STANDARD-ESSENTIAL PATENTS AND MARKET POWER

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Standard-Essential Patents and Market Power

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While most agencies that have addressed the issue recognize that intellectual property rights (IPRs), including standard-essential patents (SEPs), do not necessarily confer market power,[2] there remains much confusion over how to determine the proper relevant market and the issue of whether a particular SEP owner has market power. For example, some agency officials have contended that, while not always the case, SEPs will "generally" or "typically" confer market power absent the existence of substitutes such as competing standards. As an initial matter, empirical research suggests that standardization does not automatically confer market power, but rather frequently "crowns winners," i.e., more important technologies are natural candidates for inclusion in standards. This is particularly important in jurisdictions such as the United States, in which antitrust laws do not punish extraction of monopoly profits, but reach only exclusionary or predatory conduct. Also flowing from this finding is that the issue of whether a particular SEP holder has market power requires a case-by-case fact-specific inquiry into whether a single SEP (or portfolio of SEPs) constitutes a well-defined relevant market, whether there are potential substitutes, and the degree to which any market power is mitigated by complementarities among technologies used for the same product.

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[2] *See, e.g.*, KOREA FAIR TRADE COMM'N, REVIEW GUIDELINES ON UNFAIR EXERCISE OF INTELLECTUAL PROPERTY RIGHTS pt. (II)(2)(B) (2014), http://www.ftc.go.kr/eng/bbs.do?command=getList&type_cd=62&pageId=0401; Press Release, KFTC Rationalizes Its Regulations on SEPs to Promote Technology Innovation (Mar. 30, 2016), http://www.ftc.go.kr/eng/bbs.do (amending 2014 KFTC IP Guidelines); STATE ADMIN. FOR INDUS. & COMMERCE, RULES OF THE ADMIN. FOR INDUS. AND COMMERCE ON THE PROHIBITION OF INTELLECTUAL PROPERTY RIGHTS FOR THE PURPOSES OF ELIMINATING OR RESTRICTING COMPETITION art. 6 (2015), http://www.saic.gov.cn/zwgk/zyfb/zjl/fld/201504/t20150413_155103.html; STATE ADMIN. FOR INDUS. & COMMERCE, ANTI-MONOPOLY ENFORCEMENT GUIDELINES ON ABUSE OF INTELLECTUAL PROPERTY RIGHTS (DRAFT) art. 4 (2016), http://www.saic.gov.cn/zwgk/zyfb/qt/fld/201602/t20160204_166506.html; NAT'L DEV. & REFORM COMM'N, ANTI-MONOPOLY GUIDELINE ON INTELLECTUAL PROPERTY ABUSE (DRAFT) pt. (I)(i)(2) (2015), http://www.sdpc.gov.cn/gzdt/201512/t20151231_770313.html; U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY (DRAFT) § 2.2 (2016); Edith Ramirez, Chairwoman, FED. TRADE COMM'N, Standard-Essential Patents and Licensing: An Antitrust Enforcement Perspective 4 (Sept. 10, 2014), https://www.ftc.gov/system/files/documents/public_statements/582451/140915georgetownlaw.pdf ("[T]he same key enforcement principles [found in the 1995 IP Guidelines] also guide our analysis when standard essential patents are involved.").

Whether Standardization Confers Market Power

As the U.S. antitrust agencies recognized in their 2007 Intellectual Property Rights Report, it is important to distinguish between two sources of potential market power: "'the market power that comes from the technology on its own and the market power that comes just from the standard, the act of setting a standard that elevates a technology above the competitors.'"[3] Empirical research underscores that in certain circumstances incorporation in a standard will make a patent a "winner" in the market, but more commonly valuable technologies are natural candidates for inclusion in standards. In other words, standard development organizations (SDOs) frequently "crown winners," not create them.[4] For example, one study analyzing a database of patents declared essential to a range of standards including telecommunications technology (e.g., W-CDMA) and imaging standards (e.g., MPEG2 and MPEG4) found that the most prevalent effect of a patent's inclusion in a standard is no or a negligible impact on the value or importance of that patent, measured by forward citations. This result suggests that inclusion in a standard in itself does not necessarily or even ordinarily create market power.[5]

Determination of Market Power

The issue of whether a particular SEP holder has market power requires a case-specific inquiry. First, SEPs are self-declared to SDOs yet no SDO evaluates essentiality, which itself may change over time as the standard continues through development and as new generations are issued.[6] Until an independent legal and technical review[7] establishes that a particular patent declared "essential" is in fact essential for compliance with the standard, there should be no presumption that an SEP confers market power. Second, even restricting the analysis to truly essential patents, one cannot perfunctorily conclude that an individual SEP or a portfolio of SEPs constitutes a well-defined relevant market or that the owner possesses market power.[8] Genuinely essential patents are perfect complements, which creates a connection among patents and patent holders such that SEPs cannot be licensed in isolation. In particular, FRAND royalty rates are tied to the value the patented technologies contribute to the standard, which inherently accounts for all valuable contributions to the standard. In addition, because licensees know they must license other SEPs to be compliant with a given standard, licensees tend to push back in

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[3] U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION 39 (2007) (quoting Lauren J. Stiroh, Vice President, Nat'l Econ. Research Assoc., Remarks at Hearing: Licensing Terms in Standards Activities 321–22 (Apt. 18, 2002)).

[4] *See, e.g.*, Anne Layne-Farrar & A. Jorge Padilla, *Assessing the Link Between Standards and Patents*, INT'L J. IT STANDARDS & STANDARDIZATION RES., July–Dec. 2011, at 19, 25.

[5] *Id.* at 40-43.

[6] Anne Layne-Farrar and Michael Salinger, *The Policy Implications of Licensing Standard Essential FRAND-Committed Patents in Bundles* at 7 (July 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2846147&download=yes.

[7] Typically only conducted during litigation or if the patent is submitted for inclusion in a patent pool.

[8] Layne-Farrar & Salinger, *supra* note 6, at 7.

negotiations if they think an SEP holder is attempting to ask for more than its share. Thus, in contrast to a monopolist, which can set prices without considering the reaction of other firms, an SEP holder cannot act unilaterally and must take into account the value of other SEPs when setting its royalty rates.[9]

Conclusion

Agencies and courts should avoid presuming that a particular SEP holder has market power and instead should analyze the issue on a case-by-case basis taking into consideration issues such as whether a single SEP or portfolio of SEPs constitutes a well-defined relevant market, *whether* self-declared SEPs are truly essential to the standard at issue, whether there are potential substitutes within a given standard or across standards, and the degree to which any market power is mitigated by complementarities. Careful analysis of this sort can avoid erroneous conclusions about the existence of market power and thus help to protect both competition and innovation.

[9] *Id.*