

Standardising technology

A further look at patent ambush and FRAND licensing undertakings

by *Craig Simpson**

This article focuses on the recent approach of the US Department of Justice (DoJ), the Federal Trade Commission (FTC) and the European Commission regarding potential infringements of antitrust law arising either from patent ambush or from the failure of a patent licensor to comply with an undertaking to license standard essential patents on (fair), reasonable and non-discriminatory terms ((F)RAND) terms.

Two particular issues have recently been the subject of scrutiny by competition authorities on both sides of the Atlantic. Firstly, do these kinds of unilateral conduct constitute an infringement of antitrust or competition law? Secondly, what potential solutions (in SSO IPR policies) exist to prevent the imposition of excessive royalties or overly restrictive licensing terms and are these in themselves anticompetitive?

What are the potential infringements?

Patent ambush (or “hold up”) describes the situation where an essential patent holder participating in a standard setting organisation (SSO) deliberately and strategically (and in breach of the SSO intellectual property rights (IPR) policy) avoids disclosing a patent essential to technology underlying a standard being considered for adoption. Although definitions in IPR policies vary, a patent is generally considered “essential” if it is not technically possible to avoid infringing the patent in complying with the standard. Through the patent holder’s concealment, the standard is adopted without the standardisation committee being aware of the essential patent. The patent holder avoids any IPR policy commitment to license on (F)RAND terms and can then exploit any dominant position gained through the patent ambush by extracting “monopoly” rents and imposing other unreasonable licensing terms in the absence of effective competition.

If the SSO members had known of the essential patent, in the case where competing technologies existed, the SSO could have insisted on the patent holder agreeing to reasonable licensing terms (particularly royalties) before the standard was adopted or else could have chosen an alternative technology.

A separate issue is the refusal by standard essential patent holders to honour previous (F)RAND licensing undertakings given in accordance with SSO IPR policies and on which basis a relevant standard was adopted.

Does patent ambush breach competition law?

■ **The US perspective.** The US antitrust authorities previously confirmed in August 2006 that patent ambush did, in certain circumstances, constitute an infringement of antitrust law.

In its opinion *In the matter of Rambus Inc*, Docket No 9302, the FTC found that Rambus, a developer of technology for dynamic random access memory (DRAM), had infringed antitrust law through its exclusionary and deceptive conduct in concealing essential pending patent applications during the

adoption of a standard by the Joint Electron Device Engineering Council. Rambus’s conduct was “calculated to mislead JEDEC members by fostering the belief that Rambus neither had, nor was seeking, relevant patents that would be enforced” against products compliant with the standard. JEDEC had relied significantly on Rambus (mis)representations in adopting the standard and Rambus’s conduct had therefore resulted in unlawful monopolisation in violation of section 2 of the Sherman Act and unfair competition and deceptive practices under section 5 of the FTC Act. In February 2007, the FTC decided that the appropriate remedy for this infringement was a mandatory reduction in Rambus’s licensing royalties, with royalties to be abolished completely after three years.

However, the US Court of Appeals overturned these FTC orders in a judgment of 22 April 2008, finding that the FTC had failed to provide sufficient evidence to establish that Rambus’s conduct infringed US antitrust law. It found that the FTC’s findings on what JEDEC’s disclosure policies were, and exactly what Rambus refused to disclose, were “murky”. Even if Rambus’s conduct was deceitful in that it enabled a monopolist to charge higher prices than would have been possible under any RAND licensing agreement, the court found that this did not amount to demonstrating the “anticompetitive effect” (harm to the competitive process and thereby harm to consumers) required to constitute an infringement under the Sherman Act. While this ruling does not preclude the possibility of patent ambush being judged anticompetitive in the future, it is likely to discourage the FTC from making such determinations except where the evidence is clear cut.

■ **The EU perspective.** The European Commission’s DG Competition has yet to decide formally whether patent ambush constitutes an infringement of competition law. Neither is there any European Court jurisprudence directly on this point.

Characterising patent ambush as anticompetitive under article 81 or 82 has proved problematic, with DG Competition finding itself in a previous case limited to requesting the European Telecommunications Standards Institute (ETSI) to tighten the wording of its IPR policy to reduce the scope for its occurrence.

However, in July 2007, DG Competition took the first formal step of issuing a statement of objections concerning patent ambush by Rambus regarding its DRAM patents (following the 2006 FTC opinion). This is the first official indication from the Commission, through a formal step in an investigation, that patent ambush may constitute an infringement of EC competition law.

The statement of objections preliminarily concludes, mirroring the FTC opinion, that the appropriate remedy to such an abuse would be for Rambus to charge a reasonable and non-discriminatory royalty rate, the precise amount of which should be determined having regard to all the circumstances of the case.

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Problems with the FRAND licensing undertaking

SSOs have sought to reduce the scope for imposition of anticompetitive licensing terms for standard essential patents by making participation in standards setting conditional on adherence to the requirements of an IPR policy. These typically require disclosure of patents essential to a proposed standard, accompanied by an undertaking to license on (F)RAND terms. However, to date, the (F)RAND licensing undertaking has proved to be a blunt tool in preventing the imposition of unduly restrictive licensing terms (in particular, excessive royalties).

Firstly, the SSOs that require such an undertaking generally exclude their involvement as arbiter in disputes between commercial parties over whether licensing terms are (F)RAND. Aggrieved licensees are therefore limited to appealing to competition authorities or the courts in order to attempt to enforce the undertaking.

Secondly, until very recently, there has been no authoritative definition of what (F)RAND (particularly “fair and reasonable”) actually means in practice. Courts and competition authorities have fought shy of interfering in an area they believe is a matter of negotiation between commercial parties and which should be left to market forces.

Breaching a FRAND licensing undertaking

That said, recent developments suggest that breach of a (F)RAND licensing undertaking will constitute a breach of competition law.

US chipset manufacturer Qualcomm is the target of numerous actions in different jurisdictions for alleged breach of (F)RAND undertakings (particularly the imposition of high royalties) in licensing its patents essential to 3G mobile phone W-CDMA technology.

In a recent US case (*Broadcom Corp v Qualcomm Inc* 84 USPQ 2d (BNA) 1129 (3d Cir 2007)), the court found that “(1) in a consensus-oriented private standard-setting environment, (2) a patent holder’s intentionally false promise to license essential proprietary technology on (F)RAND terms, (3) coupled with an SSO’s reliance on that promise when including the technology in a standard, and (4) the patent holder’s subsequent breach of that promise, is actionable anticompetitive conduct”.

Meanwhile, the European Commission decided on 1 October 2007 to initiate formal proceedings against Qualcomm concerning an alleged abuse of a dominant position in connection with a complaint by major mobile telecommunications players on this issue. While this is certainly not conclusive of any Commission finding, it indicates that DG Competition may well follow the US lead.

Ex ante declaration

Faced with the inadequacies of enforcing (F)RAND, SSOs have more recently considered requiring ex ante declaration of specific licensing terms prior to adoption of the standard. In this way, IPR holders wishing to have their patented technology included in the standard compete on the basis of licensing terms (including price), as well as on the technology itself. The prospect of such requirements in SSO IPR policies have generated their own competition infringement concerns

– namely, that this might lead to cartel behaviour between competitors involved in the standard setting process.

The US antitrust authorities have recently provided some welcome clarity on this issue. In a business review letter of 30 October 2006, the DoJ approved as procompetitive a new IPR policy of the VMEbus International Trade Association (VITA) SSO which included an obligation to declare irrevocably maximum terms (maximum royalty rates and the most restrictive non-royalty terms demanded for essential rights).

Crucial to the DoJ’s decision was that the IPR policy prohibited horizontal negotiations between the SSO working group members over the specific licensing terms in deciding which technology to support for the standard. This precluded use of the ex ante process as a sham for horizontal buyer price-fixing in order to lower prices for licences in breach of section 1 of the Sherman Act. In a subsequent report in April 2007 entitled “Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition” (the IP2 report), the DoJ and the FTC confirmed that ex ante consideration of licensing terms by SSO participants is likely to be procompetitive and should be analysed under the “rule of reason” approach, rather than considered a per se violation (buyer price-fixing) under the Sherman Act.

The Commission has indicated, in the context of formally commenting on possible changes to the ETSI IPR rules, that it would take a similar approach in accepting ex ante royalty setting as procompetitive, subject to appropriate safeguards against price collusion.

Conclusion

Recent developments in both the US and the EU suggest that, in the SSO context, deception through patent ambush or hollow FRAND licensing undertakings may be actionable as an infringement of competition law.

In the US, but not the EU, competition authorities previously confirmed that both types of conduct were anticompetitive. However, the recent US Court of Appeals ruling overturning the FTC’s findings in the *Rambus* case significantly raises the bar regarding the evidence needed to establish that patent ambush constitutes an antitrust infringement.

DG Competition’s statement of objections in the *Rambus* case and its initiation of formal proceedings against Qualcomm indicate that Europe may follow the US lead. The US *Rambus* appeal ruling may, however, have knock-on effects regarding the viability of the Commission’s arguments against Rambus in Europe.

Central to any formal Commission decision in both these cases will be the question of whether competition law is, in the DoJ’s words, the appropriate tool “for limiting patent rights or reflexively reining in the power of whatever player has developed pricing power at a particular time”; or whether this should be left to the market to decide, along with tighter SSO IPR policies such as mandatory ex ante declaration of both essential patents and maximum royalty rates.

Meanwhile, the DoJ has (in its IP2 report and VITA business review letter) now given the green light to SSO IPR policies requiring ex ante declaration of specific terms, provided that this does not involve horizontal co-operation between the SSO members in choosing which technology to support.