

Open Book

A recurring feature
by John T. Ramsay, Q.C.

A review of current publications relating to the field of Intellectual Property licensing, transfer and tools therein.



“TECHNOLOGY PATENT LICENSING: An International Reference on 21st Century Patent Licensing, Patent Pools and Patent Platforms” by Larry M. Goldstein and Brian N. Kearsy

Paperback: 579 pages
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This book will appeal to a specialised audience (developers, licensors, and licensees of “standardised technology” and their legal advisors), but that audience will find it a highly useful tool. A critical issue for developers of standardised technology is the risk of patent infringement suits. There are many patents in the same space; many overlapping and some of questionable validity.

The implementation of the standard can be hindered as a result of the multitude of patent suits and the problem of royalty stacking—often the cumulative royalties that have to be paid to all the patent holders are beyond economic reasonableness. An obvious solution for this problem is co-operation amongst all the players so that they work collectively and agree not to sue each other and thus can get on with their business. This, however, is too simplistic. It flies in the face of rules preventing restraint of trade, and in particular the U.S. antitrust rules. So, when is co-operation permitted and when is it prohibited? When it is permitted, how do you make the sharing work?

Earlier this year, I was involved in a not-for-profit entity applying for funding to become a Canadian centre for excellence for micro-fluidic technology. (In hindsight, it might as well have been a NANO play for all the visibility we got from the reviewers!) We recognized that we needed to standardize the target technology, and needed to develop a mechanism for “sharing” essential patents. It was surprising to me how little literature there was on this topic. The U.S. anti-trust rules are available on the Internet as well as some precedents for patent

pools. But the material was fragmented and gave you only what the drafters selected, not the process of rejection and selection of possible solutions. This book now fills the gap.

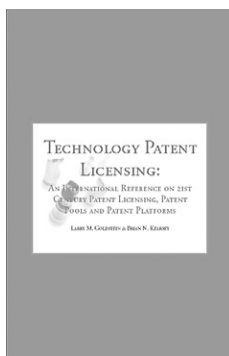
The authors participated in the development of the 3G Patent Platform, a multi-licensor arrangement for the licensing of patents essential to third generation cellular systems. This book is therefore the writing of experienced practitioners.

In the first page of their “Foreword,” the authors develop the distinction among traditional bilateral licensing (including cross-licensing), patent pools and patent platforms:

In the past, and until relatively recent times, the clearly dominant form of licensing is what is know as “bilateral licensing.” This is a license contract between one licensor and one licensee, in which the licensor grants rights to technology and the licensee pays money. The parties may also “cross-license,” which is an arrangement in which each party grants rights to the other, and there may or may not be payments from one party to the other. Cross-licensing is simply another form of traditional bilateral licensing.

More recent times, particularly the 20th century, have witnessed the creation and growth of the “patent pool.” This is an association of one or more holders of patent rights essential to the implementation of a technical standard in which the patent holders authorize an agent to license their patent rights as a group. The list of included patents, the royalty rates, and other terms and conditions, are typically very fixed. The pool approach has been applied recently, with considerable success.

The newest form of patent licensing is a hybrid of bilateral licensing and the patent pool. Called the “patent platform,” this form of licensing features centralized patent evaluation and centralized administration of the program, similar to the patent pool, but with greater flexibility of licensing terms and conditions. This organization is, in the author’s opinion, the most suitable for very complex standards that feature multiple products, multiple technologies, multiple national markets, and competition in which patent holders use their intellectual property actively to obtain commercial advantage. These are the characteristics of, for example, cellular communication standards and markets.



The authors develop the distinction further at pages 69-71.

The key character of bilateral negotiations is their individuality. There is no formal framework, patent evaluations are done by each party, and licensing is solely what the parties agree. Since each party does its own evaluation of patents, and its determination of licensing terms, the costs of negotiation are typically very high. A typical bilateral negotiation may extend over several months, and involve highly skilled personnel such as engineers and other technologists, licensing lawyers, and business developers. Although the costs of bilateral negotiations are usually high, this is the preferred approach where individual and individualized licenses are required, and where technology is simple. "License and make" contracts are standard cases for bilateral negotiations.

The patent pool is dramatically different from bilateral negotiations. In a pool, a group of patent holders "pool" their patents. Evaluation is typically conducted by one person, or a small group of people, who are not employees of any licensor but rather independent (at least to some degree). All patents found to be "essential" by the evaluators are licensed as one package to every licensee, for a standard price, regardless of the licensee's circumstances or particular needs. By the same token, each patent holder who becomes a licensor through the pool has no flexibility to change any terms of its participation in the pool, or to individualize contracts with specific licensees. That means fixed royalties, no patents outside the pool, no cross-licensing, no non-monetary compensation, and no licensing terms other than those established by the pool.

Relative to bilateral negotiations, which have no organization and hence no organization costs, the costs to organize the pool are significant. The parties must have their patents evaluated, they must set the terms of the licensing contract, and they must set up the licensing administration. However, the costs of negotiating specific licenses are quite low, since the licenses are offered to all interested parties on a "take it or leave it" basis. The pool is an excellent means for organizing licensing where the scopes of technology and product are limited, and where the number of holders of essential patents is not large. Good examples of successful patent pools are the DVD Patent Pools, and the MPEG-2 Patent Pool... The patent pool is clearly not suitable where completely individualized licenses are required (as in bilateral negotiations), or where technologies and standards are so complex that the licensors and licensees need some flexibility in negotiations (for which the patent platform is the approach of choice).

The authors, at pages 72-73, develop the unique characteristics of platform licensing (using a diagram for an assist that I will not reproduce).

Bilateral negotiations are completely flexible, but have no organized structure and no certainty of final terms and conditions in the license. Patent pools offer very clear structures, and well-known terms and conditions in a standard license that is not subject to any change. The

patent platform is unique in that it provides structure and certainty in both evaluation and licensing, while at the same time affording the licensor and licensee the maximum possible flexibility of negotiated solutions.

How does the platform provide structure and certainty? Parties joining the platform agree to submit their patent to the evaluation process, and then license any patents that are found essential, according to the terms and conditions of the SLA [Standard License Agreement]. Either party to the negotiations, the licensor or the licensee, may demand to grant or receive a license to use the essential patents according to the terms of the SLA. That is the bottom line. The parties know, in advance, which patents are essential to the work of the licensee, what will be the Standard Royalty Rate ("SRR"), and what will be the standard non-financial terms of licensing. The terms of licensing are administered by a Licensing Administrator responsible for administering the licenses, and that fact is also known to the parties. Thus, the platform provides structure and certainty.

At the same time, the parties have very broad flexibility to alter the standard terms and arrive at any agreement they wish. In a macro-sense, at least three different approaches are allowed. These approaches are: First, the parties may taken an Interim License Agreement ("ILA") on a temporary basis, then later take an SLA; Second, the parties may dispense with the ILA, and go directly to the SLA; Third, the parties may negotiate bilateral licenses totally apart from the ILA or SLA... Variations in these three approaches may be imagined, but in the end the license will either include the ILA or not, and will be modified SLA or an agreement totally apart from the SLA.

The critical criteria for successful pooling are the establishment of licenses with fair, reasonable and non-discriminatory ("FRAND") terms, and the determination of what patents (indeed, not patents, but rather specific patent claims) are "essential" and thus part of the pool. Goldilocks' rules apply; the pool and terms cannot be too large (since the inclusion of non-essential patents could constitute an anti-trust violation), nor too small (from the reluctance of some patentholders to participate in the pool), but rather must be just right.

Unfortunately "FRAND" is not well defined. Fortunately for us, the authors offer us an interpretation at pages 27-28:

Thus, there is no formal definition of the term agreed upon by the Intellectual Property community. In the absence of such a definition, we would suggest that the term FRAND should be interpreted and applied to include the following elements:

a) "Fairness" is a matter of knowledge and process, analogous perhaps to what lawyers sometimes call "Due Process" in legal proceedings. It means that there is a procedure for arriving at a result, that the procedure gives equal consideration to both sides, and that the procedure is well known to both sides before the procedure begins.

b) “Reasonable” is focused on the result, not the process. It means that the end result is something that allows both parties to feel that the outcome is acceptable, and that they can live with the outcome. Terms like “reasonable care,” and “reasonable doubt,” can never be completely defined, but in the context of patent licensing, “reasonable terms and conditions” for a license may be at least approximated.

c) “Non-Discriminatory” means that neither side suffers in comparison to similar deals struck by either of the parties with outside or “third” parties. Discrimination, like “fair” or “reasonable,” is also a very difficult word, ambiguous and laden with memory and emotion. We can say, however, that “non-discriminatory” does not require every party to get exactly the same license from every other party, but the word should mean at least that each party can say that it received a “reasonable” deal in comparison to some standard, and therefore that the deal it received was “non-discriminatory.”

At page 40, the authors provide us with the core issues about the design of the patent pool (read “platform” as well from now on):

In our view, two things are required to give some kind of objective meaning to the term FRAND. These are first, a reasonable, “credible in the industry” assurance that the patents being licensed really are “essential” to implementation of the standard, and second, a combination of known terms for license to such “essential patents,” with, however, flexibility to allow the negotiating parties to strike their own deal.

Chapter 3 is dedicated to the “Determination of Essentiality.” Let’s continue to look at the credibility issue. At pages 89-90, they write:

A credible evaluation process must provide:

1) An industry-credible, neutral, third-party evaluator;

2) A methodology for evaluation that is perceived in the industry as fair and credible for the determination of essentiality, including participation of interested parties where appropriate;

3) Deliverables from the process that are easily understandable and of immediate use. In the 3G Patent Platform process, there are two deliverables. These are the “Declaration of Essentiality,” which is a statement of intent to classify a patent as essential (but prior to the re-evaluation process), and the “Certification of Essentiality,” which is the final decision that a patent is essential.

Good faith declarations of essentiality may not be reliable or credible (Page 54-55). Keep in mind that once a patent is included in a pool or platform, it has equal value to all other included patents.

In order to administer a patent pool, you will need an entity to act as co-ordinator and licensing administrator. This administrative entity may be a for-profit or not-for-profit entity, but in either case the entity’s goals will be similar. The authors’ discussion as to the identification

of goals for this entity may give you a flavour for their writing and an indication of the detailed guidance they give us readers (at pages 313-314):

Step 3: Identify Goals

The initiative will succeed only if the participating companies can agree on the business and commercial motives for defining and operating the organized patent licensing arrangement for the relevant technical standard. What is to be achieved? The following is a non-exhaustive list of goals, or combination of goals, to be achieved by the arrangement:

- Reduce the cumulative royalty rates for all manufacturers (but not to the detriment of the patent holders).
- Maximize the usage of the technology in a range of products, in order to insure expansive royalty revenue on a global basis. (That is, maximize use of the technology.)
- Speed the earliest possible adoption of the technology.
- Help insure interoperability of services and interconnection of systems and equipment.
- Develop new markets with innovative global products.
- Reduce the transactions costs of licensing. (These costs are in money, the intensive attention of highly skilled personnel, and delay to market.)
- Insure effective and efficient collection of royalty revenues from the licensees.
- Assist in patent infringement actions.

The participating parties should be clear about the purpose and intended outcome of the initiative. If the prime intent is to resolve a known potential business problem, such as the limitation of cumulative royalty costs payable on product type X, then this should be made clear. In practice, the intended outcome is likely to be far more encompassing, in order to satisfy the diverse business demands of each participating party.

The authors consider this step to be critical. A written, unambiguous, and fully agreed statement of intent will help define the final goals of the arrangement.

Once you have established the Licensing Administrator, you need the standard licensing agreements. The authors tell us that there are three basic agreements:

(a) The Framework Agreement (the contract among the licensors to license their essential patents together);

(b) The Standard License Agreement (the standard agreement between a licensor and each individual licensee which serves as the default agreement, as the parties cannot settle on a mutually acceptable license agreement);

(c) The Interim License Agreement (the governing document until the parties entered into a negotiated agreement or default or until they default to the standard agreement).

The authors develop ten key concepts in these three basic agreements:

- (a) Concept 1: Product Categories;
- (b) Concept 2: Base Multiplier;
- (c) Concept 3: EX Works Sales Value;
- (d) Concept 4: Reference Market Value;
- (e) Concept 5: Maximum Cumulative Royalty;
- (f) Concept 6: Standard Royalty Rights;
- (g) Concept 7: Cumulative Royalty Rights;
- (h) Concept 8: Total Royalties;
- (i) Concept 9: Collection Point;
- (j) Concept 10: Review and Adjustment Process.

As you would expect, the authors dedicate a chapter to the anti-trust issues for the U.S., Europe and Japan. Critical material to understand for a pool to survive the restraint of trade challenge.

The last 250 pages out of a total of 579 pages in this book form the appendices where you can find examples of the agreements, anti-trust reviews and releases.

This is a very useful, focused book to be read only by a person with some familiarity with the topic. One criti-

cism: the authors address the problem of “fragmented” intellectual property rights, but in the early portion with a fragmented topic progression. Why have 40 or so pages on FRAND before you get to read about the distinction among bilateral licensing, patent pools and patent platforms, which to me is the essence of the topic? FRAND leads right into “Essentiality” yet the two topics are separated by a chapter of 22 pages. (Grump, grump, grump!). So speed read it and then decide what you want to read in your own progression. The material is there, and the material is good. These are complex topics and they tackle the complexity well overall.

A very focused book with lots of practical guidance for those who are involved in sharing patents. Pricey: Yes. But I spent all too many hours (non-billable as it turned out) trying to get a rudimentary handle on this topic. I wish that this book was available to me earlier. And can you imagine—Goldstein made his contribution while somehow managing his career and his role as father of seven (read 7) children!

Thanks to both of the authors for sharing their expertise and practical guidelines.