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Wragge & Co is a UK-headquartered international law firm providing a full service to clients worldwide. Formed in Birmingham in 1834, the firm now has 125 partners and more than 580 fee earners operating from offices in Birmingham, Brussels, Guangzhou, London, Munich and Paris.

Many Wragge & Co teams are acknowledged to be among the best in the UK. Highly-rated teams include projects, commercial contracts, outsourcing, pensions, employment, retail and intellectual property. Each of the team's lawyers has experience advising on large, high-value and complex projects and challenging commercial issues for clients in the public and private sectors.

The firm also has 17 specialist and dedicated sector teams, including aerospace, automotive, food and drink, healthcare, retail and public sector. Wragge & Co is ranked 6th in the list of commercial advisers to the FTSE 250. Clients include Birds Eye, HJ Heinz, CB Richard Ellis, GlaxoSmithKline, Teva, Cookson Group, SMMT, BP and British Airways.

Competition

The competition team's expertise includes Competition Commission enquiries (both sectoral and mergers); joint venture arrangements (R&D, production and distribution); IP licensing; exhaustion of rights and other free movement issues; abuse of a dominant position, especially with respect to pricing; distribution arrangements; regulatory issues arising under EU law; carrying out of compliance audits and drafting compliance programmes; public procurement law and state aid and merger control.

Intellectual Property

With a team of 36 lawyers, the Intellectual Property (IP) team is one of the largest dedicated IP practices and is known for its creative thinking, thought leadership and commercially oriented approach.

The IP team continues to build long standing relationships with some of the world's biggest companies - including British Airways, BP, Unilever, Dyson and Microsoft, Birds Eye, Camelot, Mothercare, Early Learning Centre, AstraZeneca, Marks and Spencer and Eisai on clearance, exploitation and enforcement of their IP rights

The team divides itself along sector lines - advertising and marketing, brand protection (including franchising), high tech and life sciences.

25 June 2010

Draft Communication from the Commission

Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements

Wragge & Co submissions

- 1.1 The European Commission has long regarded European standards as a means to eliminate barriers to trade. (See for instance, its 1990 Green Paper on the development of European Standardisation (COM (90) 456 Final (the “1990 Green Paper”), where the Commission stated that: “... *the single Community market will become a reality for European industry only insofar as common technical standards can be developed progressively at European rather than national level.*”)
- 1.2 The issue of standardisation and the interface with intellectual property rights (“IPRs”) come particularly to the fore in “networks markets” such as telecommunications - where both competitors and consumers benefit from interoperability and the ability to exchange information with those who use the same standard. As the Commission stated in the 1990 Green Paper: “*the main motive for promoting standardisation is economic ... to reduce costs for producers and improve the transparency of the market for consumers*”.
- 1.3 Wragge & Co believes that Section 7 “Standardisation Agreements” of the draft Guidelines could be improved in order to avoid compromising the EU standard setting regime that has been put in place over many years. Wragge & Co believes that it is important not to insert an industrial policy in relation to network industries into non-binding ‘Guidelines’ that are concerned with restrictive agreements.
- 1.4 In so doing, the Commission also conflates issues of Article 101 TFEU which addresses multilateral conduct and Article 102 TFEU which is concerned with unilateral conduct. This is not a semantic distinction. If it is the case that a single member of a Standard Setting Organisation (“SSO”) acts in bad faith and, notwithstanding a “FRAND” declaration, does not honour that declaration, is the legitimacy of the SSO and its procedures called into question - or to what extent - and where is the dividing line? And what are the consequences for the SSO and its other members?
- 1.5 The Commission appears to justify its approach on the basis that it is the very standardisation agreement that results in adoption of an IPR, or bundle of IPRs which ‘read onto’ a standard, that conveys market power to an extent that confers dominance on that IPR. “*However, irrespective of the market positioning of the different IPR holders, establishment of standards, which might take years to complete, can create or increase the market power of those IPR holders and in some circumstances, lead to abuses of a*

dominant position” (para 275 to the draft Guidelines) and “*An abuse of the market power gained by virtue of the IPR being included in a standard constitutes an infringement of Article 102*” para 284 to the draft Guidelines). Therefore, it appears the reasoning goes, principles of Article 102 TFEU may be applied to such agreements, appointing as they do proprietors of IPRs to dominant positions. Further, the argument seems to go, the proprietors of dominant positions have every incentive to abuse that dominant position. This appears to justify introduction of a policy (albeit in a set of Guidelines) which introduces effective compulsory licensing; and deprives an IPR owner of its fundamental entitlement to extract a proper rent from its proprietary interest. Thus, the draft Guidelines provide:

“The IPR policy should also require that all holders of essential IPR in technology which may be adopted as part of a standard provide an irrevocable commitment in writing to license their IPR to all third parties on fair and reasonable and non-discriminatory terms (“FRAND commitments”).para 282 to the draft Guidelines

- 1.6 This analysis erroneously assumes that where an IPR is included in a standard this will necessarily give its owner market power and place it in a dominant position. It is also simply quite wrong as a matter of law. Whether this is so will vary from market to market. Some markets, such as the mobile telephony market(s) are characterised by monopsonistic purchasers, where it is common practice for would-be licensees not to seek to pay royalties to IPR holders, but to engage in a war of attrition with IPR holders, on a multi-jurisdictional basis, challenging the IPRs in question, inter alia, as part of a negotiation tactic. In those circumstances a small innovator company holding a number of IPRs has very little market power.
- 2 Guidelines on Article 101 TFEU fail to give guidance as to where there will be an appreciable effect on competition.**
 - 2.1 The premises which the draft Guidelines set out as where the prohibition of Article 101(1)TFEU will be met are not concerned with the common orthodoxy that an appreciable effect on competition on a relevant market be established; rather they appear to be concerned to introduce an industrial policy (based on a flawed premise, as explored above).
 - 2.2 The draft Guidelines, at para. 276 appear to set conditions for when the prohibition of Article 101(1) TFEU will or will not be met: “*In the light of the above, the following paragraphs set out the conditions in which standard-setting agreements fall outside the scope of Article 101(1).*” The draft Guidelines then go on to state that: “*It is not necessary for standard-setting agreements to fulfil these conditions, but normally they will be sufficient to avoid the application of Article 101.*”
 - 2.3 Therefore, these conditions are not the only basis upon which the prohibition of Article 101(1) TFEU will not be met. However, the Guidelines give no guidance as what other analysis should be conducted as a matter of regular competition law to establish an appreciable effect on competition, a *sine qua non* for the application of Art 101 TFEU. The

Commission appears only concerned to assist SSOs insofar as they adopt the conditions enumerated in the draft Guidelines.

3 The Commission has an insufficient body of decisional practice to justify the introduction of conditions for non-application of the prohibition of Article 101(1)TFEU to standardisation agreements

3.1 The Commission has not established a theory of harm to justify the departure from established practice. More specifically, it has failed to iterate, let alone establish by means of a body of decisional practice, that IPRs are being systematically abused in the context of standardisation arrangements and the public harm that would result therefrom.

3.2 Wragge & Co takes issue with the Commission statement in its 'Frequently Asked Questions' dated 4 May 2010 accompanying the publication of the draft Guidelines where it states that *"the revision of the standardisation chapter - drawing on recent case related experience in the field - aims at ensuring that standards are set in such a way that the specific benefits of standard-setting are realised and passed on to European consumers."* (MEMO/10/163)

3.3 Notwithstanding this, it is telling that there are no cross references in the relevant parts of the Guidelines to any body of decisional practice, other than references to a limited body of case law concerning abuse of a dominant position pursuant to Article 102 TFEU.

3.4 The Commission to date has had a limited number of investigations in the area of the exploitation of IPRs in the context of standards - most recently notably Rambus; Qualcomm; and IPCOM. None of them was subject to the checks and balances inherent in the adoption of a Commission decision or subject to judicial scrutiny. Arguably, given that litigation was also taking place in parallel with the cases in question, it is questionable whether the complaints were made to advance specific commercial interests that could ordinarily have been worked out in national courts and/or by means of ordinary commercial negotiation. If these complaints have been made with respect to any other sector and in different contexts, would the Commission have dismissed such complaints on the basis that they did not fall within the Commission's priority criteria for enforcement?

3.5 There is a danger that the Commission is disturbing a long established dynamic for a limited number of "hard" cases, which were ultimately 'not proven'.

4 The proposed approach compromises the proper working of SSOs where the technology in question is IPR 'rich'

4.1 The Commission is no doubt aware of the evolution of standards setting within the EU, notably in the context of telecommunications. Wragge & Co is concerned that the draft Guidelines are based on insufficient analysis or consultation of stakeholders in the process. This can only be to the detriment of standardisation in the EU.

4.2 In 1984, when the EC decided on the "New Approach" to standardisation, standard-setting had up to that time been a cumbersome and slow process - for example, there was a need

for unanimity in decisions made by organisations such as CEN and CENELEC, and there was a lack of cohesion between harmonisation and the European standardisation process.

- 4.3 Since the advent of the new approach the European standards bodies, CEN, CENELEC and ETSI, have successfully promulgated standards which include, relevant for present purposes, voluntary standards or “technical specifications”. Again, within the context of telecommunications, there is the lauded success of the adoption by ETSI of GSM, which introduced a digital cellular technology to replace a multitude of incompatible analogue systems in Europe. The SIM card which is one of the keys to GSM's success is now an essential component of all the leading mobile communications systems.
- 4.4 Carefully worked out and negotiated within the context of this ‘edifice’ for the promulgation of pan-European standards was, what the Commission labelled at the time, the ‘partnership’ of IPRs and standards (see the Commission’s Communication - *Intellectual Property Rights and Standardisation* COM 92 (445)). That balance finds its expression in the ETSI IPR Policy where, from its inception care was taken to guard against the possibility of so-called ‘hold-up’; while at the same time having regard to the legitimate interests of IPR holders. The current iteration of the ETSI IPR policy (as found in Annex 6 to the ETSI Rules of Procedure dated 26 November 2008) contains a number of aspects that are fundamental to the timely and efficient creation of standards in a manner that maintains an inclusiveness that does not favour one class of proprietors of IPRs over others to the detriment of the promotion of world class standards.
- 4.5 Fundamental to that is that it is not mandatory for ETSI participants to provide a FRAND undertaking. This tack was tried in back in 1982, where the first iteration of the IPR Policy contained a compulsory licensing obligation whereby the proprietor of an ‘essential’ IPR would be required to license on reasonable terms. This approach was considered to favour the incumbent Public Network Operators, who had limited R&D budgets, yet also had a large appetite for IPRs.
- 4.6 The danger of this approach was also recognised by the Commission at the time: “*Although it could be argued that consumers would benefit in the short term if IPRs were compulsively licensed to serve as the basis of standards, in the long term, investment in R&D would dry up within the Community*” (emphasis added) [CEC COM (92) 445 final]. That concern is probably an even more pressing concern now than it was then.
- 4.7 Despite this controversy, an interim policy was adopted by ETSI's General Assembly on 18 March 1993 which was subject to some opposition, plus a complaint to the Commission to the effect that the IPR Policy would effectively be a system of compulsory licensing and amount to an infringement of (the then) Articles 81 and 82 EC. Before awaiting the outcome of that complaint, ETSI abandoned the policy.
- 5 **There remains no justification for what is effectively a compulsory licence**
 - 5.1 It remains the case that compulsory licensing of this nature is also contrary to the case law of the Community courts, which have established that a ‘duty to deal’ exists in ‘*exceptional circumstances*’ of abuse of a dominant position (See *Magill and Microsoft*). It is not clear

also why the Commission has altered its earlier position in considering that adoption by SSOs of a compulsory licensing policy will improve the standard setting process and enhance economic progress.

6 The law of unintended consequences

6.1 We note that the Commission recognise the different business models that proprietors of IPRs have in the context of standard agreements (see paragraphs 271-274 to the Guidelines) That being so, it is all the more incumbent on the Commission not to introduce Guidelines that will have the effect of destabilising the current status quo and which risks favouring one business model over another, to the possible detriment of being open to new business models and the timely introduction of innovative products into the EU market place.

6.2 In that context, the ‘conditions’ that the draft Guidelines set out for non-application are again relevant:

“The IPR policy should also require that all holders of essential IPR in technology which may be adopted as part of a standard provide an irrevocable commitment in writing to license their IPR to all third parties on fair and reasonable and non-discriminatory terms (“FRAND commitments”). (emphasis added). para 282 to the draft Guidelines

6.3 Wragge & Co takes issue with the use of the word ‘irrevocable’. As noted above, it is not uncommon for a small patent right holder (e.g., a SME such as a research entity/university, with limited funds) to be faced by a monopsonist would-be licensee who will not negotiate. Were that licensee to behave utterly unreasonably, wilfully increasing the costs of that SME, perhaps by challenging the validity of the IPRs in question in a number of jurisdictions, that SME would nonetheless still be obliged (even if that licensee had exhausted all of the SMEs funds on unwarranted litigation) to honour its FRAND commitment. It would be required to offer the same terms to that licensee, possibly after years of litigation, as those it had offered years ago to other more reasonable licensees.

6.4 Moreover, it would find that it would have compromised the entirety of its portfolio that it had made available to the SSO, irrespective of whether the SSO had not adopted any of its IPRs.

6.5 A further disincentive to engage in an SSO which would comply with the draft Guidelines relates to the possibility of injunctive relief. As the Commission is doubtless aware, some parties argue that a binding commitment to offer FRAND terms necessarily means that the IPR holder waives its rights to seek injunctive relief. As noted above, SMEs will not have the resources when faced with a monopsonist purchaser of technology to engage in long drawn out litigation that will take place on a multi-jurisdictional basis. The possibility of injunctive relief does at least level the playing field to a degree.

6.6 More generally, a prescriptive undertaking of this nature risks creating two classes of patent rights - ones where the rights holder is entitled to a proper return from licensees, and ones where its bargaining position vis à vis licensees is compromised. This approach

risks innovators, especially ones with limited funds, opting to stay outside the standard setting process in order to be assured of a proper return.

7 Confusion of SSOs with patent pools

7.1 The draft Guidelines appear to confuse patent pools with SSOs, as follows:

“The inclusion in a standard of substitute technologies (i.e., technology which is regarded by users/licensees as interchangeable with or substitutable for another technology, by reason of the technologies’ characteristics and intended use and which could, in the present context, be adopted in an alternative standard) may limit inter-technology competition. Where a standard is composed of substitute technologies, the arrangement can in practice amount to foreclosure of competitors by excluding one potentially competing alternative technology from being included in a different standard. As a general rule, the inclusion of substitute technologies in a standard is likely to give rise to restrictive effects on competition within the meaning of Article 101(1).

7.2 If there are a number of functional alternatives as part of an overall technical solution, there is no reason why functional alternatives could not be adopted within the context of a standard. This is commonly found in, for example, the mobile telephony field where solutions to a particular problem can be selected from two or more options, without compromising the interoperability of the overall system.

7.3 It is well-established that, in the context of patent pools, which will be implementing a standard that already exists, the combining of complementary patents is desirable - but the joint sale of substitute patents will result in licensees paying for technologies that they do not need, or in elevated royalties. (See paras 215 et seq to the Commission guidelines on technology transfer agreements:- ‘*When technologies in a pool are substitutes, royalties are likely to be higher than they would otherwise be, because licensees do not benefit from rivalry between the technologies in question*’).

7.4 That is not the case with SSOs which are very different animals to patent pools. In the context of an SSO, the licensed IPRs are not subject to a single offer but is the subject of separate negotiations between market players. It may be the case that, where an SSO has formulated a standard that comprises ‘essential’ non-substitute technology, a patent pool may evolve from members of the SSO. This is only likely to happen where the quality and value of the technology in question have become clearer. In the alternative, it may be that a number of participants in a standard elect to license their essential patents jointly (see, for example, Case No.IV/C-3/36.849 [MPEG-2 Licensing Programme](#)).

8 Ex ante disclosure of licensing terms

8.1 The draft Guidelines depart also from the orthodox approach where they state:

“To take a notable example, if standard-setting organisations provide for ex ante disclosures of most restrictive licensing terms, this will not (subject to the caveat set out above) lead to a restriction of competition within Article 101(1). In this regard, it is important that parties involved in the selection of a standard be fully informed not only as to the available technical options and the associated IPR, but also as to the likely cost of that IPR.”

- 8.2 It is unworkable for SSOs to engage in arbitrage of terms when selecting technology for inclusion in a standard. The draft Guidelines again are misguided as to the nature of an SSO, which will be considering the merits of anticipatory technology to facilitate an emerging technology. Any thinking as to terms of access will be premature. An SSO is focussed on technical outcomes - its primary aim is to design the best possible standard, and it will not be concerned with licensing issues; save to ensure that essential technology is made available on FRAND terms. Moreover, it is technical personnel who participate in SSOs, not legal or business personnel and the focus is also (quite rightly) on selecting the optimum technology.
- 8.3 It is wrong to assume that price considerations will result in a more optimum public benefit. It is more likely to reinforce the position of vested interests, as incumbent players may have deeper pockets to ‘buy’ their way into a standard, with what may be poorer technology.
- 8.4 SSOs do not have the secretariats to engage in the collective purchasing that the Commission is advocating in its draft Guidelines. Further, such collective purchasing is likely to result in an unfair result for smaller players, who may not be properly rewarded for bringing forward innovatory technology.
- 8.5 The Commission is also overlooking the multiplicity of IPRs that can be engaged in a particular standard, held by a multiplicity of parties. It would be a logistical impossibility to deliver standards for emerging technology on a timely basis, if the participants were engaged in a selection on price.
- 9 Commission Guidelines are not the appropriate instrument to opine as to the meaning of FRAND**
- 9.1 It is unhelpful for the Commission to speculate what FRAND should be in view of the extent of national litigation on this issue. This is all the more so where it is erroneously reading over on a ‘per se’ basis the assumption of market power to a proprietor of an IPR that reads onto a standard. To date, there is no clear view or judicial practice on this and any speculation as to what it may be in a Commission document is as likely to confuse as to illuminate.

For further information, contact:

Bernardine Adkins, partner, 00 44 (0)870 733 0649, Bernardine_adkins@wragge.com

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