The views stated in this submission are presented on behalf of the Sections of Antitrust Law, Intellectual Property Law, Science and Technology Law, and International Law of the American Bar Association (the Sections). They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and therefore may not be construed as representing the policy of the American Bar Association.

The Sections are pleased to submit comments on Key Issues 3, 4, and 6 of the European Commission’s Consultation on Patents and Standards (the Consultation). To avoid duplication with the report of the fact-finding study (“Background Report”) commissioned in 2013 by DG Enterprise and Industry on the issue of patents and standards, the Sections limit their comments to aspects not otherwise covered in the Background Report. The Sections’ comments reflect the expertise and experience of its members with competition and intellectual property law.

Commentary on Key Issues 3, 4, and 6

I. Key Issue 3 - Patent Transparency: “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?”

The Sections agree with the Background Report that the benefits of increased transparency in standardization should be weighed against its costs. As the Consultation states, transparency should be understood as relating to the ease with which interested parties can establish the patent situation relevant to an area of standardization. The costs of a disclosure system requiring more precise or extensive information may outweigh its benefits if, for example, a standard-setting organization’s (SSO’s) rules require royalty-free licensing (which reduces the need to evaluate the relative strength of different portfolios or avoid royalty stacking). At the other end of the spectrum, an SSO that expects potentially expensive standard-essential patent (SEP) licenses from a very large number of patent holders might go beyond current ETSI rules and require firms to disclose maximum royalty rates ex ante or notify the SSO when SEPs are transferred to other parties. Accordingly, the Sections do not recommend a single transparency policy. Instead, the Sections recommend that the European Commission permit SSOs to determine the transparency requirements that are most appropriate for their situations.

II. Key Issue 4 - Transfer of SEPs: “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 standardization involving patents?”
The Sections note that the Background Report contains a comprehensive discussion of issues relating to transfers of SEPs, and limit their comments to supplementing the Report on the specific issue of transfers to non-practicing entities (NPEs) or patent-assertion entities (PAEs).

As the Background Report notes, the best method to address the transfer of SEPs to NPEs or PAEs remains unsettled as a matter of U.S. law and policy. In particular, there has been significant debate in the United States over whether and how the antitrust laws should apply to conduct involving PAEs, and an apparent consensus that more study is needed to ground a sound enforcement policy. To that end, the U.S. Federal Trade Commission (FTC) is currently conducting a study to better understand how PAEs impact innovation and competition. For example, the FTC has said it will investigate, among other things, how PAEs are structured, the types of patents they hold and whether they honor any patent commitments they may possess, and how PAEs interact with the operating companies that transfer patents to PAEs.

III. Key Issue 6 – Notions of “Reasonable” and “Non-Discriminatory”:

“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?”

A. The Meaning of “Reasonable”

In the United States, a number of courts, including the U.S. Court of Appeals for the Federal Circuit (which has nationwide jurisdiction over claims arising under the patent laws), have provided guidance on the meaning of the “reasonable” prong of FRAND (fair, reasonable, and non-discriminatory). Although the decisions provide important guidance, the law is still evolving and a number of issues remain unsettled. In addition, other U.S. district courts are poised to rule on the issue of “reasonable” in other cases in the upcoming year. Importantly, any such decisions must follow the Federal Circuit’s binding precedent, yet will likely provide additional guidance on these issues.

Principles. The meaning of a FRAND obligation should be interpreted so as to give effect to the goal of the relevant SSO in adopting its requirement for patent holders to make FRAND commitments. The purpose of adopting a FRAND policy is generally understood to be to facilitate first development, and then successful commercial adoption of the SSO’s standards. More specifically, FRAND terms are terms that promote the following aims: (1) providing patent holders with reasonable compensation to “adequately and fairly reward[] them for the use of their IPR standards projects”; and (2) making the standard available to all (although there is a dispute as to what “all” means, including whether a FRAND commitment extends to component manufacturers or is limited to end-user devices). In addition, as the Background Report to the Consultation recognizes, many contend that a purpose of FRAND obligations is to mitigate the risk of patent hold-up.

Methods. The 15-factor test set forth in *Georgia-Pacific Corp. v. United States Plywood Corp.*, has been influential in judicial determinations of royalty damages. Under the *Georgia-Pacific* approach, courts have simulated a negotiation between the licensor and the licensee, conducted as of a time just prior to adoption of the relevant standard, to approximate the royalty that the parties would have agreed upon. This approach is consistent with the FTC’s recommendation that courts should use a hypothetical negotiation and the willing licensor/willing licensee model to determine FRAND royalty rates.
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In its recent Ericsson v. D-Link decision, the Court of Appeals for the Federal Circuit, while approving the general methodology, declined to endorse any one set of Georgia-Pacific-style factors. It cautioned that courts should not be bound by any single formula and should consider all the facts of each particular case. The several U.S. district courts that have addressed the issue of determining a reasonable royalty in the context of a FRAND obligation have applied flexible and modified versions of the Georgia-Pacific test. When applying a Georgia-Pacific analysis in the context of a FRAND commitment, certain factors of the test are irrelevant, and others may need to be adjusted. For example, factor 4 has to do with the possibility that the licensor has a policy of refusing to license its patents. However, if the licensor has given a FRAND commitment, it has typically agreed not to completely refuse to license its essential patents, making factor 4 irrelevant. Factor 8 considers the “current popularity” of the invention. In the context of a FRAND obligation, a court should consider that the “popularity” of the invention may be influenced by its being incorporated into an industry standard.

In conducting a hypothetical negotiation analysis, the following considerations have been discussed in the U.S. cases.

**Apportionment.** Under U.S. law on patent infringement, a patent holder is entitled damages equal to, at minimum, a reasonable royalty. This minimum statutory standard applies regardless of whether the patent holder has made a FRAND commitment. Case law has evolved to refine and limit the reasonable royalty standard. The Federal Circuit in Ericsson provides that a “patent holder should only be compensated for the approximate incremental benefit derived from his invention.” This refinement of the reasonable royalty standard applies in all patent infringement cases, both those that arise in a SSO/FRAND context and those that do not. In the context of a FRAND obligation, the Federal Circuit has further held that “the royalty for SEPs should reflect the approximate value of that technological contribution, not the value of its widespread adoption due to standardization.” District courts have used a similar approach.

There are a number of open issues relating to apportionment, including the use of the incremental value approach and the appropriate royalty base. The Sections take no position on these issues given the evolving U.S. case law in these areas. However, the Sections note that the U.S. Court of Appeals for the Federal Circuit has rejected formulaic rules for calculating reasonable royalty rates, explaining that this is a fact-specific inquiry that should be made on a case-by-case basis.

**Existing licenses.** The hypothetical negotiation analysis is best informed by market-set rates, when possible. Thus, in determining a FRAND royalty rate, courts should consider existing licenses. A number of courts have done so, and the Federal Circuit has recognized that “licensed-based evidence” “is relevant and reliable” if properly analyzed. While courts typically rely heavily on existing licenses, there are a number of issues to consider, such as whether the licenses were “adopted under the duress of litigation”; were determined only as part of a larger package deal; were based on large patent portfolios rendering the rate inappropriate for an agreement covering fewer patents; or were based on different standards. For such reasons, existing licenses can sometimes not be probative of a proper FRAND rate (and in some cases, a determination of a “reasonable” royalty for purposes of assessing damages without all of the other negotiated terms and conditions may not be probative of whether or not an offer to license was FRAND).

**Consideration of “patent hold-up” and “royalty stacking.”** In Ericsson, the Federal Circuit recognized that “SEPs pose two potential problems that could inhibit widespread adoption of the standard: patent hold-up and royalty stacking.” The court further held that, in order to be considered as part of a FRAND damages analysis, concerns about hold-up and royalty stacking must be proven, stating that “[c]ertainly something more than a general argument that these phenomena are possibilities is
The court further held that, in order to be considered as part of a FRAND damages analysis, concerns about hold-up and royalty stacking must be proven, stating that “[c]ertainly something more than a general argument that these phenomena are possibilities is necessary.” Instead, the court instructed that implementers must provide evidence that the SEP holder “used its SEPs to demand higher royalties from standard-compliant companies.”

B. The Meaning of “Non-Discriminatory”

The “non-discriminatory” prong of FRAND supports the principle that an SEP holder may generally not refuse to license its SEP, and therefore in a simulated negotiation the court will assume that the SEP holder would have participated in the negotiation and would have agreed to license the SEP on reasonable terms and conditions. Further, the court may assume in a simulated negotiation that an SEP holder would not seek to unfairly disadvantage a licensee because the commercial relationship between them is that of competitors.

Beyond this, U.S. case law has not substantially developed the meaning of “non-discriminatory” in the context of FRAND commitments. Moreover, little has been written about the documentary history as to the reasons for the inclusion of the term “non-discriminatory” in the IPR policies of SDOs. Notably, in the case of ETSI, the purpose appears to have been to guard against protectionist discrimination of the sort that could operate to exclude entities of certain nationalities or non-members of ETSI, not to create a requirement that all licensees must be licensed on identical terms, or to impose the equivalent of a “most-favored licensee” guarantee.

The Sections note that FRAND terms and conditions are routinely negotiated bilaterally between market participants, and as a result, different licenses can and will have different terms and conditions depending on the circumstances of each individual negotiation. Further, the Sections caution that any definition of “non-discriminatory” should take into account the economics literature on this issue. Some of this literature suggests that price discrimination is not always or necessarily harmful, and in some cases, it can increase efficiency, raise incentives to innovate by easing the recoupment of necessary upfront investments, broaden the markets served, and improve consumer welfare. In short, decision makers should study this issue further before taking a position.

CONCLUSION

The Sections appreciate the opportunity provided by the European Commission to comment on the Consultation. We would be pleased to respond to any questions the Commission may have regarding these comments, or to provide additional comments or information that may be of assistance to the Commission.

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