From Patent Hold-Up to Patent Hold-Out?

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ABSTRACT

Standardization is a process through which potential rivals cooperate to have the best technological solution adopted as the next standard. They pool together financial, human and material resources. Intellectual property rights, especially patents, are a powerful tool for them to recover investments made in the process and keep participating in it. However, to avoid abusive use of patents incorporated in de iure standards, companies contributing to the standard development have to comply with specific duties, amongst which making the technology essential to the standard available on Fair, Reasonable and Non-Discriminatory terms and conditions, i.e. the so-called (F)RAND commitment. This commitment has been created to prevent patent hold-up from patent holders, which could force implementers to enter into disadvantageous license agreements. With the changes in the cellphone market in the last ten years, the content of this (F)RAND commitment has been challenged in courts and in front of antitrust and competition authorities. The question is whether this duty, set up to avoid hold-up, is not used by some implementers to engage in “hold-out” or “reverse patent hold-up” strategies.

KEYWORDS

(F)Rand, Hold-Out, Hold-Up, Standardization, World Trade Organization (WTO)

1. INTRODUCTION

Standardization aims to define standards, which are technical rules. The process is driven by the Word Trade Organization (“WTO”)’s principles of transparency, openness, impartiality and consensus, effectiveness and relevance, coherence. Firms that may compete at a later stage collaborate by pooling human, financial and/or technical resources to have the best technological solution adopted as next standard. Once the standard has been adopted, it is made public and available to anyone wishing to implement it, whether or not they are a member of the standard-setting organization that has developed the standard. Besides interoperability and compatibility, even between competing devices (EC regulation No. 1025/2012 on standardization), standards in telecommunications also guarantee high performance (Fraunhofer Study 2011).

For the reasons mentioned above, standards are considered as a tool encouraging innovation, technology dissemination and competition. Nonetheless, standardization is closely linked to intellectual property rights (“IPRs”) and competition issues. Companies involved in standardization may hold patents. Unlike standards, which are available on an open and non-discriminatory basis, patents are exclusive rights granting their owners the power to block other parties from using the patented invention. While both aim to encourage innovation, patents and standards can appear incompatible at first sight. Even more so when patents are qualified as “standard-essential patents” (“SEPs”), as no technical alternative to these patents exist. Accordingly, each product or service implementing the standard without a license will therefore necessarily infringe the SEPs.
As a result, SEPs in principle confer their holders an increased market power by allowing them to control the standardization process and the downstream market (Shapiro 2001, Farrell et al. 2007). Consequently, in the absence of any safeguard, standardization could lead to behaviors impeding competition, as hold-up or royalty-stacking. Patent hold-up refers to the situation where SEP holders abuse their bargaining power to extract excessive royalty rates from their SEPs, potentially under the threat of an injunction. Such rates, if they are accepted by the implementer, may hamper the diffusion of the standard, as they could be financially burdensome and restrict access to the standard by implementers: the implementer will either have to accept rates “far in excess of the patent holder’s true contribution”, which are similar to a tax on products incorporating innovation; or to postpone the sale of products/services incorporating the standard to avoid paying excessive fees or costly litigations (Lemley & Shapiro 2007). Royalty stacking occurs when the cumulative royalty rate for all the patents needed for the standard is excessive: even if each SEP holder demands a reasonable fee, due to the large numbers of SEPs to implement, the aggregate royalty rate for all SEPs exploited in the standard may reveal itself excessive and non-bearable (Lemley & Shapiro 2007).

Yet, SEPs play an important role in standardization. Companies holding SEPs are those contributing the most to the development of the standard (on contributors: cf. ABIresearch 2013, on SEP holders: cf. Fraunhofer Study 2011). Since standard-setting organizations (“SSOs”) seek to “balance between the needs of standardization for public use in the field of telecommunications and the rights of the owners of IPR”, they have enacted IPR Policies to avoid anticompetitive behaviors while adequately rewarding SEP holders for their contribution to the standard. At the same time these policies shouldn’t lead to a counter-abuse on the implementer’s side.

One relevant part of the SSO’s IPR Policies is the (F)RAND commitment. Through this commitment, SEP holders agree to share their SEPs accessible on (fair), reasonable and non-discriminatory terms and conditions to any party requiring such a license, instead of keeping the technology covered by such SEPs proprietary. The purpose is to prevent any patent hold-up.

The entrance of new players in the telecommunications market, some of which did not contribute their technologies to standardization but nevertheless manufacture standardized products, have been possible thanks to de iure standards, as they enhance competition and innovation. These changes have led to some challenging in worldwide litigations the suitability of the standardization process as it is currently working.

One issue arising from the recent worldwide litigations in the telecommunication sector is whether there is a real risk of “patent hold-up”. Inversely, some players might be using the “(F)RAND commitment to engage in “reverse hold-up” (also called “hold-out”), by refusing or delaying negotiations and/or payment for the use of SEPs.

Both questions will be analyzed under IPR Policies in Europe and the United States (“U.S.”), as SSOs like the IEEE and ETSI have adopted the most litigated standards (GSM, UMTS, GPRS, Wi-Fi). Furthermore, this paper will focus on literature, case law and antitrust investigations in both geographic areas. The first section will examine the relationship between the (F)RAND commitment and the academic hold-up theory (I). The second part will examine how European and American judges and competition authorities address the question of hold-up (II). The third one will examine the potential transition from hold-up to hold-out (III).

2. THE (F)RAND COMMITMENT AND HOLD-UP

The content of the (F)RAND commitment has been challenged in courts (A) among others in order to mitigate the risk of hold-up as defined by Mark Lemley and Carl Shapiro (B).

2.1. The Content of The (F)Rand Commitment

SSOs usually don’t interfere in the negotiations of a (F)RAND license, which they consider as a purely commercial matter between companies.
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