

## Comparable licences entered in the shadow of litigation are the best benchmark

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A recent report published by the World Intellectual Property Organization on valuation methods for standard essential patents raises concerns that using comparable licences negotiated under litigation pressure to set global royalty rates may lead to rates that are not fair, reasonable and non-discriminatory. The report suggests that comparable licences influenced by litigation may distort market realities and bargaining dynamics and therefore may not reflect the true market value of the underlying technology.

This view is erroneous at best, and downright harmful to a well-functioning licensing ecosystem if it is applied widely or extended into a categorical rule that disqualifies or devalues such comparable licences simply due to the existence of litigation or injunction pressure.

For purposes of conducting market-based valuation of SEPs, comparable licences for similar patents and similar products, including licences negotiated in the shadow

of litigation, almost invariably provide the most probative evidence of market value for courts tasked with setting FRAND rates.

In this article, we argue that comparable licences, including those negotiated and concluded in the shadow of litigation, should remain the primary benchmark for setting FRAND rates.

Today, more than ever, litigation is a two-way street in SEP disputes. Implementers increasingly initiate proceedings or assert counterclaims against SEP holders, ranging from invalidity and nullity claims to competition law and worldwide rate-setting actions. Implementers face the risk of injunctions or damages, while SEP holders face the risk of delayed or lost compensation, findings of non-infringement, invalidation or nullification of asserted patents and violation of competition laws.

While lawsuits can drive up litigation costs and prolong the negotiation period for a potentially comparable licence, courts should not assume litigation pressure results in higher than market value royalty rates in the final licence agreement because litigation outcomes are fluid and can shift bargaining power on both sides.

## **Comparable licences offer the most informative benchmark**

Courts generally use three valuation methods for setting global FRAND rates – the comparable licence, top-down and bottom-up approaches. At a high level, the comparable licence approach considers actual licences covering similar patents and products offered by the SEP holder; the top-down approach calculates the proportional value of the infringed patents based on an aggregate royalty rate assumed for the entire standard; and the bottom-up approach values the incremental contribution of the infringed patents to the entire standard.

Recent cases in the UK, the Unified Patent Court and China have converged on using comparable licences as the preferred benchmark, and the top-down approach as a secondary method or cross-check on rate ranges informed by comparable licences.

Over time, this became the norm because comparable licences represent observed market outcomes, while top-down and bottom-up methods require courts to conjure value through assumptions about aggregate rates or incremental technical contribution.

The preference for comparable licences reflects the greater certainty and evidentiary support offered by actual licences for similar technology negotiated in arm's-length, market transactions, which are the best available signposts for valuation.

Despite general market and judicial preference for the comparable-licence approach, the WIPO report cautions that even comparable licences with similar characteristics as the licence in question may “unreasonably reflect the impact of litigation risk, bargaining power, information asymmetries or strategic considerations”, such that “the approach could perpetuate non-FRAND terms”.

The report blurs the line between general litigation and injunction pressure with potential “hold-up” or “hold-out” behavior, which it characterises as “non-FRAND factors” and asserts that “typical indicators of potential distortions include relatively high litigation costs compared with the expected change in royalties, the possibility of injunctive relief, fragmented litigation strategies or approaches to past sales that may reward delay”.

Those concerns may justify close scrutiny of a particular licence, but they do not establish that the mere presence of litigation makes a negotiated licence non-FRAND.

WIPO is not alone in making characterisations that could be seen as denigrating the overall comparability and legitimacy of comparable licences influenced by litigation. A similar view appears in *ZTE v Samsung*, where the Chongqing No. 1 Intermediate People’s Court analysed several prior licences, disqualifying one agreement as not comparable because it was negotiated under litigation pressure from global mutual lawsuits, while accepting another as comparable because it was concluded through voluntary negotiations without litigation or injunction pressure.

Courts should avoid any inquiry that disqualifies or devalues comparable licences on the presumption that litigation influenced the negotiation. The relevant inquiry should be whether there is actual evidence showing distortion of the agreed rate, not whether litigation was present.

In practice, every SEP licence is negotiated against the possibility of litigation. Without that enforcement backdrop, implementers have little incentive to take a voluntary licence and SEP holders have limited practical recourse for infringement.

The prospect of litigation therefore helps bring implementers to the negotiating table and is inherently part of the market realities and bargaining dynamics for SEP licensing.

The Munich Regional Court made this point in *Wilus v ASUS*, explaining that “the fact that there were infringement proceedings before the conclusion of the contract . . . should not be overestimated” because “not [an] inconsiderable proportion of market participants are not prepared to conclude licence agreements without the corresponding pressure from infringement proceedings”.

The court further concluded that “initiating infringement proceedings is a normal and acceptable part of the negotiations in order to find a licence rate that suits both sides”.

Litigation alone, in one or multiple jurisdictions, initiated by the SEP holder or the implementer, or both, cannot be sufficient reason to move away from the comparable-licences approach, which offers greater insight into market value based on concrete terms in existing licences, to either the top-down or bottom-up approach.

## **Litigation cannot be treated as contamination**

In SEP disputes, both SEP holders and implementers can initiate litigation. Each side has litigation tools that can affect bargaining power in concurrent settlement and licensing negotiations.

Comparability analysis should take into account legal risks on both sides and not assume pressure flows in only one direction. Whether or not litigation has actually been filed, both parties negotiate with the awareness that these tools may be used at any time to protect their legal and commercial interests.

SEP holders have strong incentives to conclude a licence. A FRAND commitment forecloses remedies to SEP holders that fail to make FRAND offers. Unless they offer a licence on FRAND terms, SEP holders have little likelihood of success bringing claims for injunction or damages against infringement.

As a result, they face even more pressure than implementers to reach agreement because, if negotiations fail and injunctive relief is unavailable, they have no practical way to stop uncompensated use of their patented technology.

Without litigation, SEP holders have limited tools to enforce their patent rights, while implementers may continue using standardised technology without paying until a licence is agreed. SEP holders therefore often face a choice between taking something through a licence or settlement and taking nothing while infringement continues.

A rule disqualifying or devaluing post-filing licences would penalise SEP holders for using lawful enforcement mechanisms after voluntary negotiations fail. It would also give implementers an incentive to resist voluntary negotiations and wait for the SEP holder to sue for infringement, thereby gaining the option to later argue any resulting licence is contaminated by litigation pressure.

Courts should not confuse the assertion of standard legal remedies with improper coercion. Litigation does not convert a negotiated licence into a non-market transaction.

Licences negotiated against the backdrop of litigation can be especially informative. By the time parties choose to settle, they may have the benefit of discovery, clear knowledge of each other's claims and defences, and a developed understanding of the strengths and weaknesses of their positions. Such additional information can reduce the information asymmetry that existed before litigation was initiated.

Those features can make litigation-related licences strong evidence of what informed parties are willing to accept when the relevant commercial and legal risks are visible.

Courts that categorically devalue or dismiss comparable licences merely because they were negotiated alongside litigation risks excluding valuable probative evidence. Litigation makes those licences more informative, not less.

## **Potential factors to consider in holistic comparability review**

Comparable licences concluded in the shadow of litigation should be presumed to carry the same weight as comparable licences concluded without litigation and should be assessed holistically for comparability.

For example, a SEP holder licensing the same or similar products under the same or similar SEPs might offer a lower price to an implementer that takes a licence without litigation than to an implementer that takes a licence only after litigation, given the cost, risk and delay of enforcement.

If the SEP holder has a record of offering an early-bird or no-litigation discount, and comparable licences concluded without litigation exist, courts can take that evidence into account when assessing the full set of comparable licences. But that does not justify categorically disregarding or devaluing licences concluded during or after litigation.

Courts should also consider whether the issuing court assessed the relevant FRAND claims before granting a preliminary injunction. Some have argued that when courts grant preliminary injunctions before giving the implementer a full and fair opportunity to present its FRAND defence, rates negotiated under that pressure may be distorted and should not be used as benchmarks.

In reality, this rarely occurs, but it should not be overlooked in a holistic comparability analysis.

In SEP disputes, courts should not enjoin implementers until they have considered the relevant FRAND issues. If a preliminary injunction is in fact issued without that assessment, courts should take that into account when considering whether to adjust a comparable licence concluded after the injunction took effect.

That said, SEP litigation often proceeds in multiple jurisdictions, making it difficult to conclude that developments in any one forum drove a global settlement.

Courts should therefore presume that a licence resulting from a litigation settlement is a valid benchmark unless the party challenging comparability shows that the licence was materially shaped by litigation in a court that failed to consider the FRAND defence and issued, or was about to issue, an injunction that affected the negotiation.

## **Conclusion: litigation-related licences should remain probative benchmarks**

Comparable licences concluded as a result of litigation should not be categorically disqualified or devalued in a comparability assessment. They are not perpetuating non-FRAND terms merely because they were negotiated in the shadow of litigation.

Courts tasked with setting royalty rates are facilitating licensing negotiations in the context of litigation themselves, which is more reason to consider comparable licences also negotiated alongside litigation to be directly comparable.

Litigation offers both SEP holders and implementers alike the opportunity to seek protection of their legal and commercial interests; it should not be viewed as improper coercion in the first instance.

Litigation-related licences offer just as much comparative value as any other licence, if not more, and courts should review all eligible comparable licences to adjust for any specific circumstances on a case-by-case basis.

The better framework is to start from a presumption of comparability, examine concrete evidence of distortion and adjust only in the rare instance where the challenging party shows that litigation pressure materially and improperly inflated or deflated the agreed rate.

We would encourage courts to continue using the comparable-licence approach, including licences concluded both with and without litigation, as the primary benchmark for setting global FRAND rates.



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