IP EUROPE RESPONSE TO CONSULTATION HT.5454 ON THE DRAFT REVISED HORIZONTAL BLOCK EXEMPTION REGULATIONS AND HORIZONTAL GUIDELINES

About IP Europe

IP Europe is a coalition of research and development-intensive organisations whose inventions are protected by intellectual property rights. IP Europe's goal is to promote the vital importance of Intellectual Property Rights to the European digital and knowledge-based economy and to ensure that EU policies support a world-leading innovation ecosystem. IP Europe is a member-driven organisation representing key innovators in the standardised technology space.

Introduction

With this document, IP Europe submits comments in response to the European Commission's public consultation on the draft revised Guidelines on horizontal cooperation agreements ("Horizontal Guidelines"). In doing so, IP Europe refers to the comments it provided to the General and targeted consultations of 30 September and 5 October 2021 as well as our submissions in the Evaluation and Impact Assessment phases of the review process. The responses below reflect the collective input of its members, which have extensive experience with various standard setting organisations (SSOs), standard development organisations (SDOs), and similar consortia/fora. It may not represent the complete position of the individual members, nor their respective practices, and individual members of IP Europe may have different perspectives on the various policy topics.

As indicated previously, IP Europe considers that changes to the Horizontal Guidelines should be made only in response to clear economic evidence of material harm, or in the case of evolution of the relevant law or policy. Further, we would like to emphasise once more the need for a balanced approach[1] to the Horizontal Guidelines that takes into account the growing, well-documented problem of hold-out and its implications for the well-functioning of the open standardisation system that is one of the cornerstones for innovation in Europe.

The open standardisation system – built on effective IP protection and enforcement and FRAND licensing – is generally working albeit under increased pressure of hold-out behaviour (as further discussed below). The system is providing broad access to standardised wireless technology for implementers across sectors, and for all actors in the relevant value chains. Moreover, access is provided at reasonable cost.

[1] As IP Europe has observed previously, there is only a small number of companies making significant contributions to standards as compared with a very large (and increasing number) of implementers which benefit from standardised technology. This fact has implications in terms of taking a purely statistical approach to the responses/data provided in response to the consultation. We hope that the European Commission will factor this into their assessment.

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Focus of Chapter 7 of the Horizontal Guidelines

The Guidelines are concerned with how SDOs develop standards and ensure effective access to those standards on a fair, reasonable and non-discriminatory (FRAND) basis. They are intended to provide safe harbour guidance to SDOs under Article 101.

The Guidelines are not, nor should they be, directed to bilateral licensing negotiations. Only Article 102 might have any direct applicability to such negotiations. Accordingly, the Guidelines should not ascribe whether or how an IPR holder is to license its IPR. Provided that the commitment ensures effective access to a standard on a FRAND basis, that is the end of the matter as far as the applicability of Article 101 is concerned.

FRAND and Licensing Level: the possible improvement of Paragraph 482

The debate about the licensing level in the supply chain has recently been addressed by Courts in the EU. In addition, new studies have been made comparing IPR Policies of different standard development organisations (SDOs) and illustrating the approaches chosen by those SDOs as a function of the technology that is standardised.

IP Europe has explained before how an "access for all approach", with licensing taking place at a single point in the value chain providing access for all actors along that chain, reflects decades of industry practice. European courts have also confirmed that licensing should take place at the point in the value chain where the *value* of connectivity is realised.

In *Nokia v Daimler* (Regional Court (Landgericht) of Mannheim 18 August 2020 - Case No. 2 O 34/19) the Court pointed out "*that the patent holder must, in principle, 'be given a share' in the 'economic benefits of the technology to the saleable end product at the final stage of the value chain'*."[2]

In addition, the Court found that the selling price of TCUs did not sufficiently mirror the value of Nokia's Standard Essential Patents (SEPs) for the cars produced by Daimler, which are the relevant end devices in that case. The selling price of TCUs corresponds only to Daimler's respective costs. Connectivity, on the other hand, allows Daimler to generate income from additional services offered to its clients, save costs to it and optimise its R&D expenses. Connectivity secures the opportunity to create this value. In addition, the Court noted that the acceptance of the licensing model of the Avanci platform (which grants licences exclusively to car manufacturers) by several of Daimler's main competitors serves as a further indication that focusing on the value of the protected technology for the end product is also reasonable in the automotive sector.[3]

In *Sharp v Daimler*, the Regional Court (Landgericht) of Munich on 10 September 2020 (Case No. 7 O 8818/19) indicated that "*EU competition law does not establish an obligation to license SEPs at all levels of the value chain*" and that patent holders are in principle free to choose the level of the value chain for licensing.[4]

The draft text of the Horizontal Guidelines continues to mention in paragraph 482 that:

> "*In order to ensure effective access to the standard, the IPR policy would need to require participants wishing to have their IPR included in the standard to provide an irrevocable commitment in writing to offer to license their essential IPR <u>to all third</u>*

[2] See https://caselaw.4ipcouncil.com/german-court-decisions/lg-mannheim/nokia-v-daimler.
[3] See https://caselaw.4ipcouncil.com/german-court-decisions/lg-mannheim/nokia-v-daimler.
[4] See https://caselaw.4ipcouncil.com/german-court-decisions/lg-munich-district-court/sharp-v-daimler.

parties on fair, reasonable and non-discriminatory terms ('FRAND commitment')278." [our underline]

A footnote '278' has also been added to the text referring to paragraph 53 of the CJEU decision in *Huawei Technologies Co. Ltd. v ZTE Corp. and ZTE Deutschland GmbH* (C-170/13, EU:C:2015:477), and to the Commission Decision in *Case AT.39985 – Motorola*, that predates the aforementioned CJEU decision.

However, with the Landgericht of Munich in the aforementioned *Sharp to Daimler* case, we do not believe that the text referenced in the footnote 278 provides support for maintaining the text "*to all third parties*" in paragraph 482 of the Draft Horizontal Guidelines.

Indeed, the Landgericht of Munich correctly states that whilst the CJEU pointed out that the FRAND undertaking creates 'legitimate expectations' on the part of third parties to be licensed by the patent holder, this did not create an obligation to license *all* suppliers of an end-device manufacturer. Access to the market does not necessarily require a licence, but just a 'possibility of legal use', which can be, for instance, given through a licence granted at the last level of the value chain, from which suppliers can draw 'have-made-rights'.[5]

A similar position has recently been affirmed by a United States Court of Appeals.[6] In addition, a strict application of the text of paragraph 482 Draft Horizontal Guidelines is not possible as a patent can only be licensed once in the value chain because of the principle of patent exhaustion. Patent exhaustion laws prevent or limit licensing the same patent twice or more for a particular product/service/purpose at different levels of a supply chain. This is to prevent a patent holder abusing its patent rights, e.g. by doubling its royalties by licensing both the supplier and the customer. In a complex real-world supply chain, resembling more a cobweb than a simple linear line, where multiple suppliers may supply a customer and/or multiple customers are supplied by a supplier, and where the chain may continually change, patent licensing on different levels becomes all but impossible.

Given this reality, the words "*to all third parties*" in paragraph 482 of the Horizontal Guidelines remain a concern for IP Europe. The language in this paragraph is not only in contradiction with the aforementioned court decisions, it also seems at odds with the rest of the Horizontal Guidelines, which focus on ensuring access for those wanting to use standardised technology covered by essential IPR, which is also enshrined in the access-based IPR policies of SDOs such as ETSI. After all "access" does not equate or need a "licence".

Moreover, in the recent past the original paragraph 285 has been wilfully misinterpreted by certain implementers and their industry associations as imposing a compulsory "license to all" rather than an "access to all" requirement.

[5] See https://caselaw.4ipcouncil.com/german-court-decisions/lg-munich-district-court/sharp-v-daimler.

[6] See Case 20-11032 *Continental Automotive Systems Inc. v. Avanci LLC* (Court of Appeals for the 5th Cir., 28 February 2022) https://www.ca5.uscourts.gov/opinions/pub/20/20-11032-CV0.pdf. See also Eileen McDermott, Fifth Circuit Says Auto Parts Suppliers Have No Article III Standing to Bring Antitrust Claims Against SEP Holders (IP Watchdog, 2 March 2022) ("The decision is important because it clarifies that [Internet of things] IoT suppliers have no standing to bring so-called 'license to all' claims against SEP holders who license at the end device level (OEM level)") https://www.ipwatchdog.com/2022/03/02/fifth-circuit-says-auto-parts-suppliers-no-article-iii-standing-bring-antitrust-claims-sep-holders/id=147098/.

Deleting the reference to "*all third parties*" in paragraph 482 of the current Horizontal Guidelines would eradicate the potential internal inconsistency in the Horizontal Guidelines; remove a perceived issue which is complex or difficult to interpret; reflect the widespread industry practice to license at the end-user device level in a growing number of sectors (as recently recognised by the courts in Europe and in the U.S.).

Finally, given the wide variety of standardisation activities and corresponding SDOs (as highlighted above), it would be detrimental for the Horizontal Guidelines to be interpreted in such a manner that they would prefer or, even worse, require a particular licensing level. The Draft Horizontal Guidelines indeed recognise that SDOs can adopt different IPR Policies (cf. paragraph 476).

IP Europe would therefore strongly recommend adapting the text of paragraph 482 by deleting "*to all third parties*". Similar considerations apply to the additional "*all*" that was inserted in paragraph 491, i.e. the "*all*" inserted before "*members*".

Collective Royalty Cap Setting

The Draft Horizontal Guidelines have been amended in several instances to suggest that the collective setting of a royalty cap by participants in standards development would not raise competition concerns. The Draft Horizontal Guidelines gives the collective determination of a royalty cap and/or the setting of a royalty cap by an SDO, the same treatment currently afforded to unilateral *ex ante* disclosure of most restrictive licensing terms. This is incorrect as a matter of settled competition law and IP Europe respectfully recommends that the Commission does not include these revisions.

It has long been recognised that the unilateral announcement of most restrictive license terms and the collective determination of a royalty cap are not the same: the former is unilateral conduct not subject to Article 101 TFEU[7], while the latter can constitute anti-competitive coordinated price setting. While unilateral *ex ante* disclosure could, in theory, improve price competition, the collective setting of a royalty cap does not offer this potential efficiency. Rather, it could impede price competition between technologies.

The Draft Horizontal Guidelines properly recognise that joint fixing of prices for IPR can constitute a restriction of competition by object. Paragraph 473 retains the statement from the existing Horizontal Guidelines that "*any agreements to … jointly fix prices … of substitute IPR or technology will constitute restrictions of competition by object*." However, the proposed amendments to the Draft Horizontal Guidelines contradict this principle. Specifically, amended footnote 273 states that "*this paragraph should not prevent ex ante disclosures of … a maximum accumulated royalty rate by all IPR holders.*" This creates logical inconsistency: in order for "*all IPR holders*" to announce a "*maximum … royalty,*" they must by necessity agree to jointly set the royalty.[8] To the extent that there is a way to jointly announce licensing terms without restricting competition by object, such as the techniques

[7] We note, however, the Commission's position in the Liner Shipping cases, where it was held that merely making price announcements can be construed as an invitation to collude - or "price signaling" – which can lead to illegal price coordination even without direct contact between competitors. See Case AT.39850 – Container Shipping.

[8] Revised footnote 298 further repeats this logical error by stating that "*any … joint ex ante disclosure of most restrictive licensing terms should not serve as a cover to jointly fix prices … of substitute IPR/technologies which is a restriction of competition by object.*" The joint determination of a royalty necessarily involves joint price fixing.

employed in the development of patent pools, significant procedural safeguards are necessary to address the competition concerns.

In addition, the Draft Horizontal Guidelines suggest that the collective setting of a royalty cap should normally not raise concerns under an effects-based analysis. Specifically, paragraph 500 in the revised Draft Horizontal Guidelines has been amended to suggest that, not only should the collective setting of a "*maximum accumulated royalty rate by all IPR holders*" be subject to an effects-based assessment, but that, under such an assessment, such collective royalty cap setting "*will not, in principle, restrict competition within the meaning of Article 101(1).*" As noted in more detail below, both DG Competition and other antitrust authorities / agencies have given significant prior analysis to this issue and have tended to find that the analysis of such provisions was very fact specific and not amenable to a presumption of legality. Accordingly, IP Europe is of the view that the Draft Horizontal Guidelines should not suggest that such conduct is presumptively pro-competitive.

The United States Department of Justice and Federal Trade Commission issued an analysis of these issues in their 2007 report on *Antitrust Enforcement and Intellectual Property Rights*.[9] In that report, the agencies drew a distinction between collective rate setting and "*an IP holder's voluntary and unilateral disclosure of its licensing terms,*" which the agencies determined "*is not a collective act subject to review.*"[10] The agencies expressed that "*summary condemnation would be justified if IP holders were to reach naked agreements on the licensing terms they will propose to an SSO that permits multilateral licensing negotiation.*"[11] In addition, the agencies noted that joint licensing discussions could provide an avenue for the exercise of "*group buying power,*" and noted concerns that "*joint ex ante licensing bargaining could, in theory, reduce incentives for innovation.*"[12] Even under an effects-based analysis, when – among other things - "*potential licensees refuse to license that particular patented technology except on agreed upon licensing terms,*" the agencies found the possibility that "*the ex ante negotiation among potential licensees does not preserve competition among technologies that existed during the development of the standard but may instead simply eliminate competition among the potential licensees for the patented technology.*"[13]

The views of the U.S. agencies are consistent with the opinion that DG Competition previously offered to ETSI.[14] In its letter DG Competition noted that *ex ante* price negotiation based upon unilateral royalty disclosure had the potential to promote "*competition on the basis of both technology and price,*" but that, "*whilst we appreciate the desire on the part of licensees for certainty in the royalties that they will have to pay,*" the collective setting of a royalty cap "*risks negating the possible benefits of [the aforementioned] 'pure' ex ante regime*." The letter observed that, "*whereas a 'pure' ex ante regime has the potential to bring the price down to a competitive level through competition on the basis of price … a collective ex ante royalty cap regime … does not appear to allow for any such price competition.*" Rather, the letter noted that, "*indeed, it would appear to precisely preclude any such price competition*

[9] U.S. DEPT. JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION (2007).
[10] *Id*. at 54.
[11] *Id*. at 51.
[12] *Id*. at 52-53.
[13] *Id*. at 53.
[14] *Letter from the EC Competition DG on ETSI IPR Group Discussions*, ETSI GA/IPRR05(06)12 (22 June 2006). For further discussion see IP Europe's response to the targeted questionnaire on Standardisation Agreements.

from occurring, since the price of each essential patent is fixed in advance …". Thus, under the prior guidance that DG Competition offered to ETSI, it found that the collective setting of a royalty cap actually hinders price competition between technologies.

Finally, footnote 297 in the Draft Horizontal Guidelines is inconsistent with other sections of the Draft Horizontal Guidelines. The footnote states that "*standard development organisations could take an active role in disclosing total maximum stack of royalty for the standard*." This conflicts with the guidance in amended footnote 283, which correctly observes that "*standard development organisations are not involved in the licensing negotiations or resultant agreements.*" In addition, a total royalty stack would require a 'top-down'[15] approach to determining royalties. However, footnote 287 has been amended to make clear that "*the methods described here are not exclusive and other methods reflecting the same spirit of the described methods can be used to determine FRAND rates.*" Yet, if the participants in a standard setting were to jointly set the maximum royalties for their standard, it would seem to be impossible to use any approach other than a top-down valuation.

For these reasons, IP Europe respectfully suggests that the reference to collective setting of a royalty cap be removed from the revised Draft Horizontal Guidelines, and that the original text be retained/reinstated.

Vertical Agreements and Unilateral Conduct Outside the Scope of the Horizontal Guidelines

As the Explanatory Note[16] indicates: "*The Horizontal Guidelines **provide guidance on** how to interpret and apply the HBERs and **how to self-assess compliance with Article 101(1) and Article 101(3)** of the Treaty for R&D and specialisation but also for other **types of horizontal cooperation agreements** that the HBERs do not exempt*", including "*purchasing, commercialisation, standardisation and standard terms agreements*". As such, they are intended to "*promote competition and offer legal certainty to companies in the conception and implementation of their **horizontal cooperation agreements**.*"[17]

In these circumstances, and consistent with the stated objectives of the Draft Horizontal Guidelines[18], which "*aim to provide legal certainty by assisting undertakings in the assessment of their horizontal cooperation agreements under the Union competition rules while ensuring an effective protection of competition*", IP Europe respectfully cautions the Commission to take care to ensure that the conduct described in the Draft Horizontal Guidelines is properly within their scope.

In this regard, the Draft Horizontal Guidelines are rightly focused on the application of Article 101 and specifically the potential distortion of competition by agreements between undertakings in horizontal relationships. As recent amendments clarify, however, standardisation frequently involves parties in vertical relationships, which are not properly within the scope of the Horizontal Guidelines. Further, the revised Draft Horizontal Guidelines increased reference to unilateral conduct and to potential abuse(s) of a dominant market position, which concern the interpretation and potential application of Article 102. Therefore, IP Europe requests that the Draft Horizontal Guidelines more clearly delineate the

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[15] See paragraph 487 of the Draft Guidelines.

[16] See https://ec.europa.eu/competition-policy/document/download/9cc624ba-9afc-4685-88ef-a9b4e1da12cf_en, at paragraph 3, emphasis added.

[17] *Id*. at paragraph 5, emphasis added.

[18] Draft Horizontal Guidelines, paragraph 1.

discussion of conduct that is within its scope from the discussion of conduct that falls outside its scope – including standardisation agreements involving parties in a vertical relationship.

The Draft Horizontal Guidelines acknowledge the fact that many participants in standardisation are not rivals. Paragraph 469 retains the observation in the Draft Horizontal Guidelines that participants in standardisation can be both "*upstream-only undertakings*" and "*downstream-only undertakings.*" Recognizing this, paragraph 466 is now amended to state that "*participants in standardisation are not necessarily competitors.*" IP Europe supports this amendment, which in many ways encapsulates the observation in paragraph 469. The text recognises the fact that upstream and downstream undertakings are not horizontal competitors. Rather, their relationship is vertical.

This observation begs the question, however, as to whether the competition concerns articulated in the Draft Horizontal Guidelines apply in all circumstances of standardisation. As paragraph 466 notes, *"[s]tandard development can, however, in specific circumstances where competitors are involved, give rise to restrictive effects on competition.*" When competitors are not involved – but rather the participants are in a vertical relationship – it would follow that the potential harm to competition would not occur.

Further, the revised Draft Horizontal Guidelines appear to encompass conduct that would properly fall to be considered under Article 102 TFEU as a potential abuse of dominance. Paragraph 470, for example, suggests that so-called patent "hold up" would be an abuse of dominance. Footnote 270 further states that "*high royalty fees can only be qualified as excessive if the conditions for an abuse of dominant position … are fulfilled.*" The new text in paragraph 487, which addresses methods for patent valuation, indicate that: "*These Guidelines do not seek to provide an exhaustive list of appropriate methods to assess whether the royalty fees are excessive or discriminatory under Article 102.*" While IP Europe agrees that the Commission should not be seeking to provide an exhaustive list of potential valuation methods, we question whether it is appropriate to address this issue at all in the Horizontal Guidelines as this might erroneously suggest that their purpose is to provide guidance on the analysis and potential application of Article 102. Rather than providing clarity and legal certainty to businesses, the revised Draft Horizontal Guidelines risk causing confusion.

In any event, the addition of reference to Article 102 in paragraph 487 (and elsewhere) in the revised Horizontal Guidelines is potentially misleading in terms of dominance/the existence of market power. As the Draft Horizontal Guidelines observe in paragraph 471, "*there is no presumption that holding or exercising IPR essential to a standard equates to the possession or exercise of market power*." Rather, "*the question of market power can only be assessed on a case by case basis*." In support of this proposition, the revised Draft Horizontal Guidelines cite the decision in *Case AT.39985 - Motorola*. As the cited section shows, the Commission undertook an extensive analysis of whether *Motorola* had market power. In addition to examining the extent to which industry was locked in to the standard, the Commission also examined whether the SEP implementer, Apple, had countervailing buyer power.[19]

In footnotes 278 and 282, the revised Draft Horizontal Guidelines make reference to the ruling of the Court of Justice in *Huawei v. ZTE* and the Commission's *Motorola* decision. Both of those cases involved a party seeking recourse to national courts for an order prohibiting patent infringement. However, the Horizontal Guidelines do not address such conduct nor

[19] Commission Decision in Case AT.39985 - *Motorola - Enforcement of GPRS standard essential patents*, recitals 221-270.

should they, as this is unilateral conduct which would properly fall to be considered under Article 102. As such, these references should be removed.

In the light of the above, IP Europe respectfully recommends that the Draft Horizontal Guidelines be clarified to clearly recognise that conduct involving parties in vertical relationships and unilateral conduct are outside the scope of the Horizontal Guidelines.

Licensing Negotiation Groups

According to the Explanatory Note: "*In order to continue to meet its objectives, the Chapter on standardisation agreements in the draft revised Horizontal Guidelines proposes to introduce … references to the relevant framework of assessment for licensing negotiation groups in the joint purchasing Chapter.*"[20]

To that end, paragraph 312 of the Draft Horizontal Guidelines provides that "*[j]oint purchasing arrangements **can be found** in a variety of economic sectors and involve the pooling of purchasing activities*" and, specifically, "*[g]roups of potential licensees **can also** join[t]ly negotiate licencing agreements for standard essential patents with licensors in view of incorporating that technology in their products (sometimes referred to as licensing negotiation groups).*"

At the outset, IP Europe notes that paragraph 312 appears to suggest that there are already examples of so-called licensing negotiation groups (LNGs) operating in practice. IP Europe and its members (which comprise/include the leading SEP-holders) are not aware of such examples.

Indeed, the LNG concept was introduced at a relatively late stage of the current review of the Horizontal Guidelines. They were first referenced in Section 4.2. of the SWD[21] (setting out the additional evidence gathered through other Commission initiatives) on the basis of a high-level and theoretical proposal regarding LNGs (Proposal 75) in the SEPs Expert Group report,[22] which highlighted a number of competition concerns (discussed below) and the need for scrutiny from competition authorities. As the SWD observed, according to some members of the SEPs Expert Group, "*transaction costs could be further reduced **if** implementers were allowed to form groups to jointly negotiate licenses on behalf of their group members*".

In these circumstances, the inclusion of LNGs in the Draft Horizontal Guidelines is at the least premature, in particular where there is no practical experience of LNGs and where the Draft Horizontal Guidelines do not provide an "Example" of an LNG in the joint purchasing Chapter.[23] On this basis, IP Europe considers that references to LNGs and the relevant framework for the assessment of LNGs should be removed from the joint purchasing Chapter.

Additional concerns regarding the inclusion and assessment of LNGs in the joint purchasing Chapter of the Draft Horizontal Guidelines are set out below.

[20] See https://ec.europa.eu/competition-policy/document/download/9cc624ba-9afc-4685-88ef-a9b4e1da12cf_en, at paragraph 19.

[21] See the Staff Working Document and its annexes summarising the results of the evaluation of the HBERs and Horizontal Guidelines published on 6 May 2021.

[22] See Report from the Group of Experts on Licensing and Valuation of Standard Essential Patents 'SEPs Expert Group'.

[23] In fact, there is no guidance, or even indication, in the Draft Horizontal Guidelines about how it is envisaged LNGs could/would operate in practice and what they would entail and certainly no discussion of any "*appropriate mechanism and controls*" as raised by the SEPs Expert Group.

As regards the relevant framework to assess LNGs, the Draft Horizontal Guidelines adopt the approach set out in the Expert Report by Richard Whish and David Bailey[24] – i.e. that an effects-based analysis "*applies to all types of joint purchasing arrangements in all sectors of the economy*" and that "*the joint negotiation of the terms of licences of standard essential patents by a group of potential licenses should be assessed on the basis of the likely effects on competition of such a practice*" and that "*such joint negotiations are not suitable for allocation to the object box.*"

In this context, it appears that Whish and Bailey focused on feedback provided to the Commission in the evaluation phase and impact assessment phase of the Horizontal Guidelines review rather than the more detailed and specific feedback provided to the Commission in response to the recent public consultation (which closed for comment on 5 October 2021) and the targeted questionnaire on standardisation agreements.

In any event, we note that while Whish and Bailey considered the question of whether a collective boycott by purchasers might amount to a restriction of competition by object (and pre-existing case-law) in the context of sustainability agreements, they did not undertake an equivalent exercise as regards FRAND licensing of SEPs notwithstanding the competition concerns raised by LNGs, notably those identified by the SEPs Expert Group[25], academics and industry commentators[26]) that LNGs would: (1) offer additional hold-out opportunities for implementers (coordinated hold-out/collective boycott) to delay or avoid the conclusion of licence agreements; (2) effectively operate as a buyers' cartel, which would depress SEP royalties (below FRAND levels); and (3) provide the means and opportunity for implementers of standardised technology to engage in anti-competitive information exchange and/or collusion.

In view of (1) the growing body of case law from courts across Europe highlighting the variety of hold-out strategies adopted by certain implementers of standardised technologies identified in IP Europe's previous submissions to the Commission in the context of the review of the Horizontal Guidelines;[27] (2) examples of companies, including in the IoT space, colluding to avoid taking licences to SEPs on FRAND terms;[28] and (3) the welcome (and overdue) express recognition of hold-out in paragraph 470 of the Draft Horizontal Guidelines, we would suggest that, applying the rationale of the Administrative Court in the *Cityhook* case cited by Whish and Bailey (and the observations of the Court of Justice and Advocates General set out in paragraph 2.38 of the Expert report), experience has demonstrated that the presumption of an infringement by object is justified.

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[24] See Expert report on *Horizontal Guidelines on purchasing agreements: Delineation between by object and by effect restrictions* by Richard Whish and David Bailey.

[25] See Report from the Group of Experts on Licensing and Valuation of Standard Essential Patents 'SEPs Expert Group'.

[26] See, for example, https://www.4ipcouncil.com/research/licensing-negotiation-groups-what-why-how; https://www.4ipcouncil.com/research/licensing-negotiation-groups-seps-collusive-technology-buyers-arrangements-pitfalls-and-reasonable-alternatives; https://www.4ipcouncil.com/research/economic-case-against-licensing-negotiation-groups-internet-things; SEP Licensing Negotiation Groups -- Part I; SEP Licensing Negotiation Groups -- Part II; SEP Licensing Negotiation Groups -- Part III; FOSS Patents: EU competition chief's tough talk on cartels doesn't bode well for automotive SEP licensing negotiation groups; and 'Why proposed IoT licensing negotiation groups are an antitrust non-starter', Igor Nikolic, at https://lnkd.in/gNbRcHy7.

[27] See, in particular, our submission on the Inception Impact Assessment and our responses to the public consultation and targeted questionnaire. See also See https://www.ipeurope.org/position-papers/unwilling-sep-licensees-hold-out-strategies/. See also https://www.ipeurope.org/blog/examples-of-hold-out-strategies/.

[28] See https://www.ipeurope.org/blog/is-the-smart-meter-industry-engaged-in-coordinated-hold-out/. For a further example, see Cars or Car-tels? - KIDON IP.

Equally, while paragraph 316 of the Draft Horizontal Guidelines rightly observes that joint purchasing arrangements "*normally do not amount to a restriction of competition by object if they truly concern joint purchasing*" and can be "*distinguished from buyer cartels*", the only proposal for forming an LNG of which IP Europe is aware[29] appeared to be "*aimed at, (a) coordinating those purchasers' individual competitive behaviour on the market or influencing the relevant parameters of competition through practices such as, but not limited to, the fixing or coordination of purchase prices or parts thereof (including agreements fixing wages or not to pay a price for a product) or other trading conditions, the allocation of purchase quotas, the sharing of markets and suppliers, and (b) influencing those purchasers' individual negotiations with or individual purchases from suppliers, for example through coordination on the purchasers' price negotiation strategies or exchanges on the status of such negotiations with suppliers*" as identified in paragraph 316.

In these circumstances, IP Europe would respectfully request that the Commission and/or its Experts reconsider/re-visit the question of the appropriate framework for the competitive assessment of LNGs, and specifically the question of whether an effects analysis is really more appropriate than allocating the LNGs to the 'object box', to take account of all of the evidence provided on this issue throughout the entire review process.

As regards an effects-based analysis of LNGs, according to paragraph 323 of the Draft Horizontal Guidelines, joint purchasing arrangements "*must be analysed in their* ***legal and economic context*** *with regard to their actual and likely effects on competition*", emphasis added, and that the "a*nalysis of the restrictive effects on competition generated by a joint purchasing arrangement must cover the negative effects on … the purchasing market or markets*".

When considering the legal and economic context for the analysis of LNGs, it should be noted that, in stark contrast to the joint purchasing of goods or services, in the context of SEP-licensing, the nature of open standards means that implementers have access to, use, and profit from standardised technology without first having to take a licence.[30]

In addition, as IP Europe has explained previously, some implementers engage in 'hold-out' strategies and wilfully infringe SEPs on the basis that they will only ever be required to pay FRAND royalties. These factors are key to understanding the market dynamics and to the assessment of the market power of implementers, both individually and collectively as potential parties to a joint purchasing arrangement.[31] In this regard, the significant market/buyer power of implementers is such that a joint purchasing arrangement – i.e. an LNG is likely to give rise to considerable restrictive effects on competition within the meaning of Article 101(1). The 'FRAND context' heightens, not mitigates, the risk. LNGs would be able

[29] See presentation of Uwe Wiesner for the DG GROW Webinar on 20 April 2021, available at: Webinar SEP: 20 April, presentations and documents at page 61 *et seq*.

[30] This issue is not addressed or even considered in the 'Expert report on Horizontal Guidelines on purchasing agreements: Delineation between by object and by effect restrictions' by Richard Whish and David Bailey – see kd0722013enn_purchasing_agreements.pdf (europa.eu).

[31] Currently paragraph 336 of the Draft Horizontal Guidelines merely indicates that "*the analysis of whether the parties to a joint purchasing arrangement have buying power, the number and intensity of links (for example, other purchasing agreements) between competitors in the purchasing market are relevant*". This does not reflect the specific factors/features that are relevant to the assessment of the buying power of a group of potential licensees of SEPs.

to exercise collective monopsony power over SEP-holders to force prices below a competitive level.

As regards market power, paragraph 329 of the Draft Horizontal Guidelines observes that: "*There is **no absolute threshold** above which it can be presumed that the parties to a joint purchasing arrangement have market power so that the joint purchasing arrangement is likely to give rise to restrictive effects on competition within the meaning of Article 101(1). However, **in most cases** it is unlikely that market power exists if the parties to the joint purchasing arrangement have a combined market share not exceeding 15% on the purchasing market or markets as well as a combined market share not exceeding 15% on the selling market or markets.*"

However, the negotiation of the terms of licences of standard essential patents by a group of potential licenses is not most cases. The 'ND' – i.e. 'non-discriminatory' aspect of the FRAND-commitment means that any terms negotiated with the LNG would likely have far broader implications and render the 15% market share threshold meaningless in practice. For example, it could (and most likely would) be argued that any rate negotiated by the LNG should be applicable to or indicative for many other market participants, regardless of the circumstances and market power that may be represented by the LNG vis-á-vis individual entities. As such, even if the participants in an LNG in theory represent less than 15% of the (properly defined) relevant market(s), in practice the terms negotiated with the LNG could have major impact. In these circumstances, IP Europe respectfully requests the Commission, at a minimum, to revise the Draft Horizontal Guidelines to make clear that the 15% market share 'safe harbour' does not apply to LNGs.

When considering the potential for a "*collusive outcome*", paragraph 343 of the Draft Horizontal Guidelines notes that: "*When negotiating terms and conditions with suppliers, a joint purchasing arrangement may **threaten suppliers to abandon negotiations or to stop purchasing temporarily unless they are offered better terms or lower prices**. **Such threats are typically part of a bargaining process** and may involve **collective action by purchasers when a joint purchasing arrangement conducts the negotiations**. Strong suppliers may use similar threats to stop negotiating or supplying products in their bargaining with purchasers. **Such threats do not usually amount to a restriction of competition by object** and any negative effects arising from such collective threats will not be assessed separately but in the light of the overall effects of the joint purchasing arrangement.*"

In this context, the Draft Horizontal Guidelines refer to the example of temporary stops by the members of a retail alliance in ordering certain products and observes that "[*s]uch temporary stops may result in the products selected by the individual members of the alliance being unavailable on the retailers' shelves for a limited period of time, namely until the retail alliance and the supplier have agreed on the terms and conditions of future supplies.*" Again, this underlines the stark contrast between the joint purchasing of goods or services on the one hand and the joint negotiation of SEP licenses on the other hand. As noted above, that implementers have access to, use, and profit from standardised technology without first having to take a licence and there is significant evidence of bad faith implementers engaging in a variety of hold-out strategies, including co-ordinated hold-out, to delay or avoid taking a licence on FRAND terms.

Accordingly, rather than being part of the "*bargaining process*", such threats in the context of an LNG would constitute/perpetuate hold-out – i.e. 'efficient infringement', where unlicensed implementers simply appropriate technology without compensation for the use of such technology that requires substantial R&D investments by innovators years in advance of a standard being adopted ('free riding'). Depriving innovators who are responsible for developing fundamental cutting-edge technologies (that are standardised and made available for integration into millions of connected products and services) of fair and reasonable compensation undermines their ability and incentives to invest in critical (and risky[32]) R&D for future technologies and to participate in open, collaborative, and consensus-driven standards development. This threatens the future of standardisation/standards development as well as European leadership in 5G and 6G development (and beyond).

While paragraph 332 of the Draft Horizontal Guidelines acknowledges the risk that a joint purchasing arrangement "*could discourage investments or innovations benefitting consumers*" it suggests that these risks "*may be larger for large purchasers that jointly account for a large proportion of purchases – in particular when dealing with small suppliers*". This does not (adequately) reflect the market dynamics of SEP licensing and, in particular, the suggestion that "*[r]estrictive effects on competition are less likely to occur if suppliers have a significant degree of countervailing seller power (which does not necessarily amount to dominance) on the purchasing market or markets*" is incorrect.

In any event, it is unclear how the "*bargaining process*" – i.e. threats to abandon negotiations or to stop purchasing temporarily – discussed in paragraph 332 of the Draft Horizontal Guidelines would operate within the *Huawei v ZTE* framework, which confirms that an SEP-holder may seek an injunction prohibiting the infringement of its patent or seek the recall of products for the manufacture of which that patent has been used against an unwilling licensee. In this context we also note that paragraph 470 of the Draft Horizontal Guidelines describes hold-out as conduct "*attributable solely to the user of the standard*", while this should naturally capture any 'unwillingness' by an LNG, given the significant concerns that LNGs could be used as a vehicle for coordinated hold-out, we would invite the Commission to clarify this point. One way of achieving this would be to delete the word "*solely*".

By contrast also to the conventional analysis of purchasing groups in relation to goods, it is difficult to identify efficiencies from the creation of an LNG that do not already exist and which would justify the very evident distortions of competition to which an LNG would give rise to in the standards context. The suggestion that if groups of implementers could collectively negotiate with individual or groups of SEP holders and patent pools it may lower transaction cost is theoretical. It is unclear that such efficiencies/cost-savings would be generated by LNGs in practice and it has been suggested that similar (or greater) cost savings could be achieved through patent pools.[33] In any event, for SEP-holders, any efficiencies would depend on the timely conclusion of licences and, given the hold-out risks posed by LNGs, it is unclear that such efficiencies would arise.

Finally, IP Europe understands that it has been suggested by certain stakeholders that LNGs are a necessary and/or natural counterbalance to patent pools. This demonstrates a

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[32] As paragraph 484 of the Draft Horizontal Guidelines observe, "*FRAND commitments allow IPR holders to monetise their technologies via FRAND royalties and obtain a reasonable return on their investment in R&D which by its nature is risky. This can ensure continued incentives to contribute the best available technology to the standard.*"

[33] See, for example, https://www.4ipcouncil.com/research/economic-case-against-licensing-negotiation-groups-internet-things. Equally, in its response to the public consultation, the American Bar Association indicated that it was "*skeptical that cooperation between users of standard essential technology in Collective Licensing Negotiations Groups (LNGs) would readily give rise to lower transaction cost and other efficiencies. At minimum, such initiatives require careful assessment.*" IP Europe shares this skepticism.

fundamental misunderstanding of the role and nature of pools. In particular, patent pools: (1) combine complementary technologies; (2) are optional and not exclusive; (3) provide a pro-competitive choice to direct/individual licences; (4) reduce transaction costs for licensees and SEP-holders; (5) avoid/limit the risk of so-called 'double-dipping'; and (6) in the standards context, are bound through their members to FRAND licensing commitments. This is in contrast to LNGs which conceptually pose a significant threat to competition.

In the light of the above considerations, and the significant competition concerns posed by LNGs, the inclusion of LNGs and references to the relevant framework of assessment for licensing negotiation groups in the joint purchasing Chapter of the Draft Horizontal Guidelines is misguided.

Rather than continuing to meet its objectives to "*promote competition and offer legal certainty to companies in the conception and implementation of their horizontal cooperation agreements*", the inclusion of LNGs in the Draft Horizontal Guidelines raises more questions than it provides answers.

The negotiation of FRAND licences for SEPs is not comparable with the (joint) purchasing of goods or services and, while the Draft Horizontal Guidelines reference to the need for parties to consider the relevant legal and economic circumstances, the Draft Horizontal Guidelines themselves have failed to reflect adequately, or at all, the specific features of the negotiations and the market(s) concerned. IP Europe would therefor propose that LNGs be removed from the Draft Horizontal Guidelines. Alternatively, at a minimum, the Horizontal Guidelines should be redrafted to include specific analysis of the relevant market dynamics and other factors identified in this submission.

At their current state, in seeking to fit the proverbial square peg into a round hole, the Draft Horizontal Guidelines fail to identify an appropriate framework of assessment for LNGs or consider necessary safeguards. This ill-conceived approach risks exacerbating rather than acknowledging and addressing the hold-out issue identified in paragraph 470, depriving SEP-holders of appropriate remuneration and undermining their ability and incentives to participate in risky R&D. This poses a significant threat to the delicately balanced SEP ecosystem and the future of standards development as well as European leadership and strategic autonomy.

Proposed Revisions to the Text/Language of Specific Paragraphs of the Horizontal Guidelines

In addition to the issues/areas identified above, IP Europe has identified some specific/detailed wording issues with the text/language of certain provisions of the Draft Horizontal Guidelines. These are outlined below.

<u>Paragraph 469</u>

At paragraph 469 we note an imbalance in the description of the different interest groups involved with standards development. Whilst upstream-only undertakings are said to 'maximise' their royalties, downstream-only undertakings are said only to seek to 'reduce' royalties. The correct balance would be to observe that downstream-only undertakings are incentivised to 'minimise' royalties, or even avoid them altogether.

Paragraph 470

As noted above, we welcome the addition of the last sentence in paragraph 470 of the Draft Horizontal Guidelines, recognising the phenomenon of 'hold-out'. We note however that this is said to arise where "*licensing negotiations are drawn out for reasons attributable solely to the user of the standard*"[34] (emphasis supplied). As explained above, this could be misunderstood as meaning that hold-out can only occur where delay is not in any way attributable to the licensor. That would be unrealistic since negotiation of an SEP licence can be complex and lengthy. We therefore suggest the word "*solely*" should be deleted.

Paragraphs 483 and 492

These paragraphs address disclosure requirements at SDOs; at paragraph 483 in the context of a safe harbour, and at paragraph 492 in the context of effects-based assessment.

The current safe harbour provisions include scope for the use of blanket declarations followed up by specific disclosure as the standard develops. We understand the amendments as continuing with that approach. However, with respect to the additional statement at paragraph 483 that *"Except for this case, blanket disclosure would be less likely to enable the industry to make an informed choice of technology and to ensure effective access to the market"*, it is not entirely clear to us what *"Except for this case*" means or refers to; we believe it may refer to "*reasonable endeavours to identify IPR reading on the potential standard, and to update the disclosure as the standard develops*"*,* but in any event this needs clarification. Further, blanket declarations[35] are, on the contrary, a **very useful** tool for the industry to make an informed choice of technology as they ensure access to all work contributed to the standardisation effort. We therefore believe that the changes to this paragraph 483 are misguided and thus the original text of paragraph 286 should not be modified.

At paragraph 492, in the context of effects based assessment (which will be the case for almost all SDOs, since very few require specific IPR disclosure), a sentence has been added as follows: "*Standard development agreements providing for the disclosure of information regarding characteristics and value-added of each IPR to a standard and, thereby, increasing transparency to parties involved in the development of a standard will not, in principle, restrict competition within the meaning of Article 101(1)".* Whilst this appears to be intended to encourage a particular approach it is not clear to us what that approach would be, since we do not understand what *"information regarding characteristics and value-added of each IPR"* means or refers to. This also needs clarification.

IP Europe appreciates the opportunity to provide comments on the Draft Horizontal Guidelines and remains available for any further clarification.

[34] This again raises the question of the attributability of LNGs' behaviour to users of the standardised technology.
[35] The Draft Horizontal Guidelines erroneously mention 'blanket disclosure'.