

## **ECIS' statement on *ex-ante* disclosure of licensing conditions for essential IPR**

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ECIS finds that the European Commission has recently taken steps for important changes in information and communications technology (ICT) designed to make it quicker and easier for businesses and individuals to obtain government services, benefits, and documents across the European Union. We believe these positive steps will foster new freedom of movement by its citizens, and new opportunities for businesses. Recently, in December 2010, the Commission approved the Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union ("TFEU") to horizontal co-operation agreements ("Horizontal Guidelines"), which lay out a comprehensive approach with respect to the conformity of standardisation agreements with Article 101 TFEU, and in particular provide detailed guidance on *ex-ante* disclosure of IPR, as well as the *ex-ante* disclosure of the most restrictive licensing terms (maximum royalty rates).

ECIS in general finds the *ex-ante* disclosure of IPRs and of the most restrictive licensing terms to be useful in the context of software standard setting. We believe however that encouraging *ex ante* disclosure needs to be accompanied by a Commission statement that participants in important standard-setting agreements are required by EU competition rules, and not merely by the rules of the standards organisation, to provide licences on FRAND terms (which can also be royalty-free terms, as the Horizontal Guidelines provide). On the other hand, in complex technology areas such as mobile telecommunications networks and computer hardware, the *ex-ante* declaration of excessive royalty claims can be entirely counter-productive, and the *ex-ante* disclosure of such terms may lead to excessive cumulative royalties.

### **A. The *ex-ante* disclosure of licensing conditions for essential IPR in the software sector**

More particularly, in the **software sector**, *ex-ante* disclosure of specific IPR and of licensing terms can have positive effects, due to the characteristics of the industry. *Ex-ante* policies can have significant pro-competitive effects as they are good for both consumers and businesses. They increase transparency and reduce uncertainty, allow informed business decision-making, and avoid hold-up resulting in lower costs for consumers. This is the case because in the software industry, in contrast to the telecoms sector, there are generally fewer players holding IPRs relevant to the standard; product lifecycles are short (two years or less); innovation often proceeds through incremental development of standards-compliant products; many if not all hard IPRs – *i.e.*, patents – can be developed around since alternative equally functional solutions generally exist; and IPR holders are amply rewarded if their technology is adopted for the standard through their lead time to market with a compliant implementation and the strong network effects that are often prevalent in the software sector. Thus, IPR holders generally show a willingness to license on a royalty free basis, with royalty-free FRAND licensing being the prevalent form of FRAND licensing. Examples of successful IPR-free or royalty-free

policies adopted by standards setting bodies include the ones adopted by W3C and OASIS, whose standards are widely used nowadays. In addition, in the software sector, there are limited costs associated with bringing the products into the market.

As a result, standards bodies in this sector benefit from *ex-ante* disclosures of specific essential patents and key patent terms as a means of making an informed choice of technologies, identifying the need for design-arounds and avoiding patent ambushes. In royalty-free FRAND-based standardisation efforts, the need for specific *ex-ante* declarations of IPR is eliminated because no royalties are required. Nonetheless, even in this context, it may be important to have the IPR holder identify essential IPR at the earliest stage if possible, as other terms than royalty terms may be of great importance to the definition of the standard or to the possibility for implementation of the standard by open source software developers. In these circumstances, *ex-ante* disclosure of licensing terms and conditions, and of commitments to reasonable and non-discriminatory terms, before any software standard is adopted, can help avoid patent hold ups.

**The VITA and IEEE *ex-ante* policies.** Examples of successful *ex-ante* policies adopted by standards-setting bodies include those adopted by VITA and IEEE in 2007.

The VITA policy addressed significant delay in adoption of VITA standards due to high royalty demands by participants for disclosed EPs under RAND policy. Under the VITA policy, each working group member is required to disclose their known essential patents, including patent applications, maximum royalty, and most restrictive license terms. This allows each SSO member to compare the most restrictive licensing terms associated with each alternative technology, when deciding which technology to support for inclusion in the draft specification. Disclosure of this information, enforced by the requirements that intentionally non-disclosed patents be licensed by royalty-free, permits VITA members to make more informed decisions when setting a VITA standard. The successful results to date of the VITA policy can be summarised in the following points:

- Development speed up 20%;
- SSO Membership up 10 – 15 %;
- 7 disclosures from VITA participants: all with DLAs;
- No participant patents asserted without disclosure during development.

Moreover, under the IEEE-SA policy, a member may disclose its maximum royalty terms and most restrictive licensing terms for patent claims that might be essential. The IEEE policy also provides that under limited circumstances working group members may discuss the relative costs and benefits for proposed competing patent technologies that are proposed for inclusion in an IEEE standard. Finally, the policy specifies the licensing commitments given by companies whose representatives participate in IEEE standards development are intended to bind affiliates (unless excluded) and successor transferees of the patented technologies.

## **B. The *ex-ante* disclosure of licensing conditions for essential IPR in the telecoms and computer hardware industry**

On the other hand, in **telecoms and computer hardware**, there are long evolution cycles, many patents and many patent owners. As noted before, *ex-ante* declaration of specific IPR in

this context can be entirely counterproductive. The number of essential patents is often very significant, and it often takes years from the adoption of the standard to the marketing of the products based on the standards, as a result of which *ex-ante* identification of specific patents may be impractical.

When it comes to the *ex-ante* disclosure of licensing terms in the area of telecoms, actual experience with *ex-ante* declarations in the sector confirms that IPR owners that make those statements have an incentive to declare high *ex-ante* royalties – well above the actual *ex-ante* value (which is the incremental value for the licensee over the next best alternative) – in order to maximise their share of the total royalties, even if this results in an excessive and prohibitive cumulative royalty stack. Moreover, they have no incentive to lower the declared rate, because they would create room for the last IPR owner to hold out (the last one not to lower the rate) to reap a disproportionate royalty. An *ex-ante* declaration in this context is at most an opening bid for negotiations or an auction, which by definition will be higher than the reasonable rate that is the end result of negotiations or an auction. As a result, relying on *ex-ante* declarations risks completely undermining the objective of FRAND arrangements and would be totally counterproductive.

***The "ex-ante plus" approach.*** On the contrary, it would be more effective to enable IPR holders to disclose unilaterally what they regard as the maximum commercially viable aggregate rate for a given standard, rather than merely disclosing each patent holder's individual rates. This approach is also known as "*ex-ante plus*," and is considered to be a more nuanced approach to classical *ex-ante*. Disclosure under the "*ex-ante plus*" model would be entirely unilateral and does not involve or imply any collusion whatsoever. It is no more than each patent owner articulating its own view of what a reasonable cumulative royalty would be. Actual royalties remain to be negotiated bilaterally in the normal way. More specifically, the purpose of this model would be to ensure that individual royalty rates are in principle proportionate to the respective contribution each patent owner brings. According to this system, owners of intellectual property should be required to offer a standard FRAND licence for their essential patents for each category of licensee, at a reasonable royalty rate, free of any non-assertion provisions and grant-backs. Owners of intellectual property could require reciprocal licensing of any essential patents on FRAND terms by any licensee to its essential patents. Intellectual property owners could then engage in negotiations with any given licensee over other provisions such as cross-licensing terms or non-assertion provisions, so long as the intellectual property owners' FRAND offers remain available to licensees (the "Shapiro System").

***Joint negotiations or discussion of licensing terms.*** Furthermore, it is important to ensure that joint negotiations or discussion of licensing terms, in particular royalty rates, can take place under clearly defined conditions. Unilateral disclosures should not be prohibited under EU competition rules, because they merely enable the standard setting organisations and their members to estimate the maximum potential cost of a choice of an individual technology. But circumstances will arise in which multilateral negotiations between balanced and comprehension groups of licensors and potential licensees will be needed.

***Injunctions in case of disagreement over the royalty rate or on the licence terms.*** Finally, it is important to address the issue of what happens when the patent holder of a technically essential patent, who is a party to a standardisation agreement, and bound by an obligation to license under FRAND terms seeks an injunction against a creditworthy potential licensee when both the patent holder and the potential licensee disagree over the royalty rate or on the licence

terms. In such a case, it would be contrary to the duties of national courts under Article 4 (3) TEU to order an injunction against a user contesting the validity of the patent, or arguing that it had not infringed them, unless the court had first found that the patent owner was offering FRAND terms. Allowing injunctions to be given before the FRAND royalty rate or the validity of the patent is determined would entirely alter the negotiating positions and could lead to payment of royalties well above the FRAND level.

We hope you find this input useful as part of our discussion on *ex-ante* disclosures of IPRs and of licensing terms in the standardisation context.