NOKIA

European Commission Workshop on IPR in ICT Standardisation
Brussels, 19 November 2008

FRAND Best Practice

Tim Frain, Director IPR Regulatory Affairs, Nokia Corporation

I would like to start by thanking the Commission for organising this Workshop, and for the opportunity to speak today.

If we go back to first principles, the FRAND commitment is fundamentally about ensuring access to patented technology in standards and avoiding anti-competitive effects. Specifically, owners of essential patents promise that licences will be available, subject to reciprocity, on fair, reasonable and non-discriminatory (i.e. FRAND) terms.

To be fully effective, a FRAND commitment has to be both meaningful and binding. So, it would not make sense if it was possible for an essential patent owner to obtain an injunction against anyone prepared to take a licence on FRAND terms, or if the FRAND commitment evaporated when ownership of the patent changes. If you will pardon the pun, we are talking about a 'FRAND' for life!

Earlier, when there were far fewer essential patents and patent owners than there are today, the focus was predominantly on the individual FRAND commitment.

But, as the number of essential patents and patent owners has mushroomed dramatically over the years, especially in the telecoms sector, attention has been shifting to the issue of cumulative - or total - royalty costs, meaning the overall price paid for all necessary patent licences. Nowadays there may well be many hundreds, possibly thousands of patents and tens of patent owners. There are now over 19,000 patents, and around 150 companies in the ETSI database. By any standards this represents a complex licensing scenario.

The question is how to bring more transparency and predictability to the overall royalty price tag, early in the standardisation process, so that both prospective investors and innovators can make a more informed decision about which technology path to pursue.

The challenge is two-fold. On the one hand, there is a need to ensure the **total** royalty costs remains reasonable. And by "reasonable" I mean commercially viable. Commercial viability is the yardstick by which we can say if the cumulative royalties are reasonable or not. On the other hand, to promote technology innovation, it is important that **individual** patent owners get a fair slice of the overall royalty pie, without reaping additional value *merely* because their technology is adopted as mandatory in the standard.

One approach in particular has received a lot of attention and interest recently, and that is ex-ante disclosure of licence terms, meaning that patent owners disclose at least their most restrictive financial terms before a standard is set.

Advocates of "ex-ante" believe it would promote competition not only in the technology, but also on price. Once thought to have been a "no-go" area because of anti-trust concerns, competition authorities in US and EU are increasingly signalling that "ex-ante" is not in itself anti-competitive and may even be pro-competitive.

So, for example, ex-ante disclosure of licence terms may be useful in a standard setting context where the technology is limited scope, and static, and the patent ownership profile is known or predictable and relatively stable.

But the telecoms environment is characterised by complex, dynamic standards having broad technical scope and long evolution cycles over many years. At the outset there is little more than a crude road map. The complex patchwork of technology components still has to be developed. A vast number of technical contributions will be made each year. In 3GPP, for example, tens of thousands of technical documents are submitted each year. Many contributions will include patented elements. No-one can be sure what the ultimate technology will be, who will be the key innovators and technology contributors, or even what the eventual products will look like. It is impossible to predict what the eventual ownership profile of essential patents will look like. In short, it is too early for prospective patent owners to put a meaningful price tag on the technology.

So, does ex-ante disclosure of licence terms help in this scenario? Well, we do have a very recent experience to draw on. Within the last year many stakeholders disclosed their royalty rates for future mobile technologies. It was a confidential process, to minimise competition concerns, so I cannot be too specific about the results. Suffice it to say the cumulative figure was off the scale with regard to anything that could sensibly be regarded as commercially viable. I leave you to guess which end of the scale I am talking about.

What we realised is that ex-ante disclosure of licence terms in complex, early-stage telecoms standards can actually back-fire, and end up being somewhat counter-productive, as it may risk undermining commercial confidence in the emerging technologies concerned. Any concerted effort to try and adjust the result, for example by encouraging stakeholders to reduce their individual rates, would run the risk of violating competition rules, for example as a buyers cartel.

A drawback is that ex-ante disclosure of licence terms does not in itself guarantee a FRAND outcome ex post.

So, the ex-ante process needs to be complemented by other measures to ensure that both individual rates are FRAND-compliant, and cumulative rates are reasonable.

Specifically, we can look to current FRAND best practice, and what a number of key players have called the “prevalent industry principles of FRAND[1]”.

It is quite simple, patent owners who make a FRAND commitment, also make a commitment - **an ex-ante commitment** - to a framework in which the maximum aggregate licensing costs are reasonable, and their own individual royalty claims will not exceed the proportional contribution they make to the patented technology in the standard. In other words, if the individual claims are all reasonable and do not grow disproportionately, the overall royalty pie will remain controllable and stay within reasonable bounds, so ensuring commercially viability.

This might be called the Industry Royalty Pie model, and the two component principles are often referred to as Aggregated Reasonable Terms and Proportionality (or ART and P for short).

We have seen important manifestations of this FRAND best practice in the field. In spring this year, frustrated by the ex-ante experience I mentioned before, seven companies voluntarily made a joint ex-ante public announcement of their commitment to the Industry Royalty Pie model. They also gave ball-park figures for the reasonable maximum aggregate royalty levels for so-called Long Term Evolution (LTE), i.e. next generation mobile technology platforms. Specifically they indicated single-digit percentages for handsets.

Since then several companies, including Nokia, have unilaterally and voluntarily elaborated their FRAND positions based on ART and P on their corporate websites for all to see. The formulation is different in each case, but they each provide greater transparency as to both individual and cumulative royalty rates, based on the Industry Royalty Pie model.

[1] Joint Press Release, 14 April 2008, by Alcatel-Lucent, Ericsson, NEC, NextWave Wireless, Nokia, Nokia Siemens Networks, and Sony Ericsson.

It is important to understand that ART is not any kind of royalty cap. It does not involve or imply any collusion whatsoever. It is no more than an individual patent owner's own understanding or articulation of what a reasonable cumulative royalty would be given all the market conditions. Also, Proportionality is not simply about patent counting, but reflects the respective contributions made. Actual royalties remain to be negotiated bilaterally in the normal way.

This example of FRAND best practice complements ex-ante disclosure of licence terms to provide a significantly more powerful and robust mechanism for achieving predictable and reasonable licensing costs at both the individual and cumulative level.

Even if patent owners do not publicly disclose their individual royalty rates, an ex-ante commitment to ART and P is itself an extremely valuable tool in guaranteeing that individual and cumulative royalties remain reasonable and commercially viable. You only have to look at the joint press release in April.

To sum up, let me say that, in our view, FRAND policies are not delivering the desired results in the telecoms area because they are open to bad practice. Corrective action is needed. Wider unilateral commitment to the principles of ART + P based on industry best practice will help and may even to lead to changes in the IPR policies of standardisation bodies, but if that does not happen the regulator may have to step in.

The more we can encourage patent owners to articulate an ex-ante commitment to the Industry Royalty Pie Model, with or without disclosing their individual licensing terms, the more predictability we will have of overall licensing costs, for the benefit of the entire industry, without undermining the reasonable entitlement of individual patent owners.

I and my colleagues in Nokia are at the disposal of the Commission and all stakeholders to answer any questions and discuss the ideas presented here in more detail.