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In this short note, I briefly review current practices for the evaluation of RAND licensing terms and then provide a set of coherent recommendations designed to improve the standard-setting process and the implied licensing of standard essential patents.

1. Current Practices for the Determination of (F)RAND Terms

A standard has been chosen and patents which are (claimed to be) essential to the implementation of this standard have been identified. What's next? Clearly the best outcome is one where parties agree on licensing terms without using any form of litigation or arbitration. This simple principle was indeed at the root of DG Comp's intervention in disputes between Motorola, Apple, Microsoft and Samsung. In its extended review of these disputes, the Commission made it clear that it did not want to get dragged into any consideration of what would constitute a FRAND royalty. Instead, the Commission focussed on the litigation *process* in the hope that, by ensuring that the parties' positions in such a process are (in the Commission's view) well balanced, neither party would have an excessive incentive to use litigation.

Unfortunately, even with well-balanced rules for litigation, parties do sometimes fail to agree on what constitutes a FRAND agreement. This might be because the parties have genuinely different appraisals of the value of the contribution made by a given set of SEPs or because of less innocent considerations such as attempting to foreclose a downstream rival or refusing to engage to deprive a rival from a source of income. If the parties litigate and fail to settle or if they agree to rely on the opinion of an arbitrator, then *someone* eventually has to put pen to paper and come up with a number for what a FRAND royalty would be. Indeed, even in cases where parties do not litigate or settle before the end of the litigation process, one could argue that knowing that a FRAND rate would be eventually chosen by a third party – and hence having some conjecture as to what this third party's determination might be, is a crucial element of the negotiation or settlement process. In this sense, having clear guidelines about the determination of FRAND terms is essential for *all* SEP licensing negotiations.

There are of course situations where the need for a “backstop” determination of FRAND terms is not quite as important. In particular, this is the case in industries where participants in the standard-setting process are mostly users of the standard themselves, where these participants meet repeatedly in various standard-setting bodies and when they each have an appreciable portfolio of potential SEPs. Under these conditions, the natural outcome is for the SEP-owners to just agree to cross-licenses, without paying too much attention to the actual “balance” of the portfolios involved as such trades would tend to “average out” in the longer term. This is still the norm in several industries. However, this norm has come under pressure in a number of important sectors, like electronics. This is mostly the consequence of two types of technological evolution. The first one is the increased complexity of technologies, i.e., the increased number of “components” required in order to establish a given standard. The more players there are, the harder it is to reach agreement on the base of “good hearted” bilateral agreements. Secondly, the convergence between the computer and telecom sectors means that firms with very different patent portfolios are now competitors in the relevant downstream markets: telecom firms have portfolios which are rich in

potential SEPs, while computer giants such as Apple and Microsoft do not. This too makes settlement based on cross-licensing less attractive.

So, what can we do if “putting a number” on FRAND royalties cannot be avoided. There are essentially two (complementary) approaches. The first one consists in proceeding by comparison. Such comparisons can be to previous rates charged for patents deemed essential to previous standards. In a sense, though, this approach just “passes the buck” and simply assumes that someone, somewhere in the past actually got these SEP royalties right. The second type of comparison is more interesting as it involves relying on the rates that patent-owners asked *before* the standard setting exercise ever began. The basic logic of such a comparison is compelling: if the purpose of FRAND is to prevent SEP owners from exploiting the “additional” market power which they gain from their inclusion in the standard, then rates charged before the SEP owners enjoyed such increased market powers are indeed the correct benchmark. There are some caveats however. Firstly, while such an approach deals effectively with the “hold up” issue linked to increased market power it does not deal at all with the issue of royalty-stacking. In that sense, such comparison should only provide an upper bound for a suitable royalty. The second difficulty comes from possible differences in fields of use. As patent-holders are allowed to charge different royalties for different fields of use, one cannot automatically assume that any pre-standardisation royalty payment refers to the same “field of use” as that involved in the SEP’s contribution to the standard.

The second approach is to conduct an assessment “from scratch”. The general idea here is that FRAND royalty levels should be set based on the methodology used to determine patent infringement damages but with some corrections to reflect the implication of the FRAND commitments given. As explained by other speakers, this is the approach followed by Judge Robart—who started from the well-known *Georgia Pacific* list of criteria (including some comparative measures)—and the approach used in *Innovatio*. In these approaches, the essential adjustments made to reflect the FRAND commitments and the peculiar nature of standard setting include taking into account that not licensing is not an option, considering the royalty stacking issue, trying to assess what a pre-standard situation might have been and, overall, keeping in mind that an essential part of standard setting is the desire to ensure a wide distribution of the related technology.

In my opinion, this second approach brings much to the table. Not only does it bring the debate down from ill-defined concepts to the—less glamorous but more useful—level of “number crunching, but it has the advantage to bring some consistencies between the treatment of SEPs and the treatment of other patents.

2. Recommendations

While I do appreciate the huge efforts made by Judge Robart and some of his peers in order to come up with a workable approach to the determination of FRAND rate. I cannot help but feel that the whole notion of FRAND has outlived its usefulness (if it ever had one). Put rather more crudely, it might be time to recognise that the FRAND emperor is indeed wearing very little clothing and has simply provided a number of actors with a convenient excuse for dodging their responsibility. In what follows, I briefly present a mechanism that would address a number of the issues raised by standard setting and SEP licensing without relying at all on any notion of FRAND rates. The only thing that this mechanism requires is a willingness on SSOs’ part to strengthen their internal rules. The suggested approach combines a number of elements.

Element 1: the SSO sets a cap on the total royalty for the standard.

This element is not as outrageous as it might look. Standards do not emerge randomly. What happens is that an industry reaches a stage where the need for a standard is acknowledged and when there is sufficient (patented or not) knowledge around that developing this standard appears to be feasible. Given this perceived need and the availability of a large portion of the innovations on which a standard would eventually rely, it should be possible for industry members—and hence SSOs—to have a decent idea of what the value of the standard would be and hence a good idea of what a reasonable cap might look like.

Furthermore, notice that this approach enables something that is often paid lip service to but rarely discussed: competition between standards. If a SSO announces a cap that potential users feel is too high, they are quite free to encourage/participate in another *standard setting effort*. In other words, this initial declaration does activate competition between standards and does therefore eliminate any issue of “hold up” at the level of the aggregate royalty.

Element 2: SSO members make a negative declaration of potential SEPs

So participants implicitly accept that all of their patents/applications are subject to the rules of the SSOs. They can however identify specific rights that they want to keep outside of the SSO’s sphere.

Element 3: The SSO chooses a company involved in the creation and administration of patent pools.

Joining the patent pool is not mandatory and the SSO has no involvement with the patent pool beyond choosing a company. This company has then exclusive rights to try to set up a patent pool for a given period after the standard has been determined. Of course, in accordance with current antitrust guidelines, pool members still have the right to license their property individually outside of the pool.

Element 4 : Once the standard is chosen, patent-holders make a positive declaration, listing all of the rights which they believe read on the standard.

This list should identify which aspect of the standard each right allegedly reads on. Creation of a corresponding database (hopefully with the help of the PTO) would also be desirable.

Element 5: SEP holders must reach an agreement on the sharing of the total royalty (not to exceed the declared cap) before collecting any of their licensing revenues.

This is a crucial element since it is the mechanism which allows us to side-step any determination of individual FRAND rates. This does not mean of course that no payment for using the SEPs are made. The SSO—or a company set up for that purpose—would collect the declared total royalty from standard users and keep the revenues in an escrow account. However, distribution of these revenues would not occur until SEP owners have agreed on how it should be shared. If necessary, incentives to reach an agreement quickly could be increased by charging a yearly or monthly administrative charge on the collected revenue. Notice that any revenue so raised could be used to

cover part of the costs of the standard setting process itself, which might have the additional benefit of making this process more accessible to smaller firms.

Element 6: How to deal with “outsiders”, i.e. firms that choose not to take part in the SSO but claim to hold SEPs?

In Europe, there is a potential approach for reigning this “ambush” behaviour. If a standard is dominant and important for the ability to compete downstream, then any (actual and valid) SEP that reads on the standard constitutes an “essential facility”. As such the owner of this facility can be mandated to provide access at reasonable term. Nothing would prevent a Court from judging that such “reasonable terms” involve joining the negotiations across all SEPs for a share of the total royalty stack which was declared by the SSO.

Of course such an approach would not be available in jurisdiction with a weaker (or no) essential facility doctrine. Still, in the U.S. for example, one might think that, in the spirit of *Ebay*, some form of “public interest” test might help achieve a similar result.