

# IP Europe Response to Consultation CMA174con Draft Guidance on the Application of the Chapter I Prohibition in the Competition Act 1998 to Horizontal Agreements

### **About IP Europe**

IP Europe members are research and development-intensive organisations whose inventions are protected by intellectual property rights (IPR), representing key innovators in standardised technology. IP Europe's goal is to promote the vital importance of IPR to support world-leading, sustainable innovation ecosystem.

#### Introduction

IP Europe welcomes the opportunity to participate in the Competition and Markets Authority (CMA) public consultation on the draft revised Guidance on horizontal agreements ("Horizontal Guidance"), which are intended to replace the EU's Guidelines on horizontal cooperation agreements (EU Horizontal Cooperation Guidelines) in the UK. In doing so, IP Europe refers to the comments it provided to the CMA consultation of 11 January 2022.

As indicated previously, IP Europe considers that changes to the pre-existing European Commission Horizontal Guidelines should be made only in response to clear economic evidence of material harm. Further, we would like to emphasise the need for a balanced approach<sup>2</sup> to the Horizontal Guidance that:

- acknowledges that open standards are effectively accessible;
- continues to reflect business model neutrality and does not restrict the types of undertakings that can participate in standards development or license on the basis of FRAND, thus allowing for different interests and different business models (see paragraph 9.8 of the draft Horizontal Guidance);
- does not erroneously assume that ensuring effective access to a standard requires granting a licence;
- ensures that well-accepted competition law principles govern the ex-ante declaration of royalty rates by participants in standard setting;
- does not address unilateral and vertical conduct that is not properly within the scope of the Guidance:
- does not include an unsupportable analogy which seeks to create an equivalence between joint purchasing arrangements for tangible property (passing of property rights upon agreed delivery and payment terms, allowance for an enforceable debt) and the licensing of intangible property which is effectively accessible without a licence and without payment. In the context of open standards, licensing negotiation groups (LNGs) increase the risk of patent hold out and as a concept, appear incompatible with FRAND licensing principles, legal and commercial certainty, and efficient licensing practices;
- addresses competition concerns by taking into account the growing, well-documented problem of hold-out by a few yet significant actors in the market, and the implications for the well-functioning of the open standardisation system that is one of the cornerstones for innovation in the UK as

<sup>&</sup>lt;sup>1</sup> The responses below reflect the collective input of its members, which have extensive experience with various standard development organisations (SDOs) and similar consortia/fora. It may not represent the complete position of the individual members, nor their respective practices, and individual members of IP Europe may have different perspectives on the various policy topics.

<sup>&</sup>lt;sup>2</sup> As IP Europe has observed previously, there is only a small number of companies making significant contributions to standards as compared with a very large (and increasing number) of implementers which benefit from standardised technology. This fact has implications in terms of taking a purely statistical approach to the responses/data provided in response to the consultation. We hope that the CMA will factor this into their assessment.

recently highlighted in Chapter 9 of the government's Science and Technology Framework published on 6 March 2023.

We observe that the CMA, when undertaking a review of other EU instruments formerly applicable in the UK, has previously adopted an approach whereby laws and regulations applying pre-Brexit have been retained, and only modified in so far as needed where compelling evidence demonstrates that the characteristics and needs of the UK post-Brexit are distinctly different compared to the respective characteristics and needs of the UK pre-Brexit.

Overall, it is considered that the framework of the Horizontal Guidelines, HBERs and Specialisation HBER has fostered and preserved competitive markets at the UK and EU levels, allowed for legal certainty on compliance with competition law, and has enabled consistency and efficiency in business practices. The open standardisation system – built on effective IP protection and enforcement and FRAND licensing principles – is generally working well albeit under increased pressure of hold-out behaviour (as further discussed below). The system is providing broad and effective access to standardised wireless technology for implementers across sectors, and for all actors in the relevant value chains. Moreover, access is provided at reasonable cost.

Unless clear benefits from divergence can be safely assumed, it is considered that maintaining a close connection between the respective competition frameworks in the UK, the EU and other trading partners of the UK would more likely benefit UK consumers, businesses, innovation and the UK economy overall.

### Chapter 9 of the Horizontal Guidance

Chapter 9 of the Guidance is concerned with how standard development organisations (SDOs) develop standards and ensure effective access to those standards on a fair, reasonable and non-discriminatory (FRAND) basis. They are intended to provide guidance to SDOs from the Chapter I prohibition.

The Guidance should not be directed to bilateral licensing negotiations (which might only be considered to fall under Chapter II). Accordingly, the Guidance should not prescribe whether or how an IPR holder is to license its IPR. Provided that the voluntary commitment made to an SDO ensures effective access to a standard on a FRAND basis, that should be the end of the matter as far as the applicability of Chapter I is concerned, as licensing takes place outside of the standard setting process.

### FRAND Access: Paragraphs 9.22 and 9.33

We wish to express strong and deep concern with certain aspects of paragraphs 9.22 and 9.33 of the draft Guidance. We note that the FRAND regime implemented by many standards bodies complying with the current EU Horizontal Cooperation Guidelines is properly and explicitly recognised as enabling "effective access" to a standard and is therefore procompetitive. Nevertheless, we express serious concern that the implementation of the effects-based analysis laid out in the draft Guidance, as well as the unduly narrow "safe harbour" articulated in paragraph 9.33, will have severe and unanticipated consequences.

While these two paragraphs seek to achieve a balance between access and licensing, the draft Guidance unfortunately starts from a position which does not take into account the nature of the markets concerned. Whilst it is legally true that use of a patented invention without a licence is an infringement (i) the law also provides for exhaustion of patents once there is a single licence in a value chain, and (ii) as a practical matter, in many circumstances, owners of standard essential patents (SEPs) do not require every implementer in the value chain to take a licence even though they would be legally entitled to do so, if necessary through the mechanism of enforcement proceedings. By assuming a licence is always needed for effective access, the draft Guidance is at odds with the legal position in many cases ((i) above), and with the practical operation of the markets concerned in which there are longstanding recognised commercially sound practices for efficiently licensing standard essential patents ((ii) above). As a result, the draft Guidance also appears to reflect a misunderstanding about the nature of IPR, the nature of open standards, and any voluntary commitments provided under the IPR policy of an SDO. The draft Guidance sits in tension with some court decisions. and longstanding recognised commercial practices for licensing SEPs. The presumption that a licence is needed to effectively access a standard where there is essential IPR is in error.

The legal nature of IPRs informs the whole situation as to commercial practices. Like all IPRs, a patent comprises a right to exclude, subject to proof of infringement. In consequence it is of little practical effect unless the right is asserted, particularly in an environment where it is routinely infringed. The ubiquitous nature of standardised technologies (notably the cellular wireless standards 2G, 3G, 4G etc) and the vast disparity between the number of SEP owners and the number of companies implementing standardised technology in their products and services, mean that the SEP licensing environment works in reverse. Implementers are also afforded certainty, and a form of defence, by the FRAND commitment required of SEP owners by SDOs. In these circumstances the normal commercial practice is for an implementer to use the standardised technology in its products and services. Under relevant law, in the event that an implementer is entitled to rely upon the FRAND criteria, it is required to behave in a manner which demonstrates that it is willing to take a licence on FRAND terms. In the unusual circumstance that there is irreconcilable disagreement between a licensor and potential licensee as to what constitutes FRAND terms, an implementer will not be prevented from marketing infringing products and services if it is willing to abide by terms determined by a court based on FRAND licensing principles. The issue from a competition law perspective is therefore not whether there is a licence, but whether the patent owner is seeking to deny access in a manner that would harm competition. For SEPs, it is usually the case that the patent owner has given a contractual assurance to an SDO to provide access on the basis of fair, reasonable and nondiscriminatory (FRAND) licensing principles. That the SDO IPR Policy provides for FRAND-based licensing should be all that is needed for an SDO to be in a "safe harbour" for the purposes of Chapter I's applicability to SEPs.

The assurance sought by SDOs is often, but not always, provided through some kind of commitment from an SEP owner that, if it were to seek to license its essential patented technology, it will do so on FRAND licensing principles. This is how the pre-existing EU Horizontal Guidelines have always been understood and is consistent with competition law with the UK's major trading partners. The so-called "license-to-all" concept, i.e., an implementer is entitled to a licence on request, is in fact contrary to many SDO IPR policies, gives rise to issues around compulsory licensing, patent exhaustion and inefficient licensing practice, and can exacerbate hold out as recognised in paragraph 9.10 in the draft Horizontal Guidance.

It is also notable, from a competition law standpoint, that the EU Court of Justice (CJEU), in its decision in *Huawei v ZTE*, did not start from the basis that the alleged patent infringer could not implement third party SEPs in its products without a licence. The Court started from the correct assumption that effective access was already available to the implementer (and always is). In confirming the licensing framework for a FRAND-based licensing negotiation, the court created a safe harbour under competition law for patent holders that took specific steps prior to bringing an action of patent infringement. Notably, the UK Supreme Court has taken a similar direction in *Unwired Planet v Huawei*.

The approaches taken by the CJEU and UK Supreme Court take account of the interests of patent holders, the development of innovative standards and wide adoption of the standard. The Courts rightly focus the issue not on the SEPs but rather on the conduct of the parties, on a bilateral basis, and the commercial offers made by them.

Just as importantly, an SDO IPR Policy cannot require participants to license at all levels of the value chain. This is not the nature of the social contract for patent rights being granted in return for publication of the patent, nor the contract regarding voluntary contributions to open standards – the latter of which are published and made accessible based on FRAND licensing principles in return for the right to obtain a reasonable return. All licensing negotiations for SEPs occur outside an SDO. It is not the role of these fora for international technical cooperation to intervene in the commercial sphere.

Paragraph 9.33 thus errs by not assuming that effective access to underlying IPR is already available, and that licensing at all levels of the value chain is required. Effective access is the starting point from an SDO's perspective and that of its members. Indeed, for the vast majority of standards there is no licensing of IPRs, even if IPRs cover those standards. One simple reason is that it is often not worthwhile licensing the underlying IPRs, for cost versus return reasons. Failure to license does not equate to a denial of effective access.

SDO IPR policies come in a wide variety of forms – very few seek to dictate how licensing is done beyond seeking some kind of FRAND assurance. SDOs are not well-placed to pre-determine licensing terms, and

in any case their members will typically come from a wide range of stakeholders, each with their own interests and business models. FRAND commitments are therefore deliberately brief on a number of aspects to balance those interests and in particular do not specify any licensing level or specific preference for any licensing model. In practice, for legal and policy reasons, licensing is nearly always done at a single level in a value chain for a particular technology – and this level is nearly always at or near the end product manufacturer level, and very rarely at the lowest component product level.

The debate about the licensing level in the supply chain has recently been addressed by Courts in the EU. In this regard, European courts have confirmed that licensing should take place at the point in the value chain where the *value* of connectivity is realised.

In Nokia v Daimler (Regional Court (Landgericht) of Mannheim 18 August 2020 - Case No. 2 O 34/19) the Court pointed out "that the patent holder must, in principle, 'be given a share' in the 'economic benefits of the technology to the saleable end product at the final stage of the value chain'."<sup>3</sup>

In addition, the Court found that the selling price of telematic control units (TCUs) did not sufficiently mirror the value of Nokia's SEPs for the cars produced by Daimler, which are the relevant end devices in that case. The selling price of TCUs corresponds only to Daimler's respective costs. Connectivity, on the other hand, allows Daimler to generate income from additional services offered to its clients, save costs to it and optimise its R&D expenses. Connectivity secures the opportunity to create this value. In addition, the Court noted that the acceptance of the licensing model of the Avanci platform (which grants licences exclusively to car manufacturers, not TCU manufacturers) by several of Daimler's main competitors serves as a further indication that focusing on the value of the protected technology for the end product is also reasonable in the automotive sector.<sup>4</sup>

In Sharp v Daimler, the Regional Court (Landgericht) of Munich on 10 September 2020 (Case No. 7 O 8818/19) indicated that "EU competition law does not establish an obligation to license SEPs at all levels of the value chain" and that patent holders are in principle free to choose the level of the value chain for licensing.<sup>5</sup>

We note also that at paragraph 9.22, the following is stated:

"In order to ensure effective access to the standard, the IPR policy would need to require participants wishing to have their IPR included in the standard to provide an irrevocable commitment in writing to offer to license their essential IPR on fair, reasonable and non-discriminatory terms ('FRAND commitment')<sup>363</sup>. The FRAND commitment could be drafted so as to require the IPR holder to offer a licence to any third party seeking a licence in order to implement the standard. <sup>364</sup>" [our underline]

Footnote '363' refers to paragraph 53 of the CJEU decision in *Huawei Technologies Co. Ltd. v ZTE Corp.* and *ZTE Deutschland GmbH* (C-170/13, EU:C:2015:477), and to the Commission Decision in *Case AT.39985 – Motorola*, that predates the aforementioned CJEU decision. And footnote '364' notes the underlined part to be the most permissive and to fall outside the Chapter I prohibition.

We appreciate that the draft Guidance in paragraph 9.22 does not take on an absolute "license-to-all" position, which would be highly damaging to the licensing of SEPs and in turn standardisation. However, for the reasons stated above, we have deep concerns with the emphasis on any kind of "license-to-all" safe harbour. Additionally, such a provision is more likely than not to harm competition in standardisation by discouraging contribution of new technologies to standards, at the same time as upsetting long-standing, efficient, commercial practices of licensing at a single level, which in principle are objectively procompetitive. Licensing on different levels significantly increases the likelihood of discrimination (e.g., through royalty double-dipping at different levels), while adding significant burdens and delays to obtaining licences and incentivising hold out tactics.

<sup>&</sup>lt;sup>3</sup> See <a href="https://caselaw.4ipcouncil.com/german-court-decisions/lg-mannheim/nokia-v-daimler">https://caselaw.4ipcouncil.com/german-court-decisions/lg-mannheim/nokia-v-daimler</a>.

<sup>&</sup>lt;sup>4</sup> See <a href="https://caselaw.4ipcouncil.com/german-court-decisions/lg-mannheim/nokia-v-daimler">https://caselaw.4ipcouncil.com/german-court-decisions/lg-mannheim/nokia-v-daimler</a>.

<sup>&</sup>lt;sup>5</sup> See https://caselaw.4ipcouncil.com/german-court-decisions/lq-munich-district-court/sharp-v-daimler.

With respect to the reference in footnote 363 to the CJEU decision, we note that the Landgericht of Munich correctly states that whilst the CJEU pointed out that the FRAND undertaking creates 'legitimate expectations' on the part of third parties to be licensed by the patent holder, this did not create an obligation to license *all* suppliers of an end-device manufacturer.<sup>6</sup>

A similar position has recenly been affirmed by a United States Court of Appeals. In addition, a strict application of the "license-to-all" text of paragraph 9.22 is not possible as a patent can only be licensed once in the value chain because of the principle of patent exhaustion. Patent exhaustion laws prevent or limit licensing the same patent twice or more for a particular product/service/purpose at different levels of a supply chain. This is to prevent a patent holder abusing its patent rights, e.g., by doubling its royalties by licensing both the supplier and the customer. In a complex real-world supply chain, resembling more a cobweb than a simple linear line, where multiple suppliers may supply a customer and/or multiple customers are supplied by a supplier, and where the chain may continually change, patent licensing on different levels would be extremely inefficient and becomes all but impossible.

Given this reality, the words "to any third parties" in paragraph 9.22 (and likewise "to all third parties" in the pre-existing Horizontal Guidelines) remain a concern for IP Europe. The language in this paragraph is not only in contradiction with the aforementioned court decisions, it also seems at odds with the rest of the Guidance. The rest of the Guidance rightly focuses on ensuring effective access for those wanting to use standardised technology covered by essential IPR, which is also enshrined in the access based IPR policies of SDOs such as ETSI. After all, as noted, "access" does not equate to a need for a "licence".

Moreover, the original paragraph 285 of the Horizontal Guidelines (now 9.22 in the draft Guidance) has in the recent past been wilfully misinterpreted by certain implementers and their industry associations as imposing a compulsory "license-to-all" rather than an "access-for-all" requirement.

Deleting the text referring to "any third parties" in paragraph 9.22 of the draft Guidance, together with removing proposed new paragraphs 9.33 and 9.44 and footnote 391, would be sufficient to: eradicate the potential internal inconsistency in the Guidance; provide clarity that 'effective access' is the consequence of the open standards ecosystem and that an IPR holder cannot be required to offer a licence to any third party seeking a licence in order to implement the standard; remove a perceived issue which is complex or difficult to interpret; and reflect the widespread industry practice to license at the end-user device level in a growing number of sectors (as recently recognised by the courts in Europe and the U.S.A.). Finally, given the wide variety of standardisation activities and corresponding SDOs (as highlighted above), it would be detrimental for the Horizontal Guidance to be interpreted in such a manner that it would prefer or, even worse, require a particular licensing level. The draft Guidance indeed recognises that SDOs can adopt different IPR Policies

IP Europe would therefore strongly recommend adapting the text of paragraph 9.22 by deleting the underlined sentence, in addition to removing proposed new paragraphs 9.33 and 9.44 and footnote 391.

### Collective Royalty Cap Setting

The draft Horizontal Guidance amends the EC's current Horizontal Guidelines in several instances to suggest that SDOs would not raise competition concerns by disclosing the maximum royalty stack for a standard.

As a threshold matter, IP Europe notes that the approach taken by the CMA in its draft Guidance provides greater clarity than the text proposed by the European Commission in its 2022 draft Horizontal Guidelines,

<sup>&</sup>lt;sup>6</sup> See https://caselaw.4ipcouncil.com/german-court-decisions/lg-munich-district-court/sharp-v-daimler.

<sup>&</sup>lt;sup>7</sup> See Case 20-11032 *Continental Automotive Systems Inc. v. Avanci LLC* (Court of Appeals for the 5<sup>th</sup> Cir., 28 February 2022) https://www.ca5.uscourts.gov/opinions/pub/20/20-11032-CV0.pdf. See also Eileen McDermott, Fifth Circuit Says Auto Parts Suppliers Have No Article III Standing to Bring Antitrust Claims Against SEP Holders (IP Watchdog, 2 March 2022) ("The decision is important because it clarifies that [Internet of things] IoT suppliers have no standing to bring so-called 'license to all' claims against SEP holders who license at the end device level (OEM level)") <a href="https://www.ipwatchdog.com/2022/03/02/fifth-circuit-says-auto-parts-suppliers-no-article-iii-standing-bring-antitrust-claims-sep-holders/id=147098/">https://www.ipwatchdog.com/2022/03/02/fifth-circuit-says-auto-parts-suppliers-no-article-iii-standing-bring-antitrust-claims-sep-holders/id=147098/</a>.

the latter which could be interpreted as giving the collective determination of a royalty cap the same treatment currently afforded to unilateral *ex ante* disclosure of most the restrictive licensing terms – an outcome that would be incorrect as a matter of settled competition law. In particular, footnote 358 to paragraph 9.13 has been amended to clarify that "genuine unilateral ex ante disclosures <u>by individual IPR holders</u> of their most restrictive licensing terms" are not prevented (emphasis added to reflect amendments).

The draft Guidance properly recognises that joint fixing of prices for IPR can constitute a restriction of competition by object. Paragraph 9.13 retains the concept from the existing Horizontal Guidelines that "any agreements to reduce competition by jointly fixing prices [...] of substitute IPR or technology will constitute restrictions of competition by object". Footnote 358 to paragraph 9.13 further notes that it "does not prevent standard development organisations disclosing the total maximum stack of royalty for the standard.". While the announcement by an SDO of the royalties individually set by patent holders could conceivably be consistent with competition law, it is critical that this activity not serve as cover for the joint setting of royalty rates or create a false impression. It has long been recognised that the unilateral announcement of most restrictive licence terms and the collective determination of a royalty cap are not the same: the former is unilateral conduct not subject to Article 101 TFEU8, while the latter can constitute anti-competitive coordinated price setting. While unilateral ex ante disclosure could, in theory, improve price competition, the collective setting of a royalty cap does not offer this potential efficiency. Rather, it could impede price competition between technologies.

Similarly, under the effects-based analysis, in footnote 388 to paragraph 9.42, the draft Guidance takes the position that "standard development organisations could take an active role in disclosing the total maximum stack of royalty for the standard". The footnote contemplates that "IPR holders can share the total royalty stack," which it is asserted would operate "similar to the concept of a patent pool." Paragraph 9.42 further states that such "disclosure [...] of a maximum accumulated royalty rate by all IPR holders" would not only be subject to an effects-based assessment, but that, under such an assessment, such collective royalty cap setting "will not, in principle, restrict competition within the meaning of the Chapter I prohibition". As noted in more detail below, both DG Competition and other antitrust authorities / agencies have given significant prior analysis to this issue and have tended to find that the analysis of such provisions was very fact specific and not amenable to a presumption of legality. Accordingly, IP Europe is of the view that the draft Guidance should not suggest that such conduct is presumptively pro-competitive, or that an SDO could operate similar to a patent pool.

The United States Department of Justice and Federal Trade Commission issued an analysis of these issues in their 2007 report on *Antitrust Enforcement and Intellectual Property Rights*. In that report, the agencies drew a distinction between collective rate setting and "an IP holder's voluntary and unilateral disclosure of its licensing terms," which the agencies determined "is not a collective act subject to review.". The agencies expressed that "summary condemnation would be justified if IP holders were to reach naked agreements on the licensing terms they will propose to an SSO that permits multilateral licensing negotiation.". In addition, the agencies noted that joint licensing discussions could provide an avenue for the exercise of "group buying power," and noted concerns that "joint ex ante licensing bargaining could, in theory, reduce incentives for innovation.". Even under an effects-based analysis, when – among other things - "potential licensees refuse to license that particular patented technology except on agreed upon licensing terms," the agencies found the possibility that "the ex-ante negotiation among potential licensees does not preserve competition among technologies that existed during the development of the standard but may instead simply eliminate competition among the potential licensees for the patented technology.". In a contractive subject to review."

<sup>&</sup>lt;sup>8</sup> We note, however, the European Commission's position in the Liner Shipping cases, where it was held that merely making price announcements can be construed as an invitation to collude - or "price signaling" – which can lead to illegal price coordination even without direct contact between competitors. See Case AT.39850 – Container Shipping.

<sup>9</sup> U.S. DEPT. JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION (2007).

<sup>&</sup>lt;sup>10</sup> *Id*. at 54.

<sup>&</sup>lt;sup>11</sup> *Id*. at 51.

<sup>&</sup>lt;sup>12</sup> *Id*. at 52-53.

<sup>&</sup>lt;sup>13</sup> *Id*. at 53.

The views of the U.S. agencies are consistent with the opinion that DG Competition previously offered to ETSI. <sup>14</sup> In its letter to ETSI, DG Competition noted that *ex ante* price negotiation based upon unilateral royalty disclosure had the potential to promote "competition on the basis of both technology and price," but that, "whilst we appreciate the desire on the part of licensees for certainty in the royalties that they will have to pay," the collective setting of a royalty cap "risks negating the possible benefits of [the aforementioned] 'pure' ex ante regime.". The letter observed that, "whereas a 'pure' ex ante regime has the potential to bring the price down to a competitive level through competition on the basis of price [...] a collective ex ante royalty cap regime [...] does not appear to allow for any such price competition.". Rather, the letter noted that, "indeed, it would appear to precisely preclude any such price competition from occurring, since the price of each essential patent is <u>fixed in advance [...]</u>". Thus, under the prior guidance that DG Competition offered to ETSI, it found that the collective setting of a royalty cap actually hinders price competition between technologies.

Finally, footnote 388 in the draft Guidance is inconsistent with other sections of the draft Guidance. It conflicts with the guidance in amended footnote 371, which correctly observes that "standard development organisations are not involved in the licensing negotiations or resultant agreements.". In addition, a total royalty stack would require a 'top-down'<sup>15</sup> approach to determining royalties. However, footnote 375 has been amended to make clear that "the methods described here are not exclusive and other methods reflecting the same spirit of the described methods can be used to determine FRAND rates.". Yet, if the participants in an SDO were to jointly set the maximum royalties for their standard, it would seem to be impossible to use any approach other than a top-down valuation.

For these reasons, IP Europe respectfully suggests that the reference to maximum royalty stacks be removed from the revised draft Guidance, and that the original text be retained/reinstated.

# Vertical Agreements and Unilateral Conduct Outside the Scope of the Horizontal Guidance

A stated objective of the draft Horizontal Guidance is to "explain how the CMA applies competition law and, in particular, the Chapter I prohibition in the Competition Act 1998 (CA98) to horizontal agreements." <sup>16</sup> The Introduction to the Guidance goes on to reiterate that "horizontal agreements are agreements entered into between actual or potential competitors.". <sup>17</sup> IP Europe respectfully cautions the CMA to take care to ensure that the conduct described in the draft Guidance is properly within its scope.

In this regard, the draft Guidance is rightly focused on the application of Chapter I and specifically the potential distortion of competition by agreements between undertakings in horizontal relationships. As recent amendments clarify, however, standardisation frequently involves parties in vertical relationships, which are not properly within the scope of Horizontal Guidance. It is odd therefore that the revised draft Guidance has increased reference to unilateral conduct and to potential abuse(s) of a dominant market position, which concern the interpretation and potential application of Chapter II. Therefore, IP Europe requests that the Guidance more clearly delineate the discussion of conduct that is within its scope from the discussion of conduct that falls outside its scope – including standardisation agreements involving parties in a vertical relationship.

The draft Horizontal Guidance acknowledges the fact that many participants in standardisation are not rivals. Paragraph 9.8 retains the observation that participants in standardisation can be both "upstream-only undertakings". Recognising this, paragraph 9.5 is now amended to state that "participants in standardisation are not necessarily competitors". IP Europe supports this amendment, which in many ways encapsulates the observation in paragraph 9.8. The text recognises the fact that upstream and downstream undertakings are not horizontal competitors. Rather, their relationship is vertical.

This observation begs the question, however, as to whether the competition concerns articulated in the draft Guidance apply in all circumstances of standardisation. As paragraph 9.5 notes, "[s]tandard

<sup>&</sup>lt;sup>14</sup> Letter from the EC Competition DG on ETSI IPR Group Discussions, ETSI GA/IPRR05(06)12 (22 June 2006).

<sup>&</sup>lt;sup>15</sup> See paragraph 487 of the Draft Guidelines.

<sup>&</sup>lt;sup>16</sup> Draft Horizontal Guidance, paragraph 1.1.

<sup>&</sup>lt;sup>17</sup> Draft Horizontal Guidance, paragraph 1.1.

development can, however, in specific circumstances where competitors are involved, give rise to restrictive effects on competition". When competitors are not involved – but rather the participants are in a vertical relationship – it would follow that the potential harm to competition would not occur.

Further, the revised draft Guidance appears to encompass conduct that would properly fall to be considered under Chapter II as a potential abuse of dominance. Paragraph 9.10, for example, suggests that so-called patent "hold up" would be an abuse of dominance. Footnote 355 further states that "high royalty fees can only be qualified as excessive if the conditions for an abuse of dominant position [...] are fulfilled.". The new text in paragraph 9.27, which addresses methods for patent valuation, indicates that: "This Guidance does not seek to provide an exhaustive list of appropriate methods to assess whether the royalty fees are excessive or discriminatory under the Chapter II prohibition.". While IP Europe agrees that the CMA should not be seeking to provide an exhaustive list of potential valuation methods, we question whether it is appropriate to address this issue at all in the Horizontal Guidance as this might erroneously suggest that its purpose is to provide guidance on the analysis and potential application of Chapter II. Rather than providing clarity and legal certainty to businesses, the revised draft Horizontal Guidance risks causing confusion.

In any event, the addition of reference to Chapter II in paragraph 9.27 (and elsewhere) in the proposed Horizontal Guidance is potentially misleading in terms of dominance/the existence of market power. As the draft Guidance observes in paragraph 9.11, "there is no presumption that holding or exercising IPR essential to a standard equates to the possession or exercise of market power." Rather, "the question of market power can only be assessed on a case-by-case basis". In support of this proposition, the proposed draft Guidance cites the decision in Case AT.39985 - Motorola. As the cited section shows, the European Commission undertook an extensive analysis of whether Motorola had market power. In addition to examining the extent to which industry was locked-in to the standard, the Commission also examined whether the SEP implementer, Apple, had countervailing buyer power. <sup>18</sup>

In footnote 363, the proposed draft Guidance makes reference to the ruling of the Court of Justice in *Huawei v. ZTE* and the Commission's *Motorola* decision. Both of those cases involved a party seeking recourse to national courts for an order prohibiting patent infringement. However, the current Horizontal Guidelines do not address such conduct. With respect, nor should any future Guidance from the CMA, as this is unilateral conduct which would properly be considered under Chapter II. As such, these references should be removed.

In the light of the above, IP Europe respectfully recommends that the draft Horizontal Guidance be clarified to clearly recognise that conduct involving parties in vertical relationships and unilateral conduct are outside the scope of the Horizontal Guidance.

### Licensing Negotiation Groups ("LNGs")

Paragraph 6.2 of the draft Guidance provides that "[j]oint purchasing arrangements can be found in a variety of economic sectors and involve the pooling of purchasing activities" and, specifically, "[g]roups of potential licensees may seek to jointly negotiate licensing agreements for standard essential patents with licensors in view of incorporating that technology in their products (sometimes referred to as licensing negotiation groups)."

At the outset, IP Europe notes that paragraph 6.2 appears to suggest that there are already examples of so-called licensing negotiation groups (LNGs) operating in practice. IP Europe and its members (which include leading SEP holders) are not aware of such examples.

In fact, the LNG concept was introduced at a relatively late stage of the current review of the European Commission's proposed draft Horizontal Guidelines. They were first referenced in Section 4.2. of the Staff Working Document<sup>19</sup> (setting out the additional evidence gathered through other Commission initiatives) on the basis of a high-level and theoretical proposal regarding LNGs (Proposal 75) in the SEPs Expert

<sup>&</sup>lt;sup>18</sup> Commission Decision in Case AT.39985 - *Motorola - Enforcement of GPRS standard essential patents*, recitals 221-270

<sup>&</sup>lt;sup>19</sup> See the <u>Staff Working Document and its annexes</u> summarising the results of the evaluation of the HBERs and Horizontal Guidelines published on 6 May 2021.

Group report,<sup>20</sup> which highlighted a number of competition concerns (discussed below) and the need for scrutiny from competition authorities.

In these circumstances, the inclusion of LNGs in the draft Guidance is at the least premature - in particular where there is no need for, or practical experience of, LNGs. The draft Guidance does not provide an "Example" of an LNG in the joint purchasing Chapter. In most cases, it is anticipated that LNGs would be the mechanism whereby competitors could engage in anti-competitive discussions for licensing SEPs with the sole or main aim of reducing or limiting price, thereby facilitating a collusive outcome on the market. On this basis, IP Europe considers that references to LNGs and the relevant framework for the assessment of LNGs should be removed from the Guidance.

LNGs raise significant competition concerns. Notably those concerns identified by the SEPs Expert Group<sup>22</sup>, as well as academics and industry commentators<sup>23</sup> that LNGs would: (1) offer additional hold-out opportunities for implementers (coordinated hold-out/collective boycott) to delay or avoid the conclusion of licence agreements; (2) effectively operate as a buyers' cartel, which would depress SEP value below FRAND levels; (3) provide the means and opportunity for implementers of standardised technology to engage in anti-competitive information exchange and/or collusion; and give rise to greater risks of inefficient and uncertain licensing arrangements (particularly if one or a few members of a so-called LNG breach or terminate a collectively 'negotiated' licence agreement).

In view of (1) the growing body of case law from courts across Europe highlighting the variety of hold-out strategies adopted by certain implementers of standardised technologies identified in IP Europe's previous submissions to the UK's Intellectual Property Office, the European Commission and the CMA in the context of the review of their Horizontal Guidelines;<sup>24</sup> (2) examples of companies, including in the IoT space, colluding to avoid taking licences to SEPs according to the FRAND licensing framework;<sup>25</sup> and (3) the welcome (and overdue) express recognition of hold-out in paragraph 9.10 of the draft Guidance, experience has demonstrated that the presumption of an infringement by object is justified.

Equally, while paragraph 6.8 of the draft Guidance rightly observes that joint purchasing arrangements "normally do not amount to a restriction of competition by object if they truly concern joint purchasing" and paragraph 6.9 states they can be "distinguished from buyer cartels", the only proposal for forming an LNG of which IP Europe is aware<sup>26</sup> appeared to be aimed at: (a) coordinating those purchasers' individual competitive behaviour on the market or influencing the relevant parameters of competition through, for example, fixing or coordinating purchase prices or other aspects of prices (including agreements fixing wages or not to pay a price for a product) or other trading conditions, allocating purchase quotas, and sharing markets and suppliers; and (b) influencing those purchasers' individual negotiations with or individual purchases from suppliers through, for example, coordinating the purchasers' price negotiation strategies or exchanging competitively sensitive information on the status of such negotiations with suppliers" as identified in paragraph 6.9.

In these circumstances, IP Europe respectfully requests that the CMA consider carefully the question of the appropriate framework for the competitive assessment of the LNG concept, and specifically the

<sup>&</sup>lt;sup>20</sup> See Report from the Group of Experts on Licensing and Valuation of Standard Essential Patents 'SEPs Expert Group'.

<sup>&</sup>lt;sup>21</sup> In fact, there is no guidance, or even indication, in the draft Guideance about how it is envisaged LNGs could/would operate in practice and what they would entail and certainly no discussion of any "appropriate mechanism and controls" as raised by the SEPs Expert Group.

<sup>&</sup>lt;sup>22</sup> See Report from the Group of Experts on Licensing and Valuation of Standard Essential Patents 'SEPs Expert Group'.

See, for example, <a href="https://www.4ipcouncil.com/research/licensing-negotiation-groups-what-why-how;">https://www.4ipcouncil.com/research/licensing-negotiation-groups-what-why-how;</a>;

<a href="https://www.4ipcouncil.com/research/licensing-negotiation-groups-seps-collusive-technology-buyers-arrangements-pitfalls-and-reasonable-alternatives;">https://www.4ipcouncil.com/research/economic-case-against-licensing-negotiation-groups-internet-things;</a>; SEP Licensing Negotiation Groups -- Part I; SEP Licensing Negotiation Groups -- Part II; FOSS Patents: EU competition chief's tough talk on cartels doesn't bode well for automotive SEP licensing negotiation groups; and 'Why proposed IoT licensing negotiation groups are an antitrust non-starter', Igor Nikolic, at <a href="https://lnkd.in/gNbRcHy7">https://lnkd.in/gNbRcHy7</a>.

See <a href="https://www.ipeurope.org/position-papers/unwilling-sep-licensees-hold-out-strategies/">https://www.ipeurope.org/position-papers/unwilling-sep-licensees-hold-out-strategies/</a>. See also <a href="https://www.ipeurope.org/blog/examples-of-hold-out-strategies/">https://www.ipeurope.org/blog/examples-of-hold-out-strategies/</a>.

<sup>&</sup>lt;sup>25</sup> See <a href="https://www.ipeurope.org/blog/is-the-smart-meter-industry-engaged-in-coordinated-hold-out/">https://www.ipeurope.org/blog/is-the-smart-meter-industry-engaged-in-coordinated-hold-out/</a>. For a further example, see <a href="Cars or Car-tels?">Cars or Car-tels?</a> - KIDON IP.

<sup>&</sup>lt;sup>26</sup> See presentation of Uwe Wiesner for the DG GROW Webinar on 20 April 2021, available at: Webinar SEP: 20 April, presentations and documents at page 61 et seg.

question of whether an effects analysis is really more appropriate than allocating the LNG concept to the 'object box', to take account of all of the evidence provided on this issue throughout the entire review process.

As regards an effects-based analysis of the LNG concept, according to paragraph 6.17 of the draft Guidance, joint purchasing arrangements "must be analysed on a case-by-case basis in their legal and economic context with regard to their actual and likely effects on competition" (emphasis added), and the "analysis of the restrictive effects on competition generated by a joint purchasing arrangement must cover the negative effects on [...] the purchasing market or markets".

When considering the legal and economic context for the analysis of the LNG concept, it should be noted that, in stark contrast to the joint purchasing of tangible goods or services, in the context of SEP licensing, the nature of open standards means that implementers have access to, use, and profit from standardised technology without first having to take a licence.

In addition, as IP Europe has explained in previous white papers, some implementers engage in 'hold-out' strategies and wilfully infringe SEPs on the basis that they will only ever be required to pay FRAND royalties.<sup>27</sup> These factors are key to understanding the market dynamics and to the assessment of the market power of implementers, both individually and collectively as potential parties to a joint purchasing arrangement.<sup>28</sup> In this regard, the significant market/buyer power of implementers is such that an LNG is likely to give rise to considerable restrictive effects on competition within the meaning of Chapter I. The 'FRAND context' heightens, not mitigates, the risk. LNGs would be able to exercise collective monopsony power over SEP holders to force prices below a competitive or sustainable level.

As regards market power, paragraph 6.24 of the draft Guidance observes that: "There is **no absolute threshold** above which it can be presumed that the parties to a joint purchasing arrangement have market power so that the joint purchasing arrangement is likely to give rise to restrictive effects on competition within the meaning of the Chapter I prohibition. However, **in most cases** it is unlikely that market power exists if the parties to the joint purchasing arrangement have a combined market share not exceeding 15% on the purchasing market or markets as well as a combined market share not exceeding 15% on the downstream selling market or markets."

However, the negotiation of the terms of licences to standard essential patents by a group of potential licensees is not "most cases" and would likely have far broader implications and render the 15% market share threshold meaningless in practice. For example, it could (and most likely would) be argued that any rate negotiated by the LNG should be applicable to or indicative for many other market participants, regardless of the circumstances and market power that may be represented by the LNG vis-á-vis individual entities. As such, even if the participants in an LNG in theory represent less than 15% of the (properly defined) relevant market(s), in practice the terms negotiated with the LNG could have major impact. In these circumstances, IP Europe respectfully requests that the CMA, at a minimum, revise the Guidance to make clear that the 15% market share 'safe harbour' does not apply to the LNG concept.

When considering the potential for a "collusive outcome", paragraph 6.38 of the draft Guidance notes that: "When negotiating terms and conditions with suppliers, a joint purchasing arrangement may threaten suppliers to abandon negotiations or to stop purchasing temporarily unless they are offered better terms or lower prices. Such threats may be part of a bargaining process and may involve collective action by purchasers when a joint purchasing arrangement conducts the negotiations. Suppliers in a strong market position may use similar threats to stop negotiating or supplying products in their bargaining with purchasers. Such threats made collectively by joint purchasing groups do not usually amount to a restriction of competition by object, although they may in some cases give rise to negative effects. Any such negative effects arising from such collective threats should not be assessed separately but should be assessed in the light of the overall effects of the joint purchasing arrangement."

<sup>&</sup>lt;sup>27</sup> See supra n. 24.

<sup>&</sup>lt;sup>28</sup> Currently paragraph 6.31 of the draft Guidance merely indicates that "the analysis of whether the parties to a joint purchasing arrangement have buying power, the number and intensity of links (for example, other purchasing agreements) between competitors in the purchasing market are relevant". This does not reflect the specific factors/features that are relevant to the assessment of the buying power of a group of potential licensees of SEPs.

In this context, the draft Guidance refers to the example of temporary stops by the members of a retail alliance in ordering certain products and observes that "[s]uch temporary stops may result in the products selected by the individual members of the alliance being unavailable on the retailers' shelves for a limited period of time, namely until the retail alliance and the supplier have agreed on the terms and conditions of future supplies." Again, this underlines the stark contrast between the joint purchasing of tangible goods or services on the one hand and the joint negotiation of SEP licences on the other hand. As noted above, implementers have access to, use, and profit from standardised technology without first having to take a licence and there is significant evidence of a small number of significant bad faith implementers engaging in a variety of hold-out strategies, including co-ordinated hold-out, to delay or avoid taking a licence on FRAND terms.

Accordingly, rather than being part of the "bargaining process", such threats in the context of an LNG would constitute/perpetuate hold-out – i.e., 'efficient infringement', where unlicensed implementers simply appropriate technology without compensation for the use of such technology that requires substantial R&D investments by innovators years in advance of a standard being adopted ('free riding'). Depriving innovators who are responsible for developing fundamental cutting-edge technologies of fair and reasonable compensation undermines their ability and incentives to invest in critical (and risky<sup>29</sup>) R&D for future technologies and to participate in open, collaborative and consensus-driven standards development (with the standards being effectively accessible for integration into millions of connected products and services). This threatens the future of standardisation/standards development in 5G and 6G (and beyond).

While paragraph 6.27 of the draft Guidance acknowledges the risk that a joint purchasing arrangement "could discourage investments or innovations benefitting consumers" it suggests that these risks "may be larger for large purchasers that jointly account for a large proportion of purchases – in particular when dealing with small suppliers". This does not (adequately) reflect the market dynamics of SEP licensing and, in particular, the suggestion that "[r]estrictive effects on competition are less likely to occur if suppliers have a significant degree of countervailing seller power (which does not necessarily amount to dominance) on the purchasing market or markets" is incorrect.

In any event, it is unclear how the "bargaining process" discussed in paragraph 6.38 of the draft Guidance – i.e. threats to abandon negotiations or to stop purchasing temporarily for a finite number of tangible products or services – could operate within the *Huawei v ZTE* licensing framework, which confirms that a SEP holder may seek an injunction prohibiting the infringement of its patent or seek the recall of products for the manufacture of which that patent has been used against an unwilling licensee. In this context, we also note that paragraph 9.10 of the draft Guidance describes hold-out as conduct "attributable solely to the user of the standard", while this should naturally capture any 'unwillingness' by an LNG. Given the significant concerns that LNGs could be used as a vehicle for coordinated hold-out, we would invite the CMA to clarify this point. One way of achieving this, if an LNG concept is introduced, would be to delete the word "solely".

By contrast also to the conventional analysis of purchasing groups in relation to tangible goods, it is difficult to identify efficiencies from the creation of an LNG that do not already exist and which would justify the very evident distortions of competition to which an LNG would give rise in the standards context. The suggestion that if groups of implementers could collectively negotiate with individual or groups of SEP holders and patent pools it may lower transaction costs is hypothetical. It is very unclear that efficiencies or cost-savings would be generated by LNGs in practice and it has been suggested that similar (or greater) cost savings could be achieved through patent pools.<sup>30</sup> In any event, for SEP holders, any efficiencies would depend on the timely conclusion of licences and, given the hold-out risks posed by LNGs, it is unclear that such efficiencies would arise and an increased risk of collective non-compliance with FRAND-based licensing principles.

<sup>&</sup>lt;sup>29</sup> As observed in paragraph 9.25 of the draft Guidance, "FRAND commitments allow IPR holders to monetise their technologies via FRAND royalties and obtain a reasonable return on their investment in R&D which by its nature is risky. This can ensure continued incentives to contribute the best available technology to the standard."

<sup>&</sup>lt;sup>30</sup> See, for example, <a href="https://www.4ipcouncil.com/research/economic-case-against-licensing-negotiation-groups-internet-things">https://www.4ipcouncil.com/research/economic-case-against-licensing-negotiation-groups-internet-things</a>. Equally, in its response to the public consultation, the American Bar Association indicated that it was "skeptical that cooperation between users of standard essential technology in Collective Licensing Negotiations Groups (LNGs) would readily give rise to lower transaction cost and other efficiencies. At minimum, such initiatives require careful assessment." IP Europe shares this skepticism.

Finally, IP Europe understands that it has been suggested by certain stakeholders that LNGs are a necessary and/or natural counterbalance to patent pools. This demonstrates a fundamental misunderstanding of the role and nature of pools. In particular, patent pools: (1) combine complementary technologies; (2) are optional and not exclusive; (3) provide a pro-competitive alternative to direct/individual licences; (4) reduce transaction costs for licensees and SEP holders; (5) avoid/limit the risk of so-called 'double-dipping'; and (6) are known to adopt a policy of FRAND-based licensing. This is in contrast to LNGs which conceptually pose a significant threat to competition.

In the light of the above considerations, and the significant competition concerns posed by LNGs for potential licensees, the inclusion of LNGs and references to the relevant framework of assessment for licensing negotiation groups in the joint purchasing Chapter of the draft Guidance is misguided.

Rather than continuing to meet its objectives to "help businesses assess certain categories of horizontal agreements and establish whether they [...] comply with competition law", the inclusion of LNGs in the draft Guidance raises more questions than it provides answers.

The negotiation of FRAND licences for SEPs is not comparable with the (joint) purchasing of tangible goods or services and, while the draft Guidance references the need for parties to consider the relevant legal and economic circumstances, the draft Guidance itself has failed to reflect adequately, or at all, the specific features of the negotiations and the market(s) concerned. IP Europe would therefore propose that the concept of LNGs be removed from the draft Guidance. Alternatively, at a minimum, the Guidance should be redrafted to include specific analysis of the relevant market dynamics and other factors identified in this submission.

In its current state, in seeking to fit the proverbial square peg into a round hole, the draft Guidance fails to identify an appropriate framework of assessment for LNGs or consider necessary safeguards. This risks exacerbating rather than acknowledging and addressing the hold-out issue identified in paragraph 9.10, depriving SEP holders of appropriate remuneration and undermining their ability and incentives to participate in risky R&D. This poses a significant threat to the standards ecosystem, FRAND-based licensing, the future of standards development and UK leadership through meeting its innovation strategy.

# Proposed Revisions to the Text/Language of Specific Paragraphs of the Horizontal Guidance

In addition to the issues/areas identified above, IP Europe has identified some specific/detailed wording issues with the text/language of certain provisions of the draft Horizontal Guidance. These are outlined below.

### Paragraph 9.8

At paragraph 9.8 we note an imbalance in the description of the different interest groups involved with standards development. Whilst upstream-only undertakings are said to 'maximise' their royalties, downstream-only undertakings are said only to seek to 'reduce' royalties. The correct balance would be to observe that downstream-only undertakings are incentivised to 'minimise' royalties, or even avoid them altogether (as set out in paragraph 267 of the EU Horizontal Guidelines). In addition, it could be noted also that there are interests of vertically integrated companies that both develop technology and sell products. They have mixed incentives (again, as set out in paragraph 267 of the EU Horizontal Guidelines).

### Paragraph 9.10

As noted above, we welcome the addition of the last sentence in paragraph 9.10 of the draft Guidance, recognising the phenomenon of 'hold-out'. We note however that this is said to arise where "*licensing negotiations are drawn out for reasons attributable solely to the user of the standard*"<sup>31</sup> (emphasis added). As explained above, this could be misunderstood as meaning that hold-out can only occur where delay is

<sup>&</sup>lt;sup>31</sup> This again raises the question of the attributability of LNGs' behaviour to users of the standardised technology.

not in any way attributable to the licensor. That would be unrealistic since negotiation of a SEP licence can sometimes be complex and lengthy. We therefore suggest the word "solely" should be deleted.

### Paragraphs 9.23, 9.24 and 9.34

These paragraphs address disclosure requirements at SDOs; at paragraphs 9.23 and 9.24 in the context of a safe harbour, and at paragraph 9.34 in the context of effects-based assessment.

The current safe harbour provisions include scope for the use of blanket declarations followed up by specific disclosure as the standard develops. We understand the amendments as continuing with that approach. In the experience of IP Europe Members, blanket declarations<sup>32</sup> are a **very useful** tool for both the SDO and for industry to make an informed choice of technology as they ensure access to all work contributed to the standardisation effort. We therefore believe that the changes to paragraphs 9.23 and 9.24 are misguided and thus the original text of paragraph 286 from the current Horizontal Guidelines should not be modified.

At paragraph 9.34, in the context of effects-based assessment (which will be the case for almost all SDOs, since very few require specific IPR disclosure), a sentence has been added as follows: "Standard development agreements providing for the disclosure of information regarding characteristics and value-added of each IPR to a standard and, thereby, increasing transparency to parties involved in the development of a standard will not, in principle, restrict competition within the meaning of the Chapter I prohibition". Whilst this appears to be intended to encourage a particular approach it is not clear to us what that approach would be, since we do not understand what "information regarding characteristics and value-added of each IPR" means or to what it refers. This also needs clarification.

IP Europe appreciates the opportunity to provide comments on the draft Horizontal Guidance and remains available for any further clarification.

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<sup>&</sup>lt;sup>32</sup> The Draft Horizontal Guidelines erroneously mention 'blanket disclosure'.