FIXING FRAND

Rationalizing The Basis For “Fair, Reasonable And Non-discriminatory” Licensing of Standards-Essential Patents

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Overview

- Background – What is FRAND and what’s wrong with it?
- The FRAND “solution” landscape
- Optimizing solutions
Standards Development 101

- Interoperability standards
- Voluntary consensus standards development organizations (SDOs)
Patent Issues in Standard Setting

- Patent stacking

- Patent “hold up”
**SDO Policies** address Hold-Up

- **Disclosure Policies**
  - SDO participants must disclose essential patents prior to approval

- **Licensing Policies**
  - SDO participants commit to license essential patents [often on Fair, Reasonable and Nondiscriminatory (FRAND) terms]
Under Nash bargaining conditions:

- bilateral *ex ante* negotiations between patent holders and standards implementers
- with genuine non-discrimination commitments
- should result in consistent, equilibrium royalties

(Gilbert 2011)
But ... FRAND Smart Phone Litigation 2010-2012
Implementers and Patent Holders did not engage widely in bilateral *ex ante* negotiations:

- High transaction costs
  - Many standards, many patent holders
- Reliance on cross-license history
- Uncertain product markets
- Uncertain patent quality
- Mutual Assured Destruction
- Sleeping Dogs
- FRAND security blanket
**FRAND Issues in Litigation**

- **Scope of Commitment**
  When is the FRAND commitment breached?
  - Magnitude of royalty demand
  - How long should the parties negotiate?

- **Theories of Liability**
  - Antitrust – Sherman §2, FTC §5
  - Breach of Contract
  - Estoppel

- **Remedy**
  What are appropriate remedies for breach?
  - Judicial determination of royalty rate?
  - When, if ever, can injunctive relief be sought?
FRAND’s Failings

- **Indeterminacy**
  - No generally-accepted definitions of parameters

- **Subjectivity**
  - Reasonableness in the “eye of the beholder”

- **Non-transparency**
  - Licensing negotiations typically secret – limiting comparative information

- **Legal Effect**
  - Enforceability of obligation and potential remedies are unclear
Do we need to fix FRAND?

- **YES**
  - Unpredictable cost basis destabilizes markets
  - Loose standards enable abuse/strategic behavior
    - Harm to competition, competitors and consumers
  - Unpredictable outcomes destabilize standardization process

- **NO**
  - Majority of patent holders (defensive owners) don’t seek royalties anyway – don’t prod them
  - FRAND is simply an “insurance policy”
  - Bilateral negotiation is most efficient means of determining what’s reasonable
Proposed FRAND “fixes” - Governmental

- Judicial/Legislative/Agency Approaches
  - Policy Interpretation
    - Royalty base
    - Non-discrimination
  - Damages limits
    - Geo. Pacific
    - Royalty base
  - Enforcement limits
    - Patent Unenforceability (unclean hands, deception)
    - Injunctive Relief (elimination → e*Bay weighting)
Proposed FRAND “fixes” – Private (SDO)

- Policy Interpretation
  - Royalty base
  - Non-discrimination

- Transparency Enhancements
  - Ex Ante term disclosure
  - Prior license disclosure

- Anti-Stacking/Coordination Measures
  - Royalty caps
  - Step-down
  - Collective negotiation

- Enforcement Limitations
  - Injunctive Relief (elimination → e*Bay weighting)
  - Limited enforcement period

- Royalty Arbitration

- De Novo Structures
  - Royalty Auctions
  - Patent Pools
Fixing FRAND: Meta-analysis

- **Solution Typology**
  - Governmental v. Private
  - Compliance (royalty) v. Enforcement (remedy/injunction)

- **Variables**
  - **Implementability**
    - Cost/Time/Difficulty of implementation
    - Likelihood of broad adoption
  - **Market Impact**
    - Magnitude of potential combined effect on patent holders and implementers (independent of “direction” of effect)
Observations

- Compliance (royalty)
  - SDO-based solutions have broader impact than case-by-case judicial reasonableness determinations

- Remedies
  - If reasonableness/royalty level is determined, unnecessary to tweak injunction tests (e*Bay works)

- Greatest implementability+impact (royalty control)
  - Royalty arbitration
  - Anti-stacking measures
Constructing a Solution

- Defining the Commitment (SDO-level)
  - Early patent disclosure
  - Rough essentiality filter (crowd-sourcing)
  - Ex Ante collective rate cap
  - Fast-track arbitration
  - Optional: Central licensing agent/pool

- Remedies
  - No adjustment of injunctions (E*Bay)
  - Non-participants – antitrust scrutiny

- Promotion/Take-up
  - Agency (DOJ/FTC/EC) support
  - ANSI, ETSI, other major SDOs
Further Work

- Quantification of meta-analysis
- Economic modeling of solution
- Your comments welcome!