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Licensing and litigation under the RAND umbrella

Recent court decisions show that a commitment to a standards-setting organization, while flexible, is far from toothless.

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Large swaths of the economy, and immensely valuable patent portfolios, are entwined with standardized technologies. The owners of thousands of patents "essential" to standards have given voluntary commitments to standards-setting organizations (SSOs) to license those patents on "Reasonable and Non-Discriminatory" (RAND) terms. But both patent owners and prospective licensees confront the question: What does this RAND commitment mean? Does it seriously compromise the patent owner's ability to extract revenues from its patent? Or is it, on the other hand, an effectively unenforceable platitude?

The answer is critical to patent owners, investors, potential licensees and attorneys who advise them.

In fact, a RAND commitment, while indeed flexible, is far from toothless.

What does that RAND commitment mean? First, the language of relevant SSO rules generally requires that the patent holder that has made a RAND commitment offer licenses on RAND terms in good faith to all who wish to practice the standard. Courts (including recently the District Court of The Hague, Netherlands, in its Oct. 14, 2011, decision in *Samsung v. Apple*) have found this to be a binding obligation, refusing to grant injunctive relief to a patent holder that offered licenses only on blatantly unreasonable terms.

Second, the bedrock purpose of the SSOs' RAND licensing requirements is to ensure that necessary licenses are meaningfully "available"; given this recognized purpose, royalty demands that effectively preclude commercialization of the standard, or block standardization by all but the patent holder, could not be "reasonable." Beyond this, there may be no universally applicable definition. Certainly, there is nothing in the text or origin of the RAND requirements of major SSOs that dictates any particular allocation of value between licensors and licensees.

Responding to this reality, some commentators have complained that RAND is too loosely defined, and have called on SSOs, courts or regulators to invent more formulaic definitions. A recent report issued by the Federal Trade Commission argued this line. FTC, "The Evolving IP Marketplace," March 2011. However, it appears that SSO intellectual property rights policies have defined RAND loosely by design, not inadvertence. SSOs are nominally free to adopt whatever licensing policies they like, but they are in fact constrained by the need to secure participation by innovators as well as manufacturers, and to attract the contributions of high-value as well as merely incremental IP to their standards.

The uniformity of the result of this real-world balancing act is striking. Although a few commentators over the years have advocated that SSOs should require royalty-free licensing of members' "essential" patents, or have advocated some form of cumulative "cap" on royalties for such patents, almost no SSOs have gone down this road. A very few SSOs over the years have adopted royalty-free licensing requirements, but the overwhelming majority of SSOs internationally have been content to rely on the concept of "reasonableness" without attempting further definition, and there is no sign of any trend toward more detailed licensing obligations in SSO rules.

THE REASONS FOR FLEXIBILITY

This "stubborn" persistence in flexibility is not really surprising. The relative value of intellectual property (as a proportion of the total value of the product) will vary hugely from one standardized product to another. For example, low in the case of simple compatible plugs, and high in the case of cellular phones. That value balance may also shift substantially from one generation of a technology to the next. For example, the total industrywide research-and-development investment required to bring 3G cellular phones to the market far exceeded that required for 2G phones, while the market price for handsets remained generally steady. An SSO licensing rule that prohibits recovery of IP value through royalties (as in the case of a royalty-free licensing requirement), or that attempts to cap total royalties at a constant rate, cannot meet the endless variety of investment and value equations. It is likely for this same reason that patent statutes in jurisdictions around the world do not attempt to impose any formula for fixing royalty-based infringement damages, but instead go no farther than specifying that "reasonable" royalties should be awarded.

In addition, companies commonly negotiate an almost endless variety of value-creating exchanges within the complex licensing and cross-licensing agreements that predominate in high-technology industries. These are often not confined to royalty payments alone, but may include up-front payments, incentives to spur early adoption, volume discounts, joint development funds or other forms of co-investment, and more. To break out and impose any formulaic limitations on just the royalty portion of these complex relationships would severely constrain the range of possible value-creating deals, harming all participants and ultimately consumers. The alternative of asking courts to attempt to value and balance the noncash components of these relationship-building deals would likely produce results no more predictable than the simple "reasonableness" requirement on which SSOs currently rely.

The bottom line for the adviser today is that RAND continues to leave very wide flexibility to the negotiation room.

But is saying that RAND is loosely defined and fact-specific really a polite way of saying that it is meaningless and effectively unenforceable? Far from it. A patent holder that assumes that RAND is an inconsequential platitude would be making a grave error.

INTERNATIONAL RECOGNITION

The force of a RAND commitment is empirically visible in the real world. Courts in the United States and Europe are entertaining "failure to offer RAND license terms" defenses. See, e.g., *Nokia v. Apple*, No. 1:09-cv-00791-GMS (D. Del. settled 2011); *Samsung v. Apple* (Tribunal de Grande Instance de Paris, pending); *Samsung v. Apple* (Dist. Ct. The Hague, pending). Although injunctions based on nonessential patents issue as a matter of course under the patent laws of countries around the world, important injunctions against the sale (or importation) of a standardized product based on a RAND-committed patent have been almost nonexistent despite the fact that standards and essential patents have existed for decades. With exceedingly rare exceptions, we do not see nonpracticing entities (often referred to as "patent trolls") purchasing and asserting patents that are subject to a RAND commitment; clearly, a RAND commitment is perceived to limit upside royalty demands, the likelihood of obtaining an injunction and the in terrorem value of a patent.

This makes sense. Once a defense of "failure to offer RAND terms" has been raised, a court is unlikely to issue an injunction against the infringer that attempted in good faith to take a license, until the RAND defense has been adjudicated. See, e.g., *Samsung v. Apple* (Tribunal de Grande Instance de Paris, Dec. 8, 2011); *Samsung v. Apple* (Dist. Ct. The Hague, decision dated Oct. 14, 2011). Cf. *Motorola Mobility v. Apple* (Mannheim, Germany, Regional Ct., Dec. 9, 2011, rejecting RAND defense when Apple did not first attempt to obtain a license). Whatever the merits and final result, the patent owner thus faces the certainty of additional procedural hurdles, expenses and delays before it can obtain an effective remedy against an unlicensed infringer. Potential licensees know this, too, which means that this reality will overhang the license negotiation room as well, driving down the threat value of patents subject to RAND commitments — and inevitably affecting the negotiation.

And all of this skips over the first and likely most common "enforcement" mechanism of RAND. The vast majority of standards-essential patents are held by major industry players — companies that are participants in multiple standards-setting organizations and projects, and that are repeat players in successive generations of standards. While such companies are negotiating licenses in one conference room, they almost invariably have teams cooperating — or contending — in ongoing standardization projects elsewhere in the world. A patent holder that is seriously unreasonable in its demands in the negotiation room can expect a cold reception for its technologies at the next standardization meeting.

In recent years, the number of patents made subject to a RAND commitment for one standard or another has shot up, and increasing numbers of companies find "essential patents" to be essential to their businesses. This trend has created new commercial realities, and a new necessary step in "due diligence" on patents. When considering a corporate acquisition built around IP value, a portfolio purchase or a potential license, or the costs and benefits of launching (or being on the receiving end of) patent litigation, advising counsel will want to know from the start whether the key patents have ever been made subject to a RAND commitment by any previous owner.

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