

# COMMENT

## The European Commission proposal for a regulation on standard essential patents: a curate's egg

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Standard Setting; Essentiality; EU Law; Competition Law; FRAND; SEPs; Intellectual Property.

### A. Overview

On 27 April 2023, the European Commission (the “Commission”) proposed a new regulation on the licensing of standard essential patents (the “Proposal”).<sup>2</sup> The objective of the Proposal is to facilitate standard essential patent (“SEP”) licensing

negotiations by providing clarity on several aspects: transparency as to who owns SEPs and which SEPs are essential; transparency on fair, reasonable and non-discriminatory (“FRAND”) terms and conditions;<sup>4</sup> and dispute resolution for the determination of FRAND terms.<sup>5</sup>

The European intellectual property landscape is already undergoing major upheaval with the launch of the Unified Patent Court (the “UPC”).<sup>6</sup> If the Proposal is adopted, it could play a major role in shaping the future of innovation and standard setting in the European Union. The Proposal is, however, controversial, and it is not certain that it will survive parliamentary scrutiny as it is.

The Proposal provides for the following significant changes:

- i. The European Union Intellectual Property Office (the “EUIPO”) would establish a Competence Centre<sup>7</sup> to set up and maintain an EU-wide register for SEPs, including details of relevant standards, registered SEPs and SEP holders,<sup>8</sup> and terms of the SEP holder’s FRAND licensing commitment. SEP holders seeking to license their SEPs for royalties and to enforce them in the EU

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<sup>2</sup> Proposal for a Regulation of the European Parliament and the Council on standard essential patents and amending Regulation (EU)2017/1001, 27 April 2023 COM(2023) 232 final, 2023/0133 (COD), available at [https://single-market-economy.ec.europa.eu/system/files/2023-04/COM\\_2023\\_232\\_1\\_EN\\_ACT\\_part1\\_v13.pdf](https://single-market-economy.ec.europa.eu/system/files/2023-04/COM_2023_232_1_EN_ACT_part1_v13.pdf). The Commission called for feedback on the Proposal, and responses were published in August 2023, see [https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13109-Intellectual-property-new-framework-for-standard-essential-patents/feedback\\_en?p\\_id=32054345](https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13109-Intellectual-property-new-framework-for-standard-essential-patents/feedback_en?p_id=32054345). The publication of the Proposal follows a call for evidence and a public consultation in early 2022 (available at [https://single-market-economy.ec.europa.eu/news/commission-seeks-views-and-input-fair-licensing-standard-essential-patents-2022-02-15\\_en](https://single-market-economy.ec.europa.eu/news/commission-seeks-views-and-input-fair-licensing-standard-essential-patents-2022-02-15_en)). The Proposal complements the recently updated *EU Strategy on Standardisation; Setting global standards in support of a resilient, green and digital EU single market*, 2 February 2022, COM(2022) 31 final. See Proposal, Explanatory Memorandum, para. 1. See also: European Commission, Joint Research Centre, R. Bekkers, J. Henkel, E. M. Tur, et al., *Pilot study for essentiality assessment of standard essential patents*, Publications Office of the European Union, 2020, <https://data.europa.eu/doi/10.2760/68906>; European Commission, Joint Research Centre, R. Bekkers, E. Raiteri, A. Martinelli, et al., *Landscape study of potentially essential patents disclosed to ETSI: a study carried out in the context of the EC ‘Pilot study for essentiality assessment of standard essential patents’ project*, N. Thumm (editor), Publications Office, 2020, <https://data.europa.eu/doi/10.2760/313626>; European Commission, Joint Research Centre, J. Baron, C. Pentheroudakis, N. Thumm, *Licensing terms of standard essential patents: a comprehensive analysis of cases*, N. Thumm (editor), Publications Office, 2018, <https://data.europa.eu/doi/10.2791/32230>.

<sup>3</sup> SEPs are patents that protect technology that is incorporated in a standard. SEPs are “essential” in the sense that implementation of the standard requires use of the inventions covered by SEPs for technical reasons.

<sup>4</sup> The FRAND commitment is a voluntary contractual commitment given by the SEP holder to the benefit of third parties implementers of the standard. Commitments may slightly differ, depending on each standard development organization’s policy.

<sup>5</sup> The Proposal is without prejudice to EU competition rules. Recital 2 and Article 1(7).

<sup>6</sup> See Agreement on a Unified Patent Court, (2013/C 175/01), OJ C 175, 20 June 2013, p. 1–40, available at [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:42013A0620\(01\)](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:42013A0620(01)). The launch of the UPC on 1 June 2023 represents an important milestone for SEP enforcement. The UPC will provide a single European venue for patent infringement actions – including SEPs – that can award damages and issue injunctions in up to 17 EU Member States. See M. Stierle, *The Rise of the Unified Patent Court: A New Era*, IIC-International Review of Intellectual Property and Competition Law, 1-3, 2023; G.B. Born, S. Ebermann, *A New Patent Mediation and Arbitration Centre for Europe*, Journal of International Arbitration, 40(3), 2023.

<sup>7</sup> On the Competence Centre, see Proposal, Title II.

<sup>8</sup> “SEP holder” is an entity that holds one or more SEPs.

- would have to register the patents in a SEP register;<sup>9</sup>
- ii. The EUIPO would conduct non-binding checks to determine whether a patent is essential to a standard;<sup>10</sup>
  - iii. Before launching a litigation, parties to a SEP licensing dispute would have to go through a mandatory conciliation procedure administered by the EUIPO. An independent conciliator would seek to help the parties reach mutually acceptable FRAND licensing terms and conditions. At the end of the process, if the parties fail to reach agreement, the conciliator will issue a non-binding report with recommendations on the FRAND rate;<sup>11</sup>
  - iv. SEP holders could jointly agree on an aggregate royalty for using a standard (again, potentially with the help of a conciliator). Both implementers<sup>12</sup> and SEP holders could request the EUIPO to provide a non-binding expert opinion on the aggregate royalty. This could then serve as a basis for FRAND royalty determination for individual patent portfolios, and for the distribution of the royalty stack.<sup>13</sup>

The Proposal clarifies, appropriately, that it “*does not apply to royalty-free licensing*”, acknowledging that, whilst licensing on FRAND terms and conditions includes licensing royalty-free, “*most issues arise with royalty-bearing licensing policies*”.<sup>14</sup>

While the Proposal aims to address a number of outstanding issues inherent in the current legal framework for SEPs,<sup>15</sup> such as the criteria for determination of FRAND rates, and inefficiency of parallel licensing negotiations with individual licensees,<sup>16</sup> there are various concerns with the Proposal that deserve further consideration during the legislative process.

The remainder of this article summarizes the Proposal in more detail and provides a preliminary assessment of its main provisions.

## B. Critical Assessment

### Scope

The Proposal only applies to future standards.<sup>17</sup> Existing standards can only be brought into scope by a delegated act of the Commission, for which a high

<sup>9</sup> On the registration of SEPs, see Proposal, Title III, Chapter 3.

<sup>10</sup> On the essentiality checks of SEPs, see Proposal, Title V.

<sup>11</sup> On FRAND determination, see Proposal, Title VI.

<sup>12</sup> “Implementer” is an entity that manufactures goods and/or provides services in compliance with an industry standard.

<sup>13</sup> On the aggregate royalty, see Proposal, Title III, Chapter 2.

<sup>14</sup> Proposal, Recital 7 and Article 1. See European Commission, *Impact Assessment Report Accompanying the Document Proposal for a Regulation of the European Parliament and of the Council on Standard Essential Patents and Amending Regulation (EU) 2017/1001*, SWD(2023) 124 final (“Impact Assessment”), at 55: “*A royalty free SEP licensing obligation was rejected because from an economic perspective whether or not a standard should be royalty-free depends on the economic interest of standard contributors to be subject to such IPR policy and there cannot be general rules that would determine that.*” See also *id.*, at 90-92. The European Commission investigated whether royalty-free licensing with universal reciprocity was in compliance with EU competition law, in case AT.40805 - *AOM AV1 licensing conditions*, but closed the case without enforcement action. See press release, May 23, 2023, “*Alliance for Open Media Welcomes the European Commission’s Decision to End Its Preliminary Investigation of the AOM Royalty-Free Licensing Policy*” at <https://aomedia.org/press%20releases/preliminary-aom-royalty-free-licensing-policy-investigation/>

<sup>15</sup> For the current legal framework, see: Communication Setting out the EU Approach to Standard Essential Patents, COM(2017)712 final, 29 November 2017, endorsed by Council Conclusions on the enforcement of Intellectual Property Rights, 6681/18, 1 March 2018; Directive 2004/48/EC of the European Parliament and of the Council of 29 April 2004 on the enforcement of intellectual property rights, OJ L 157, 30 April 2004, pp. 45-86; Regulation (EU) No. 608/2013 of the European Parliament and of the Council of 12 June 2013 concerning customs enforcement of intellectual property rights, OJ L 181, 29 June 2013, pp. 15-34; Regulation (EU) No. 1025/2012 of the European Parliament and of the Council of 25 October 2012 on European standardisation, OJ L 316, 14 November 2012, pp. 12-33, as amended by Regulation (EU) 2022/2480, OJ L 323, December 19, 2022, pp. 1-3; EU Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements, OJ C 89, 28 March 2014, pp. 3-50; and EU Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal cooperation agreements, OJ C 259, 21 July 2023, pp. 1-125, at pp. 96-107. See also “*Commission Adopts Revised Horizontal Block Exemption Regulations and Horizontal Guidelines*”, available at <https://www.clearyantitrustwatch.com/2023/06/commission-adopts-revised-horizontal-block-exemption-regulations-and-horizontal-guidelines/>.

<sup>16</sup> The Proposal does not contemplate licensee negotiation groups (“LNGs”) formed by SEP implementers. While SEP owners can team up within patent pools, it remains uncertain whether implementers can do so, too. There are arguments that LNGs create comparable efficiencies as patent pools and should be treated in the same way. This clarification could be achieved through the planned revision of the Commission’s Technology Transfer Guidelines. See [https://competition-policy.ec.europa.eu/public-consultations/2023-technology-transfer\\_en](https://competition-policy.ec.europa.eu/public-consultations/2023-technology-transfer_en).

<sup>17</sup> Proposal, Article 66. Article 1(3)-(4) moreover allows certain standards to be exempted by delegated act “[w]here there is sufficient evidence that [...] SEP licensing negotiations on FRAND terms do not give rise to significant difficulties or inefficiencies affecting the functioning of the internal market.”

bar is set.<sup>18</sup> This means that standards that have been and continue to be subject of much dispute will not be covered, such as Wi-Fi, 4G and 5G.<sup>19</sup>

### ***SEP Registration***

The Proposal establishes a “Competence Centre” within the EUIPO (which currently focuses solely on trademarks and design rights)<sup>20</sup> to set up and maintain an EU-wide register for SEPs. This register would include the following information:

- Information on relevant standards;
- Details of the registered SEP, including identification, date of registration, and the standard version, technical specifications and specific sections for which the patent is considered essential;
- Details of the SEP holder and its legal representatives; and
- Information on licensing, including the terms of the SEP holder’s FRAND licensing commitment, the existence of any public standard terms and conditions for SEP licensing to SMEs and the availability for licensing through patent pools.<sup>21</sup>

Registration of SEPs will be mandatory for enforcement purposes.<sup>22</sup> SEP holders would need to request registration of their SEPs within six months following the Competence Centre’s creation of an entry in the register for the relevant standard, or the grant of the SEP by the relevant patent office.<sup>23</sup>

If a SEP is not registered within the time-limit, the SEP holder will not be able to enforce it in court and will not be able to collect royalties or past damages for any use of the SEP from the time-limit until the date of registration.<sup>24</sup> Updates to reflect relevant changes would also have to be notified to the Competence Centre within six months from the change occurring, or the registration will be suspended until the inaccurate or incomplete information is remedied.<sup>25</sup> The intention is that implementers can readily identify SEP holders so as to seek a license.

### *The SEP registry risks a duplication of effort*

In principle, transparency is desirable, to the extent it allows implementers to predict the licensing costs of marketing standard-compliant products. The European Telecommunications Standards Institute (“ETSI”) has urged the Commission to rethink its Proposal, stressing that ETSI already maintains its own database, which contains not only essentiality declarations (as the envisaged EUIPO SEP register would) but also technical specifications.<sup>26</sup> It should be kept in mind, however, that the ETSI database is limited to ETSI standards, and does not include SEPs claimed to read on other standards.

### *Non-registration might in some cases leave implementers worse off*

Many patentees declare more patents as SEPs than are actually essential in order to stake a claim to a greater share of royalty stacks than they actually deserve (the perceived problem of “over-declaration”).<sup>27</sup> Many SEP holders also issue “blanket

<sup>18</sup> The Commission must find that “*the internal market is severely distorted due to inefficiencies in the licensing of SEP.*” Proposal, Article 66(4).

<sup>19</sup> Several stakeholders in the automotive industry argued that the scope of the Proposal therefore unjustifiably favors holders of wireless communication standards, “*for which the automotive industry has had to accept license offers from SEP holders that were made under pending injunction proceedings or under the imminent threat of such proceedings.*” See position papers on the Proposal submitted by the European Automobile Manufacturers’ Association (14 July 2023) and the Volkswagen Group (17 July 2023), available at [https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13109-Intellectual-property-new-framework-for-standard-essential-patents/feedback\\_en?p\\_id=32054345](https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13109-Intellectual-property-new-framework-for-standard-essential-patents/feedback_en?p_id=32054345).

<sup>20</sup> The Proposal acknowledges this: “*the EUIPO has extensive experience with managing databases, electronic registers and alternative dispute settlement mechanisms [...] [i]t is necessary to equip the competence centre with necessary human and financial resources to fulfil its tasks.*” Proposal, recital 12. In any case, the EUIPO’s alleged “*extensive experience with [...] alternative dispute settlement mechanisms*” is actually primarily in European Union trade mark or design matters in *inter partes* proceedings on-going at the EUIPO. These are much simpler matters than the ones the Proposal suggests to assign to the EUIPO.

<sup>21</sup> Proposal, Articles 4 and 19-25.

<sup>22</sup> Proposal, Articles 19-25.

<sup>23</sup> Proposal, Article 20.

<sup>24</sup> Proposal, Article 24.

<sup>25</sup> Proposal, Article 20.

<sup>26</sup> See ETSI, Proposal for a Regulation on SEPs – ETSI views, 14 April 2023, available at [https://www.documentcloud.org/documents/23780757-dg-23-07\\_proposal-for-a-regulation-on-seps-etsi-views56](https://www.documentcloud.org/documents/23780757-dg-23-07_proposal-for-a-regulation-on-seps-etsi-views56). ETSI maintains a comprehensive digitalized database with information on declared SEPs for ETSI standards.

<sup>27</sup> The processes established by standard developing organizations for the submission of SEP declarations are primarily designed to facilitate the development of standards, not to provide a basis for SEP licensing. SEP holders are encouraged to declare patents that they believe are either

declarations”, not identifying their patents, but promising that if they have any, these will be licensed on FRAND terms.<sup>28</sup> The drawback of this current system is the lack of transparency, but there is at least some promise of constraints on licensing demands for the patents included in a padded patent list or blanket declaration.

The proposed system would curb these practices, and promise transparency at a cost, but may not deliver on that promise: if SEPs are not registered timely, they cannot be enforced. SEP holders may have an incentive to argue that their undeclared SEPs are not technically essential and not subject to FRAND obligations, but still valid and infringed. There would be no constraints on injunctions or royalties for non-SEPs. Implementers in turn will argue that they are standard-essential. This scenario could increase disputes, and could turn out problematic for implementers, if patents are found to be merely “commercially essential” but not “technically essential”, allowing injunctions and royalty charges above FRAND level.

### *SEP holders may litigate outside the EU*

SEPs may have an incentive to enforce their patents outside the EU (for example, in the United Kingdom, the United States, China, or India) while seeking a worldwide license including the EEA.<sup>29</sup> This would allow SEP holders to circumvent the application of the proposed regulation altogether (and to avoid the essentiality test and FRAND constraints).

### *Essentiality Checks*

The Proposal includes essentiality checks for registered SEPs.<sup>30</sup> The proponents hope that this will improve transparency in the SEP landscape and help implementers assess whether they need a license.

Essentiality checks would be carried out annually and would cover patents from each SEP holder and each specific standard in the register. SEP holders may also propose up to 100 of their SEPs for review.<sup>31</sup>

The results of the non-binding essentiality checks would be published in the SEP register, indicating only whether the outcome of the assessment was positive or negative.<sup>32</sup> Although the results of the essentiality checks are not legally binding, they can be presented as evidence before stakeholders, patent pools, public authorities, courts and arbitrators.<sup>33</sup>

Essentiality checks are commonplace for SEPs included in patent pools, and pool-checked SEPs are exempted to avoid duplication.<sup>34</sup> Such pools can only include complementary (*i.e.*, essential) patents, so as to avoid pools turning into licensing cartels and tying devices if they were to include substitute (*i.e.*, non-essential patents).<sup>35</sup> There are some issues, however:

### *Essentiality checks are not comprehensive*

The Proposal provides that no more than one SEP from the same patent family may be examined for

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essential to the standard or may become essential depending on the development process. This has encouraged “over-declaration” for some standards, particularly in connectivity technologies. Several authors have argued that many patents declared to standard-setting organizations are not actually essential. See, e.g., J. L. Contreras, *Essentiality and Standards-Essential Patents*, in *Cambridge Handbook of Technical Standardization Law: Competition, Antitrust, and Patents* 209, 222-23 (J. L. Contreras ed., 2017).

<sup>28</sup> “Blanket declarations” serve to inform implementers as to the identity of possible SEP holders and to provide some assurance that they will not block a standard if they hold SEPs (*i.e.*, by refusing to license the SEPs covering the standard). However, they do not provide details on the existence, relevance or number of relevant SEPs for the standard. See European Commission, *Group of Experts on Licensing and Valuation of Standard Essential Patents ‘SEPs Expert Group’ - full contribution*, 2021, at 47.

<sup>29</sup> J. Baron, P. Argue-Castells, A. Leonard, T. Pohlman, and E. Sergheraert, *Empirical Assessment of Potential Challenges in SEP Licensing*, European Commission, 2023, at 112.

<sup>30</sup> Proposal, Articles 28-33. On essentiality in SEPs, see J. L. Contreras, *Essentiality and Standards-Essential Patents*, in *Cambridge Handbook of Technical Standardization Law: Competition, Antitrust, and Patents* 209, 222-23 (J. L. Contreras ed., 2017).

<sup>31</sup> Proposal, Article 29.

<sup>32</sup> Proposal, Article 33. The lack of an essentiality check or an ongoing essentiality check does not preclude licensing negotiations or any court or administrative procedure in relation to a registered SEP (*Id.*, Article 28).

<sup>33</sup> Proposal, Article 28.

<sup>34</sup> See Article 29(4) in conjunction with Article 8 point (b) of the Proposal. Patent pools are an agreement between two or more parties to license one or more of their patents to one another or to third parties. See [https://www.wipo.int/export/sites/www/ip-competition/en/studies/patent\\_pools\\_report.pdf](https://www.wipo.int/export/sites/www/ip-competition/en/studies/patent_pools_report.pdf).

<sup>35</sup> See Communication from the Commission, Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements, paras 250-255.

essentiality<sup>36</sup> and that the result of the essentiality check applies to all SEPs in the same patent family.<sup>37</sup>

However, a singular examination does not allow automatic assumption that other patents in the same family are essential to a standard or not.<sup>38</sup>

### *Assessing essentiality by samples may be unreliable*

Checks will not be carried out on all patents, but only on a sample. Patents selected for random check will not be rechecked in order to assure reliability of the sample.<sup>39</sup> The exact sampling methodology has yet to be defined.<sup>40</sup> The use of samples is not without problems. It inevitably introduces a margin of error, as a sample size must include many patents to be meaningful.<sup>41</sup>

Some have recommended the use of artificial intelligence for essentiality reviews. In the absence of a widely accepted method for assessing a large portfolio of filed patents, however, the results of these essentiality assessments may be inaccurate.

### *Essentiality checks do not eliminate litigation*

The essentiality finding is not binding, and can be relitigated. Even if parties accept the non-binding essentiality determination, they may still be in disagreement in relation to infringement and validity

issues, especially if the reasons are not made available.<sup>42</sup> The transparency is therefore limited and does not pre-empt disputes.

### *FRAND determination procedure*

The Proposal provides for a mandatory conciliation procedure aimed at assisting parties in negotiating FRAND rates (see Fig. 1 below). The procedure, to be administered by the Competence Centre, would have to be completed within nine months.<sup>43</sup> It can be initiated at the request of the SEP holder, a potential implementer, or by both parties voluntarily to resolve FRAND disputes.<sup>44</sup>

Parties to a SEP dispute would be required to go through the conciliation procedure before they can initiate patent infringement proceedings or a FRAND assessment before a Member State court or the UPC.<sup>45</sup>

The procedure involves a “conciliator” chosen by the parties from a group of three candidates proposed by the EUIPO from a roster. If the parties fail to agree on a candidate, the Competence Centre would appoint the conciliator.<sup>46</sup>

The parties will be requested to make submissions and proposals.<sup>47</sup> The conciliator will assist them in their endeavour to reach a FRAND rate and will make

<sup>36</sup> Proposal, Article 28(3).

<sup>37</sup> Proposal, Article 33(1).

<sup>38</sup> Similar problems arise in relation to different patent claims in the same patent. Sometimes claims from multiple members of a patent family are standard-essential. However, there could also be a case where only one member of a patent family contains essential claims. If one of the patent family members that has no essential claim gets checked, the patent family as a whole will be erroneously declared non-essential.

<sup>39</sup> Proposal, recital 27. The Commission argues that “[a]llowing for appeals to the assessments of randomly sampled patents produces few benefits, and significant costs” (Impact Assessment, footnote 294). However, this statement is difficult to reconcile with the right of appeal that should be guaranteed to the parties in case of error and inaccuracy.

<sup>40</sup> Proposal, Article 29.

<sup>41</sup> See K. Mallinson, *Essentiality Checks Might Foster SEP Licensing, But Do Not Stop Over-Declarations from Inflating Patent Counts and Making Them Unreliable Measures* (16 November 2022), arguing that sample sizes of thousands of patents would be required to provide even only modest levels of precision in essential patent counts; available at <http://dx.doi.org/10.2139/ssrn.4278639>.

<sup>42</sup> M. Lemley, T. Simcoe, *How essential are standard-essential patents*, Cornell Law Rev. 104, 2019, at p. 617.

<sup>43</sup> Proposal, Article 37.

<sup>44</sup> Proposal, Article 34.

<sup>45</sup> Proposal, Article 34(1). SEP holders may seek a provisional injunction “of a financial nature” (*i.e.*, not a sales ban but a requirement on implementers to make a deposit or post a bond to cover license fees) before the conclusion of the FRAND Determination Procedure. However, the parties are required to request the national court to suspend proceedings on the merits for the duration of the FRAND determination (*id.*, Article 34(4)). The Proposal’s restriction on access to courts during the pendency of the FRAND procedure has been criticized. The limitation is arguably in line with the Court of Justice of the European Union (“CJEU”) judgement on an Italian regulation requiring non-binding dispute resolution prior to court proceedings in disputes between consumers and telecommunications operators (CJEU, Joined cases C-317/08, C-318/08, C319/08 and C-320/08 (2010), *Allassini and Others v Telecom Italia S.p.A.*, ECLI:EU:C:2010:146). See Proposal, Explanatory Memorandum, para. 3. However, the maximum duration of the dispute resolution in those cases was shorter.

<sup>46</sup> Proposal, Article 39.

<sup>47</sup> Written submissions including evidence and expert opinions can be submitted (Article 43).

proposals.<sup>48</sup> At the request of a party, or if the conciliator deems it necessary, an oral hearing will be scheduled.<sup>49</sup> The FRAND determination will focus on terms for a global license, unless the parties agree otherwise.<sup>50</sup>

If, at the end of the procedure, the parties have not yet settled, the conciliator will make a final proposal on the FRAND rate, which the parties may or may not accept.<sup>51</sup> If the parties do not settle or if they reject the conciliator's proposal, the conciliator will terminate the procedure and issue a report on the determination of FRAND terms and conditions. The non-confidential part of this report will contain the parties' final proposal and the methodology used by the conciliator to make the determination, and can then be used as evidence in court proceedings.<sup>52</sup> The purpose of the report is therefore twofold: to encourage settlement and to provide transparency on the process and recommended FRAND terms and conditions in cases of disagreement.<sup>53</sup>

### *Confidential nature of the EUIPO's findings*

The report on the determination of FRAND terms and conditions includes: (i) a confidential assessment of the FRAND determination; (ii) a confidential summary of the main issues of disagreement; and (iii) a non-confidential methodology and the assessment of the determination of FRAND terms and conditions by the conciliator. Only the latter will be publicly available.<sup>54</sup>

However, the confidentiality of the results removes much of their potential wider benefit (*i.e.*, transparency), as other market participants cannot use the information developed by the Competence Centre in their own FRAND negotiations.

### *Limited impact of non-binding FRAND determinations*

The Proposal delays disputes, but does not require the parties to commit to be bound by the FRAND determination. As currently drafted, the Proposal provides that:

- i. Whoever triggers the FRAND determination process (the SEP holder or implementer) need not initially state whether they accept the determination as binding;
- ii. When responding, the other party will have to state whether “*it commits to comply with [the] outcome*” of the FRAND determination.<sup>55</sup> However, it is not clear how binding such a “commitment to comply” can be, as the Proposal does not explicitly state that the parties must enter into a license agreement on that basis;
- iii. In any case, the outcome of the FRAND determination process will not be binding unless the party that initiated the process also agrees to be bound.

A non-binding FRAND determination may be helpful, but may not be sufficient. It does not cover terms and condition that are directly relevant for royalties, or controversial practices such as the refusal to license upstream to component manufacturers. Most importantly, past experience mediating FRAND determinations shows that parties may both think they are better off litigating – SEP holders may prefer to seek injunctions, and implementers may prefer to challenge validity. Mandatory mediation would not change this. Even if the litigation leads to review of royalty levels, national courts are free to ignore non-binding FRAND determinations.

This is a particular concern in German courts, which tend to refuse to assess whether proposed license terms are FRAND, and may require a licensee to accept the SEP holder's offer so long as it is not “absolutely unacceptable”.<sup>56</sup> They even tend to issue injunctions without reviewing the SEP holder's FRAND offer at all, in violation of the principles set

<sup>48</sup> At least five months before the nine-month limit, the conciliator will notify to the parties a written recommendation of FRAND determination (*Id.*, Article 51). At the latest 45 days before the nine-month limit, the conciliator will submit a reasoned proposal for a FRAND determination (*Id.*, Article 55).

<sup>49</sup> Proposal, Article 53.

<sup>50</sup> Proposal, Article 38(6) and recital 11.

<sup>51</sup> Proposal, Article 56.

<sup>52</sup> Proposal, Article 57.

<sup>53</sup> Proposal, Recital 41.

<sup>54</sup> Proposal, Article 57.

<sup>55</sup> Proposal, Article 38(2).

<sup>56</sup> See, for instance, Munich I Regional Court judgment of 5 August 2022 (21 O 8890/21) – “*keepawake-message*”, available at <https://www.gesetze-bayern.de/Content/Document/Y-300-Z-GRURRS-B-2022-N-34498?hl=true>.

by the EU Court of Justice in case C-170/13 – *Huawei Technologies*.<sup>57</sup> The high license rates extracted under the threat of these injunctions are then invoked as a comparators to determine subsequent royalty rates determinations.

Alternative approaches have been put forward, such as requiring SEP holders and implementers to enter into a “reciprocal FRAND agreement” modelled on the FRAND injunction decisions of the UK courts.<sup>58</sup> Under this proposal, SEP holders would be required to offer implementers a reciprocal FRAND agreement in which the SEP holder agrees to forego patent infringement remedies like injunctions, and the implementer agrees to enter into a license on FRAND terms determined in negotiations between the parties or (if no agreement is reached) set by a third party. Implementers would have until 30 days after a finding of infringement to accept the offer. If they reject it, they are subject to infringement remedies (including injunctions). A failure to comply with the third-party determination would be addressed in a contract action before a national court over FRAND terms rather than in a patent infringement proceeding.

An alternative would be a system whereby either party could make an irrevocable offer to agree on third-party rate determination, creating a rebuttable presumption of willingness to take a license, for the purposes of determining whether an injunction is available.<sup>59</sup> Acceptable rate setting options would include:

- Arbitration, for instance, under WIPO FRAND arbitration rules;<sup>60</sup>
- In Germany, an offer to enter into a “rate setting” agreement;<sup>61</sup>
- In the UK, a SEP holder request for a court to issue a “FRAND injunction”;<sup>62</sup>
- In The Netherlands an offer to agree on “binding advice”;<sup>63</sup>
- A request for a declaratory judgment on the meaning of FRAND, where possible, under contract law, or a claim for specific performance of the third-party beneficiary arrangement inherent in FRAND undertakings.

	SEP holder offers rate setting	SEP holder refuses rate setting
User offers rate setting	Injunction denied; parties settle, or third party sets terms	Injunction denied unless user refuses FRAND terms
User refuses rate setting	Injunction granted unless user offers FRAND terms	Follow <i>Huawei/ZTE</i>

<sup>57</sup> CJEU, Case C-170/13 – *Huawei Technologies* (2015) ECLI: EU:C:2015:477 (“*Huawei/ZTE*”). The CJEU in *Huawei/ZTE* determined the conditions under which a SEP holder can demand an injunction without abusing its position. By placing obligations on both the SEP holder and the SEP implementer, whereby the former should demonstrate it is a willing licensor complying with its FRAND licensing commitment and the latter should show that it is a willing licensee seeking a FRAND license, the CJEU has defined a helpful framework that applies to both parties’ behavior during their negotiations.

<sup>58</sup> See F. Gonell (Qualcomm), *The European Commission can achieve its goals without putting European participation in future standards at risk. Will it?*, 18 April 2023, LinkedIn. The proposal: (i) would allow the implementer to be free from the threat of an injunction by agreeing to enter into a license on FRAND terms as confirmed by a court or an agreed neutral third party; (ii) would address any concerns about the German courts’ application of the *Huawei/ZTE* framework resulting in injunctions against unwilling licensees without sufficient inquiry into whether the patent holder has made a FRAND offer.

<sup>59</sup> See Dolmans, “*The EC should, and can, incentivise FRAND rate setting by third parties if the parties can’t reach agreement*”, 19 May 2021, slide 97 onwards at [file:///C:/Users/MDolmans/Downloads/Presentations%20Webinar%20on%20Enforcement%20\(1\).pdf](file:///C:/Users/MDolmans/Downloads/Presentations%20Webinar%20on%20Enforcement%20(1).pdf), and <https://www.clearygottlieb.com/-/media/files/the-european-commission-should-and-can-incentivise-frand-arbitration-pdf.pdf>

<sup>60</sup> See WIPO Arbitration for FRAND Disputes, available at <https://www.wipo.int/amc/en/center/specific-sectors/ict/frand/annex1/>.

<sup>61</sup> See Section 315 of the German Civil Code (*Bürgerliches Gesetzbuch* - BGB).

<sup>62</sup> See *Unwired Planet v. Huawei* [2020] UKSC, 26 August 2020; *InterDigital v. Lenovo*, [2023] EWHC 539 (Pat), 16 March 2023. For more detail, see M. Dolmans, *FRAND licensing commitments – Back to first principles*, Elsevier, World Patent Information 69 (2022) 102113.

<sup>63</sup> See Article 7:900 of the Dutch Civil Code (*Burgerlijk Wetboek* - BW).

If a licensor or licensee refuses to agree to rate setting, that should be regarded as a rebuttable presumption that it is “unwilling.” The party refusing the rate determination could then rebut the presumption of unwillingness by proposing a rate that is FRAND.<sup>64</sup>

This alternative solution is designed to encourage a reasonable outcome, as both parties would have an incentive to agree on a rate: (a) if the SEP holder offers third-party rate determination and the implementer refuses, an injunction is available unless the implementer has offered a FRAND rate; (b) if the implementer offers third-party rate determination and the SEP holder refuses, no injunction is issued unless the SEP holder has offered a FRAND rate and the implementer refuses; (c) if neither offers third-party rate determination, the *Huawei/ZTE* process is followed. The court would have the last word on the FRAND rate.<sup>65</sup>

### ***Determination of Aggregate Royalties***

The Proposal also includes a procedure for determining an aggregate royalty (*i.e.*, the total maximum price) for using a standard before or shortly after its publication.<sup>66</sup> The objective is to determine the total royalty stack of the standard transparent, so that implementers can factor royalties into the cost of their products.

Three scenarios are considered:

- i. SEP holders for which FRAND commitments have been made may jointly notify the Competence Centre of the aggregate royalty which they have agreed

upon, which the Competence Centre shall publish.<sup>67</sup>

- ii. Where there is no agreement among SEP holders on an aggregate royalty, certain SEP holders may request the Competence Centre to appoint a conciliator to assist them. In this case, the role of the conciliator would be to facilitate the decision-making by the participating SEP holders without making any recommendation for an aggregate royalty.<sup>68</sup>
- iii. Finally, SEP holders and/or implementers will be able to ask the Competence Centre for an expert opinion on an aggregate royalty. When this request is made, the Competence Centre will appoint a panel of three conciliators and manage a process in which all interested stakeholders will be invited to participate. After receiving information from all of the participants, the panel will provide a non-binding expert opinion on the aggregate royalty.<sup>69</sup>

*SEP holders may have an incentive to declare a high royalty upfront*

Statements on aggregate royalties have been useful in the past, since they established parameters for FRAND rates for 3G and 4G mobile standards licensing.<sup>70</sup> But those statements were made by firms which were industry leaders at the time, and which both owned SEPs and implemented the standards. They had balanced incentives. As mentioned above, the Proposal allows for different multiple groups of SEP holders to jointly notify their views,<sup>71</sup> which could arguably lead to a variety of declarations, and confusion.<sup>72</sup> Furthermore, it is unlikely to be easy for

<sup>64</sup> But see *InterDigital v Lenovo* [2023] EWHC 539 (Pat) ([920]). The Court noted that it could not decide that Lenovo’s refusal to agree to an arbitration was the act of an unwilling licensee. It doubted that a SEP licensor which has been demanding supra-FRAND rates and was an unwilling licensor can automatically transform itself into a willing licensor simply by offering third-party adjudication of FRAND terms whilst continuing to demand supra-FRAND rates.

<sup>65</sup> In *Optis v Apple* Lord Justice Arnold urged “SDOs like ETSI to make legally-enforceable arbitration of [FRAND] disputes part of their IPR policies”. See *Optis Cellular Technology LLC v Apple Retail UK Ltd* ([2022] EWCA Civ 1411) ([115]).

<sup>66</sup> According to the Proposal, “‘aggregate royalty’ means the maximum amount of royalty for all patents essential to a standard.” Proposal, Article 2(10).

<sup>67</sup> Proposal, Article 15.

<sup>68</sup> Proposal, Article 17.

<sup>69</sup> Proposal, Article 18.

<sup>70</sup> See, for instance “Industry leaders NTT DoCoMo, Ericsson, Nokia and Siemens, and Japanese manufacturers reach a mutual understanding to support modest royalty rates for the W-CDMA technology worldwide; Ensures fair and competitive pricing for W-CDMA handsets and infrastructure equipment”, press release 6 November 2002, at [https://www.sec.gov/Archives/edgar/data/924613/000110465902006769/j6199\\_6k.htm](https://www.sec.gov/Archives/edgar/data/924613/000110465902006769/j6199_6k.htm).

<sup>71</sup> Proposal, Article 15.

<sup>72</sup> For example, some SEP owners could announce an aggregate rate of \$10 per product, another 5% of the end-product price, while a third group would prefer a lower \$1 per-product rate. In addition, several licenses indicate lump sum payments. Translating between running-rate ad valorem and monetary amounts per unit, and between these and lump sum payment figures, in order to make comparisons, is subject to a number of



any SEP holder to jointly reach any consensus within the 120 days' timeframe set out in Article 15(3). The short timeframe is exacerbated by the lack of guidance on the process and voting rules for approving the aggregate royalty.

In addition, it is not clear what difference the joint notifications of aggregate royalty rates would make to the existing practice of unilaterally announcing licensing terms.<sup>73</sup> SEP holders may view the *ex ante* declaration of their individual maximum royalties, or an aggregate royalty, as an opening bid in negotiations. They may therefore be incentivized to declare a high royalty in the hope that if the price is driven down in negotiations by caps and discounts, they will end up with more than if they had declared a low royalty to begin with. In such a situation, Cournot complement problems may lead to an excessive aggregate royalty, especially if SEP holders are not also active as implementers, and not all of the SEP holders participate in the exercise.<sup>74</sup> To reduce that risk, aggregate royalty calculations should ideally be accompanied by an effort to form a single patent pool for each standard.

SEP holders who are also significant implementers may have various incentives. On the one hand, they may wish to generate a positive network effect for a new standard by charging low royalties and encouraging other SEP holders to do the same. On the

other hand, if they can net off their royalty payments against amounts due to other large SEP holders, they may have an incentive to charge high royalties so as to lower their variable costs, and perhaps even exclude implementers with no or few SEPs from the market. When assessing aggregate royalty declarations, it is therefore important to take into account market conditions and, where possible, to rely on hedonic pricing<sup>75</sup> or contingent valuation analysis (even if only as a cross-check).<sup>76</sup>

## C. Conclusions

Markets that rely on technologies have thrived through licensing-based business models predicated on the ability to engage in arm's-length negotiations over licensing terms, and to obtain injunctions in the event of deliberate patent infringement. But SEPs present unique challenges, and risks of abuse.

The Commission is of the view that the EU-wide rules on transparency regarding SEPs and FRAND terms included in the Proposal would have a harmonizing effect within the EU, which would facilitate the work of national courts and the newly-launched UPC.<sup>77</sup>

Like the proverbial "curate's egg", the Proposal is good in parts, while hard to swallow as a whole. It deviates from approaches adopted elsewhere.<sup>78</sup> The

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subjective assumptions. See R. Jacob, I. Nikolic, *Comments Regarding the Draft EU Regulation on Standard Essential Patents*, International Center for Law & Economics, 28 July 2023.

<sup>73</sup> The Commission acknowledges that SEP holders may already publicly announce their royalty programs in advance. See Impact Assessment, at 84-85.

<sup>74</sup> Cournot complements theory indicates that prices will be higher when complementary inputs are provided by different suppliers acting independently. SEPs are necessarily complements - patented technologies are not in competition with each other once they have been selected for use in a standard and have become SEPs, and so the implementation and licensing of all of them is required. Different owners of complementary patents tend to set the rate they demand independently, ignoring that other patentees will do the same. The resulting royalty stack may exceed the optimal amount, leading to multiple monopoly rents. See M. Lemley, C. Shapiro, *Patent Holdup and Royalty Stacking*, 85 Tex. L. Rev. 1991, 2007 at 1992-93.

<sup>75</sup> In *InterDigital v Lenovo* (*InterDigital v Lenovo* [2023] EWHC 539 (Pat)), *InterDigital* characterised a "hedonic regression" as "an econometric analysis which seeks to isolate the fair market value of each of the technology generations over the previous, all other things being equal [...]. Thus, holding the screen size, processing power, brand and an array of other features of a device steady, it seeks to answer the question 'how much more is a phone worth by reason of the presence of the new technology generation'" ([823]). The Court, however, concluded that in that case "the hedonic price regression analysis was an experiment which was inserted into this trial via expert report without any of the usual procedural safeguards being observed" ([878]).

<sup>76</sup> Aggregate royalty determinations were used as a cross-check in *Unwired Planet International Ltd v Huawei Technologies (UK) Co Ltd* [2020] UKSC 37; [2021] 4 C.M.L.R. 3. However, they were overturned in *TCL v Ericsson* (*TCL v Ericsson*, Case No. 8:14-cv-00341-JVS-DFM (C.D. Cal. 2019)), and dismissed in *InterDigital v Lenovo* (*InterDigital v Lenovo* [2023] EWHC 539 (Pat)). On balance, they have played a secondary role in FRAND determinations. Licensing terms of comparable licenses are generally the primary indicator used to determine whether an SEP holder has made a FRAND licensing offer – even though the comparators could be affected by injunction threats. See *Ericsson v D-Link*, 773 F.3d 1201 at 1228 (Fed. Cir. 2014); at pp. 41-42.

<sup>77</sup> See Proposal, Explanatory Memorandum, para. 2. However, the Proposal may also inspire governments in other world regions to intervene further in the determination of FRAND royalty rates. In the absence of inter-governmental coordination at the global level, such efforts in different regions may result in different and potentially incompatible regulatory requirements applying in different parts of the world. See J. Baron, "The Commission's Draft SEP Regulation – Focus on Proposed Mechanisms for the Determination of Reasonable Aggregate Royalties", 2023, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4537591](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4537591).

<sup>78</sup> Since the UK Supreme Court's decision *Unwired Planet v. Huawei* in August 2020, SEP enforcement has spread across borders, as courts in the UK, China and other jurisdictions have signaled a willingness to resolve such disputes by imposing global licenses. In March 2023, the High Court

cost-effectiveness of the mandatory registration and essentiality checks is doubtful, taking into account that standards and even patent claims evolve over time, and essentiality determination is complicated. The rate determination may be more useful. Perhaps the most effective measure could be to amend the Proposal to encourage third-party rate setting proceedings that are binding on the parties, so as to incentivize them to reach a negotiated agreement.<sup>79</sup>

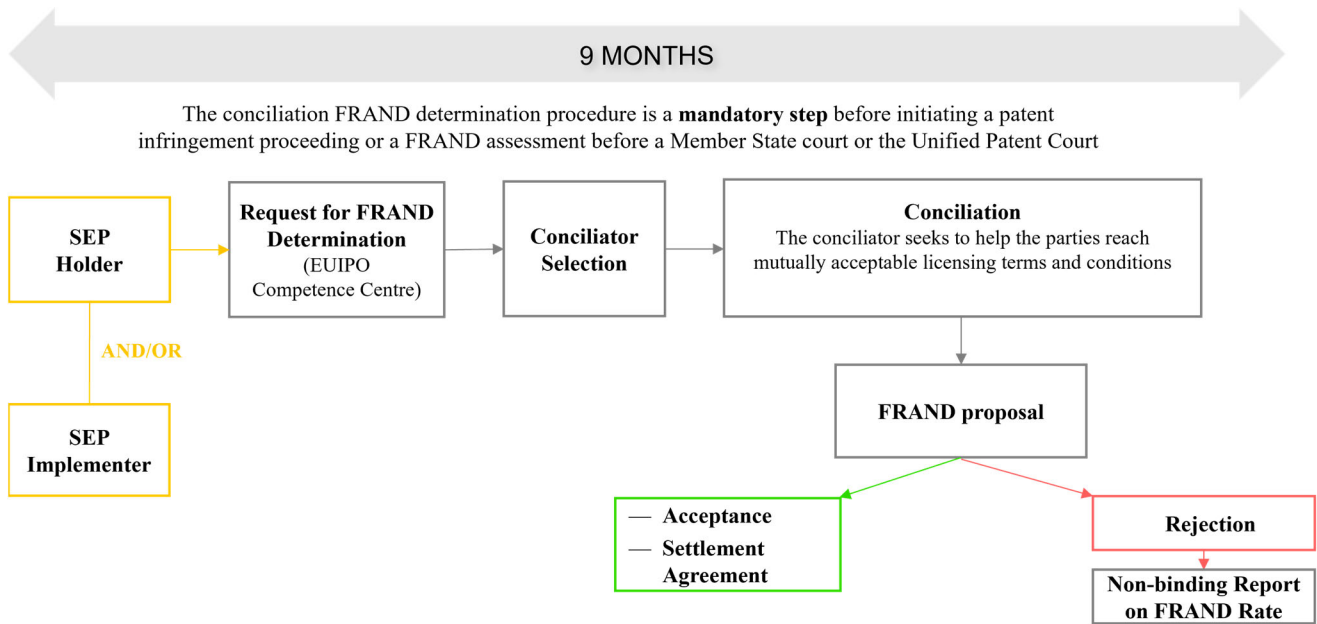
The publication of the Proposal is only a first step in the legislative process, and is controversial, especially with SEP holders. It awaits further discussion in and agreement from the Council of the European Union and the European Parliament before official adoption, with changes expected.

It remains to be seen whether the final version will retain all aspects of the current draft. The provisions on transparency of FRAND terms may be strengthened, and rate determination may become mandatory, whereas provisions on registration and *ex ante* essentiality determination (and associated delays) may be weakened or abandoned as too costly and insufficiently effective.

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of Justice issued a ruling in *InterDigital v. Lenovo*, the country's second global FRAND rate decision, further cementing the UK courts' stance on SEP enforcement. For a third decision, see *Optis v. Apple* [2023] EWHC 1095 (Ch), adopted in May 2023. In the United States, courts routinely undertake the task of determining global FRAND rates, but they do that with the consent of both parties, either to resolve claims of FRAND violations or to calculate the amount of damages for infringement claims. See Decision of the United States District Court for the Central District of California, *TCL v. Ericsson*, Case No. 8:14-cv-00341-JVS-DFM. In China, courts have claimed their jurisdiction to determine global FRAND terms in specific cases, which may impact the EU industry. See Chinese Supreme Court, ruling of 19 August 2021, *OPPO v. Sharp*, Zui Gao Fa Zhi Min Xia Zhong No. 517; Order of the Wuhan Intermediate Court of 23 September 2020, *Xiaomi v. Interdigital*, (2020) E 01 Zhi Min Chu 169 No. 1; and Order of the Wuhan Intermediate Court, *Samsung v. Ericsson*, (2020) E 01 Zhi Min Chu No. 743. Due to concerns about the compatibility of China's policy in this area with its World Trade Organization ("WTO") obligations, the EU has launched a complaint before the WTO against China's practice of issuing broad anti-suit injunctions to prevent the enforcement of SEPs in other jurisdictions. See DS611: *China-Enforcement of Intellectual Property Rights, World Trade Organization* (2022), available at: [https://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds611\\_e.htm](https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds611_e.htm). On global licensing, J. L. Contreras, *Global Rate Setting: A Solution For Standards-Essential Patents?*, 94 Wash. L. Rev. 701, 2019.

<sup>79</sup> As any major regulatory intervention into the determination of FRAND rates carries the risk of increasing fragmentation in the global SEP licensing ecosystem and injecting significant uncertainty, a more incremental approach is warranted. See J. Baron, "*The Commission's Draft SEP Regulation – Focus on Proposed Mechanisms for the Determination of 'Reasonable Aggregate Royalties'*", 2023, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4537591](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4537591).



*Fig. 1. Stylized flowchart of the conciliation FRAND determination procedure.*