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Trade Secrets and Antitrust Law

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TRADE SECRETS AND ANTITRUST LAW

Harry First*

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I. Introduction

The antitrust treatment of trade secrets has remained largely hidden. There has been little separate focus on the competition problems that trade secrets may present, even though trade secret protection was raised as a defense in early antitrust litigation. The U.S. federal antitrust agencies' Intellectual Property Licensing Guidelines treat trade secrecy the same way they treat other forms of intellectual property.[1] Antitrust commentary focused on trade

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[1] *See* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY § 2.1 (1995), *available at* http://www.usdoj.gov/atr/public/guidelines/0558.pdf [hereinafter "IP Guidelines"]. A more recent report issued by the federal enforcement agencies similarly treats trade secrets the same as other forms of intellectual property. *See* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION (2007),

secrets is scarce.[2] In a sense, the antitrust metes and bounds circumscribing the use of trade secrets are as elusive as trade secrets themselves.

There is no inherent reason for trade secrets to have escaped antitrust scrutiny. The core of a trade secret is the competitive significance of undisclosed information, so the possession and use of trade secrets would seem bound to raise antitrust questions. For example, can dominant firms be forced to disclose trade secret information to rivals? Those who have such information frequently license its use to others. What restrictions can be placed on a licensee's use of such information, particularly when the licensee is a competitor of the licensor, or on the licensee's sales of products that embody trade secrets?

The purpose of this chapter is to reveal the competition issues that trade secrecy protection raises. This inquiry shows that although the antitrust treatment of trade secrets fits generally into the debate over the proper antitrust treatment of intellectual property rights, the arguments for according deference to the use of confidential trade secret information are somewhat different, and far weaker, than the arguments for according such deference to the holders of either patents or copyrights.

The chapter begins with the fundamental issues for antitrust analysis of trade secrets: What is a trade secret and what consequence should flow from a firm's decision to choose the trade secret regime when it wants to protect information? The next section maps the state of the law dealing with antitrust and trade

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http://www.usdoj.gov/atr/public/hearings/ip/222655.pdf [hereinafter "Promoting Innovation"]. The IP Guidelines are discussed *infra* notes 25–26 and accompanying text.

[2] *See, e.g.*, A.B.A. SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS, 1156–57 (6th ed. 2007) [hereinafter ALD 6] (briefly noting various antitrust doctrines implicated by trade secrets law); JERRY COHEN & ALAN S. GUTTERMAN, TRADE SECRETS PROTECTION AND EXPLOITATION 379–95 (BNS Books 1998) (stating that most trade secret licenses are upheld by antitrust courts); HERBERT HOVENKAMP, MARK D. JANIS & MARK A. LEMLEY, IP AND ANTITRUST: AN ANALYSIS OF ANTITRUST PRINCIPLES APPLIED TO INTELLECTUAL PROPERTY LAW § 33.8c (Aspen Publishers 2007) (noting that "several" courts have upheld horizontal geographical restrictions involving trade secret licenses on the ground that each restriction was "ancillary" to a technology-sharing joint venture); 2 MELVIN F. JAGER, TRADE SECRETS LAW §§ 11:1–6 (West 2009); Rudolph Peritz, *Competition policy and its implications for intellectual property rights in the United States*, *in* THE INTERFACE BETWEEN INTELLECTUAL PROPERTY RIGHTS AND COMPETITION POLICY 190–93 (Steven D. Anderman ed., Cambridge University Press 2007) (stating that trade secret protection generally does not cause antitrust problems).

secrets, beginning with the early history (which predates the Sherman Act), and then discusses how the courts have dealt with licensing issues under Section 1 of the Sherman Act and with exclusionary conduct under Section 2. The final section sets out and applies a more general framework for antitrust analysis of trade secrets, proposing three guiding principles: 1) Trade secrets should receive no deference or presumptions when raised as a defense to anticompetitive conduct. 2) Antitrust courts, when assessing the economic consequences of trade secret protections, should be mindful of the legal properties of trade secrets. 3) Antitrust courts should respect—but not expand—the bargain that trade secret protection provides to its holders to incentivize investment in the production of information.

II. Analytical Fundamentals

A. What Is A Trade Secret?

Definitional issues loom large in understanding trade secrets, beginning with the question of what sort of right a trade secret is. Some argue that a trade secret is a property right; some argue that it is an *intellectual* property right.[3] Trade secrecy protection can claim state common law tort roots, for it provides an ex post cause of action for misappropriation by an agent or a knowing third party, but trade secrecy protection can also be the product of contract, whether express or implied.[4] Trade secrets now also find some definition in state statutory law (primarily the Uniform Trade Secrets Act[5]), in federal law (the Economic

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[3] *See, e.g.*, Richard Epstein, *The Constitutional Protection of Trade Secrets Under the Takings Clause*, 71 U. CHI. L. REV. 57, 60 (2004) (arguing that the protection of trade secrets is closely analogous to physical property rights); Mark A. Lemley, _, supra/infra this volume.

[4] *See* RESTATEMENT (FIRST) OF TORTS § 757 (1939) (recognizing a cause of action for using or disclosing another's trade secret); RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 39 cmt. h (1995) (acknowledging the analogy between trade secrecy and "claims in tort alleging the appropriation of ideas," while pointing out that plaintiffs often "rely on contract claims alleging an express or implied-in-fact promise by the recipient"); Katarzyna A. Czapracka, *Antitrust and Trade Secrets: The U.S. and the EU Approach*, 24 SANTA CLARA COMPUTER & HIGH TECH. L.J. 207, 213–215 (2008) (discussing the roots of trade secrecy protection in contract theory).

[5] UNIF. TRADE SECRETS ACT § 1 (1985) (defining trade secrets as "information [that] derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and . . . is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.").

Espionage Act of 1996[6]), and, to a degree, in international treaties (TRIPS Article 39[7]).

Related to the question of the mixed legal basis for trade secrets is the question of what sort of information can qualify as a trade secret. The problem here is that "information" has no conceptual boundary and the three usual qualifications on what information trade secrecy protects—the information must be used in business, provide a competitive advantage, and be secret—are similarly broad.[8] To further complicate things, trade secrets are sometimes lumped in with "know-how," an even less precise type of information that seems to have no legal definition whatsoever.[9] The result is that calling something a "trade secret" tells us very little about the type of information that we are being asked to protect.

There is one important way in which trade secrets have *not* been characterized, however. Courts have generally not called a

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[6] Economic Espionage Act of 1996, 18 U.S.C. § 1839 (2006) (defining trade secrets as "all forms and types of financial, business, scientific, technical, economic, or engineering information [if] the owner thereof has taken reasonable measures to keep such information secret; and . . . the information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by, the public . . . .").

[7] Agreement on Trade-Related Aspects of Intellectual Property Rights, Art. 39, Dec. 15, 1993, 33 I.L.M. 81, 98 (1994) (defining trade secrets as information that "is secret in the sense that it is not . . . generally known among or readily accessible to persons within the circles that normally deal with the kind of information in question . . . has commercial value because it is secret [and] has been subject to reasonable steps . . . to keep it secret.").

[8] *See* Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470, 474–75, 493 (1974) (finding that Ohio law, which adopted this three-part test, was valid and not preempted by federal patent law).

[9] Antitrust commentators often use the terms interchangeably. *See* ALD 6, *supra* note 2, at 1156 n.570; S. Chesterfield *The Patent-Antitrust Spectrum of Patent and Know-How License Limitations: Accommodation? Conflict? Or Antitrust Supremacy?*, 15 Pat. Trademark & Copy. J. Res. & Ed. 1, 18 (1971) ("In my discussion I use the terms "trade secret" and "secret know-how" as virtually interchangeable"). Economists refer generally to the difficulties of exchanging non-codified knowledge, without regard to legal characterization. *See, e.g.*, Eric Brousseau, Natalia Lyarskaya & Carlos Muniz, *Complementarities Among Governance Mechanisms: An Empirical and Theoretical Assessment of Cooperative Technology Agreements*, *in* WORKING WITHIN THE BOUNDARIES OF INTELLECTUAL PROPERTY 229, 233 (Rochelle C. Dreyfuss, Harry First, & Diane L. Zimmerman eds. 2010) ("[T]he impossibility of fully codifying knowledge leads to a weaker protection of intellectual property rights . . . .").

trade secret a "monopoly."[10] This is unlike other intellectual property rights, particularly patent and copyright, which have a long history of being seen in monopoly terms. For some time the monopoly label led courts to restrict patent and copyright holders in their sales of products protected by these rights, particularly in their ability to tie together complementary products.[11] Although the Supreme Court has long recognized that patents do not necessarily confer monopoly power, it was not until 2007 that the Court finally rejected the economic equation of patent rights and monopoly.[12]

From the point of view of antitrust analysis, the fact that trade secrets do not come freighted with the monopoly tag is paradoxically liberating, because it helps us see how trade secrets do and do not function:

(1) Trade secrets are about appropriability. They provide protection for confidential firm-specific information so as to allow those who have access to the information to appropriate the economic benefits that the information can provide. Trade secrets do not come with the legislative assumption that monopoly profits are needed to incentivize the production of this information. On the contrary, trade secrecy protection simply recognizes that businesses create all sorts of information and would have trouble competing effectively were their operations simply on view to their competitors.

(2) Trade secrets come with no legislative assumption about the innovative quality of the information being protected. Unlike patents, for example, there is no economic policy to give the holders of trade secrets additional profits so that they will produce the optimal level of secret information. If a mattress seller provides "secret" instructions to its sales people on how best to sell a mattress, we might protect those secrets from being

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[10] That is, other than the Federal Circuit. *See* Dow Chem. Co. v. Exxon Corp., 139 F.3d 1470, 1474 (Fed. Cir. 1998) (describing Ohio's law of trade secrets as having "granted monopoly protection to processes and manufacturing techniques.").

[11] *See, e.g.*, United States v. Glaxo Group Ltd., 410 U.S. 52, 61-62 (1973).

[12] *See* Illinois Tool Works Inc. v. Indep. Ink, Inc. 547 U.S. 28, 46 (2007) (holding that "a patent does not necessarily confer market power upon the patentee"). For an earlier case recognizing that patents do not by themselves confer an economic monopoly, *see* Standard Oil Co. of Indiana v. United States, 283 U.S. 163, 175 (1931) (recognizing competing patented processes for producing "cracked" gasoline and finding that "no monopoly" resulted from cross-licensing the patents in question) (Brandeis, J.).

misappropriated by a faithless employee, but that does not make the sales method innovative, nor would there be any sound reason to protect this sales method through the grant of a patent, thereby excluding others from selling mattresses in a similar way.[13]

(3) Firms have the option of exploiting secret information in whatever way they think will maximize profits, whether it is through keeping the information within the firm or sharing the secrets with others outside the firm in a cooperative working relationship.[14] Whatever competitive significance the confidential information has comes from the economic benefits the information confers on those who use it, rather than being directly connected to a specific product that embodies that information. In contrast to patented products or copyrighted products, there are no "trade secreted" products.

B. Regime Choice

Parties often have a choice of legal regime for protecting information. For example, under federal law, trade secrets can include "patterns, plans . . . programs, or codes,"[15] any of which could be protected under copyright law. Similarly, federal law includes as trade secrets "prototypes, methods, techniques, processes, [and] procedures," any of which might be eligible for patent protection. Taking just one industry as an example, developers of software interfaces have shifted their protective regime from trade secrets, to copyright, then to patent, and finally back to trade secrets in an effort to find the legal regime that gives them the most protection for this type of information.[16] Each regime has its legal advantages and disadvantages.

When invention is involved, the closest potential legal substitute for trade secrecy is the patent system. Economists suggest that firms will have the greatest incentive to patent where inventions are self-revealing in use, because those inventions

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[13] This does not mean that the mattress seller might not want such a patent, or even that the Patent Office might not (outrageously) grant such a patent. *See* Harry First, *Controlling the Intellectual Property Grab: Protect Innovation, Not Innovators*, 38 RUTGERS L. REV. 365, 378–79 (2007) (discussing a patent on "Methods of Promoting Sleep Systems").

[14] *See* Brousseau et al., *supra* note 9, at 233.

[15] 18 U.S.C. § 1839(3) (2006).

[16] *See* Pamela Samuelson, *The Strange Odyssey of Software Interfaces and Intellectual Property Law* (U.C. Berkeley Public Law Research Paper No. 1323818, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1323818.

cannot be kept secret once the product that embodies them is publicly sold.[17] Conversely, firms have incentives to use trade secrecy for inventions that can be kept secret for longer than the patent term. Firms may choose to rely on trade secret protection for other types of inventions as well, particularly because of the time and expense associated with obtaining a patent.[18]

The two regimes are not perfect legal substitutes, however. Patents provide a clearer property right, because of the registration and specification requirements, but they also come with a fixed, limited term. Trade secrets are undefined until it is time to litigate, and they last as long as the firm can keep a secret—long for Coca-Cola, shorter for many high-technology companies that cannot delete all knowledge from ex-employees' brains.[19] For an invention to qualify for a patent it must be useful and non-obvious, and it is tested by government examination before being accorded protection.[20] For a writing to qualify for copyright, it must be original.[21] Trade secrets may be valuable because they are secret, but there is no threshold of originality for protection except in cases where the public availability of the secret information undercuts the claim that it had been kept secret.[22] So, for example, information in a database may be protected by trade secrecy, while at the same time, the database will be unprotected by copyright because it lacks originality.[23]

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[17] *See* Mark A. Lemley, *The Surprising Virtues of Treating Trade Secrets as IP Rights*, 61 STANFORD L. REV. 311, 338–39 (2008) (giving paper clip as an example of an invention which could easily be analyzed and reproduced without the protection of a patent); Katherine J. Strandburg, *What Does The Public Get? Experimental Use and the Patent Bargain*, 2004 WISC. L. REV. 81, 104-07 (discussing self-revealing and non-self revealing inventions vis-à-vis trade secrecy and patenting).

[18] *See* JAMES BESSEN & MICHAEL J. MEURER, PATENT FAILURE: HOW JUDGES, BUREAUCRATS, AND LAWYERS PUT INNOVATORS AT RISK 218, 289 n.3 (2008).

[19] *See* Edwin Mansfield, *How Rapidly Does New Industrial Technology Leak Out?*, 34 J. INDUS. ECON. 217, 219–21 (1985) (explaining that information about the detailed nature and operations of a new product or process is in the hands of at least some rival firms within a year, on the average, after a new product is developed, and sometimes within six months).

[20] 35 U.S.C. §§ 101–103, 131 (2006).

[21] 17 U.S.C. § 102(a) (2006).

[22] *See, e.g.*, CVD, Inc. v. Raytheon Co., 769 F.2d. 842 (1st Cir. 1985) ("Once a trade secret enters the public domain, the possessor's exclusive rights to the secret are lost.").

[23] *See* Feist Publ'ns, Inc. v. Rural Tel. Serv. Co., Inc., 499 U.S. 340, 364 (1991).

It is fair to assume that when firms choose one regime over another to protect information, they have made a rational cost-benefit decision. Each legal regime will have varying incidents depending on its statutory bases and purposes. Private parties cannot combine regimes to get all the protection they would like. They must take the bitter with the sweet.

How should this strategic choice affect antitrust analysis? At present, neither antitrust courts nor antitrust enforcement agencies appear to be paying any sustained attention to regime choice. The current federal antitrust enforcement agency guidelines relating to licensing intellectual property, issued in 1995, analyze trade secrets as but one form of intellectual property. Although these guidelines recognize that there are "clear and important differences" among the "intellectual property regimes of patent, copyright, and trade secret," the guidelines state that "the governing antitrust principles are the same."[24] Indeed, despite the acknowledged legal differences among these regimes, nowhere in the guidelines do these distinctions make a difference.

The guidelines do not distinguish among the various forms of intellectual property protection because they see these forms as all performing the same economic function, that is, providing "incentives for innovation and its dissemination and commercialization by establishing enforceable property rights for the creators of new and useful products, more efficient processes, and original works of expression."[25] Certainly, some trade secrets do protect innovative products or processes, but, as we have seen, trade secrecy protects "information" that may have nothing to do with innovation (a database, for example, or a customer list).

Antitrust enforcers have not always taken the position that antitrust analysis should be the same without regard to whether a patent or a trade secret is involved. Justice Department enforcement guidelines issued in 1977 made some effort to give lesser scope to the licensing of trade secrets than to the licensing of patents, stressing the lack of Congressional mandate for trade secrets and the lack of patent law's disclosure *quid pro quo* for legal protection.[26] But these distinctions have been lost under the

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[24] IP Guidelines, *supra* note 1, § 2.1.

[25] *Id.* § 1.0.

[26] *See* U.S. DEP'T OF JUSTICE, ANTITRUST GUIDE FOR INTERNATIONAL OPERATIONS, Cases E, F, at 32–33 (1977). *See also* Richard H. Stern, *The Antitrust Status of Territorial Limitations in International Licensing*, 14 PAT. TRADEMARK & COPY. J. RES. & ED. 580, 589–94 (1970–1971) (discussing the

current guidelines, with antitrust analysis focusing more on economic effects than on legal categories and ignoring the different legal properties of the trade secrets regime.

Regime choice should matter to antitrust analysis, however, because the nature of the legal protection granted the right-holder is related to the economic reasons for that protection. Parties that choose trade secrets over patent are making a decision that may very well reflect what they feel needs protecting the most, as well as accepting the trade-offs that such a decision entails. Parties that choose trade secrecy do not make public disclosure, but they do gain protection from misappropriation, even when "free" appropriation might advance competition in the short run. By not taking the "patents for disclosure" bargain they also lose the ability to keep others from developing the same invention through reverse engineering, a significant risk associated with trade secret protection.[27] In assessing the economic effects of restrictive agreements or exclusionary conduct related to trade secrets, good economic analysis will pay attention to these legal choices that the parties have made.

III. Antitrust Treatment of Trade Secrets: The State of the Law

A. Historical Background

1. Pre-Sherman Act

Courts began considering the potential anticompetitive effects of protecting trade secrets long before passage of the Sherman Act in 1890. They did so in the context of the common law rule that contracts "in restraint of trade" were considered void, but that some types of contracts could be enforceable so long as the restraint in the agreement was "not unreasonable."[28] Four important pre-Sherman Act cases show the difficulties in applying this reasonableness test when trade secrets are involved.

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analogy between patent and trade secret licensing) (author was chief of the Patent Section of the Antitrust Division).

[27] *See* Bonito Boats, Inc. v. Thunder Craft Boats, Inc., 489 U.S. 141, 150–151 (1989) (discussing the bargain of legal protection and disclosure faced by patent recipients).

[28] *See* Oregon Steam Navigation Co. v. Winsor, 87 U.S. 64, 66–67 (1874) ("It is a well-settled rule of law that an agreement in general restraint of trade is illegal and void; but an agreement which operates merely in partial restraint of trade is good, provided it be not unreasonable and there be a consideration to support it.") (upholding a territorial division of markets).

The first is *Vickery v. Welch*,[29] the first reported trade secrets case in the United States, which was decided by the Massachusetts Supreme Court in 1837.[30] Welch sold his chocolate manufacturing plant to Vickery "'together with his exclusive right and art or secret manner of making chocolate, and all information pertaining to his said manner of making chocolate.'"[31] Welch subsequently refused to convey this alleged exclusive right or "art," stating "'that I have no patent or other exclusive right or arts except what I have gained by my skill and experience . . . and do not hereby even impliedly covenant not to communicate the results of my experience to others.'"[32] In fact, it appeared that "two or three others" knew this "secret art" but had agreed not to divulge it so long as Welch was still manufacturing chocolate.[33]

Vickery sued on Welch's bond. The court gave judgment on the bond for Vickery.[34] The court had no trouble finding Welch's claim inconsistent with his contractual obligation, rejecting the argument that the contract was void because it was in restraint of trade.[35] The court reasoned that if the secret art were worth anything, "the defendant would use the art and keep it secret, and it is of no consequence to the public whether the secret art be used by the plaintiff or by the defendant."[36] The court assumed that the value of the transaction was affected by the covenant to convey the exclusive right to the secret, but it did not explore the question whether the public would have been better off had the price been lower, the secret non-exclusive, and the defendant left free, "for love or money, to communicate the secret to all other people."[37]

The second case is *Taylor v. Blanchard*,[38] decided by the Massachusetts Supreme Court nearly thirty years later. Taylor manufactured shoe-cutters, the manufacture of which the court described as "an art" known only to the plaintiff and three other

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[29] 36 Mass. 523 (1837).

[30] *See* Melvin F. Jager, 2 TRADE SECRETS LAW § 11:3 (2008).

[31] 36 Mass. at 523.

[32] *Id.* at 523–24.

[33] *Id.* at 524.

[34] *Id.* at 527.

[35] *Id.*

[36] *Id.*

[37] *Id.*

[38] 95 Mass. 370 (1866).

business firms.[39] Blanchard, who was "wholly ignorant of the business," became Taylor's partner, agreeing that if the partnership ended, he would not divulge "any of the secrets" relating to the business nor establish any shoe-cutter business in Massachusetts.[40] Three years later the business dissolved, Blanchard opened a competing business in Boston, and Taylor sued to collect liquidated damages.[41]

Competition concerns won out in this case. The court began its opinion by pointing out that "[t]he law has always regarded monopolies as hostile to the rights and interests of the public."[42] One exception to this policy is for grants to use a new invention for a limited period, "indulged for the encouragement of ingenuity"; patent and copyright laws "rest on this ground."[43] Another exception is for "contracts for the partial restraint of trade," which might be upheld "to a reasonable extent."[44] Citing *Vickery v. Welch*, the court noted that a party might lawfully bind himself not to carry on a "secret trade" or not to divulge the secret.[45] But the court in this case rejected the argument that Taylor's art was "secret."[46] The method for manufacturing shoe-cutters might not be "generally known to the public," but it was carried on "in three different towns in the Commonwealth, by three different parties, who had no connection in business with the parties to this contract."[47] Whether there was anything unusual (or innovative) about Taylor's process that might favor protection was of no apparent concern to the court; nor was the court much concerned about assessing how much competition there was among the various shoe-cutters or whether excluding Blanchard would affect that competition. It was enough for the court that "[c]ombinations of men in business . . . often succeed in obtaining exorbitant profits from the public."[48]

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[39] *Id.* at 370.

[40] *Id.* at 371.

[41] *Id.*

[42] *Id.* at 372.

[43] *Id.*

[44] *Id.* at 373.

[45] *Id.* at 374.

[46] *Id.*

[47] *Id*. at 373–74.

[48] *Id*. at 375.

The third case, *Peabody v. Norfolk*,[49] was decided by the Massachusetts Supreme Court only two years after *Taylor v. Blanchard*. Peabody had for many years engaged in "inventing and adapting machinery, and originating and perfecting a process, to manufacture gunny cloth from jute butts."[50] Once successful, he built a "large factory" and hired Norfolk, a machinist, to be the engineer of the factory, requiring him to sign a contract to consider the machinery "sacred" and to prevent others from learning how to use it.[51] Less than two years later, Norfolk left Peabody's employ, with models and drawings, and was helping others to set up a competing plant. Peabody sought to enjoin Norfolk from communicating the secrets to others.[52]

The court's approach was now more like the approach in *Vickery* than the approach in *Taylor v. Blanchard*. The court easily rejected a defense argument that the contract should be void as in restraint of trade but it made no mention of the evils of monopoly. Instead, the court wrote somewhat expansively about what we would today consider the economic justifications for upholding such contracts: "It is the policy of the law, for the advantage of the public, to encourage and protect invention and commercial enterprise."[53] This encouragement could be done through protecting good will, trade marks, patents on "new and useful" inventions, and secret processes of manufacture "whether a proper subject for a patent or not."[54] The court recognized that secret processes are protected differently than patents—there is no "exclusive right to it as against the public, or against those who in good faith acquire knowledge of it."[55] But the court also recognized that such secrets are protected for a somewhat different purpose—"to prevent . . . a breach of trust."[56]—and noted that Justice Story had stated the policy for protecting trade secrets "in the broadest terms," as follows: Courts will restrain a party from disclosing secrets "'communicated to him in the course of a

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[49] 98 Mass. 452 (1868). *Peabody* is credited with "crystallizing the law of trade secrets in the United States." *See* Robert G. Bone, A New Look at Trade Secret Law: Doctrine in Search of Justification, 86 CAL. L. REV. 241, 252 (1998).

[50] 98 Mass. at 453.

[51] *Id.*

[52] *Id.* at 454.

[53] *Id.*

[54] *Id.* at 457–58.

[55] *Id.* at 458.

[56] *Id.* at 458.

confidential employment; and it matters not, in such cases, whether the secrets be secrets of trade or secrets of title, or any other secrets of the party important to his interests.'"[57]

These three early cases look surprisingly familiar. The economic problems entrepreneurs faced in the 1800s are the same as entrepreneurs face today. Inventors need capital and labor for manufacturing; the manufacturing process takes skill and knowledge; skill and knowledge are hard to convey and hard to protect, at least to the degree necessary to appropriate their benefits. Courts seek to protect relations of trust and contracts that enable knowledge and skill to be transferred, recognizing that such arrangements can incentivize invention. At the same time, the courts recognize that such agreements can harm the public by restraining competition. Somehow a balance must be struck, as the court said in *Taylor v. Blanchard*, "for the sake of the public, and not for the sake of the parties."[58]

The fourth significant case, however, shows how trade secrets can easily go beyond the paradigmatic examples—inventor/investor or employer/faithless employee—and be used to create much broader anticompetitive arrangements. This case also shows the tendency of common law courts to weight the interests of secrecy and invention over the interests of the public in competition.

The case is *Fowle v. Park*,[59] decided by the U.S. Supreme Court in 1889, one year before passage of the Sherman Act. *Fowle* involved "Wistar's Balsam of Wild Cherry," a "medicinal preparation" good for "certain complaints and diseases."[60] In 1844 its original inventor had conveyed the formula and manufacturing rights in enumerated states to one Butts, who then conveyed his rights to Fowle. At the same time the inventor conveyed the rights in other states to Park. In the conveyances, both Fowle and Park agreed not to sell the elixir below a set price.[61] Between 1849 and 1864 both Fowle and Park were selling small amounts of the product west of the Rockies "in competition."[62] As this area became more populated, Fowle paid Park to agree not to sell in the

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[57] *Id.* at 459.

[58] Taylor v. Blanchard, 95 Mass. at 373.

[59] 131 U.S. 88 (1889).

[60] *Id.* at 88.

[61] *Id.*

[62] *Id.*

West. Over time, however, Park began selling in Fowle's territories, at prices below those specified in the original agreements. In 1884, Fowle sued for an injunction and damages.[63]

The Supreme Court was "unable to perceive" how the contract could be regarded as "so unreasonable" as to be unenforceable.[64] The Court's reasoning combined the policies of protecting trust and protecting incentives. The inventor, the Court wrote, had "property" in the "secret process of manufacturing the article he had discovered," so his grantees "could claim relief as against breaches of trust in respect to it."[65] Further, the policy of the law "is to encourage useful discoveries by securing their fruits to those who make them."[66] Harking back to the reasoning in *Vickery v. Welch*, the Court wrote that "[i]f the public found the balsam efficacious, they were interested in not being deprived of its use, but by whom it was sold was unimportant."[67]

Lost in the Supreme Court's analysis was any concern for competition or for assessing how innovative the formula for "Wistar's Balsam of Wild Cherry" was. The public was not quite indifferent as to who was selling the medication; presumably consumers preferred to buy it at Park's lower price. Similarly, the law might want to incentivize invention, but how confident could the Court be that this "secret" process—discovered and conveyed forty years before Fowle ever brought suit—was still even secret, let alone (in the Court's words) a "useful discovery"?

2. Early Sherman Act Decisions

Fowle v. Park played a minor role in the legislative history of the Sherman Act. In the debate in the House of Representatives, Representative Morse placed the Supreme Court's decision into the Congressional Record.[68] Morse's concern was not the protection of trade secrets or innovation, but the protection of what he called the "contract system" of specifying minimum resale prices as a way to prevent "cutthroat competition" and "insure quality."[69] Although Morse approved "suppress[ing] great combinations that

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[63] *Id.*

[64] *Id.* at 97.

[65] *Id.*

[66] *Id.*

[67] *Id.*

[68] *See* 21 CONG. REC. 5,954–55 (June 11, 1890).

[69] *Id.* at 5,954.

oppress the people," he wanted manufacturers and merchants to be able to control resale prices, a result which the Supreme Court had allowed under the common law by upholding the agreements in *Fowle*.[70] No one took up Morse's argument, however, and the Sherman Act passed with its deliberately ambiguous language outlawing "restraints of trade or commerce."[71] As Representative Culberson explained, when reporting the bill on behalf of the House Judiciary Committee: "Now, just what contracts . . . will be in restraint of the trade or commerce mentioned in the bill will not be known until the courts have construed and interpreted this provision."[72]

Courts were soon presented with cases raising the question whether the type of agreements used in *Fowle* would be lawful under the new Act. In two important decisions the courts tilted the rule of reason balance back towards competition, a result more traceable to the courts' careful reasoning than to the change in the legal regime. Interestingly enough, both cases involved the same price-cutter whom Fowle had successfully sued, John D. Park.[73]

The first case is *John D. Park & Sons Co. v. Hartman*,[74] decided by the Sixth Circuit in 1907. Hartman manufactured "Peruna," then the most popular "patent medicine" on the market (although there was no patent, of course).[75] Peruna was manufactured under a secret formula "known only to him and his trusted employees."[76] Hartman sold Peruna to distributors with a required minimum resale price. Park managed to get supplies of

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[70] *See id.*

[71] 15 U.S.C. § 1.

[72] 21 CONG. REC. 4,089 (May 1, 1890).

[73] *See Patent Medicine Trade; Efforts to Secure a New Plan for Distributing Articles: Cutters Still Defy Wholesalers*, N.Y. TIMES, Nov. 29, 1895, at 8; *18 Years Getting A Suit To Trial; Action of John D. Park & Sons Co. Against Alleged Drug Trust Almost Ready*, N.Y. TIMES, June 7, 1915, at 7; Rudolph J.R. Peritz, *"Nervine" and Knavery: The Life and Times of* Dr. Miles Medical Company, *in* ANTITRUST STORIES 74–90 (Eleanor M. Fox & Daniel A. Crane eds., 2007) (discussing the wide scope of contemporaneous litigation involving assertions of exclusionary rights by intellectual property holders).

[74] 153 F. 24 (6th Cir. 1907).

[75] *See* Peritz, *supra* note 73, at 80.

[76] Hartman v. John D. Park & Sons Co., 145 F. 358, 359 (C.C.E.D. Ky. 1906). It turned out that "Peruna" was in fact a mixture of 72.5% water, 27.07% alcohol, and nearly all the rest burnt sugar; numerous "chemists and doctors" agreed that "the stuff had absolutely no medical value." E.E. Munger, *Education as an Adjuvant*, *in* THE MEDICO-PHARMACEUTICAL CRITIC AND GUIDE 138 (William J. Robinson ed., 1907).

Peruna which it then sold to retailers below the fixed minimum price.[77]

Judge Lurton's opinion addressed two critical issues. The first was whether trade secrets deserved the same legal exemption from competition rules as patents and copyrights. The second was whether the price restraints that Hartman placed on its wholesale and retail distributors were reasonable, either at common law or under the new Sherman Act. The former involved what we would think of today as the conflict between antitrust and intellectual property; the latter involved the proper analytical approach for applying the rule of reason.

Lurton firmly rejected equivalent treatment for trade secrets and patents and copyrights. As he understood the law at the time, patentees and copyright holders could impose resale price restraints on their buyers or licensees.[78] Lurton pointed out, however, that trade secrets were different, both legally and economically. The holder of a trade secret "cannot appeal to the protection of any statute creating a monopoly in his product" or giving him any "special property" interest.[79] The economic value of a trade secret comes from keeping the information secret, so the law will protect the transfer of the secret information under a promise of confidentiality, just as the law protects the transfer of other types of information upon similar promises.[80] Were it otherwise, "'there could be no sale of secret processes of manufacture.'"[81] But the public remains free to discover the process, if it can, and, once discovered, "anyone has the right to use it."[82]

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[77] 145 F. at 359.

[78] 153 F. at 27. This would soon change, as the Supreme Court would come to hold that resale price restraints were not within the statutory rights of patentees or copyright holders and violated the Sherman Act. *See, e.g.*, Bobbs-Merrill Co. v. Straus, 210 U.S. 339, 351 (1908); Straus v. Victor Talking Mach. Co., 243 U.S. 490, 501 (1917); United States v. Gen. Elec. Co., 272 U.S. 476, 489 (1926) ("It is well settled . . . that where a patentee makes the patented article, and sells it, he can exercise no future control over what the purchaser may wish to do with the article after his purchase. It has passed beyond the scope of the patentee's rights.").

[79] 153 F. at 29.

[80] *See id.* at 30–30 (discussing the examples of stock quotations and news).

[81] *Id.* at 31 (quoting Ammunition Co. v. Nordenfeldt, L.R. 1 Ch. Div. 630 (1894)).

[82] *Id.* at 29.

Lurton also rejected the argument—implicit in the earlier trade secrets cases from *Vickery v. Welch* to *Fowle*—that because trade secret owners have the right to keep the process secret and not share it with others, or even to not make the product at all, it should not matter to the public whether the product is produced and sold by the trade secret holder or by others.[83] Lurton pointed out, however, that the only thing that trade secret law protects is the secret itself, not the product manufactured under the secret.[84] Distribution of the product would not reveal that secret—except to the extent that the buyer might lawfully figure it out—so there was no economic reason to allow the trade secret owner to control further trade in the product. The manufacturer of a product produced under secret process should be treated just the same as "the man who grows potatoes."[85] Neither product's "commercial value" will "vanish" if subjected to the normal principles that govern restraints of trade.[86]

Lurton then went on to the second issue, applying common law principles to Hartman's contracts. The legal test was the "ancillary restraints" doctrine, developed by then-Judge Taft nine years earlier in the already-famous *Addyston Pipe* case:[87] Are the covenants "ancillary to a principal contract" and "no more than necessary to afford a fair protection to the business of the complainant and not so large as to interfere with the interests of the public"?[88] Lurton saw the "prime object" of this agreement as the suppression of competition among wholesalers and retailers (in other words, this was primarily a dealers' cartel), with only an incidental benefit to the manufacturer that was not intended to protect its "retained business" from the buyer's competition, as would be the case in the sale of a business with a covenant not to compete.[89] The economic effects, though, were large. This was a "general system" of contracts: "The single covenant might in no way affect the public interest, when a large number might."[90]

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[83] *See id.* at 30.

[84] *See id.* at 29.

[85] *Id*. at 33.

[86] *Id.*

[87] *See* United States v. Addyston Pipe Co., 85 Fed. 271 (6th Cir. 1898).

[88] 153 F. at 41, 43 (citing *Addyston Pipe*, 85 Fed. at 281, 282).

[89] 153 F. at 45.

[90] *Id.* at 41, 43. Lurton began his opinion by noting that this type of agreement had "generally been adopted" by retail and wholesale druggists in the

Further, there were no competing manufacturers to supply the product—there was only one "Peruna." Thus, retailers not bound by the agreement could not supply the public with a substitute. The result of the agreement, then, would be sales "at a higher price to the consumer than would otherwise have been paid."[91] This was not in the interests of the public. Allowing the parties to suppress allegedly "demoralizing" low prices would "whittle away broad economic principles lying at the bottom of our public policy."[92]

The reasoning and result in *Hartman* were echoed in the second important case, the Supreme Court's 1911 decision in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*[93] *Dr. Miles* later became enshrined in antitrust jurisprudence as the case holding that vertical resale price agreements are illegal per se (although the Court did not use such terms then), a precedent that lasted ninety-six years before being overruled in 2007.[94] At the time of its decision, however, the case was more a reprise of Judge Lurton's decision in *Hartman*. Indeed, *Dr. Miles* was argued by the same lawyers on both sides who had argued *Hartman*, and it was decided below by Judge Lurton for the same Sixth Circuit panel (his opinion began by noting that there was "no substantial difference" between the contracts or products in the two cases).[95] By the time *Dr. Miles* reached the

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United States, "a business which amounts to more than $60,000,000 annually." *Id*. at 26.

[91] *Id.* at 45.

[92] *Id.* at 46. Included in the price-cutters about which Hartman complained were "department stores." *Cf.* Bobbs-Merrill Co. v. Straus, 210 U.S. 339, 351 (1908) (invalidating a minimum price restriction imposed on Macy's for the sale of a copyrighted book).

[93] 220 U.S. 373 (1911).

[94] *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 907 (2007).

[95] *See* Dr. Miles Med. Co. v. John D. Park & Sons Co., 164 F. 803, 809 (6th Cir. 1908) ("We see no substantial difference between the systems of contracts under which the Dr. Miles Medical Company is now conducting its business and that under which Dr. Hartman carried on his business as a manufacturer of Peruna, considered by this court at length in the case of John D. Park & Sons v. Hartman."). The legal difference was that Dr. Miles recast the relationship between it and its wholesalers and retailers as one of "agency" and the transfers of the product as "consignments." 220 U.S. 373, 397–98. While Lurton found this to be subterfuge, *see* 164 F. 804–05, the Supreme Court in *Dr. Miles* avoided the issue by finding that the system was intended to bind wholesalers or retailers even if they purchased the products from parties other than Dr. Miles. *See* 220 U.S. at 399. *See also* Peritz, *supra* note 73, at 86–89.

Supreme Court, Lurton had been appointed an Associate Justice. Although he recused himself from the case, the Court's opinion closely followed his views.

The first issue was whether price-restrictive agreements involving trade secrets should be treated the same as price-restrictive agreements involving patents.[96] As in *Hartman*, the Court carefully distinguished the two rights. Patents are given to an inventor for a fixed time "to stimulate invention."[97] Dr. Miles, however, "has no statutory grant" and "has not seen fit to make the disclosure required by the statute."[98] As in *Hartman*, the Court also distinguished between communicating the secret and selling the manufactured product: "It is said that the [medicinal] remedies 'embody' the secret. It would be more correct to say that they are manufactured according to the secret process and do not constitute a communication of it."[99]

The second issue was whether the agreements unreasonably restrained trade. The Court here did not invoke the "ancillary restraints" doctrine discussed in *Hartman*, but its articulation of the proper test was quite similar. The restraint, the Court wrote, must be reasonable "both with respect to the public and to the parties" and must be "limited to what is fairly necessary" to protect the covenantee.[100] This was not a case of a sale of a business or goodwill or the "right to use a process of manufacture," nor was it a single transaction "conceivably unrelated to the public interest."[101] Rather, the agreements were intended to "maintain prices" primarily for the benefit of

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[96] Note that the Court had previously held that the grant of a copyright does not include the right to set resale prices. *See Bobbs-Merrill*, 210 U.S. at 350–51. The law remained otherwise for patents. *See, e.g.,* E. Bement & Sons v. Nat'l Harrow Co., 186 U.S. 70, 92 (1902) ("[The Sherman Act] clearly does not refer to that kind of a restraint of interstate commerce which may arise from reasonable and legal conditions imposed upon the assignee or licensee of a patent by the owner thereof, restricting the terms upon which the article may be used and the price to be demanded therefore. Such a construction of the act, we have no doubt, was never contemplated by its framers."); United States v. Gen. Elec. Co., 272 U.S. 476, 494 (1926) (upholding a limit on selling prices imposed in a license to manufacture and vend).

[97] *Dr. Miles*, 220 U.S. at 401.

[98] *Id.* at 402.

[99] *Id.* at 403.

[100] *Id.* at 406.

[101] *Id.* at 407.

the dealers, leading the Court to treat the agreement "no better . . . [than if] the dealers themselves . . . formed a combination."[102] Dr. Miles having sold its product at prices satisfactory to itself, "the public is entitled to whatever advantage may be derived from competition in the subsequent traffic."[103]

To twenty-first century eyes, the two *Park* cases may look a little quaint, or even humorous. The "medicines," after all, were widely known to be composed mostly of alcohol, and their claims for efficacy strain credulity.[104] But the economic interests involved were substantial. As Lurton pointed out at the very beginning of his opinion in *Hartman*, the annual revenues of the proprietary medicine business were more than $60 million.[105] We cannot know whether Lurton or the Justices on the *Dr. Miles* Court were skeptical of the companies' secret formulae, unlike the *Fowle* Court's uncritical view of "Wistar's Balsam of Wild Cherry." But they were less willing to give broad immunity to trade secret claims where the innovation had never been tested by public examination, where the inventor did not disclose its invention for later public use, and where the protection could last far longer than the term of a patent.

Both cases are also important for their key analytical points. On the intellectual property side, the courts recognize that the economic value of trade secrets lies in being able to keep information secret but still transact around it. This means enforcing promises not to disclose secrets that transferees make to transferors, but it does not imply that trade secrets are the equivalent of patents. Rather, the products made through secret processes can be subject to the same competition rules as any other

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[102] *Id.* at 407–08.

[103] *Id.* at 409. *See* Thomas C. Arthur, *The Core of Antitrust and the Slow Death of* Dr. Miles, 62 SMU L. REV. 437, 456–62 (2009) (discussing the *Dr. Miles* case). *See also id.* at 446 (noting the nearly complete absence of any discussion of resale price maintenance in the legislative history of the Sherman Act) (citing Joseph E. Fortenberry, *A History of the Antitrust Law of Vertical Practices*, 11 RESEARCH IN LAW AND ECONOMICS 133, 209 n.161 (Richard O. Zerbe, Jr., ed. 1988))

[104] *See* Munger, *supra* note 76.

[105] *See* John D. Park & Sons Co. v. Hartman, 153 F. 24, 26 (6th Cir. 1907). Another indication of the economic interests involved is that counsel for the drug companies was Alton Parker, former Chief Judge of the New York Court of Appeals and the Democratic presidential candidate in 1904 (he was defeated by Theodore Roosevelt). *See* ALBERT H. WALKER, HISTORY OF THE SHERMAN LAW OF THE UNITED STATES 249 (1910).

product (whatever those rules might be)—they are to be treated no differently than potatoes. On the competition side, both courts condemned agreements that raise price; and both courts sought to keep competitive restrictions as narrow as possible in light of whatever permissible objectives the parties might have.

Neither case, however, disturbed a key point in *Fowle v. Park*. In *Fowle*, Park had been given the right to use the secret process as a manufacturer, subject to territorial and pricing limitations on sales of the product.[106] The courts in *Hartman* and *Dr. Miles* were able to distinguish *Fowle*, pointing out that in *Hartman* and *Dr. Miles*, Park was only a purchaser of the product, not a sharer of a secret.[107] This is certainly an important distinction, but it allowed the courts to avoid passing on the question whether price and territorial restrictions in a trade secret manufacturing license might be unreasonable restraints of trade, particularly when they clearly limit price competition between two direct manufacturing competitors. The question left open, to use Judge Lurton's words, was whether such restrictions were "no more than necessary to afford a fair protection to the business of the complainant and not so large as to interfere with the interests of the public."[108]

B. Current Law: Restraints of Trade

1. Price Restraints

Antitrust law has traditionally condemned price-fixing agreements, whether between competitors (horizontal) or between buyers and sellers fixing resale prices (vertical). The general view, which has its roots in the early cases such as *Addyston Pipe* and *Dr. Miles*, is that such agreements are per se unlawful.

Whether the per se rule would be applied to price restraints in trade secret licensing today, however, is unclear. As an historical matter, there has not been a legal challenge to *Dr. Miles*' apparent approval of such restraints in the context of licensing a trade secret to manufacturers that are competitors, and the Supreme Court later approved such licensing in the

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[106] *See* Fowle v. Park, 131 U.S. 88, 88 (1889).

[107] *See Hartman*, 153 F. at 32-33; *Dr. Miles,* 220 U.S. at 402.

[108] *Hartman*, 153 F. at 43.

patent context.[109] Nevertheless, subsequent twentieth-century commentators have taken the view that the courts would no longer approve such price restrictions,[110] and the federal agencies' 1995 IP Guidelines treat price restrictions as per se illegal, even when the manufacturer is the licensee and first seller of the product.[111]

The view that price restraints are per se unlawful has been taken in light of the background antitrust rule that all price fixing agreements are per se unlawful, whether between competitors (horizontal) or between a manufacturer and its distributor (vertical). In 2007, however, in *Leegin v. PSKS*,[112] the Supreme Court overruled *Dr. Miles*' per se ban on vertical resale price agreements.[113] Although the Court did not consider the application of its decision in the trade secrets or intellectual property context—indeed, no one raised the issue—it is difficult to avoid the conclusion that vertical resale price agreements when a trade secret license is involved would today be considered under the rule of reason.

Leegin raises two questions for trade secret licensing that courts have not yet faced. Suppose that a trade secret licensor (TS) licenses a manufacturer (M) to produce a product (P) using the trade secret. Setting the price at which M can sell P would appear to fall squarely within *Leegin*'s rule of reason holding. But suppose that TS is also a manufacturer of P. Is the price restraint now between competitors, and therefore subject to a per se rule? Or suppose that TS does not itself manufacture P, but licenses M_1, M_2, . . . M_n to manufacture P and then sets their selling prices. Is TS now orchestrating a horizontal cartel of Ms, making the agreements per se unlawful? There is precedent for viewing such

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[109] *See* United States v. General Electric Co., 272 U.S. 476, 493 (1926) ("[P]rice fixing is usually the essence of that which secures proper reward to the patentee.").

[110] *See, e.g.*, David R. Macdonald, *Know-How Licensing and the Antitrust Laws*, 62 MICH. L. REV. 351, 363 (1964) (arguing that "reliance upon *Dr. Miles* or *General Electric* seems ill-advised, even with respect to patent licenses," and more so with respect to "know-how").

[111] *See* IP Guidelines, *supra* note 1, § 5.2 & n.34.

[112] Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007).

[113] *See id.* at 907.

cases as horizontal,[114] but whether the courts will do so in a trade secret licensing case is hard to predict.

The second question is how to do the rule of reason analysis. *Leegin* gives precious little guidance, even with respect to its own situation, that is, the distribution of branded goods where the seller has no apparent market power and the product is subject to interbrand competition (Leegin made handbags and belts, presumably selling them in competitive markets.[115]) In the trade secrets context, however, the facts may be quite different. Depending on the quality of the trade secret, TS may have sufficient market power to price above the competitive level. Arguably, this could shift the burden to TS to show a plausible efficiency justification for the price restraint, ultimately requiring the court to balance this justification against the anticompetitive effect of the higher selling prices. Again, it remains to be seen whether this will be the result after *Leegin*.

2. Territorial and Use Restraints

Although the per se illegality of territorial restraints, whether horizontal or vertical, has a somewhat checkered antitrust history,[116] courts in trade secrets cases have applied a rule of reason analysis and have almost always upheld the restraints. This result is consistent with *Fowle* and the dictum *in Dr. Miles* approving such restrictions.[117]

Two cases well illustrate the courts' approach. One involved a 1934 agreement between an English company that owned "certain secret processes, recipes and formulae" for making

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[114] *See* United States v. Gen. Motors Corp., 384 U.S. 127 (1966) (finding a price agreement between General Motors and three associations of GM automobile dealers to be per se unlawful).

[115] *See Leegin*, 551 U.S. at 882, 883 (discussing the relevant market).

[116] *Compare* White Motor Co. v. United States, 372 U.S. 253, 261 (1963) (holding that vertical territorial restrictions are not per se violations of the Sherman Act), *with* United States v. Arnold, Schwinn & Co., 388 U.S. 365, 379 (1967) (holding that it is "unreasonable without more for a manufacturer to seek to restrict and confine areas or persons with whom an article may be traded after the manufacturer has parted with dominion over it"), *with* Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 58 (1977) (overruling *Schwinn* and returning to the *White Motor* approach of applying the rule of reason to vertical non-price restraints). *See also* United States v. Topco Assocs., Inc., 405 U.S. 596 (1972) (holding that a territorial sales restriction imposed by a cooperative association of supermarket chains was a per se unlawful horizontal restraint).

[117] *See supra* text accompanying notes 59-67, 97-99.

flux (no patents were involved) and a U.S. company to which it gave the exclusive license to manufacture and sell the fluxes in the U.S. and Canada.[118] The English company agreed not to sell in the U.S. and Canada, and the U.S. company agreed not to export to any other countries.[119] Seventeen years later the U.S. company sold $4.00 worth of flux to a buyer in Mexico. The English company declared the U.S. company in breach of the agreement and began making flux in the United States.[120] When the U.S. company sued to enforce the territorial restriction, the English company defended by arguing that the parties had entered into "an 'international cartel agreement' which violates our [U.S.] antitrust laws by dividing the world's markets."[121]

Not surprisingly, the court was unimpressed with the English company's change of heart. Echoing *Vickery v. Welch*, the court wrote that the English company "could make disclosures or not; sell or not; as it pleased and the public had no legal interest whatever in that choice."[122] The court also pointed out that this was a single contract, the two firms were not competitors at the time, there was no price agreement, and that although the fluxes "are no doubt good and valuable," they were not "the only ones available or in use in the manufacture of metal castings."[123] The court concluded that the license restraint was "only ancillary to a valid primary purpose" and was not "unreasonable."[124]

The second case tells a more complicated industrial story, this time involving the monopolization of cellophane.[125] Cellophane was first produced commercially in France in 1917 by La Cellophane S.A. DuPont, which produced synthetic fabrics, heard of La Cellophane's success and entered the business. La Cellophane, however, had a distinct competitive advantage because of the "secret, novel" process for manufacturing cellophane that it had developed through operational

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[118] *See* Foundry Servs., Inc. v. Beneflux Corp., 110 F. Supp. 857, 857–858 (S.D.N.Y. 1953).

[119] *See id.* at 858.

[120] *See id.*

[121] *Id*. at 860.

[122] *Id.*

[123] *Id.*

[124] *See id*. at 860–61.

[125] *See* United States v. E.I. Du Pont de Nemours & Co., 118 F. Supp. 41 (D. Del. 1953), *aff'd*, 351 U.S. 377 (1956).

experimentation.[126] In 1923 DuPont and La Cellophane formed the DuPont Cellophane Company, and La Cellophane granted DuPont Cellophane the exclusive right to make and sell cellophane in North and Central America under La Cellophane's secret processes; La Cellophane was given the rest of the world.[127] It was estimated at the time that it would have taken DuPont several years to develop a competitive production technique.[128]

In 1947 the Justice Department brought suit against DuPont for monopolizing the cellophane market. One of the Department's arguments was that DuPont had acquired its monopoly illegally by engaging in a per se unlawful division of world markets, effected through the creation of DuPont Cellophane and the licensing of La Cellophane's trade secrets.[129] The district court disagreed with the Department's view of the agreements. Stressing DuPont's weak competitive position when the deal was struck, the high value of the trade secrets that La Cellophane licensed, and the riskiness of the cellophane venture even with La Cellophane's help, the court held the agreements lawful.[130] Citing both *Fowle* and *Dr. Miles*, the court wrote: "Among the ancillary restraints which are considered reasonable, both under common law and the Sherman Act, are those which limit territory in which the contracting parties may use the trade secret."[131]

The Justice Department's litigating posture in *DuPont*, however, led the district court away from some difficult issues. For one, the court was not asked to do a full rule of reason analysis because the Department presented the trade secret licensing as a per se violation. The court's rule of reason analysis is thus more like the rough balancing done in the earlier common law cases, taking account of the economic benefits of the agreement to the parties and the utility of La Cellophane's innovations but not

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[126] *See* 118 F. Supp. at 218.

[127] *See id.* at 57–58.

[128] The district court and the Supreme Court did not quite agree on just how long it would have taken DuPont. *Compare* 118 F. Supp. at 59 ("Evidence shows DuPont could not have developed a successful process for cellophane manufacture in less than five to eight years and then only at very substantial cost.") *with* 351 U.S. at 382 n.4 ("It was estimated that in 1923 it would have taken four or five years of experimentation by a new producer of cellophane to attain this production technique.").

[129] *See* 118 F. Supp. at 218–220.

[130] *See id.* at 220.

[131] *Id*. at 219. The Justice Department did not appeal the court's ruling on this point. *See* 351 U.S. at 379.

focusing on the consumer welfare loss from the territorial allocations, nor on the question whether the incentives for innovation would have been equally well served by a more limited agreement. For another, the Department's argument focused on the legality of the agreements when made in 1923, rather than on the question whether the agreements had an unreasonable effect on competition in 1947, when suit was brought. Had the case been framed differently, the court would have been required to consider whether trade secret territorial restraints—unlike patent territorial restraints—can be of unlimited duration.

An opportunity to advance the analysis on these two issues was presented in 1994 when the Justice Department brought suit against Pilkington, an English company.[132] In the late 1950s Pilkington developed a new commercially successful method for producing flat glass, called the float process. In 1962 Pilkington entered into patent and know-how licensing agreements with all its principal glass making competitors (which were still producing flat glass through other methods).[133] The licensees were permitted to use the patents and know-how only in a specified country or countries; they could not export their glass, build new plants outside their assigned territories, or sublicense the technology.[134] By the time the Department brought suit, Pilkington's principal patents had expired and all royalty obligations had been concluded. Yet Pilkington continued to enforce the territorial restrictions regarding its know-how, unless the licensee could prove that all the float glass technology it was using had become public.[135] A "substantial part" had, but not all.[136]

The Justice Department alleged that Pilkington's agreements had created a worldwide cartel preventing U.S. firms not only from exporting flat glass, but also from exporting their services in building float glass plants in foreign countries, where there was strong demand for new plants.[137] These territorial restraints, the Department alleged, were not justified by any intellectual property rights "of substantial value," given the

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[132] Complaint, United States v. Pilkington PLC, Civ. A. No. CV 94-345 (D. Ariz. May 25, 1994), *available at* http://www.usdoj.gov/atr/cases/f0000/0014.pdf.

[133] *See id.* at 8.

[134] *See id.* at 8–9.

[135] *See id.* at 10.

[136] *Id.* at 11.

[137] *See id.*

expiration of the patents and the disclosure of much of the technology.[138] Because Pilkington had no intellectual property rights of substantial value, the restraints were "neither ancillary nor reasonably necessary" to any legitimate transaction and were, therefore, "unreasonable restraints of trade."[139]

The Justice Department settled its suit against Pilkington with a consent order, so the Department's legal theory was never tested in court. Nevertheless, the case is a good example of government enforcers paying closer attention to the actual economic value of the apparently secret technology involved and, implicitly, taking account of the change in circumstances from when the original license agreements were entered into. A trade secret license, even if permissible under the antitrust laws when made, can become unreasonable over time, preventing competition among the licensees and with the licensor, and lasting longer than is necessary to provide incentives for innovation.

3. Tying

There is a long history of litigation over tying the sale of intellectual property right-protected products to the sale of products that are not protected. The issue arose first in the patent area, leading Congress to pass Section 3 of the Clayton Act in 1914, condemning the practice.[140] Over time the Supreme Court came to hold that ties involving patents were per se violations of

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[138] *See id*. at 10.

[139] *See* Competitive Impact Statement at 10, United States v. Pilkington PLC, Civ. A. No. CV 94-345 (D. Ariz. May 25, 1994),, *available at* http://www.usdoj.gov/atr/cases/f220800/220861.pdf. For other cases where courts have weighed the value of the licensed information, although at the date when the license agreements were made, *see* United States v. Timken Roller Bearing Co., 83 F. Supp. 284, 313 (N.D. Ohio 1949) (holding that the defendant's know-how was not a "secret process," but consisted of "designs, data showing how defendant manufactured its product, the advice of defendant's employees and help of like nature"), *aff'd*, 341 U.S. 593 (1951); United States v. Imperial Chemical Indus., 100 F. Supp. 504, 592 (S.D.N.Y. 1951) (finding that the defendants' license agreements served to accomplish a "world-wide allocation of markets"); United States v. General Electric Co., 82 F. Supp. 753, 846 (D.N.J. 1949) (no clear evidence what the trade secrets were). *See also* A. & E. Plastik Pak Co. v. Monsanto Co., 396 F.2d 710, 715 (9th Cir. 1968) (characterizing the trade secret agreements in these cases as "subterfuges" for market division and price fixing).

[140] Clayton Antitrust Act, 15 U.S.C. § 14 (2006). The Court had originally approved the practice as a matter of patent law, *see* Henry v. A.B. Dick Co., 224 U.S. 1, 17–19 (1912), but reversed its view after the passage of Section 3. *See* Motion Picture Patents Co. v. Universal Film Mfg. Co., 243 U.S. 502, 516–17 (1917) (overruling *A.B. Dick*).

Section 1 of the Sherman Act, an approach subsequently extended to copyrights.[141] Commentators later pointed out, however, that although patents and copyrights give their owners certain rights to exclude others from using an invention or copying a work, these legal rights did not necessarily confer economic power (or "market power") on the seller.[142] In the 1995 Intellectual Property Guidelines, the federal enforcement agencies accepted this critique and disavowed the view that intellectual property rights, in themselves, conferred market power.[143] In 2006, in *Illinois Tool Works v. Independent Ink*,[144] the Supreme Court agreed as well, overruling its prior case law and holding that market power in a tying case could not be presumed merely from the fact that the tying product was protected by a patent.[145]

Trade secrets did not go through the same legal development as patents and copyrights. In fact, the courts have specifically rejected the argument that trade secrets should be treated like other intellectual property rights in tying cases.[146] Given the variability of the quality of the information that can be protected by trade secrets, as well as the permissibility of lawful discovery through reverse engineering, a non-presumption approach to trade secret ties made good sense even when patent and copyright ties were per se unlawful. It is certainly correct

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[141] *See* United States v. Loew's, Inc., 371 U.S. 38, 49 (1962) (holding that tying arrangements, of both patented and copyrighted products, "both by their inherent nature and by their effect injuriously restrained trade") (internal citations omitted).

[142] See, *e.g.,* 10 PHILIP AREEDA, HERBERT HOVENKAMP, & EINER ELHAUGE, ANTITRUST LAW ¶ 1737a (2d ed. 2004) ("[T]here is no economic basis for inferring any amount of market power from the mere fact that the defendant holds a valid patent"); WILLIAM LANDES & RICHARD POSNER, THE ECONOMIC STRUCTURE OF INTELLECTUAL PROPERTY LAW 374 (2003); Kenneth J. Burchfiel, *Patent Misuse and Antitrust Reform: "Blessed be the Tie?"*, 4 Harv. J.L. & Tech. 1, 57 & n.340 (1991) (noting that the existence of a market power presumption had been extensively criticized); 1 HOVENKAMP, JANIS, & LEMLEY, *supra* note 2, § 4.2a ("[C]overage of one's product with an intellectual property right does not confer a monopoly").

[143] *See* IP Guidelines, *supra* note 1, § 2.2. The agencies included trade secrets as well as patents and copyrights. *See id.*

[144] Illinois Tool Works, Inc. v. Independent Ink, Inc., 547 U.S. 28 (2007).

[145] *See id.* at 33–43 (canvassing legal history and commentators' critiques).

[146] *See, e.g.*, In re Data General Corp. Antitrust Litigation, 490 F. Supp. 1089, 1113–1114 (N.D. Cal. 1980), ("Unlike the copyright issue, it has never been held that trade secrets protection is sufficient to create a presumption of economic power."), *rv'sd on other grounds*, Digidyne Corp. v. Data General Corp., 734 F.2d 1336 (9th Cir. 1984).

today, when patent and copyright ties are not considered per se unlawful.

This does not mean that ties involving trade secrets are per se lawful under Section 1. Unlike trade secret licensing restrictions on price or territory, tying arrangements involving products produced under trade secrecy do not come freighted with the ancillary restraints doctrine—there is nothing to which the tying arrangement is "ancillary." Rather, the questions they raise would be those involved in any tying analysis: (1) does the seller's trade secret confer market power; (2) what are the anticompetitive effects of the tying sale; and (3) are there any efficiency justifications for the tie.

It is certainly possible that a trade secret could be sufficiently strong to confer market power on its possessor. Indeed, trade secret litigation abounds with allegations of the novelty and essentiality of the trade secret that its possessor is trying to protect. In previous tying litigation, where products have often been protected by other intellectual property rights as well as by trade secrets, legal doctrine led the parties away from focusing on the economic advantages conferred by trade secrets as opposed to patent or copyright protection.[147] Post-*Illinois Tool*, however, this may change, leading litigants to examine more carefully the quality of the trade secrets a seller claims.

C. Current Law: Monopolization

1. Refusal to Supply

A critical assumption in the trade secrets restraint of trade cases, whether at common law or under Section 1 of the Sherman Act, has been that the holder of the trade secret can always keep the secret to itself rather than disclose it to others, whether to a partner or to an employee. Because the trade secret holder had this

[147] In *Digidyne*, for example, the software plaintiffs argued that the defendant's copyright and trade secret protection in its software, when combined, should give rise to a presumption of market power; the court of appeals held for the plaintiffs on the ground that the copyright in the software could be presumed to confer market power to impose the tie. *See* 734 F.2d at 1344. One of the plaintiffs, however, was a hardware maker that argued that Data General's CPU was protected through trade secrecy. The district court had found that the plaintiff made "an impressive factual showing that Data General actually possesses economic power by virtue of its trade secrets," relying, in part, on Data General's president's statement doubting that anyone could design a Data General "emulator" without infringing on Data General's trade secrets. *See Data General*, 490 F. Supp. at 1115.

option, the law could be indifferent as to which option the holder chose, or what restrictions the holder, as licensor, put on the licensee to whom it disclosed. The public is in the same position whether the secret is kept by the secret's originator or kept, with restrictions, by the secret's licensee.

Does this argument change if a monopolist controls the trade secret? Courts have often pointed out that a monopolist, "as a general matter," can "'freely . . . exercise his own independent discretion as to parties with whom he will deal."[148] There can be exceptions, of course, but, as the Court notes in *Trinko*, the courts have been "very cautious in recognizing such exceptions,"[149] something which has been true without regard to whether the monopolist's product is protected by an intellectual property right or not. The reason for this caution, *Trinko* points out, is the "uncertain virtue" of forced sharing and the difficulty courts can have in "identifying and remedying" the monopolizing conduct.[150]

The trade secrets case that best illustrates this cautious approach is *Berkey Photo, Inc. v. Eastman Kodak, Inc.*,[151] a private treble-damages action involving Kodak's introduction of a new small camera and film. Kodak had a monopoly position in the camera and film markets; Berkey was a competitor in the camera market.[152] Camera makers' abilities to innovate were limited by the fact that they could not introduce a new camera unless there were film that fit. This left Kodak free to design new cameras with new film formats at its own pace. Indeed, competitors like Berkey could not even begin to design a competing new camera until they knew the size of the new film's cartridge and its format.[153]

Less than two months before Kodak introduced the new small camera and film that led to the litigation, it provided Berkey, at a charge of $60,000, eleven pages of specifications and notes relating to the new film format.[154] These disclosures, however, were inadequate to allow Berkey to be present "at the starting line"

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[148] *See* Verizon Comm'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 408 (2004)(quoting United States v. Colgate & Co., 250 U.S. 300, 307 (1919) (internal quotations omitted)).

[149] *See id.*

[150] *See id.*

[151] 603 F.2d 263 (2d Cir. 1979).

[152] *See id.* at 267.

[153] *See id.* at 279–84.

[154] *See id.* at 280–81.

when Kodak introduced its new camera, so Berkey sued for the profits it lost over the 18 months it took to catch up.[155]

The court of appeals rejected, as a matter of law, Berkey's claim that Kodak's failure timely to disclose the specifications was monopolizing conduct in violation of Section 2.[156] Although technically Kodak did not claim legally protectable trade secrets in this information, there was little doubt that Kodak had kept this information confidential, and the court treated it as such. Relying on an earlier Supreme Court trade secrets case,[157] the court pointed out that "a firm may normally keep its innovations secret from its rivals as long as it wishes."[158] Were the rule otherwise, the incentives to innovate would be lessened: "The first firm, even a monopolist, . . . has a right to the lead time that follows from its success."[159] Further, a liability rule for failure to pre-disclose secret information would be difficult to apply and enforce. How would a monopoly firm or a court figure out how detailed the information must be, and when would the information be sufficiently "'ripe' for disclosure?" These uncertainties, the court felt, would have "an inevitable chilling effect on innovation."[160]

The court thus appeared to shut the door on a monopolization claim for a refusal to supply confidential information prior to a product's introduction. Nevertheless, one should be cautious in taking the position that all failures to predisclose confidential information are per se lawful. For example, in 1998 the Federal Trade Commission issued a complaint against Intel for changing its policy of sharing pre-release technical information with three customers that designed and sold products using Intel chips.[161] Intel did so in apparent retaliation for patent infringement suits that the customers had filed against either Intel or Intel's customers, which alleged that Intel technology was infringing patents on their microprocessor technology.[162] The FTC alleged that because most firms that

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[155] *See id.* at 281.

[156] *See id.*

[157] *See* Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470 (1974).

[158] 603 F.2d at 281.

[159] *Id.* at 283.

[160] *Id.* at 282.

[161] *See* Complaint, In the Matter of Intel Corp., No. 9288 (Fed. Trade Comm'n June 8, 1998), *available at* http://www.ftc.gov/os/1998/06/intelfin.cmp.htm.

[162] *See id.* ¶¶ 13, 18.

develop microprocessor-related technologies were "dependent on Intel" and "vulnerable to retaliation," Intel's conduct could diminish incentives those firms had to innovate in the microprocessor market that Intel monopolized.[163] The FTC settled the case shortly before trial, so its theories were never tested in court. Nevertheless, the fact-pattern is a reminder of how trade secret information may be used strategically to maintain monopoly power.[164]

The most significant decision requiring a monopolist to disclose trade secret information, however, comes not from a U.S. court, but from Europe. At issue was a request that Sun Microsystems made to Microsoft in 1998 to provide it with "the complete information" that would allow Sun's server operating systems to be fully interoperable with networks of servers and PCs running Microsoft's Windows operating system.[165] When Microsoft refused, Sun petitioned the European Commission to initiate proceedings against Microsoft for abuse of dominant position in violation of Article 82 of the EC Treaty (the rough analogue to Section 2 of the Sherman Act). As the Commission subsequently pointed out, Sun's request for interoperability information, to be implemented in Sun's products, might reveal "innovations that are currently not disclosed" and which are "protected by trade secrecy."[166] Indeed, Microsoft pointed out that although some of the requested information was protected by patent, and therefore publicly disclosed, the communications

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[163] *See id.* ¶¶ 14, 39.

[164] *See FTC Staff, Intel Withdraw Case from ALJ In Anticipation of Reaching Settlement*, 76 Antitrust & Trade Reg. Rep. (BNA) 237 (March 11, 1999) (describing arguments made in the parties' pretrial briefs before an FTC Administrative Law Judge). The settlement order is available at http://www.ftc.gov/os/1999/08/intel.do.htm. Intergraph's related antitrust suit was ultimately unsuccessful because it did not allege that the refusal to supply the information harmed competition in any market in which it and Intel competed. See Intergraph Corp. v. Intel Corp., 195 F.3d 1346, 1357 (Fed. Cir. 1999). Nevertheless, the Federal Circuit's opinion showed great skepticism toward Intergraph's argument that failure to disclose the information violated Section 2. *See id.* at 1357–58 ("The notion that withholding of technical information and samples of pre-release chips violates the Sherman Act, based on essential facility jurisprudence, is an unwarranted extension of precedent and can not be supported on the premises presented.").

[165] *See* Case COMP/C-3/37.792—Microsoft Corp., Comm'n Decision, 2007 O.J. (L 32) 23, ¶ 185 (Mar. 24, 2004), *available at* http://ec.europa.eu/competition/antitrust/cases/decisions/37792/en.pdf.

[166] *Id.* ¶ 190.

protocols that Sun sought for interoperability "remain highly proprietary and confidential."[167]

In 2004 the Commission determined that Microsoft's refusal to supply the requested information violated Article 82.[168] The Commission concluded that Microsoft had followed a "leveraging strategy" to extend its dominant position in the PC operating systems market into the adjacent work group server operating system market.[169] By withholding interoperability information, Microsoft had deprived competitors in the work group server operating systems market of information that was "indispensable" for viable competition, thereby allowing the company to exploit "a range of privileged connections" between its Windows operating system and its work group server operating system.[170]

The Commission never decided, however, whether Microsoft's proprietary information actually qualified as protected trade secrets, or whether Microsoft actually had the patent and copyright protection it claimed, because Microsoft never made the relevant specifications available for review.[171] Rather, the Commission assumed the information was protected in some way, but concluded that these protections were not, in themselves, sufficient justification for failing to supply the requested information, in light of the competitors' need for the information and the positive effect that supplying the information would have on their incentives to innovate.

On review, the European Court of First Instance upheld the Commission's decision, agreeing that the refusal to supply the requested information was likely to eliminate effective competition in the work group server operating system market.[172] In its argument before the Court, the Commission raised the possibility that trade secrets should be treated differently—and less favorably—than either patents or copyrights in terms of any

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[167] *Id.* ¶ 190 n.249.

[168] *Id.* ¶ 784.

[169] *Id.* ¶ 1063.

[170] *See id.* ¶¶ 1063–65.

[171] *See id.* ¶190.

[172] *See* Case T-201/04, Microsoft Corp. v. Comm'n, 2007 E.C.R. II-3601 ¶ 620 (Ct. First Instance), *available at* http://curia.europa.eu/jurisp/cgi-bin/gettext.pl?lang=en&num=79929082T19040201&doc=T&ouvert=T&seance=ARRET [hereinafter CFI *Microsoft* Decision].

"presumption of legitimacy" of a refusal to supply, because "the protection that such secrets enjoy under national law is normally more limited than that given to copyright or patents."[173] The Commission also argued, however, that there was no need to decide this issue, and the Court agreed.[174] The Court noted that the Commission's decision had assumed the legal validity of Microsoft's patent, copyright, and trade secret claims and then judged Microsoft's behavior under the test which was "most favorable" to Microsoft.[175] Similarly, the Court decided to treat trade secrets as "equivalent" to the other intellectual property rights, finding no need to treat them any less favorably.[176]

The Court also considered Microsoft's argument that forced disclosure of its protected interoperability information would diminish its incentives to innovate. The Court determined that once the Commission had proved the adverse competitive impact of the failure to disclose, Microsoft then had the burden of showing how its incentives to innovate would be adversely affected. The Court wrote that Microsoft had not carried its burden, instead merely putting forward "vague, general and theoretical arguments."[177] The Commission, by contrast, had examined the widespread industry practice of commonly disclosing interoperability information and had pointed out that Microsoft's fear that Sun, or other competitors, might simply copy ("clone") its products was exaggerated.[178]

The decision in the European *Microsoft* case has been highly controversial and was much criticized by U.S. Justice Department officials at the time, who took the view that a refusal to license intellectual property should never be a violation of Section 2 of the Sherman Act.[179] This view, however, did not

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[173] *Id.* ¶ 280.

[174] *See id.* ¶ 283.

[175] *See id.* ¶¶ 284, 289, 313.

[176] *See id.* ¶ 289.

[177] *Id.* ¶ 698.

[178] *See id.* ¶ 710.

[179] *See* Harry First, *Netscape is Dead: Remedy Lessons From the* Microsoft *Litigation* 20–21 (NYU Law and Economics Research Paper No. 08-49, 2008) *available at* http://ssrn.com/abstract=1260803 (describing the U.S. Department of Justice's immediately critical reaction to the European judgment); Bo Vesterdorf, *Article 82 EC: Where Do We Stand after the* Microsoft *Judgment?*, 1 ICC GLOBAL ANTITRUST REV. 1, 14 (2008) (arguing that the CFI's judgment "may have what some might call negative consequences for holders of IPRs, which perhaps might deter investments that otherwise would be made and in

differentiate among the different types of intellectual property protection, and it was articulated in the context of a broader policy view that unilateral refusals to deal in general should not be found to violate Section 2.[180] In 2009, moreover, the Obama administration Justice Department withdrew the Report embodying this general policy view, bringing into question how current enforcement officials would evaluate refusals to license intellectual property rights by monopoly firms like Microsoft.[181]

2. Bad Faith Litigation

A familiar problem in antitrust law is the alleged bad faith assertion of an intellectual property right as part of an effort to exclude competitors. If the intellectual property right holder has sufficient market power, such efforts can give rise to a violation of Section 2, either as monopolization or attempted monopolization. Most of these cases involve patents, but some have involved trade secrets.

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turn have negative consequences for competition") (author was President of the CFI and participated in the court's *Microsoft* decision), *available at* http://www.icc.qmul.ac.uk/GAR/GAR2008/Vesterdorf.pdf. *See also* Promoting Innovation, *supra* note 1, at 32 ("The Agencies also conclude that antitrust liability for mere unilateral, unconditional refusals to license patents will not play a meaningful part in the interface between patent rights and antitrust protections."); Gerald F. Masoudi, Deputy Assistant Att'y Gen., U.S. Dep't of Justice, Intellectual Property and Competition: Four Principles for Encouraging Innovation 5, Address Before the Digital Americas 2006 Meeting (April 11, 2006), *available at* http://www.usdoj.gov/atr/public/speeches/215645.pdf (arguing that although "outside the intellectual property realm" parties are sometimes liable for refusing to deal with others, that does not mean that "there must also be some circumstance in which the unilateral, unconditional refusal to license a patent must constitute an antitrust violation," and suggesting that liability for such a refusal to license "has not found support in U.S. legal decisions").

[180] *See* U.S. DEP'T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT 127 (2008), *available at* http://www.usdoj.gov/atr/public/reports/236681.pdf [Hereinafter Section 2 Report] ("The Department thus concludes that antitrust liability for unilateral, unconditional refusals to deal with competitors should not play a meaningful part in Section 2 enforcement.").

[181] For the statement withdrawing the Report, see Christine Varney, Assistant Att'y Gen,. U.S. Dep't of Justice, Vigorous Antitrust Enforcement in this Challenging Era, Remarks as Prepared for the Center for American Progress (May 11, 2009), *available at* http://www.usdoj.gov/atr/public/speeches/245711.pdf.

The leading trade secrets case is *CVD v. Raytheon*.[182] Raytheon manufactured two chemical-based materials that were the only ones suitable for certain government defense uses, such as windows on missiles and jet aircraft. Raytheon manufactured these materials under the "cvd process," which no other firm in the world used.[183] In 1979 an engineer who had worked at Raytheon for twenty years told Raytheon that he was leaving to form a competing company to manufacture the materials using the cvd process. Raytheon told him that he could not do so without infringing Raytheon's trade secrets.[184] Their dispute eventually became a Section 2 case in which the plaintiff-competitor showed both the invalidity of the trade secrets claim and Raytheon's bad faith in asserting it. For the former, the plaintiff proved the extent to which Raytheon had made details of the cvd process public (including reports to the federal government and papers published in scientific journals). To show bad faith, plaintiff proved that Raytheon had never followed any of its usual internal procedures for demarcating trade secret-protected matters.[185]

The court of appeals upheld the jury's verdict for the plaintiff-competitor, finding that "[t]he assertion of trade secret claims in bad faith . . . is a predatory practice" that can violate Section 2 of the Sherman Act, so long as the plaintiff can show monopoly power or an attempt to monopolize.[186] The court analogized the case to antitrust liability for bad faith patent infringement suits. The court pointed out that the rationale behind both types of legal protection is similar—"to encourage invention"—even while recognizing that the "cornerstone" of trade secret protection is secrecy and the scope of rights is narrower, affording no protection against independent development.[187] Perhaps because trade secret law allows more room for independent competition, the court allowed the plaintiff's suit even though the defendant had only threatened trade secret litigation but had never actually brought it.[188]

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[182] CVD, Inc. v. Raytheon Co., 769 F.2d. 842 (1st Cir. 1985).

[183] *See id.* at 847–48.

[184] *See id.* at 848.

[185] *See id.*

[186] *Id.* at 855.

[187] *See id.* at 850.

[188] *See id.* at 848. This was in contrast to the case law at the time on bad faith patent litigation, which required an infringement suit to have been brought. *See id*. at 851. Subsequent cases have been more liberal, allowing a Sherman Act claim where there is a reasonable expectation that an infringement suit would be filed. *See* Hydril Co. LP v. Grant Prideco LP, 474 F.3d 1344, 1350

Raytheon is somewhat unusual in that it does not involve patents at all. Other cases involve the more familiar combination of patents and trade secrets to protect technology. For example, in *A. & E. Plastik Pak v. Monsanto*,[189] the plaintiff alleged that Monsanto acted in bad faith when it claimed trade secret protection for a manufacturing process after its patent expired, in an effort to stop the plaintiff from manufacturing a competing product (with the assistance of a former Monsanto engineer).[190] Similarly, in *International Technologies Consultants, Inc. v Pilkington PLC*,[191] a private suit involving the technology for making float glass, the plaintiff alleged a multi-year effort to exclude it from the market for designing float glass plants by filing numerous lawsuits baselessly asserting trade secret protection for the float glass technology after the relevant patents had expired.[192]

The court of appeals in *Pilkington* was appropriately appalled at the effort to use a bogus trade secrets claim to protect technology that should have been in the public domain:

> Alistair Pilkington invented an ingenious new method of making high quality flat glass at high speed, much less expensively than by grinding and polishing it, in the 1950's. He thereby made a great contribution to cheap, good plate glass for everyone. There was no way to exploit his invention while keeping it a close secret, as with the formula for Coca-Cola, because the weight and fragility of glass required that the method be used in factories around the world. The patent enabled the Pilkington company to take

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(Fed. Cir. 2007). *Cf.* Christopher R. Leslie, *The Anticompetitive Effects of Unenforced Invalid Patents*, 91 MINN. L. REV. 101, 125–26 (2006) ("No actual enforcement, or even a direct threat of litigation, is required to create anticompetitive effects.").

[189] A. & E. Plastik Pak Co., Inc. v. Monsanto Co., 396 F.2d 710 (9th Cir. 1968).

[190] The court, in dictum, indicated that such conduct could be a violation of the antitrust laws. *See id.* at 715.

[191] 137 F.3d 1382 (9th Cir. 1998).

[192] *See id.* at 1388. ITC's allegations involve conduct similar to that alleged in the Justice Department's 1994 complaint, see *supra* text accompanying notes 132-139. Although ITC's complaint was filed in 1993 in the same district court as the Justice Department's, there is no mention of ITC's allegations in either the Department's complaint or settlement.

> exclusive benefit of the idea for a limited period of time, even though numerous other people necessarily knew the method almost immediately. * * * We do not know whether [the defendants] have conspired to prevent others from using the ideas in Pilkington's expired patents, in violation of the antitrust laws, by means of unjustified litigation and threats of litigation. But if they have, as the complaint alleges, then the world is being deprived of the economic value of Alistair Pilkington's great invention. Indeed, in poorer areas of the world, doubtless people lack windows to let in the sun and keep out the rain, wind, cold, and insects, because of improper exploitation of monopoly pricing.[193]

IV. An Analytical Framework for Antitrust and Trade Secrets

A. General Principles

I would like to suggest three general principles for analyzing antitrust cases involving trade secrets. First, trade secrets should not be treated as the equivalent of other intellectual property rights. This means that there should be no presumption that the restrictions that trade secret holders impose are welfare-enhancing and therefore procompetitive. Second, antitrust economic analysis of trade secrets should take account of their essential legal properties—trade secrets are not necessarily innovative, and their legal protection can last far longer than might be necessary to incentivize their production, but this legal protection will be lost once the secret is out. Third, in assessing the competitive effects of protecting trade secrets, trade secret holders should get the benefits of their bargain but no more—a time-unlimited right to appropriate the value of whatever can be kept secret, but no right to monopoly profits and no right to restrict others from independent discovery.

1. Trade Secret Distinctiveness: No Deference, No Presumptions

It is fair to say that the current approach to applying antitrust law where intellectual property rights are involved has been one of deference. That is, courts and enforcers have generally been willing to defer to the decisions that intellectual

[193] *Id.* at 1392–93.

property rights holders have made when attempting to maximize the rents they can get from their inventions or writings. This policy of deference is rooted in a simple Schumpeterian view of the incentives for innovation—monopoly profits are "the baits that lure capital on to untried trails."[194] Antitrust enforcers and courts should therefore be quite careful in restricting the profits that intellectual property owners can obtain, lest they diminish the incentives for innovation.

Courts have recognized that trade secret protection also serves the goal of incentivizing innovation.[195] Particularly when it comes to manufacturing processes, the ability to maintain proprietary control over information allows innovators to get returns from their efforts. Courts recognize that getting an invention—even a patentable one—from idea to production is a complex process. Experimentation is necessary and it is often difficult to reduce every aspect of production to writing. This is the lesson of chocolate making, gunny cloth manufacture, and cellophane, to take just a few examples from the case law discussed above.

The courts have also recognized another important purpose of trade secret protection, the preservation of confidential relationships. Much of trade secret law is shaped in the context of faithless agents or partners. The law's desire to protect these relationships may have many roots, whether located in notions of "commercial ethics and fair dealing,"[196] or an instinct about the importance of maintaining social networks of trust for organizing enterprises efficiently, or a realization that innovation may require the enforcement of legal norms relating to the sharing of information.[197]

Although these ideas have often led the courts to defer to trade secret claims, there are some cases that take what I will call a neutrality approach toward trade secrecy. In these cases, courts

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[194] JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM, AND DEMOCRACY 90 (3d ed. 1950).

[195] *See* Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470, 471 (1974) (noting that "trade secret law will encourage invention and prompt the innovator to proceed with the discovery and exploitation of his invention, and to license others to exploit secret processes").

[196] *See* CVD, Inc. v. Raytheon Co., 769 F.2d 842, 850 (1st Cir. 1985).

[197] *See* Katherine J. Strandburg, *Norms and the Sharing of Research Materials and Tacit Knowledge*, *in* WORKING WITHIN THE BOUNDARIES OF INTELLECTUAL PROPERTY 85–110 (Rochelle C. Dreyfuss, Harry First & Diane L. Zimmerman eds. 2010).

have not assumed that trade secret holders should be permitted to maximize their returns like other intellectual property rights holders. Rather, these courts have paid attention to three key inter-related differences between trade secrets and other forms of intellectual property protection, particularly patents: 1) duration; 2) absence of a federal right; and 3) lack of a disclosure bargain.

1) Duration: Patents have a fixed term (now twenty years); trade secrets have no fixed term.[198] A policy of deference to patents thus has some natural limitation—at some time the protection will run out. A policy of deference to trade secrets is not limited in this way. Protection runs out when the secret is out, something that clever reverse engineering can help along. Courts have paid most attention to the length of protection in those cases when trade secrets are being used to avoid the patent's fixed term.[199]

2) Absence of a federal statutory right: Beginning with Judge Lurton's opinion in *Hartman*, courts have seen a distinction between the "monopoly" given by federal patent law and the lesser protection afforded under state trade secret law.[200] Although the courts have put this argument in somewhat formal legalistic terms, a better way of looking at it is that federal patent law is intended to provide the patent holder with the profits that are "reasonably within the reward" of the patent grant, that is, the profits from whatever monopoly power the patent allows the patentee to exercise.[201] There is no such maximizing policy in trade secret law. Rather, the policy is to protect the secret from being misappropriated by others, in part to advance the law's interest in

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[198] Copyrights are now effectively unlimited in duration. *See* Eldred v. Ashcroft, 537 U.S. 186, 208 (2003) (approving Congress' extension of copyright protection until 70 years after the author's death through the Sonny Bono Copyright Term Extension Act, Pub. L. No. 105-298, 11 Stat. 2827 (1998)).

[199] *See, e.g.*, Christianson v. Colt Indus. Operating Corp., 486 U.S. 800, 805–06 (1988) (rejecting a defendant's trade secret claim that was filed only after an expired patent was found to be invalid). *But see* Aronson v. Quick Point Pencil Co., 440 US 257 (1979) (holding that a contract to pay royalties for the defendant's product, signed alongside an application to patent the product, should be enforced even when the patent application is denied and the defendant's trade secrets become public in the process).

[200] *See* John D. Park & Sons Co. v. Hartman, 153 F. 24, 32–33 (6th Cir. 1907). The federal Economic Espionage Act, 18 U.S.C. §§ 1831–39, makes it a crime to steal or misappropriate a trade secret, but provides no private rights for the trade secret holder and is not directed at providing incentives for innovation. *See* ROGER MILGRIM, MILGRIM ON TRADE SECRETS § 12.6(3) (discussing the exclusively criminal provisions of the Act).

[201] United States v. Gen. Elec. Co., 272 U.S. 476, 489 (1926).

protecting fiduciary relationships and in part to advance innovation. The goal is not necessarily to maximize the return the secret's holder can get.

3) Lack of a disclosure bargain: Beginning with the Supreme Court's 1911 decision in *Dr. Miles*, courts have paid attention to the fundamentally different bargain that is struck under the patent and trade secret regimes.[202] Patentees get exclusive use of the invention—that is, protection against independent invention—in return for disclosing their information to the public. Trade secret holders get no such right and make no such disclosure. Courts generally keep the parties to their bargain lest trade secrets become like patents but without the disclosure bargain and without any time limit.[203]

There is a fourth key difference between patents and trade secrets, but it is one to which the courts have not paid attention—the lack of any ex ante or ex post review of the quality of the innovation protected as a trade secret. This difference, however, is another important reason not to give deference to trade secrets in antitrust litigation.

A strong policy of deference to patent holders reflects a maximalist view of intellectual property, resting on an economic argument that suboptimal innovation will occur unless inventors are able to appropriate the full monopoly returns from their inventions. Critics of expansive intellectual property rights, on the other hand, argue for parsimony in rewarding intellectual property rights holders—intellectual property rights holders should be given just enough to incentivize innovation, but no more.[204]

Whatever one thinks about these two positions, however, both sides advance their positions in the context of a system where a government agency screens inventions before a patent can issue and where the invention must meet statutory standards of patentability (novelty, utility, and non-obviousness).[205] In recent years critics on both sides of the presumption debate have become concerned about the quality of ex ante review and the lowering of standards for patent grants. This has led to proposals for

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[202] *See* Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373, 401–403 (1911).

[203] *See, e.g., id.*

[204] The debate is discussed in First, *supra* note 13, at 376.

[205] *See* 35 U.S.C. § 101 (2000) (utility and novelty); id. § 103 (amended in 2004) (nonobviousness).

improving the Patent and Trademark Office,[206] as well as to judicial decisions making it harder to get patents.[207]

Trade secrets go through no such ex ante review, nor are they subject to any quality review ex post. This is yet another reason why trade secrets should come to the courts with no presumptions, either legal or factual, about their innovativeness.[208] For all the courts know, an "invention" protected by a trade secret could be the equivalent of the patent medicines of yore—just alcohol, bitters, and water. If we are skeptical about the quality of reviewed inventions, shouldn't we be even more skeptical about the quality of unreviewed inventions?

2. Trade Secrets' Legal Properties and their Economic Effects

Modern economic analysis in antitrust cases applies a rule of reason balance—an effort to balance the anticompetitive effects of particular arrangements (harm to consumer welfare or the competitive process) against any procompetitive (efficiency) justifications. Although courts in Section 1 trade secrets cases have often used the language of "ancillary restraints" to structure this rule of reason balancing, this doctrine has never been fully embraced by the Supreme Court and its exact meaning is unclear.[209] Better analysis avoids this categorizing effort, looking directly at economic effects. This is true in Section 2 cases as well, where, despite much controversy over various phrasings of

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[206] *See, e.g.*, Mark A. Lemley & Carl Shapiro, *Probabilistic Patents*, 19 J. ECON. PERSP. 75 (2005); Robert P. Merges, *As Many as Six Impossible Patents Before Breakfast: Property Rights for Business Concepts and Patent System Reform*, 14 BERKELEY TECH. L.J. 577 (1999).

[207] *See*, *e.g.*, KSR Intern. Co. v. Teleflex Inc., 550 U.S. 398, 419 (2007) (rejecting the Federal Circuit's test for obviousness for having become a "rigid and mandatory" formula and writing that "[g]ranting patent protection to advances that would occur in the ordinary course without real innovation retards progress . . . .").

[208] *Compare* 35 U.S.C. § 282 (2002) ("A patent shall be presumed valid."), *with* 17 U.S.C. § 410(c) (In any judicial proceedings the certificate of a registration made before or within five years after first publication of the work shall constitute prima facie evidence of the validity of the copyright and of the facts stated in the certificate. The evidentiary weight to be accorded the certificate of a registration made thereafter shall be within the discretion of the court.").

[209] *Cf*. Texaco Inc. v. Dagher, 547 U.S. 1, 7 (2006) (although stating that ancillary restraints are "valid" while "naked restraints" are not, Court also notes that the ancillary restraints doctrine has "no application here" because the business practice involved "the core activity of the joint venture itself," namely, the pricing of its goods).

the "test" for finding monopolizing conduct, in the end the courts are most likely to assess a monopolist's conduct using a rule of reason balance.[210]

Analyzing the competitive effects of a restraint involving a trade secret requires assessing the economic value of the trade secret. This is not the same as requiring the trade secret holder to prove that it has confidential information that would be protectable under state law as a "trade secret." Rather, it involves an assessment of the secret information itself in light of the market effect of the practice under consideration (whether a license or a refusal to supply) and the efficiency justification for the practice.

Each of the legal properties of trade secrets discussed above—no requirement of innovation, maintenance of secrecy, and indefinite duration—can affect this competitive analysis, because these legal properties relate to the efficiency justification a trade secret holder might advance to support a restrictive or exclusionary practice. To take one example, courts assessing the procompetitive effect of a restriction involving a trade secret should require some proof of innovation before finding that the restriction is a necessary incentive for innovation. Another example would be to recognize that as a secret leaks out, so too does the efficiency gain in restricting a licensee's use of it. This means that even if a trade secret license might have been justified when entered into, as a way to allow innovators to share their technology and thereby diffuse innovation, this efficiency justification may diminish over time. Finally, even though trade secret protection can theoretically last forever, at some point society will have paid the innovator the full social value of the invention. At that point the trade secret holder might still be able to prevent misappropriation of its secret but should not be able to use the secret to continue to reap monopoly profits.

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[210] *See*, *e.g.*, United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001), *cert. denied*, 534 U.S. 952 (2001); Varney, *supra* note 181 (arguing that, "following . . . *Microsoft*," the DOJ should "look closely at both the perceived procompetitive and anticompetitive aspects of a dominant firm's conduct, weigh these factors, and determine whether on balance the net effect of this conduct harms competition and consumers."). For a discussion of the possible tests, *see, e.g.*, Section 2 Report, *supra* note 180; ANTITRUST MODERNIZATION COMMISSION, REPORT AND RECOMMENDATIONS 81–83 (2007), *available at* http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf (reaffirming the appropriateness of the rule of reason in Section 2 cases). The Commission did call for greater judicial clarity in refusal to deal cases. *See id.* at 83 (advocating a clearer declaration that "[i]n general, firms have no duty to deal with a rival in the same market").

3. Respect the Bargain

All intellectual property regimes have internal balances that moderate the scope of protection and help balance the trade-off between exclusion and access. In patent law, for example, the exhaustion doctrine ends the power of the patentee to control use of a product after the first lawful sale.[211] In copyright, there is a statutory exemption for fair use.[212]

Courts are often called upon to interpret these balancing doctrines within the context of the relevant intellectual property regime. There are occasions, however, when an intellectual property right holder attempts to tilt the internal balance in a way that also restricts competition, and the case gets framed as an antitrust violation rather than as an intellectual property right violation. A patent holder, for example, might transfer its product under a single use license, trying to avoid the first sale doctrine so as to have an enforceable patent right. If the conduct also gives rise to an antitrust claim, however, courts will be required to decide how to interpret the scope of the intellectual property right, so as to determine whether the purported license is really a subterfuge for anticompetitive conduct.[213]

For trade secrets, the internal balance is spelled out in the bargain that trade secrets holders make in choosing trade secrecy over some other form of intellectual property protection. They get to exclude others from gaining unauthorized access to the protected information, and they are not required to make any showing of the innovative quality of that information, but they can't keep others from figuring out the information on their own, whether by reverse engineering or by independent invention.

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[211] *See* Quanta Computer, Inc. v. LG Elecs., Inc., 128 S.Ct. 2109, 2117–18 (2008); Adams v. Burke, 84 U.S. 453, 455 (1873).

[212] 17 U.S.C. § 107. *See* Sony Corp. of America v. Universal City Studios, Inc., 464 U.S. 417, 432–33 (1984);

[213] *See* Mallinckrodt, Inc. v. Medipart, Inc., 976 F.2d 700, 701 (Fed. Cir. 1992) (holding that single-use only restriction could be enforced through patent infringement suit, the restriction being neither patent misuse nor a per se antitrust violation); Harry First, *Controlling the Intellectual Property Grab*, *supra* note 13, at 386-90 (criticizing *Mallincrodt* and subsequent cases). *Compare* Straus v. Victor Talking Mach. Co., 243 U.S. 490, 501 (1917) (rejecting enforcement of "license notice" attached to phonograph machines; "real and poorly-concealed purpose is to restrict the [resale] price"); Dr. Miles Med. Co. v. John D. Park & Sons Co., *supra* note 95 (describing as "subterfuge" defendant's effort to characterize product transfers as "consignments" rather than sales).

As in other areas of intellectual property, courts can be required to take account of this internal balance in the context of antitrust litigation.[214] Respecting that balance, and the trade secret owner's original bargain, means that the courts should be particularly concerned about the ways in which trade secret holders try to restrict information from becoming more widely known. For example, post-employment restrictions with substantial anticompetitive effect could be narrowly confined to cases of clear breaches of fiduciary duty, thereby respecting trade secrets' internal balance of exclusion while not unduly burdening access and adversely affecting competition. Similarly, efforts to keep licensees from reverse-engineering could be narrowly construed so as to be sure that the legal limitations on the scope of trade secrecy protection are maintained.

B. Applying the General Principles

1. Price and Territorial License Restrictions

It is time to lay to rest the dictum from *Hartman* and *Dr. Miles* that restrictions on price and territory in licenses to manufacture using a trade secret are lawful under the Sherman Act.[215] The dictum is a holdover from *Fowle v. Park* and the pre-Sherman Act days, when the question was whether such agreements were unenforceable as general restraints of trade. Later courts, however, have not closely analyzed the competitive effect of these restraints, usually preferring to take refuge in the "ancillary restraints" label rather than doing a full rule of reason analysis.[216]

Although a doctrinal argument can be made for treating these restraints as per se unlawful when they can be characterized as horizontal,[217] for illustrative purposes it is more helpful to see how these restraints might be analyzed under a rule of reason approach that takes proper account of trade secrecy protection.[218]

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[214] *See, e.g.*, Bonito Boats, Inc. v. Thunder Craft Boats, Inc., 489 U.S. 141, 160 (1989) (reaffirming the right of third parties to reverse-engineer products to discern their composition, even when protected by a trade secret).

[215] *See supra* text accompanying notes 106-108.

[216] *See, e.g.*, Foundry Servs., Inc. v. Beneflux Corp., 110 F. Supp. 857, 857–858 (S.D.N.Y. 1953).

[217] *See supra* notes 109-111 and accompanying text.

[218] Use of a rule of reason also recognizes that trade secret licenses are often complex and raise at least a facial claim of an efficiency justification. *Cf.* Broadcast Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1, 19–20 (1979) (finding that a blanket performing rights license offered by collective

Thus, our analysis would begin with an assessment of likely anticompetitive effects and then consider the efficiency justifications that trade secret protection might raise.

Looking first at the anticompetitive effects, in many of the price and territorial licensing cases discussed above it is quite likely that the restrictive agreements raised prices. First, a number of the cases involved competitors or potential competitors, either at the time the license was first entered into (e.g., the cellophane makers in *DuPont* and the glass makers in *Pilkington*) or, at least, by the time litigation occurred (the flux makers in *Beneflux*). Second, in *Fowle v. Park*, although the original trade secret licensor was the inventor of the formula and apparently not a manufacturer, the national system of price and territorial restraints that his licensing created was designed to prevent competition between his two licensees.[219] The licensees themselves strengthened this anticompetitive outcome by making a later agreement not to compete in the West, an area to which the original agreement apparently did not extend.[220] The case thus went beyond a simple inventor/manufacturer license, which might have no impact on price competition, to involve a much broader system whose effect on price was apparent (after all, Fowle was complaining of Park's price competition).

When we examine the efficiency justifications, the analysis should start with a "no presumption" principle for trade secrets. This means placing the burden on the trade secret holder to demonstrate efficiency justifications, rather than just relying on a presumption that the confidential information actually described the sort of innovation whose creation we might want to incentivize with monopoly profits.

The strongest of our cases for the innovativeness of the secret information appears to be *DuPont* cellophane, where the trade secrets for the manufacturing process gave La Cellophane a strong competitive advantage over a struggling DuPont.[221] Weaker is *Pilkington*, a case where the patents, rather than trade secrets,

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organizations of composers, authors, publishers, and broadcasters should be viewed under the rule of reason because the blanket license "facially" appeared to be "designed to increase economic efficiency and render markets more, rather than less, competitive") (internal quotation marks omitted).

[219] 131 U.S. 88, 88 (1889).

[220] *See id.*

[221] *See* United States v. E.I. Du Pont de Nemours & Co., 118 F. Supp. 41, 53 (1951).

were critical and where most aspects of the "secret" process became known fairly quickly once a licensee began to manufacture float glass. Once the patents expired in *Pilkington* it was apparently difficult to make out a case for the innovativeness of the trade secrets standing alone.[222] The weakest is the formula for Wistar's Balsam of Wild Cherry in *Fowle v. Park*. The "secret" there is the least innovative—more akin to the bartender's mix of a cocktail than to a new or non-obvious invention.[223]

The two other legal properties of trade secrets—continued secrecy and length of protection—interact in a way that will likely make the efficiency justification weaker as time goes on. That is, the longer the restriction is in place, the more likely it is that the secret has worn thin, and the less necessary it is to continue rewarding the innovator with a monopoly.

It is hard to tell from the facts of most of the cases examined above how thin the secrecy had become (*Pilkington* being the exception), but in all of the cases the competitive restrictions on price or territory had been in effect for a substantial period of time prior to being challenged. Particularly dubious in this regard is *Fowle v. Park*, where the restraints had been in effect for forty years before Fowle brought suit.[224] Surely the need "to encourage useful discoveries by securing their fruits to those who make them," as the Court put it in *Fowle*, had been fully satisfied by then.[225] *Beneflux* is closer to the line. The territorial restraints had been in force for seventeen years when suit was brought to enforce them, coincidentally the length of the patent term at the time—a good, even if not perfect, reference point.[226] Of course, it is impossible to calibrate accurately how much reward is enough. The challenge in a rule of reason analysis will be to weigh time against innovative quality and secrecy to determine whether the justification for a territorial restriction still holds, particularly when

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[222] *See supra* text accompanying notes 138-139.

[223] For a discussion of protecting cocktails through trade secrets, see Czapracka, *supra* note 4, at 221 & nn.71–80 (discussing Mason v. Jack Daniel Distillery, 518 So. 2d 130 (Ala Civ. App. 1987) (finding that a cocktail recipe comprised of Jack Daniel's whiskey, Triple Sec, sweet and sour mix, and 7-Up was a valid trade secret). *See also* KFC Corp. v. Marion-Kay Co., Inc., 620 F. Supp. 1160, 1170 (D. Ind. 1985) (finding that KFC may impose restrictions on its licensees' reproduction of its seasoning blend, protected by a trade secret)).

[224] *See* 131 U.S. at 88.

[225] *Id.* at 97.

[226] *See* Foundry Servs., Inc. v. Beneflux Corp., 110 F. Supp. 857, 857–58 (S.D.N.Y. 1953).

there is the less restrictive alternative of royalties without territorial allocation.[227]

The *DuPont* cellophane case presents the most interesting fact-pattern.[228] The territorial restraints in question had been in effect for twenty-four years at the time the Justice Department brought suit. The facts indicate that La Cellophane's process was likely innovative at the time it was licensed to DuPont; indeed, it was critical for making commercially successful cellophane. On the other hand, evidence in the record also indicates that DuPont could have figured out how to make cellophane successfully within, at most, eight years (presumably by independent invention).[229] Thus, at least for this eight-year period—in effect, La Cellophane's lead time—La Cellophane would arguably be entitled to supra-competitive returns on its process, assuming, of course, that the process was innovative. It is hard to see, however, why the parties should be allowed to continue to divide world markets beyond that time, particularly where the restraint ends up being in effect even beyond the patent term.[230]

2. Monopoly Firm Conduct

One of the most contested areas of antitrust law in recent years has been the question whether a monopoly firm has any duty to license to a competitor its patent or copyright in circumstances where the refusal to license would maintain a monopoly. The first chapter of the federal antitrust enforcement agencies' 2007 Intellectual Property Report, for example, was devoted to this issue, ultimately concluding that antitrust liability for "mere unilateral, unconditional refusals to license" would not play a "meaningful part" in antitrust enforcement regarding patent rights.[231] This view reflected the Justice Department's

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[227] *See* Aronson v. Quick Point Pencil Co., 440 U.S. 257, 264–266 (1979) (allowing time-unlimited royalties for trade secrets even where the patent on the invention did not issue).

[228] *See supra* notes 125–131 and accompanying text.

[229] *See supra* note 128.

[230] This argument is consistent with the position taken by the Justice Department in its 1977 guidelines for international operations. *See* GUIDE FROM THE U.S. DEPARTMENT OF JUSTICE, ANTITRUST AND INTERNATIONAL OPERATIONS 31 (1977) (parties to a territorial restraint in a know-how license that extends beyond the time that the licensee would need to develop the technology on its own "bear the burden of proving the necessity of the restraint").

[231] *See* IP Report, *supra* note 1, at 32.

contemporaneous condemnation of an earlier Ninth Circuit case, which had upheld a jury verdict arising out of a monopolist's refusal to sell patented replacement parts to competitors in the service aftermarket.[232]

Critical to the courts' and enforcers' views in this area has been the presumption that the dominant firm's refusal to license its intellectual property right is justifiable, both as a matter of statutory construction of the Patent Act (or Copyright Act) and because of the economics of innovation.[233] In the area of trade secrets, however, there should be no such legal or economic presumption.

With regard to the legal claim, as the courts recognized in the early Sherman Act cases, there is no statutory right in the trade secrets area similar to the patentee's exclusive right to "make, use, or sell" the patented invention.[234] The only legal right a trade secret owner has is the right to prevent others from misappropriating the secret.

Without a legal presumption that the refusal to license a trade secret is justifiable, a court would be required to examine the case for a monopolist trade secret holder's claim that the failure to supply otherwise secret information is economically efficient. Using the general principles proposed above, the analysis would first examine the innovativeness of the withheld information and then consider the duration of protection and the question of how secret the withheld information might be.

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[232] *See* Image Technical Servs., Inc. v. Eastman Kodak Co., 125 F.3d 1195, 1200 (9th Cir. 1997). For enforcement views, see, e.g., R. Hewitt Pate, Assistant Att'y Gen., U.S. Dep't of Justice, Competition And Intellectual Property In The U.S.: Licensing Freedom And The Limits Of Antitrust, Address at the 2005 EU Competition Workshop 4 (June 3, 2005), *available at* http://www.usdoj.gov/atr/public/speeches/209359.pdf ("[T]he argument is that there must . . . be *some* circumstance in which the unilateral, unconditional refusal to license a patent must constitute an antitrust violation. With a single much-criticized exception [*Kodak*], this is an argument that has never found support in any U.S. legal decision. At this point in the development of U.S. law, it is safe to say that this argument is without merit.").

[233] *See, e.g.*, Pate, *supra* note 232, at 4 ("A unilateral, unconditional refusal to license a valid patent cannot, by itself, result in antitrust liability under U.S. law.").

[234] 35 U.S.C. § 271(a) (2000). It is debatable, however, whether the statutory right to exclude use precludes antitrust liability for failure to sell the product made under a patent. *See* Harry First, Microsoft *and the Evolution of the Intellectual Property Concept*, 2006 WIS. L. REV. 1369, 1426.

Although there have not been many antitrust cases involving a refusal to supply secret information, one area in which this issue has arisen is the refusal to disclose interface information. As a general matter, interfaces will likely have a weak claim to innovativeness. Interface information is usually critical simply because the maker of a complementary product needs to know the specifications of the interface. Whether the interface represents some new or non-obvious invention is not what matters most, although, of course, there can be innovation in designing interfaces. The critical issue is how to plug into the monopolist's product, something that becomes important to competition by virtue of the complementary product manufacturer's dependence on the monopoly producer.

The European *Microsoft* case is a good example of a case where the interface information was important because of the dominant firm's market position rather than the innovative quality of the interface itself. In that case Microsoft's monopoly was in the PC operating system market.[235] Sun, its competitor in network server operating systems, needed interoperability information so that its workstations could operate in a network of Microsoft PCs and servers and communicate with both.[236] In the Court of First Instance the European Commission disputed the innovativeness of the communications protocols that Sun sought, arguing that the secret information's value "lies not in the fact that it involves innovation but in the fact that it belongs to a dominant undertaking."[237]

The CFI ultimately did not decide whether the interface information was innovative, choosing to uphold the Commission's decision on the assumption that it was, but the Commission faced the issue head-on in its subsequent decision involving Microsoft's lack of compliance with its order to license the information at a reasonable royalty rate.[238] The Commission determined that if the fees were to be more than nominal, the information had to be innovative in the sense that it was not "obvious to persons skilled in the art."[239] To make this assessment, the Commission hired

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[235] *See* CFI *Microsoft* Decision, *supra* note 172, ¶¶ 30–31.

[236] *Id.* ¶¶ 2, 36.

[237] *Id.* ¶¶ 276, 280.

[238] *See id.* ¶ 620.

[239] *See* Commission Decision of 10 Nov. 2005, Case COMP/C-3/37.792, imposing a periodic penalty payment pursuant to Article 24(1) of Regulation No 1/2003 on Microsoft Corporation (Microsoft) ¶ 105, *available at*

technical experts to review each of the 173 non-patented protocols that Microsoft had not disclosed. The experts ultimately concluded that only seven of the protocol technologies were innovative.[240]

Similarly, in *Berkey v. Kodak* the withheld interface information would appear to have lacked much of an innovative quality.[241] Although Kodak disclosed eleven pages of specifications to Berkey relating to interoperability, the specifications only involved the size of the film cartridge and the fit in the new camera.[242] Kodak's innovation was in making a small camera with film that would produce acceptable-quality images, not in engineering the fit between the two.[243]

The fact that an interface lacks innovation, however, does not end the antitrust analysis. Two more issues remain relating to trade secrecy—time and the amount of secrecy involved. In interface cases, these issues can be difficult to assess when there is a trade-off between competition and innovation. Interfaces may not be that difficult to reverse-engineer once the product is on the market (it took Berkey eighteen months to do so, for example). This means that they will not stay secret for long. A modest amount of lead-time may give the innovator a modest return on a modest invention, but even incremental advances can increase consumer welfare.

The optimal approach from a competition and innovation perspective would be for the monopolist to license the interface sufficiently in advance of introduction to allow the complementary producer to adapt its product. In this way the innovator would get a return on its innovation without skewing competition in the complementary product market. Given the potential administrative

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http://ec.europa.eu/comm/competition/antitrust/cases/decisions/37792/art24_1_decision.pdf.

[240] *See* Commission Decision of 27 Feb. 2008, Case COMP/C-3/37.792 (Microsoft) ¶ 175 & n.201, *available at* http://ec.europa.eu/comm/competition/antitrust/cases/decisions/37792/decision2008.pdf. The Commission determined that the protocols that were patented were presumptively innovative. *See id.* ¶ 132. *See also id.* ¶ 151 (concluding that Microsoft's expert witness "confirms the Commission's assessment that Microsoft in order to meet its product design goals largely relies on combinations of existing solutions and slight improvements to known approaches, which are dictated by ordinary engineering skills and common sense, rather than on innovative protocol technology").

[241] 603 F.2d 263 (2d Cir. 1979).

[242] *Id.* at 281.

[243] *Id.* at 270.

problems in assessing the timeliness of disclosure and reviewing the price at which it is made, however, courts are no doubt warranted in being cautious about finding liability for the failure to license interface information. Nevertheless, a per se rule of *legality* is unwarranted as well. This is particularly true in cases such as *Berkey*, where the monopolist had disclosed interfaces in the past and had even done so in the case that gave rise to the litigation, albeit in an untimely way. Further, the concern for administrability is likely overdrawn. In the settlement of the monopolization litigation against Microsoft in the United States, Microsoft has been required to license application programming interfaces ("APIs") and communications protocols.[244] The court's experience in administering the decree has been mixed—API disclosure has gone smoothly, but technical problems have plagued the protocol disclosure.[245] The *Microsoft* experience at least shows, however, that courts are unwarranted in giving carte blanche to monopolists to keep interface information secret, out of fear that remedy will prove impossible to administer.

Rule of reason analysis, especially when considered alongside our experience with administering decrees requiring disclosure, indicates that there may very well be times when a monopolist's refusal to license trade secret information should be found to violate Section 2 of the Sherman Act. Maintaining monopoly may cause serious consumer injury and retard innovation in an industry. A weakly-innovative trade secret should not be used as a justification for withholding information in such circumstances.

V. Conclusion

This chapter has reviewed the application of antitrust law to trade secrets. That review found more history than one might have predicted and less careful analysis than one might have hoped. Trade secrets cases raised competition issues even before the passage of the Sherman Act. Although the initial Sherman Act cases reveal a careful understanding of the legal properties of trade secret protection and a desire to limit the ability of trade secret holders to use trade secret licenses to restrict competition, once

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[244] *See* Harry First & Andrew I. Gavil, *Re-Framing Windows: The Durable Meaning of the* Microsoft *Antitrust Litigation*, 2006 UTAH L. REV. 641, 693–695 (2006) (analyzing the settlement decree's forward-looking requirements that Microsoft license those APIs necessary for interoperability with Windows as well as its communication protocols used to control communication between desktop PCs and servers).

[245] *See id.* at 698–704.

past these early cases the courts have too often fallen into a reflexive pattern of protecting trade secret holders at the expense of competition and consumer welfare.

Much of the problem with antitrust analysis of trade secrets has come from the failure to appreciate the differences between trade secret protection and other forms of intellectual property protection. As an economic matter, trade secrets are, of course, intended to provide some protection for innovations, thereby acting as an incentive for their production, but they have never been intended to provide monopoly rents. Rather, the core purpose of trade secret protection has been to protect against misappropriation and thereby promote relationships of trust. These relationships have important economic and social benefits, enabling cooperative enterprises to succeed, but protection against misappropriation does not require giving monopoly profits to the trade secret holder.

This chapter has suggested some general principles for analyzing trade secret claims in antitrust cases, the first and most important of which is to begin the analysis without presuming that the trade secret is innovative. Instead, trade secret holders would need to show that their secret is innovative and that the benefits of enforcing secrecy outweigh the costs of restricting competition. More careful analysis of the economic costs and benefits of protecting particular trade secrets should lead the courts to pay more attention to the effect of the trade secret owner's conduct, not only on consumer welfare but also on the competitive process, which, in itself, is important for stimulating innovation.