

To:

European Commission  
DG Enterprise and Industry  
Unit A4 - Industrial Competitiveness Policy for Growth  
Avenue d'Auderghem 45, 1040 Brussels, Belgium  
[ENTR-SEP@ec.europa.eu](mailto:ENTR-SEP@ec.europa.eu)

Name of the submitting organization:	<b>Nokia</b>
Type of respondent:	<b>Enterprise</b>
Country of residence or location of headquarters:	<b>Espoo, Finland</b>
Name, contact details including an e-mail address:	<b>Leo Baumann</b> Director EU Affairs Head of Nokia EU Representative Office Government Relations, Nokia Corporation +32 475 690 955 <a href="mailto:Leo.Baumann@nokia.com">Leo.Baumann@nokia.com</a> <a href="http://www.nokia.com">www.nokia.com</a>
EU Transparency Register: ID:	<b>35167875358-33</b>
Contact details of organisation's head office:	Karaportti 3, 2-4 P.O. box: 226 Espoo 02610 FINLAND
Contact details of the organisation's Belgium office:	Rue de la Science 14b Brussels BELGIUM Telephone number: (+32) 475690955

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*European Commission Consultation:*

**Patents and Standards: A modern framework for standardisation involving intellectual property rights**

15 February 2015

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Nokia welcomes the opportunity to respond to this Consultation on Patents and Standards. Our response is structured as follows:

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## **Introduction**

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**Nokia urges the European Commission to adopt an overarching policy approach which encourages and incentivizes investment in open standardization to ensure the future viability of truly open standards and hence the continued success of the mobile technology industry in Europe.**

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**Mobile technology standards have revolutionized the world.** The wide interoperability and dramatic performance improvements in mobile communications standards (such as the 2G, 3G and 4G mobile standards) have made mobile technologies the most rapidly adopted consumer technologies of all time. Consumer adoption has grown to an astounding 3.4 billion connections and is expected to exceed 8 billion by 2020<sup>1</sup>. Consumers worldwide value mobile technologies at 11% to 45% of their income, and one third would rather give up 20% of their annual salary than give up personal use of a mobile phone. Consumer costs and prices have plummeted. The average mobile subscriber cost per megabyte decreased 99% between 2005 and 2013. Smartphones are now available for less than \$40<sup>2</sup>.

**Investment in standardized technologies lie at the heart of mobile technology.** Wide interoperability and high end-to-end performance are pre-requisites for mobile technology to work as it does. **The success of the mobile industry has required hundreds of billions of euros of risk-inherent, up-front investment in R&D in standardized technologies.** Without a standardized interoperability framework either an array of competing non-interoperable technologies would emerge or a single proprietary solution could come to dominate the market. In a world where different countries still use different power plugs, open standards in mobile technologies have resulted in a phenomenal level of interoperability where anyone can make a phone call to anyone else in the world regardless of the brand of products they are using or the country they are in.

**The success of mobile standards has enticed many new entrants into the industry making competition fiercer than ever.** New entrants are able to spring-board off the R&D investments made by others without incurring upfront R&D costs of their own. Many new entrants have been extremely successful. However, new entrants in particular are increasingly reluctant to pay their fair share of the R&D cost inherent in creating the successful market in which they operate. This behaviour, known as ‘free-riding’, confers an unfair competitive advantage to the detriment of other firms that do bear their fair share of the inherent R&D cost through FRAND compensation.

**Unwillingness to pay FRAND compensation has increased.** In the past, the avaricious behaviour of SEP owners (so-called patent ‘hold-up’) raised regulatory concerns, while implementers readily entered into FRAND negotiations. The courts and regulators have taken steps to address overly-zealous patentee behaviour. Now the pendulum has swung the other way. Patent owners are ready to grant FRAND licences, but implementers (even major reputable companies) exhibit aggressive ‘hold-out’, reluctant and unwilling to take FRAND licences. ‘Free-riding’ and ‘hold-out’ are now significantly more serious problems in the real commercial world than ‘hold-up’. Today the majority of mobile phone manufacturers are unlicensed under most of the SEPs they are using. Ten years ago most manufacturers were licensed.

**Unwillingness has many guises.** Unwillingness manifests itself in many different ways, for example in dilatory negotiations and delay tactics, or even outright refusal to negotiate a FRAND licence. It has not helped that SSOs and regulators are questioning the FRAND framework because unwilling licensees invoke the on-going debate and resulting legal uncertainty as reasons or excuses for delaying FRAND licence negotiations. For this reason it is in the interests of unwilling licensees for the policy and

<sup>1</sup> [http://www.gsma-mobileeconomy.com/GSMA\\_ME\\_Report\\_2014\\_R2\\_WEB.pdf](http://www.gsma-mobileeconomy.com/GSMA_ME_Report_2014_R2_WEB.pdf)

<sup>2</sup> [https://www.bcgperspectives.com/content/articles/telecommunications\\_technology\\_business\\_transformation\\_mobile\\_revolution/](https://www.bcgperspectives.com/content/articles/telecommunications_technology_business_transformation_mobile_revolution/)

regulatory debate to continue as long as possible without clear resolution. Questions about the availability of injunctive relief, the meaning of reasonableness and the question of the appropriate licensing level have all turned into excuses for unwilling licensees to avoid taking a licence. It should be clear that there is an obligation for implementers using SEPs to conclude FRAND licenses in a timely manner. Otherwise the current standardization eco-system will be jeopardised.

**Aggregate royalties for standardized mobile technologies are reasonable and sustainable.** The debate about ‘royalty stacking’ in the mobile industry is not new. From the earliest days, as the number of SEP owners began to grow, fears have been expressed that aggregate royalties might escalate out of control. The best indicator of the sustainability of patent royalties in the mobile sector is the tremendous success the industry has enjoyed. There is no economic, legal or other empirical evidence or even any credible indication that the aggregate patent ‘royalty stack’ would constitute an unsustainable burden on the industry historically, currently, or in future.

**Continued investment in mobile open standards is crucial.** Mobile technologies have become a cornerstone of our economy. But consumers demand even more: 90% of 3G and 4G consumers are eager for advances above and beyond the currently available mobile technology<sup>3</sup>. Global mobile data is expected to increase eleven-fold between 2013 and 2018, and data speeds are expected to continue their steep upwards trajectory<sup>4</sup>. Meeting such expectations and demands requires significant continued investments in standardized technologies.

**Evidence-based Policy.** Changes in the legislative and regulatory framework should not be contemplated without a basis of sound empirical evidence of systemic market failings with the current FRAND system. Nor should changes be made without a prior understanding of their impact on the viability of the delicate standardisation eco-system. Any changes should have as their primary and overarching objective the encouragement of investment in R&D in open standards, as well as the promotion and conclusion of efficient FRAND-based SEP licensing. Policy must not be driven by those with the loudest voice or deepest pockets in this debate.

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## Conclusion

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**Nokia sees this consultation as an important exercise in gathering empirical evidence, and we trust the European Commission will scrutinize the results and weigh them carefully and avoid any changes in the policy or regulatory framework that are not supported by empirical evidence of systemic problems in the current system.**

**Also, we trust the results of this consultation will enable the Commission to restore legal certainty in the FRAND environment and so remove uncertainty as a weapon from the armoury of excuses used by unwilling licensees to avoid taking FRAND licences.**

<sup>3</sup> [http://www.gsma-mobileeconomy.com/GSMA\\_ME\\_Report\\_2014\\_R2\\_WEB.pdf](http://www.gsma-mobileeconomy.com/GSMA_ME_Report_2014_R2_WEB.pdf)

<sup>4</sup> [http://www.cisco.com/c/en/us/solutions/collateral/service-provider/visual-networking-index-vni/white\\_paper\\_c11-520862.pdf](http://www.cisco.com/c/en/us/solutions/collateral/service-provider/visual-networking-index-vni/white_paper_c11-520862.pdf)

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## Response to the Eight Key Issues

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**QUESTION 1. Standardisation involving patents is common in the telecommunication industry and in the consumer electronics industry. Which other fields of standardisation comprise patent-protected technologies or are likely to do so in the future?**

### **Patents will play an important role in open standardisation in more and more fields**

Standardization provides interoperability and enhances and optimises end-to-end performance. In today's increasingly interconnected world the consumer demand for interoperable high performance technologies is likely to increase. As the "Internet of Things" becomes more and more a reality a growing spectrum of products and devices will become interconnected and able to "talk to each other", for example cars, medical appliances, heating controls systems, domestic appliances such as fridges, to name but a few. It is expected that literally tens of billions of different devices will be interconnected within the next 5 years. The proliferation of these devices will require increased performance from the mobile telecom infrastructure, representing on the one hand enormous opportunities but also increased demand for open standardization.

Patents are a key ingredient in open standardisation because they allow participating companies to disclose and share their new technology openly and early, knowing that their inventions will be protected.

So, not only will open standardisation become increasingly important across many more sectors outside telecoms, those standards will, and indeed should, include patented technologies.

In all fields where standardisation is likely to bring benefits to consumers, policy makers must ensure the right drivers and incentives for standards to continue to be developed in an open, consensual manner, and avoid tendencies towards fragmented or closed proprietary solutions.

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**QUESTION 2. A variety of rules and practices govern standardisation involving patents. Which elements of these rules and practices are working well and should be kept and/or expanded? Which elements on the other hand can be improved?**

### **Market driven FRAND licensing must be upheld with the right balance of incentives**

The FRAND framework inherently provides a balance between the exclusive nature of patents and the collective nature of standards. It serves two main purposes: (1) to ensure that a standard is accessible to implementers; and (2) to provide innovators a return on their investments in order to incentivize continuous investment in further development of open standards. Properly functioning FRAND licensing will lead to a virtuous cycle of continuous R&D investment followed and incentivized by successful implementation.

The FRAND framework has generally worked well historically in telecoms, and is still fundamentally fit for purpose. What has changed, however, is the behaviour of some actors. New entrants are able to spring-board off the R&D investments made by others without incurring upfront R&D costs of their own. But these new entrants in particular are increasingly unwilling to pay their fair share of the R&D cost inherent

in creating the successful market in which they operate. This behaviour, known as ‘free-riding’, confers an unfair competitive advantage to the detriment of other firms that do bear their fair share of the inherent R&D cost through FRAND compensation. The correct balance of incentives needs to be restored to ensure continued investment in R&D in standards technologies.

A virtuous FRAND licensing cycle has facilitated the unparalleled success of the mobile technology industry thus far. The vast majority of FRAND licensing in mobile technology sector has been based on voluntary license arrangements, and only a fraction of cases have led to litigated disputes. However to the extent the balance of incentives in the current climate has moved in favour of the licensee and is not restored this will inevitably lead to more disputes in future and undermine open standardisation.

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**QUESTION 3. Patent transparency seems particularly important to achieve efficient licensing and to prevent abusive behaviour. How can patent transparency in standardization be maintained/increased? What specific changes to the patent declaration systems of standard setting organizations would improve transparency regarding standard essential patents at a reasonable cost?**

#### **Patent transparency: problem before solution**

Patent transparency is a key ingredient in open standardisation. Most SSOs in telecoms have rules aimed at ensuring transparency of SEPs. Enhancements certainly may be possible to increase essential patent transparency, not only around the disclosure process, but also around patent quality, to minimise the incidence of invalid as well as inessential patents. It is noted that procedures do already exist today for challenging the *validity* of patents generally, e.g. opposition proceedings before the EPO and revocation proceedings before certain national patent offices. These procedures, while available, are rarely used in the context of SEPs. Perhaps it would be fruitful to review existing procedures and their applicability or non-applicability to SEPs and explore why current procedures are not used more for SEPs before contemplating introducing any new SEP-specific procedures.

Discussions around patent transparency are beginning to emerge in SSOs, most notably in ETSI, where this topic started to be addressed in January 2015. Nokia is contributing and will continue to contribute actively to these discussions. One specific question posed by the European Commission in this context is whether it might be possible and useful for ETSI to have a database of granted SEPs which have been checked for essentiality. The preliminary discussions in ETSI recognized that this is a complex issue touching on many aspects both legal and practical, including cost versus incremental benefit and where any cost burden would lie. The overarching message that came out of this preliminary discussion highlighted the importance of first understanding and articulating the problem around SEP transparency before trying to come up with a solution. Hopefully, this consultation will help in that process.

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**QUESTION 4. Patents on technologies that are comprised in a standard are sometimes transferred to new owners. What problems arise due to these transfers? What can be done to prevent that such transfers undermine the effectiveness of the rules and practices that govern standardisation involving patents?**

**Transfers of SEPs do not undermine rules and practices governing standardization involving patents**

Concerning the transfer of SEPs in particular it is important for a new owner of a SEP to adhere to the applicable FRAND undertaking made by a predecessor in title. Otherwise the entire FRAND undertaking could be undermined and circumvented simply by transferring SEPs. However, nowadays this is usually taken into account in the IPR policies and other relevant rules of the SSOs, which in essence require any new owners of SEPs also to be bound by the FRAND undertaking requirements of such policies and rules. To the extent that SSOs have not adapted their Policies accordingly we would support such changes.

However, such Policy changes should not seek to impose more restrictive conditions on transfer generally over and above conveying the FRAND obligation with the SEP. The transferability of SEPs and other patents, like any property rights, facilitates commerce and investment in commercial activity, and is therefore not only beneficial for a market economy but an essential building block of society. Any question relating to possible problems arising out of transferring SEPs from one owner to another should always be viewed against this background and with the understanding that any problems that may arise in connection with transferring property rights will always be small compared to problems that would arise if property rights were not transferable.

A vibrant marketplace for patents (including SEPs) represents the much needed funding and encouragement for investment in research and development activities. Organisations that acquire patents in effect bear some of the R&D cost (and risk) that has gone into the development of the patented technology they acquire by compensating the entity that has carried out that R&D (whether it is a company, university or other entity).

An example of such funding is the French based sovereign investment fund France Brevets ([www.francebrevets.com](http://www.francebrevets.com)) that is financed among others by the state of France and is fully dedicated to patents. France Brevets could be described as a “non-practising entity” that is using French taxpayer money to fund R&D investment through acquiring patents. France Brevets recently announced<sup>5</sup> their first license agreement under their Near Field Communication licensing program that includes both SEPs and non-SEPs they have acquired.

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<sup>5</sup> [http://www.francebrevets.com/sites/default/files/FB\\_signs\\_LGE\\_RELEASE\\_18TH%20AUGUST.pdf](http://www.francebrevets.com/sites/default/files/FB_signs_LGE_RELEASE_18TH%20AUGUST.pdf)

**QUESTION 5.** Patent pools combine the complementary patents of several patent holders for licensing out under a combined licence. Where and how can patent pools play a positive role in ensuring transparency and an efficient licensing of patents on technologies comprised in standards? What can public authorities and standard setting organizations do to facilitate this role?

**Patent pool formation should be market driven**

In Nokia's experience, patent pools are more typical, and indeed successful, in the consumer electronics environment, where they generally deal with a relatively narrow well-defined 'package' of technology such as STB, DVD or Blu-ray. While patent pools aim to provide "one-stop" shop licensing, i.e. a single collective license fee for all patents contained in the pool, there are some significant drawbacks. For example patents outside the pool are not and cannot be included in the collective licence, and as such are 'out of scope'. It may not even be fully clear what patents exist outside the pool. Nor does a patent pool provide licensees with any indemnification against infringement of 'out of scope' patents. On the other hand, patent owners cannot be compelled to join a pool, and there are disadvantages or disincentives for patent owners to join, for example reduced control over their own patents. In short, a licence from a patent pool does not guarantee complete freedom of action under the relevant standard, and to that extent does not imply a fully transparent and fully effective solution. In areas like telecoms which involve complex technologies both converging and complementary, which are constantly developing and evolving over long periods, patent pools do not have any track record of success.

In circumstances where patent pools are appropriate they should and will be formed by commercial actors. Where the market determines that patent pools are not appropriate, public authorities should not be encouraging or facilitating them, let alone setting them up. In any case, public authorities should always ensure a level playing field for all market actors. Policy, supported by the legislative and regulatory framework, should have as its primary overarching objective the promotion of efficient market driven patent licensing.

Any royalty rates agreed in the context of market driven patent pools should be viewed only in the context of the respective patent pool and not be used as proxies for FRAND terms to any greater extent than any other existing license agreements.

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**QUESTION 6.** Many standard setting organizations require that patents on technologies included in their standards are licensed on "fair", "reasonable" and "non-discriminatory" (FRAND) terms, without however defining these concepts in detail. What principles and methods do you find useful in order to apply these terms in practice?

**The principles of FRAND determination should be market driven, not prescribed**

Market driven FRAND licensing promotes negotiated results which minimize transaction costs and provide highest consumer benefits. Prescribing FRAND (e.g. by mandating a royalty base) may in effect constitute price regulation.

There are broadly three scenarios where FRAND is applied in practice:



- (1) The vast majority of cases get resolved by license negotiations between individual SEP licensors and licensees. If the SEP licensor has an established programme for its SEP portfolio with set FRAND rates which others have already agreed then these rates, and expected sales of the licensee, will form a basis for negotiations.

Otherwise, the parties will typically determine FRAND terms by first holding technical discussions where a sample of the whole portfolio is considered. Each will look into the extent to which the patents are utilised by the standard, the geographic scope, the age profile, success in previous litigation and other aspects. Because it is impracticable to review each and every patent, the parties will typically use proxies such as sampling, citation analysis or third party studies. The parties will also be aware of other licensing transactions in which they have been involved, or have public information about third party transactions. They will form a view about the value that they think is appropriate for this transaction based on those.

Freedom for the parties to choose the methods and principles for determining FRAND terms encourages and promotes negotiated resolutions.

- (2) Where the negotiations between individual SEP holders and implementers are not successful, a court or an arbitrator may be called upon to determine whether the relevant SEP portfolio offer made in negotiations is or is not FRAND, or in cases where no FRAND offer has been made, to determine FRAND terms for such portfolio.

When an arbitrator or a court seeks to determine a portfolio FRAND rate, it will usually order each party to disclose their relevant existing agreements. When those are available the best approach is to use them as comparators to determine FRAND compliance or a FRAND rate. Economists and econometric experts can generally determine rates from lump sum or cross licenses using various methods. For most licensing parties the most important concern is often that they are paying or receiving a non-discriminatory market rate. Verifying or setting a rate with reference to existing license data helps to ensure this.

Otherwise, the court or arbitrator will consider other relevant factors which would include for example the portfolio of SEPs in question, the term of the license, the products licensed, the business model for selling or distributing such products, the standards covered, the extent of market adoption of the standardized functionalities, the agreement structure, the value of any grant back license or any other non-monetary compensation, payment arrangements, and the field of use that are intended to be covered in each situation, etc.

- (3) Where neither of the preceding alternatives applies, a court or an arbitrator may set out to determine a rate for a single SEP. However, a single SEP hardly ever covers an entire standard and a licensee mostly needs a license to all relevant SEPs. Therefore, a process of determining a FRAND rate for a single SEP in isolation will not resolve the dispute between the parties and can be an indication of unwillingness of one of the parties to achieve a resolution. Where a court nonetheless does determine a single SEP rate, the same principles are applicable as in other patent disputes. Ideally the court would set a rate based on a comparable patent for comparable use.

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**QUESTION 7. In some fields standard essential patents have spurred disputes and litigation. What are the causes and consequences of such disputes? What dispute resolution mechanisms could be used to resolve these patent disputes efficiently?**

### **SEPs do not spur disputes and litigation in the mobile technology sector**

It is a fact of life that where there are sizable commercial interests at stake, disputes and litigation usually occur. Patent disputes have been a trait of rapidly emerging, commercially important competitive technologies since the time of the industrial revolution. Examples include cotton making machinery (1770s-80s), telephony (1870s-80s, nearly 600 patents involved), sewing machines (1850s), light bulbs (1880s), and transistors (1960s). While such disputes and litigation may at the outset seem undesirable, they can also be viewed as a positive signal with respect to the proper functioning of the rule of law in a market economy. In our experience any judgments and awards given by courts and other governmental instances have been followed and respected.

Given the considerable size, as well as the competitive and dynamic nature of the mobile technology sector, and the number of SEPs, the amount of SEP litigation is relatively small. Furthermore, the SEP litigation that does occur is largely due to companies that are unwilling to pay FRAND royalties, not to companies that would be demanding supra-FRAND royalties. We are not aware of any courts or other dispute resolution instances making statements that they could not cope with the amount of SEP litigation (in the ICT sector or otherwise). We have no reason to believe that the amount of SEP litigation would in any way be a threat to the proper functioning of the court system or other dispute resolution forums anywhere in the world.

A recent case study<sup>6</sup> of US litigation makes the following findings:

- Litigation in the smart phone market is not driven by SEP's. The large majority of patents asserted in these cases are not related to standards (out of a total of 111 cases 35 included patents that were pleaded as SEPs).
- Zero injunctions or active exclusion orders were awarded for SEPs (as compared to 16 patents that were unrelated to standards).
- The potentially temporary spike in smart phone litigation (for SEPs and non-SEPs) was primarily driven by a handful of device manufacturers that were late and highly-successful entrants in the mobile wireless industry. It appears that smart phone litigation is on a decline.

One factor that might cause litigation is the current legal uncertainty spurred by the continuing regulatory and policy debate. To give just one example, a SEP owner may claim a FRAND royalty based on the price of a handset in line with traditional practice whereas implementers will now want to argue that the ongoing policy debate casts doubt on that approach, preferring instead a royalty based on the price of a chip in the handset. Suffice it to say, the difference between the positions of the licensor and potential licensee is likely to be so great as to preclude a negotiated settlement, and so the SEP holder has little alternative but turn to litigation. The specific problems with 'chip level licensing' are addressed in more detail in our answer to question 6.5.1 in the Annex.

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<sup>6</sup> [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2492331](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2492331) "Smart Phone Litigation and Standard Essential Patents" by Kirti Gupta and Mark Snyder

**QUESTION 8. How can holders of standard essential patents effectively protect themselves against implementers who refuse to pay royalties or unreasonably delay such payment? How can it be ensured that injunctions based on standard essential patents are not used to (a) either exclude companies from implementing a standard or (b) to extract unreasonable, unfair or discriminatory royalties?**

**SEP owners should retain the fundamental right of access to justice to ensure timely and efficient FRAND compensation for use of their SEPs. Opportunistic and abusive behaviour by infringers must not be tolerated or condoned.**

A SEP holder must retain the fundamental right to go to court and ask for the dispute to be settled in an appropriate judicial forum in a timely manner and seek the usual remedies including an injunction. Otherwise an infringer has no incentive to negotiate and conclude a license on any terms. In practice it is often only the start of legal proceedings, with the attendant threat of an injunction, which compels an infringer to change its behaviour and come to the negotiating table, i.e. start acting as a willing licensee.

There is a misplaced and unsupported belief that the availability of injunctive relief means SEP owners are avariciously seeking royalty rates in excess of FRAND and that this is blocking standards. This essentially hypothetical ‘problem’ is known as ‘patent hold-up’. It has caught the imagination of academics, economists and policy makers alike. However, in practice the real problem is not SEP owners seeking unjustified royalty rates, but ‘hold out’ by implementers unwilling to take licences on offered FRAND terms for the SEPs they are infringing. In reality ‘hold-out’ is a significantly more serious problem in the real commercial world than the hypothetical risk of patent ‘hold-up’.

Injunctions are in practice rare in all fields of standardization. Although Nokia has defended many SEP infringement claims, it has only been subjected to an injunction on one patent, which it had already designed around. Although injunctions have been granted in other cases, Nokia is not aware of any mobile phone manufacturer actually having been excluded from a market under a SEP. In many jurisdictions, no injunction will be enforced until all appeal routes have been exhausted and the UK in particular has made it clear that it will stay all injunctions pending the outcome of the appeal process (*see Nokia v HTC*).

Hence the risk of injunctions being used to exclude companies from implementing standards or to extract unreasonable royalties has so far been purely hypothetical. Nevertheless some actors with deep pockets and loud voices, whose business models rely on implementing standards, have spread scare stories about the theoretical risks of being excluded from the market, catching the imagination of some academics and policy makers.

### **Protection against abuses**

Intervention by antitrust authorities is appropriate in individual cases where the behaviour of the SEP holder is clearly abusive, having regard also to the behaviour of the potential licensee. To illustrate, Nokia referred a case to the European Commission where IPCom attempted to circumvent FRAND obligations by claiming that, as a purchaser of certain declared essential patents, it was not bound by the FRAND undertaking provided by the original patent holder, Bosch. In that case, the European Commission intervened and ordered IPCom to adhere to the FRAND commitment of the previous owner of the patents.

Nokia trusts the ability and discretion of competition authorities to intervene in situations where there are signs of clear abuse, and similarly trusts national courts to conduct appropriate analysis before granting an injunction in an alleged SEP infringement case.

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