Essential Questions About Standard-Essential Patents in the U.S. and EU

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In November 2012, the ABA Section of Antitrust held a program on standard-essential patents ("SEPs"). This article summarizes that program and provides an update on related developments in the U.S. and the EU.

The November 27, 2012 Program

The panel featured Dina Kallay (then-Counsel for Intellectual Property and International Antitrust at the FTC),* Lars Kjolbye (a partner at Covington & Burling in Brussels and former senior EC enforcer), Alvaro Ramos (the Legal Director of Cisco Systems in Brussels), and Ali Stoeppelwerth (a partner at WilmerHale). The panel was moderated by Koren Wong-Ervin.

What are SEPs?

Kallay explained that SEPs are patents that are technically essential to the practice of a technology standard; a patent is essential if a standard cannot be implemented without that patent being infringed. Standards are generally designed by voluntary consensus through standard-setting organizations ("SSOs"), which are private-sector organizations engaged in the development of standards. In the United States alone, there are approximately 50,000 private-sector voluntary standards, developed by more than 600 institutions.

Defining F/RAND

According to Kallay, F/RAND (i.e., "Fair, Reasonable And Non-Discriminatory") licensing rates should be set at a level that avoids hold-up. Referring to the FTC's 2003 report on promoting innovation, Kallay stated that F/RAND rates should be related to the ex ante value of the IP. In Kallay's opinion, the value should be determined based on a point in time before the standard was "irreversible." In response to a question about the "non-discriminatory" aspect of F/RAND, Kallay responded that "all cash" transactions should reflect an identical royalty, while there could be differences where cross licenses are involved.

Injunctions and Exclusion Orders

According to Kallay, the FTC's position is that a F/RAND commitment is a declaration of an intent to license that is inconsistent with seeking an injunction. Kjolbye highlighted the significant leverage that such a remedy can bring to a negotiation, stating that injunctions and exclusion orders should be permitted only in situations where there is an unwilling licensee. Stoeppelwerth noted the difficulty in defining an "unwilling licensee." Kjolbye suggested that alternative dispute resolution could be a useful way to make such a determination.

The panel discussed the FTC's recent consent decree in *In the Matter of Robert Bosch GmbH's*. In an unprecedented decision, the FTC required Bosch to agree to license its SEPs to competitors on F/RAND terms and to abandon its claims for injunctive relief as part of a merger settlement.[1] The settlement was approved by a 3-2 vote by the FTC Commission, with Commissioners J. Thomas Rosch and Maureen Ohlhausen opposing the portions of the consent relating to SEPs. According to Kallay, *Bosch* should not be read to mean that a patent holder is always violating Section 5 of the FTC Act when it seeks an injunction on a SEP; she said that there are "more bases you need to hit" to rise to the level of a violation. Kallay did, however, say that where a patent holder cannot pursue an injunction, the FTC views a suit for willful infringement (with treble damages) as a robust remedy.

In response to a question regarding whether the *Noerr-Pennington* doctrine protects a SEP holder who seeks an injunction or an exclusion order, Kallay observed that the FTC's position is that it does not. Instead, according to the FTC, a party who makes a F/RAND commitment has waived its right to engage in this type of "petitioning."

"Commercially Essential" Patents

The panel members agreed that "hold up" with commercially essential patents may constitute a more significant problem in Europe where "exploitative" conduct can give rise to a violation. In the U.S., the lack of support for the essential facilities doctrine likely means that a refusal to license commercially essential intellectual property will not constitute a violation.

The agencies have since confirmed that the antitrust analysis for commercially essential patents is different than for SEPs. For example, on December 5, 2012, then-DOJ Deputy Assistant Attorney General for Economic Analysis Fiona Scott-Morton explained that "the difference that causes F/RAND encumbered SEPs to be of concern to competition authorities including the [DOJ]" is the presence of a collective decision by competitors.[2] In this regard, Dr. Scott-Morton noted that unlike SEPs, "commercially essential" patents are not imbued with market power that stems from a collective decision by competitors. Rather, the power of a commercially essential patent springs only from a single innovation deployed unilaterally by its owner.[3] She went on to explain that imposing restraints on the exploitation of a commercially essential patent would be antithetical to the goal of the antitrust laws.

Transfer of F/RAND-Encumbered SEPs

The panelists generally agreed that F/RAND commitments should transfer with SEPs. Kallay said that this is the FTC's view as well, as exemplified in the N-Data consent decree.[4] When asked about transfers to patent-assertion entities ("PAEs), Stoeppelwerth said that it is important to look at the incentives of the original owner, and the potentially different incentives of the acquirer. Ramos added that the essential question is whether the purpose of the acquisition is to harm rivals. Where a PAE has relationships with companies that practice a patent, this is a factor that has to be evaluated. The panelists seemed to reach a consensus that there is so far no certain mechanism for evaluating the competitive impact of transfers of large intellectual property portfolios. When a transaction is reportable under the Hart-Scott-Rodino Act, the agencies will, of course, review it. When a transaction is not reportable, however, the panel seemed to agree that agencies in both the U.S. and EU are more likely to take a "wait and see" approach.

The Role of Standard-Setting Organizations

Kallay noted that the FTC has taken no official position on how SSOs should govern. The DOJ has, however, offered numerous suggestions for SSOs. For example, in remarks prepared for the ITU-T Patent Roundtable in October 2012, Deputy Assistant Attorney General Renata B. Hesse set forth the following suggestions for SSOs:

- "Establish procedures that seek to identify, in advance, proposed technology that involve patents that the patent holder has not agreed to license on F/RAND terms, and consciously determine whether that technology should be included in the standard";
- "Make it clear that licensing commitments made to the standards body are intended to bind both the current patent holder and subsequent purchasers, and that such commitments extend to all implementers of the standard," whether or not they are members of the SSO;
- Require licensors to offer "licensees the option to license [SEPs] on a cash-only basis and prohibit the mandatory cross-licensing of patents that are not essential to the standard or a related family of standards, while permitting voluntary cross-licensing of all patents";
- "[L]imit a patent holder's right to seek an injunction to situations where the standards implementer is unwilling to have a neutral third-party determine the appropriate F/RAND terms or is unwilling to accept the F/RAND terms approved by such a third-party";
- Take steps to lower the transaction costs of determining F/RAND terms, including "exploring setting guidelines for what constitutes a F/RAND rate or devising arbitration requirements"; and
- "Consider ways to increase certainty that patent holders believe that disclosed patents are essential to the standard after it is set."[5]

Hesse also encouraged firms to "seize the opportunity to eliminate some of the ambiguity that requires difficult ex post deciphering of the scope of a F/RAND commitment."[6] Similarly, in March 2013, DG Competition Chief Economist Kai-Uwe Kühn, Fiona Scott-Morton and Chief FTC Economist Howard Shelanski wrote a paper contending that "SSOs can substantially reduce the problem of hold-up and litigation . . . by reforming their IPR policies."[7]

Recent Developments

Since the November 2012 program, there have been a number of important developments related to SEPs.

EC Statement of Objections to Samsung on Potential Misuse of Mobile Phone SEPs

In December 2012, the EC sent a Statement of Objections to Samsung Electronics Co., Ltd., informing Samsung of its preliminary view that Samsung's seeking injunctions against Apple in various Member States on the basis of its mobile phone SEPs amounts to an abuse of a dominant position prohibited by EU antitrust rules.[8] The EC Press Release states that, "[w]hile recourse to injunctions is a possible remedy for patent infringements, such conduct may be abusive where SEPs are concerned and the potential licensee is willing to negotiate a license" on F/RAND terms.[9]

In the Matter of Motorola Mobility LLC and Google Inc.

On January 3, 2013 the FTC voted 4-1 to accept a consent agreement package designed to prevent Google from using injunctions on F/RAND-encumbered SEPs against willing licensees.[10] Under the Proposed Order, prior to seeking injunctive relief, Google and Motorola must:

- at least six months prior to pursuing injunctive relief, make a binding written offer to license that contains a full description of all material commercial terms proposed;
- at least 60 days prior to pursuing injunctive relief, make a binding written offer to use binding arbitration to establish a licensing agreement; and
- negotiate with the potential licensee for at least 6 months.

Furthermore, if a potential licensee seeks judicial relief for a F/RAND determination, Google must not seek an injunction during the pendency of the proceeding, including appeals. All licensees, whether they choose arbitration or litigation, must commit to honoring the independently determined royalty rate. Google may condition the offer to license on reciprocity (i.e., conditioning an offer to license on receiving a cross-license to the licensee's F/RAND-encumbered SEPs to the same standard), but may not require the potential licensee to license any patent claim not essential to a standard practiced by the potential licensee or to license any other patents or intellectual property.

The proposed order includes the following exceptions, permitting Google and Motorola to seek injunctive relief for alleged infringement of a F/RAND-encumbered SEP against a potential licensee who:

- is outside the jurisdiction of the U.S. District Courts;
- has stated in writing or sworn testimony that it will not license the SEP on any terms;
- refuses to enter a license agreement covering the SEP on terms that have been set in the final ruling of a court or through binding arbitration;
- fails to provide the written confirmation as requested by Google in a F/RAND Terms Letter (a binding irrevocable commitment to cross-license F/RAND Patents on F/RAND terms) within thirty days of receiving the letter; or
- is seeking injunctive relief against Google based on infringement of the potential licensee's F/RAND-encumbered SEP.

DOJ and USPTO Joint Policy Statement on Remedies for F/RAND-Encumbered SEPs

On January 8, 2013, the DOJ and the USPTO issued a joint policy statement on the availability of injunctive relief for F/RAND-encumbered SEPs in judicial proceedings under section 337 of the Tariff Act of 1930.[11] The statement contends that, "[i]n some circumstances, the remedy of an injunction or exclusion order may be inconsistent with the public interest. This concern is particularly acute in cases where an exclusion order based on a F/RAND-encumbered patent appears to be incompatible with the terms of a patent holder's existing F/RAND licensing commitment to an SDO [standard setting organization].[12]

The DOJ and USPTO urged the International Trade Commission ("USITC") to consider whether a patent holder has acknowledged voluntarily through a commitment to license its patents on F/RAND terms that money damages, rather than injunctive or exclusionary relief, is the appropriate remedy for infringement.[13] The statement further recommends that "it may be appropriate for the USITC, as it has done for other reasons in the past, to delay the effective date of an exclusion order for a limited period of time to provide parties the opportunity to conclude a F/RAND license."[14] Importantly, the Statement submits that an exclusion order may be an appropriate remedy in some circumstances, "such as where the putative licensee is unable or refuses to take a F/RAND license and is acting outside the scope of the patent holder's commitment to license on F/RAND terms."[15]

Microsoft Corp. v. Motorola, Inc.

On April 19, 2013, U.S. District Court Judge James Robart became the first U.S. judge to determine a RAND royalty rate and range for SEPs in a dispute between Microsoft Corp. and Motorola, Inc. The court adopted a modified-version of the *Georgia-Pacific* factors to recreate a hypothetical negotiation between the parties. The court determined that "the parties in a hypothetical negotiation would set RAND royalty rates by looking at the importance of the SEPs to the standard and the importance of the standard and the SEPs to the products at issue."[16] The court further stated that "a proper methodology for determining a RAND-royalty should address the risk of royalty-stacking by considering the aggregate royalties that would apply if other SEP holders made royalty demands of the implementer."[17] Furthermore, "a RAND commitment should be interpreted to limit a patent holder to a reasonable royalty on the economic value of its patented technology itself, apart from the value associated with incorporation of the patented technology into the standard."[18] Lastly, the court held that, "[d]espite concerns with using a pool rate as the *de facto* RAND royalty rate, the court concludes that under certain circumstances, patent pools can serve as indicators of a royalty rate that falls within the range of royalties consistent with the RAND commitment."[19]

Motorola contended that it was entitled to a royalty rate of 2.25% of the net selling price of Microsoft's Windows and Xbox products for both its H.264 and 802.11 SEP portfolios. Microsoft contended that the MPEG LA H.264 patent pool was the best indicator of a RAND royalty rate for Motorola's H.264 SEPs. The court concluded that certainof Motorola's patents contributed little to the standards and played only minor importance in the overall functionality of Microsoft's Xbox. Although the court agreed "as a general matter that patent pools tend to produce lower rates than those that could be achieved through bilateral negotiation," the court nevertheless found that "the MPEG LA H.264 patent pool is an indicator of a RAND royalty rate" for Motorola's SEPs.[20] Taking all of these factors into account, the court settled on a RAND rate of 0.555 cents per unit for Motorola's H.264 SEPs, and 3.471 cents per unit for Motorola's 802.11 SEPs.

Conclusion

The DOJ, FTC, and EC are active in the area of SEPs and have expressed the intention to remain that way. In addition to monitoring the agencies, practitioners should pay close attention to SEP-related litigation both in the U.S. and abroad, as court decisions are also likely to have an important impact on policy in this area.

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* Ms. Kallay was speaking on her own behalf, not for the FTC or any commissioner.

1 FTC Decision and Order (Nov. 26, 2012), *available at* www.ftc.gov/os/caselist/1210081/121126boschdo.pdf.

2 Scott-Morton Speech, *The Role of Standards in the Current Patent Wars*, at 6 (Dec. 5, 2012), *available at* www.justice.gov/atr/public/speeches/289708.pdf.

3 *Id.* at 5-6.

4 Decision and Order, *In the Matter of Negotiated Data Solutions LLC* (Sept. 22, 2008), *available at* www.ftc.gov/os/caselist/0510094/080923ndsdo.pdf.

5 Renata B. Hesse, Six "Small" Proposals for SSOs Before Lunch, Remarks as Prepared for the ITU-T Patent Roundtable, at 9-10 (Oct. 10, 2012), *available at* articles.law360.s3.amazonaws.com/0385000/385506/ITU%20- %20Six%20Small%20Proposals%20for %20SSOs%20Before%20Lunch.pdf.

6 *Id.* at 11. Another example is a recent speech by former Acting Assistant Attorney General Joseph Wayland, *Antitrust Policy in the Information Age: Protecting Innovation and Competition* (Sept. 21, 2012), *available at* www.justice.gov/atr/public/speeches/287215.pdf.

7 Kai-Uwe Kühn, Fiona Scott Morton, and Howard Shelanski, *Standard Setting Organizations Can Help Solve the Standard Essential Patent Licensing Problem*, CPI (March 2013), at 1, *available at* www.competitionpolicyinternational.com/assets/Free/ScottMortonetalMar-13Special.pdf.

8 EC Press Release, *Antitrust: Commission sends Statement of Objections to Samsung on potential misuse of mobile phone standard-essential patents* (Dec. 21, 2012), *available at* europa.eu/rapid/press-release_IP-12-1448_en.htm.

9 *Id.*

10 FTC Decision and Order, *available at* www.ftc.gov/os/caselist/1210120/130103googlemotorolado.pdf.

11 DOJ-USPTO, *Policy Statement on Remedies for Standard-Essential Patents Subject to Voluntary F/RAND Commitments* (Jan. 8, 2013), *available at* www.justice.gov/atr/public/guidelines/290994.pdf.

12 *Id.* at 6.

13 *Id.* at 9.

14 *Id.* at 10.

15 *Id.* at 7.

16 Findings of Fact and Conclusions of Law at 7.

17 *Id.* at 25.

18 *Id.* at 25-26.

19 *Id.* at 164.

20 *Id.* at 160, 164.