



900 17th Street NW, 11th Floor
Washington, DC 20006
Tel 202.783.0070
Fax 202.783.0534
www.ccianet.org

ATEAC Business Center
Rond Point Schuman 11
B-1040 Brussels, Belgium
Tel 32.2.888.8462
www.ccianet.org

Computer & Communications Industry Association

Comments of the Computer & Communications Industry Association On the Public Consultation Regarding the Proposed Revised Guidelines for the Assessment of Horizontal Cooperation Agreements under EU Competition Law

The Computer & Communications Industry Association is a mission-focused trade association that promotes open markets, open systems, and open networks. CCIA represents large, medium-sized, and small companies in the high technology products and services sectors, including computer hardware and software, electronic commerce, telecommunications and Internet products and services. CCIA has long been active in European policies that affect information and communications technology (ICT) industries and sectors. CCIA is particularly concerned about the evolution of patent policy and practice, which heavily influences the developments of standards in the technology sectors.

Summary

These comments focus on selected specific issues in the Draft Guidelines, namely: (1) they commend the Guidelines' (a) support for good faith disclosure of essential intellectual property rights in the standards-setting process, (b) hostility to hold-ups and abusive licensing practices, (c) endorsement of (F)RAND licensing for essential IPR, and (d) emphasis on the importance of transparency in standards documentation; (2) they raise the concern that the Draft Guidelines appear inimical to royalty-free standard setting; and (3) they suggest that further guidance be provided about the application of the Draft Guidelines to specific scenarios.

Non-disclosure of Patents in Standard-Setting and the Risks of Standards Hold-up¹

CCIA has long argued that patents should not endanger investments in other forms of knowledge creation and use. Patent policy and practice should respect the creation, management, and exchange of knowledge developed under incentives other than exclusionary

¹ This subject and the ideas presented here are discussed at length in Brian Kahin, "Common and Uncommon Knowledge: Reducing Conflict Between Standards and Patents", in Laura DeNardis, ed., *Opening Standards*, ch. 11 (MIT Press, forthcoming 2010).

rights. Specifically, CCIA has argued that the patent incentive should not be enhanced by opportunities for surprise, hold-up, and extortion, which have been increasingly common in the U.S. standard-setting context.

The European technology sector's patent experience is markedly different from the United States. It is characterized by a more rigorous patent examination, an absence of continuation applications, a less litigious culture, and less acceptance of contingency fees to fund litigation, among other factors. However, these factors do not render European markets immune from the same economic and institutional interests that have precipitated an explosion of patenting and an erosion of quality in the U.S. patent system. European policy should therefore be developed cognizant of the problems encountered in the U.S. system.

Effective standards are largely taken for granted, and yield value to the public when they are ubiquitous and invisible. This ubiquity can prove most valuable to "patent trolls," or non-producing entities, whose business model is "being infringed."² The inadvertent incorporation of a patent in a standard permits the non-producing entities to extract large settlements from companies with products on the market. The possibility of an injunction means that producers risk having to shut down an entire product line if a single patented function (among the tens of thousands of functions a complex information technology product performs) is found to infringe.

For patented technology embedded in standards, the economic risk is far worse. Not only is the standard likely to be deeply embedded and impractical to excise, it will be implemented widely, perhaps by every firm in the global market. A patent infringed by an adopted standard becomes far more valuable in time than it would have been had the standards developers known about it when they had the ability to work around it. Since all implementations, including downstream uses, are potential targets, the incentives to ambush are high, and, sadly, this naked opportunism has been encouraged by poorly reasoned jurisprudence.³

To mitigate risks of holdup, actors in standards-setting efforts are commonly asked to disclose potentially relevant patents. Many companies are reluctant to commit to full disclosure due to the scope of their own portfolios, and the inherent opacity of patents – even one's own patents. As Frederick J. Telecky of Texas Instruments (TI) explained in a 2002 hearing before the U.S. Federal Trade Commission, "TI has something like 8000 patents in the United States

² Markus G. Reitzig et al., "On Sharks, Trolls, and Their Patent Prey - Unrealistic Damage Awards and Firms' Strategies of 'Being Infringed'", 36 *Research Policy* 134 (2007).

³ See, e.g., *Kingsdown Medical Consultants v. Hollister*, 863 F.2d 867, 874 (Fed. Cir. 1988).

that are active patents, and for us to know what’s in that portfolio, we think, is just a mind-boggling, budget-busting exercise to try to figure that out with any degree of accuracy at all.”⁴ By the same token, however, it is unreasonable to expect an uncapitalized standards effort to figure out the potential effect of thousands of patents that may be held by companies inside or outside the process—especially when it is impossible to identify unpublished or yet-to-be-filed patent applications.

Standards organizations try to mitigate potential problems by asking all participants to agree to license any of their patents that may be needed to practice the standard on a (fair), reasonable and nondiscriminatory (“(F)RAND”) basis – a practice the Draft Guidelines encourage. See ¶¶ 282-283. Alternatively to (F)RAND licensing, standard-setting actors may engage in *ex ante* licensing, which is viewed by the Federal Trade Commission and the Department of Justice as potentially pro-competitive, and not a *per se* antitrust violation.⁵

As the Guidelines appear to anticipate, patent holders in a standards process may have an incentive to “launder” their commitments to license (or not assert), so that a nonparticipant transferee might assert the patent holder’s rights against a standard. Accordingly, it is prudent to ensure that such commitments run with the relevant intellectual property rights (IPR). See ¶ 286. It is also encouraging that the Draft Guidelines indicate that IPR policy should require good faith disclosure of essential IPR, *see* ¶ 281, as this will encourage and protect standards-based capital investment. Encouraging and protecting investment has become the principal rationale of intellectual property and IT standards. Standards-driven investments may in fact exceed IPR investments, as they are multiplied across companies, extend down value chains, and across networks of complements. Open standards processes further ensure the quality and accessibility of the knowledge behind the standard.

CCIA also commends the Draft Guidelines’ recognition of the importance of transparency as it pertains to adequately documenting the standard. See ¶ 301. Making available

⁴ Frederick J. Telecky, “Statement at FTC/DOJ Hearings on Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy,” FTC/DOJ hearings (February 28, 2002). Available at <http://www.ftc.gov/opp/intellect/020228telecky.pdf>.

⁵ U.S. Department of Justice and Federal Trade Commission, “Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition” (2007) pp. 49-56. It bears noting that neither (F)RAND commitments nor *ex ante* licensing are effective against patent holders outside the standards-setting process, since they are not bound by any disclosure or licensing commitments. The holder of an inadvertently infringed patent will have great incentives to extract or “extort” as much as possible of the sunk investments based on the standard.

adequate information about the standard prevents anticompetitive abuse of the standardization exemption. Clear, up-to-date, and complete information on how to implement the standard is crucial to fully realize the efficiency gains conferred by well-conceived standardization agreements, as information asymmetries will inhibit interoperability. It is therefore prudent for the Draft Guidelines to condition the exemptions conferred by Article 101(3) on information transparency.

Concerns Regarding Royalty-Free Standard Setting

While the Draft Guidelines generally seem to support robust and open standard setting in the technology sectors, they also pose a significant threat to royalty-free standard setting, and should be revised accordingly.

The Draft Guidelines state:

“with respect to unrestricted participation and the procedure for adopting the standard, the rules for the standard-setting organisation, and in particular its IPR policy, should guarantee that all relevant actors can participate in the process leading to the selection of the standard. Notably, the relevant rules should not exclude or discriminate against specific groups of IPR holders. **There should be no bias in favour or against royalty free standards, depending on the relative benefits of the latter compared to other alternatives.** The standard-setting organisations should also have objective and non-discriminatory procedures for allocating voting rights.”

See ¶ 278 (emphasis supplied).

While not as clear as it should be, this single sentence appears to attack the most basic differentiation among standards efforts, since it appears to preclude a standard-setting effort from adopting a policy of seeking to produce royalty-free standards. Without explanation, it casts uncertainty on the most common practice in setting software standards and contradicts the policy of the European Interoperability Framework favoring open standards. It appears to discourage many participants, especially small entities, from participating in standards processes since they will have no assurance that the standard will end up usable.

The “relative benefits” of royalty-free licensing are well known in the standards world, which is why general policies favoring royalty-free have become increasingly popular, especially for software standards. Since royalty-bearing standards break the distribution model for open source software, open source based firms will be disadvantaged if they cannot develop royalty-free standards. The battle over the royalty-free policy in the World Wide Web Consortium in the

early 2000s is well-documented and widely remembered, especially for the role played by open source developers and companies attuned to the potential of open source software.

Royalty-free standards are favored because they promote rapid uptake. Unlike traditional standards setting, which often takes place in relatively mature markets, ICT standards setting is critical to deploying new technology and developing the market. The royalty-free environment around the early commercial Internet was responsible for its rapid growth and uptake because anyone could implement the technology without asking permission and knowing that there would be no licensing cost. In turn, this benefited the rapid development of Internet-dependent services, applications, and uses – both proprietary and nonproprietary.

Furthermore, a royalty-free approach to standards-setting means that the standards process will not be slowed by haggling over the value of patents and licenses. This can create problems in terms of overall licensing costs (royalty-stacking) and in terms of allocating royalties among patent holders. Although these problems must be dealt with head-on in patent pools, for standards developed under a (F)RAND policy, licensing problems are basically “kicked down the road” to be dealt with by companies individually as legal and business matters. This just spreads the problem around and keeps it out of sight. The costs can be very burdensome, disproportionately so for small companies who must face better-resourced negotiators with strong bargaining positions. Ironically, small entities may face demands for access to their own patents in the course of a (F)RAND negotiation. The costs of (F)RAND licensing (and possible inequities) are private and dispersed, so it is easy to overlook them under the assumption that (F)RAND is a meaningful standard.

It is important to recognize that a royalty-free policy does not shut out patent holders. Firms are willing to license patents royalty-free for many reasons. Typically, the license is limited to the practice of the standard. It may also be limited to a specific field of use. If an implementer desires to use the patent outside of these terms, permission is needed and so a royalty may be required. The patent holder is often a leader in the field and benefits to the extent that it already has a head start. Frequently, the patent holder has separate but complementary intellectual property that it can then license for a fee. If the patent holder is a producing company, it can have other complementary assets that give it an advantage in the market.

Patent holders may claim that their royalty-bearing technology is superior to public domain technology or technology that is offered without royalties. However, if a royalty-bearing

standard reflects genuinely superior technology, then there should be a market for a royalty-bearing standard above and beyond the royalty-free standard.

By imposing this presumption against royalty-free policies, the Draft Guidelines would appear to favor the concentration and barriers to entry that are characteristic of certain telecommunications equipment and services. It would effectively limit competition in software – one of the sectors within ICT where innovation is the most open and competitive. Further, by diminishing broad-based incentives for standards setting, the effects would extend further into standards for software-dependent business processes and services, i.e., much of the global economy. The Commission should remove or clarify this guideline.

Further Guidance on Application of the Guidelines

Given the challenges in mapping rules of general application onto decision-making in technology development, the Draft Guidelines' hypothetical examples illustrating the application of their principles to cases in the standards context (*see generally* ¶¶ 315-323) should be useful to market actors.

Additional guidance should be offered however, particularly in the form of applying these rules to the contemporary problems evident at the intersection of standards, technology patents, and licensing, as discussed above. Accordingly, CCIA recommends that the Draft Guidelines explore and discuss other hypothetical scenarios where the Guidelines might be applied, specifically including cases involving non-disclosure of patents in standard-setting, and with respect to royalty-free standards.

Respectfully submitted,

Erika Mann
Computer & Communications
Industry Association (CCIA)
ATEAC Business Center
Rond Point Schuman 11
B-1040 Brussels, Belgium
32.2.888.8462

Brian Kahin
Matthew Schruers
Computer & Communications
Industry Association (CCIA)
900 Seventeenth Street, NW
11th Floor
Washington, DC 20006
(202) 783-0070