc.*, 682 F. Supp. 20, 21 (D. Del. 1988); *IP Innovation, LLC, v. Thomson, Inc.*, No. 1:03-CV-0216, 2004 WL 771233, at *3 (S.D. Ind. Apr. 8, 2004).

⁴¹ See, e.g., *Del Giudice v. S.A.C. Capital Mgt., LLC*, No. 06-1413, 2009 WL 424368 (D.N.J. Feb. 19, 2009) (dismissing complaint where basis came from documents disclosed in separate litigation pursuant to a protective order).

4. Quick Peek Productions Shift The Burden of Review to The Receiving Party.

Quick Peek productions are meant to reduce costs associated not only with privilege review, but also review for responsiveness. In the latter sense, quick peek productions reverse the traditional rule that the producing party bears the expense of its own document production. The receiving party must bear the expense of reviewing its adversary's documents. This is particularly troubling in the context of massive amounts of e-discovery. As the Sedona Conference Best Practices suggest, "Responding parties are best suited to evaluate the procedures, methodologies, and technologies for preserving and producing their own electronically stored information."⁴² It follows naturally that a receiving party will have difficulty reviewing the ESI efficiently and effectively, given the party's lack of familiarity with the ESI.⁴³

Quick peek productions, moreover, encourage rather than discourage data dumps. In light of the fact that reviewing an adversary's ESI is a heightened expense for the reviewing party, parties will likely use a quick peek production as a strategic weapon; a way of increasing litigation costs and burying the most relevant documents. While this is not a new practice, at least before quick peek productions producing parties had to review the large amount of ESI and incur the corresponding expense before it could unload gigabytes and terabytes of data on its opponent. The result of placing the burden on the receiving party, moreover, is that it will need to utilize analytic software search tools to cull out the wheat from the shaft. But if the quick peek productions require the use of analytic software, there is no reason why the searches should not be done on the front-end and protect privileged materials through the process.

C. Courts Should Compel Quick Peek Productions in Rare Circumstances.

The legal and practical considerations identified above make clear that courts should not casually compel quick peek productions on non-consenting parties. In fact, quick peek productions may actually decrease efficiency and increase costs and expenses. In addition, quick peek productions threaten the basis and vitality of the attorney-client privilege. But this is not to say that courts should never compel parties to produce their documents in quick peek form.

Courts should reserve the option to compel quick peek productions as a sanction on parties that are found to egregiously violate their discovery obligations. The tobacco litigation in Minnesota, for instance, would have been a candidate for a compelled quick peek production on the defendants. Throughout the course of the litigation, the defendants repeatedly withheld highly relevant documents on improper claims of privilege.⁴⁴ While the eventual conclusion resulted in waiver of privilege for related documents, the extreme costs and delay associated with the extended special master review was unacceptable. Unfortunately, improper privilege designation and similar discovery abuses occur all too frequently in courts across the country. Court-compelled quick peek productions are one means to address this problem, short of the expense and delay associated with special masters and *in camera* review.

If parties are repeatedly refusing to produce relevant documents or grossly over-designating documents as privilege, then courts should find that those parties forfeited their right to review their documents and the court should require those parties to produce their files without a privilege review. Under these extreme circumstances, the court has authority to take extreme action, not only to manage its docket, but also to curb discovery abuses.⁴⁵ The party (or parties) that is required to produce documents through a quick peek manner, moreover, has little to complain about because the party had the opportunity to review its documents and it abused that privilege.

⁴² *The Sedona Principles: Best Practices Recommendations & Principles for Addressing Electronic Document Production*, Principle 6 (2d ed. June 2007).

⁴³ *See id.* at comment 6.c.

⁴⁴ *See Minnesota v. Philip Morris, Inc.*, No. C1-94-8565, 1998 WL 257214, at *7 (Minn. Dist. Ct. Mar. 7, 1998) (highlighting "the intentional and repeated misuse of claims of privilege").

⁴⁵ Districts courts may even dismiss a case in its entirety for egregious discovery violations. *See, e.g., National Hockey League v. Metropolitan Hockey Club, Inc.*, 427 U.S. 639, 642 (1976).

CONCLUSION

The concept of quick peek productions is not new. But the use of quick peek productions is. Now that quick peek productions are more viable in light of Rule 502, courts, attorneys, and parties will have to address a number of additional issues that will arise if quick peek productions are used. These issues will always present a fundamental tension of competing vital values. On the one hand, the burden and costs associated with twenty-first century “e-discovery” has the danger of excluding many parties from the civil justice system. In order to keep the courthouse’s doors open to all, there needs to a system that allows disputes to be decided on the merits and not precluded by exorbitant discovery costs. On the other hand, however, the attorney-client relationship is justified by confidentiality between lawyer and client. Any changes to our system that fractures the confidentiality of this relationship risk severe and dangerous long-term consequences. These issues, therefore, require thorough discussion and analysis in seeking the proper balance between controlling litigation costs and protecting the attorney-client privilege. Parties, nonetheless, should be able to discuss, analyze, and decide the proper balance for themselves. Courts that force quick peek productions—in addition to risking mandamus appeals and reversal—unfairly remove that decision from the parties.

THE PROTECTIVE ORDER TOOLKIT: PROTECTING PRIVILEGE WITH FEDERAL RULE OF EVIDENCE 502¹

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Introduction

In *The Associate*, bestselling novelist John Grisham describes a law firm document review room as a “long dungeon-like room with no windows, a concrete floor, poor lighting, and neat stacks of white cardboard boxes.”³ A senior associate informs the first year associates entering the room that, “someday in court, it will be crucial for our litigators to tell the judge that we have examined *every* document in this case.”⁴ In the days of paper discovery, such reaching declarations to the bench might have been possible, but in today’s computerized world of electronic discovery, such statements might seem outlandish, perhaps even unethical.⁵

When young staffers on Capitol Hill heard that The Judicial Conference was developing policies to reduce the efforts required to protect attorney-client privilege, there was a common sigh of relief. As former law firm associates, many legislative aides remembered the doldrums of document review. Gaining non-partisan support for Federal Rule of Evidence (FRE) 502 from this group was just the start.

This article summarizes the rules reform efforts of hundreds of attorneys, academics, jurists, policy leaders, legislative aides, think tank members, and legislators; many of whom are also members of The Sedona Conference®. Federal Rules policy reform would be impossible without the commitment of these participants. Thanks to their efforts we now have FRE 502, which “reaffirms and reinforces the attorney-client privilege and work product protection by clarifying how they are affected by, and withstand, inadvertent disclosure in discovery.”⁶

I have four main goals in writing this article:

1. To discuss the problem that FRE 502 sought to correct.
2. To correlate that problem to a real-life case in an historical narrative of FRE 502.
3. To provide an overview of the common law surrounding FRE 502.
4. To identify relevant considerations when drafting Protective Orders.

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3 John Grisham, *The Associate*, 152 (Doubleday) (2009).

4 *Id.*

5 A simple dispute can involve millions of electronic documents. The likelihood that a litigant can actually review *every* document decreases with increasing data volumes. A party signing such an implausible affirmation might face sanctions under Fed. R. Civ. P. 26(g). Similarly, a party making overbroad requests might also confront sanctions. See *Mancia v. Mayflower Textile Servs. Co.*, 253 F.R.D. 354 (D. Md. 2008). (“Rule 26(g) imposes an affirmative duty to engage in pretrial discovery in a responsible manner that is consistent with the spirit and purposes of Rules 26 through 37. In addition, Rule 26(g) is designed to curb discovery abuse by explicitly encouraging the imposition of sanctions. The subdivision provides a deterrent to both excessive discovery and evasion by imposing a certification requirement that obliges each attorney to stop and think about the legitimacy of a discovery request, a response thereto, or an objection”).

6 154 Cong. Rec. H7818 (Sept. 8, 2008) (remarks of Rep. Jackson-Lee).

If you take only one thing from this article, remember this: *The strongest privilege protections and waiver avoidance is granted to those who not only follow the guidance of FRE 502 but also mutually agree upon an adequately drafted Protective Order.*⁷ The two devices are not exclusive.

The Growing Problem of Privilege Review: Volume and Cost

The attorney-client privilege and work product protections act as vital organs to criminal and civil litigation in the United States. By protecting the confidentiality of communications between clients and their attorneys, our legal system encourages free-flowing, candid inquiry in the attorney-client relationship and protects documents prepared by attorneys to assist their clients in litigation.⁸

Prior to the advent of the personal computer, courts struck down blanket privilege protections and required litigants to zealously protect privileged communications by thoroughly reviewing and analyzing document collections prior to producing a final set to an opponent.⁹ Document review became the traditional hazing of first-year associates as they protected their client's claim of privilege by mind-numbingly pulling and logging privileged documents from a discreet production set of banker's boxes.¹⁰

However, as *The Sedona Conference® Best Practices Commentary on the Use of Search and Information Retrieval Methods in E-Discovery* theorizes, "traditional approaches to searching for relevant [or privileged] evidence are no longer practical or financially feasible" in today's electronic universe where we consider it more appropriate to send an e-mail, post a twitter, or click out a text message rather than make a phone call or (dare I say) meet in person.¹¹

We can blame technology for the data deluge. Cheap storage, web applications, and electronic mailboxes that can store a person's lifetime discourse all *Kindle* the fire endangering privilege protection.¹² However, it is not just data. The traditional pre-FRE 502 approach dictates that attorneys screen vast quantities of documents to guarantee that document collections in response to a discovery request do not include a privileged document for fear that a disclosure would waive the privilege for all documents on that subject matter.¹³ Fear of waiver forces clients to pay stratospheric litigation data management fees from vendors, steadily increasing hourly rates at law firms compound the problem.¹⁴

7 The Sedona Conference has undertaken a mission to promote collaboration between parties in discovery. See *The Sedona Conference® Cooperation Proclamation: The Sedona Conference® Working Group Series* (July 2008). Available at <http://www.thosedonacorporation.org/>. The Federal Rules of Civil Procedure also provide a vehicle for collaboration, see Rule 26(f).

8 The purpose of the attorney-client privilege is to encourage "full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and the administration of justice." *Upjohn Co. v. United States*, 449 U.S. 383, 389, 101 S. Ct. 677, 66 L. Ed. 2d 584 (1981).

9 "The party claiming that the privilege exists bears the burden of proving that it applies to the communication at issue." *Rhodes citing Sampson v. Sch. Dist. of Lancaster*, 2008 WL 4822023, at *3 (E.D. Pa. 2008) (citing *In re Grand Jury Empanelled Feb. 14, 1978*, 603 F.2d 469, 474 (3d Cir. 1979)). "Because it impedes full and free discovery of the truth, the attorney-client privilege is strictly construed." *Relion, Inc. v. Hydra Fuel Cell Corp.*, 2008 U.S. Dist. LEXIS 98400 (D. Or. Dec. 4, 2008) citing *Weil v. Investment Indicators, Research & Mgmt., Inc.*, 647 F.2d 18 (1980). (Interestingly, even after FRE 502 was signed into law, many courts recite privilege protection precedent from an era when secretaries used typewriters [i.e. computers were not a primary communications device]. Arguably, the common law will gradually move as parties fine-tune clawback agreements, Protective Orders, and exploit the benefits of FRE 502. The appendix of this commentary includes guidance that litigants can use to help protect privilege while saving costs).

10 See Fed. R. Civ. P. 26(b)(5)(B), (2009).

11 Jason Baron, et al., *The Sedona Conference® Best Practices Commentary on the Use of Search and Information Retrieval Methods in E-Discovery*. The Sedona Conference® Journal, 8 Sedona Conf. J. 189, (Fall, 2007). See also, Steve Lorb, *Is Information Overload a \$650 Billion Drag on the Economy?*, December 20, 2007, available at <http://bits.blogs.nytimes.com/2007/12/20/is-information-overload-a-650-billion-drag-on-the-economy/>. (Not only attorneys have trouble managing client data. The phenomenon of "e-mail bankruptcy" is another indicator that users are buried by the data avalanche).

12 The probability for missing a privileged document in a data set increases proportionally as data volumes increase. On March 8, 2009 Google's free "gmail" service permits a user to store up to 7.3 Gb free of charge. Google Terms of Service, <http://www.google.com/accounts/TOS?hl=en>. *The Sedona Conference® Best Practices Commentary on the Use of Search and Information Retrieval Methods in E-Discovery* (August 2007) n.2. ("One gigabyte of electronic information can generate approximately 70,000-80,000 of text pages, or 35 to 40 banker's boxes of documents"). Coincidentally, the "Kindle" is a portable electronic book reader, for a description of the device see Amazon Kindle - Wikipedia, http://en.wikipedia.org/wiki/Amazon_Kindle.

13 Baron at 199, n. 13. ("Compare \$1 to store a gigabyte of data with \$32,000 to review it (i.e., assuming one gigabyte equals 80,000 pages, and assuming that an associate billing \$200 per hour can review 50 documents per hour at 10 pages in length, such a review would take 160 hours at \$200/hr, or approximately \$32,000).") For a discussion on subject matter waiver, see Ashish Prasad and Vazantha Meyers "The Practical Implications of Proposed Rule 502." *The Sedona Conference Journal*, 8 Sedona Conf. J. 133, (Fall 2007).

14 Although thwarted by the recent economic downturn, history indicates most law firms have increased their rates year-over-year. See Sandhya J. Bathija, *Law Firms' Rates Edge Up Again: Firms are steadily increasing hourly billing rates across the board*, The National Law Journal, December 11, 2006, <http://www.law.com/jsp/article.jsp?id=1165582605881>. (stating perpetual increases) *Distinguished* from Kathy Robertson, "Usual increase in law firm billing rates not happening this year." San Francisco Business Journal Friday, January 23, 2009 (citing a poor economy that affects firms' ability to increase fees) <http://sanfrancisco.bizjournals.com/sacramento/stories/2009/01/26/focus2.html>.

In short, privilege protection, a fundamental building block of our legal system, is in danger because the cost of protecting it is becoming too great. The increasing expense of privilege review stems from both growing data volumes and escalating attorney fees. As our litigation process becomes more electronic, policy leaders must adapt antiquated rules to address new concerns.

Rulemaking History: Advisory Committee on the Federal Rules of Evidence

On April 24, 2006, The United States Judiciary Advisory Committee on the Federal Rules of Evidence held a mini-conference inviting a broad-based coalition of judges, academics, and practitioners to discuss the state of privilege protection in litigation and the need for rules reform.¹⁵ After the hearings, the committee approved the proposed new Rule 502 for publication to the general public and scheduled two hearing dates where the committee would consider public testimony.

On January 29, 2007, Anne Kershaw and I joined 22 other speakers in courtroom 24A at 500 Pearl Street in New York to testify before The Advisory Committee about the benefits of Proposed Federal Rule of Evidence 502.¹⁶ We sought to persuade the Advisory Committee to approve the expansion of privilege protection for all parties in litigation and regulatory filings by providing hard data about the true cost of protecting privilege for a single matter.

In the Kershaw-Oot testimony, we described the laborious and tedious process of multi-tier document review that litigants wade-through in an effort to locate relevant documents and to prevent privileged information from disclosure. We stated that both plaintiffs and defendants (like Verizon) use this expensive and time-consuming process in hopes to avoid the (pre-FRE 502) perils that occur when a party inadvertently produces a privileged document. Most importantly, we informed the advisory committee on the true cost of responding to document requests and protecting privilege for a single real-life matter.¹⁷ Verizon spent over \$13.5 million reviewing and logging documents for relevancy and privilege in a single matter.¹⁸

The “gold-standard” of attorney document analysis does not necessarily amount to a high level of precision when attempting to protect privilege or even review for relevancy.¹⁹ For example, in the *Blair and Maron* study, attorneys over-estimated their ability to create and develop queries to assess the relevancy of 40,000 documents relevant to a transit accident.²⁰ “Lawyers estimated that their refined search methodology would find 75% of relevant documents, when in fact the research showed only 20% or so had been found.”²¹ Additionally, anyone conducting a simple keyword search of the Enron data can find privileged e-mails that attorneys should have withheld from the production.²²

Not only is manual document review the least efficient method to search for data, it may provide inferior results compared to other available methods.²³ In the preliminary results of its premier study, *The Electronic Discovery Institute* announced that two computer-assisted document review systems had a higher rate of agreement with an original three tier manual attorney review than a second manual attorney review of the same data set.²⁴ Moreover, the study also concluded that the two

15 The materials for the April 24, 2006 meeting can be found at http://www.uscourts.gov/rules/Agenda_Books.htm The Sedona Conference® Advisory Board was represented at the meeting by several members and observers.

16 Anne Kershaw is an attorney, expert, scholar on electronic discovery and processes. See <http://www.akershaw.com>.

17 For a transcript of the testimony, see <http://www.uscourts.gov/rules/2007-01-29-Evidence-Minutes-Transcript.pdf>. For a copy of the PowerPoint presentation presented to the Rules Committee, see http://ediscoveryinstitute.org/pubs/The_Real_Cost_of_Privilege_05.pdf. The 2005 matter discussed at the hearing required Verizon to collect both electronic and paper documents from 83 employees in ten states. The extracted data set hosted on the e-discovery vendor's servers equaled 1.3 terabytes and yielded 2.4 million documents.

18 See Gartner RAS Core Research Note G00148170, *Cost of eDiscovery Threatens to Skew Justice System*, 1D# G00148170, (April 20, 2007), at http://www.akershaw.com/Documents/cost_of_e_discovery_threatens_148170.pdf. (Coincidentally, this 2005 statistic is often cited as one of the few data-points available regarding the cost of document review in complex litigation and regulatory filings in the United States). See also Adreas Kluth, *The Big Data Dump*, *The Economist*, August 28, 2008, at http://www.economist.com/business/displaystory.cfm?story_id=12010377. See also, Daniel Fisher, “The Data Explosion,” *Forbes*, October 1, 2007 at <http://www.forbes.com/forbes/2007/1001/072.html>.

19 For a full, well informed discussion about problems with assessing large data volumes for litigation see Baron, *Supra*.

20 David C. Blair and M.E. Maron, *An Evaluation of Retrieval Effectiveness for a Full-Text Document-Retrieval System*, *Communications of the ACM*, Volume 28 Number 3, p. 289 (March 1985).

21 For a discussion of the Blair and Maron study, see Baron, *Supra* at 206.

22 See *Enron Broadband Servs., L.P. v. Travelers Cas. & Sur. Co. of Am. (In re Enron Corp.)*, 349 B.R. 115, 125 (Bankr. S.D.N.Y. 2006). (Although litigants waived attorney-client privilege on those documents in furtherance of fraud, attorneys should have withheld other non-fraudulent attorney-client communications). A searchable database of produced documents in the Enron matter are available at <http://www.enronexplorer.com>.

23 For more information on the analysis of data retrieval systems see The National Institute of Standards and Technology TREC Legal Track (TREC) at <http://trec-legal.umiacs.umd.edu/>.

24 See *Electronic Discovery Institute Study: Effectiveness of Document Review and Analysis Systems for Litigation and Regulatory Response*. (Preliminary Study Results at http://ediscoveryinstitute.org/pubs/EDI__LegalTech_2008.pdf).

computer-assisted methods could have completed the project in one-third of the time at a savings on cost of over 60%.²⁵ It's not difficult to conclude that computers can replicate query instructions on large data sets more succinctly than fatigued contract attorneys and associates staring at computer monitor for twelve hours per day.

The second half of the Kershaw-Oot testimony discussed alternate less-expensive techniques to protect privilege that would be possible if FRE 502 was enacted. We presented an example of how a litigant could “bucket” or “set-aside” documents that contain law-firm domain names and documents that advanced search engines can flag as potentially privileged.²⁶ If a producing party had a multi-jurisdictionally enforceable Protective Order under FRE 502 with a claw-back, that party could feel more comfortable rapidly producing or even providing an initial quick-peek to the remaining corpus of data. The parties could also exchange electronically exported logs of the “potentially privileged” withheld bucket. Subsequently, the requesting party could develop better targeted search methods and requests for the set-aside data sets. Allowing litigants to conduct a real initial investigation furthers both a better understanding of the case and the goals of Federal Civil Procedure Rule 1.²⁷

Rulemaking History: Advisory Committee Report

After the public hearings, the Advisory Committee issued a *Report of the Advisory Committee of Evidence Rules* on May 15, 2007 modifying the previously published proposed rule.²⁸ The report dropped the selective waiver provision, stretched the jurisdiction of the rule (and Protective Orders) to state forums (for disclosures made in federal court) and productions to federal agencies, almost eliminated subject-matter waiver, and instituted guidelines of reasonableness to avoid waiver for inadvertent disclosure.²⁹

The report cited precedent that “set out multi-factor tests for determining whether the inadvertent disclosure is a waiver.”³⁰ Although the report did not codify the inquiry, it included a pentad test drawn from the case law. In determining whether waiver applies for inadvertent disclosures, courts should consider:

1. The reasonableness of the precautions taken;
2. The time taken to rectify the error;
3. The scope of discovery;
4. The extent of discovery; and
5. The over-riding issue of fairness.³¹

The Advisory Committee also provided guidance to courts with additional considerations when interpreting the *reasonableness of the precautions taken*. Interestingly, the additional considerations refresh twenty-year-old waiver tests with elements contemplating the massive data volumes litigants face when managing discovery. The reasonableness considerations include:

1. The number of documents to be reviewed;
2. The time constraints for production;
3. The use of software applications and linguistic tools in screening for privilege; or
4. The implementation of an efficient records management system before litigation.³²

²⁵ *Id.*
²⁶ <http://www.uscourts.gov/rules/2007-01-29-Evidence-Minutes-Transcript.pdf>.

²⁷ F.R.C.P. 1.

²⁸ See *Report of the Advisory Committee on Evidence Rules* at http://www.uscourts.gov/rules/Reports/2007-05-Committee_Report-Evidence.pdf.

²⁹ *Id.*

³⁰ *Id.* citing *Lois Sportswear, U.S.A., Inc. v. Levi Strauss & Co.*, 104 F.R.D. 103, 105 (S.D.N.Y. 1985) and *Hartford Fire Ins. Co. v. Garvey*, 109 F.R.D. 323, 332 (N.D.Cal. 1985).

³¹ *Id.*

³² *Id.*

Finally, the committee expressly stated that FRE 502 does not require a post production review, but litigants should follow up on any obvious indications of inadvertent production.³³

Rulemaking History: “I’m Just a Bill”

Both The Committee on Rules of Practice and Procedure and The Judicial Conference approved the proposed rule for transmittal to Congress.³⁴ On September 26 2007, Hon. Lee Rosenthal, Chair of The United States Judicial Conference transmitted the resulting proposed FRE 502; developed from over 70 public comments, the testimony of over 20 witnesses, the views of the Subcommittee on Style, and the Advisory Committee’s own judgement.³⁵ The transmittal letter also included a proposed Committee Note that the Judicial Conference sought to include in the legislative history of FRE 502.³⁶

Senator Leahy introduced the proposed rule in the Senate on December 11, 2007. On January 31, 2008, the Senate Judiciary Committee approved the bill unanimously without amendment and published its findings to the full Senate with a written report.³⁷ After incorporating the Advisory Committee Notes, the bill passed in the Senate on February 27, 2008 and The House of Representatives on September 8, 2008. The bill was enacted as Public Law 110-322 on September 18, 2008 to amend the Federal Rules of Evidence to address the waiver of the attorney-client privilege and the work product doctrine.³⁸

FRE 502: At a Glance

The Appendix of this Article contains an official version of Federal Rule of Evidence 502. The table below summarizes its contents:

Federal Rule	Description
502(a)	Limits subject matter waiver of undisclosed documents to instances of intentional disclosure where similar subject communications ought [in fairness] to be considered together.
502(b)	Mandates non-waiver for unintentionally disclosed documents when reasonable steps were taken to prevent disclosure and the producing party took reasonable steps to correct the error.
502(c)	Limits the instances when a litigant can carry a disclosure in a state court proceeding to a federal proceeding.
502(d)	Prescribes the use of Protective Orders and mandates court ordered non-waiver for any other federal or state proceeding.
502(e)	Prescribes the use of Protective Orders by suggesting that confidentiality agreements only bind the parties to the agreement, unless it is incorporated into a court order.
502(f)	Binds state courts to a federal court’s determination of non-waiver.
502(g)	Defines attorney-client privilege and attorney work product.

³³ *Id.*
³⁴ Because the draft rule involved an evidentiary privilege, congressional action was required before the rule could be adopted. See 28 U.S.C. Section 2074(b) (“Any such rule creating, abolishing, or modifying an evidentiary privilege shall have no force or effect unless approved by Act of Congress.”).
³⁵ Letter from Hon. Lee H. Rosenthal to Hon. Patrick Leahy, Hon. Arlen Specter, Hon. John Conyers, Jr., and Hon. Lamar Smith, transmitting Proposed New Federal Rule of Evidence 502 to Judiciary Committee, (September 26, 2007).
³⁶ *Id.*
³⁷ S. Rep. No.110-264, (February 25, 2008) (“The rule proposed by the Standing Committee is aimed at adapting to the new realities that accompany today’s modes of communication, and reducing the burdens associated with the conduct of diligent electronic discovery.”).
³⁸ See 154 Cong. Rec. S1317 (Feb. 27, 2008) (remarks of Sen. Leahy) (“I ask unanimous consent to have printed in the Record the Judicial Conference’s Committee Note to illuminate the purpose of the new Federal Rule of Evidence and how it should be applied.”); 154 Cong. Rec. H7818 (Sept. 8, 2008) (remarks of Rep. Jackson- Lee) (“In order to more fully explain how the new rule is to be interpreted and applied, the Advisory Committee also prepared an explanatory note, as is customary, for publication alongside the text of the rule. The text of the explanatory note appears in the Record in the Senate debate.”). Administration of George W. Bush, Acts Approved by the President, 1234 (2008).

In short, FRE 502 creates a national standard governing the effect of inadvertent disclosures on the attorney-client privilege.

FRE 502: The Cases

Coincidentally, judicial interpretations of FRE 502's reasonableness standards have stirred significant response from the legal community.³⁹ Citing recent decisions, critics of FRE 502 argue that the rule provides little solace to the burden of mounting privilege review costs. However, naysayers forget that the true benefit of FRE 502 derives from the portability of non-waiver rights that a party maintains through a Protective Order. FRE 502 orders grant litigants the ability to better cooperate on the terms of discovery and pave the path for parties to create solid terms to prevent waiver from inadvertent disclosure. A litigant is in the best position if he maps out a response plan to inadvertent disclosures in a fully-vetted Protective Order before documents even change hands.⁴⁰ Courts have already ordered litigants to collaborate with one another to address the problematic costs of a privilege review using FRE 502.⁴¹

Unfortunately, most of the litigants involved in current FRE 502 rulings failed to seek court sanctioned protection early in the discovery process. Thus, the cases to-date rely on disparate interpretations of reasonableness. Below is a sample of the case law invoking FRE 502:

Cases Where Courts Protected the Privilege of Inadvertently Disclosed Privileged Communication

Alcon Mfg. v. Apotex, Inc.

Some courts have set a reasonable standard for protecting privilege by using FRE 502 to empower Protective Orders to find non-waiver. For example, in a patent dispute before the U.S. District Court for the Southern District of Indiana, the court found non-waiver when the plaintiff inadvertently disclosed a privileged document electronically and later complied with the Protective Order by making a good-faith representation that the disclosure was inadvertent and by taking prompt remedial action when they discovered the disclosure.⁴² Judge Baker paralleled his ruling of non-waiver to the purpose statement of the FRE 502 Advisory Committee Note.⁴³ He concluded, "perhaps the situation at hand could have been avoided had plaintiffs' counsel meticulously double or triple-checked all disclosures against the privilege log prior to any disclosures. However, this type of expensive, painstaking review is precisely what new Evidence Rule 502 and the Protective Order in this case were designed to avoid."

Rhoads Industries, Inc. v. Building Materials Corp.

Other courts tend to rule in favor of protecting privilege under FRE 502 by heavily weighing common law factors after completing a FRE 502 analysis. For instance, in *Rhoads Industries, Inc. v. Building Materials Corp.*, plaintiff (Rhodes) produced over 800 privileged documents and asserted that the production was inadvertent.⁴⁴ Although Judge Baylson ruled in favor of waiver for 120 inadvertently produced privileged documents that plaintiff neglected to timely log under FRCP 26(b)(5), the court resisted a ruling of waiver for the inadvertently produced documents that plaintiff included on a privilege log.⁴⁵ In his ruling, Judge Baylson applied FRE 502 in conjunction with a

39 Leonard Deutchman, *First Take on Federal Rule of Evidence 502*, Pennsylvania Law Weekly (December 11, 2008).

40 Model Protective Order language is available in the Appendix of this article.

41 *Spieker v. Quest Cherokee, LLC*, 2008 U.S. Dist. LEXIS 88103 at 13 (D. Kan. Oct. 30, 2008) (Magistrate Judge Humphreys recently addressed both collaboration and FRE 502 in *Spieker v. Quest Cherokee*. The court ruled, "Defendant estimates that a "privilege and relevance" review by counsel will cost approximately \$ 250,000. However, Federal Rule of Evidence 502 was recently enacted to reduce the costs of exhaustive privilege reviews of ESI. The parties need to address Rule 502 in any future production and cost discussions.")

42 *Alcon Mfg. v. Apotex, Inc.*, 2008 U.S. Dist. LEXIS 96630 (S.D. Ind. Nov. 26, 2008).

43 "Concluding otherwise would undermine one of the main purposes of new Evidence Rule 502, which codifies the primary purpose of the provisions ... of the Protective Order in this case: to address the "widespread complaint that litigation costs necessary to protect against waiver of attorney-client privilege or work product have become prohibitive due to the concern that any disclosure (however innocent or minimal) will operate as a subject matter waiver of all protected communications or information" which is "especially troubling in electronic discovery." *Id.* at 18 citing Fed. R. Evid. 502 Advisory Committee's note.

44 *Rhoads Industries, Inc. v. Building Materials Corp.*, 254 F.R.D. 216 (E.D. Pa. 2008).

45 Fed. R. Civ. P. 26(b)(5) requires the logging of documents withheld for privilege. Plaintiff first received notice of its 5/13/2008 inadvertent disclosure from Defendant on 6/5/2008. Plaintiff did not submit its final privilege log until 11/12/2008, some 6 months after initial notice. The court called Rhodes' failure to submit a complete privilege log by 6/30/2008 "too long and inexcusable." Judge Baylson cited two cases that might define a reasonable time period to provide an amended privilege log. A court will likely find a two month delay untimely, whereas a court may determine a response of less than a month is prompt. See *Rhodes*, 8-9, comparing *Get-A-Grip, II, Inc. v. Hornell Brewing Co., Inc.*, 2000 WL 1201385 (E.D. Pa. 2000) to *In re Total Containment, Inc.*, 2007 WL 1775364, at *8 (Bankr. E.D. Pa. 2007).

multi-part test detailed in *Fidelity & Deposit Co. of Md. v. McCulloch*.⁴⁶ Under the five-part *Fidelity* test, Judge Baylson ruled that although four of *Fidelity* factors favored waiver, the final factor, “Whether the overriding interests of justice would or would not be served by relieving the party of its errors,” should be heavily weighted to favor *Rhodes*.⁴⁷ The court ruled against waiver concluding, “loss of the attorney-client privilege in a high-stakes, hard-fought litigation is a severe sanction and can lead to serious prejudice.”⁴⁸

Of equal importance to those seeking to protect privilege, twelve days after the court’s ruling of non-waiver of privilege for logged documents under FRE 502, plaintiff sought clarification from the court on how it should qualify *e-mail strings*⁴⁹ to determine if the communication appeared on a privilege log prior to June 30.⁵⁰ The court ruled that each privileged message within the string must be separately logged in order to claim privilege; a litigant could not merely log the top tier (most recent) message and expect privilege protection for the entire string.⁵¹ However, the plaintiff was not required to indicate that the e-mail was part of a string, as this disclosure could form a “breach of attorney-client privilege because the act of itemization might force parties, by disclosing what was sent to the attorney, also to disclose the nature of the privileged information.”⁵² The court supported its ruling with precedent on privilege logging methodology.⁵³ However, parties seeking the protection of FRE 502 should consider an alternate approach.

The drafters of FRE 502 sought to reduce the costs of litigation by reducing the burden on litigants to protect privilege. Judge Baylson’s ruling on e-mail strings is important to the FRE 502 discussion for several reasons. Privilege review is expensive.⁵⁴ Similarly, accounting for privilege by manually logging individual parts of a string is a core component of the *Rhodes* privilege review methodology.⁵⁵ Privilege logging is expensive and time consuming because logging individual parts of e-mail strings is programmatically difficult and often technically impossible to provide an accurate representation of who actually received a lower part of the e-mail string.⁵⁶

As a solution to the logging dilemma, parties could collaborate and negotiate for a jointly favorable production and logging methodology in a court approved Protective Order.⁵⁷ Under FRE 502, the parties may enforce the Protective Order in federal and state court; thereby avoiding waiver and protecting privilege if the parties followed an agreed upon logging methodology.⁵⁸ For example, if the parties agree to a Protective Order using the bucketing and logging methodology outlined in the previously discussed Kershaw-Oot testimony (perhaps agreeing to top-tier logging), the parties could avoid significant expense, share data with greater speed, all while protecting privilege. In the end, *Rhodes* could have shielded against mistakes with a fully vetted Protective Order.

46 *Rhodes supra* citing *Fidelity & Deposit Co. of Md. v. McCulloch*, 168 F.R.D. 516 (E.D. Pa. 1996). (The *Fidelity* test is substantially similar to the test that appeared in the Federal Rules of Evidence Advisory Committee Note).

47 *Rhodes supra* note 44, at 10.

48 *Rhodes supra* note 44, at 10.

49 An e-mail string is “a series of e-mails linked together by e-mail responses or forwards. The series of e-mail messages created through multiple responses and answers to an originating message. Also referred to as an e-mail thread. Comments, revisions, and attachments are all part of an e-mail string.” *The Sedona Conference® Glossary: E-Discovery & Digital Information Management* 2d ed., available at <http://www.sedonaconference.org>.

50 *Rhodes Industries, Inc. v. Building Materials Corp.* (Memorandum Re: Clarification of Memorandum Dated November 14, 2008 RE: Privilege Logs of Emails) (November 26, 2008) (As a sanction for failure to timely log documents [as ordered] for six months, the court ordered plaintiff to produce any privileged document not logged prior to June 30, 2008). Fed. R. Civ. P. 26(b)(5) requires a withholding party to log documents withheld for privilege.

51 *Rhodes Industries, Inc. v. Building Materials Corp.* (Memorandum Re: Clarification of Memorandum Dated November 14, 2008 RE: Privilege Logs of Emails) (November 26, 2008).

52 *Id.* citing generally Paul R. Rice, Attorney Client Privilege in the United States Section 11:6.1 (2d ed. 2008) (providing a general discussion of this issue and citing cases).

53 *Muro v. Target Corp.*, 250 F.R.D. 350 (N.D. Ill. 2007).

54 See n. 24 and Kershaw-Oot testimony *supra*.

55 Fed. R. Civ. P. 26(b)(5). In *Rhodes*, the court found waiver where the producing party failed to log individual parts of an e-mail string. See *Rhodes* (November 26, 2008) *supra*.

56 Logging older messages in a string is difficult. Many e-mail clients (such as RIM’s pervasive Blackberry Enterprise Server) convert parsed data fields (to, from, cc, bcc, etc.) to ASCII text. This conversion of structured data to unstructured text causes the inability to programmatically capture metadata fields for all but the top-tier, most recent message. For instance, when a user forwards an e-mail, the e-mail client converts fielded metadata to ASCII text. The forwarded message will not programmatically capture the metadata from lower-tier messages metadata and will lose the “bcc” field from sent messages that are later forwarded. Another example of this problematic conversion is how fielded names and e-mail addresses change to ASCII aliases in lower-tier older messages. For example, “john.smith@legal.company.com” might convert to merely “John Smith” in the ASCII string. Determining the identity of authors in lower-tier older parts of a string is difficult for litigants analyzing e-mail collections at large companies that have more than one employee with the same name.

57 See Sedona Collaboration Proclamation, *Supra*.

58 In *Rhodes*, Judge Baylson did not preclude alternate court ordered logging options stating, “I have some hesitation in adopting a broad, black-letter rule.” *Rhodes* (November 26, 2008), *supra* at 6.

Koch Foods of Alabama, LLC v. General Electric Capital Corp.

Courts confronting the issue of inadvertent disclosure for the first time or with little state law guidance tend to adopt the balancing test when assessing waiver. For example, in the poultry equipment ownership dispute *Koch Foods of Alabama, LLC v. General Electric Capital Corp.*, District Court Judge Thompson upheld an order of non-waiver that applied the 5-factor test.⁵⁹ The court ruled that “if the Alabama Supreme Court were to confront the issue of inadvertent waiver, it would likely adopt the more comprehensive and sensitive totality-of-the-circumstances analysis. . . . But, more importantly, the totality-of-the-circumstances approach allows for a more comprehensive and sensitive assessment of the often complex and sensitive concerns presented in inadvertent waivers.”⁶⁰ Judge Thompson’s ruling upheld the magistrate judge’s order of non-waiver where a privileged e-mail was found tucked in middle of 37-page lease agreement contained in a 3,758 page production, the document was included in Koch’s privilege log, and Koch immediately objected and asserted privilege when document presented at deposition of its CFO.⁶¹

Laethem Equip. Co. v. Deere & Co.

Courts may also find non-waiver through a strict FRE 502(b) examination without turning to a five-factor federal common law analysis. In *Laethem Equip. Co. v. Deere & Co.*, the U.S. District Court for the Eastern District of Michigan found non-waiver when plaintiff inadvertently produced two “M&M” disks to defendant that contained privileged attorney-client communication. As neither party argued that the disclosure was anything but inadvertent, the court turned to the additional factors of FRE 502(b) that “sets forth explicit factors for the court to consider” in its analysis.⁶²

The court found that plaintiff took reasonable precautions to protect its privilege due to the relatively small inadvertent disclosure in relation to the voluminous discovery produced.⁶³ Further, “the materials were copied by defense counsel outside of the “inspect and copy” procedure established by the parties, which would have given counsel for plaintiffs the opportunity to conduct a privilege review of the data on the disks prior to turning that data over to defendants.”⁶⁴ Finally, the court determined that plaintiff promptly took reasonable steps to rectify the error, as plaintiff’s counsel objected to Defendant’s use of the disclosed materials and demanded their return on multiple occasions in writing starting on the very first day of their disclosure while obtaining an order for their return three weeks after initial knowledge of the inadvertent disclosure.⁶⁵ Accordingly, the court found reasonable precautions were taken under FRE 502(b) and ruled that plaintiff did not waive its privilege.

Heriot v. Byrne

Courts have also considered vendor error when weighing the factors of an inadvertent disclosure. In the copyright dispute *Heriot v. Byrne*, defendant sought sequestered documents that had been inadvertently produced as a result of a vendor mistake.⁶⁶ Defendant argued that plaintiffs’ counsel was “asleep at the switch” by not re-examining the documents received from the vendor.⁶⁷ The court ruled against waiver stating that FRE 502, “does not require the producing party to engage in a post-production review to determine whether any protected communication or information has been produced by mistake.”⁶⁸ In its analysis, the court further ruled that the disclosing party undertook reasonable precautions to protect privilege when that party enlisted non-lawyers to manually “review the documents prior to production, assigned them codes, and provided them to the Vendor to properly disclose.”⁶⁹ In addition, Judge Ashman ruled that plaintiff’s counsel

⁵⁹ *Koch Foods of Alabama, LLC v. General Electric Capital Corp.*, 2008 U.S. Dist. LEXIS 3738 (M.D. Ala. Jan. 17, 2008).

⁶⁰ *Id.* at 18.

⁶¹ *Id.*

⁶² *Laethem Equip. Co. v. Deere & Co.*, 2008 U.S. Dist. LEXIS 107635 at 107728 (E.D. Mich. Nov. 21, 2008).

⁶³ *Id.* at 28.

⁶⁴ *Id.*

⁶⁵ *Id.* at 29.

⁶⁶ *Heriot v. Byrne*, 2009 U.S. Dist. LEXIS 22552 (N.D. Ill. Mar. 20, 2009).

⁶⁷ *Id.* at 38.

⁶⁸ *Id.* (“Plaintiffs had no duty to re-review the documents after providing them to the Vendor. That would be duplicative, wasteful, and against the spirit of FRE 502. Additionally, imposing on disclosing parties a duty to re-review would chill the use of e-vendors, which parties commonly employ to comply with onerous electronic discovery. Against this grain the Court cannot cut.”).

⁶⁹ *Id.* at 43.

took prompt steps to rectify the error when plaintiff's counsel notified defendant's counsel within twenty-four hours of noticing the error and demanded that the defendants destroy those documents; all prior to depositions.⁷⁰ Finally, after an *in camera* review, the court reserved its ruling on privilege protection pending a resubmission of the privileged documents and privilege log because defendant's submission was a "befuddling assemblage of documents."⁷¹ The court ordered the defendants to submit an amended privilege log and a revised compilation of documents after they are organized chronologically.⁷²

Preferred Care Partners Holding Corp. v. Humana, Inc.

Other courts have ruled against waiver for inadvertent disclosure, abandoning a multi-part case law analysis in favor of the direct statutory FRE 502(b) analysis by simply ruling that the two tests are substantially similar; finding non-waiver even when a party failed to meet its discovery obligations pursuant to a scheduling order.⁷³ In the breach of confidentiality dispute *Preferred Care Partners Holding Corp. v. Humana, Inc.*, Magistrate Judge Simonton conducted an *in camera* review and concluded that four inadvertently produced documents did not constitute waiver.⁷⁴ Again, the court found Humana took reasonable precautions to protect its privilege because some of the emails contained a header "**PRIVILEGED ATTORNEY/CLIENT COMMUNICATION**" and Humana's counsel undertook approximately thirty-three hours of privilege review over a three day period.⁷⁵ Interestingly, the court conducted a FRE 502(b) analysis, avoiding the common law "overriding interests of justice" test.⁷⁶ In doing so, the court evaded an analysis of Humana's sluggish discovery conduct in the case; a factor that might have caused Judge Simonton to order waiver because other courts have weighed the overriding interests of justice heavily.⁷⁷ Even so, those courts seem to use this test to rule against waiver of privilege.⁷⁸

Am. Coal Sales Co. v. N.S. Power Inc.

Other courts have also ruled in favor of protecting privilege by comparing common law to FRE 502 analysis. For example, in a breach of contract case before the U.S. District Court for the Southern District of Ohio, *Am. Coal Sales Co. v. N.S. Power Inc.*, Defendant included in its Reply in Support of its Motion for Summary Judgment, an e-mail from plaintiff's employee to its in-house attorney.⁷⁹ Plaintiff states that the e-mail was a privileged attorney-client communication that was inadvertently disclosed, and plaintiffs sought to strike the e-mail from the record and to enter a Protective Order. Magistrate Judge Able applied the *Nilavar* test and ruled that plaintiff "took reasonable precautions to avoid inadvertent disclosures by having two attorneys review documents prior to production; that inadvertent production of one document out of over 2,000 documents produced does not weigh in favor of waiver; that the extent of the waiver was not great because the document had not worked its way into the fabric of the litigation; that plaintiff took prompt measures to rectify the disclosure; and that the overriding interests of justice and fairness did not conclusively counsel in favor of waiver."⁸⁰ The district court ruled that even though Magistrate Judge Abel should have applied FRE 502, his application of the *Nilavar* test was not contrary to law as the *Nilavar* factors were similar to those identified in FRE 502(b) and Advisory Committee Note.⁸¹

⁷⁰ *Id.* at 46.

⁷¹ *Id.* at 66.

⁷² *Id.* (Many of the documents contain multiple e-mails and forwarded e-mails, an incestuous intermingling of privileged and unprivileged documents. Some of these e-mails are entirely unprotected and can nowise be claimed as covered by the attorney-client privilege").

⁷³ *Preferred Care Partners Holding Corp. v. Humana, Inc.*, Case No. 08-20424-CIV, "Order Regarding Documents for In Camera Review" (S.D. Fla., April 9, 2009) ("The undersigned...concludes that it is both just and practicable to apply Rule 502 to the case at bar, because PCP does not object to the application of Rule 502 and because there is no substantive difference between the two standards in light of the facts presented in this particular case") (On January 16, 2009, Humana produced 10,000 pages of documents, approximately two months after the expiration of the discovery deadline).

⁷⁴ *Id.* (Although the court found non-waiver of four documents, the court ruled that Humana voluntarily waived privilege on one document, as "Humana acknowledged at the April 3, 2009 hearing, it volunteered the details of its so-called "purr and purge scheme" in light of the fact that it forms a central component of its defense to PCP's motion for sanctions; and, those details are now a matter of public record").

⁷⁵ *Preferred Care Partners*, at 8-9.

⁷⁶ *Preferred Care Partners*, at 7 ("Although the final element of the relevant circumstances test – whether the overriding interests of justice would be served by relieving a party of its error – is not incorporated into the Rule 502 test, the undersigned concludes that the application of this aspect of the test to the circumstances in the case at bar would not alter the result").

⁷⁷ See *Rhodes, supra*.

⁷⁸ *Id.*

⁷⁹ *Am. Coal Sales Co. v. N.S. Power Inc.*, 2009 U.S. Dist. LEXIS 13550 (S.D. Ohio February 23, 2009).

⁸⁰ *Id.* at 6-47.

⁸¹ See Advisory Committee Note, *supra*.

Reckley v. City of Springfield

Courts have ruled liberally when determining if reasonable precautions to protect privilege were taken by a disclosing party under FRE 502. For example, in *Reckley v. City of Springfield*, Defendant City of Springfield inadvertently produced five e-mails to plaintiff.⁸² Plaintiff's counsel later presented the disclosed documents during deposition and sought to question plaintiff's former supervisor using the disclosed documents. Judge Merz cited FRE 502(b) and ruled that plaintiff took reasonable steps to prevent disclosure because, "at least some of the e-mails in Exhibit 49 have ATTORNEY-CLIENT PRIVILEGED endorsed on them and Defendants' counsel took prompt steps to claim the privilege and seek return of the e-mails after they were disclosed."⁸³ The Court concluded that the e-mails "retain[ed] their privileged status and plaintiff must deal with them as provided in Fed. R. Civ. P. 26(b)(5)."⁸⁴

Kumar v. Hilton Hotels Corp.

Courts have continued to rule liberally against waiver when applying the multi-part test identified in the Explanatory Note of FRE 502(b); even finding non-waiver by interpreting the intent of the producing party's counsel when determining if that party undertook reasonable precautions to protect the privileged material. In the employment discrimination case, *Kumar v. Hilton Hotels Corp.*, Magistrate Judge Pham ruled against waiver of sixty-one inadvertently produced documents where the e-mails were marked "Attorney/Client Privileged Information" and Hilton's counsel attached a note instructing a legal assistant to redact some of the e-mails at issue.⁸⁵ Once more, the court weighed counsel's intent to redact and the mere marking of the documents heavily when determining if reasonable precautions were undertaken. The court also ruled that "Hilton promptly took steps to rectify the error and mitigate the damage of the disclosures, as Hilton's counsel immediately contacted Kumar's counsel to notify him of the inadvertent disclosure and to attempt to retrieve the documents. Hilton also took immediate steps to notify the court of this claim by filing the emergency motion. Finally, the number and magnitude of the disclosures in light of the overall document production weigh against waiver."⁸⁶

Cases Where Courts Ruled in Favor of Waiver for Inadvertently Disclosed Privileged Communication

Sitterson v. Evergreen Sch. Dist. No. 114

Yet, courts require a disclosing party to at least take *some* reasonable precautions to protect its privilege. In *Sitterson v. Evergreen Sch. Dist. No. 114*, an appeal from a trial court decision over waiver of documents in an underlying contract dispute, the Court of Appeals of Washington found waiver after invoking FRE 502 to conduct the pervasive "balanced" common law analysis.⁸⁷ As neither party argued that the waiver was advertent, the *Sitterson* court moved on to balance five *Alldread* factors to decide if the disclosing Defendant waived its privilege on four advisory letters between the District and its attorney.⁸⁸ Using the five factored precedent, the court ruled that defendant waived its privilege. First, counsel for the disclosing party "offered no evidence of any precautions he or his office took to prevent the disclosures."⁸⁹ Second, the panel was troubled by the "disclosing party's failure to notice or remedy the error until three years after it was made."⁹⁰ Third, the court found such a small document production of 439 documents manageable and not the enormous quantity of documents

⁸² *Reckley v. City of Springfield*, 2008 U.S. Dist. LEXIS 103663 (S.D. Ohio Dec. 12, 2008).

⁸³ *Id.*

⁸⁴ *Id.*

⁸⁵ *Kumar v. Hilton Hotels Corp.*, 2009 U.S. Dist. LEXIS 53387, 9-10 (W.D. Tenn. June 16, 2009). (Magistrate Judge Pham concluded, "the disclosure was inadvertent, as it is clear Hilton intended to redact these portions of the documents prior to production. Hilton took reasonable steps to prevent disclosure, as evidenced by the fact that the Barkley email begins with the words 'Attorney/Client Privileged Information' in bold letters, and Hilton's trial counsel attached a note to D000010 and D000013 directing her legal assistant to redact the Barkley email and the numbering prior to producing the documents to Kumar).

⁸⁶ *Id.*

⁸⁷ *Sitterson v. Evergreen Sch. Dist. No. 114*, 147 Wn. App. 576 (Wash. Ct. App. 2008).

⁸⁸ The five factors enumerated in *Alldread* are: "(1) the reasonableness of precautions taken to prevent disclosure; (2) the amount of time taken to remedy the error; (3) the scope of discovery; (4) the extent of the disclosure; and (5) the overriding issue of fairness." *Id.* at 588 citing *Alldread v. Gren.*, 988 F.2d 1425, 1433 (5th Cir. Miss. 1993).

⁸⁹ *Id.*

⁹⁰ *Id.* at 588-589. See also *In re Grand Jury Investigation of Ocean Transp.*, 604 F.2d 672, 675 (1979) (where documents were turned over one year prior to the assertion of privilege, and they had already been copied, digested, and analyzed by the time of the motion, the court found that "the disclosure cannot be cured simply by a return of the documents. The privilege has been permanently destroyed.").

that FRE 502 intended to correct by excusing an inadvertent production of privileged documents.⁹¹ Finally, the Court of Appeals ruled that the issue of fairness favored neither party. Defendant's inadvertent disclosures dealt with its counsel's interpretation of plaintiff's contract claim. Because the jury based its award in quantum meruit, the panel concurred that the disclosures did not unjustly prejudice either party.

SEC v. Badian

Not only do courts require a disclosing party to at least take *some* reasonable precautions to protect its privilege, courts require the disclosing party to attempt to rectify the error in a reasonable amount of time. For example in *SEC v. Badian*, Magistrate Judge Eaton applied common law FRE 502 factors to conclude that non-party Rhino waived any claim of privilege for documents inadvertently produced.⁹² First, the court stated that it has “been shown no evidence that Rhino or Bryan Cave LLP took any precautions to weed out any possibly privileged documents.”⁹³ Second, the court found the next factor –the extent of disclosures problematic. Rhino originally stated that that as much as 5% (or 3400 documents) of its production contained inadvertently produced privileged material. Even though Rhino later reduced that number to just 260 documents, the court found that “this is still a significant number of documents.”⁹⁴ Third, the court turned to the amount of time Rhino took to rectify the error. The court determined that Rhino's failure to make any attempt at rectifying the error for five years was an unreasonable time under the *Lois Sportswear* standard.⁹⁵ Finally, in analyzing the overarching issue of fairness standard, the court determined there was “no fairness” in precluding the SEC from using the documents produced by Rhino's counsel, but declined to extend waiver beyond those actually produced.⁹⁶

Clarke v. J.P. Morgan Chase & Co.

Some courts have conducted a waiver analysis even after ruling the disclosure was not privileged using an essential element test.⁹⁷ In the employment case *Clarke v. J.P. Morgan Chase & Co.*, the court ruled an e-mail was not privileged after conducting a three-factor test as enumerated in *United States v. Construction Prods. Research*.⁹⁸ In *Clarke*, the produced e-mail lacked any indication of attorney-client communication on its face.⁹⁹ The e-mail did not state that any of the contents were privileged or confidential.¹⁰⁰ Thirdly, the e-mail most likely was beginning an effectuation of a corporate policy change rather than obtaining or providing legal advice.¹⁰¹ Because of these three factors the court ruled that the e-mail was not privileged.

Coincidentally, even though the court determined the produced e-mail was not privileged, Judge Freeman conducted a further analysis for waiver as if the e-mail was actually afforded the protection of privilege.¹⁰² The court looked to FRE 502(b) and enumerated four common law factors from *Business Integration Services, Inc. v. AT&T Corp.*, that parallel a 502(b) analysis.¹⁰³ In applying the *Business Integration Services* test, Judge Freeman ruled that defendant did “not appear to have taken

91 *Sitterson v. Evergreen Sch. Dist. No. 114*, 147 Wn. App. 576 (Wash. Ct. App. 2008).

92 *SEC v. Badian*, 2009 U.S. Dist. LEXIS 9204 (S.D.N.Y. Jan. 26, 2009) (The parties agree that a claim of inadvertence is governed by the four factors set forth in *Lois Sportswear, U.S.A., Inc. v. Levi Strauss & Co.*, 104 F.R.D. 103, 105 (S.D.N.Y. 1985) (Sweet, J.), and its progeny such as *Business Integration Services, Inc. v. AT&T Corp.*, 251 F.R.D. 121, 129 (S.D.N.Y. 2008)).

93 *Id.* at 8.

94 *Id.* at 11.

95 *Id.* at 16 (“Rhino chose to turn over its email files without stating that it was withholding any portions on the basis of privilege [nor did Rhino] provide any internal list in 2003 of any documents that they were withholding from the SEC on the basis of privilege”).

96 *Id.* at 17.

97 *Clarke v. J.P. Morgan Chase & Co.*, 2009 U.S. Dist. LEXIS 30719 (S.D.N.Y. Apr. 10, 2009) citing *United States v. Construction Prods. Research*, 73 F.3d 464, 473 (2d Cir. 1996) (“The essential elements that must be shown by a party asserting the attorney-client privilege are: “(1) a communication between client and counsel, which (2) was intended to be and was in fact kept confidential, and (3) [was] made for the purpose of obtaining or providing legal advice”).

98 *Id.* at 6.

99 *Id.* (the sender was neither an attorney nor his agent; the e-mail did not state that it contained privileged information; the e-mail did not state that any of the information incorporated therein had been obtained from counsel or was based on communications from counsel or even that counsel had been consulted; nor did it state that the policy change reflected in the e-mail was intended to implement a recommendation of counsel).

100 *Id.* at 10 (“the e-mail did not flag that any of its contents, in particular, were privileged and should not be communicated”).

101 *Id.* (The court declined a final determination regarding whether the e-mail was drafted for the purpose of conveying or obtaining legal advice because the producing party failed to meet the first two factors) (“Defendant failed to satisfy its burden to show that the recipients of the e-mail would have reasonably understood that they were even receiving legal advice, which was intended to be held in confidence”).

102 *Id.* at 13.

103 *Id.* at 14 citing *Business Integration Services, Inc. v. AT&T Corp.*, 251 F.R.D. 121, 129 (S.D.N.Y. 2008). (“These same factors are also generally weighed by the Court in the context of extrajudicial disclosures. . . . More particularly, the Court should consider (1) the reasonableness of the precautions to prevent inadvertent disclosure, (2) the time taken to rectify the error, (3) the extent of the disclosure, [and] (4) an over[arching] issue of fairness and the protection of an appropriate privilege which . . . must be judged against the care or negligence with which the privilege is guarded”).

particular care to prevent the dissemination of the e-mail or the supposedly privileged portions of its contents to the reclassified employees.”¹⁰⁴ Furthermore, the inadvertently disclosed e-mail was “on top of the stack” of a small production of 532 pages.¹⁰⁵ Judge Freeman stated that the defendant should have become aware and assessed the privileged status of the e-mail at the latest on the date of initial disclosures on September 15, 2008 and at the minimum started an investigation into the privileged nature of the e-mail on the date of production on December 11, 2009.¹⁰⁶ The defendant did neither. The court also ruled the defendant took too much time to rectify the error. “It was not until February 17, 2009, more than two months after the e-mail had been produced by Plaintiffs [and six days after the document was used in plaintiff’s deposition]...that Defendant’s counsel, for the first time, asserted a claim of privilege.”¹⁰⁷ Third, the court determined that the extent of the disclosure was unreasonable given the volume of the document production and location of the e-mail in the collection.¹⁰⁸ Finally, the court weighed the issues of fairness heavily to favor plaintiff, because “plaintiffs should not have been forced to alter their deposition preparation at the last minute, so as to take account of Defendant’s belatedly raised claim.”¹⁰⁹

Relion, Inc. v. Hydra Fuel Cell Corp.

Other courts have ruled in favor of waiver by unique interpretations of the FRE 502(b) reasonable precautions standard. In *Relion, Inc. v. Hydra Fuel Cell Corp.*, the court ruled that disclosing counsel should have taken “all reasonable means” to protect privilege; a much greater burden than the reasonable precautions standard set out in FRE 502(b).¹¹⁰ In *Relion*, plaintiff’s counsel sought the return of its client’s privileged documents by seeking enforcement a Protective Order. Plaintiffs inadvertently disclosed a three inch thick file of “question documents” in its production of documents that “occupied over 40 feet of shelf space.”¹¹¹ The production was reviewed by counsel prior to production, but the question document folder was inadvertently left in the collection. Magistrate Judge Hubel ruled that because he found no surprise or deception on the part of the receiving party’s counsel, and the disclosing party had several opportunities to inspect the documents in various formats, he “conclude[d] that Relion did not pursue all reasonable means of preserving the confidentiality of the documents produced to Hydra, and therefore that the privilege was waived.”¹¹²

Coincidentally, the court might have arrived at a different result by applying the five-factor test included in the Legislative History of FRE 502 because four of five factors favored the plaintiff and non-waiver.¹¹³ However, Judge Hubel could have still found waiver using the five factor test by heavily penalizing the plaintiff for “the time taken to rectify the error” and weighing that single factor with more force than the other four. As Judge Baylson’s ruling in *Rhoads Industries, Inc. v. Building Materials Corp.* strongly weighed a single factor [the interest of justice] to conclude non-waiver, here Judge Hubel might be able to weigh a different factor to find waiver.¹¹⁴ Even so, additional guidance from the courts is necessary to determine how the five factors interplay with one another. Again, litigants should consider negotiated threshold points for each of the five reasonableness factors and include language in the Protective Order to define when privilege is actually waived.

AHF Community Development v. City of Dallas

Some courts may look to the producing party’s failure to act affirmatively on knowledge of inadvertent disclosure. For example, in a unlawful conduct case, *AHF Community Development v. City of Dallas*, plaintiff AFH moved for determination that defendant City of Dallas waived privilege as to emails inadvertently included on disc produced due to conversion to new litigation management software.¹¹⁵ While the court declined to construe FRE 502 in its opinion, the court enlisted the factors

104 *Clarke* at 14.

105 *Id.* at 15.

106 *Id.*

107 *Id.* at 18.

108 *Id.* at 21 (“it should be noted that the volume of Plaintiff’s discovery was not so large that the e-mail would have been difficult for Defendant to identify. On the contrary, the document’s existence in that production would have been readily apparent”).

109 *Id.*

110 *Relion, Inc. v. Hydra Fuel Cell Corp.*, 2008 U.S. Dist. LEXIS 98400 at 9 (D. Or. Dec. 4, 2008).

111 *Id.* at 7.

112 *Id.* at 9.

113 The Standing Committee Report n. 29 available at http://www.uscourts.gov/rules/Reports/2007-05-Committee_Report-Evidence.pdf.

114 See Footnote 42, *supra*.

115 *AHF Cmty. Dev., LLC v. City of Dallas*, 2009 U.S. Dist. LEXIS 10603 (N.D. Tex. Feb. 12, 2009).

of *Allread v. City of Grenada* to rule that the privilege was voluntarily waived.¹¹⁶ Although the court determined that the disclosure was indeed inadvertent, the court stated that the failure of defendant to act when “emails clearly labeled as attorney-client privileged were marked as exhibits, shown to a witness at deposition, and the subject of substantive questioning – all without objection.”¹¹⁷ The court therefore ruled that the defendant failed to take reasonable precautions to protect its privilege and also failed to correct the error within a reasonable time.

Outlook: Effective Use of FRE 502 Protective Orders

In all of the cases stated where a litigant was subject to waiver, had the parties agreed upon a court ordered FRE 502 non-waiver order, the outcome would likely have been different. I have included a brief discussion of the cases where courts have either effectively suggested or entered Rule 502 protective orders to protect against waiver or privilege. These cases also provide evidence of an evolving trend of cooperation in discovery.¹¹⁸

Whitaker Chalk Swindle & Sawyer, L.L.P. v. Dart Oil & Gas Corp.

Federal courts can mandate the use of FRE 502 protective orders to protect privileged when discovery materials contain significant privileged information and there is a fear of disclosure in another court or forum. For example, in an attorney fee dispute, *Whitaker Chalk Swindle & Sawyer, L.L.P. v. Dart Oil & Gas Corp.*, district court Judge Means denied a stay, but evoked FRE 502 to mandate a protective order that would prevent against the disclosure of privileged information from his court in another state court forum.¹¹⁹ The court ruled, “Dart has not pointed to any reason why a Texas court would not recognize an order entered under Rule 502, nor is this Court aware of a basis for a Texas court to find privileges waived in state proceedings based on a Federal court’s order requiring discovery in a federal case to proceed...Accordingly, it is within this Court’s authority to order discovery to proceed and that by complying with such order Dart has not waived the attorney-client or work-product privilege in the Esperada suit.”¹²⁰ Judge Means further assisted the parties by integrating the terms of the protective order into his opinion.¹²¹ In addition to reviewing the Model Protective Order Terms in the appendix of this article, a litigant should consider reviewing Judge Means’s guidance in this opinion when drafting a FRE 502 protective order.

Tremont LLC v. Halliburton Energy Servs.

Other courts have used FRE 502 to strengthen the effect of confidentiality orders. In *Tremont LLC v. Halliburton Energy Servs.*, Judge Lee Rosenthal entered a Rule 502 order that not only protected privileged information, but restricted the parties from producing a confidential index to “any other person.”¹²² Again, a review of Judge Rosenthal’s October 29, 2008 order in this case will provide litigants with additional guidance when negotiating FRE 502 protective orders.¹²³

D’Onofrio v. SFX Sports Group, Inc.

Other courts have used FRE 502 protective orders to aid in the effort for parties to cooperate.¹²⁴ For example, in *D’Onofrio v. SFX Sports Group, Inc.* a wrongful termination case, Magistrate Judge John M. Facciola suggested an order protecting defendant’s privileged information even when the defendant agreed to provide the plaintiff’s counsel with attorney notes taken by the defendants under certain conditions.¹²⁵ Taking exception to these conditions, the plaintiff’s counsel

116 *Id.* citing *Allread v. City of Grenada*, 988 F.2d 1425 (5th Cir.1993).

117 *Id.* at 16.

118 See *The Sedona Conference® Cooperation Proclamation*; The Sedona Conference Working Group Series (July 2008).

119 *Whitaker Chalk Swindle & Sawyer, LLP v. Dart Oil & Gas Corp.*, 2009 U.S. Dist. LEXIS 15901 (N.D. Tex. Feb. 23, 2009)/

120 *Id.* at 10.

121 *Id.* at 12.

122 *Tremont LLC v. Halliburton Energy Servs.*, 2009 U.S. Dist. LEXIS 27389 (S.D. Tex. Mar. 31, 2009) (“In the present case—the “2008 Case”—this court entered an order under Federal Rule of Evidence 502 to apply to document production. The Rule 502 Order stated that “the Tremont Parties production of the Tremont Index to Halliburton will not constitute any waiver of any privilege of any kind and will not cause the Tremont Parties to be required to produce the Tremont Index to any other person, including but not limited to, Georgia-Pacific Corporation, Milwhite, Inc., or M-I, LLC”).

123 *Tremont LLC v. Halliburton Energy Servs.*, No. 08-1063 at 35 (S.D. Tex. Mar. 31, 2009) (Judge Rosenthal’s FRE 502 protective order is available for download via PACER at <https://ecf.usd.uscourts.gov/>).

124 See *The Sedona Conference® Cooperation Proclamation*; The Sedona Conference® Working Group Series (July 2008).

125 *D’Onofrio v. SFX Sports Group, Inc.*, 256 F.R.D. 277, (D.D.C. 2009).

argued the plaintiff should be granted access to the attorney notes for relevancy determinations. Judge Facciola granted the motion in part, finding the defendants were allowing access to these documents for efficiency's sake not because the plaintiff was entitled to the documents. Of equal importance in this was the use of statistical sampling to identify privilege logging errors.¹²⁶ Yet again there emerging problem of search and retrieval touches the privilege issue.

Conclusion: From Courts to Effective Protective Orders

In review, although most courts analyze FRE 502 to rule in favor of non-waiver, the sample cases above interpret the rule differently. Some invoke common law, while others interpret FRE 502 strictly. One court ruled that a disclosing party merely affixing "Attorney-Client Privilege" to a document took reasonable precautions to protect its privilege, while another court ruled that a litigant deploying a thorough attorney review to locate privilege documents waived its privilege because it did not do enough to protect its privilege. Others cases have required a specific privilege logging methodology.

Litigants should avoid the hazardous variability of inadvertent disclosures protected under FRE 502(b). The most effective method to protect a client's privilege is to negotiate with your opponent for a Protective Order with a clawback provision that is now enforceable in both state and federal jurisdictions under FRE 502(d).

The cases in this article highlight a few of the variables that a litigant should consider when drafting a Protective Order. I include sample language in the appendix of this Article which addresses some (but not all) of the salient points a protective order should cover.

Appendix

Model Protective Order Provisions (as distributed at The 11th Annual Sedona Conference® on Complex Litigation)¹²⁷

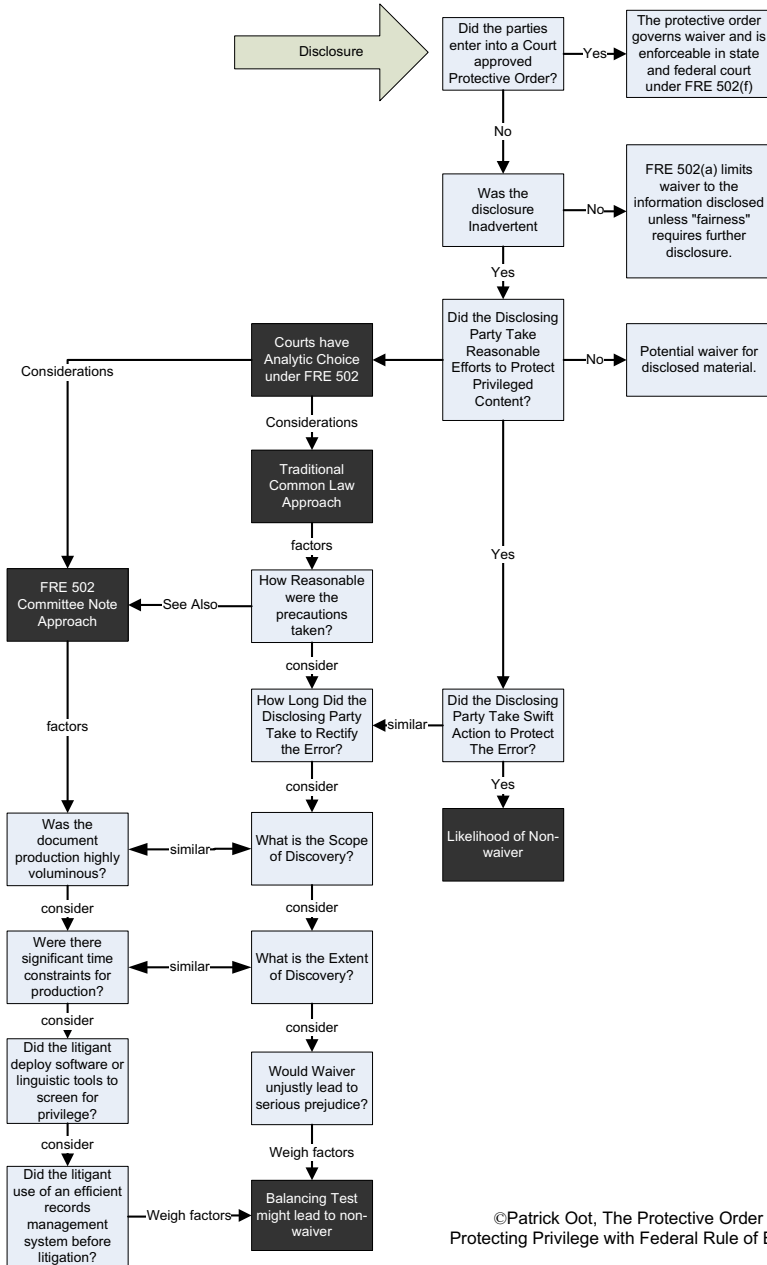
Pursuant to Rule 502 of the Federal Rules of Evidence, the inadvertent disclosure of protected communications or information shall not constitute a waiver of any privilege or other protection (including work product) if the Producing Party took reasonable steps to prevent disclosure and also took reasonable steps to rectify the error in the event of an inadvertent disclosure. The Producing Party will be deemed to have taken reasonable steps to prevent communications or information from inadvertent disclosure if that party utilized either attorney screening, keyword search term screening, advanced analytical software applications and/or linguistic tools in screening for privilege, work product or other protection. In the event of the inadvertent disclosure of protected materials, the Producing Party shall be deemed to have taken reasonable steps to rectify the error of the disclosure if, within thirty (30) days from the date that the inadvertent disclosure was discovered or brought to the attention of the producing party, the Producing Party notifies the Receiving Party of the inadvertent disclosure and instructs the Receiving Party to promptly sequester, return, delete, or destroy all copies of the inadvertently produced communications or information (including any and all work product containing such communications or information). Upon receiving such a request from the Producing Party, the Receiving Party shall promptly sequester, return, delete, or destroy all copies of such inadvertently produced communications or information (including any and all work product containing such communications or information), and shall make no further use of such communications or information (or work product containing such communications or information). Nothing herein shall prevent the Receiving Party from challenging the propriety of the attorney-client, work product or other designation of protection.

¹²⁶ *D'Onofrio v. SFX Sports Group, Inc.*, 256 F.R.D. 277, 279 (D.D.C. 2009) ("Defendants also agreed at the hearing to permit plaintiff to test the validity of the privilege log using statistical sampling. Defendants offered to allow plaintiff's expert to select a representative sample, that would be made available to plaintiff's counsel for his review to determine whether the privileges asserted were in fact appropriate. Defendants' offer is conditioned on three criteria with which plaintiff takes issue: (1) the documents be designated 'attorneys' eyes only,' (2) the sample exclude documents that were created on or after March 17, 2006, and (3) plaintiff's expert tell defendants what method he uses to generate the statistical sample prior to doing so").

¹²⁷ These model protective order provisions were drafted through the collaboration of several active Sedona Conference® members and their colleagues including Tom Allman (Former General Counsel, BASF), Maura Grossman (Wachtell, Lipton, Rosen & Katz), Patrick Oor (Verizon), John Rosenthal, & Charles Molster (Winston & Strawn), Jennifer Tomaino (Verizon), Ken Withers (The Sedona Conference®), and Anne Stukes.

Within 60 days of the production of documents, the parties will provide privilege logs for protected materials withheld for attorney-client privilege or pursuant to the work product doctrine (or other privileges or doctrines). The privilege logs shall contain names or e-mail addresses extracted from the topmost e-mail message or hard copy document (To, From, CC, BCC), the date of the topmost e-mail or document, and the basis for the assertion of a privilege or other protection. The Producing Party shall provide a privilege log for all withheld e-mail or hard-copy documents or other materials [including redacted materials]. The Producing Party shall produce e-mail chains and strings, and shall only redact those portions of the e-mail chain that are protected, leaving all other materials unredacted. The Producing Party shall log all protected content in e-mail chains and strings by logging the topmost e-mail of the e-mail chain or string, as well as sufficient information regarding the redacted material to allow the Receiving Party and the Court to make a cogent evaluation of the appropriateness of the assertion of a privilege or other protection. The Producing Party shall create a single log entry for each e-mail chain or string. A Producing Party's logging of the topmost e-mail shall be deemed to assert protection for all of the protected material in an e-mail string or chain, including multiple redactions or multiple segments. Nothing herein shall prevent the Receiving Party from challenging the propriety of the designation of attorney-client privilege, work product or other designation of protection.

Navigating FRE 502 in Federal Court



IN REM, QUASI IN REM, AND VIRTUAL IN REM JURISDICTION OVER DISCOVERY

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I. INTRODUCTION

According to *Black's Law Dictionary*, *in rem* [Latin for “against a thing”] is jurisdiction “involving or determining the status of the thing, and therefore the rights of persons generally with respect to that thing.” Accordingly,

“An action *in rem* is one in which the judgment of the court determines the title to property, and the rights of the parties, not merely as between themselves, but also as against all persons at any time dealing with them or with the property upon which the court had adjudicated.”¹

A small step removed is *quasi in rem* jurisdiction [again, Latin for “as if against a thing”] which is jurisdiction “involving or determining the rights of a person having an interest in property located within the court’s jurisdiction.”²

The concepts of *in rem* and *quasi in rem* jurisdiction include not only the court’s power to adjudicate the rights to a given item of property, but “the power to seize and hold it.”³ *Quasi in rem* jurisdiction is, technically, jurisdiction over a person, rather than an item of property, but jurisdiction based upon that person’s interest in the property located within the court’s territory.

Back in the day of documents on paper, the establishment of *in rem* and *quasi in rem* jurisdiction, by a specific court, over a specific body of documentary evidence, was established by the straightforward mechanism of creating a “document depository,” located with the court’s jurisdictional territory. Indeed, in the early years of determining appropriate transferee venues under the multidistrict litigation statute, 28 U.S.C. Section 1407, the location of documents was an important consideration, since the effort and expense in relocating large bodies of documents was substantial.⁴ The physical location of documents was, accordingly, a convenient basis upon which to determine the location of the federal multidistrict litigation involving it.⁵ While the resulting *in rem* or *quasi in rem* jurisdiction of the MDL transferee court over the body of documents with evidentiary significance to the litigation was not frequently remarked, that is perhaps because it did not need to be: it was beyond peradventure and literally went without saying.

We are now well into the era of virtual documentation, in which documentary evidence consists significantly, if not primarily, of electronically created, transmitted, and stored data, which may or may not have a paper back-up, in a specific place. Document depositories, in the traditional

¹ R.H. Graveson, *Conflicts of Laws*, 98 (7th. ed. 1974).

² *Black's Law Dictionary*, (7th Ed.).

³ *Id.*

⁴ See, e.g., reference to the “massive document depository” as a factor supporting transfer of related actions to the District of Arizona under 28 U.S.C. Section 1407 in *Lexecon, Inc. v. Milberg Weiss Bershad Hynes & Lerach*, 523 U.S. 26, 30 (1998).

⁵ The location of documents (typically at a defendant’s headquarters) was a major consideration in the Judicial Panel’s early transfer decisions. See, e.g., *In re 1980 Decennial Census Adjustment Litigation*, 506 F. Supp. 648 (Jud. Pan. Mult. Lit. 1981); *In re Upjohn Co. Antibiotic “Cleocin” Prod. Liab. Litig.*, 450 F. Supp. 1168 (Jud. Pan. Mult. Lit. 1978); *In re Sundstrand Data Control, Inc., Patent Litigation*, 443 F. Supp. 1019 (Jud. Pan. Mult. Lit. 1978). Recent transfer orders of the Panel, such as those on the Panel’s website, www.jpml.uscourts.gov, are notable for their frequent omission of this factor.

sense, are no longer pre-existing: they must be created, and more and more courts are dispensing with this step as costly and unnecessary. The result is, at least theoretically, a savings of time and costs, because documentary evidence may be produced, as well as stored, electronically, and the days of branch library-sized paper document depositories, located within the MDL transferee court's jurisdictional territory, may be a thing of the past. However, this evolution may have given rise to a problem which simply did not previously exist: determining which court has jurisdiction to determine the status of documentary evidence (as relevant or irrelevant; privileged or non-privileged) and of the rights of persons (the requesting and producing parties and their counsel) with respect thereto.

To the extent that determinations of privilege and potential relevance are discretionary, qualitative and/or subjective in nature, and given the often inescapable fact that litigation involving the same evidence is pending in multiple jurisdictions (which may or may not be formally or informally coordinated), the question of which court is or should be the sole or primary adjudicator of evidentiary disputes is a live one. The new Rule 502(d) "clawback" provisions,⁶ which protect the privilege of inadvertently produced documents, and hence potentially promote production, facilitate cost-effective discovery, and reduce disputes, can work optimally only if the parties and their counsel may have a reasonable degree of confidence that disputes over such discovery will be adjudicated once, with binding effect. The old-fashioned concepts of *in rem* and *quasi in rem* jurisdiction may merit revival to address this emerging and predictably recurring problem.

II. IN REM AND QUASI IN REM: A PRIMER

The federal courts, as tribunals of limited jurisdiction, have had a particular interest in defining the nature, and delineating the bounds, of *in rem* and *quasi in rem* jurisdiction.

While the vast majority of federal cases are actions *in personam*, there is no constitutional or statutory limitation on the power of a federal court to entertain actions *in rem* or, under certain circumstances, actions *quasi in rem*. See 14 C. Wright, A. Miller & E. Cooper, *Federal Practice and Procedure*, Section 3631, at 3 (2d ed. 1985). Jurisdiction predicated on the presence of property or assets within a federal court's geographical domain has a long history. See *Pennoyer v. Neff*, 95 U.S. 714, 24 L.Ed. 565 (1878). *In rem* and *quasi in rem* jurisdiction arising from a court's territorial power over the property is typically invoked when persons with claims to the property are nonresidents and securing personal jurisdiction difficult or impossible. 4 C. Wright & A. Miller, *Federal Practice and Procedure*, Section 1070, at 417 (2d ed. 1987).

Much debate still surrounds the use of *quasi in rem* jurisdiction, clouded in part by varying definitions of two jurisdictional concepts. Technically, *in rem* jurisdiction relates to the determination of title to, or the status of, property located within the court's territorial limits. *Federal Practice and Procedure*, Section 1070, at 422. A court's authority stems directly from adjudicating the ownership or other rights with respect to the property and the judgment is effective against all persons with an interest in the property.⁷

A *quasi in rem* action does not directly relate to the property, although it may represent the asset that will be used to satisfy a subsequent judgment, should plaintiff prevail. *Federal Practice and Procedure*, Section 1070, at 422. Most courts and commentators support continued reliance on *in rem*

6 The Federal Rules of Evidence now include Rule 502, which addresses "Attorney-client privilege and work product; limitations on waiver." The Rule protects against inadvertent disclosures as follows:

(b) Inadvertent disclosure. When made in a Federal proceeding or to a Federal office or agency, the disclosure does not operate as a waiver in a Federal or State proceeding if:

(1) the disclosure is inadvertent;
 (2) the holder of the privilege or protection took reasonable steps to prevent disclosure; and
 (3) the holder promptly took reasonable steps to rectify the error, including (if applicable) following *Federal Rules of Civil Procedure 26(b)(5)(B)*.

(d) Controlling effect of a court order. A Federal court may order that the privilege or protection is not waived by disclosure connected with the litigation pending before the court—in which event the disclosure is also not a waiver in any other Federal or State proceeding.

7 See, e.g., 28 U.S.C. Section 1655 (1988) (granting federal court jurisdiction to hear cases involving title, liens, claims or encumbrances as to real or personal property).

and *quasi in rem* jurisdictional bases where the property is the subject matter of the litigation or at least a significant ingredient in it, while questioning its use in the absence of minimum contacts.⁸

The same principles of minimum contacts that govern personal jurisdiction are relevant in determining the proper assertion of *quasi in rem* jurisdiction. The location of the property remains a significant factor, however, as it “may bear on the existence of jurisdiction by providing contacts among the forum State, the defendant, and the litigation. *Shaffer v. Heitner*, 433 U.S. 186, 207 (1977).⁹

The federal courts often have an adequate basis to exercise both *in rem* and *quasi in rem* jurisdiction in class action proceedings. The assets of a settlement trust or common fund resulting from a court-approved settlement may constitute the *res*. Each absent class member has some contact with the jurisdiction, since each seeks to recover monies from the *res* and hence expects to benefit from the forum’s protection of the settlement assets.¹⁰

III. IS DISCOVERY A THING?

The Latin word “*res*,” literally “thing,” has been applied to a broad array of items and matters in Anglo-American law: real and personal property, items of physical evidence, and indeed, disputes themselves. We speak of a controversy finally adjudicated as “*res judicata*.” In tort law, we say of a self-evident injury, or the instrumentality that must have caused it: “*res ipso loquitur*.” Indeed, a metaphysical inquiry yields no material distinction between the piece of paper upon which words are written, printed, or typed, and email that documents the same thought, intention, agreement, or occurrence. Indeed, all evidence involving words, onscreen, on paper, or digitally encoded, involves the visible and lasting artifact of an invisible, and perhaps ephemeral, thought, that became a word, and it relates to a deed (of commission, omission, or concealment) that is potentially relevant to a statutory or tort claim or defense.

When persons fall within the jurisdiction of the court, the evidence of their intentions and conduct likewise, and logically, falls under that jurisdiction: *quasi in rem*. Persons may simultaneously come within the jurisdiction of multiple courts, as a result of claims derived from the same course of conduct or event. Thus, persons and the evidence relating to their intent and conduct, may be metaphysically divided among multiple jurisdictions, all of which are empowered to adjudicate the rights and disputes related thereto. As a result, we have inconsistent, and potentially contradictory, rulings involving the admissibility, privilege, and production of documentary evidence. It is because such inconsistent or contradictory results are possible (often times within the allowable range of judicial discretion) that we have costly and time-consuming discovery disputes.

Theoretically, if one court were empowered by exercise of *in rem* or *quasi in rem* jurisdiction, over a body of documentary evidence, and the rights and interests relating thereto, the costs, expense and delay of discovery disputation would markedly decrease, and predictability and consistency would be enhanced. Opportunities for gamesmanship would decline, and it is pleasant to think that potentially relevant and non-privileged evidence would more likely be produced, and available for an ultimate determination of claims and defenses on their merits.

Assuming such an exclusive exercise of *in rem* or *quasi in rem* jurisdiction is possible, by whom is it most appropriate? The first court before whom the dispute is filed, and in which the

8 See *Cargill, Inc. v. Sabine Trading & Shipping Co.*, 756 F.2d 224, 227-8 & n.2 (2d Cir. 1985); *Spungin v. Chinetti Int'l Motors*, 515 F. Supp. 31 (E.D.N.Y. 1981); *Drexel Burnham Lambert Inc. v. D'Angelo*, 453 F. Supp. 1294, 1296-97 (S.D.N.Y. 1978); *In re: Joint Eastern and Southern District Asbestos Litigation*, 129 B.R. 710, **232237 (1991).

9 In *Shaffer*, the Supreme Court held that securing personal jurisdiction over a nonresident defendant through the seizure of property located within the state, but unrelated to the action, violated due process. *Id.* at 207. The plaintiff had seized defendant’s shares in a Delaware corporation to obtain jurisdiction to resolve a dispute unrelated to any acts within the state. *Id.* Without additional contacts, the Court found that jurisdiction offended traditional notions of fair play and substantial justice. *Id.* Thus, for *quasi in rem* actions, due process requires the court to look beyond the mere physical existence of the property within the forum. The *Shaffer* decision has inspired considerable controversy. See, e.g., Silberman, *Shaffer v. Heitner*—“The End of an Era,” 53 N.Y.U. L. Rev. 33 (1978); Kalo, “Jurisdiction as an Evolutionary Process: The Development of *Quasi In Rem* and *In Personam*, Principles,” 1978 Duke L.J. 1147.

10 *Joint E. & S. Dist. Asbestos Litigation, id.* at 800 (“Constructive possession of the [settlement] Trust and the preservation of its assets suffices to warrant the exercise of jurisdiction.”).

disputing parties appear? The first such *federal court*? MDL transferee court to which numerous related federal actions are sent for coordinated discovery and other pre-trial proceedings? Or simply the court(s) within which the documentary evidence happens to be situated?

The last alternative, *in locus in rem* jurisdiction, is the most traditional, but probably the least useful in the e-discovery context. It is easy to determine the location of original written documents and physical evidence. But copies of documents are portable, and virtual documents are (or easily can be) everywhere. With respect to electronic discovery, ubiquity is a given.¹¹

Within the federal system, documents and discovery originating in, located in, or sent to a number of federal courts may be retrieved and collected in a single federal jurisdiction through the statutory multidistrict litigation process. In MDL parlance, pretrial proceedings (including discovery) are said to be “centralized” within a single transferee district in order “to eliminate duplicative discovery, prevent inconsistent rulings, and conserve the resources of the parties, their counsel and the judiciary.”¹² Thus, within the federal system, out of many potential discovery fora, one is created, and that one may exercise essentially plenary jurisdiction (at least during pretrial proceedings) over the processes and products of discovery. This is the ideal scenario under which new Rule 502 potentially operates to speed the pace, maximize the scope, and minimize the disputes surrounding the protection of potentially relevant documents (including e-discovery).

State courts are beyond the mandate of Section 1407 centralization. While many states that have analogous coordination statutes which operate within state boundaries,¹³ other states do not, and there is no inter-state centralization system. Coordination among state courts, and between federal and state courts is often implemented, and has become a recommended “best practice” within the diffuse institution of complex litigation.¹⁴

If an MDL transferee court is designated early enough in related multijurisdictional proceedings, that court may have the opportunity to exercise protective jurisdiction over discovery such that production flows freely with Rule 502 protections against inadvertent disclosure in place. If, however, as is often the case, state court proceedings are running ahead of the federal litigation, and discovery is underway, the parties may revert to traditional over-withholding of documents as a precaution against waiver, unless and until a court that implements and honors Rule 502 procedures emerges as a recognized “center of gravity” for the litigation such that it may exercise *in rem*, *quasi in rem*, or its virtual equivalent, to operate as a sanctuary in which the free flow of discovery information may safely occur.¹⁵

IV. THE (COMPLEX) LITIGATION’S THE THING

Class action and other complex litigation¹⁶ often, but not always, culminates in the judicial review and approval of a settlement that, in turn, requires ongoing jurisdiction and administration of a settlement trust or common fund, or the enforcement of injunctive or equitable relief. This is the classic arena of *in rem/quasi in rem* jurisdiction. The dual nature of our federal/state court system has led to attempted end-runs around traditionally “limited” federal jurisdiction by litigants (often

11 The venerable maxim, “Wherever you go, there you are,” (attributed to, *inter alia*, Thomas á Kempis, P.J. O’Rourke, Art Linkletter, and Buckaroo Banzai.) applies with particular force to e-discovery.

12 See, e.g., *In re Bausch & Lomb, Inc. Contact Lens Solution Prod. Liab. Litig.*, 444 F. Supp. 2d 1336, 1338 (J.P.M.L. 2006).

13 See, e.g., California Code of Civil Procedure, Sections 404, *et seq.*; California Rules of Court, Rules 3.520, *et seq.*

14 See, e.g., *Manual For Complex Litigation Fourth* (Federal Judicial Center 2004) Sections 20.3-20.313.

15 The Judicial Panel on Multidistrict Litigation frequently uses the term “center of gravity” to connote a confluence of circumstances (including but not limited to the location of documents, witnesses, evidence, related proceedings, parties, or some combination of the foregoing) that justifies the transfer and centralization of cases from across the country in that district. See, e.g., *In re Municipal Derivatives Antitrust Litigation* (MDL No. 1950), 560 F. Supp. 2d 1386, 1387 (JPML 2008).

16 The class action court’s jurisdiction over absent class members, and its broad supervisory power over all aspects of a formal Rule 23 class action, have long been recognized. This is quintessential equity jurisdiction. Many mass torts and other complex litigation scenarios are not brought as class actions, and in others class certification may be denied. Neither circumstance has prevented courts from characterizing the cases before them as “quasi-class” actions, subjecting the parties to the courts’ “broad equitable powers,” including the power to cap and limit attorney fees. *In re Vioxx Prod. Liab. Litig.* (MDL No. 1657), 574 F. Supp. 2d 606, 611 (E.D. La. 2008), *citing In re Zypresra Prod. Liab. Litig.* (MDL No. 1596), 424 F. Supp. 2d 488, 492 (E.D.N.Y. 2006) (“The judiciary has well-established authority to exercise ethical supervision of the bar in both individual and mass actions”) and *In re Guidant Corp. Prod. Liab. Litig.* (MDL No. 1708), 2008 U.S. Dist. LEXIS 17535 (D. Minn. 2008). Judge Wersten has further expanded the concept of the non-class mass tort action as a “quasi-class action” to the situation of a “quasi-aggregate” action, extending the judicial power to review and modify private contingent fee agreements in single-plaintiff trials that were preceded by common issues adjudications. See *McMillan v. City of New York*, 2008 U.S. Dist. LEXIS 78711 (E.D.N.Y. 2008).

opting-out or objecting class members) who seek to ignore or evade the settlement terms, or attempt to obtain damages from a settling defendant in addition to the settlement fund. In such instances, federal courts have explored the consistencies and tensions between the All Writs Act and the Anti-Injunction Act, often finding in the former the injunctive mechanism to protect their ongoing jurisdiction from interference, invoking the concept of *in rem* jurisdiction to justify the halt of parallel or related state court proceedings.¹⁷ It is illuminating to summarize this analysis, as it has, and may constructively continue, to be adopted outside the context of a settlement fund or trust as the foundational “*res*.”

Federal district and appellate courts have analyzed both multidistrict (“MDL”) and large class actions to *in rem* actions.¹⁸ The analogy is based, in part, on the institutional demands of such litigation on the supervising court, as well as on the limited resources of a defendant in a large mass tort, securities, or antitrust case (*e.g.*, the rigors of class or mass litigation may jeopardize the viability of corporate defendants and their ability to satisfy a mass or class judgment or fund a global settlement), as well as the court’s interest in the equitable treatment of plaintiffs who may be competing for a fair share of dwindling resources.¹⁹

The Second Circuit, upholding an All Writs Act injunction against state court proceedings in *In re Baldwin-United Corp.*, 770 F.2d 328, 337 (2d Cir. 1985), was both categorical and succinct:

“the need to enjoin conflicting state proceedings arises because the jurisdiction of a multidistrict court is analogous to that of a court in an *in rem* action or in a school desegregation case, where it is intolerable to have conflicting orders from different courts.” 17 C. Wright & A. Miller & E. Cooper, *supra*, Section 4225 at 105 n.8 (Supp. 1985).

the district court had before it a class action proceeding so far advanced that it was the virtual equivalent of a *res* over which the district judge required full control. Similar authority for the injunction comes from the court’s power to protect and effectuate its order provisionally approving [the 18 settlements].”

Other courts have solidified and expanded upon this concept. As noted in *In re: School Asbestos Litigation*:

In class action contexts, such as *In re Baldwin-United*, courts have noted the similarity of complex litigation to *in rem* actions. Where a complex proceeding is “so far advanced that it was the virtual equivalent of a *res* over which the district court judge required full control,” *In re Baldwin-United*, 770 F.2d at 337, the “in aid of jurisdiction” exception authorizes the stay of state court proceedings when “the state court proceeding may effectively deprive the federal court of the opportunity to adjudicate as to the *res*” *Mitchum v. Foster*, 407 U.S. 225, 2357 (1972).

In a multi-defendant class action, the labeling of the class action as a “*res*” over which the district judge should be permitted to exercise full control, including

17 A court may enjoin state court proceedings “where necessary in aid of its jurisdiction.” 28 U.S.C. Sections 1651; 2283. It is well-settled that “if an action is *in rem* or *quasi in rem*, the court first obtaining jurisdiction over the *res* could enjoin suits in other courts involving the same *res*.” Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, Federal Practice and Procedure Section 4221 (2d Ed. 2005); *Vendo Co. v. LekroVend Corp.*, 433 U.S. 623, 641 (1977); *Mitchum v. Foster*, 407 U.S. 225, 235-37, 32 L. Ed. 2d 705, 92 S. Ct. 2151 (1972); *Standard Microsystems Corp. v. Texas Instruments, Inc.*, 916 F.2d 58, 60 (2d Cir. 1990); *In re VisaCheck/MasterMoney Antitrust Litig.*, 2005 U.S. Dist. LEXIS 18693, *8 (E.D.N.Y. 2005).

18 See, *e.g.*, *In re Baldwin-United Corp.*, 770 F.2d 328, 337 (2d Cir. 1985) (securities class action was “so far advanced that it was the virtual equivalent of a *res* over which the district judge required full control.”); *In re Diet Drugs Prods. Liab. Litig.*, 369 F.3d 293, 306 (3d Cir. 2004); *In re Diet Drugs*, 282 F.3d 220, 235 n.12 (3d Cir. 2002); *Battle v. Liberty Nat’l Life Ins. Co.*, 877 F.2d 877, 882 (11th Cir. 1989); *In re Corrugated Container Antitrust Litig.*, 659 F.2d 1332, 133435 (5th Cir. 1981).

19 See *In re Diet Drugs*, 369 F.3d at 296-97; *In re Joint Eastern and Southern Dist. Asbestos Litig.*, 134 F.R.D. 32, 37-38 (E.D.N.Y. & S.D.N.Y. 1990); *VisaCheck*, 2005 U.S. Dist. LEXIS 18693 at *9.

the stay of parallel state proceedings, is especially appropriate where a settlement has been reached with many of the defendants and the judge seeks to supervise the administration of the settlement. See *In re Corrugated Contained Antitrust Litigation*, 659 F.2d 1332 (5th Cir. 1981).²⁰

In one of its reviews of procedural attacks upon the massive and complex class action settlement in the “*Diet Drugs*” MDL litigation, the Third Circuit thoroughly explored the concept, and statutory and jurisprudential support, for the powerful complex litigation-*in rem* analogy. Writing to affirm the district court’s All Writs Act injunction of a purported “mass opt out” by a Texas-court-certified subclass from the federal court-approved class settlement in *In re: Diet Drugs Prod. Liab. Litig.*, 282 F.3d 220 (3d Cir. 2002), Judge Scirica conducted a comparative and harmonizing analysis of the apparently contradictory powers of the All Writs and Anti-Injunction Acts.²¹ The Court recognized that the Anti-Injunction Act might trump the All Writs Act in ordinary *in personam* actions:

In ordinary actions *in personam*, each court is free to proceed in its own way and in its own time, without reference to the proceedings in the other court. Whenever a judgment is rendered in one of the courts and pleaded in the other, the effect of that judgment is to be determined by the application of the principle of *res adjudicata* by the court in which the action is still pending *Kline v. Burke Constr. Co.*, 260 U.S. 226, 230, 67 L. Ed. 226, 43 S. Ct. 79 (1922). Therefore, it may not be sufficient that state actions risk some measure of inconvenience or duplicative litigation. *In re Baldwin-United Corp.*, 770 F.2d 328, 337 (2d Cir. 1985). An injunction may issue, however, “where the state court action threatens to frustrate proceedings and disrupt the orderly resolution of the federal litigation. *Winkler v. Eli Lilly & Co.*, 161 F.3d 1196, 1202 (7th Cir. 1996). In other words, the state action must not simply threaten to reach judgment, it must interfere with the federal court’s own path to judgment.” *Diet Drugs*, 282 F.3d at 234.

The All Writs Act’s injunctive powers may, however, be invoked where the federal court’s jurisdiction is *in rem*:

While, as noted the “necessary in aid of jurisdiction” exception does not ordinarily permit injunctions merely to prevent duplicative actions *in personam*, federal courts are permitted to stay later-initiated state court proceedings over the same *res* in actions *in rem*, because “the exercise by the state court of jurisdiction over the same *res* necessarily impairs, and may defeat, the jurisdiction of the federal court already attached.”

* * *

We have recognized another category of federal cases for which state court actions present a special threat to the jurisdiction of the federal court. Under an appropriate set of facts, a federal court entertaining complex litigation, especially when it involves a substantial class of persons from multiple states, or represents a consolidation of cases from multiple districts, may appropriately enjoin state court proceedings in order to protect its jurisdiction. *Carlough v. Amchem Prods.*,

²⁰ *In re Asbestos School Litigation*, 1991 U.S. Dist. LEXIS 5142, *6 (E.D. Pa. 1991).

²¹ The All Writs Act provides “all courts established by Act of Congress may issue all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law. 28 U.S.C. Section 1651. The power granted by the All Writs Act is limited by the Anti-Injunction Act, 28 U.S.C. Section 2283, which prohibits, with certain specified objections, injunctions by federal courts that have the effect of staying a state court proceeding.... The Anti-Injunction Act prohibits most injunctions “to stay proceedings in a State court.” 28 U.S.C. Section 2283.

The Anti-Injunction Act does “not preclude injunctions against the institution of state court proceedings, but only bars stays of suit already instituted. *Dombrowski v. Pfister*, 380 U.S. 479, 484 n.2 (1965). However, the Anti-Injunction Act allows such injunctions “as expressly authorized by Act of Congress, or where necessary in aid of its jurisdiction, or to protect or effectuate its judgments. 28 U.S.C. Section 2283.

Inc., 10 F.3d 189, 202-04 (3d Cir. 1993). *Carlough* involved a nationwide class of plaintiffs and several defendants – primarily manufacturers of asbestos-related products – and third-party defendants – primarily insurance providers. We found the complexity of the case to be a substantial factor in justifying the injunction imposed. 10 F.3d at 202-03. *Diet Drugs*. *Id.*

Implicit in the *Carlough-Diet Drugs* analysis is the recognition that preserving and protecting “the federal court’s flexibility and authority to decide”²² complex nationwide cases (whether MDLs or class actions) makes special demands on the court [implicitly, the challenge of fulfilling Fed. R. Civ. P. 1’s overarching “just, speedy, and inexpensive determination of every action and proceeding” directive that may justify an injunction otherwise prohibited by the Anti-Injunction Act. The *Diet Drugs* decision mustered an impressive array of authority (or at least anecdotes) in support of this thesis.²³

Likewise, *Diet Drugs* collects specific instances in which the “courts have analogized complex litigation cases to actions *in rem* The *in rem* analogy may help to bring into focus what makes these cases stand apart ... where complex cases are sufficiently developed, mere exercise of parallel jurisdiction by the state court may present enough of a threat to the jurisdiction of the federal court to justify the issuance of an injunction.”²⁴ The insight of *Diet Drugs* is that, for both the traditional *in rem* action and the modern complex case, is that “in both kinds of cases state actions over the same subject matter have the potential to ‘so interfere with a federal court’s consideration or disposition of a case as to seriously impair the federal court’s flexibility and authority to decide the case.’”²⁵

Much of the jurisprudence gathered by *Diet Drugs* concerned the propriety of injunctions issued by federal courts in the context of impending global settlements.²⁶ The need for consistency and predictability of discovery ruling – and thus the potential attraction of applying an *in rem* or *quasi in rem* analogy to discovery and documents – arises much earlier in the proceedings. It is thus significant that *Diet Drugs* acknowledges and cites two instances of federal courts using the analogy to protect their discovery rulings: *Winkler v. Eli Lilly*²⁷ and *Harris v. Wells*.²⁸

V. DOES THE COMPLEX LITIGATION – *IN REM* ANALOGY APPLY TO DISCOVERY?

In *Harris v. Wells*, a (non-class, non-MDL) corporate dispute involving officers, directors, and shareholders of AroChem International, the district court issued an All Writs Act injunction against Delaware Chancery Court discovery requests that “mirror previous discovery requests” made in the federal court, to enable it to “retain control over discovery matters.”²⁹

22 *Diet Drugs*, 282 F.3d at 235.

23 See, e.g., *Hanlon v. Chrysler Corp.*, 150 F.3d 1011 (9th Cir. 1998); *Winkler*, 101 F.3d at 1203 (“The Anti-Injunction Act does not bar courts with jurisdiction over complex multidistrict litigation from issuing injunctions to protect the integrity of their rulings.”); *Welsch v. Folsom*, 6 F.3d 1465, 1470 (11th Cir. 1993); *Battle v. Liberty Nat’l Life Ins. Co.*, 877 F.2d 877, 882 (11th Cir. 1989); *Baldwin-United*, 770 F.2d at 337-38; *In re Corrugated Container Antitrust Litig.*, 659 F.2d 1332, 1334-35 (5th Cir. Unit A 1981) (approving injunction in a “complicated antitrust action[that] has required a great deal of the district court’s time and has necessitated that it maintain a flexible approach in resolving the various claims of the many parties.”); *In re Columbia/HCA Healthcare Corp. Billing Practices Litig.*, 93 F. Supp. 2d 876 (M.D. Tenn. 2000); *In re Lease Oil Antitrust Litig. (No. II)*, 48 F. Supp. 2d 699, 704 (S.D. Tex. 1998); *Harris v. Wells*, 764 F. Supp. 743 (D. Conn. 1991); *In re Asbestos Sch. Litig.*, 1991 U.S. Dist. LEXIS 5142, No. 83-0268, 1991 WL 61156 (E.D. Pa. Apr. 16, 1991), *aff’d mem.*, 950 F.2d 723 (3d Cir. 1991); *In re Joint E. & S. Dist Asbestos Litig.*, 134 F.R.D. 32 (E.D.N.Y. & S.D.N.Y. 1990). As one court reasoned, “the district court had before it a class action proceeding so far advanced that it was the virtual equivalent of a *res* over which the district judge required full control. *Baldwin-United*, 770 F.2d at 337; see also *Welsch*, 6 F.3d at 1470; *Battle*, 877 F.2d at 882 (“It makes sense to consider this case, involving years of litigation and mountains of paperwork, as similar to a *res* to be administered.”).

24 *Diet Drugs*, *id.* at 235.

25 *Id.*, 282 F.3d at 235; *Coast Line R.R. Co. v. Bhd of Locomotive Engrs.*, 398 U.S. 281, 295 (1970).

26 “The threat to the federal court’s jurisdiction posed by parallel state actions is particularly significant where there are conditional class certifications and impending settlements in federal actions. Many – though not all – of the cases permitting injunctions in the complex litigation cases involve injunctions issued as the parties approached settlement.... Complex cases in the later stages – where, for instance, settlement negotiations are underway – embody an enormous amount of time and expenditure of resources. It is in the nature of complex litigation that the parties often seek complicated, comprehensive settlements to resolve as many claims as possible in one proceeding. These cases are especially vulnerable to parallel state actions that may ‘frustrate the district court’s efforts to craft a settlement in the multi-district litigation before it.’ *Carlough*, 10 F.3d at 203 (quoting *Baldwin-United*, 770 F.2d at 337), thereby destroying the ability to achieve the benefits of consolidation.” *Diet Drugs*, 282 F.3d at 236.

27 101 F.3d 1196, 1202 (7th Cir. 1996).

28 764 F. Supp. 743, 745-46 (D. Conn. 1991).

29 764 F. Supp. at 746.

In *Winkler v. Eli Lilly & Co.*, on appeal arising out of the *Prozac* MDL proceedings, the Seventh Circuit faced the issue of “whether a federal court has the authority to protect the integrity of a discovery order” in the Anti-Injunction Act/All Writs Act context.³⁰ The *Winkler* court noted the “strong and long established policy against forum shopping,” which balance the Anti-Injunction Act “principles of federalism and comity,” and acknowledged that the “district courts’ power to control multidistrict litigation is established by statute, 28 U.S.C. Section 1407, and . . . with that power comes the duty to exercise it as efficiently as possible . . . an important aspect of that control is to prevent predatory discovery, especially of sensitive documents, ensuring that litigants use discovery properly as an evidence gathering tool, and not as a weapon. . . . Indeed, an express purpose of consolidating multidistrict litigation for discovery is to conserve judicial resources by avoiding duplicative rulings. Where a litigant’s success in a parallel state court actions would make a nullity of the district court’s ruling, and render ineffective its efforts, especially to manage the complex litigation at hand, injunctive relief is proper.”³¹

Adding to this observation the district court’s express powers of the All Writs Act to issue “such commands as may be necessary or appropriate to effectuate and prevent the frustration of orders it has previously issued in the exercise of jurisdiction otherwise obtained,” and the court’s established parallel construction of the “aid of jurisdiction” language of both the Anti-Injunction and All Writs Acts, the *Winkler* court concluded: “Consequently, we believe the two statutes in concert permit a district court, under certain circumstances, to issue an injunction to safeguard a pre-trial ruling like the discovery order at issue here.”³²

The specific injunction in *Winkler* was overturned, not as an improper injunction, *per se*, but on an abuse of jurisdiction standard, as unnecessarily broad, because it went beyond “those persons (and their counsel) whose cases are presently part of federal multidistrict litigation, or who were properly part of such multidistrict litigation at the time the ruling in question was made.”³³ Where the defendant’s documents are involved, this limitation presents no problem: a federal court can issue an order to protect such from inconsistent (or even duplicative) discovery forays. A defendant named in federal multidistrict litigation may find a haven there from “predatory discovery” proceedings in state courts.

Those courts entrusted with MDL and other complex proceedings are currently investing thousands of judicial hours grappling with the challenges of electronic discovery, including an increase in the sheer volume of data that is subject to discovery requests. Privilege logs, for example, may now include thousands rather than scores of documents, and the trial preparation process that the courts are called upon to manage can bog down in a privilege backlog. A privilege log, and the documents to which it refers (whether they are tangible or virtual) is arguably a *res*, and the division of its contents into privileged and non-privileged categories, once accomplished via the investment of substantial sweat equity, ought to be *res judicata*.

The recent experience of the *Vioxx* MDL court is illustrative. In *In re Vioxx Prod. Liab. Litig.*, 501 F. Supp. 2d 789 (E.D.La. 2007), the court describes a situation in which it was faced with privilege disputes involving over 30,000 documents. After the Fifth Circuit had vested the transferee court’s own privilege determination (based upon a document-by-document review), a court-appointed special master reviewed and made recommendations on a representative sample of the documents. The parties shared the considerable costs of this process, which resulted in a determination that the bulk of the documents were non-privileged and subject to production. This investment of judicial and litigant resources in the determination of the discoverability of, and the resulting sweat equity in “documents” which were mostly “print-outs of electronic communications, primarily internal company e-mails and attachments gives renewed currency to the *in rem* analogy “at the dawn of the age of electronic discovery.” 501 F. Supp. at 790.

30 101 F.3d at 1202.

31 *Id.*, citing *Marrise v. Am. Academy of Ortho. Surgeons*, 726 F.2d 1150, 1161 (7th Cir. 1989), *rev’d on other grounds*, 470 U.S. 375 (1989), and *Matter of Orthopedic Bone Screw Prod. Liab. Litig.*, 79 F.3d 46, 48 (7th Cir. 1995).

32 101 F.3d at 1203.

33 *Id.*

VI. CONCLUSION

In the age of paper discovery, courts designated to preside over complex litigation had literal *in rem* jurisdiction over the physical depositories of documentary evidence, located within their territory, and entrusted to administration by court-appointed counsel.³⁴ This jurisdiction was taken for granted, unremarkable (and unremarked upon), and the transition to d-discovery (and virtual depositories) was heralded as an opportunity for substantial court savings and increased convenience: documents could be everywhere at once.³⁵ Only now are we coming to grips with the collateral challenge of jurisdiction and enforcement occasioned by documents more mobile than the persons who authored them. The need for orderly and consistent adjudication of disputes over the relevance or privileged status of virtual documents may call for the exercise of virtual *in rem* jurisdiction.

The federal courts' development of the *in rem* analogy to embrace complex litigation itself as "the virtual equivalent of a *res*"³⁶ was based in part on the quantity of documentary evidence and discovery itself (including depositions) that featured in the judicial case management of complex litigation, whether class actions, mass torts, or MDLs. Now that e-discovery untethered to a particular place, and occupying only virtual space, has become the norm, this complex task has literally taken on an additional dimension. This in turn arguably heightens the necessity, and hence the force, of the virtual *in rem* jurisdiction concept.

The "complex litigation as *res*" analogy, which enabled courts, considering All Writs Act injunctions to preserve the integrity of their rulings against contradictory or inconsistent decisions in parallel proceedings, to ground such extreme judicial acts on a traditional *in rem* foundation, did not spawn an avalanche of injunctive writs. Despite, or because of, its power, the All Writs Act has been used sparingly over the years, only after efforts at informal coordination and inter-court accommodation failed.

Applying the *in rem* analogy to discovery would be equally unlikely to touch off an injunction tsunami, especially as the federal courts have increasingly recognized the great advantages of active federal/state court coordination, particularly in multi-jurisdictional mass torts.³⁷

What recognition and revival of the virtual *in rem* analogy has the potential to accomplish, if applied to the discovery context, is a reduction in the cost, waste, delay and gamesmanship of discovery disputation, as litigants recognize that the new protections of the federal discovery provisions will be applied consistently and enforced centrally, by a single court taking charge of the discovery process and product as recognized components of a complex litigation *res*.

34 See, e.g., *Manual for Complex Litigation, Third* (Federal Judicial Center 1995), Section 21.444 Document Depositories. The latest edition of the *Manual* replaces much of the discussion of physical depositories with the observation that "techniques such as CD-ROM and the Internet reduce the need for physical storage facilities, inspection, and copying." *Manual for Complex Litigation, Fourth* (Federal Judicial Center 2004) Section 11.444 at p. 77.

35 *Id.* At p. 28.

36 *Diet Drugs*, 282 F.3d at 235; *Baldwin-United*, 770 F.2d at 337.

37 See, e.g., *In re: Vioxx Prod. Liab. Litig.* (MDL No. 1657), 2008 U.S. Dist. LEXIS 95097, *7 (E.D. La. 2008); *Manual For Complex Litigation, Fourth*, Sections 20.3; 22.4.

E-DISCOVERY, PRIVACY, AND THE TRANSFER OF DATA ACROSS BORDERS: PROPOSED SOLUTIONS FOR CUTTING THE GORDIAN KNOT

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Summary

Globalization has “shifted into warp speed.”² Individuals and businesses now collaborate and compete at a breakneck pace and information has become the new global currency. The ease with which electronic information is now created, moved, and stored, however, places profound stress on the existing international discovery system. This paper calls for the recognition of a practical solution to the issue of litigation discovery and cross-border data transfer between the United States, the European Union, and elsewhere. Finally, this paper also calls for a re-writing of the Hague Evidence Convention. It is time for a modern, global and effective solution.

Introduction

Here is the scenario. You are an in-house counsel or a retained litigator that represents a large company in the United States. The client, though, like so many companies, now does business all over the world. It has offices in Europe, Asia, Latin America, and Australia. The employees at this company are technologically sophisticated. They demand smart phones and unified messaging. They want their voicemails delivered to their email inbox and hand-held devices. They “twitter” and belong to social networking sites. They work on virtual teams and many employees have not seen the inside of an actual office for years. In short, this hypothetical company is a lot like every fast-moving, quick thinking, and globalized company in the world: hungry for information and armed with the financial capital to make things happen.

Now imagine the following: this company, your client, gets sued in the United States. The lawsuit is filed in federal court and not long after the lawsuit is filed your adversary requests a meaningful meet-and-confer under Rule 26(f) of the Federal Rules of Civil Procedure. They want to talk e-discovery. They want to talk location of servers, back-up tapes, hold order systems, unified and instant messaging, and global retention and record preservation policies. They are interested in the data created by your employees who sit in cafes in Paris, while sending messages to customers in Dubai, and using a shared database that sits on a server in Singapore. Put simply, they know what they want, you know they will likely request it under the broad U.S. Federal Rules of Civil Procedure, and you also know it is going to cost you millions of dollars to preserve, collect, process, and review it.

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2 See Thomas Friedman's *The World is Flat: A Brief History of the Twenty-First Century* (2005).

As a sophisticated litigator and practitioner, you know that there are data privacy laws and “blocking statutes” that prevent you from simply collecting the electronic data of the company’s employees located in Europe, Asia, Latin America, and Australia. As a result of these restrictions, the normal rules of collection, processing, and review that apply in the United States do not apply here. Further, as in all litigation, time is not on your side. You need to access this data quickly, assess the strengths and weaknesses of your case, and determine if there is any truth to the allegations brought by your adversary. In order to do this, though, you are going to have to make sense of EU data privacy laws, country specific data privacy laws, and blocking statutes that may subject you to civil or criminal penalties if violated. In short, you need a practical solution to a complicated problem that, until recently, did not really exist on such a large scale.

In the past, practitioners faced with conducting discovery abroad usually turned to The Hague Evidence Convention,³ the Restatement on Foreign Relations,⁴ or the Restatement on Conflict of Laws.⁵ The problem is that these tomes and principles were not drafted with an eye towards our new globalized world. While they contain important ideas and wisdom on the underlying considerations involving taking discovery from abroad, none of these treaties or guides offers a practical, workable, and quickly deployable solution.

On February 11, 2009, the Article 29 Working Party published a paper entitled: “Working Document 1/2009 on pre-trial discovery for cross border civil litigation”⁶ (hereinafter referred to as WP 158). Acknowledging the horns of the dilemma that threaten to gore so many EU corporations and EU affiliates of US corporations, the Working Party in WP 158 proposes guidance to aid those multinationals caught between US cross-border discovery obligations and EU data protection and privacy laws.

Those hoping for absolution through the Working Party’s efforts, however, will be disappointed. Its guidance, the Working Party explained, was made in recognition “. . . that the parties involved in litigation have a legitimate interest in accessing information that is necessary to make or defend a claim, but this must be balanced with the rights of the individual whose personal data is being sought.” While understanding the seemingly inconsistent obligations that arise when cross-border discovery requires access to or disclosure of protected personal data, the Working Party is also mindful of the limitations on its own authority. As stated by the Working Party:

Although this paper sets out guidelines it is to be noted that resolving the issues of pre-trial discovery is beyond the scope of an Opinion by the Working Party and that these matters can only be resolved on a governmental basis, perhaps with the introduction of further global agreements along the lines of the Hague Convention.

In short, the Working Party, while wanting to help, is not in the business of giving corporations a “free pass” to ignore EU privacy obligations only because US discovery laws are in conflict. On the other hand, through its guidance, the Working Party does demonstrate that, in appropriate circumstances, and with appropriate measures in place to safeguard personal data, a certain level of harmonization is achievable.

The question of how data controllers reach this place of peaceful coexistence is the focus of this paper and, while not perfect, a possible solution is suggested. This paper will also propose

3 The Convention on the Taking of Evidence Abroad in Civil or Commercial Matters (otherwise known as the “Hague Evidence Convention”) is a multilateral treaty that was signed by the U.S. in 1970. The Hague Evidence Convention offers optional procedures in the form of minimum standards with which contracting states agree to comply in order to facilitate the taking of evidence abroad. It “does not modify the law of any contracting state [including the Federal Rules of Civil Procedure], require any contracting state to use its procedures either in requesting evidence or in responding to requests, nor compel any contracting state to change its own evidence gathering procedures.” *Société Nationale Industrielle Aérospatiale v. U.S. District Court for the Southern District of Iowa*, 482 U.S. 522, 534 (1987). Under the Convention parties may seek a Letter of Request or Letter Rogatory be sent from the Convention authorities to a foreign court to compel production of evidence. However, this procedure may be “unduly time consuming and expensive, as well as less certain to produce needed evidence than direct use of the Federal Rules.” *Id.* at 542.

4 The Restatement (First and Second) of Foreign Relations was originally drafted in 1962 and later revised in 1965. The Restatement (Third) of Foreign Relations was published in 1986.

5 The Restatement (First) Conflict of Laws was originally drafted in 1934 and was later revised in 1971.

6 Working Paper, Working Document 1/2009 on Pre-Trial Discovery for Cross-Border Civil Litigation, 00339/09/EN, WP 158 (Feb. 11, 2009) [hereinafter WP 158] (this is a working document and initial consideration for public comment). The paper can be found at: http://ec.europa.eu/justice_home/fsj/privacy/docs/wpdocs/2009/wp158_en.pdf.

the idea of a single document – a Certificate of Compliance for the Transfer of Personal Data Across Borders – that will attempt to memorialize the protections contemplated by European Union data privacy experts and governments when data is collected and processed in the European Union for purposes of responding to discovery requests or governmental investigations in the United States. In the meantime, the authors echo the Working Party’s admonition that a more perfect solution lies in “further global agreements” by the governments on both sides of the Atlantic. This paper concludes with a suggested strategy that may help lead towards that sort of international stipulation between nations.

The Recent Article 29 Working Party Paper

Our analysis of WP 158 starts with the candid admission that our interpretation may not accurately reflect the intent of the Working Party. We think it unlikely, however, that the Working Party would acknowledge the heightened pressure on multinational corporations to comply with seemingly inconsistent laws, introduce their writing with the stated purpose of providing “guidance,” but then fail to provide a viable path out of the labyrinth. In our view, the Working Party has come to the conclusion that a balance is attainable between the individual’s privacy rights in the European Union and the multinational’s need to prosecute a legal claim or defend itself against a cause of action in the United States. This balance, we think, is attainable by taking reasonable precautions to safeguard personal data along the lines described by the Working Party.

Permissible Processing

To begin with, the Working Party clearly identifies the act of preserving personal data for litigation purposes as constituting “processing” under the Directive but recognizes that, under appropriate conditions, this processing may be legitimized.⁷ Article 7 of the Directive sets out the limited circumstances under which personal data may be processed and, for each ground stated, its scope and procedural requisites. Three of the various circumstances described in Article 7 appear to permit processing for US discovery purposes but, as the Working Party points out, two of these are illusory.

Consent of the data subject, for example, will permit a data controller to process the data subject’s personal data pursuant to Article 7(a). The Working Party discourages “consent” as a valid means of legitimizing the processing of data, however, because it is difficult to obtain truly voluntary consent under the strictures of Article 2(h) and because the data subject retains the right to withdraw consent at any time, which is antithetical to the US discovery process.⁸

A second possible but equally unattainable form of legitimizing the processing of personal data is under Article 7(c), which permits processing if “necessary for compliance with a legal obligation to which the controller is subject.” The Working Party notes, however, that this channel is available only where the legal obligation arises from application of the law of a Member State.⁹ In other words, as has been previously found by the Working Party, the “legal obligation” that is the condition precedent of Article 7(c) does not include within its definition a US law or court order, except when that law or order is enforced through an EU judicial authority pursuant to the Hague Convention.¹⁰ Further, a multinational subject to a US preservation obligation typically does not have the year or more it will take to get relief through the Hague. Article 7(c), consequentially, is of little use to the multinational, especially for preservation purposes, when “processing” in the form of a litigation hold is immediately required upon learning of litigation or recognizing that litigation is reasonably likely.

⁷ *Id.* at p. 8.

⁸ *Id.* at p. 9 (“relying on consent may . . . prove to be a ‘false good solution’, simple at first glance but in reality complex and cumbersome.”) (quoting from Working Document on Common Interpretation of Article 26 (1) of Directive 95/46/EC of 24 October 1995, at p. 11, 2093/05/EN, WP 114 (Nov. 25, 2005) [hereinafter WP 114].

⁹ *Id.* at p. 9.

¹⁰ Working Party, Opinion 1/2006 on the Application of EU Data Protection rules to Internal Whistle-blowing Schemes in the Fields of Accounting, Internal Accounting Controls, Auditing Matters, Fight Against Bribery, Banking, and Financial Crime, at 9, 00195/06/EN, WP 117 (Feb. 1, 2006) [hereinafter WP 117] (citing Privacy Directive Article 6.); Working Party, Opinion 10/2006 on the Processing of Personal Data by the Society for Worldwide Interbank Financial Telecommunication (SWIFT), at 21, 01935/06/EN, WP 128 (Nov. 22, 2006) [hereinafter WP 128].

The last of the three exceptions under Article 7 raised by the Working Party holds the most promise and seems to be the recommended course of action. Article 7(f) recognizes as lawful the processing of personal data if “necessary for the purposes of legitimate interests pursued by the controller or by the third party or parties to whom the data are disclosed, except where such interests are overridden by the interests for fundamental rights and freedoms of the data subject.”

It is helpful here that the Working Party has previously recognized that a US legal requirement constitutes a “legitimate interest” for purposes of Article 7(f).¹¹ The Working Party in WP 158 reiterates that earlier position, this time specifically recognizing that a US discovery order may be sufficient to permit processing pursuant to Article 7(f), albeit within certain limitations:

Compliance with the requirements of the litigation process may be found to be necessary for the purposes of a legitimate interest pursued by the controller or by the third party to whom the data are disclosed under Article 7(f).

But that does not end the inquiry. For processing to be lawful under Article 7(f), the “legitimate interests” of the controller or third party must not be ‘overridden by the interests for fundamental rights and freedoms of the data subject.’¹² This balancing test, according to the Working Party, requires consideration of proportionality, relevancy to the litigation and the consequences to the data subject.¹³ Moreover, if the balancing test tips in favor of the data controller, adequate safeguards need to be put in place.

Proportionality

In order to use the “legitimate interests” grounds of Article 7(f) as the means for processing personal data in response to US discovery, the data controller must comply further with Article 6 of the Directive, which requires that the personal data must be:

- (a) processed fairly and lawfully;
- (b) collected for specified, explicit and legitimate purposes and not furthered processed in a way incompatible with those purposes;
- (c) adequate, relevant and not excessive in relation to the purposes for which they are collected;
- (d) accurate; and,
- (e) kept in a form which permits identification of data subjects for no longer than is necessary for the purposes for which the data were collected for which they are further processed.

The Working Party envisions a process where the proportionality of Article 6 may be satisfied by the data controller through its active management of the process; steering a course towards harmonization by employing such measures as petitioning the US court for appropriate limitations on the discovery of personal data through protective orders; engaging third party neutrals in the European Union to “filter” or narrow the scope of what will be further processed and possibly disclosed; and, involving data protection officials early, presumably to liaise with affected data subjects and confirm personal rights are honored.¹⁴

11 See WP 128, note 10, p. 18. (Where an entity was subject to both US and EU jurisdictions, “[i]t cannot be denied that SWIFT has a legitimate interest in complying with subpoenas under U.S. law.”)

12 WP 158, note 6, p. 9 (quoting from the Directive, Article 7(f)).

13 *Id.* at p. 10.

14 *Id.* at pp. 10-11.

Adequate Safeguards

When the “legitimate interests” of the data controller, viewed through the prism of proportionality, favor processing of personal data, the Directive requires that certain safety measures are in place for the protection of the data subject. The “adequate safeguards” that justify processing of personal data are described by the Working Party in various parts of the Opinion and include:

- (1) maintaining shorter retention periods relative to personal data to reduce the number of personal data records that may exist at the time a litigation hold is issued;
- (2) achieving transparency pursuant to Articles 10 and 11 of the Directive, meaning:
 - (a) giving data holders advance, general notice of the possibility of their personal data being processed for litigation;¹⁵ and,
 - (b) identifying to the data subject any recipients of their data, the purposes of the processing, the categories of data concerned and the existence of the data subject’s rights in those cases where personal data is actually processed for litigation purposes;¹⁶
- (3) providing notice that the data subjects have the right to object to processing pursuant to Article 14 of the Directive;¹⁷ meaning the data controller must additionally provide information concerning:
 - (a) the right to object at any time on compelling legitimate grounds to the processing of data related to the data subject;¹⁸
 - (b) the existence, purpose and functioning of its data processing;¹⁹
 - (c) the recipients of the personal data;²⁰ and,
 - (d) the right to access, rectification and erasure of the personal data pursuant to Article 12;²¹

(The Working Party further advises that the appropriate data protection authorities should be notified of the proposed processing activities);²²
- (4) considering the use of culling to separate the relevant from the irrelevant so that “a much more limited set of personal data may be disclosed as a second step”;²³
- (5) considering whether culling may be conducted by a trusted third party in the European Union to reduce the number of personal records to be processed;²⁴
- (6) considering whether personal data should be anonymised or at least pseudoanonymised to protect the data subjects identity;²⁵

15 *Id.* at p. 11.

16 *Id.*

17 *Id.* at p. 10.

18 *Id.* at p. 18.

19 *Id.*

20 *Id.*

21 *Id.* at p. 12 (recognizing the friction between a data subject’s right to modify data and the US discovery obligation to preserve, the Working Party suggests that the burden is on the party receiving the data to petition the US court for the appropriate protective order).

22 WP 128, note 10, at p. 19.

23 WP 158, note 6, p. 10.

24 *Id.*

25 *Id.*

(7) recognizing that sensitive personal data should be managed under Article 8, which may require, for example, the express consent of the data subject to process sensitive personal data, as well compliance with any specific Member State requirements;²⁶

(8) recognizing that special categories of data, such as doctor/patient confidential materials, should be managed in exclusive ways, according to the applicable special obligations that apply in those circumstances;²⁷ and,

(9) ensuring that “. . . all reasonable technical and organizational precautions to preserve the security of the data to protect it from accidental or unlawful destruction or accidental loss and unauthorized disclosure or access” have been taken by the data controller, and, in this regard, the Working Party conveyed that:

(a) these requirements are to be imposed on law firms, litigation services, experts, court services and others involved with the litigation and having access to the personal data;

(b) the data controller would remain responsible for the resulting processes; and,

(c) notwithstanding the data controller’s ultimate responsibility, third party recipients should be bounded by the principles of the Directive, process the data only for the specific purposes for which it was collected, comply with the retention periods and maintain the data’s confidentiality.²⁸

Transfer to Third Countries

As we think the above analysis demonstrates, the Working Party has helped multinationals to identify a mechanism by which personal data that is truly relevant and necessary for US litigation may be processed by the data controller pursuant to Article 7(f) when adequate safeguards are in place. The final question is whether the same data may be lawfully transferred to the United States to fulfill the data holder’s legal obligations in discovery. The Working Party clearly answered this question in the affirmative. What is less clear by its guidance is which of the several procedural mechanisms are available to justify the transfer, or under what circumstances each transfer protocol may be used lawfully to transfer personal data.

The Working Party, for example, states its preference of the use of Binding Corporate Rules (BCRs) or Safe Harbor where a significant amount of data is to be transferred.²⁹ Neither of these, however, are traditionally viewed as valid transfer options when dealing with the fulfillment of US discovery obligations. BCRs are designed for use with regard to the transfer of personal data *within the same corporate group* at a multinational level.³⁰ Moreover, BCRs require approval by the national data protection authority having jurisdiction over the personal data in question, a condition that is not likely to exist in most cases when litigation arises. More to the point, the Working Party has made it clear in prior writings that BCRs cannot be used to justify onward transfers to third parties that are not part of the BCR corporate group.³¹

Reference to use of Safe Harbor as a transfer mechanism for US discovery purposes seems equally misplaced. Safe Harbor is a procedure designed to create the presumption of adequate data protection standards by signatory corporations and permits transfer amongst those corporations that are Safe Harbor recognized. Onward transfer to non-qualified third persons for discovery purposes is prohibited.³²

26 *Id.*

27 *Id.*

28 WP 158, note 6, p. 12.

29 *Id.* at p.13.

30 Working Party, Working Document: Transfers of Personal Data to Third Countries: Applying Article 26 (2) of The EU Data Protection Directive to Binding Corporate Rules for International Data Transfers, at 6, 11639/02/EN, WP 74 (June 3, 2003) [hereinafter WP 74].

31 *Id.* at p. 10-11 (“Transfers of personal data to companies outside the corporate groups would remain possible but not on the basis of arrangements put in place by legally enforceable corporate rules but on the basis of any other legitimate grounds under Article 26 of the Directive . . .”).

32 *U.S. Department of Commerce, Safe Harbor Privacy Principles* (July 21, 2000) (can be found at www.export.gov/safeharbor/SH_Privacy.asp).

Presumably in recognition of these limitations, the Working Party refers to the Hague Convention and “urges that this approach should be considered first as a method of providing for the transfer of information for litigation purposes.”³³ Proceeding under the Hague Convention, however, also has significant limitations, some of which the Working Party recognizes.³⁴

Perhaps in recognition of these limitations concerning BCRs, Safe Harbor, and the Hague Convention, the Working Party cautiously acknowledges that “[w]here the transfer of personal data for litigation purposes is likely to be a single transfer of all relevant information, then there would be a possible ground for processing under Article 26(1)(d) of the Directive where it is necessary or legally required for the establishment, exercise or defence of legal claims.”³⁵

Article 26(1) of the Directive identifies the exceptions to the rule of Article 25 that precludes onward transfer of personal data to countries not providing an adequate level of data protection.³⁶ Article 26(1)(d) permits such a transfer to a third country if “the transfer is necessary . . . for the establishment, exercise or defence of legal claims.”

The implication in WP 158 that discovery obligations imposed by US litigation justifies a transfer under Article 26 (1)(d) “for the establishment, exercise or defense of legal claims” is supported by a similar conclusion reached by the Working Party in its prior writing, in which it demonstrated the reach of this exception by referring hypothetically to the permitted transfer of personal data by an EU subsidiary to its US parent in defense of a claim brought by an employee of the parent in a US court.³⁷

It is also worth noting that in a prior writing the Working Party noted that “. . . this exception [Article 26(1)(d)] can only be applied if the rules governing criminal or civil proceedings applicable to this type of international situation have been complied with, notably as they derive from the provisions of the Hague Conventions of 18 March 1970 (“Taking of Evidence” Convention) and of 25 October 1980 (“Access to Justice” Convention).³⁸ While not clear, it is presumed that the Working Party does not mean by this reference that application must first be made to proceed under the Hague Convention but rather that all the same safeguards must be “complied with.” A contrary interpretation would be inconsistent with the Working Party’s current position that “urges,” but does not require, use of the Hague Convention when that procedure is potentially available.

An Imperfect Solution

In WP 158, the Working Party has plotted a course through the maze that stands before those multinational corporations caught between US discovery and EU data privacy laws. The Working Party’s philosophy appears to be that, although not easily traveled, at least one route can be safely negotiated largely by demonstrating respect for, and thereby achieving compliance with, the spirit and the letter of both sets of rules.

Two years ago, a number of data privacy and legal commentators called for a sort of hybrid approach to the above problem by suggesting a standardized set of “legal processes protocols.”³⁹ The proposed solution closely resembles the model suggested by the Article 29 Working Party. In an article published in *Privacy & Security Law*, Crosley *et al.* argued that “U.S. discovery processes are not necessarily antithetical to European values” and that the “debate has vastly overstated these differences.” More importantly, though, the authors offered a practical way forward; they maintained that “the key to a long term-solution to this issue is to achieve an understanding that the processing of EU personal data in compliance with U.S. discovery rules should be treated as legitimate when conducted within a framework of stringent legal process data protection controls.”

33 WP 158, note 6, p. 14.

34 *Id.* at p. 13 (“. . . not all Member States . . . have signed . . . and even if a State has signed it may be with reservations.”).

35 WP 158, note 6, p. 13.

36 WP 114, note 8, p. 6.

37 *Id.* at p. 15.

38 *Id.*

39 See “A Path to Resolving European Data Protection Concerns with U.S. Discovery,” Crosley, Raul, McNicholas, and Dwyer in *Privacy & Security Law*, Vol. 6, No. 41, (October 15, 2007).

Crosley *et al.*, further suggested that “[a] scheme of legal process protocols could well form the basis to initiate a dialogue with EU authorities . . .” and that these “protocols” could contain: 1) “extensive advance notice” and disclosure to employees (and any other data subjects); 2) a comprehensive “EU Data Protective Order” and/or “an EU Model Contract for data transfers incident to discovery;” 3) the use of a special Protective Order; and 4) the use of a Special Discovery Master. The authors contemplated that this protocol would provide “clear and complete” disclosure to the EU employees of multinationals that describe “the data processing method, identify prospective data recipients, and inform data subjects of their rights under applicable U.S. law and EU data protection laws . . . as well as the means for enforcing those rights.” The authors argued that “such disclosures may most easily take the form of a special section of, or addendum to, the company’s privacy policy . . .”

The authors then suggested that “a special protective order, issued by the U.S. Court, specifically to address EU data protection concerns about the processing of personal data during litigation” would also help effectuate the proportionality principle – or the idea that the data to be transferred be “adequate, relevant and not excessive in relation to the purposes for which they are collected and/or further processed.” Such a protective order could restrict the scope of the disclosures ordinarily allowed under U.S. discovery rules, possibly by allowing processing of EU documents containing personal data only when they are demonstrated to be directly relevant to the issues presented, as opposed to being merely “reasonably calculated to lead to the discovery of admissible evidence.”⁴⁰ Finally, and in order to ensure “transparency both to data subjects and EU data protection authorities” the protective order could contain, they suggested, the appointment of a “special discovery master to monitor compliance with EU data protection requirements.”

In the end, the mechanisms for data transfer mentioned above are all systemic. At their core, they are all compliance regimes that take time and infrastructure to implement. The hybrid approach proposed by Crosley *et al.* is creative but also seems to rely on approval by some greater authority and this seems a bit unwieldy. What we need is an easily deployed and self-authenticating approach: a single document that captures the spirit of compliance with data privacy but does not require layers of bureaucracy to implement. What we need is a new approach.

A New Approach: A Proposed Certificate of Compliance for the Transfer of Data Across Borders

While the suggested approach by Crosley *et al.* makes sense and certainly is better than the current state of affairs, the solution may be made even more pragmatic and simple to effectuate. For example, requiring a special master to oversee any transfer of personal data out of the EU will be cumbersome and unwieldy – whether in the context of litigation or even for an informal investigation. What would a multinational corporation do, for example, when faced with a U.S. government investigation involving the transfer of data from employees located in one of their offices in Europe but where no formal legal proceeding had been filed in the U.S.? Should the company or counsel hire a retired judge, as they might in the case of arbitration, and have that individual oversee the process? This would take time, resources, and would require educating someone on EU privacy and the local laws of the countries from where the data was being exported. In short, it would be unduly burdensome and, in the end, perhaps unworkable.

Adherence to any data privacy law, whether in the EU or in any other part of the world, is about compliance. Different countries have different views on what is public and private information. These ideas are fundamental. And as such, they are a function of national identity and the human experience as it has developed in that part of the world. Companies, however, now operate in every part of the world. And in order to conduct business in different parts of the planet, the individuals who run those companies need to be mindful, respectful, and *comply* with the laws and norms of the places in which they operate.

40 See U.S. Federal Rule of Civil Procedure 26.

What if a multinational company and its counsel could create a single document that addressed data privacy laws in the European Union (or elsewhere) but did not require them to simultaneously create an entire compliance program dedicated to the transfer of data out of the EU? The document, much like the Model Contract suggested by Crosley *et al.* above, would address the various requirements of the 95/46 Directive as well as the ideas set forth in WP 158, drafted by the Article 29 Working Party. It would also simplify the process for a company and its counsel so that compliance would be more likely because it would be self-authenticating.

Such a document – or a Certificate of Compliance for Transfer of Personal Data Across Borders (hereinafter “Certificate of Compliance”) – would accompany the data (like a modern day bill of lading that accompanies physical cargo) from one jurisdiction to another. Further, this document would be filed with the local DPA as evidence that the company and counsel that seek to transfer that data are aware of the data privacy laws of the country where the data resides, understand their obligations under those laws, and will *comply* with the data privacy restrictions of the country in which they operate.

The Certificate of Compliance would contain the following provisions: 1) a statement concerning the purpose for which the data is being collected and confirm that the data will not be used for any other purpose (this would include a brief description of the litigation, investigation, or matter in the U.S. as well as the recipient of the data); 2) a statement as to how and when the data will be collected (this would include time, date, by whom and with what technical tool the data will be collected); 3) that all reasonable measures are being taken in order to limit what data is being collected (for example, that search terms will be run against the data in order to narrow the data set to only the most relevant information and confirming that the non-responsive data will not be processed along with the responsive data); 4) an identification of the types of data that will be collected (e.g., email, Word documents, PowerPoint, etc.).

The Certificate of Compliance should also: 5) confirm that this data is subject to a protective order and include a copy of the protective order as an attachment to the Certificate of Compliance (the protective order should specifically mention the EU privacy law that governs the transfer of data and confirm compliance with same, limit the number of individuals who will have access to the EU-transferred data, and provide consequences if the data privacy law is not complied with); 6) set forth the resources available to the employee should they have questions about their privacy rights (at a minimum, this would mean identifying the appropriate DPA in the applicable country and a means to contact the DPA office); 7) confirm that all reasonable steps will be taken in order to protect the data from accidental or unlawful destruction; 8) confirm that a copy of the Certificate of Compliance has been filed with the proper DPA; and 9) identify and include the signature of the person responsible for overseeing the collection, processing, review, and production of the data (most likely the attorney overseeing the matter or the company’s privacy officer).

A Certificate of Compliance can, and should be, this straightforward and simple. As Crosley *et al.* have suggested, the current debate between complying with data privacy laws while still being able to conduct discovery under the U.S. federal rules has been “vastly overstated.” Companies that operate in the United States but with offices located abroad want to do the right thing. Until now, however, there has not been a workable solution to this conflict of legal obligations. Furthermore, the Article 29 Working Party “sees the need for reconciling the requirements of the US litigation rules and the EU data protection provisions. [And] [i]t acknowledges that the Directive does not prevent transfers for litigation purposes”⁴¹

A Certificate of Compliance is the first step. It is practical, easily deployed, and attempts to address the data privacy concerns raised by both the Directive and the recent paper by the Article 29 Working Party. What companies and their counsel really need, though, is a long term solution to a problem that will only continue to expand. The Hague Evidence Convention has the four walls and

41 See the Article 29 Working Party paper: “Working Document 1/2009 on pre-trial discovery for cross border Civil litigation,” at http://ec.europa.eu/justice_home/fsj/privacy/docs/wpdocs/2009/wp158_en.pdf.

the beginning of a solid foundation upon which to build a meaningful multi-lateral treaty for collecting electronic evidence from abroad. But the treaty needs a renovation. It needs to read like a modern document that understands how information moves, is stored, and can be collected with the click of a button. The next part of this paper is a look at the current Hague Evidence Convention, its use or non-use, and makes some suggestions of what a new treaty should look like.⁴²

A Long Term Solution: Rethinking the Hague Evidence Convention

In terms of its usefulness to conduct e-discovery across borders, the Hague Evidence Convention is in dire need of help. The treaty suffers from a number of failings, some self-imposed, some imposed by interpreting bodies. First, and in light of the U.S. Supreme Court's decision in *Aérospatiale*, the treaty has essentially become "discretionary" for U.S. and foreign litigants in U.S. courts.⁴³ Second, Article 23 of the treaty specifically permits a contracting State to "declare that it will not execute Letters of Request issued for the purpose of obtaining pre-trial discovery of documents as known in Common Law countries."⁴⁴ Third, the Convention does not take into consideration the data privacy laws of many countries. Fourth, the Convention does not offer a solution to the issue of "blocking" statutes. Finally, requests for e-discovery under the Convention are "rare"⁴⁵ and the Convention offers no real guidance for conducting e-discovery abroad.

In 1970, the United States signed on to the Hague Convention on the Taking of Evidence Abroad in Civil and Commercial Matters. Pursuing discovery through this treaty, it seemed, would establish a formalized process for conducting discovery abroad. But that was not to be. In *Aérospatiale*, a French aircraft manufacturer, defending a plane crash case in Iowa, argued that the Convention was the sole means of gathering evidence within the territories of the contracting countries, including France and the United States.⁴⁶

After determining that the Convention was not a preemptive replacement for the Federal Rules, the Supreme Court considered two possibilities: first, that international comity required "a first resort" to use of the Convention procedures; or second, that the Convention contains alternative procedures which American courts have the option of employing.⁴⁷ With a narrow 5-4 split, the Court rejected a rule requiring "first resort to Convention procedures" and instead held that in each case trial courts determine whether to apply Convention procedures or the Federal Rules after considering three things: "(1) the particular facts, (2) sovereign interests, and (3) the likelihood that resort to [Convention] procedures will prove effective."⁴⁸

In May 2008, the Permanent Bureau of the Hague Conference on Private International Law issued a questionnaire to Member States and State Parties in preparation for the Special Commission Convention which was held in February 2009. The goal of the questionnaire and the convention were to define key issues facing the Hague Evidence Convention as well as "assist the Permanent Bureau in drafting parts of a possible new edition of the Practical Handbook on the Operation of the Evidence Convention and/or a possible Guide to Good Practice" in relation to specific issues arising from the operation of the Convention.⁴⁹

The Permanent Bureau drew a number of interesting conclusions from the responses to the questionnaire. Among them, the Bureau found that "the statistics provided by responding States do

42 As the Article 29 Working Party acknowledged in the 11 February 2009 white paper: "Although this paper sets out guidelines it is to be noted that resolving the issue of pre-trial discovery is beyond the scope of an Opinion by the Working Party and that these matters can only be resolved on a governmental basis, perhaps with the introduction of further global agreements along the lines of the Hague Convention."

43 In *Société Nationale Industrielle Aérospatiale v. United States District Court*, 482 US 522 (1987), the Supreme Court determined that the Hague Convention did not displace the Federal Rules in relation to foreign-based discovery; rather, it was a permissive supplement. See also "The Mandatory/Non-Mandatory Character of the Evidence Convention" issued by the Permanent Bureau of the Hague Conference on Private International Law, 10 December 2008.

44 See Article 23 of the Hague Evidence Convention.

45 See "Summary of Responses to the Questionnaire of May 2008 Relating to the Evidence Convention, with Analytical Comments," drawn up by the Permanent Bureau, February 2009 at http://www.hcch.net/index_en.php?act=text.display&ctid=48.

46 *Id.* at 524-525, 529.

47 *Id.* at 529, 533.

48 *Id.* at 538, 544.

49 See p. 4 of "Summary of Responses to the Questionnaire of May 2008 Relating to the Evidence Convention, with Analytical Comments," (hereinafter "Summary Report") drawn up by the Permanent Bureau, February 2009 at http://www.hcch.net/index_en.php?act=text.display&ctid=48.

not permit many firm conclusions to be drawn, however it is possible to say with some confidence that the Convention appears to be widely used, with, at very least, over 1500 uses of Chapter I, and 2500 uses of Chapter II, in 2007.⁵⁰ The Bureau also found that the “high use of the Convention is reflected in a high level of overall satisfaction with the Convention.”⁵¹ Finally, the Bureau made a number of important recommendations regarding the timeliness of responding to Letters of Request (4 months if the request was for oral evidence and 6 months for “all other requests.”).

The report also included a number of observations on e-discovery and blocking statutes. It found that “requests for e-discovery are rare, but are becoming a reality.”⁵² The report noted that “some such requests have been successfully executed . . . [but] very few data are available on the practical difficulties that can arise in respect of such requests.”⁵³ The report then concluded that “requests for discovery relating to electronically stored information are likely to increase . . . [and that] such requests should be treated in the same manner as requests for hard copy documents.” As for blocking statutes, the report noted that “blocking statutes are reasonably common, but far from universal. [W]here they do exist, such Statutes are rarely used.”⁵⁴

Unfortunately, what the report did not include are practical solutions to the issue of conducting e-discovery across borders. In light of a recent French Supreme Court decision,⁵⁵ it also likely underestimates the likelihood that States will begin to enforce their blocking statutes where they are made aware that protected information is being disclosed pursuant to a foreign court proceeding. What, then, should the Bureau have recommended in terms of conducting e-discovery abroad? What should it have recommended in terms of blocking statutes?

A new Hague Evidence Convention needs to do more than just “recognize” e-discovery, blocking statutes, and data privacy concerns around the globe. While the details of a new international treaty is too ambitious for this paper and outside of its intended scope, we applaud the Working Party’s recognition that a more perfect solution to the cross-border discovery conundrum lies in “further global agreements” between the EU, US and other sovereignties. We believe that any real long term solution mandates immediate steps in that direction.

We think, as well, that to begin to construct a workable multinational accord, a concerted analysis is needed to determine the shortcomings of today’s Hague Convention. We believe that by studying what has not worked, and the frustrations experienced by multinationals trying to comply with seemingly inconsistent laws, the best resolution can be obtained, and a new Hague Evidence Convention can rise like a phoenix from the ashes.

We therefore suggest that the contours of any new treaty or modifications to the Hague Convention begin with at least the following considerations:

1. The process for application to the international tribunal to aid in cross-border discovery or transfer of data must be simple, expeditious, reliable and repeatable;
2. The determinations made by the international tribunal must be prompt, capable of enforcement and willingly enforced by the signatory countries;
3. *Aéropatiale* must be abandoned or at least set aside in those cases where application is made to the international tribunal for enforcement of discovery orders;

50 Interestingly, of the 1500 requests under Chapter I, 477 of those requests were for oral testimony, 215 of the Requests for documentary evidence, 77 requests for bank records, and 55 requests were for written interrogatories. In short, the majority of the requests did not involve e-discovery. See p. 16 of the Summary Report.

51 See page 6 of the report. Interestingly, when one looked at the actual responses of the Member states a slightly different story also emerged. For example, in responding to the question: How do you rate the Convention? India responded: “Excellent. Prima-facie the objects of the Convention appear to be excellent. However since no request have been received for execution under the Convention, no specific comments can be provided at this stage.” For a full copy of the Member State responses go to: <http://hcch.e-vision.nl/upload/wop/2008synopsis20.pdf>.

52 See page 51 of the Summary report.

53 *Id.*

54 See p. 26 of the Summary Report.

55 Cour de Cassation Chambre Criminelle [Cass. Crim.], Paris, Dec. 12, 2007, Juris-Data no. 2007-332254 (France’s Supreme Court upheld criminal conviction and fine against French attorney for conducting a private investigation on behalf of US litigants, finding that information sought was of an economic, financial, or commercial nature and was aimed at collecting evidence for use in a foreign judicial procedure).

4. Blocking statutes must be abandoned or at least set aside in those cases where application is made to the international tribunal for enforcement of discovery orders;
5. The laws of each signatory country must be respected but compromise also must be expected so that fairness and reasonableness should always prevail; and,
6. When the scope of discovery in one country encroaches on the rights of individuals of the another country, those courts involved and the international tribunal should resort to a tiered approach that prioritizes discovery on a sliding scale basis. This means, for example, that discovery that is least objectionable and mostly of a business nature should be made available first and based on broad concepts of relevancy and materiality. Discovery that infringes on individual rights should require a higher burden of persuasion and would be permitted pursuant to a more narrow scope as to what is relevant and material. Discovery that seeks highly sensitive information of a private or delicate nature should not be permitted absent a showing of 'good cause,' meaning that the information is necessary, is not otherwise available from other sources and that the request is not intended to embarrass or harass.

Conclusion

These six concepts are familiar to courts in almost every country. As Crosley, *et al.* determined, we are not all that much different. Basic concepts of 'search for the truth' and 'respect for individual rights' are the cornerstones of the judiciaries of both the European Union and the United States. The differences, and therefore the friction, arise more because of a fear of the unknown. By developing an international framework that is speedy, reliable and one that fairly resolves cross-border discovery issues, consistent with data privacy rights, these biases, we are confident, will cease to exist.

Epilogue by The Sedona Conference®

On June 10-11, 2009 The Sedona Conference® held its International Programme on Cross-Border eDiscovery, eDisclosure & Data Privacy Conflicts in Barcelona, Spain. The preceding paper was presented at that conference and subject to dialogue by the almost 100 conference participants and faculty from The Sedona Conference®, the European Commission, various EU member state Data Protection Authorities, the US and UK judiciary, the US State Department, and the US National Archives and Records Administration, as well as lawyers and others from more than 10 countries.

The conference began with a keynote address by Dr. Alexander Dix, the Commissioner for Data Protection and Freedom of Information, Berlin, Germany, and Chair of the Article 29 Working Party Subgroup on Cross-Border Discovery. That was followed by a series of discussions regarding the recent Article 29 Working Party Document 158 on pre-trial discovery for cross border civil litigation, and the recently-published Sedona Conference® Framework for Analysis of Cross-Border Discovery Disputes (available free for download and personal use at www.thesedonaconference.org).

Day One of the conference continued with discussion of similar issues found within arbitration and ADR, including the sufficiency of ADR procedures to satisfy the privacy of data concerns and exceptions found in the EU Data Privacy Directive Article 29. There was also discussion of the four current data-transfer paradigms (the Hague Evidence Convention, the US Safe Harbor Program, Binding Corporate Rules, and Model Contracts) and the imminent Mutual Legal Assistance Treaty (MLAT), their applications and their limitations.

Day Two of the conference focused on practical solutions, with the preceding paper providing the background and stimulus for the dialogue. Thus, the participants reviewed and discussed the concept of a “certificate of compliance” with nine content and procedural elements that would address personal privacy, risk awareness, and data protection around specific collections of information.

After the conference, The Sedona Conference® held a short meeting of its International Working Group on Electronic Information Management, Discovery and Disclosure (WG6). At that meeting, it was agreed that WG6 would provide a formal response to the Article 29 Working Party Document 158, and, using the preceding article as a starting point, prepare a sequel to its Framework for Analysis paper focusing on practical solutions for accomplishing cross-border data transfers in civil litigation consistent with the EU Data Privacy Directive, and other statutes and rules governing pre-trial discovery and data transfers across borders.

CHANGING PRIVACY AND DATA PROTECTION IN JAPAN

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- I. Introduction
- II. The Culture of Privacy in Japan
 - (1) Privacy in a Communitarian Society
 - (2) The Rebirth of Privacy
- III. Data Protection in Japan
 - (1) Act on the Protection of Personal Information in 2003
 - (2) Recent Developments
- IV. Conclusion

I. INTRODUCTION

If privacy is a universal human need and fundamental human right, why does it take such diverse forms? The concept of privacy differs from place to place, from time to time, and from person to person. Since privacy laws in each country aim to reflect the social practices and values of that culture, no privacy advocate can achieve cross-border privacy protection without recognizing the norms of each culture.

We have been discussing what privacy means for more than a century. While there is some consensus as to the importance of privacy, the word “privacy” is currently used to describe a myriad of different things: information privacy, territorial privacy, and autonomy. In 1890, two lawyers from Boston, Samuel Warren and Louis Brandeis, defined privacy as “the right to be let alone.”² Since then, many scholars and lawyers have also attempted to define the concept. Whereas Americans understand privacy to mean control over knowledge about oneself,³ a form of self-interested economic behavior,⁴ anti-totalitarian right,⁵ we in Japan think in terms of the protection of private life as well as the right to control information regarding oneself in the context of society.

When we carefully examine the cultural background to each meaning of privacy, we may understand something more about privacy. For example, as I mentioned earlier, one of the first men to use the expression was Louis Brandeis, a Boston lawyer who later served as a Supreme Court Justice. What is more, Brandeis was Jewish. Brandeis’s work on privacy was clearly influenced by Jewish culture and the concept of *tikkun olam*, the duty each of us has to heal a broken world.⁶

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² Samuel D. Warren & Louis D. Brandeis, *The Right to Privacy*, 4 HARV. L. REV. 193, 196 (1890).

³ See e.g., ALAN WESTIN, *PRIVACY AND FREEDOM* 7 (1967); Charles Fried, *Privacy*, 77 YALE L. J. 475, 482-3 (1968).

⁴ See Richard A. Posner, *The Right of Privacy*, 12 GA. L. REV. 393, 409 (1978).

⁵ See Jed Rubenfeld, *The Right of Privacy*, 102 HARV. L. REV. 737, 787 (1989).

⁶ Erwin Chemerinsky, *Rediscovering Brandeis’ Right to Privacy*, 45 BRANDEIS L. J. 643, 643 (2007).

The aim of this article is not to seek a universal definition of privacy, but rather to introduce the culture of privacy which exists in Japan today. I will demonstrate, from my personal perspective, the dynamic aspects of privacy and data protection in Japan which have been emerging from evolving social practices and values, by introducing the Act of 2003 and some important recent developments.

II. THE CULTURE OF PRIVACY IN JAPAN

(1) Privacy in a Communitarian Society

Privacy is traditionally regarded as a concept of Western culture, but careful analysis of the Western understanding of privacy reveals slight differences between the European culture of privacy and that of America. At the conceptual core of privacy, "American privacy law is a body caught in the gravitational orbit of liberty values, while European law is caught in the orbit of dignity."⁷ In the United States, as recognized in *Griswold v. Connecticut*⁸ and *Katz v. United States*,⁹ social anxieties and ideals focus primarily on the police and other officials and around the ambition to secure the blessings of liberty, whereas the European privacy law we see today is the result of a centuries-long revolt against the style of status privileges, making Europeans more sensitive to matters of respect and personal dignity.

What about the Asian culture of privacy? In my view, Asian people formerly regarded privacy as a symbol of selfishness or self-centeredness. We have a long history of respecting and valuing the community and public. If privacy is understood to be based on individualism, then we did not have such a strong individualistic culture in Japan and therefore our awareness of privacy must have been relatively low. One famous motto of Japanese culture is "devoting oneself to the public, sacrificing one's private interests" (*messhi-hoko*). We have a long tradition of sacrificing private interests for the public good. For example, there is the history of *Bushi-do* (the Way of the Warrior), under which *samurai* fight not for their own interest, but for that of the *Shogun* (General), the head of the community.¹⁰ "Devoting oneself to the public, sacrificing one's private interests" is thus a virtue in Japanese culture. I would describe the Japanese culture of privacy as "privacy effected by the public." The tradition of a communitarian culture once embodied the obligations set by the members of a community to one another and defined the substance and boundaries of the distinction between public and private.¹¹

(2) The Rebirth of Privacy

While Japan has no long tradition of privacy, we have seen a rapid development in technology with a corresponding increase in the desire to protect privacy. In a landmark judgment in 1964, the Tokyo District Court recognized the right to privacy as "the legal right and assurance that one's private life will not be unreasonably disclosed to the public."¹² Japan later enacted its first privacy Act in 1988, at a time when many Asian countries had no such legislation. The 1988 Act on the Protection of Computer-Processed Personal Information Held by Administrative Organs responded to the changing needs of society in the face of the rapid advancements in technology. Finally, as we shall see in the next part, new, comprehensive legislation for the protection of personal information was enacted in 2003.

Several cases regarding privacy protection have also been dealt with by the Supreme Court. For example, in 1967, the Court held that individuals have the right not to be photographed without permission, as a freedom of private life.¹³ The Court also held that personal information, such as name, address, and telephone number, is legally protected as information regarding privacy, and such

7 See James Q. Whitman, *The Two Western Cultures of Privacy: Dignity Versus Liberty*, 113 YALE L. J. 1151, 1163 (2004).

8 381 U.S. 479 (1965) (The Court held that a state law prohibiting the use of contraceptives violated the zones of privacy).

9 389 U.S. 347 (1967) (The Court held that the police needed a warrant under the Fourth Amendment to wiretap).

10 For an eloquent work of Bushido, see INAZO NITOBE, *BUSHIDO, THE SOUL OF JAPAN* (1900). One interesting example mentioned by Nitobe is that "American husbands kiss their wives in public and beat them in private; the Japanese beat theirs in public and kiss them in private," which stands for their dignity as *samurai*.

11 Some discussion on the communitarian aspect of privacy can be seen in the United States. See, e.g., Robert C. Post, *The Social Foundations of Privacy: Community and Self in the Common Law Tort*, 77 CAL. L. REV. 957 (1989).

12 Judgment of Tokyo District Court, September 28, 1964, *Hanrei-jihō* Vol. 385, p. 12.

13 Judgment of Supreme Court, December 24, 1967, *Keishū* Vol.23 No12 p.1625.

information cannot be transferred to a third party without the individual's consent.¹⁴ Furthermore, the Supreme Court considered the privacy issues associated with the traffic-tracing technology known as "N system," which can search and find stolen or speeding cars among the millions traveling on roadways,¹⁵ and the fingerprinting of foreign residents.¹⁶

Throughout the last half-century, Japan clearly embraced a culture of privacy and recognized privacy as both a right and interest, notwithstanding the fact that there was no explicit constitutional provision for the protection of privacy.

III. DATA PROTECTION IN JAPAN

(1) Act on the Protection of Personal Information in 2003

On May 30, 2003, the Act on the Protection of Personal Information was finally enacted after a two-year controversy in the Diet, and entered into force in April 2005.¹⁷ As shown in the diagram below, the Act comprises two parts: Chapters 1 to 3 provide the basic ideals and principles covering both the public and private sectors, and Chapters 4 to 6 lay down the general obligations for the protection of personal information held by the private sector. The public sector is covered by the Act on the Protection of Personal Information Held by Administrative Organs enacted in 2003. These Acts are firmly rooted in the eight principles of the OECD Privacy Guidelines in 1980, supplemented by Basic Policy and 37 guidelines (as of April 2009) established by the relevant ministries.

Three distinctive features can be observed from the Japanese Act. First, the Act is effectively enforced by the relevant competent Ministers. Every Minister may collect reports from businesses, provide advice to them, or make recommendations and issue orders in the event of a data breach. In fiscal year 2007-08, there were 848 cases of unauthorized disclosure.¹⁸ The Cabinet Office further announced, after collecting reports from every ministry, that there were 83 cases concerning the collection of reports from business entities and no cases of recommendations or orders.¹⁹ Every case of data breach is judged by the competent Minister, who can carefully examine each field of business using his or her technical knowledge and experience.

Secondly, many ministries have authorized private business entities, which are called "authorized personal information protection organizations." The number of authorized organizations was 37 as of March 2009, and their role is to instruct and support protecting personal information for small businesses, ensure proper handling of personal information, and handle complaints in their own business sectors. For example, one of the organizations invented the PrivacyMark system, which is widely used in Japan for proving proper handling of personal information.

Finally, it is interesting to note, from the viewpoint of Japanese culture, that when a business leaks a large amount of personal information, the harm suffered is not the loss of control of personal information, but rather the disruption in its relationship with customers and the community. As we have a culture of apology, businesses which have leaked customers' information tend to apologize in advertisements placed in newspapers, and they are often willing to compensate without court orders.²⁰

In this way, we have seen autonomous efforts by businesses in the context of their relationship with society even after the Act entered into force.

14 Judgment of Supreme Court, September 11, 2003, *Minshu* Vol. 57, no. 8, p. 973.

15 Judgment of Supreme Court, February 14, 1986, *Keishu* Vol. 40, no. 1, p. 48 (The Court held that the N system did not violate the right to privacy).

16 Judgment of Supreme Court, December 15, 1995, *Keishu* Vol. 49, no. 10, p. 842 (The Court held that a person has the right not to be forced to provide his or her fingerprints, but the government had a legitimate interest in fingerprinting immigrants for the purpose of administering their residence).

17 Further details are available at the homepage of the Office of Personal Information Protection, Cabinet Office http://www5.cao.go.jp/seikatsu/kojin/index_en.html (last visited May 15, 2009).

18 See Cabinet Office, *Summary Report on the Implementation Status of Act on the Protection of Personal Information in FY 2007* (September, 2008) at 10. There were 893 cases of unauthorized disclosure in FY 2006, and 1556 in FY 2005.

19 *Id.* at 3. There were 60 cases of collection of reports and 4 cases of recommendation in FY 2006.

20 For example, Mitsubishi UFJ Securities leaked the information of about 50,000 customers in April 2009. They apologized in five newspapers and offered each customer JPY 10,000 (\$100) in compensation for mental distress.

(2) Recent Developments

Since the Act entered into force, we have seen several developments in privacy protection in Japan. I will introduce two recent developments in privacy protection: international obligations and the emergence of new technology.

As for international obligations, Japan is an active member of both the OECD and APEC, and the Government of Japan has been consistently working with these international organizations regarding privacy protection. In April 2008, the Government of Japan revised its Basic Policy in response to demands for the international harmonization of data protection, mentioning its support of the OECD recommendation on Cross-Border Cooperation in the Enforcement of Laws Protecting Privacy in 2007²¹ and the progress made in APEC and the EU. In particular, APEC launched the Data Privacy Pathfinder Project²² in June 2007, whose goal is to develop a system in the APEC region that ensures accountable cross-border flows of personal information for the protection of consumers while facilitating business access to the benefits of electronic commerce.²³ Of the nine projects, Japan has supported all but two of them (Project 4 & 8), which has not been substantially started as of December 2008, making use of the experience of the autonomous approach by businesses in Japan. We expect that the new projects of OECD and APEC will serve as an experiment for the cross-border protection and global flow of personal information.

Secondly, Japan has created many new technologies giving rise to privacy threats, including biometrics, RFID, surveillance, and other privacy-related technologies. For example, mobile phones can be used to access the Internet, pay rail and bus fares, and execute payments at some shops. Passports and driver's licenses contain IC chips, which enable the remote control of personal information. PINs are no longer needed for withdrawing cash from ATMs or entering rooms with restricted access at companies; instead, biometric checks serve to identify the individual. Recently, in terms of consumer protection, we have seen several protests against the Google Street View service by some local governments because Street View itself compromises privacy in the community. Both the national and local governments are seeking proper measures by setting some guidelines or voluntary rules regarding the use of new technology to ensure harmony and consistency with the Japanese culture of privacy.

IV. CONCLUSION

The main issue for privacy is the definitions of "self" and "other" in the particular culture.²⁴ In this paper, I have examined some special aspects of the Japanese culture of privacy from my personal perspective. We have seen that there have been some successful transplants of "privacy" from Western culture to Japanese business activities and the right to privacy is widely supported in citizens' everyday lives. On the other hand, its form may be somewhat different from its birth in Western culture, as seen from the reaction to cases of unauthorized disclosure, where social relationships are still of great importance.

Information flows across cultures, but privacy is deeply rooted in individual cultures. The task of creating rules for cross-border privacy is hard, but must be realized in the age of a global information community. Our task is not to realize the universal values of privacy which persist in every society, but rather to tolerate the differences between cultures of privacy in the process of developing cross-border privacy rules. We will be able to complete the task by recognizing the essence of privacy and its cultural background.

21 Available at <http://www.oecd.org/dataoecd/43/28/38770483.pdf> (last visited May 15, 2009).

22 The nine projects of APEC Data Privacy Pathfinder Project are (1) self-assessment guidelines for organizations, (2) private and public sector accountability agent recognition criteria, (3) compliance review process of CBPRs, (4) directories of compliant organizations and contact information of organizations and accountability agents for use by consumers, (5) contact directories for data protection authorities and privacy contact officers within economies, as well as with accountability agents, (6) templates for enforcement cooperation arrangements, (7) templates for cross-border complaint handling forms, (8) scope and governance of the CBPR system, and (9) a pilot program that can test and implement the results of the projects leading to the testing of a complete system.

23 The latest information regarding the Data Privacy Pathfinder Project is available at http://aimp.apec.org/Documents/2009/ECSG/SEM1/09_ecsg_sem1_027.doc (last visited May 15, 2009).

24 For an excellent empirical study of the Japanese culture of privacy, see Dan Rosen, *Private Lives and Public Eyes: Privacy in the United States and Japan*, 6 FL. J. INT'L L. 141 (1990).

THE SEDONA CONFERENCE®
COMMENTARY ON PRESERVATION,
MANAGEMENT AND IDENTIFICATION OF
SOURCES OF INFORMATION THAT ARE
NOT REASONABLY ACCESSIBLE

*A Project of The Sedona Conference® Working Group on
Electronic Document Retention & Production (WG1)
July 2008*

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* This Commentary was the subject of dialogue at three Working Group Meetings, and many Working Group Members submitted comments and edits as well. Thanks go to all who participated in the dialogue that led to this Commentary. In addition, we thank all of our Working Group Series™ Sustaining and Annual Sponsors, whose support is essential to our ability to develop Working Group Series publications. For a listing of our sponsors just click on the "Sponsors" Navigation bar on the homepage of our website.

This Sedona Conference® Commentary focuses on the decision making process relating to the preservation of sources of electronically stored information that may contain discoverable information that is “not reasonably accessible.”¹ The “reasonable accessibility” distinction - introduced by the 2006 Federal E-Discovery Amendments as part of the “two-tiered” approach to discovery - plays a role in, but is not wholly determinative of, preservation obligations.

The central dilemma of preservation planning in the absence of the opportunity to discuss discovery requests or reach prior agreement among the parties is predicting exactly which sources of information may actually be discoverable in a given case. No bright-lines exist.² The primary duty is to make reasonable assessments in good faith.³

To assist litigants and the courts, we have developed the following Guidelines that summarize our recommendations for making those assessments.⁴ The Guidelines also discuss how parties may “identify” inaccessible sources that will not be preserved and emphasize the value of cooperative efforts to reach agreements on preservation topics in dispute that reflect the unique demands of each case.

The Guidelines are:

Guideline 1. Where litigation is anticipated but no plaintiff has emerged or other considerations make it impossible to initiate a dialogue, the producing party should make preservation decisions by a process conforming to that set forth in the Decision Tree in Figure 1.

Guideline 2. As soon as feasible, preservation issues should be openly and cooperatively discussed in sufficient detail so the parties can reach mutually satisfactory accommodation and also evaluate the need, if any, to seek court intervention or assistance.

Guideline 3. In conjunction with the initial discussions or where appropriate in the response to discovery requests, parties should clearly identify the inaccessible sources reasonably related to the discovery or claims which are not being searched or preserved.

Guideline 4. A party should exercise caution when it decides for business reasons to move potentially discoverable information subject to a preservation duty from accessible to less accessible data stores.

Guideline 5. It is acceptable practice, in the absence of an applicable preservation duty, for entities to manage their information in a way that minimizes accumulations of inaccessible data, provided that adequate provisions are made to accommodate preservation imperatives.

Guideline 6. An entity should encourage appropriate cooperation among legal and other functions and business units within the organization to help ensure that preservation obligations are met and that resources are effectively utilized.

1 Rule 26(b)(2)(B) defines sources that are “reasonably accessible” as being so because of “undue burden or cost.” For convenience of reference, sources of this type are sometimes referred to herein as “inaccessible sources.”

2 The Advisory Committee decided that federal rulemaking should focus on mandating early discussion of preservation “issues” while providing targeted guidance [Rule 37(e)] for courts facing motions for sanctions.

3 *Texas v. City of Frisco*, 2008 WL 828055 (E.D. Tex. March 27, 2008) (“[W]hile they do not specifically address pre-suit litigation hold requests, the Rules of Civil Procedure contemplate that the parties will act in good faith in the preservation and production of documents. See Fed. R. Civ. P. 37.”).

4 In some circumstances, the intentional destruction of potentially relevant evidence can lead to criminal prosecution. See, e.g., 18 U.S.C. Sections 1512(c) and 1519. While this paper is not intended to address the criminal consequences of failing to preserve relevant evidence, it may be of analytical assistance to those dealing with criminal matters.

Introduction

The 2006 Amendments to the Federal Rules of Civil Procedure provide that electronically stored information that is not reasonably accessible because of undue burden or cost need not be reviewed or produced in discovery absent agreement or an order issued for “good cause, considering the limitations of Rule 26(b)(2)(C).”⁵ Rule 26(b)(2)(B) also requires that a party “identify” those sources it does not intend to search or from which discovery will not be made.

The Amendments are *not*, however, the source of pre-discovery obligations to preserve potential sources of discoverable electronically stored information, a task left to the common law.⁶ The duty to preserve applies to any and all relevant documents, tangible things, or electronic information in the possession, custody, or control of a party⁷ no matter where located. The knowledge or belief that litigation has begun or is imminent “triggers” preservation obligations and requires that reasonable steps be undertaken to maintain relevant and discoverable information pending discovery,⁸ including third party discovery.⁹

The Committee Notes to Rules 26(b)(2) and Rule 37(e) make clear that preservation obligations may apply even when electronically stored information is located on an inaccessible source. The Note to Rule 26(b)(2) provides that “[a] party’s identification of sources of electronically stored information as not reasonably accessible does not relieve the party of its common-law or statutory duties to preserve evidence.” Moreover, the Note to Rule 37(e) instructs that parties may not “exploit the routine operation of an information system to thwart discovery obligations by allowing that operation to continue in order to destroy specific stored information that it is required to preserve.”¹⁰

5 Rule 26(b)(2)(C) contains the “proportionality” limitations added in 1983 and formerly found in Rule 26(b)(2). See Wright and Miller, “Inaccessible” Electronically Stored Information, 8 Fed. Prac. & Proc. Civ. 2d Section 2008.2 (2007).

6 See *Silvestri v. GM*, 271 F.3d 583 (4th Cir. 2001).

7 See *Leon v. IDX Systems*, 464 F.3d 951, 955-957, 961 (9th Cir. 2006)(upholding sanction against a terminated whistleblower plaintiff who had deleted data from his company-furnished laptop).

8 See *The Sedona Conference® Commentary on Legal Holds: The Trigger & The Process* (August 2007 Public Comment Version www.thesedonaconference.org) Guideline 1 (“Reasonable anticipation of litigation arises when an organization is on notice of a credible threat it will become involved in litigation or anticipates taking action to initiate litigation”).

9 See *The Sedona Conference® Commentary on Non-Party Production and Rule 45 Subpoenas* [Working Draft, March 2008 www.thesedonaconference.org], citing at pp 3-4; *In re Napster, Inc. Copyright Litigation*, 2006 WL 305086, at *6 (N.D. Cal. Oct. 25, 2006)(service of and compliance with a non-party subpoena is not necessarily sufficient notice of future litigation).

10 A producing party can face a Hobson’s choice between the burden and cost of preservation and the risk of sanctions for failing to do so. Parties engaged in ongoing, recurrent litigation can also face a serial preservation duty dilemma, in which preserved data sources that would not be kept for any other reason may become subject to preservation duties in subsequent litigation.

Preservation Obligations

It has been left to the case law and best practice guidelines such as *The Sedona Principles* to provide *de facto* “national standards” for preservation obligations in the absence of party agreement. Principle 5, for example, provides that implementation of preservation duties requires “reasonable and good faith efforts,” but that it is “unreasonable to expect parties to take every conceivable step to preserve all potentially relevant data.” Comments 5.c. and 5.d. to Principle 5 recommend use of a “repeatable, documented” process in implementing “legal” or “litigation” holds, a topic that is the subject of *The Sedona Conference® Commentary on Legal Holds: The Trigger & The Process*.¹¹

This approach is representative of the evolving case law¹² and is buttressed by Principle 6, which provides that responding parties are “best situated” to evaluate the detailed procedures, methodologies and technologies “appropriate for preserving and producing their own electronic data and documents.” As noted in *Zubulake v. UBS Warburg* (“*Zubulake IV*”), “[because] there are many ways to manage electronic data, litigants are free to choose how this task [preservation] is accomplished.”¹³

The best way to avoid post-production preservation disputes is by developing early agreement on contentious preservation issues through transparent and cooperative efforts. However, there will be instances when preservation decisions will be required in advance of the opportunity to develop such understandings or seek court guidance. Under those circumstances, a party should act in a reasonable and good faith manner¹⁴ based on its best understanding of that which is likely to be needed in discovery.

To help guide this process, we recommend:

Guideline 1. *Where litigation is anticipated but no plaintiff has emerged or other considerations make it impossible to initiate a dialogue, the producing party should make preservation decisions by a process conforming to that set forth in the Decision Tree in Figure 1 and as described above.*

Working Group 1 has developed a multi-step approach to preservation decisions, which is equally applicable to all sources of information, whether accessible or inaccessible.¹⁵ This logical approach is graphically portrayed in the Decision Tree in Figure 1 below. In summary:

The initial step requires an initial assessment of what type of information would be relevant and discoverable, based on what is then known, much as is done in assessing the scope of a litigation hold. After determining the relevant issues, a party should next assess what potential data sources might reasonably contain that information. To help perform that assessment, the party must attempt to identify custodians who might have created or controlled relevant information, and locate where that information is kept.

Based on that preliminary analysis, the party should then assess whether each identified data source contains potentially discoverable information, taking into account what is known or knowable at the time about the potential discovery. If a party is neither actually aware nor should be aware of that possibility, there is no obligation to preserve the source. However, if the opposite is true, the next step is to assess the perceived accessibility of the source on which it may be found. If the source in question is not reasonably accessible, it may nonetheless still have to be preserved if the producing party does not have a reasonable belief that the information is available on other, more accessible sources.

11 See *The Sedona Conference® Commentary on Legal Holds: The Trigger & The Process* (August 2007 Public Comment Version), *supra*, Guideline 6 (“Depending on the circumstances, a written legal hold (including a preservation notice to persons likely to have relevant information) should be issued.”).

12 See *Miller v. Holzmann*, 2007 WL 172327 (D. D.C. Jan. 17, 2007) (holding that *Sedona Principle 5* is reasonable and in accordance with developing case law).

13 220 F.R.D. 212, 218 (S.D.N.Y. 2003).

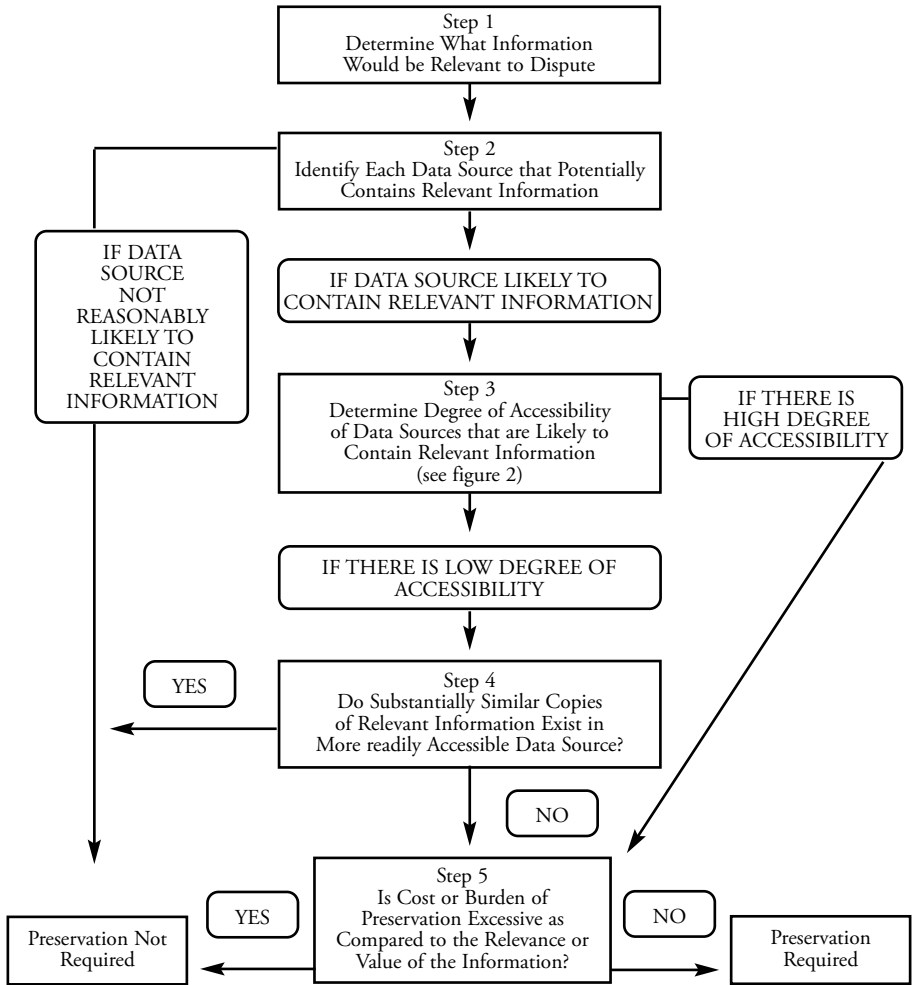
14 Rule 37(e), as renumbered after the 2007 Style Amendments, provides that in the absence of exceptional circumstances, rule-based sanctions should not issue “for failing to provide electronically stored information lost as a result of the routine, good-faith operation of an electronic information system.” See *Escobar v. City of Houston*, 2007 WL 2900581, at *18 (S.D. Tex. Sept. 27, 2007) (applying rule in context of recycling of audio tapes).

15 See, e.g., *Wm T. Thompson v. General Nutrition Corporation*, 593 F. Supp. 1443, 1455 (C.D. Cal. 28, 1984) (“While a litigant is under no duty to keep or retain every document in its possession once a complaint is filed, it is under a duty to preserve what it knows, or reasonably should know, is relevant to the actions, is reasonably calculated to lead to the discovery admissible evidence, is reasonably likely to be requested during discovery, and/or is the subject of a pending discovery request.”).

However, whether the source is readily accessible or not, the Decision Tree makes it clear that the accessibility assessment is not the final word. As a fifth and final step, only when the perceived benefit to discovery of the information is not outweighed by the burdens and costs involved is preservation required. This “proportionality” analysis is similar to the familiar principles, which courts use in determining production from such sources.¹⁶

The Decision Tree is set forth below in Figure 1:

Figure 1: Decision Tree for Determining ESI Preservation Obligations



¹⁶ By way of analogy from the production context, *See* Ronald J. Hedges, *Judges, Lawyers, and the New Rules*, 43 TRIAL 20, 22 (Apr. 2007) (“[I]n the end, we have to use the same test to determine whether discovery should go forward – the so-called proportionality rule, which had been Rule 26(b)(2) and is now 26(b)(2)(C). That rule provides that a judge can deny or limit or condition a discovery request that is too burdensome or expensive.”).

This analysis - which has necessarily been simplified for ease of explanation – is based in large measure on principles that emerged before, and which were clarified by, the 2006 Amendments.

We turn now to a more detailed discussion of each of these steps in the Decision Tree.

Step One Analysis - Relevance and Responsiveness

Electronically stored information need not be preserved, absent an agreement or court order, in the absence of a reasonable belief that it is potentially relevant information that is likely to be discoverable in litigation.

An initial question in any preservation analysis is whether the information which may be contained on a source is potentially discoverable in the action. The assessment necessarily depends upon what the potential preserving party knew or reasonably should have known at the time. There will always be sources of information which clearly cannot contain discoverable information because of the origin of the information on the source or the time parameters involved.

In the matter of *In re Kmart Corporation*,¹⁷ for example, there was no evidence Kmart knew that discoverable information existed among email being destroyed pursuant to a preexisting policy. The court rejected the comparison to *Zubulake* as “wishful thinking” because there was no reason to anticipate the need for the information. Similarly, in *Healthcare Advocates v. Harding, Early, Follmer & Frailey*,¹⁸ no duty to retain electronic screen shots was found when the producing party neither “knew or should have known” that temporary cache files would be sought in litigation.¹⁹

Where actual notice of the potential discoverability is lacking, or where the potential relevance is not obvious, efforts by a potential requesting party to provide notice that information should be preserved can become significant. A general demand for preservation is not sufficient, however. For example, in *Frey v. Gainey Transportation Services, Inc.*,²⁰ a fifteen page demand letter was deemed to be “an [ineffectual] effort on the plaintiff’s part to sandbag a defendant in the event that any of those materials were not preserved” where no particularly relevant items were sought.

A requesting party should not ignore the issue. If the requesting party can identify with particularity sources of information that it believes will be relevant and discoverable in the litigation, it should notify the producing party, especially if the relevance of the information is not immediately apparent. In *re Veeco Instruments, Inc. Securities Litigation*,²¹ the court held that it “would be unreasonable for the [requesting party] to assume that back-up tapes were being searched given that . . . no discussions on the subject were held.”²² Similarly, in *Petcou v. C.H. Robinson Worldwide, Inc.*,²³ the court refused to fault a party for failing to impose an entity-wide preservation order on deletion of email where the requesting party had not indicated the need to do so.²⁴

The need for affirmative action is especially true where the nature of the information sought is temporary or ephemeral.

Illustration. In a trade secrets action against defendant involving the theft of a secret formula, plaintiff believes that an employee of defendant received the trade secret on his computer via a non-company authorized, web-based email account. Plaintiff needs screenshots of the email pages and related communications to prove the theft of trade secrets, which can only be secured “forensically” by immediately obtaining the web browsing history found in areas of the operating system where “temp,”

17 371 B.R. 823 (Bkrcty, N.D. Ill. 2007).

18 497 F. Supp. 2d 627, 640-41 (E.D. Pa. 2007).

19 *Id.* at 641 (“[T]hey had no reason to believe that their activities would subject them to a lawsuit for ‘hacking,’ [and the failure to preserve] is not an action that shocks the conscience.”).

20 2006 WL 2443787 (N.D. Ga. Aug. 22, 2006).

21 2007 WL 983987 (S.D.N.Y. Apr. 2, 2007).

22 *Id.* at *1.

23 2008 WL 542684 (N.D. Ga. Feb. 25, 2008) (“It does not appear that Defendant acted in bad faith in following its established policy for retention and destruction of e-mails.”).

24 *See also Markesfare Annunciation, LLC v. United Fire & Casualty Insurance Co.*, 2007 WL 3273440 (E.D. La. Nov. 5, 2007) (refusing to consider a motion for sanctions because the preservation issue should have been raised in a timely manner “as opposed to bypassing this step in the discovery process and seeking sanctions directly.”).

“cache,” and “hidden” files reside, but are constantly and automatically being overwritten. Plaintiff must provide expedient and specific notice to preserve such web e-mail data since the data is not in the company’s authorized email server, is inaccessible, and is constantly being overwritten via automated processes.

Thus, in *Columbia Pictures v. Bunnell*,²⁵ the court refused to find a duty to preserve information temporarily residing in RAM where the producing party had no reason to anticipate a request for the information in discovery.²⁶

Another example is where a requesting party fails to raise the need for preservation of metadata pending discovery. As noted in *Kentucky Speedway, LLC v. NASCAR*,²⁷ “whether metadata is relevant or should be produced is [an issue] which ordinarily should be addressed by the parties in a Rule 26(f) conference.”²⁸

In *O’Bar v. Lowe’s Home Centers, Inc.*,²⁹ the court required parties to discuss “whether production will be of the Native File, Static Image, or other searchable or non-searchable formats.”³⁰ In *Kentucky Speedway*, the court relied on the failure to raise the topic in early discussions as a reason for refusing a belated attempt to seek metadata.

Step Two Analysis – Identification of Data Sources

After determining the type and nature of information that would be relevant to the dispute, an organization should make reasonable efforts to identify the data sources that potentially contain that information.

Once a party identifies the information that would be relevant to a pending or imminent dispute, it must determine where that information likely resides. This task typically involves identifying (1) the custodians who created or control relevant information and (2) the data sources where the custodians’ information resides. This process should be conducted as part of an organization’s efforts to implement a legal hold. In the *Commentary on Legal Holds*, The Sedona Conference® has offered guidance:

For large preservation efforts, a process that is planned, systemized and scalable is ideal, while an ad hoc, disjointed and/or manual process can result in undue burden and expense. An example of an inefficient process involves collecting immense amounts of information from every custodian, server and restored back-up tape without any initial effort to identify relevant information. With no means to triage the information and to filter out irrelevant ESI, the collection may be overbroad, with a great deal of irrelevant information aggregated into a central repository where it is then finally processed and searched.³¹

An organization should consider all data sources within its “possession, custody, and control” that are likely to include relevant, unique information.³² This includes data sources within the physical possession of the organization, and other sources within the possession or custody of third parties, pursuant to contractual or other relationships, such as information held by Application Service Providers (ASPs) and other service providers.³³

25 2007 WL 2080419 (C.D. Cal. May 29, 2007), *motion to review denied*, 245 F.R.D. 443, 446 (C.D. Cal. 2007) (requiring preservation and future production of information temporarily stored in RAM, which was highly relevant and could be logged with minimal efforts).

26 The magistrate judge held that “the defendants’ failure to retain the Server Log Data in RAM was based on a good faith belief that preservation of data temporarily stored only in RAM was not legally required” because, *inter alia*, there had been “no specific request by the defendants to preserve Server Log Data present solely in RAM.” 2007 WL 2080419, at *14. During a colloquy about the case at an E-Discovery Conference, the point was made by a magistrate judge that there could very well be occasions when the duty to preserve such ephemeral information will be obvious and steps may have to be undertaken to preserve it if the need and relevance outweigh the burdens and costs of doing so (See Figure 1, Decision Tree, Steps Four and Five).

27 2006 WL 5097354 (E.D. Ky. Dec. 18, 2006).

28 *Id.* at *8 (failure to notify of demand for metadata until seven months after production of electronic and hard copy of documents).

29 2007 WL 1299180 (W.D. N.C. May 2, 2007).

30 *Id.* at *4 (adapted from the “Suggested Protocol for Discovery of Electronically Stored Information” available at <http://www.mdd.uscourts.gov/news/ESI/Protocol.pdf>).

31 See *The Sedona Conference Commentary on Legal Holds: The Trigger & the Process* (August 2007 Public Comment Version), *supra*, at 11.

32 *Id.*, at 12.

33 *Id.*

This assessment will be easier to make for some data sources than for others. For example, information stored in media that requires special restorative efforts to place it in a form where it can be viewed is, by definition, difficult to assess. However, based on knowledge of date ranges, individuals or business units involved, or other features, it may be possible to make reasoned judgments.

Step Three Analysis – Relative Accessibility

The relative accessibility of a source of potentially discoverable information is best evaluated by assessing the burdens involved in viewing, extracting, preserving, and searching the source as well as other relevant factors imposed by the location, including the dispersion and the volumes involved.

The use of “accessibility” of an information source as a differentiator in the Federal Rules can be traced to two important influences.

First, Texas Rule 196.4, adopted in 1999, adopted a distinction between production that required a prior court order and that which did not because the information was available to the producing party in the ordinary course of business.³⁴ Second, the initial *Zubulake* opinion³⁵ adopted the concept of “accessibility” in connection with determining when and whether to allow cost shifting.³⁶

The Advisory Committee adopted elements of both concepts in instituting the “two-tiered” standard for e-discovery production, now found in Rule 26(b)(2)(B), whereby production from inaccessible sources can be ordered only upon a showing of “good cause, considering the limitations of Rule 26(b)(2)(C).”³⁷

The Federal Rules do not define “not reasonably accessible” other than to caution that it turns on the presence or absence of “undue burden or cost.” Under the emerging case law at the time of the 2006 Amendments, there was a reasonable consensus, as outlined in the introductory remarks in the 2005 Advisory Committee Report,³⁸ that the following data types were often deemed not to be reasonably accessible without undue burden or cost:

- information on databases whose retrieval cannot be quickly accomplished because the database software is not capable of extracting the information sought without substantial additional programming;
- information stored on media that must be transformed into another form before search and retrieval can be achieved;
- deleted information whose fragments remain only accessible by forensics; and
- legacy data remaining from obsolete systems that is unintelligible on successor systems.

As noted in the Decision Tree, and as the Advisory Committee made clear, the inaccessibility of a potential source, in and of itself, does not determine whether it must be preserved, which depends on the facts of each case (See Decision Tree, Steps 4 and 5).

³⁴ See Texas Rule 196.4 (“The responding party must produce the electronic or magnetic data that is responsive to the request and is reasonably available to the responding party in its ordinary course of business.”).

³⁵ *Zubulake v. UBS Warburg* (“*Zubulake I*”), 217 F.R.D. 309 (S.D.N.Y. 2003). There have been at least five *Zubulake* decisions. In addition to *Zubulake I*, three others address electronic discovery. See *Zubulake III*, 216 F.R.D. 280 (S.D.N.Y. July 24, 2003); *Zubulake IV*, 220 F.R.D. 212 (S.D.N.Y. 2003); *Zubulake V*, 229 F.R.D. 422 (S.D.N.Y. 2004).

³⁶ For a concise summary of the history of cost-shifting before and after the 2006 Amendments, an excellent resource is Mazza et. al, *In Pursuit of FRCP 1: Creative Approaches to Cutting and Shifting the Costs of Discovery of Electronically Stored Information*, 13 Rich. J. L. & Tech. 11 at *99 (Spring 2007).

³⁷ Fed. R. Civ. P. 26(b)(2)(C)(iii) requires that a “court *must* limit the frequency or extent of discovery otherwise allowed by these rules or local rules if it determines [that] “the burden or expense of the proposed discovery outweighs its likely benefit. . . .” (emphasis added). For a discussion of the post-Amendment decisions applying these principles to inaccessible sources, see Thomas Y. Allman, *The ‘Two-Tiered’ Approach to E-Discovery: Has Rule 26(B)(2)(b) Fulfilled Its Promise*, 14 Rich. J. L. & Tech. 7 (Spring 2008).

³⁸ Final Report, Standing Committee (2005) at C-42.

In an effort to assist in the analysis of relative accessibility as called for in Step 3, Sedona has identified twelve factors which should be considered, as set forth in Figure 2 below entitled the “Sedona Accessibility NRA Factors.” These factors include both *Media Based Factors* and *Data Complexity Factors*.

A. Media Based Factors

The Media Based Factors (Numbers 1-6, Figure 2) are alternative categories of storage media, arranged in descending orders of accessibility, as inspired by *Zubulake I*,³⁹ a pre-2006 Amendment decision which used the “reasonably accessible” concept for other purposes. In *Zubulake I*, the court found that the time and expense required to retrieve documents and electronic data depends primarily on whether such information “is kept in an accessible or inaccessible format ...[and] [w]hether electronic data is accessible or inaccessible turns largely on the media on which it is stored.”⁴⁰

Zubulake I broke down electronic data into five categories, (1) active on-line data (hard drives, for example); (2) near-line data (typically, robotic storage devices such as optical disks); (3) offline storage/archives (removable optical disks or magnetic tape media which can be labeled and stored in a shelf or rack); (4) backup tapes (devices like tape recorders that read data from and write it onto a tape in a manner typically not organized for retrieval of individual documents or files); and (5) erased, fragmented or damaged data (such data can only be accessed after significant processing).⁴¹ The first three categories of media types were considered by the Court to be “accessible” and the last two categories were considered inaccessible.

The first six Sedona Accessibility Factors (See Figure 2) correspond to the media based categories from *Zubulake I*, with the exception that the fifth category from that decision has been subdivided by Sedona for ease of use.⁴²

B. Data Complexity Factors

The Sedona Conference® also believes, however, that consideration must be given to the unique complexities of retrieval and review of data from any given source, depending upon the nature of the burdens involved. Accordingly, we have suggested six *additional* Sedona Accessibility Factors (See Figure 2) that should be considered along with the media based factors in reaching an overall measure of the relative inaccessibility of the data source.

For example, claim forms which are scanned to an active on-line server storage device in a “TIF” graphics format that does not allow for text search are “Active on-line data,” but because the Search Complexity (Factor 11) is high and manual review is expensive, a more nuanced and complete view is that the source of those claim forms is relatively inaccessible for purposes of analysis.

Thus, we recommend that the user address *both* the media and data complexity factors under the facts and circumstances of the case before arriving at a relative accessibility rating for purposes of the Decision Tree.

The quality of the documentation related to the “not reasonably accessible decisions” will be of importance in discovery related motions and assist the court in determining whether a party acted reasonably, even if mistakenly, under the facts and circumstances of a given case.

³⁹ *Zubulake v. UBS Warburg* (“*Zubulake I*”), 217 F.R.D. 309, 321-322 (S.D. N.Y. 2003).

⁴⁰ *Id.* at 318.

⁴¹ We have modified the fifth *Zubulake I* category by splitting the concept into “Physically damaged media” and “Legacy media.” Physically damaged media involves media that cannot be read without forensic assistance or specialized software tools and Legacy media involves orphaned media where it is difficult to locate a compatible drive or device to read the typically old or legacy media.

⁴² That the data is deemed “accessible” does not mean it is readily available, “the time it takes to actually access [such] data ranges from milliseconds to days, [however] the data does not need to be restored or otherwise manipulated to be usable”. Inaccessible data, on the other hand, is not readily usable. Backup tapes must be restored ... fragmented data must be defragmented, and erased data must be reconstructed. That makes such data inaccessible.” *Id.* at 318-321.

Figure 2
Accessibility Factors

	Factors	Examples
1	<i>Active on-line data</i>	Hard drives, PDAs, network storage
2	<i>Near-line data</i>	Robotic storage devices such as optical disks
3	<i>Offline storage/archives</i>	Removable optical disks or magnetic tape media which can be labeled and stored in a shelf or rack
4	<i>Backup tapes</i>	Sequential access devices typically not organized for retrieval of individual documents or files
5	<i>Physically damaged media</i>	Damaged CDs or DVDs that cannot be read by an ordinary drive or damaged hard drives and tapes
6	<i>Legacy media</i>	Difficult or impossible to locate a compatible drive or device to read the typically "orphaned" legacy media
7	<i>Transient complexity</i>	Web pages constantly being deleted and overwritten to make room for further storage
8	<i>Hidden complexity</i>	Deleted files after recycle bin has been emptied which cannot be viewed without specialized knowledge or tools
9	<i>Extraction complexity</i>	Data fragments found in the slack space which are difficult to copy
10	<i>Preservation complexity</i>	Cache and temp files created by a PC difficult to preserve without disabling operating system
11	<i>Search complexity</i>	Static graphical images not OCR'd
12	<i>Dispersion complexity</i>	Numbers of PDA devices needed to be reviewed for preservation of data from a central synchronized location

Step Four Analysis – Availability of Alternative Sources

When assessing the need to preserve inaccessible sources, an important factor is whether the identical or substantially similar information is available through more accessible sources.

In most instances, it is reasonable to rely upon the existence of alternative sources of the same or substantially similar information as a reason for not preserving a particular source of the same information. This is true whether the source in question is itself reasonably accessible (in which case the information is essentially duplicative) or may be deemed to be inaccessible (in which case it is not only duplicative, but more onerous to retrieve and utilize). The Committee Note to Rule 37(e) suggests that whether affirmative action is required often depends on "whether the party reasonably believes that the information on such sources is likely to be discoverable and not available from reasonably accessible sources."

Illustration i. In a dispute over the termination of an employee, the active email accounts of key players are captured as soon as a producing party reasonably anticipates litigation, and the question is raised as to whether it is necessary to set

aside existing backup media for the email servers, which are routinely overwritten. One of the factors to consider is whether deleted information will not be found in the active accounts and is therefore available only on one or more of the existing backup media.

Illustration ii. Under the same set of facts as above, the issue is whether it is necessary to make a mirror image or otherwise preserve the hard drive from the workstation or from the laptop used by the former supervisor of the terminated individual who has left the company for unrelated reasons.

The resolution of the issue often turns on the reasonableness of the belief of the party responsible for the source at issue. The burden of proof on the issue may vary with the circumstances. In *Cache La Poudre Feeds v. Land O'Lakes*,⁴³ the court sanctioned the failure to retain the hard drives of key former employees while questioning the basis for the General Counsel's belief that the relevant information could be found in a more readily accessible location, given that the General Counsel was aware that email backup tapes were not being retained, but were being recycled. In *Best Buy Stores v. Developers Diversified Realty*,⁴⁴ however, no sanctions issued because the party questioning the failure to act did not argue and prove that database materials were uniquely available from the inaccessible source.⁴⁵

In *Disability Rights Council v. WMTA*,⁴⁶ the Magistrate Judge noted a failure (which the court described as "indefensible") to prevent the automatic deletion of email, including "possibly relevant and discoverable emails."⁴⁷ As recently noted by two well-regarded e-discovery thought leaders,⁴⁸ "[a] party cannot be acting in good faith unless it takes some steps to preserve information once litigation is reasonably anticipated."

One of the more subtle issues involves the degree of responsibility of a party whose employees disregard otherwise reasonable legal hold or litigation hold instructions. In *Hawaiian Airlines, Inc. v. Mesa Air Group*,⁴⁹ for example, a court entered an adverse inference instruction against a party that could have, but did not, make backups of the hard drives of a key executive immediately after suit was filed. The court found that the employer had a duty to act given the risk that high level employees might do "wrongful and foolish things, like destroying evidence, under the pressure of litigation." The reasonableness of reliance on employees to follow directions must be assessed in the context of the particular facts and circumstances.

Step Five Analysis – the Proportionality Principle

If the burdens and costs of preservation are disproportionate to the potential value of the source of data at issue, it is reasonable to decline to preserve the source.

The concept of proportionality pervades discovery obligations resting on the Federal Rules of Civil Procedure. Rule 1 highlights the imperative that all of the procedural rules, including the discovery rules, "be construed and administered to secure the just, speedy, and inexpensive determination of every action and proceeding." Proportionality underlies the concept in Rule 26(b)(2)(B) that data sources can include those which are "not reasonably accessible because of undue burden or cost." And Rule 26(b)(2)(C) of the Federal Rules provides, in part, that the ability to conduct discovery must be limited to those instances where the anticipated benefits outweigh the burdens and costs of the discovery.

43 2007 WL 684001 (D. Colo. March 2, 2007).

44 247 F.R.D. 567 (D. Minn. 2007) (reversing Magistrate Judge opinion and noting that any relevant ESI could be gathered manually without the need for restoration of the database).

45 *Id.* at 571.

46 242 F.R.D. 139 (D.D.C. 2007).

47 *Id.* at *146 (noting that users may defeat the automatic deletion by archiving the email, which a majority of employees did not do).

48 See Shira A. Scheindlin and Jonathan M. Redgrave, "E-Discovery: Technology Requires Greater Care in Preserving Evidence," April 2008 ABA Journal, at p. 53.

49 2007 WL 3172642 (Bkrcty. D. Ha. Oct. 30, 2007) (CFO intentionally scrubbed files from laptop computers after receiving legal hold notice).

These considerations of proportionality are intended to balance the costs and potential benefits of discovery and are applicable, by way of analogy, to implementation of the duty to preserve.⁵⁰ As noted in Comment 2.b of *The Sedona Principles*, “[o]therwise, transactional costs due to electronic discovery will overwhelm the ability to resolve disputes fairly in litigation.”

It is the proportionality principle that reconciles, under the Decision Tree analysis, the widely varying circumstances under which a party - in the absence of agreement - must make its decisions independent of the technical characteristics of the data source. For example, an employee’s local drive may not warrant forensic imaging in a straightforward commercial dispute, whereas it could be crucial to (and thus need to be preserved) in a trade secret case.

In weighing proportionality, the burdens and costs of accessing and preserving the information on the source, as already identified in Step Three, are balanced against the reasonably anticipated need and significance of the information in the imminent or pending cases. If such costs and burdens do not outweigh the reasonably anticipated importance in that context, preservation is warranted. Conversely, if the burdens and cost of preservation is disproportionate to the reasonably anticipated value, preservation would not be required.

Illustration. In a dispute where potentially discoverable information is stored on a cell phone SIM file, the data source is assessed as relatively inaccessible. Given this determination, the issue then becomes, under Step Four of the Decision Tree, whether the information sought is uniquely available on the SIM card. If so, the ultimate issue, as posed by Step Five, is whether the perceived benefit to ultimate discovery is outweighed by the burdens and costs of the preservation of the information.

The duty to preserve does not require a disproportionate investment in hardware or software to effectuate such preservation. For example, in *Proctor & Gamble Company v. Haugen*,⁵¹ the Court of Appeals reversed an order of sanctions because the preservation steps not taken would have required installation of a new server or the purchase of archival data from a third party.⁵² Similarly, in *Malletier v. Dooney & Bourke, Inc.*,⁵³ an entity maintaining a chat room function for its customers was not required to activate or install a method of recording the comments.

Similarly, a party is not required to create information that does not exist. In *Getty Properties Corp. v. Raceway Petroleum*,⁵⁴ the Court denied an adverse inference for a failure to “create and preserve” alarm history reports prior to being ordered to do so because the failure to “create more reports than it used in the daily activities of its business is not the kind of willful action that discovery sanctions are intended to redress.” Similarly, in *Phillips v. Netblue*,⁵⁵ the failure to preserve URLs to advertisements or to memorialize hyperlinks images was not sanctioned because “[t]his is not a complaint regarding [an] alleged failure to preserve evidence, but rather [an] alleged failure to gather evidence.”⁵⁶ (Emphasis in original.)

Finally, the principle of proportionality also plays an important role in deciding whether specific metadata should be preserved. It is often advisable to preserve sources of electronically stored information in native file formats with metadata if there is a possibility that production will be subsequently sought in that form.⁵⁷ Comment 12.b of *The Sedona Principles*⁵⁸ suggests that

50 See *Oxford House v. City of Topeka, Kansas*, 2007 WL 1246200 (D. Kan. April 27, 2007) (no duty to maintain email or recover from backup media given that cost was not justified by low probability that information would be recovered).

51 427 F.3d 727 (10th Cir. 2005).

52 *Id.* at 739.

53 2006 WL 3851151 (S.D.N.Y. Dec. 22, 2006).

54 2005 WL 1412134 (D.N.J. June 14, 2005).

55 2007 WL 174459 (N.D. Cal. Jan. 22, 2007).

56 This holding may be inconsistent with *Columbia Pictures v. Bunnell*, *supra*, 2007 WL 2080419 (C.D. May 29, 2007) (Magistrate Judge Chooljian); *aff'd*, 245 F.R.D. 443 (C.D. Cal. 2007), where the Magistrate Judge ordered a party to begin to preserve temporary information which could be logged without undue burden. See Thomas Y. Allman and Kevin Brady, *Can Random Access Make Good Law?* *The National Law Journal*, Vol. 30, No. 15 (December 10, 2007) (noting that *National Union Electric v. Matsushita* (1980), held that “common sense” required production in machine-readable format despite the fact that the information did not exist in that precise form).

57 See *United States v. O’Keefe Cr. No. 06-249 (PLF/JMF)*, 2008 WL 449729 (D.D.C. Feb. 18, 2008) (applying amended Rule 34(b) as persuasive authority in the criminal discovery context to require the government to preserve electronically stored information in its native format with metadata until the motion regarding production ruled upon).

58 See *Sedona Principle 12* (2nd ed. 2007) (decisions should take into account the need to produce reasonably accessible metadata that will enable the receiving party to have the same ability to access, search, and display the information as the producing party where appropriate or necessary in light of the nature of the information and the needs of the case).

organizations “evaluate the potential benefits of retaining native files and metadata (whether or not it is produced) to ensure that documents are authentic and to preclude the fraudulent creation of evidence.”

However, if the necessity to do so is not obvious, the burdens associated with any enhanced privilege review and the possibility that the metadata will not be needed for production purposes may be taken into account in deciding whether or not to preserve. For example, cases involving patent, unfair competition, trademark, and antitrust often raise disproportionate review concerns because the metadata may include privileged material and thus require extensive review.⁵⁹

Guideline 2. *As soon as feasible, preservation issues should be openly and cooperatively discussed in sufficient detail so the parties can reach mutually satisfactory accommodation and also evaluate the need, if any, to seek court intervention or assistance.*

Rule 26(f) lists “issues” relating to preservation as among the key topics for discussion prior to development of Scheduling Orders under Rule 16(b). This paradigm shift contemplates greater transparency about preservation issues and also implies, as its necessary corollary, that waiver of subsequent spoliation claims may result where parties do not take advantage of the opportunities to discuss the issues.

Accordingly, the parties should discuss issues relevant to preservation in sufficient detail to adequately explore the possibility of reaching agreement on practical methods of resolving contentious issues. This includes, for example, the anticipated form or form of production and the related need for metadata and native format so that the matter can be resolved while the information is still in native format. This preserves the ability of the producing party to prepare an appropriate extract of any metadata that may be required or to make production in some variant of a native file format.

A number of practical examples exist. For example, in *In re Celexa and Lexapro Products Liability Litigation*,⁶⁰ the parties agreed that the producing party could set aside for future consideration a selection of existing backup media while resuming recycling of the remainder. Further, in the case of *In re Genetically Modified Rice Litigation*,⁶¹ the agreed order required the parties to take reasonable steps to preserve defined information from active files in native format pending discovery.

Illustration. The class representative in a complex pharmaceutical class action seeking discoverable information from a multitude of databases is informed that they are not programmed to isolate and produce information regarding the issues in the case. After consultation, an agreed process is established whereby the parties will identify experts to discuss the best technical means of preserving the information pending the discovery phase.⁶²

In preservation discussions, parties “should pay particular attention to the balance between the competing needs to preserve relevant evidence and to continue routine operations critical to ongoing activities. Complete or broad cessation of a party’s routine computer operations could paralyze the party’s activities.”⁶³ However, willful continuance of a routine operation involving destruction when preservation obligations are known to apply is not an example of “good faith” operation of that system.

Where parties are unable to reach agreement, either or both should consider whether to seek court resolution of preservation issues involving inaccessible sources. Although the Advisory

59 See Jack E. Pace, III & John D. Rue, *Early Reflections on E-Discovery in Antitrust Litigation: Ten Months Into the New Regime*, 22 ANTITRUST 67, 69 (2007) (“[T]he costs associated with just the additional privilege review that would be necessary for each and every production of ESI (including metadata) could be staggering.”).

60 2006 WL 3497757 (E.D. Miss. Nov. 13, 2006). See also Friedberg, “*To Recycle or Not to Recycle, That is the Hot Backup Tape Question*,” 201 PLI/Crim. 205, 217 (2005) (recommending alternatives to avoid suspension of email backup rotation).

61 2007 WL 1655757 (E.D. Mo. June 5, 2007).

62 See *In re Serquel Products Liability Litigation*, 2007 WL 219989, at *4 (M.D. Fla. Jan. 26, 2007). That this effort is no small task can be seen from *In re Serquel Products Liability Litigation*, 2007 WL 2412946, at *12 (M.D. Fla. Aug. 21, 2007) (criticizing the “purposeful sluggishness” of defendant in carrying out obligations under the agreed order).

63 Committee Note, Rule 26(f).

Committee discouraged *ex parte* or unreasonably broad preservation orders,⁶⁴ it also acknowledged the practical benefits of preservation orders and clearly contemplated that courts would and should entertain them, where appropriate. In some cases, it may also be appropriate to allocate the costs of preservation if the marginal value is minimal.⁶⁵

Guideline 3. *In conjunction with the initial discussions or where appropriate in the response to discovery requests, parties should clearly identify the inaccessible sources reasonably related to the discovery or claims which are not being searched or preserved.*

Rule 26(b)(2)(B) requires that a party “identify” any inaccessible sources it does not intend to search in order to qualify for the presumptive limitation on the need to search. However, the Rule and the Committee Note do not dictate when or how that identification must be made.

There are several opportunities to make the necessary identification of such sources.

A. Initial Disclosure (Rule 26(a)(1))

Rule 26(a)(1) requires a listing of inaccessible sources not being searched only if there is a credible possibility that they may contain information that a party “may use to support its claims or defenses.”

B. Meet and Confer

The Committee Note to Rule 26(f) suggests that parties discuss whether the information that may be sought in discovery is reasonably accessible. This should be accomplished in sufficient detail so that the requesting party can make its own determination as to whether it wishes to seek production from any inaccessible sources not being searched. Some local rules make this discussion mandatory at or prior to the “meet and confer.”⁶⁶

A list of possible topics for discussion include:

- Type of back-up and disaster recovery media used.
- Identity and version of legacy software or systems, and when such software or systems achieved “legacy” status within an organization.
- Information sufficient to describe the system(s) or protocols used by the party to map, archive, and manage the back-up processes and procedures.
- Information describing sources of information that are or may be duplicative or substantially similar to the information sought – and the processes used to locate those sources.
- Internal or third-party estimates of costs associated with accessing the various sources of data involved.
- Detail about the capture and retrieval protocol under consideration, and the internal cost of data capture and retrieval (human capital of an organization to restore or extract data).

⁶⁴ *Id.* (“The requirement that the parties discuss preservation does not imply that courts should routinely enter preservation orders. A preservation order entered over objections should be narrowly tailored. Ex parte preservation orders should issue only in exceptional circumstances.”).

⁶⁵ See *Treppel v. Biwail Corp.* (S.D.N.Y. 2006) (“If the demanding party seeks the preservation of information that is likely to be of only marginal relevance but is costly to retain, then rather than deny a preservation order altogether, a court may condition it upon the requesting party assuming responsibility for part or all of the expense.”).

⁶⁶ See “Guidelines for Discovery of Electronically Stored Information,” District of Kansas, Para. 4(g), available at <http://www.ksduscourts.gov/guidelines/electronicdiscoveryguidelines.pdf> (“If the responding party is not searching or does not plan to search sources containing potentially responsive information, it should identify the category or type of such information.”). See also *Default Standard for Discovery Of Electronically Stored Information, Appendix K*, Northern District of Ohio (“Prior to the Rule 26(f) conference, the parties should [discuss] whether . . . electronically stored information is of limited accessibility [such as] those created or used by electronic media no longer in use, maintained in redundant electronic storage media, or for which retrieval involves substantial cost.”), available at http://www.ohnd.uscourts.gov/Clerk_s_Office/Local_Rules/AppendixK.pdf.

- “Extenuating circumstances,” including any potential opportunity-cost issues associated with allocating internal staff to restore or extract data (e.g., an organization relying on a new product roll-out for survival).
- The anticipated form or forms of production to be sought, the need for metadata, and the form of preservation of information pending discovery.

Parties may also wish to document their discussion of factors supporting their claim of inaccessibility. The documentation should include, if feasible, any costs or other burdens created by such preservation.

C. Objections to requests for production

A party seeking discovery under Rule 34(a) must set forth, by individual item or by category, the items sought with “reasonable particularity.” A written response must be made stating compliance or, if the request is objected to, the “reasons for the objection.”

The potential sources of discoverable information that are not being searched should be clearly identified in any response, in a manner analogous to traditional objections, if this has not already been adequately conveyed at the meet and confer or otherwise. Formal objections may also include the information sufficient to accomplish the identification.

D. Form and Content of Identification

Rule 26(b)(2)(B) does not explicitly define what information must be furnished in any “identification,” thus leaving room for differing approaches. The Committee Note suggests that the party “identify, by category or type” the sources it is neither searching nor producing. The Committee Note also states, however, that the identification should “to the extent possible” provide enough detail to enable the requesting party to determine if it wishes to seek additional information or challenge the designation.

More than one round of discussions and supplemental disclosures may be necessary to provide adequate identification. The totality of the information provided should be the touchstone of compliance. There should be no single formula or mechanical requirement.

Guideline 4. *A party should exercise caution when it decides for business reasons to move potentially discoverable information subject to a preservation duty from accessible to less accessible data stores.*

A party may decide, for business reasons, to store potentially discoverable information subject to a preservation duty in any media it chooses provided that the information can still be produced in discovery.⁶⁷ In *Best Buy Stores v. Developers Div. Realty*,⁶⁸ for example, a court dealt with information that had been stored on backup media after an earlier litigation. The District Court, overruling a Magistrate Judge, refused to sanction the producing party, noting that the information remained available for discovery but could more likely be acquired directly.⁶⁹

In *Quinby v. WestLB AG*,⁷⁰ a court refused to sanction a party for moving email to backup media from active media, but did decline to shift the costs of restoring email from the inaccessible media, noting the conflicting view of another Magistrate Judge in *Treppel v. Biovail*.⁷¹ The court held that a party should be free to preserve electronic evidence in any format it chooses and cautioned that any other result would implicate “a whole range of document storage practices, such as off-site storage in ‘dead’ files,” and would “create the potential for punishing routine business practices that do not destroy documents or alter them in any material sense.”

67 See *Quinby v. WestLB AG*, 2005 WL 3453908 (S.D.N.Y. Dec. 15, 2005) (“*Quinby I*”).

68 247 F.R.D. 567 (D. Minn. 2007).

69 *Id.* at 571.

70 2006 WL 2597900 (S.D.N.Y. Sept. 5, 2006).

71 See *Treppel v. Biovail*, 223 F.R.D. 363, 372 (S.D.N.Y. 2006) (“conduct that hinders access to relevant information is sanctionable, even if it does not result in the loss or destruction of evidence”).

Guideline 5. *It is acceptable practice, in the absence of an applicable preservation duty, for entities to manage their information in a way that minimizes accumulations of inaccessible data, provided that adequate provisions are made to accommodate preservation imperatives.*

All organizations necessarily employ some type of management, formal or not, of their organization to meet regulatory, legal, and business needs. When information in electronic form accumulates in data sources which are difficult to access, however, it can become impracticable to assess their content and thereby manage them in a compliant manner. Efforts to do so are complicated over time by changes and upgrades in technology. Mergers, acquisitions, and sales of blocks of business add organizational challenges to the already daunting technical issues involved in accommodating differing systems. This problem can be compounded when entities fail to adopt appropriate policies and procedures that are responsive to the issues.

Effective management of information - including information stored on inaccessible sources - is largely governed by business and regulatory considerations, and courts will defer to those decisions provided that no actions are undertaken which are intended to and do interfere with the access to the information for discovery purposes.⁷²

Federal law requires a variety of regulated entities to adopt policies and procedures to ensure the security of information, to protect against unauthorized access or use, and to destroy the information through special, secure methods.⁷³ Absent regulations and specific preservation obligations, public and private organizations and individuals are empowered to minimize the volume of inaccessible data retained. The following are examples of ordinary course of business practices that could be considered:

- Overwriting residual data on hard drives.
- Overwriting or destroying used hard drives prior to repurpose or disposal of workstations or other hardware devices.
- Removing some metadata from documents in retaining them as records or when transmitting them to others.⁷⁴
- Restricting the capture of back-up data to the purpose of disaster recovery restoration, rather than archival data storage, and limiting the life of back-up data to the minimum time period necessary to fulfill the purpose of disaster recovery.
- Identifying inaccessible data sources containing legacy data; using reasonable efforts to assess whether the sources contain data subject to retention obligations or preservation duties; and in the absence of a reasonable basis to conclude that retention obligations or preservation duties apply, compliantly disposing of such legacy data sources.

These practices also help reduce the information security risks associated with inaccessible data held in common nesting places such as back-up tapes, workstations, and other portable data storage devices, information sources that foreseeably will leave the entity's facilities in normal use or through hardware repurposing or retirement.

72 See *Arthur Anderson LLP v. United States*, 544 U.S. 696 (2005) (destruction of information pursuant to a "valid document retention policy" is not "wrongful" under "ordinary circumstances"). See *Stevenson v. Union Pacific Railroad Company*, 354 F.3d 739, 746 (8th Cir. 2004) (holding that "some indication of an intent to destroy the evidence for the purpose of obstructing or suppressing the truth" is required); but see *Residential Funding Corporation v. DeGeorge Financial Corp.*, 306 F.3d 99, 107-8 (2d Cir. 2002) (determining culpability by negligence standard). Compliant data management practices regarding information security are discussed in ISO 27002, which "establishes guidelines and general principles for initiating, implementing, maintaining, and improving information security management in an organization." ISO 27002.1.

73 See, e.g., 8 C.F.R. Section 274a.2(g) (entities retaining employee I-9 records in digital format); 12 C.F.R. part 30 Appendix B (credit unions and other financial institutions); 16 C.F.R. Section 314.3 (Gramm-Leach-Bliley regulated financial institutions); 17 C.F.R. Section 248.30(a) (SEC registered brokers, dealers, investment companies and investment advisors); 29 C.F.R. Section 1904.29(b)(6) (employers maintaining privacy case information related to OSHA 300 logs and OSHA 301 Incident Reports); 45 C.F.R. Section 164.306 (HIPAA covered entities); 16 C.F.R. Section 682 (requiring secure destruction of consumer report information). The great majority of states' privacy laws go further, imposing additional privacy protections not generally preempted by federal law and requiring entities to notify state residents of security breaches regarding their personal information.

74 To retain all metadata would effectively limit the prevention of tampering in many commonly used software programs. For example, common technology that protects documents against tampering, such as the "pdf" format or the Write-Once-Read-Many technology used in many email archives, does not capture all of the transactional or embedded metadata in word processing documents, e-mail, or other e-communications.

Guideline 6. *An entity should encourage appropriate cooperation among legal and other functions and business units within the organization to help ensure that preservation obligations are met and that resources are effectively utilized.*

Many organizations assign the lead coordination role for e-discovery response to their Legal Department, which collaborates with IT, compliance, and records management departments or functions. Other organizations prefer to create multi-disciplinary teams representing those departments or functions and others.

In any case, the task is to avoid or minimize miscommunications that can occur between Legal and IT, both in imposing and monitoring holds and preparing for discussions with opposing counsel. Counsel need to more actively and effectively participate in the e-discovery process. Both internal and retained counsel⁷⁵ should be concerned about the degree to which a party meets its obligations to preserve inaccessible information. In *Phoenix Four, Inc. v. Strategic Resources Corporation*,⁷⁶ the court sanctioned a party and its law firm for failure to locate inaccessible information because it did not conduct a “methodical survey of [Defendants] sources of information” in the manner said to be required by the 2006 Amendments.

The Committee Note to Rule 26(f) suggests that counsel should become “familiar” with a client’s information systems to a sufficient degree necessary to permit discussion of potential issues that may be involved.⁷⁷ Local District Rules⁷⁸ and electronic discovery “guidelines”⁷⁹ often reinforce this expectation and in some cases mandate a degree of preparation beyond that implied by the Committee Note.⁸⁰

Consideration should also be given to implementing enhanced technology to improve internal processes. A diligent and cooperative effort with the IT functions of entities may yield opportunities for relatively cost-effective investments that will assist in managing inaccessible information.

The outsourcing of IT and document management functions and of less accessible information stores by many organizations imposes a need to be able to rely on the abilities of third parties to implement the hold procedures of their customer organizations when the third parties maintain ESI within their customers’ control.⁸¹ These obligations should be addressed specifically at the commencement of the relationship, and vendor management participation in preservation teams and processes can be important.

The degree to which a party must or should employ recently developed technology or revised business practices should be justified by business considerations. Information Management-related risks are recognized as a significant component of business risk,⁸² and many business expenditures on information technology can be leveraged for business and compliance purposes. Some organizations treat needs for compliant preservation activities as just one dimension of their need to gain greater control over their information assets and sensitive data.

75 The ABA Discovery Standards distinguish between the preservation obligations of a party and the responsibilities of its counsel. See ABA CIV. DISCOVERY STANDARDS (1999), as amended (August 2004) (limiting, in Standard 10, counsel responsibilities to those involving advice regarding preservation and consequences of failures). Compare *Zubulake v. UBS Warburg*, 229 F.R.D. 422, 435 (S.D. N.Y. 2004) (“*Zubulake V*”) (“counsel [both employed counsel and outside counsel] [are] responsible for coordinating her client’s discovery efforts. In this case counsel failed to properly oversee UBS in a number of important ways, both in terms of its duty to locate relevant information and its duty to preserve and timely produce that information”).

76 2006 WL 1409413 (S.D. N.Y. May 23, 2006).

77 A failure to acquire sufficient knowledge to engage in such discussions arguably violates the ethical obligation to provide competent representation. See ABA MODEL RULES OF PROF’L CONDUCT R. 1.1 (2002) (“legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation”). Compare *Thompson v. Jiffy Lube Int’l*, No. 05-1203-WEB, 2006 WL 3388502, at *2 (D. Kan. Nov. 21, 2006) (failure to take action regarding order relating to email system “raises serious questions about counsel’s experience, knowledge of applicable law, and resources available [to represent class]”).

78 See, e.g., E.D. & W.D. ARK. LOC. R. 26.1; D. DEL.R. 16(4)(b); D.N.J. LOC. CIV. R. 26.1; D. WYO. LOC. R. 26.1.

79 See “Guidelines for Discovery of Electronically Stored Information,” District of Kansas, ¶1, (Oct. 2006), available at <http://www.ksd.uscourts.gov/guidelines/electronicdiscoveryguidelines.pdf>.

80 See *Id.* at Paragraph 2 (requiring disclosure of “individuals with knowledge of their client’s electronic systems” prior to the conference). See Steven C. Bennett, *The Ethics of Electronic Discovery*, Vol. 17 No. 2 PRAC. LITIGATOR 45, 48 (Mar. 2006) (emphasizing the obligation to provide “competent” representation).

81 See *Tomlinson v. El Paso Corp.*, 2007 WL 2521806 (D.Colo. Aug. 31, 2007)(production of ERISA data maintained by third party must be produced as within custody and control).

82 Richard Hunter, *IT Risk: Turning Business Threats into Competitive Advantage*, Harvard Business School Press, 2007.

The business case for improvements in advanced search and storage options will necessarily continue to evolve. As recent and future technology substantially lessens the burdens and costs of locating relevant ESI on back-up media or in other less accessible information stores, technology to make archival systems more accessible and searchable also improves. Therefore, the periodic destruction of back-up media not needed for the disaster recovery purposes for which they were designed, and the reliance for archival and preservation purposes on more accessible and searchable media designed for those purposes, is likely to remain good practice. We currently have active Working Groups in the areas of 1) electronic document retention and production; 2) protective orders, confidentiality, and public access; 3) the role of economics in antitrust; 4) the intersection of the patent and antitrust laws; (5) Markman hearings and claim construction; (6) international e-information disclosure and management issues; and (7) e-discovery in Canadian civil litigation. See the "Working Group Series" area of our website www.thesedonaconference.com for further details on our Working Group Series and the Membership Program.

THE SEDONA CONFERENCE® COMMENTARY ON ACHIEVING QUALITY IN THE E-DISCOVERY PROCESS

*A Project of The Sedona Conference® Working Group
on Best Practices for Document Retention and
Production (WG1)*

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Preface and Acknowledgement

Welcome to another major publication in The Sedona Conference® Working Group Series: *The Sedona Conference® Commentary on Achieving Quality in the E-Discovery Process*. This effort is an outgrowth of our Working Group on Electronic Document Retention and Production (WG1) and represents the work of a diverse group of lawyers and representatives of firms providing consulting and legal services.

The mission of Working Group 1 of The Sedona Conference has been to provide the bench and bar with educational guides with the aim of describing what constitute best practices in the area of e-discovery. The present Commentary recognizes that the exponentially increasing volume of electronically stored information that is stored and made subject to litigation, investigations, and regulatory activities, necessitates fundamental changes in thinking and practice on the part of the legal profession. As outlined here, these include greater reliance on automated methods in gauging the quality of document productions, including the use of sampling and other forms of measurement, as well as greater attention paid to project management of the e-discovery process. This Commentary is intended to be read in conjunction with *The Sedona Conference® Commentary on the Use of Search and Information Retrieval Methods in E-Discovery* (2007), which recognized the need for automated processes being utilized to find relevant electronic evidence, and urged that best practices include new ways of thinking about that subject. As is the case with respect to prior commentaries, we fully understand that the matter of what constitutes best practices in maintaining “quality” in a particular legal case will necessarily be subject to change, given the accelerating pace of technological developments that the law is struggling to keep up with. We hope that our efforts will assist the legal profession in this area, and we welcome all feedback at tsc@sedona.net.

The present Commentary was originally conceived at the Mid-Year Meeting of WG1 in Phoenix, Arizona, in the Spring of 2007. Through the efforts of many individual contributors, several successive drafts were prepared for comment by the full WG1 membership in successive mid-year and annual meetings. I especially want to acknowledge the contributions to the overall success of this project made by Jason R. Baron and Macyl A. Burke, who took the lead roles in editing the Commentary, and managing the efforts of the editorial team, respectively. I also wish to acknowledge the invaluable editorial assistance provided by senior contributing editor Thomas Y. Allman, as well as the drafting contributions and editorial comments provided by members of The Sedona Conference® along the way, including (in alphabetical order): David Baldwin, Todd Elmer, Maura Grossman, Joe Guglielmo, Bruce Hedin, David Kessler, Joan Krammer, Kate Krause, Brandon Leatha, Mike Leonard, David McCann, Joe Looby, Tim Moorehead, Chris Paskach, Herbert Roitblat, Catherine Ronis, David Wetmore, and Thom Wisinski. I am most grateful that several leading experts in statistics, including Ian Ayres, Douglas Hubbard, and Kenneth Wachter, volunteered their time in reviewing one or more successive drafts. I wish to further acknowledge that many other individuals in WG1 and the RFP+ Vendor Panel spent time in providing comments and collaborating on earlier proposals for material to be included in the Commentary. Finally, on behalf of The Sedona Conference®, I wish to thank everyone involved in devoting their time and attention during the drafting and editing process.

Richard G. Braman
Executive Director
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April 2009

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Executive Summary

The legal profession is at a crossroads: the choice is between continuing to conduct discovery as it has “always been practiced” in a paper world — before the advent of computers, the Internet, and the exponential growth of electronically stored information (ESI) — or, alternatively, embracing new ways of thinking in today’s digital world. Cost-conscious clients and over-burdened judges are demanding that parties now undertake new approaches to solving litigation problems. The central aim of the present Commentary is to introduce and raise awareness about a variety of processes, tools, techniques, methods, and metrics that fall broadly under the umbrella term “quality measures,” and that may be of assistance in taming the ESI beast during the various phases of the discovery workflow process. These include greater use of project management, sampling, and other means to verify the accuracy of what constitutes the “output” of e-discovery. Such collective measures, drawn from a wide variety of scientific and management disciplines, are intended only as an entry-point for further discussion, rather than any type of all-inclusive checklist or cookie-cutter solution to all e-discovery issues.

While the notion of expressly building in and accounting for “quality” may appear somewhat novel in the legal discovery context, there is no shortage of competing ideas about quality methods and techniques in the greater world. These include the philosophies and combined works of such individuals as Joseph Juran on quality control,¹ W. Edwards Deming on “quality management” (TQM) and “statistical process control” (SPQ),² Armand V. Feigenbaum on “total quality control” (TQC),³ Phil Crosby on “zero defects,”⁴ Bill Smith of Motorola and “Six Sigma,”⁵ as well as “Capability Maturity Model Integration” (CMMI),⁶ and a host of Japanese “lean” methods, including Kaizen (continuous improvement).⁷

As used in this Commentary, the term *quality control* involves the specific procedures, tools and techniques that ensure high quality is maintained throughout various stages of the e-discovery process (i.e., while people are conducting specific tasks). *Quality assurance*, on the other hand, refers to the methods and metrics used at the end of the process to assess and ensure that an e-discovery process is complete and accurate.

Sanctions aside, there are at least four reasons for seeking to assess the quality of an e-discovery process:

- Failure to employ a quality e-discovery process can result in failure to uncover or disclose relevant evidence which can affect the outcome of litigation.
- An inadequate e-discovery process may allow privileged or confidential information to be inadvertently produced.
- Procedures that measure the quality of an e-discovery process allow timely course corrections and provide greater assurance of accuracy, especially of innovative processes.
- A poorly planned effort can also cost more money in the long run if the deficiencies ultimately require that e-discovery must be redone.

1 JURAN'S QUALITY CONTROL HANDBOOK (J.M. Juran & Frank M. Gryna eds. 4th ed. 1988); see also "Joseph M. Juran," http://en.wikipedia.org/wiki/Joseph_Juran.

2 W. Edwards Deming, OUT OF THE CRISIS (1982); see also "W. Edwards Deming," http://en.wikipedia.org/wiki/W._Edwards_Deming; "Statistical Process Control," http://en.wikipedia.org/wiki/Statistical_process_control.

3 Armand V. Feigenbaum, TOTAL QUALITY CONTROL (1961); see also "Armand V. Feigenbaum," http://en.wikipedia.org/wiki/Armand_V._Feigenbaum.

4 Philip B. Crosby, QUALITY IS FREE: THE ART OF MAKING CERTAIN (1979); see also "Zero Defects," http://en.wikipedia.org/wiki/Zero_Defects.

5 See Paul Keller, SIX SIGMA DEMYSTIFIED (2005); KPMG, "Six Sigma in the Legal Department: Obtaining Measurable Quality Improvement in Discovery Management (2006)," http://www.us.kpmg.com/RutUS_prod/Documents/12/SSigma.pdf; see also "Six Sigma," http://en.wikipedia.org/wiki/Six_Sigma.

6 See Mary Beth, Chrissis et al., CMMI: GUIDELINES FOR PROCESS INTEGRATION AND PRODUCT IMPROVEMENT (2d. ed. 2006).

7 See M. Imia, KAIZEN: THE KEY TO JAPAN'S COMPETITIVE SUCCESS (1986); see also "Continuous Improvement," http://en.wikipedia.org/wiki/Continuous_improvement; G. Taguchi, INTRODUCTION TO QUALITY ENGINEERING (1986); see generally, William Truscott, SIX SIGMA: CONTINUAL IMPROVEMENT FOR BUSINESSES (2003) (comparatively summarizing many of the above "quality" methods).

Thus, the identification and use of best practices in collection, review and production are essential. Lawyers will always be free to decide how they choose to practice law; the market will, however, decide who the winners and losers are. Winning in e-discovery increasingly means adopting lean, efficient business practices. These practices include (but are not limited to) using project management and appropriate measures of quality to reduce costs and to mitigate risk.

Of course, the reasonableness of a party's discovery process must be evaluated on a case-by-case basis in the context of the value and importance of the matters in dispute, and no single practice, process or quality-checking measure should be assumed to be appropriate in any and all circumstances.

The discussion in this Commentary is based on the following guiding general principles:

Principle 1. In cases involving ESI of increasing scope and complexity, the attorney in charge should utilize project management and exercise leadership to ensure that a reasonable process has been followed by his or her legal team to locate responsive material.

The discovery phase of litigation is best conducted under the direction of the active leadership of an attorney, acting individually or as Team Leader,⁸ who is responsible for overseeing the full e-discovery process using project management and other skills and techniques. This individual or the team he or she leads should have sufficient experience in the various phases of e-discovery to effectively execute the management duties. Realistically, of course, it may be necessary to delegate the responsibilities for various phases of the process, but care must be taken to obtain regular status updates, maintain frequent contact with the team at all levels, and ensure the effective and appropriate dissemination of information to and from team members.

Principle 2. Parties should employ reasonable forms or measures of quality at appropriate points in the e-discovery process, consistent with the needs of the case and their legal and ethical responsibilities.

A producing party must make a "reasonably diligent search for e-mails and other electronic documents"⁹ sought in discovery, and parties are required to work cooperatively to formulate discovery plans which are embodied in pre-trial discovery orders.¹⁰ These processes can be enhanced by applying reasonable measures of quality such as using various forms of sampling at different phases of the process; using independent testing to report whether results can be replicated and confirmed; adopting reconciliation measures for different phases of the e-discovery process; and employing inspection to verify and report whether discrepancies were noted. The quality measures utilized should be adequately documented, by individuals qualified to do so, for later use in support of the process that has been employed.

Federal Rule of Civil Procedure 26(g)(1), which requires certification of accuracy and good faith in requesting and responding to discovery, necessitates a form of quality assurance by counsel based on an appropriate level of attention paid to ensuring accurate results. This is especially true given the exponential increases in the volume and sources of ESI in the average case, and the new discovery tools and processes that rely on automated means of collecting, filtering, searching, and reviewing massive amounts of potential evidence in the form of ESI. As discussed below, reasonable project management often entails using various forms or measures of quality at different phases of the process.

Principle 3. Implementing a well-thought out e-discovery "process" should seek to enhance the overall quality of the production in the form of: (a) reducing the time from request to response; (b) reducing cost; and (c) improving the accuracy and completeness of responses to requests.

The type of quality process that this Commentary endorses is one aimed at adding value while lowering cost and effort. A well-defined discovery process will include such measures as

⁸ See discussion, *infra* at Part II.A.2.

⁹ *Wingnut Films v. Katja Motion Pictures Corp.*, 2007 WL 2758571, at *5 (C.D. Cal. Sept 18, 2007).

¹⁰ *Board of Regents of Univ. of Neb. v. BASF Corp.*, 2007 WL 3342423, at *5 (D. Neb. Nov. 5, 2007) (emphasizing the duty to cooperatively plan discovery and affirmatively certify accuracy and good faith as part of an "open discovery process").

employing good project management practices that tailor the process to the specific case circumstances; using iterative and adaptive processes that allow for learning and correction; and, where appropriate, making use of statistically valid metrics in order to monitor progress and obtain valid measures of the accuracy of the effort.

Principle 4. Practicing cooperation and striving for greater transparency within the adversary paradigm are key ingredients to obtaining a better quality outcome in e-discovery. Parties should confer early in discovery, including, where appropriate, exchanging information on any quality measures which may be used.

Transparency and mutual cooperation between and among parties in the discovery process will contribute significantly to ensuring quality, maintaining best practices, and reducing claims of spoliation in complex e-discovery. The discovery phase should no longer be a place for extended argument and advocacy. Rather, discovery should be viewed as an opportunity for cooperation and transparency, in the spirit of Federal Rule of Civil Procedure 1.¹¹ The appropriate time for advocacy and argument arrives once discovery is completed — not before. See *The Sedona Conference® Cooperation Proclamation* (2008) (promoting “open and forthright information sharing, dialogue (internal and external), training, and development of practical tools”). It is a fundamental mission of *The Sedona Conference®* to persuade requesting and producing parties that collaboration and dialogue on matters concerning ESI are appropriate, if not necessary.

The meet-and-confer “conference” is best viewed as a *process*. It should start as early as practicable and should extend through the entire discovery lifecycle — identification, preservation, collection, search, review, and production — including discussions, where appropriate, on which search and review processes or technologies will be used, and what quality steps will be taken to ensure that these tools have accurately captured responsive documents. The thrust of the recent amendments to the Federal Rules of Civil Procedure has been open and forthright sharing of information by all parties and “removing contentiousness as much as practicable.”¹²

¹¹ Fed. R. Civ. P. 1 (providing that the rules governing procedures in civil actions “should be construed and administered to secure the just, speedy, and inexpensive determination of every action and proceeding”).

¹² *Board of Regents*, 2007 WL 3342423, at *5.

I. INTRODUCTION

“For the rational study of the law the black letter man may be the man of the present, but the man of the future is the man of statistics and the master of economics.”

— Oliver Wendell Holmes, *The Path of the Law* (1897)

Oliver Wendell Holmes was right, in ways he could not have imagined over a hundred years ago. Nearly a decade into the 21st Century, the legal profession faces the challenge of an exponentially increasing avalanche of electronically stored information with all of its attendant complexity.¹³ As recently characterized by one federal district court judge, “With the rapid and sweeping advent of electronic discovery, the litigation landscape has been radically altered in terms of scope, mechanism, cost, and perplexity. This landscape may be littered with more casualties than successes” *PSEG Power N.Y., Inc. v. Alberici Constructors, Inc.*¹⁴ Continuing to practice law in a manner divorced from what constitutes best practices drawn from other disciplines, and without concern for measures of “quality,” will increasingly end up as a recipe for failure.

Not surprisingly, the case law,¹⁵ industry literature¹⁶ and law firms seeking a “comparative advantage”¹⁷ have increasingly emphasized the quality measures to be undertaken during e-discovery. In *Victor Stanley v. Creative Pipe*,¹⁸ for example, one of the reasons a party failed to carry its burden of excusing inadvertent production of privileged documents was a lack of demonstration, *inter alia*, of “quality-assurance testing.”¹⁹

Our discussion of the role of quality builds upon Principle 11 of the Sedona Principles:

A responding party may satisfy its good faith obligation to preserve and produce relevant electronically stored information by using electronic tools and processes, such as data sampling, searching, or the use of selection criteria, to identify data reasonably likely to contain relevant information.²⁰

The Commentary to Sedona Principle 11 notes that:

Depending on the nature of the sources of data, both manual and automated procedures for collection may be appropriate in particular situations. Whether manual or automated, the procedures must be directed by legal counsel to assure compliance with discovery obligations. . . . *Regardless of the method chosen, consistency across the production can help ensure that responsive documents have been produced as appropriate.*²¹ (Emphasis added).

Achieving “consistency across the production” requires sound project-planning oversight and can often be enhanced by use of measurements of the quality of the outcome integrated into the overall e-discovery process. As management expert Peter Drucker once declared, “If you can’t measure it, you can’t manage it.”²²

13 See George L. Paul & Jason R. Baron, *Information Inflation: Can The Legal System Adapt?*, 13 RICH. J.L. & TECH. 10 (2007), <http://law.richmond.edu/jolt/v13i3/article10.pdf>.

14 2007 WL 2687670, at *1 (N.D.N.Y. Sept. 7, 2007).

15 See *William A. Gross Construction Associates, Inc. v. American Manufacturers Mutual Insurance Co.*, 2009 WL 72495, * 1 (S.D.N.Y. March 19, 2009) (“This Opinion should serve as a wake-up call to the Bar in this District about the need for careful thought, quality control, testing, and cooperation with opposing counsel in designing search terms or keywords to be used to produce emails or other electronically stored information”); *In re Sequel Products Liability Litigation*, 244 F.R.D. 650, 662 (M.D. Fla. 2007) (“Common sense dictates that sampling and other quality assurance techniques must be employed to meet requirements of completeness” and “[i]f [defendant] took such steps, it has not identified or validated them”).

16 See, e.g., Ashish Prasad, Kim Leffert and Shauna Fulbright-Paxton, “Cutting to the Document Review Chase,” *Business Law Today* (Nov./Dec. 2008), at <http://www.abanet.org/buslaw/blt/2008-11-12/prasad.shtml> (highlighting need for quality control during document review); “Affordable, Reliable, Quality Assured E-Discovery Services,” at <http://www.bostonlit.com/services.htm> (promising “an accurate and legally defensible report outlining exactly what was done with your data”); Doug Greene, “Document Review (Part 2 – Planning, Organizing and Managing)” (March 14, 2009), at <http://www.ediscoveryevangelist.com/2009/03/document-review-part-2-planning.html> (management section of a document review plan should include quality control procedures in place).

17 Thomas E. Stevens and Wayne C. Matus, *Gaining a Comparative Advantage in the Process*, NAT’L L. J., Aug. 25, 2008 (suggesting use of quality-assurance techniques such as sampling to check results), reprinted at <http://www.law.com/jsp/legaltechnology/pubArticleL1.jsp?id=1202424251053>.

18 250 F.R.D. 251 (D. Md. 2008).

19 *Id.* at 262.

20 See *The Sedona Principles, Second Edition: Best Practices, Recommendations & Principles for Addressing Electronic Document Production* (2007) [hereinafter *The Sedona Principles, Second Edition*], http://www.thesedonaconference.org/content/miscFiles/TSC_PRINCP_2nd_ed_607.pdf.

21 *Id.* at 58 cmt. 11.c.

22 “The Coming of the New Organization,” HARV. BUS. REV. (Jan.-Feb. 1988) at 70.

The ultimate goal in discovery is to identify, collect and cull documents and ESI from a larger corporate or institutional data universe and then search for and retrieve the relevant or responsive non-privileged materials with whatever tools or methods have been made available (whether automated, human, or some combination of the two). Where appropriate, the process should incorporate some form of useful metrics to quantify the accuracy of the resulting output.

There is no single “best way” through the e-discovery maze. A Department of Justice investigation of price-fixing by executives of a publicly-traded corporation may demand that a very different form of e-discovery process be adopted than a routine commercial dispute involving formation and performance of a commercial contract. In the first case, counsel may want to review every document in the possession of these important custodians to master the issues and the facts of the case and to ensure that no “hot” documents are missed, even if it means reviewing a large amount of non-responsive material. In the second case, using automated tools to identify the potentially responsive documents (typically, for later human review prior to production), with sampling to test whether the remaining documents are non-responsive may be adequate to the task. In both examples, however, pro-active leadership will require appropriate analysis of the suitability of the methods.²³ In determining the resources to be allocated, the amount of risk of overlooking relevant or privileged material will be weighed against the advantages of automation, efficiency, and cost savings.

This Commentary is not intended to serve as a comprehensive roadmap covering all possible uses of quality measures and metrics throughout the e-discovery process. The creativity of the vendors and the bar will ensure that concrete applications of quality techniques will be advanced. Nor have we any bias towards particular methods, tools or technologies or a point of view that asserts that sampling or other types of quality measures are invariably required in every type of litigation. Indeed, the drafters believe that the solution to problems created by scale are not solved by technology *per se*, which is merely a tool, but by better use of team leader skills, project management, and quality measures.

Part II. A contains a discussion highlighting the importance of a thoughtful, well-defined e-discovery process, as well as the need for project management by an attorney in charge as team leader. Part II.B makes the case for why quality matters, and provides examples of five general measures of quality as benchmark guidance. Part II.C summarizes judicial approaches to sampling. Part III consists of *selected* examples of how quality measures may be applied in various phases of e-discovery, including data collection, review, and production. For the reader so inclined, Appendix A contains a primer on statistical sampling.

II. ACHIEVING QUALITY THROUGH PROJECT MANAGEMENT AND BETTER MEASUREMENT

A. THE IMPORTANCE OF PROJECT MANAGEMENT

1. The Need For a Well-Defined Process

Before embarking on any complex e-discovery project, it is important to recognize, first and foremost, the importance of the process that manages the task, whether it involves “simple” human review or application of automated tools and more sophisticated techniques. Successfully meeting the challenges posed by the large and heterogeneous document collections that are common in e-discovery requires a range of contributions – by people, by technology, by methodology, and so on. Technologically advanced tools, however “cutting edge” they may be, will not yield a successful outcome unless their use is driven by people who understand the circumstances and requirements of the case, as guided by thoughtful and well-defined methods, and unless their results are measured for accuracy. The first step, then, is the development of a well thought-out process in which the applicable review method can be applied.

²³ In particular, it is crucial to make good strategic and tactical decisions about how to go about locating relevant evidence in a body of collected ESI either before or during the review process. To that end, the present Commentary dovetails, and should be read in conjunction with, *The Sedona Conference® Best Practices Commentary on the Use of Search and Information Retrieval Methods in E-Discovery* (“*Sedona Search Commentary*”), 8 *Sedona Conf. J.* 189 (2007), which more narrowly focuses on new ways of thinking about issues involving search and information retrieval.

Some of the key process elements that lay the groundwork for the effective application of technology are listed below. An effective process will usually include most, if not all of these elements:

Leadership. The process should be led by a person who will be responsible for assuring that a discovery process reflects a reasonable good-faith effort to be complete and accurate.

Tailoring. The discovery process should be tailored to the specific size, risks, needs and circumstances of the case or investigation that is the occasion for the retrieval effort.

Expertise. The effort should incorporate and draw on the appropriate range of expertise required to meet and accomplish the goals set for it in a timely and cost-effective manner.

Adaptability. The process should be iterative and adaptive, allowing for learning and course correction as the project unfolds.

Measurement. Where appropriate, elements of the process should employ metrics in order to monitor the progress of the effort and to ensure consistent quality of results.

Documentation. The overall process should be documented to ensure coordination and communication within the discovery team and to increase the defensibility of the process.

Transparency. The selection, design, implementation, and measurement of a process should be able to be explained in a clear and comprehensive way to the relevant fact-finder, decision-maker, tribunal, or regulator, as well as to opposing counsel as may be appropriate.

2. Project Management and The Need For A Team Leader

The overall quality of any e-discovery project will be enhanced by paying increased attention to project management — a discipline popularized by Henry Gantt, with roots in a variety of fields, including construction, engineering, and defense.²⁴ In a nutshell, project management “is the discipline of organizing and managing resources (e.g., people) in such a way that the project is completed within defined scope, quality, time and cost constraints.”²⁵ An almost universal key to the success of any project is the appointment of a project leader, whose responsibility is to:

Lead the team in figuring out what the project is (planning, scheduling, and requirements gathering), shepherding the project through design and development work (communication, decision making, and mid-game strategy), and driving the project through to completion (leadership, crisis management, and end-game strategy).²⁶

Applied to the process of e-discovery, it is essential that the role of project leader be clearly and decisively vested in one or more individuals who are empowered by the client to manage the effort of counsel and service providers. This function is often filled by a designated outside counsel but may, in some cases, be handled by internal client counsel. To borrow an analogy from the construction field, the leader is the “Legal Architect.” In deference to the terminology more often used in the litigation context, and the fact that a combination of expertise and talent often is required, we refer to that individual as the “lead e-discovery attorney in charge,” or, most concisely, the “Team Leader.”²⁷

The Team Leader, working with the client and the service provider(s), will define the project’s budgets, goals and objectives and develop a plan for achieving the tasks and activities that need to be performed. He or she must understand both the substantive and strategic aspects of the

²⁴ In 1917, Henry Gantt developed the “Gantt Chart,” a tool used for scheduling work (first in factories) using a standard format for the display of scheduling information. Kathy Schwalbe, INFORMATION TECHNOLOGY PROJECT MANAGEMENT, 30 (5th ed. 2007). See generally “Project Management,” http://en.wikipedia.org/wiki/Project_management.

²⁵ *Id.*

²⁶ Scott Berkun, THE ART OF PROJECT MANAGEMENT 8 (2005).

²⁷ The use of the singular here and *passim* is not intended to exclude the possibility that in certain legal contexts, one or more “lead” attorneys with clearly defined duties may end up playing a substantial role in facilitating the overall e-discovery team effort.

litigation. Where possible, the Team Leader should have experience in the various phases of e-discovery and, to the extent feasible, should balance his or her role in developing the facts of the case, interviewing witnesses, and so forth, with leadership of the team efforts in discovery.

Among other things, the Team Leader should obtain regular updates and ensure the effective and appropriate dissemination of information to team members. While it may not be practicable to talk with every team member every day, it may be necessary to have daily communication with at least some team members in order to carry out this function effectively.

Given the highly specialized nature of some e-discovery tasks, such as processing of information, the availability of competent assistance, including that of third-party vendors, is often essential.

The Team Leader, or other counsel participating in the discovery process, will typically be required by court or agency rules governing production to sign the discovery responses, an act which has consequences if the court or agency subsequently challenges the diligence and accuracy of the effort.²⁸ Because of the sheer volume of ESI, we are in “an age of electronic discovery when attorneys may not [be able to] physically touch and read every document within the client’s custody and control,”²⁹ and attorneys bound by the rules must be sufficiently comfortable in making such a certification that reasonable, good-faith efforts have been made to locate and produce the responsive material called for by the document or information request. Where responsibility and accountability for different phases of the discovery process have been divided, it will be necessary for the reliance by the certifying attorney on the efforts of the team member to be “reasonable.”³⁰ In such circumstance, it is important that the parties communicate effectively with each other to help ensure a seamless, reasonable and defensible overall process.

A more comprehensive discussion of the advantages of project management is beyond the scope of the present paper. However, as is increasingly being recognized,³¹ the discipline may yet hold great promise in terms of providing lawyers exercising a leadership role with a coherent framework for managing large-scale e-discovery endeavors of all kinds.

B. THE NEED TO MEASURE QUALITY IN E-DISCOVERY

The concept of quality — long an important consideration for many business processes, especially, as discussed, in manufacturing — increasingly is being applied to the e-discovery process. In the e-discovery context, the assurance of quality deals with the usefulness of the results of a given task, as measured by the likelihood that a particular tool or method has adequately and accurately collected or captured responsive documents and ESI.

What are the barriers to successful adoption of quality measures in e-discovery? For one thing, the variety and changing needs of cases have necessitated an ad hoc approach to discovery management.³² Moreover, in many cases important parts of a process are delegated to third parties or rely upon complex processes and software managed by third parties, thus requiring reliance upon the incorporation of appropriate quality tests and measurement in those

28 Under Federal Rule of Civil Procedure 26(g), for example, one who signs a discovery response is deemed to have certified that, to the best of the person’s knowledge, information and belief “formed after a reasonable inquiry” that the response is “complete and correct” at the time of its making and is not interposed for an improper purpose. See *Mancia v. Mayflower*, 253 F.R.D. 354, 361 (D. Md. 2008) (noting that Rule 26(g) requires “approaching the process properly in accordance with the letter and spirit of the discovery rules”); accord, *Cache La Poudre Feeds v. Land O’Lakes*, 244 F.R.D. 614, 628-630 (D. Colo. 2007) (noting that counsel is required to undertake a reasonable investigation to identify and preserve relevant materials in course of responding to discovery requests).

29 *Qualcomm, Inc. v. Broadcom Corp.*, 2008 WL 66932 at *8 (S.D. Cal. Jan. 7, 2008), *vacated in part and remanded*, 2008 WL 638108 (S.D. Cal. March 5, 2008).

30 Where in-house counsel performs the efforts to search and produce, certifying counsel may rely “on assertions by the client and on communications with other counsel as long as that reliance is appropriate under the circumstance.” Advisory Committee Note, Rule 26, Subdivision (g) (1983). Cf. *Qualcomm, supra*, n.29. One way that certifying counsel can do this is to forward the draft discovery request, response, or objection electronically to in-house counsel (and where appropriate, the relevant in-house IT representative), to facilitate review and confirmation that the submission is complete and accurate before it is served or filed.

31 See, e.g., Jeane Thomas & Ben Hawksworth, *Master Mining: Three Views on EDD Project Management*, *LawFirm Inc.* (March/April 2006), http://www.lexisnexis.com/applieddiscovery/NewsEvents/PDFs/200604_LawFirmInc_MasterMining_EDD.pdf; Courtney Ingraffia Barton, “Project Planning: A Sample of Key Questions to Ask,” *id.*

32 Litigation projects involving custom specifications defined by the user, while highly configurable and flexible, lead to a non-standardized approach that does not lend itself to repeatability and inherent engineered quality.

processes.³³ Finally, there is considerable confusion about how to best define and measure the quality of the outcome, in the absence of a universally acknowledged standard of acceptance. In traditional discovery, that standard has always been one of reasonableness, rather than perfection, and this Commentary is not intended as arguing to the contrary.³⁴

1. Why Does Quality Matter?

Faced with uncertainty surrounding the issue, some lawyers may ask if assuring quality in electronic discovery is really that important. Sanctions aside, we believe quality is extremely important, for four principal reasons:

First, failure to employ a quality e-discovery process can result in failure to uncover or disclose key evidence. This reason is the most compelling and, potentially, the one with the greatest consequences for a party involved in a case. A simple example: if search terms are used without quality testing, they may not find the lone exculpatory document, or the “hot” document (and its many near duplicates) that can be used to convince an opponent to settle a matter — or to convince the party itself to settle. Depending on the size and scope of the case, the implications can be expensive and far-reaching.³⁵

Second, a poorly conceived or managed e-discovery process may allow privileged or confidential information to be inadvertently produced.³⁶ This is probably the most common concern that prompts counsel to strive to perform a resource-intensive manual review of electronic documents, with the attendant prohibitive increase in costs. For example, there are frequently aspects of collection and review that involve corporate intellectual property, trade secret and otherwise confidential ESI. A quality process identifies these items and designates them for protective treatment earlier rather than later in the process.

Third, e-discovery processes that measure quality are more defensible because they provide metrics and, if properly implemented, allow for course corrections. Measuring the quality of discovery processes as they occur, or reasonably soon thereafter, allows the attorney(s) functioning as Team Leader to determine if the discovery processes are working in the manner intended, or if there is a systemic or systematic error that is biasing or corrupting the results, and that necessitates some kind of modification.

Fourth, poor quality can also cost a party more money in the long run if deficiencies are noted in the documents produced, motion practice ensues and, if in the end e-discovery must be redone. The fact is that, although higher quality historically came at a higher cost, that is not necessarily the case today. It is often less expensive to engineer quality into the process than to add it on after the fact. Today, many quality programs require that the process implemented must measure, track, and report the savings that will be realized from the application of that process.

These points raise a related issue that the parties involved in e-discovery should know: the distinction between quality control and quality assurance.

Quality control involves engineering quality into the actual process. It reflects the procedural safeguards that are built into the process to ensure high quality throughout, and it takes place while people are conducting specific tasks. For example, if someone is moving 10 items from point A to point B, the quality control step in that process would be to count the items before the move and after the move to ensure that all of the items were transferred (i.e., a “reconciliation”). This Commentary suggests that quality control should be built in to the e-discovery process.

33 See Rachel Ford, *Quality Assurance and Quality Control Take Center Stage*, <http://www.lexisnexis.com/AppliedDiscovery/clientResources/spotlight4.asp> (discussing performance speed, usability, security, data validation, compatibility and regression testing as quality features of systems used).

34 While the reasonable standard is not a bright-line rule and lends itself to ambiguity, confusion and, at times, disputes, it also is a standard that is easily adaptable to the numerous different discovery contexts and cases.

35 See, e.g., *Qualcomm*, *supra*, n.29.

36 See, *Victor Stanley*, *supra*, n.18.

Quality assurance, on the other hand, typically takes place after the process is complete; where one must make an assertion as to what was done, how well it was done, and whether the output met a certain predetermined standard. Quality assurance generally refers to the procedures designed to serve as the basis for certifications and reliance. Because quality assurance generally involves an intensive third-party audit of process and activities, it can be much more intensive and expensive — particularly in a large, complex e-discovery process. For many e-discovery projects, a full-scale quality assurance process may not be practical or financially feasible, and thus would be unwarranted.

Five principal measures of quality are especially useful in regard to e-discovery.

2. Five Measures of Quality

a. Judgmental sampling

Accountants typically use a form of judgmental sampling as a form of quality control to find material misstatements where there are many similar financial transactions, greatly reducing the cost of the audit while maintaining its integrity. A typical example is accounts payable, where a large number of invoices pass through and are subjected to the same procedures, thus allowing representative samples to be drawn.³⁷

What can be described as “judgmental sampling” has also been used in traditional discovery.³⁸ Attorneys often select a few random or significant folders of electronic documents coded by a particular reviewer to determine if he or she is making the correct responsiveness calls. Upon review of the results of the judgmental sample, the more senior attorney may, based on the exercise of informed judgment, request additional samples and may require a heightened second-level review if the perceived error rate is unacceptable. A judgmental sample, unlike a statistically valid sample, does not permit one to make statements based on scientific proof about the population the sample was drawn from with statistical confidence, but can nevertheless be very helpful.³⁹

This method is especially useful as a quality check on discretionary processes such as collection and review. For example, an experienced professional can review a report from the collection phase that lists evidence sources collected for each custodian, and may identify gaps in the collection (e.g., a hard drive was not collected for a particular custodian). The professional selects this and other apparent exceptions and has staff research the anomaly and perform remedial action (e.g., collect the hard drive) or annotate the collection report (e.g., note that the individual does not use a personal computer), as appropriate.⁴⁰

The selection of keywords as search terms for responding to discovery requests is a special form of judgmental sampling based on many factors, including prior knowledge as well as educated guesses with respect to what a collection of ESI may contain.⁴¹ There will always be some measure of informed judgment to be applied in the selection of search or filtering criteria at various phases of e-discovery. Notably, the initial results produced by human judgmental sampling can be further refined through greater use of iterative processes.⁴²

b. Independent testing

Third-party professionals can be retained to examine a process or approach, and to report on whether results can be replicated and confirmed. One such example might be automated or highly technical processes, such as processing, searching and production operations which have been challenged on the basis of repeatability and accuracy. Thus, a native file-processing application (i.e.,

³⁷ Janet L. Colbert, *Audit Sampling*, INTERNAL AUDITOR (Feb. 1, 2001), at 27.

³⁸ The distinction between “judgmental” and “statistical” sampling is discussed in more detail in the Appendix (“Sampling 101 for the E-Discovery Lawyer”).

³⁹ The reviewer may be aware of, and take into account, the source of the documents, the size of the populations, the types of information at issue and the degree to which the results conform to other sources of oral, written, or physical testimony or evidence.

⁴⁰ Similarly, an experienced professional can review a report from the review phase that lists the documents marked or reviewed by reviewer, per hour, or relevant documents per custodian and from a high level may be able to identify outliers or other unusual patterns.

⁴¹ See *Sedona Search Commentary*, supra n.23, passim.

⁴² See G. Paul & J. Baron, *Information Inflation*, supra n.13.

software that converts files from their “native” or “proprietary” form into a generic form, such as .TIFF images, for further processing) might be tested. Such tests can help confirm (or disconfirm) the software’s reported efficacy at completely extracting files from an e-mail container, accurately displaying such files for review, and completely indexing the searchable text in such files. Currently, these “black box” technologies are often only described by what they can do — not by what they cannot do — leaving the industry in a caveat emptor situation. This is expected to change, as there have been a few widely reported deficiencies in the capability of certain native file processing technologies to completely render e-mail, extract embedded objects, search compound documents or containers, extract metadata, and the like.⁴³

c. Reconciliation techniques

Reconciliation to account for the impact of a process (i.e., comparing inputs to outputs) has long been used in the fields of accounting, manufacturing and engineering, and may have some applicability to the e-discovery process. Thus, applying reconciliation to the e-discovery process might involve comparing what volumes of e-mail or ESI entered a process, what remains in a process (after, for example, de-duping), and what exits a process. This can be extremely helpful in determining whether e-mail or other files were handled correctly and in identifying gaps in the process that may have resulted in the omission or incomplete handling of files.⁴⁴

d. Inspection to verify and report discrepancies

Inspection and observation of participants in the e-discovery process resembles the original form of quality review which was part of the apprenticeship model for training junior attorneys. Inspection is especially useful as a quality check on processes such as collection and review. The deployment of seasoned experts to inspect and observe the performance of tasks by less-experienced staff can improve quality on a project. For example: during collection, it is often advisable to have senior legal and technical participants involved in the initial custodian interviews. Experienced staff can coach less-experienced staff, as well as further define or refine the process (such as by improving the custodian interview questionnaire). During the review phase, it is equally advisable to improve quality by having a seasoned reviewer observe the review and provide guidance. This should be done on a frequent and iterative basis.

e. Statistical sampling

The concept of measuring the quality of the output of a process by sampling is not new. Acceptance sampling,⁴⁵ for example, was used by the US military 60 years ago to test the quality of bullets manufactured for use during WWII and to spot design defects and improve production.

Today, some form of acceptance sampling is used as a quality control tool by virtually every large and medium-sized manufacturing company in the world. For example, Boeing’s instructions to its suppliers require that they “perform either 100% inspection or acceptance sampling for receiving inspection.”⁴⁶ This can be seen as a fundamental type of quality control, which is composed of many methods, depending upon the application.

Standards organizations such as the International Standards Organization (ISO), a network of the national standards institutes of 157 countries, have created procedures and guidelines for acceptance sampling. Statistical sampling is also required by many governmental agencies to test the quality of a given population of products.⁴⁷

⁴³ One additional method to verify systems and processes is to employ “known sample” testing, where systems and processes are applied to a known collection with defined characteristics to measure the results. This is very useful in establishing the basic scope and functionality of search systems and review protocols. In particular, this method is used by legal service providers to test prospective reviewers against a “test folder” of already-coded documents, to establish how well the reviewers can absorb and apply a given review protocol.

⁴⁴ Reconciliations from the phases before and after native file processing are extremely complex.

⁴⁵ First introduced in the 1920’s by Walter A. Shewhart, this approach is referred to as “Statistical Process Control,” and uses statistical tools to observe the performance of the production line to predict significant deviations that may result in rejected products. By maximizing the efficiency of war production, William Edwards Deming popularized the use of this quality control method.

⁴⁶ The Boeing Co., Quality Assurance Manual, at D8-4890.105 (2001), <http://www.boeing.com/companyoffices/doingbiz/terms/d8-4890.105.pdf>.

⁴⁷ For example, the U.S. Department of Agriculture uses sampling plans to test the quality of most of the products it regulates and has codified sampling requirements in Title 7, § 43 of the U.S. Code. The Internal Revenue Service allows the use of sampling estimates by taxpayers to determine amounts where other estimates are not feasible.

As noted, statistical sampling permits statements to be made about the population from which the sample was drawn with statistical confidence and is helpful when one wants to get as close to the truth as possible, but time and cost prohibit the testing of each item, or such testing is technically infeasible. It is a “scalable solution,” one that works well regardless of the size of the sampled population.

In the e-discovery context, statistical sampling can serve as a check on the effectiveness of search terms and other automated tools in identifying responsive information and on the reviewers’ ability to correctly code documents. A party could identify a statistically valid document sample that the tools or search terms did not identify as potentially responsive and review them for responsiveness. By doing so, the party can provide an estimate of the number of responsive documents appearing in the documents that were not selected for review. Based on the results of such testing, the parties can take informed actions such as modifying the search terms or applying other methods to close the gap between what was selected and what was responsive.

Statistical sampling can also be used to measure the probable error rate for a project, a key custodian’s documents, or even for a specific document reviewer. An acceptable error rate can be defined, and document groups with error rates above this threshold can be re-reviewed and re-tested until the results meet or exceed the quality standard.⁴⁸

3. When Are Quality Measures and Metrics Appropriate?

While some or all of the preceding techniques can be helpful in measuring and improving the quality of e-discovery, there is no universal consensus on when and how they should be applied or even what constitutes a quality process. Nor can one expect to simply transfer “off the shelf” industrial techniques to e-discovery.⁴⁹ That is why, to the extent practical, parties should agree at the outset on which quality-based tools and techniques, if any, should be used during each phase of e-discovery and how assertions of quality will be made and where appropriate, measured.

Because it is not practical to apply every (or any) metric to every step in every case, legal teams must prioritize and agree which quality measures get applied where, based on various factors that include, among others, the value of the claims or damages, the size and complexity of the case, and the time and resources the parties have to spend on the matter. Clients, opposing parties, courts and regulators may have a very important say in the selection of these procedures as well.

In the case of complex matters — for instance, an SEC or criminal investigation — a team may opt or be required to do judgmental sampling, independent tests, and inspections as every phase unfolds, and then do statistical sampling, reconciliations and independent testing at the end of the process because money is no object and the process must be as complete as it can be.

At the other end of the spectrum may be a very small case where the use of quality metrics likely would be light, if they were even used at all. In other words, the marginal utility of an assessment of the quality of the process must be weighed against and proportional to the burdens and costs involved and the anticipate benefits.

Some of the other types of questions to consider in assessing the appropriateness of the use of quality methods and metrics are:

48 For example, a review team has a set of documents to review for a particular custodian, say 100,000. A smaller team can then review a random sample of those documents to determine how many were incorrectly coded (either as responsive or non-responsive). The team would also decide an acceptable error rate, e.g., 5%. If the number of incorrectly coded documents for the particular custodian is above this threshold the team can review additional documents, conduct searches if there was a common error in coding (e.g., an issue missed by a number of reviewers). The team would then perform another random sample to determine whether the error rate is now within the established, acceptable threshold.

49 In analyzing the quality of a given review process in ferreting out “responsive” documents, one may need to factor in a scale of relevance — from technically relevant, to material, to “smoking gun”— in ways which have no direct analogy to the industrial-based processes referenced above. Indeed, most quality applications assume one is looking at independent and fairly homogenous events (i.e., events of similar or like character), with an implied inference that probability affects each item equally. This may or may not be the case in the e-discovery context, and therefore it may be important to understand notions of variance and how much variance should be tolerated coming out of a given process.

- Whether and how quality measurement tools and methods will be used? Will quality measurement be made as part of a culling function, or further downstream, at the stage of relevance assessment?
- Who will be applying the tools and methods? Will they be applied by specialists or by non-specialists (e.g., attorneys, paralegal and/or litigation support staff)? If by the latter, consideration must be given to the transfer of case-specific knowledge to the users, to the training of the users in their effective use, and to the overall usability of the tools and methods themselves.
- How will the output be used? Will the tools and methods be used for testing or assessment purposes only (e.g., in order to learn more about the target collection, in order to navigate more efficiently through the documents, in order to prioritize the review, and so on), or will they be used to discern what should receive further review from what should not?

4. The Need For Documenting A “Quality” Process

Employing the above measures of quality in e-discovery may be prudent, even necessary, in many settings; however, failure to adequately document the steps taken to sample, test, inspect, reconcile, or verify one’s results, may affect the outcome of particular litigation. In *United States v. O’Keefe*,⁵⁰ consistent with earlier case law,⁵¹ the Court noted the importance of providing a court with appropriate explanations in cases where the parties have not agreed upon the use of keywords and the search task is performed unilaterally.⁵² In *Victor Stanley*, the Court found that defendants were “regrettably vague” in describing their selection of keywords as to “how they were developed, how the search was conducted; and what quality controls were employed to assess their reliability and accuracy.”⁵³ Accordingly, the Court went on to hold that attorney-client privilege had been waived. Challenges in that type of situation should be explained by one qualified to do so, not merely by conclusory arguments by counsel.⁵⁴ Documenting the process employed will also be helpful in situations where courts pro-actively encourage parties to cooperatively discuss sampling and other protocols used as part of the overall discovery plans.⁵⁵

At the outset of any quality e-discovery process, the attorney in charge or Team Leader should set out the documentation standards and controls to be employed, so as to ensure their ultimate defensibility. He or she should act under the assumption that there will be a discovery challenge to every aspect of the process employed, and include quality measures in the overall project plan. This entails updating documentation along the way, as decisions are made, to best assure that declarations and other statements regarding the outcome of the process will be adequately supported if and when the need arises at a later time.

C. JUDICIAL APPROACHES TO SAMPLING

The Federal Rules of Civil Procedure expressly acknowledge the use of “sampling” as a means of reducing what the drafters recognized as the enormous burdens posed by the volume of ESI in litigation. For example, in connection with Rule 26(b)(2)(B), the Advisory Committee noted the affirmative role that sampling may play when assessing if “good cause” has been shown to order production. Thus, the Committee Note to the Rule provides that “[p]arties may need some focused discovery, which may include sampling of the sources, to learn more about what burdens

⁵⁰ 537 F. Supp. 2d 14 (D.D.C. 2008).

⁵¹ See *Judicial Watch, Inc. v. U.S. Dep’t of Justice*, 185 F. Supp. 2d 54, 64 (D.D.C. 2002) (expressing inability to determine if a search was “reasonably calculated” to recover documents where the party failed to explain keywords used).

⁵² *Accord, Equity Analytics, L.L.C. v. Lundin*, 248 F.R.D. 331 (D.D.C. 2008) (involving file extensions).

⁵³ 250 F.R.D. at 256. See also *Walter A. Gros Construction Associates, Inc., supra*, n.15 (highlighting need for attention being paid to quality control in developing search terms); *Rhoads Indus., Inc. v. Bldg. Materials of Am.*, 254 F.R.D. 216, 224 (E.D. Pa. 2008) (referencing need for “proper quality assurance testing,” citing to *Victor Stanley*).

⁵⁴ 250 F.R.D. at 261, n.10 (to be accomplished by “affidavits or other equivalent information from persons with the requisite qualifications and experience”).

⁵⁵ See, e.g., *Columbia Pictures Indus. v. Bunnell*, 2007 WL 2080419, at *14, n.32 (C.D. Cal. May 29, 2007) (court “encourages the parties to meet and confer regarding sampling”); *Zurich American Ins. Co. v. Ace American Reins. Co.*, 2006 WL 3771090, at *2 (S.D.N.Y. Dec. 22, 2006) (court ordering parties to devise a protocol for sampling).

and costs are involved in accessing the information, what the information consists of, and how valuable it is for the litigation in light of information that can be obtained by exhausting other opportunities for discovery.”⁵⁶

In the litigation context, the term “sampling” can have a number of meanings depending upon how the sample is selected and the purpose for which it is used. Thus, courts distinguish between “judgmental” sampling and “statistical” sampling, the latter of which has been traditionally used primarily in determining “adjudicative facts.”⁵⁷

As early as 1963, survey conclusions based on “random sampling”⁵⁸ and the application of probabilistic principles were deemed admissible in court as evidence to establish facts in dispute.⁵⁹ Thus, statistical sampling has been routinely used in discrimination cases to assess whether discrimination has occurred.⁶⁰ These cases draw on probability theory to determine whether the observed variations at issue may have resulted from chance, or whether they demonstrate a pattern of intentional misconduct.⁶¹

Most recently, in the “light cigarettes” class action litigation,⁶² Judge Weinstein concluded that “[s]ampling and survey techniques are well-accepted alternatives for the trial judge facing crippling discovery and evidentiary costs” and that “[g]reater reliance on statistical methods is required by the profound evolution in our economic communication and data compilation and retrieval systems in recent decades.”⁶³ The court noted that the Supreme Court had recently permitted sampling as a method for the Internal Revenue Service to assess unreported tips by restaurant employees.⁶⁴

As described below,⁶⁵ statistical sampling can help provide assurance of the accuracy of automated or other tools used to reduce the size of a given population of ESI for purposes of review.

Statistical or probabilistic sampling stands in contrast to the less formal “judgmental” sampling which is often used to facilitate the exercise of discretion by a court or by a party seeking to assess the quality of a process. This is the context referred to in the Committee Note to Rule 26(b)(2)B quoted above. Courts routinely utilize samples of arbitrary size drawn from a population of potential sources to help them exercise their judgment as to the extent to which a party should restore backup tapes, and who should bear the costs of doing so. In the cases of *McPeck v. Ashcroft*⁶⁶ and *Zubulake v. UBS Warburg LLC*,⁶⁷ for example, the Courts utilized informal sampling techniques in connection with assessment of the marginal utility of investing resources in the restoration and recovery of ESI from backup tapes. Similarly, in *Quinby v. WestLB AG*,⁶⁸ the Court refused to require a producing party to absorb the full cost of restoring and searching backup tapes where a review of a sample showed that “only a small percentage of the e-mails produced are relevant.”⁶⁹

The use of keyword searches to cull or filter relevant information from massive amounts of ESI is an example of the use of judgmental sampling the effectiveness of which is subject to evaluation

56 In a different context — acknowledging the power of one party to compel a sample from another under certain circumstances not relevant here — Rule 34(a) was amended to state that “[a]ny party may serve on any other party a request to produce and permit the party making the request, or someone acting on the requestor’s behalf, to inspect, copy, test, or sample any designated documents or electronically stored information” in the respondent’s possession, custody or control, and also includes provision for entering on to the premises of the responding party “for the purpose of inspection and measuring . . . testing, or sampling . . .” (emphasis added).

57 *Rosado v. Wyman*, 322 F. Supp. 1173, 1180 (E.D.N.Y. 1970), *aff’d*, 437 F.2d 619 (2d Cir. 1970), *aff’d*, 402 U.S. 991 (1971).

58 See Appx. A, *infra*.

59 In *Zippo Mfg. Co. v. Rogers Imports, Inc.*, the plaintiff manufacturer of cigarette lighters employed three surveys of the relevant smoking population to demonstrate a likelihood of confusion among consumers in support of its claim for trademark infringement. 216 F. Supp. 670 (S.D.N.Y. 1963). For an interesting and comprehensive discussion of court decisions involving statistical sampling, see Laurens Walker & Joan Monahan, *Sampling Evidence at the Crossroads*, 80 S. CAL. L. REV. 969 (2007), *online version at* http://law.bepress.com/uva/lwps/uva_publiclaw/art62.

60 See, e.g., *Castaneda v. Partida*, 430 U.S. 482, 495-96 (1977); *Stewart v. General Motors Corp.*, 542 F.2d 445, 449 (7th Cir. 1976). See also *Capaci v. Katz & Besthoff, Inc.*, 711 F.2d 647, 653-57 (5th Cir. 1983).

61 See *Ageloff v. Delta Airlines, Inc.*, 860 F.2d 379, 383-84 (11th Cir. 1988); see also *G.M. Brad & Co., Inc. v. U.S. Home Corp.*, 759 F.2d 1526, 1538-40 (11th Cir. 1988) (expert testimony established profit projections based on industry standards).

62 *Schwab v. Philip Morris USA, Inc.*, 449 F. Supp. 2d 992, 1247 (E.D.N.Y. 2006), *rev’d on other grounds sub. nom. McLaughlin v. Am. Tobacco Co.*, 522 F.3d 215 (2d Cir. 2008).

63 *Schwab*, 449 F. Supp. 2d at 1244-45.

64 See *United States v. Fior D’Italia, Inc.*, 536 U.S. 238, 247-48 (2002); see also *Schwab*, 449 F. Supp. 2d at 1244.

65 See generally discussion *infra*, Part III.B.2.

66 202 F.R.D. 31, 34-5 (D.D.C. 2001).

67 217 F.R.D. 309, 324 (S.D.N.Y. 2003).

68 245 F.R.D. 94 (S.D. N.Y. 2006).

69 The court found that the number of relevant documents was “quite low when compared to the volume of documents produced.” *Id.* at 109.

by testing. “For example, a producing party could apply a certain set of keywords and/or concepts to cull down a sample of the collection and then analyze the results.”⁷⁰ Trial or pilot runs of combinations of words may be tested in an iterative fashion to extrapolate the effectiveness of the chosen set. In the case of *Clearone Communications v. Chiang*,⁷¹ for example, the Court noted that an initial effort to modify conjunctive search terms was, in effect, a first step in a “sampling” process to avoid over-inclusiveness. As noted by another court, “Common sense dictates that sampling and other quality assurance techniques must be employed to meet requirements of completeness.”⁷²

III. APPLYING QUALITY MEASURES IN E-DISCOVERY

Discovery involves locating and delivering non-privileged documents and ESI responsive to non-objectionable discovery requests using a reasonable search method tailored to the needs of the case. The question for the producing party is how best to capture and properly produce this deliverable, and how and what resources need to be allocated to this project.

Each case or matter — whether a discrimination claim, patent dispute or antitrust “second request” — has its own dynamics which will shape the project plan. A series of predictable decisions will be required and each phase of discovery has quality aspects which need to be considered. A non-comprehensive list of examples drawn from select phases of the discovery process follows.

A. THE DATA COLLECTION PHASE

1. Building on Traditional Approaches to Document Collection

Until recently, lawyers well knew how to ask for and collect “documents.” Key custodians would be asked to gather their hard copy documents and files into boxes, which were made available to lawyers or paralegals to review essentially each and every page for relevance and privilege reviews. This time-worn process admittedly grew more complex in large litigations, e.g., antitrust actions or products liability class actions, where tens or hundreds of thousands of boxes of documents were collected from a corporate enterprise, to be reviewed by legions of junior and contract attorneys.⁷³ Much the same process continues to be employed today for reviewing huge bodies of evidence that exist only in hard-copy form.

With the advent of computers, the Internet, network servers, e-mail, and the explosion in forms of ESI, the collection process has necessarily had to adapt to the rapid changes and volume considerations involved. Yet, there is still a need to understand what to ask for that would be potentially relevant, what the sources of those items might be, and what key players would best know about the relevant materials. What has materially changed is the need to engage IT and business professionals who are knowledgeable about the sources and locations of ESI within the enterprise. These are the types of persons who will be informed on the subject of what ESI is online, near-line and offline, what may be zipped or encrypted, and what may be found on backups, CDs, DVDs, virtual storage devices, servers, removable storage devices (e.g. flash drives, iPods, etc.), and archives of all kinds. Potentially all of these topics must be covered in any e-discovery process to collect or cull out that which is relevant to the particular litigation or investigation from the larger universe of ESI.

2. Applying Measures of Quality to the Data Collection Process

While there is no legal principle mandating *perfection* in the collection phase of discovery, parties do have obligations to perform discovery processes reasonably and ethically, showing appropriate professional care and judgment. Given the ad hoc nature of the process, it is not

⁷⁰ See Mia Mazza, Emmalena K. Quesada, Ashley L. Sternberg, *In Pursuit of FRCP 1: Creative Approaches to Cutting and Shifting the Costs of Discovery of Electronically Stored Information*, 13 RICH. J. L. & TECH. 11, at [38] (2007)(when results show the use of those combinations did not except a large volume of relevant information it validates and supports their use to cull down the remainder of the collection).

⁷¹ 2007 WL 3275300 (D. Utah Nov. 5, 2007), modified 2008 WL 920336 (D. Utah April 1, 2008).

⁷² *In re Seroquel Prods. Liab. Litig.*, 244 F.R.D. at 622 (emphasis added). See also *In re Vivox Prods. Liab. Litig.*, 2006 WL 1726675, at *2 (appellate court urging parties “adhering to a statistically sound protocol for sampling documents” as an aid in reducing the trial court’s burden over reviewing the assertion of privilege on 30,000 documents), *on remand*, 501 F.Supp.2d 789 (E.D. La. 2007).

⁷³ See, e.g., *Transam. Computer v. IBM*, 573 F.2d 646, 648 (9th Cir. 1978) (refusing to find waiver of privilege where “unique circumstances” existed requiring production within a three-month period of approximately 17 million pages creating “monumental” problems because not “grouped or barched together”).

surprising that objective benchmarks, standards and regulations specific to the governing of this process do not exist. Absent these standards, how does one ensure that collection workflow is going to be successful?

Quality control processes employed prior to the review of ESI are an essential element to demonstrate the “reasonableness” of a party’s discovery efforts; they also support a quality chain-of-custody process for purposes of tracking and documentation. Parties using a well-designed discovery methodology should be able to account for all of the electronic information they collect (as well as identify the ESI they did not collect), even though they may review and ultimately produce only a small portion of that information. As a general proposition, these quality control procedures have two main purposes: data accountability and anomaly detection. The complexity associated with multi-location collection from large numbers of custodians, live systems, archives and forensic images makes effective quality control processes essential. Without them, parties are more vulnerable to potential challenges related to omission of potentially relevant data, spoliation, conversion of data, or other issues arising in the later review and production phases of discovery.

The collection and initial processing of ESI can be measured and managed through the gathering and reporting of key metrics. This analysis should be applied as early in the workflow as possible, helping to communicate the details about the composition of the collected ESI. Simple metrics such as how much and what type of data for each custodial source has been collected can be very helpful to the planning process.⁷⁴ This can help with early detection of potential issues such as metadata loss, encryption, corruption, unsupported or unknown file types, non-searchable ESI and other unpredictable issues. It can also help prevent unexpected cost and burden at the time of review and production, for example, by the selection of a review tool that is unable to handle the multiple languages contained in the ESI.

3. Data Collection: Best Practice Guidelines

The selection, organization and filtering of ESI through the use of a search protocol⁷⁵ is a critical element in reducing the volume of information to be collected and thus the time and cost of collection. In addition, keyword search techniques are well known and may be used for this purpose. More advanced technologies have emerged that employ complex algorithms for ESI filtering and organization and may, in some cases, be useful at the collection stage. Regardless of the technology chosen, all filtering methods require a well-defined process. Without these basic steps, the use of any filtering technology will likely result in gross over- or under-inclusion of responsive ESI. The process includes several steps:

- Understanding the composition of source ESI;
- Defining the goals of the filtering;
- Applying the filter and testing the results.

Understand the composition of the ESI targeted for filtering. There are many types of documents: some documents are handwritten, some are written in one or more languages other than English, others are compressed (e.g., zip files), encrypted or protected, and some are composed of images without searchable text such as electronic faxes or scanned paper documents. This may result in having to format, convert, translate or process documents so that they can be filtered. For example, scanned paper documents must first be run through optical character recognition (OCR) software to extract searchable text. Without a well-defined process for all file types, some files may be ignored or missed during the filtering phase of the electronic discovery workflow. Finally, the handling of handwritten documents should be separately addressed.

⁷⁴ For example, if a party has collected an average of 20% of ESI from several custodian sources, the custodian with only 5% of ESI collected will stand out. Creating a corporate or case level data map in the earliest assessment stages of a case gives counsel a framework to analyze and make comparisons of the collection metrics.

⁷⁵ See *Treppel v. Bivvail Corp.*, 233 F.R.D. 363, 372 (S.D.N.Y. 2006) (discussing importance of a “search protocol” in assuring a “diligent search” involving a “reasonably comprehensive search strategy”).

Defining clear goals for the filtering process. The team needs to understand the intent of the filtering – such as reduction of volume by exclusion, inclusion, organization or classification of ESI — so that the appropriate tool can be utilized, and the process is explainable.

Applying the filter and testing the outcome. The filtering process should be iterative and needs to be repeated until the desired goals are met. It is not sufficient to blindly run a filtering tool and trust that it is achieving the desired results. One must evaluate the outcome of the search, looking to identify errors in how the filter rules were set up or applied. Key metrics, such as the number of included or excluded documents by keyword or filtering criteria, can be used to evaluate the outcome. Examining the high and low number of search hits can uncover issues with how the search was constructed, the choice of terms, or even issues with the data. For example, finding zero search hits on a key term or concept may point out that a search term is spelled incorrectly or that many of the documents do not contain searchable text. On the opposite end of the spectrum, finding a term that hits on a high percent of the ESI may indicate that the term is too broad or may need to be combined with additional qualifying search terms.⁷⁶

Maintaining Data Accountability. It is critical to maintain the identification of the original source of data at each stage of processing, such as the file location, the directory and drive mappings on hard drives, as well as the contents and file counts for each unique source for each custodian. Best practices also call for clear documentation of what was done and not done. If Internet e-mail is not processed for review, that should be documented. If a party uses forensic tools to recover deleted e-mails from a custodian's mailbox, that should be documented, including the tool used and the results. By applying a custodian-based view to the data, the party can report the total number of items from all sources applicable to each custodian (e.g., the live e-mail server, e-mail archive, hard drives, network shares, and removable media). Searching the review database for all items associated with a custodian should yield a result that matches the total number of items from the processing report.

A cornerstone of data accountability is establishing the counts of files on media before processing begins.⁷⁷ From this defined starting point, the party should make adjustments to file counts reflecting processing results for each source:

- Elimination of system files (e.g., based on the National Software Reference Library or “NSRL” filter);⁷⁸
- Deductions for certain file types not processed (such as databases);
- Deductions for items that could not be processed (e.g., corrupt or virus-infected files, or documents created by special forms of proprietary software);
- Deductions for duplicates not processed;
- Deductions for items not selected by filters.

In addition, it is also important to note files processed but not indexed, such as encrypted files or images.

The raw data regarding the electronic information is also useful for identifying anomalies in the data collected. Investigating and resolving these anomalies and exceptions in the data can serve as an additional quality control check that may discover errors or omissions in the collection process. At a minimum, investigating anomalies may help to answer questions about the collection process that other parties or the court may have. Indexing exceptions that are not documented are

⁷⁶ Sampling can also be useful in testing the effectiveness of filters, i.e., samples can be drawn and reviewed from both the set of documents hit by a filter and from the set excluded by a filter, so as to provide evidence as to whether the filter casts too wide or too narrow a net. Sample-based testing of filters, in which all data (filtered and unfiltered) is in-scope for testing, allows for informed, iterative development, ideally leading to more effective filters.

⁷⁷ Note that file counts can, however, be misleading. Container files (e.g., PSTs) can and should be “exploded” for the purpose of fully indexing and understanding the overall data set and data profile.

⁷⁸ See <http://www.nslr.nist.gov/>.

of particular concern, since the items are loaded into the database and appear to be available for searching, analysis and review.⁷⁹

Additional special issues involving e-mail conversion. Conversion of e-mail from one format to another is often necessary during the collection and processing of ESI. While processing in native format is desirable, many service providers do not natively support all e-mail formats; thus, conversion of non-supported e-mail to a supported format may be required. Given the potential for data loss or alteration (for example, loss of formatting, bold, italics, underlining, and so forth) arising as a result of such “conversions,” it is prudent to ascertain the steps taken to assure a quality result.⁸⁰

Ultimately, of course, the quality and completeness of the collection phase will be directly related to the care and planning, as well as the ability to adapt to changing needs, that are built into the protocol executed under the leadership of the Team Leader.

B. THE REVIEW AND PRODUCTION PHASES

1. Introduction

Producing parties review documents or ESI for relevance and responsiveness before they are produced, as well as to determine if any privilege or exemption is applicable.⁸¹

Effective management of the review phase requires organization and advance planning. Thoughtful structuring of the review process and coding protocols, sufficient attention to staffing, and open communication and collaboration among attorneys, clients, and legal service providers are hallmarks of well-managed document reviews. Attention to quality control throughout the process is paramount to providing meaningful and cost-efficient results.

Traditional large-scale document reviews typically have involved a significant number of individuals of varying expertise and responsibility. Leadership by the key individuals who manage the diverse roles and tasks in coordination with the lead e-discovery attorney or Team Leader is crucial in the following respects:

- Providing clear guidelines governing “knowledge transfer” from the trial team and senior managers to the document review team and those assisting on a particular review project. Such guidelines also ensure an adequate “knowledge transfer” from those familiar with the documents and data *back* to the trial team and senior managers;
- Developing the relevant responsiveness and privilege criteria;
- Determining search methodologies;
- Ensuring consistency to the extent possible, especially in any areas relying on human review and judgment; and
- Providing for objective quality benchmarks to measure the performance and effectiveness of the review process.

⁷⁹ If they are not indexed, any keyword searches performed against the data will not include those items. Therefore a review that is based at least in part on the results of keyword searches may overlook these items.

⁸⁰ Among the questions that could be asked of a service provider with regard to e-mail conversion are: (i) what e-mail formats require conversion for processing; (ii) what conversion software will be used and for what purpose was the software developed; (iii) what known limitations in the software exist, including the above-described data loss or alteration; (iv) how has the software been tested or vetted prior to selection for use, and how has the conversion process been tested or validated; (v) what is done to investigate or remediate errors; (vi) what errors are typical; (vii) does the conversion process alter date and time-values; (viii) does the conversion process preserve e-mail addresses, resolved names, entire e-mail headers, blind copies (bcc’s), etc.; (ix) does the process retrieve e-mail from all containers in the mail store; (x) does the conversion process handle duplicates, e-mail threads, encrypted messages, corrupt messages, foreign languages, Rich Text formatted e-mails, HTML formatted e-mails; and (xi) does the conversion process handle non e-mail objects (e.g., calendar entries, contacts, notes, etc.)?

⁸¹ Throughout this section, the term “privilege” is used to refer to both the attorney client privilege and the attorney work product doctrine.

2. Using Automated Methods to Reduce the Initial Burden of Review

As discussed in connection with the collection process, and as set forth in the *Sedona Search Commentary*, there are a number of automated tools that are of great assistance in reducing the overall data universe, in at least four fundamental ways: first, by helping to identify only a portion of the universe of “collected” ESI as potentially responsive based on whatever automated search methodologies and protocols are employed; second, by de-duping (or tagging) identical or “near” identical ESI so that a particular ESI object is reviewed only once; third, by eliminating certain types of files that likely are not relevant (e.g., video and program files); and fourth, by identifying and eliminating obvious spam from the review population.⁸²

A number of legal service providers recently have begun offering various forms of automated tools that promise to significantly reduce the number of electronic documents to be manually reviewed by extracting the documents most likely to be responsive to a discovery request, and leaving the remainder unselected and unreviewed.⁸³ Given the huge explosion in the cost of complying with e-discovery requests, tools that reasonably and appropriately enable a party to safely and substantially reduce the amount of ESI that must be reviewed by humans should be embraced by all interested parties — plaintiffs, defendants, the courts, and government agencies.

For example, to conduct an automated search process utilizing statistical sampling, the first step would be to effectively share and transfer knowledge among counsel and the managing team and those with knowledge of the corpus of ESI that is the subject of discovery. The knowledge gained in this process will be used in the development of one or more search strategies (e.g., Boolean searches, concept searches, metadata filters, language-based approaches using taxonomies and ontologies, statistical clustering techniques, or other proprietary strategies). Once the responsive data set has been characterized, a random sample of categorized material is chosen and reviewers will review this small, but statistically significant, sample. This random sample will contain both responsive and unresponsive material, and reviewers classify these documents as they normally would under a manual review. The results of this classification are then compared to the results reached by the chosen categorization method(s). When there is a difference between the determination made by the human reviewer and the categorization method, the legal team reviews the document and decides which is correct. Adjustments are then made to the search strategy. Sometimes the differences require modifications so that a particular type of document is filtered in the future.

This iterative process of sampling and refinement is continued until the rate of difference between the automated methods and human review meets the acceptable threshold of accuracy defined for the project. Once it has, the final categorization is run on the entire data set and the responsive documents can then be prepared for production, subject to any further privilege or other manual reviews as deemed necessary.

Another approach is a “blended review” process, combining the use of manual review by humans with automated review using software. Specifically, automated tools can help reduce the workload when manual review is required. For example, where potentially privileged documents are involved, a “privilege” vocabulary identifying attorney names can be used in conjunction with a vocabulary identifying topically relevant information. In this way, the privileged documents can be identified and then subcategorized by relevancy, allowing the manual reviewers to start with, and focus on, the most pertinent privileged documents.

Once the ESI universe has been reduced to the population of documents that will actually be reviewed, there are review tools on the market that help review teams organize and more effectively work with what still may be a considerable volume of electronic data. For example, a number of service providers offer categorization and clustering tools that pull together documents relating to identical or similar topics, so they can be reviewed together — accelerating the speed of review and

⁸² See 8 Sedona Conf. J. at 208-211.

⁸³ The magnitude of the cost reduction depends on the percentage of responsive documents in a data population, the number of different issues relevant to the data request or subpoena, and the extent to which human review is applied.

ensuring better consistency in the treatment of the documents.⁸⁴ Other providers offer e-mail threading, which likewise pulls together all the related e-mails from a given e-mail chain so they can be reviewed together — as opposed to randomly dispersed throughout a document set to be reviewed by different reviewers.

Although all of these review tools are quite useful in reducing the time spent reviewing ESI, in most present-day litigation there will still be, to a greater or lesser extent, a need to manually review some portion of the population to determine responsiveness to a particular e-discovery request. Moreover, it is still common for all or some portion of the data to be reviewed a second time (i.e., by means of a different reviewer) for privilege, and/or as a quality check on the first-level review.

To the extent that automated search and retrieval methods are used for reducing the ESI data set to a more manageable size for purposes of review, a party may be called upon to demonstrate to opposing parties, courts, and government agencies, that its chosen method and tool accurately captured a reasonably sufficient number of the relevant, nonprivileged ESI in existence, and that the remaining unreviewed and unproduced ESI is irrelevant. *See also discussion, supra*, Part II.B.3.

In citing to the above *Sedona Search Commentary*, as well as to the federal government's TREC Legal Track research initiative,⁸⁵ the Court in *Victor Stanley* stated that “there is room for optimism that as search and information retrieval methodologies are studied and tested, this will result in identifying those that are most effective and least expensive to employ for a variety of ESI discovery tasks.”⁸⁶

Additionally, while case law will have to evolve in this area in terms of challenges to particular discovery processes, expertise based on experience with judgmental and iterative sampling as well as the existence of accepted statistical sampling techniques can be cited. As noted in an article summarizing legal principles related to e-discovery:

As with any technology, it is imperative to perform frequent, thorough checks to make sure that the searches are working, perhaps by using a sampling method. . . . The needs of the litigation at issue should dictate what technology gets used, and how, in order to strike the optimal balance possible between recall and precision. The key to defensibility is that litigants employ these search strategies as part of a reasonable, good-faith, well-documented discovery protocol. Lawyers must understand where the search technology fits into that protocol and have confidence that they have taken measures to ensure the quality of their searches (footnotes and internal quotes omitted)⁸⁷

Thus, as noted earlier, sampling techniques can be used to establish, within a certain confidence level, that unreviewed and unproduced material in the form of ESI is likely to be irrelevant to a particular discovery request.⁸⁸

3. “Clawbacks,” Rule 502, and Reliance on Automated Methods

In addition to the tools and techniques set forth in Part III, increasingly high-volume amounts of ESI in litigation will require new and creative strategic approaches to efficiently reach closure in discovery. The “clawback” provision of amended Fed. R. Civ. P. 26(b)(5) (that allows for the return or “clawback” of inadvertently produced privileged materials), is further buttressed by the passage of Federal Rule of Evidence 502 (generally immunizing parties engaging in “clawback” from third-party challenges if their agreement is included in a court order). In light of these developments, and without employing labor-intensive manual review (except for spot checking for responsiveness and privilege), counsel may well wish to assess their client's interest in producing all potentially responsive

84 See Ramana Venkata & Michael A. Geibelson, *Overcoming E-Discovery Challenges with New Technologies*, 30 L.A. LAWYER, June 2007, at 46 (“Quality control measures, document organization, and batch tagging can significantly lower the cost of e-discovery and help satisfy client demands for finite, predictable e-discovery costs”).

85 See <http://trec-legal.umiacs.umd.edu>; see also *Sedona Search Commentary, supra* n.33, at 215.

86 250 F.R.D. at 261 n.10.

87 M. Mazza, E. Quesada, A Sternberg, *supra* n.70, at [33] (litigants looking for a ‘holy grail’ in automated technology will not find it) (footnotes and internal quotes omitted).

88 The same techniques can be used to determine, within a certain confidence level, that the produced documents are in fact relevant.

documents gathered as the result of automated search and filtering methods.⁸⁹ That is, even with a clawback agreement in place, a party may wish to perform sufficient sampling and other quality controls to reach a level of comfort on matters of relevance and privilege. This allows the majority of documents to be produced without manual review, except where a traditional manual review will be employed over documents initially identified through automated means as withholdable on grounds of privilege. This approach substantially reduces the costs and burdens of producing and requesting parties, and ideally the pros and cons of doing so should be discussed at a “meet and confer.” Adoption of this approach does not, however, obviate the need for employment of measures of quality at every stage.

4. Quality Control Guidelines for Responsiveness and Privilege

The use of quality control tools throughout the review process, involving hybrid combinations of human review and other technological methods, can provide ongoing performance statistics and resolve potential ambiguity in training and instructions. Indeed, when quality checking is combined with training, a resource-intensive review process can be made much more efficient by improving the quality of initial reviews with iterative feedback.

As in traditional document review, there are two basic approaches to quality checking first-level reviewers’ coding when dealing with data or ESI. One approach is to have a second level of review performed — ideally by a senior lawyer — on some or all of the coded ESI. Another is to run statistical analyses of coded documents to check for consistency across reviewers, and then conduct a targeted second-level review where there are unexplained statistical variations.

However, as recent research⁹⁰ and common sense confirm, members of any legal team can disagree on relevance assessments of specific ESI. The standard for first-level reviewers (often contract attorneys) should therefore never be perfection, especially given that “reasonable minds” can differ on exactly what is or is not relevant to a particular request. To further enhance the quality of first-level review, guidance should be continually refined to assist the reviewers in getting at least the “easy” documents right and in coming as close as possible to the desired result on close-call documents.

Review for privilege can require an even more nuanced legal analysis and, as such, can be a more expensive review per document than review for relevance or confidentiality. Complexities include the use of e-mail strings and internal legal department communications.⁹¹ Incorporating processes that safely minimize the number of records being reviewed for privilege will lead not only to a more efficient, cost-effective review, but also to faster turnaround for production and higher quality privilege logs. These processes might include:

- Creating a “potentially privileged” category of documents that obtains more scrutiny from more experienced reviewers. This can involve the use of file extensions, document sources, keyword searches, metadata filters, and any internal designations of privilege. (Obvious examples of potential key words that a party may consider using include “privilege,” “work product,” “legal,” “counsel,” lawyer names, firm names, and firm domains, as well as combinations and roots of these terms.)
- Identifying structured data sources where data is never in the hands of an attorney and is not created for any litigation purpose. However, companies and counsel need to be aware that such data sources may contain information that is nonetheless

89 See generally Advisory Committee Note to Rule 502: “Depending upon the circumstances, a party that uses advanced analytical software applications and linguistic tools in screening for privilege and work product may be found to have taken “reasonable steps” to prevent inadvertent disclosure”; see also *Rhoads Industries*, *supra*, n.54 (citing to Advisory Note).

90 Data collected from the first year of the TREC Legal Track showed substantial variance in how human subject volunteers “assess” relevance or nonrelevance in response to a hypothetical production requests under FRCP 34. See Jason R. Baron, David D. Lewis, & Douglas W. Oard, “TREC 2006 Legal Track Overview,” *Fifteenth Text Retrieval Conference (TREC 2006) Proceedings*, <http://trec.nist.gov/pubs/trec15/papers/LEGAL06.OVERVIEW.pdf>. This result is in line with other well-known studies in the “information retrieval” literature, including those previously conducted as part of TREC.

91 See, e.g., *Muro v. Target Corporation*, 243 F.R.D. 301 (N.D. Ill. 2007) (intermingling of non-privileged communications with privileged communications in a strand or string of e-mail); *In re Vioxx Products Liability Litigation*, 501 F.Supp.2d at 815 (adopting Special Master Report involving review of in-house lawyer communications); *Victor Stanley, Inc.*, 250 F.R.D. at 262 (failure to carry burden of excusing inadvertent production of privileged documents because of lack of demonstration of, *inter alia*, “quality-assurance testing”).

prohibited from disclosure by operation of law, regulation or contract, or that is confidential or proprietary for other reasons.⁹²

Quality control going forward. After the review of an initial subset of ESI has been completed and all reviewers are deemed to be performing adequately, the team should implement a quality control protocol to apply on a going-forward basis. This protocol should be adjusted to accommodate the reviewers' growing understanding and new developments in the case.

For example, the system should address the percentage of ESI checked as well as the methods for selecting ESI to be checked. It is rarely necessary for a team to review 100% of the responsive ESI population a second time; instead, sampling measures may be appropriate. To guard against inadvertent production of privileged ESI, in some reviews a 100% check is made of ESI with attorney names (and/or other terms commonly associated with privileged documents). Prudence also suggests checking 100% of the ESI in the production queue that originates from the files of custodians known to work closely with attorneys.

Consistency checking. Every discrete object in the review population should ultimately be coded as responsive or not. Accordingly, a check can be done to locate any ESI that exists in the database without this essential coding. Rather than waiting until the end of the review, this check can be done on a rolling basis as the review proceeds (e.g., at the conclusion of review for each relevant custodian). Additionally, consistency in coding across like documents is important, and measures should be adopted to ensure or increase the likelihood that duplicate or near duplicate documents are being coded in the same fashion.

Other inconsistent combinations should be identified, and the database should be regularly searched for these errors both to correct them and to determine their source so as to avoid creating more errors. Listed below are a few examples of consistency searches, but they will necessarily vary from review to review:

- ESI coded as responsive without coding for potential privilege (where known subsets of the population are in fact considered privileged);
- ESI coded as potentially privileged without coding for privilege type;
- ESI coded as non-responsive and noteworthy;
- ESI coded as non-responsive and potentially privileged;
- ESI coded as needing redacting but no redaction has been applied.⁹³

Additional common practices for quality control during the review process include:

- Comparing coding among reviewers on a common subset of ESI, and providing individual or group feedback following results;
- Developing a system for *early* review and assessment before reviewers get too far into review (e.g., first 100 coded ESI objects automatically get sent to second-level review team for assessment);
- Selecting a group of documents created by running a search with the reviewer's name and the targeted codes that will give a broad idea of how each reviewer is handling certain codes;

⁹² Where parties or their counsel are unwilling or unable to determine that a group of records are completely barren of privileged material, they may wish to consider an offer to produce these documents under a "quick peek" agreement.

⁹³ State-of-the-art review platforms offer support for structures such as mutually exclusive tag groups, that help enforce these consistency rules during the review process. As they evolve, they may be support for many more such structures ("if it gets this tag, it must also have this one") that make it easier for inconsistencies to be identified. Wherever possible, these should be understood and fully utilized in the design of the review.

- Analyzing the daily tracking sheet data log and/or service provider software-generated statistics to identify the frequency of second-level changes to first-level reviewers' coding, and targeting areas of frequent disagreement;
- Conducting early assessment of ESI marked "privileged" to identify any misunderstandings about privilege and providing feedback;
- Conducting detailed quality review of "potentially noteworthy" ESI;
- Conducting detailed quality review of key custodians or high-level custodians (such as the CEO) to assess the need for early client feedback;
- Running tests to identify logically inconsistent coding (*e.g.*, "responsive" tag but no responsive coding category selected);
- Tracking rates of review: (*i.e.*, the time taken per reviewer), and investigating any outliers compared to peer reviewers;
- Gathering metrics on the overall review process itself, including ESI/documents reviewed per hour, "pages" per hour, sampling for congruence, and total costs.

The hosting service provider and/or litigation support project manager can aid with statistical review tracking (both for substance and pace) for all levels of review. Service providers offer different options for review tracking and can provide reports that track, among other things, the number of "pages" reviewed, the number of ESI objects coded with a particular field, the hourly average of "pages" reviewed, and the number of times second-level reviewers change the coding of a particular first-level reviewer.

At least three additional types of quality concerns may arise in connection with document review:

Review of data "exceptions." It is not unusual for providers and software applications to have difficulty processing obscure, password-protected, or corrupted records in the data set. Some data may also be unreadable; characters may be scrambled or random. Service providers typically refer to such documents as "exceptions." Service providers should be able to provide "exception reports" continuously throughout the review and address those issues on an ongoing basis. Because exceptions can take considerable time to resolve, waiting until the end of the review to address these issues is a mistake because it can interfere with timely production. If the provider is not able to remedy the problem, third-party consultants may be called in to process the data with different tools. Some password-protected materials can be "cracked," and others may need to be returned to the client for input. Finally, the content of the exception data should be considered. If it can be determined from the file name or type that it is not likely to contain relevant information, a party should consider whether to inform the opposing party or government agency that the file will not be processed further.

ESI in foreign languages. Another category of ESI that would be commonly set-aside during review is foreign language materials. It may be necessary to obtain translations (informal translations with Internet tools may suffice for initial review), so time should be built into the production schedule to get these materials translated, reviewed, coded, and processed for production.

Loose electronic media. If certain types of media have not been made part of the primary review database (such as video or audio tapes, disks, DVDs, CDs, etc.), it is important to build time into the review schedule for review of those materials prior to the last production.

Pre-production clean-up and additional quality control checks. Once the review of a set of documents and ESI is completed, the service provider and the team must complete pre-production tasks and conduct final quality checks to ensure that all documents are properly loaded, numbered, and labeled on the final production medium. Although many teams implement quality control

measures throughout the review process, it is important to develop a plan for final quality review of the production, which could include performing an appropriate analysis to verify that all ESI coded as responsive and not privileged has been included in the productions. This review could also include checking for:

Inadvertent production of privileged ESI. Ensuring that no documents marked “privileged” have been loaded onto the production media. The team may also want to run important attorney names through the pre-production set as a final check. It is important that the team verify that all redactions are properly applied in all production formats.

Non-responsive ESI. Ensuring that no non-responsive data has been loaded onto the production media.

Inconsistent or illogical coding of ESI. Identify all documents containing inconsistent or illogical coding (e.g., the reviewer checked a responsive coding category button and also checked “non-responsive”).

Data formats and labeling. Confirming that all data on the production media has been loaded in the required or agreed-upon format.⁹⁴ Care should also be taken to ensure that all the documents on a disk or other production media are properly labeled, including any necessary confidentiality or FOIA designations, and that the disks or other production media themselves are also properly labeled for production.

5. Final Quality Checking at Production

While quality checking should be undertaken at each stage of the review process, a final check is appropriate prior to production:

- Each production to opposing counsel should be quality checked to ensure that no materials designated as privileged were accidentally included in the production. Quality checking can include:
 - (1) Randomly spot checking the production and re-reviewing particular records;
 - (2) Checking to ensure that the number of files being produced matches the expected number of files (i.e., doing a file count) to ensure that extra (hidden or not-hidden) files are not being included;
 - (3) Checking that the size of the files being produced is approximate to the expected size of the files to ensure that extra information is not being included;
 - (4) Re-running keyword searches over the production similar to those used in creating a “potentially privileged” category. Documents returned by the search can be reexamined to ensure they are not privileged; and
 - (5) Running data format or pattern searches over the production to find potentially unredacted but protected personal information (e.g., ###-##-####, to look for Social Security numbers).
- Where structured data is being produced to opposing parties, samples of the set that is being produced should be reviewed in the format it is being produced to ensure that the correct number of data fields are being produced and that the fields that were redacted are not included in the production.
- To the extent possible, the legal team should organize their review in advance so that objective data (authors, recipients, dates) can be automatically populated into privilege logs. Contemporary review tools can support this process to a considerable extent, greatly simplifying the process of generating privilege logs. Such information, however, should be reviewed for accuracy and completeness.

⁹⁴ The service provider should also check the production media to ensure that all data will be readable and that no data has become corrupted.

Conclusion

“The future is already here – it’s just not evenly distributed.”⁹⁵

The tremendous growth in the volume and complexity of ESI, and the increasing scrutiny imposed on the e-discovery process by opposing parties and the courts — which brings with it increased risk of spoliation sanctions — compel the legal profession to implement best practices to achieve greater quality in all phases of the e-discovery process, including in its collection, review and production phases. In today’s legal environment, using project management, measures of quality, and statistical sampling are ways in which to adopt lean, efficient and smart business practices. Put another way: just as *Moneyball*⁹⁶ demonstrated the value of applying new statistical measures to assess baseball talent, even if running counter to “tried and true practices” based on intuition and culture, this Commentary posits that legal practice needs to incorporate the best thinking from other disciplines, even if lawyers need to learn new techniques, and even if some of the “mystique” of legal work is left behind.⁹⁷

In the end, cost-conscious firms, corporations, and institutions of all kinds intent on best practices, as well as over-burdened judges, will demand that parties undertake new ways of thinking about how to solve discovery problems — including employing better project management and better measures of quality to achieve optimum results, as outlined here. The technical and management-orientated quality processes discussed above need to be incorporated into every trial lawyer’s continuing education and daily practice. These processes also dovetail with, and support The Sedona Conference® Cooperation Proclamation — which calls for incorporation of the best thinking of “disciplines outside the law” to achieve the goal of the “just, speedy, and inexpensive” determination of every action. In the end, striving to attain a quality outcome in the conduct of litigation is consistent with the highest ethical calling of the legal profession.

⁹⁵ William Gibson, quoted in *The Economist* (Dec. 4, 2003), see http://en.wikipedia.org/wiki/William_Gibson.

⁹⁶ See Michael Lewis, *MONEYBALL: THE ART OF WINNING AN UNFAIR GAME* (2003). For a good summary of the book’s thesis, see <http://en.wikipedia.org/wiki/Moneyball>.

⁹⁷ See also Ian Ayres, *SUPERCRUNCHERS: WHY THINKING BY NUMBERS IS THE NEW WAY TO BE SMART 10* (Bantam Dell 2007). Ayres, a Yale Law School professor and econometrician, writes:

We are in a historic moment of horse-versus-locomotive competition, where intuitive and experiential expertise is losing out time and time again to number crunching. In the old days many decisions were simply based on some mixture of experience and intuition. Experts were ordained because of their decades of individual trial and error experience. We could trust that they knew the best way to do things, because they’d done it hundreds of times in the past. Experiential experts had survived and thrived. If you wanted to know what to do, you’d ask the grey-hairs. Now something is changing. Business and government professionals are relying more and more on databases to guide their decisions.

For a general overview of the growing field of analytics and business intelligence, see Thomas H. Davenport & Jeanne G. Harris, *COMPETING ON ANALYTICS: THE NEW SCIENCE OF WINNING* (2007).

Appendix A: Sampling 101 for E-Discovery Lawyer

The basic concept of sampling certain items from a population to better understand the characteristics of the whole population is simple and straightforward. Sampling is a familiar concept that is accepted by most people, including those tasked with reviewing electronic documents for relevancy or responsiveness, and privilege. The application of sampling that people are probably most familiar with is with polling in national elections. Pollsters sample only a very, very small percentage of the voting public, but must take great care so as to ensure that the small number they are polling constitutes a genuinely representative sample of the entire population. On the basis of such a small but representative sample, the pollsters can predict:

- What percentage of voters would vote for a particular candidate;
- What the margin of error of the poll is (in statistical parlance, this is known as the “confidence interval”); and
- How certain they are that this result would hold up — within the margin of error — when applied to the population at large. This is known as the “confidence level.”

But mention “statistical sampling” in most other contexts and there is such apprehension about the process and the math involved, such that, at least to date, statistical sampling is rarely used or cited in assessing the quality and consistency of the electronic document review process. Ultimately, lawyers are left in an unfortunate situation, since the document review process is very well suited to the application of statistical sampling to improve quality and reduce costs.

This section seeks to demystify the basics of statistical sampling and explain how it can be effectively applied to a typical large electronic document review process.

Sampling: Judgmental (Nonprobabilistic) vs. Statistical

- Sampling involves the use of a subset of a population to represent the whole population. Probability sampling, or random sampling, is a sampling technique in which the probability of getting any particular sample may be calculated. “Judgmental” or “nonprobability sampling” does not meet this criterion — thus, judgmental sampling techniques *cannot* be used to infer from the sample to the general population. Any generalizations obtained from a nonprobability sample must be filtered through one’s knowledge of the topic being studied. Performing nonprobability sampling is generally considered less expensive than doing probability sampling, but the results are of limited value.

Examples of nonprobability sampling include:

- Judgmental sampling: Sampling performed on a sample set that was selected based on the judgment of the person doing the sampling. For example, a researcher chooses the sample based on who or what they think would be appropriate for the study, as in conducting an isolated case study of just one group, or making any choices based on relationship proximity, not science. A common example in the e-discovery context would be keyword searching itself, which is a more-or-less informed technique universally used by lawyers and legal professionals to produce a sample slice of a given ESI universe of data, based on the *a priori* judgment of those selecting the keyword terms.

Examples of statistical sampling:

- “Random Samples”

A sample is a subject chosen from a population for investigation. A random sample is one chosen by a method involving an unpredictable component. Random sampling can also refer to taking a number of independent observations from the same probability distribution, without involving any real population. A probability sample is one in which each item has a known probability of being in the sample.

The sample will usually not be completely representative of the population from which it was drawn — this random variation in the results is known as sampling error. In the case of random samples, mathematical theory is available to assess the sampling error. Thus, estimates obtained from random samples can be accompanied by measures of the uncertainty associated with the estimate. This can take the form of a standard error, or if the sample is large enough for the central limit theorem to take effect, confidence intervals may be calculated.

A simple random sample is selected so that every possible item has an equal chance of being selected from the population.

A self-weighting sample, also known as an EPSEM (Equal Probability of Selection Method) sample, is one in which every individual, or object, in the population of interest has an equal opportunity of being selected for the sample. Simple random samples are self-weighting.

- **“Stratified sampling”** involves selecting independent samples from a number of subpopulations, group or strata within the population. Great gains in efficiency are sometimes possible from judicious stratification. An example of this would be varying the sampling percentage based on document type.
- **“Cluster sampling”** involves selecting the sample units in groups. For example, a sample of telephone calls may be collected by first taking a collection of telephone lines and collecting all the calls on the sampled lines. The analysis of cluster samples must take into account the intra-cluster correlation which reflects the fact that units in the same cluster are likely to be more similar than two units picked at random.

Additional Common Sampling Terminology:

- **“Blind Sample”** — a selected sample whose composition is unknown except to the person submitting it. This type of sample is used to test the validity of the measurement process.
- **“Acceptance Sampling”** — a statistical procedure for accepting or rejecting a batch of merchandise or documents. Acceptance sampling involves determining the maximum number of defects discovered in a sample before the entire batch is rejected.
- **“Confidence interval”** — A range that contains the true population prevalence estimate a specified percentage of the time, if repeated sampling of the population were performed. For example, a 95% confidence interval is a range that contains the true population estimate 95% of the time. A smaller range indicates an estimate that is more precise. Small sample sizes or cells with low numbers generate less precise estimates and will have wider confidence intervals.

Statistical Sampling Basics

There are three key factors that determine the reliability and precision of the inferences that can be made about a population based on a statistical sample: 1) the randomness of the sample selection; 2) the variability of the sample results; and 3) the sample size.

One expects a properly-drawn random sample to be representative of the population from which it comes, but any estimate based on the sample will naturally differ to some extent from the corresponding measurement based on the whole population. One expresses the likely extent of

difference by presenting a confidence interval, say a 95% confidence interval, around our estimated value. One who will have confidence that the true value computed from the whole population would lie within our confidence interval 95% of the time. That is, if one draws samples over and over and compute estimates and intervals in the same way, one will be capturing the true value within the confidence interval 95% of the time.

The variability of the sample results affect how precise one can be in describing the true population values. This sampling variability is summarized by the quantity called the “standard error,” which is used in the construction of confidence intervals. One may say “the population contains X% items, + or – Y%,” when X is the estimated value and Y is its standard error. In many cases, a confidence interval stretches about two standard errors above and below the estimate.

A simple sampling example might help to illustrate these concepts more effectively. If one were to reach into a back-pack full of coins, mix them up thoroughly and then pull out a single handful of all pennies, one might naturally believe that the bag contains all pennies based on the single handful that had been directly examined. However, a confidence interval for the proportion of pennies would stretch from zero percent to some low but non-zero percent, depending on how many coins there were in the handful. The thorough mixing of the bag’s contents helps to achieve the randomness of the sample selection. However, the bag might well contain, say, 2% dimes, and a handful-sized sample might happen by chance not to scoop up any of the dimes. The width of the confidence interval expresses this uncertainty.

This example is simplistic and it is easy to imagine dumping out the contents of the bag to confirm the inference based on the relatively random sample of one handful from one bag. But how sure can one really be of the remaining contents of the bag based on looking at a single handful of pennies? There would always be some doubt about the remaining contents of the bag. What if the handful of coins included several different denominations instead of all pennies? What could be said about the bag’s contents then? And what if there were hundreds or thousands of bags full of coins? And what if samples taken from a number of them yielded an assortment of coins instead of all one denomination? Making an inference about the contents of all of the bags and perhaps the value of the all the coins in all the bags combined, becomes a more challenging problem, but one that has been largely solved by statistics, as long as the objective is to get a reasonable estimated value for the population and not necessarily the exact value.

The mathematical formulae used in statistical sampling provide reliable, quantifiable estimates for making statements or inferences about the population based on the sample results. And, the less variability found in the sample results, the narrower a confidence interval can be, keeping the same level of confidence. Together, the variability of the sample results and the size of the sample are the two critical determinants of how wide a 95% confidence interval will come out to be. With a larger sample, we can have a tighter interval within which we are confident of capturing the true value. But uncertainty goes down slowly with sample size. We must quadruple the size of the sample to halve the width of a confidence interval.

Since the basic concept of sampling is relatively simple why is the application of sampling in the realm of document reviews so challenging to implement? Perhaps it is because of the perceived high level of risk of getting the “wrong” answer about any single item or document in the population. Building on the previous example, it seems that the approach of dumping out all the bags and examining all their contents would lower the risk of missing a few gold coins that might not be predicted or detected by sampling from the population. When performing document reviews for a legal proceeding, the attorneys involved will typically take an analogous approach of gathering all the documents and files from selected individuals and reviewing all that contain certain search terms or keywords. This approach should lower the absolute risk of missing a “smoking gun” or “privileged” document that could dramatically affect the outcome of the matter involved.

Since sampling can typically achieve only a “reasonable” rather than an “absolute” level of confidence about the entire population, it is often considered to be unsuitable for determining whether a group of documents contains any that are privileged or responsive. Presumably, the only

way to determine whether documents are privileged or responsive is to look at them all and have the reviewers identify those that are privileged or responsive. However, since the reviewers are only people and people make mistakes, it makes sense to test their work for quality and consistency.

Sampling can be a very efficient method of determining whether or not the reviewers have achieved the necessary and acceptable level of quality and consistency in their work. There are two distinct approaches to sampling to find the proportion of correctly marked documents in the population. The first involves process sampling for acceptance, based on an approach that examines or inspects documents selected from in-process batches. The second, quality control testing, is performed by selecting a random sample from the entire population. Both of these methods or approaches can in theory be applied to a document review project.

The number of items to be tested or inspected is referred to as the sample size. The overall number of sample items selected from the entire review population for quality control testing will typically be less than the sum of the individual samples drawn to test in-process review batches. However, the benefit of testing individual review batches is that the review process can be adjusted to improve quality as the review is performed, thereby increasing the likelihood that the overall population will meet the established "acceptable quality limits" when the process is completed.



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