

Japan SEP Licensing Guide Also Aims To Prevent Abuse

By Jay Jurata and Emily Luken (August 27, 2018, 4:53 PM EDT)

Law360 recently published an article by David Kappos, former director of the U.S. Patent and Trademark Office, describing and analyzing the Japan Patent Office's final draft of its "Guide to Licensing Negotiations Involving Standard Essential Patents." We agree with Kappos that the guide reflects a balanced approach to issues involving standard-essential patents subject to a commitment to license on fair, reasonable and nondiscriminatory terms. We also agree that the guide should serve as a valuable resource to both SEP holders and potential licensees. However, some of the article's characterizations of the theoretical and practical issues underlying SEP disputes are misguided. This article provides further perspective on those issues, and discusses other aspects of the guide that merit further attention.



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Consistent with an approach rooted in balance, the guide recognizes the significance of an SEP holder's FRAND commitment, which is intended to ensure downstream innovators have access to standardized technology while providing adequate compensation to SEP holders for their inventions. Importantly, the FRAND commitment is designed to mitigate against the risk of holdup, a problem that occurs when SEP holders wield their strong bargaining power to demand exorbitant royalties from potential licensees after they are locked into using a particular standardized technology. The guide properly notes that the FRAND commitment applies both to the licensing negotiation process as well as the terms of the license that is the product of those negotiations.



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Although the guide appropriately considers the rights of both SEP holders and potential licensees, it expressly acknowledges and expands upon concerns over potential abuses of SEPs. Such abuses include holdup, royalty stacking, seeking injunctions on FRAND-encumbered SEPs, and overdeclaration of SEPs.

Holdup

The guide states that "controversy" exists between SEP holders and potential licensees as to which is a more serious problem: holdup or holdout, whereby a potential licensee unnecessarily delays accepting a SEP license. But the guide also notes that "with courts continuing to grant injunctions, hold-up remains an issue for implementers."^[1] Thus, although the guide acknowledges that some SEP holders argue that holdout presents a greater threat than holdup, it does not endorse that view. Indeed, Kappos' claim that concerns over holdup "have since proven overblown at best" belies a well-established and growing body

of legal precedent that recognizes the contrary. In fact, in every single case where a court has been forced to determine a FRAND royalty rate, it has been orders of magnitude below what the SEP holder demanded.

Kappos' claim that "it is now understood that holdout is a more serious threat to the innovation ecosystem" is similarly unsound. While the Antitrust Division of the U.S. Department of Justice — to which Kappos cites — has recently expressed that holdout may be a bigger problem than holdup, this position remains an outlier view. For this reason, a large and prominent group of former government officials and law professors described the DOJ's current position as inconsistent "with the broad bipartisan legal and economic consensus that has existed for over a decade regarding standard setting."

Royalty Stacking

The guide also acknowledges that some commentators argue that there is no "concrete proof"[2] of royalty stacking. Royalty stacking occurs when a standard implicates so many patents that, in the aggregate, royalties due to the various patent owners "stack" on top of each other and become excessive. But again, simply acknowledging that a view exists is not tantamount to endorsing that view.

If anything, the guide errs toward acknowledging royalty stacking as a potential form of SEP abuse. The guide's treatment of royalty stacking occurs in the context of a broader discussion of the various methodologies used to calculate an appropriate FRAND royalty, including the top-down and bottom-up methods. Under the top-down approach, the aggregate royalty attributable to a standard under all SEPs is calculated and then allocated to the SEP owner in suit; under the bottom-up approach, the court determines the contribution of the asserted SEPs in isolation, often in conjunction with comparable licenses. Significantly — and consistent with the recent *TCL v. Ericsson* decision — the guide suggests performing a top-down calculation as a cross-check to a bottom-up, when that method is employed, to assess royalty stacking concerns.[3]

Injunctions on FRAND-Encumbered SEPs

Consistent with antitrust guidelines the Japan Fair Trade Commission amended in 2016, the guide acknowledges that an SEP holder seeking an injunction on a FRAND-encumbered SEP against a willing licensee may constitute a violation of competition law.[4] With respect to injunctions, the guide adopts an approach largely tracking the framework laid out by the Court of Justice of the European Union in *Huawei v. ZTE* establishing the respective obligations on the part of SEP holders and potential licensees for acting in good faith during licensing negotiations.

This framework explicitly affirms that injunctions on FRAND-encumbered SEPs should only occur under rare circumstances. Contrary to Kappos' assertion that the guide "notes evolving approaches among global competition authorities regarding the contexts in which injunctive relief is a suitable remedy for innovators," the guide states that "[l]egal precedents across the world seem to be converging toward permitting injunctions concerning FRAND-encumbered SEPs ... only in limited situations." [5]

Overdeclaration of SEPs

The guide also recognizes that a prospective licensee can still express a willingness to enter into a license without waiving the right to challenge essentiality, validity, and infringement (among other things) or being deemed to be acting in "bad faith." [6] Providing potential licensees with this line of defense is another effort to address the real world problem of SEP overdeclaration. Numerous studies

have shown that the overwhelming majority of “SEPs” that are declared essential, when tested in court, end up being neither valid nor infringed by products practicing the standard.

Conclusion

Over the past decade, courts and regulatory agencies around the world have been confronted with identifying solutions to the difficult problem of SEP abuse. The Japanese Patent Office’s guide represents the latest such example of those ongoing efforts. The guide is intended to, and does, strike an appropriate balance between SEP holders and potential licensees. At the same time, it recognizes the necessity to enforce the limitations arising from voluntary FRAND commitments and the necessity of enforcing them so as not to distort competition in downstream product markets.

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[1] Guide p. 1.

[2] Id. p. 42.

[3] Id.

[4] Id. p. 22.

[5] Id. p. 1.

[6] Id. p. 12.