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The Fair Standards Alliance

Response to UKIPO consultation paper on 'Industrial Strategy: Intellectual Property Call for Views'

The Fair Standards Alliance (FSA) is an association that has been incorporated to promote a number of Key Principles regarding the licensing of standards-essential patents (SEPs) on a fair and reasonable, and non-discriminatory (FRAND) basis. We believe that FRAND means something. It means that patent owners are entitled to reasonable compensation for their contributions to the standard, while standard implementers are entitled to licenses on fair and non-discriminatory terms. Behaviours that support these fundamental principles should be encouraged; abuses that undermine these fundamental principles should be discouraged.

The FSA membership constitutes a broad range of industry stakeholders. Our member companies work in different markets, different technologies and different levels of the supply chain. The FSA includes companies that individually spend millions (or in some cases, billions) of Euros annually developing technologies, participating in standards development and licensing SEPs to others. Together, our members own more than 300,000 patents, and spend more than \$100 billion in annual R&D.

The FSA's membership includes prominent product companies and consumer brands, that develop, market and sell standardized goods, and who may license SEPs from others. Indeed, most of our member companies are both patent holders and implementers. Each of our members favours balanced approaches to SEP issues that address the legitimate interests of both SEP holders and of potential licensees.

We would like to thank the UK Intellectual Property Office (UKIPO) for providing this opportunity to comment. We do not offer answers on each of the points covered in the consultation, but offer some balanced views on key matters that the FSA finds important to emphasize.

Key FRAND principles

Fundamentally, we believe that the core principles of an equitable, effective and enforceable licensing methodology for SEPs for which a FRAND commitment has been provided should

be designed to facilitate good-faith negotiations and to reduce the need for parties to seek recourse to courts or arbitrators.

The lack of an umbrella of common expectations of what FRAND means will not only hamper good-faith negotiations, but also puts good-faith patent holders and implementers at risk of losing out on legitimate claims and defenses against bad-faith behavior.

While it would not be appropriate for UKIPO to set a single pre-defined methodology to calculate the value of a FRAND royalty, or to determine a closed set of FRAND terms, we suggest UKIPO establishes the criteria and guidelines for licensors and licensees to consider when designing and reviewing licensing offers under a FRAND commitment.

Such guidelines should reflect at minimum the following points:¹

- *FRAND should mean Fair and Reasonable and Non-Discriminatory to ALL.* Holders of FRAND-encumbered SEPs should offer licenses on fair and reasonable and non-discriminatory terms to all companies, organizations, and individuals at all levels of the supply chain of an end product who implement, or wish to implement, the relevant standard or respective portions of the standard. Refusing to license implementers of a SEP simply because of its position in the product supply chain, or under the pretext of more efficient licensing or under an alleged necessity to track and identify final usage amounts to a breach of a FRAND commitment, and violates the basic commitment to license on a non-discriminatory basis.^{2,3} Tolerating discriminatory refusals to license SEPs threatens to undermine incentives for a wide variety of standard-setting participants, who will be prevented from licensing the standard they helped to develop. Deviating from this principle or allowing for exceptions will create confusion, and simply be wrong. We also refer to the FSA's position paper on the topic for further details.⁴
- *Patents should be valued based on the claimed invention.* As patents should be valued based on the claimed invention, in most circumstances, FRAND licensing rates should be determined with reference to the device, or the part of the device, that implements the patented invention; this ensures that the patent holder obtains fair compensation for what it actually invented, and not compensation for the value of others' work or contributions. It is important to not blindly base royalty rates for SEPs on the overall value of an end device that makes use of the SEP's invention, but to rather carefully consider the actual value that the SEPs contribute to the technology addressed by the invention. Often, that assessment can greatly be aided by considering the smallest component that actually implements the patented invention. When that part can be isolated as a separately saleable unit (e.g., a brick for building various types of buildings), a fair royalty rate will typically bear a relation to the price of that unit.

¹ See in particular the FSA position paper "Key Principles" (12 November 2015), available at <http://www.fair-standards.org/wp-content/uploads/2016/08/FSA-POSITION-PAPER-June2016.pdf>.

² It also disturbs the supply of products in the established value chain. In practice, there are contractual obligations in the value chain for the supplier to deliver products free of legal faults, so that they can be used without infringing patents. Suppliers will not be able to fulfill their responsibilities in case SEP holders have no legal obligation to provide a FRAND license to any user in the value chain. Unclear licensing behavior of SEP holder and lack of rules result in interferences of the synergy between supplier and implementer. The unpredictable warranty risks bears the risk of delivery stops of the suppliers and increased product prices.

³ Such licensing approach may be considered "effective" and "convenient" to a SEP licensor, but such "convenience" is only marginal when compared to the efficiencies created by making FRAND licenses available throughout the supply chain.

⁴ The FSA position paper "SEP licenses available to all" (24 June 2016), available at <http://www.fair-standards.org/wp-content/uploads/2016/09/160621-FSA-Position-Paper-SEP-licenses-available-to-all.pdf>.

- *Fair and reasonable royalties for a SEP must not exploit the fact that the standard cannot be implemented without licensing the SEP.* A FRAND royalty must reflect only the value of the SEP, not the additional value conferred on it by its inclusion in the standard. The value of the standard reflects contributions from the entire community that developed the standard, and from the ecosystem having adopted the standard, rather than by the SEP holder alone.
- *Fair and reasonable royalties for a SEP must take into account the actual and potential aggregate royalty demands for other SEP's.* A FRAND rate must consider royalties for other patents required to implement the standard. The goal of widespread adoption of a standard cannot be achieved if these aggregate demands are not considered when determining a FRAND rate, or else a "royalty stack" will be created that makes implementing the standard uneconomical.
- *Enhanced transparency regarding FRAND-encumbered SEP licensing.* SEP holders that are willing to provide demonstrably non-discriminatory rates should be open and transparent about the rates they seek to charge for their SEPs, what patents are being licensed, and their basis for believing that the patents are essential, valid SEPs. By requiring extensive secrecy from all licensees, some SEP holders seek to prevent prospective licensees from knowing the terms that have been offered to others, and thereby from reliably evaluating whether the terms they are negotiating are FRAND. While voluntary provisions regarding confidentiality certainly are permissible, the use of SEP leverage to force potential licensees to accept excessive secrecy is improper. In addition to harming the particular licensees involved, such practices harm the public interest in ensuring a robust and fair SEP licensing ecosystem. We refer to the FSA's position paper on the topic for further details.⁵
- *Injunctions Should Be Available Only in Limited Circumstances, and requests be reviewed in accordance with the principles of equity and proportionality.* The ability of a SEP holder to threaten a good-faith implementer with an injunction distorts licensing negotiations to the detriment of that implementer. Therefore, when deciding on the appropriateness of injunctive relief in respect of one or more SEPs, factors such as the market participation of the patent holder, proportionality, and the interests of the general public should be taken into consideration. Under these considerations, and especially when a SEP holder has voluntarily committed to license its patents under Fair, Reasonable and Non-Discriminatory terms, a ruling made in favour of damages or a licence as opposed to injunctive relief will often provide for a more proportionate remedy. We refer to the FSA's position paper on the topic for further details.⁶
- *A FRAND promise should extend to a transferee if the SEP is sold.* If a FRAND-encumbered SEP is transferred, the initial transferee and all subsequent transferees must remain bound by the FRAND commitment.
- *No Patent Tying – Only Relevant Patents should be Required to be Licensed.* While some parties may voluntarily and mutually agree to broader licenses, a holder of a FRAND-encumbered SEP should not be able, as a condition of granting a FRAND license to the SEP, to require implementers to (i) take licenses to patents that are not

⁵ See the FSA position paper "Transparently FRAND: The Use (and Misuse) of Confidentiality Obligations in FRAND Licensing Negotiations" (15 February 2017), available at <http://www.fair-standards.org/wp-content/uploads/2017/02/170213-FSA-Position-Paper-Transparency-FRAND-L.pdf>.

⁶ The FSA position paper "Injunction in accordance with the principles of equity and proportionality" (23 January 2017), available at <http://www.fair-standards.org/wp-content/uploads/2017/01/FSA-Injunction-Position-Paper-23-January-1.pdf>.

essential to the standard, or that are invalid or not infringed by the implementer; or (ii) grant a license to the implementer's patents that are not essential to the standard.

'IP Licensing Resolution'

We also wanted to take the opportunity to offer some specific thoughts on the section around the 'IP licensing resolution', in which you indicate as follows:

We are aware that IP trading can present some companies with barriers to innovation, notably in the area of Standard Essential patents (SEPs), where we are told that the issue of portfolio fragmentation can lead to spiralling costs to innovators operating in standards-reliant sectors.

The 'fragmentation' or 'proliferation' of SEP portfolios is a significant problem for many companies making standards compliant products. In order to understand the problem of portfolio fragmentation we can use the following example:

In 2012, a patent holder (Company A) has a portfolio of 1000 standard essential patents (SEPs) which are essential to LTE wireless technology. Company A voluntarily commits to the standards setting organisation (SSO) to license its SEPs to anyone requesting a license upon FRAND terms. Company A decides that its FRAND rate for its LTE SEPs is €2.00 per unit. Company X requests a license to the LTE SEPs for its IoT products. Company A licenses the portfolio of LTE SEPs to Company X for 5 years (until 2017) at €2.00 per unit, and Company A collects the royalties from Company X. Company X pays the €2.00 on time for each unit sold throughout the term, so Company X is paying €2.00 for 10 patents

Company A realises that it does not need all of its portfolio of 1000 patents, as it has a dominant position whether it has 100 patents or 500 patents, so after 3 years it decides to sell off parts of its portfolio. It sells a part of its portfolio (100 patents (or 10% of the portfolio)) to Company B for £10 million, and then sells another 10% (another 100 patents) to Company C for another £10 million.

Company A now has 800 LTE SEPs, and £20 million in the bank (from the sales of its portfolio). Company B and Company C now have 100 patents each.

In 2018, when the 5 year license has expired, Company X contacts Company A to seek a new license. Company A says its FRAND rate for its LTE SEP portfolio is still €2.00. It does not tell Company X that it has sold off 200 patents (to Companies B and C). Company X enters into the license for another 5 years (to 2023).

Out of the blue, Company B writes to Company X and says that it has a portfolio of LTE SEPs and that Company X needs to enter into a patent license or they will be sued. Company B says that its FRAND rate is €1.00 per unit. Company X now has to incur tens of thousands of pounds in legal and experts fee to investigate the claims of Company B.

Then along comes Company C. It contacts Company X and says it needs to enter into a patent license or they will be sued by Company C. Company C says that its FRAND rate is €0.99 per unit. Company X now has to incur more tens of thousands of pounds in legal and experts fee to investigate the claims of Company C.

So in this example, Company X now has three companies demanding a total of €3.99 per unit for EXACTLY the same 1000 SEPs. Company X is not getting any more. It

is looking to obtain a license to the same 1000 LTE patents, but it has cost it thousands more in fees and management time, and the royalty rate for its IoT device has nearly doubled.

What was one license discussion (with Company X) is now three or more license discussions.

What was one license fee is now three or four license fees, which are cumulatively significantly more than they were before.

Even more egregious is the fact that Company A might agree with Company B to take a cut (perhaps 70%) of the license fees that Company B secures. So Company A is now in effect getting €2.70 from Company X - €2.00 direct from Company X and €0.70 (70% of €1.00). It has also received the £10 million from Company B.

The FSA believes that guidelines need to be provided to curb this type of abuse of the principles of FRAND licensing.

Conclusion

Our members are united in the view that unfair and unreasonable SEP licensing practices pose a significant risk to the innovation eco-system, create barriers to entry for new market players, threaten to stifle the full potential for economic growth across major industry sectors, and ultimately harm consumer choice.

We believe that our experiences with licensing behaviours, successes and abuses in connection with SEPs can provide the UKIPO with valuable insight as it reviews the SEPs, FRAND issues, and considers possible updates and clarifications.

Providing clarity on licensing of SEPs on FRAND terms based on the principles identified above will further enhance and strengthen the UK's IP regime.

We hope that the UKIPO finds our perspectives helpful, and thank the UKIPO for its efforts to promote a healthy IP ecosystem that promotes innovation, and benefits industries and consumers.

We would be pleased to make ourselves available should you have any follow-up questions or wish to have further insight regarding our perspectives.

Sincerely,

The Fair Standards Alliance
Committed to Innovation

Further information about the alliance is available at www.fair-standards.org/.