

Patent Licensing Restrictions Not Regarded As Tying

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The Court of Appeals for the Federal Circuit (CAFC) considered the issue of whether certain patent licensing restrictions in license agreements may constitute unlawful tying arrangements in *Monsanto Co. v. Scruggs*, 459 F.3d 1328 (Fed. Cir. 2006). The CAFC determined that the license restrictions contained in Monsanto's license agreements did not constitute antitrust violations.

Background and Law

Monsanto holds a number of patents related to two separate types of genetic material; one patent relates to glyphosate herbicide resistance (Roundup Ready trait) and the other patent relates to insect resistance (Bollgard trait). Monsanto licensed the patents to seed companies who integrate genetic material covered by the patents into seeds for distribution to farmers. Seeds sold by seed companies include seeds with the herbicide resistance only, and seeds with both the herbicide and insect resistance.

Monsanto required any farmers that purchased the genetically altered seeds to sign license agreements (Grower License Restrictions, Grower Incentive Agreements, and Seed Partner Agreements) that included a number of restrictions on the sale and distribution of the genetically altered seeds. Between 1996 through 1998, each of the license agreements expressly required that if a farmer decided to use a glyphosate herbicide on plants grown from the seeds covered by the patents, the farmer had to use Monsanto's Roundup® herbicide. From 1996 through 1998, Monsanto's Roundup® herbicide was the only glyphosate herbicide approved by the Environmental Protection Agency (EPA). The license agreements included an incentive program that gave farmers price incentives if they only used Roundup® herbicide on crops containing Monsanto's patented technology. The license agreements also included a no-replant provision that prohibited the farmer from replanting any seeds derived from the first crop produced by the genetically altered seeds.

According to Section 1 of the Sherman Antitrust Act, 15 U.S.C. §§ 1-7 (Sherman Act), "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce . . . is [] declared to be illegal." In particular, tying arrangements fall under Section 1 of the Sherman Act where a "tying arrangement is the sale or lease of one product on the condition that the buyer or lessee purchase a second product." *Monsanto Co. v. Scruggs*, 459 F.3d at 1338. A tying arrangement exists, if there are 1) two separate products or services; 2) the sale of one product or service is conditioned on the purchase of another; 3) the seller has market power in the tying product; and 4) the amount of

interstate commerce in the tied product is not insubstantial. *Eastman Kodak Co. v. Image Tech, Serv., Inc.*, 504 U.S. 451, 461-62 (1992). Unlawful tying is also established when a seller conditions the sale of a first product upon the buyer agreeing not to purchase a different product from another supplier. *Northern Pacific Railway Co. v. United States*, 356 U.S. 1, 5-6 (1958) (“[a] tying arrangement may be defined as an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier.”).

To establish a Section 2 violation of the Sherman Act, one has to prove “that the party charged had monopoly power in a relevant market and acquired or maintained that power by anticompetitive practices.” *Monsanto Co. v. Scruggs* 459 F.3d at 1339.

The defendant Scruggs bought some of Monsanto’s genetically altered seeds and harvested a crop. Scruggs then replanted some of the seeds derived from his first harvest and from subsequent harvests. Monsanto subsequently sued Scruggs for patent infringement based on the no-replant policy, in part, for using unlicensed seeds that included genetic material covered by Monsanto’s patents. Scruggs denied infringement, counterclaimed for invalidity of the Monsanto patents and claimed that Monsanto’s license agreements violated antitrust laws and constituted patent misuse. The trial court granted summary judgment for Monsanto on the antitrust claims, and the CAFC affirmed the trial court’s decision.

Scruggs Argued

On appeal, Scruggs reiterated his antitrust assertions arguing that Monsanto’s Grower License Restrictions, Grower Incentive Agreements, and Seed Partner Agreements violated the Sherman Act. Scruggs argued that the Grower License Restrictions and the Seed Partner Agreements unlawfully tied the purchase of seeds containing genetic material covered under Monsanto’s patents to the purchase of its herbicide Roundup®. Scruggs argued that Monsanto unlawfully tied the herbicide resistant trait to the insect resistant trait in cotton seeds. This, Scruggs argued, unlawfully tied the patented herbicide resistance to the patented insect resistance.

Monsanto Argued

In response to Scruggs’ assertions of antitrust violations, Monsanto argued that sale of seeds, including the genetic material covered under the Monsanto patents, was not conditioned on purchase of Monsanto’s Roundup® herbicide. Rather, the license agreements only required a customer to use Roundup® if the customer decided to use a glyphosate herbicide. Monsanto also argued that as Roundup® was the only available glyphosate herbicide approved by the EPA from 1996 – 1998, Monsanto’s licenses could not constitute anticompetitive practices.

Discussion of the CAFC Decision

The CAFC found that Scruggs did “not point to sufficient evidence to establish that Monsanto’s behavior constitutes illegal tying.” *Monsanto Co. v. Scruggs*, 459 F.3d at 1340. Addressing Monsanto’s grower incentive program, the Court stated that the “grower incentive program was optional, not coerced.” *Id.* Therefore, because Monsanto provided the incentive program as an option, the Court found no tying violation.

The Court declined to find unlawful tying for Monsanto’s requirement that customers buy Roundup® if the grower used a glyphosate herbicide. The Court commented that “Monsanto’s seed partners were not forced to buy Roundup under the seed partner agreements.” *Id.* Rather, the license agreements only required that *if* the farmers used a glyphosate herbicide with the genetically altered seeds, *then* the farmer must also use Monsanto’s Roundup® herbicide. The Court reasoned that, because Monsanto did not condition the sale of seeds covered under the Monsanto patents on the purchase of Monsanto’s Roundup® herbicide, there was no violation of the Sherman Act. This conclusion appears to be at odds with the holding of *Northern Pacific Railway Co. v. United States*, 356 U.S. 1, 5-6 (1958), which held that “a tying arrangement may be defined as an agreement by a party to sell one product but only on the condition that the buyer . . . agrees that he will not purchase that product from any other supplier.” Under the logic of *Northern Pacific*, unlawful tying occurs, not only when the sale of one product or service is conditioned on the purchase of another, but also when there are prohibitions on buying different goods or services from competitors. Following this logic, Scruggs argued that due to Monsanto’s license agreements, growers had to agree not to purchase herbicide from anyone other than Monsanto in violation of the Sherman Act.

While on its face the license restrictions appeared to run afoul of *Northern Pacific*, the CAFC declined to find an antitrust violation when no actual anticompetitive result could be pointed to by Scruggs. Monsanto argued that its contract provisions lacked any anticompetitive effect and therefore, could not constitute a violation of the Sherman Act. The Court agreed with Monsanto, noting that because the only EPA approved glyphosate herbicide was Monsanto’s, the contract provisions could not have an anticompetitive effect. *Monsanto Co. v. Scruggs* 459 F.3d at 1341. The Court reasoned that, “even if growers elected to use such herbicides . . . they would not be legally free to use competing brands.” *Id.* Accordingly, the Court concluded that Scruggs failed “to show that the challenged contracts had an actual adverse effect on competition.” *Id.*

While the Court consistently refused to apply an expansive reading of the Sherman Act, it should be noted that when Monsanto’s competitors applied for and obtained regulatory approval for glyphosate herbicides other than Monsanto’s Roundup®, Monsanto modified its contracts to authorize use of any

alternative herbicide that met EPA requirements. This appears to have been an important distinction in this case. While the CAFC did not outline a rule with regard to tying arrangements, the Court took a practical business approach in determining whether an antitrust violation had occurred.

The Court also declined to find that Monsanto unlawfully tied the herbicide resistant trait to the insect resistant trait in cotton seeds, stating “there is no merit to the argument that Monsanto illegally tied the sale of cotton containing the Roundup Ready® gene to the sale containing the Bollgard trait.” *Monsanto Co. v. Scruggs* 459 F.3d at 1340-41. The trial court found that the record did not support Scrugg’s assertion that Monsanto engineered a shortage of single trait cotton seeds which forced growers to buy stacked trait seed. *Id.* The CAFC further commented that “Monsanto sells cotton without the Bollgard trait and there is no evidence that Monsanto engineered a shortage of Roundup Ready® cotton.” *Id.* Therefore, while Scruggs asserted that Monsanto unlawfully stacked patented genetic material (e.g. insect and herbicide resistance) into seeds, the Court found that no antitrust violation occurred because Monsanto made available seeds that had only one of the two patented traits.

The Court failed to address at least one tying issue. The Court relied heavily on the fact that Monsanto’s license restrictions had no actual anticompetitive effect, and therefore, even though the license restrictions appeared to run afoul of *Northern Pacific*, declined to find tying. However, Monsanto did not offer a seed solely with the insect resistant genetic material. If a farmer wanted to use herbicide on seeds with the patented insect resistance, the farmer had no choice but to use Roundup® because the insect resistance was only offered in seeds with the herbicide resistance. Therefore, Monsanto’s conduct did have an actual adverse effect on competition because Monsanto’s failure to offer a seed with only insect resistance prevented farmers from using other herbicides with insect resistant seeds. This issue was left unanswered by the Court.

Points to take away

- The incentive program offered by Monsanto was not an antitrust violation because the “program was optional, not coerced.”
- The CAFC declined to find unlawful tying, even though, on its face, the license agreement appeared to run afoul of *Northern Pacific*, because no actual adverse effect on competition occurred.
- The CAFC left unanswered whether stacking multiple patented genetic traits into a single seed, and then using a license agreement to prohibit buyers from using a competitive product, is unlawful tying.