Standard Essential Patents, Patent Assertion Entities, and Injunctions*

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*These remarks do not necessarily represent the views of the Federal Trade Commission or any individual commissioner.
Introduction/Outline

• I will not be discussing “pay for delay”.
• Injunctions, patent hold-up, and SEPs
• The other Google matter
  – A very brief discussion of legal theories
  – A more detailed discussion of economic theories
• Patent assertion entities
  – Antitrust issues
  – Consumer protection issues
Injunctions and Patent Hold-Up

• Seeking an injunction (or an exclusion order) as a remedy for patent infringement likely increases negotiated royalties.

• Licensee may be willing to pay a higher royalty to avoid litigation and redesign costs.
Injunctions and Patent Hold-Up

• Injunctions and SEPs
  – It is not possible to design around SEPs and remain compliant with the standard.
  – SEPs are different from commercially essential patents.
  – Licensee may be willing to pay its entire margin to avoid an injunction.
  – Patentee appropriates both value of patented invention and value of licensee’s downstream innovation.
Injunctions and Patent Hold-Up

• Injunctions and SEPs: Short run effects
  – Potentially none
  – Prices of final goods may not change if
    • royalty payments are lump sum or
    • licensee is unable to pass through running royalties to price.
  – Looks a lot like rent-shifting without any obvious impact on final goods consumers.
Injunctions and Patent Hold-Up

• Injunctions and SEPs: Long run effects
  – Hold-up is more than rent-shifting in the long run
  – Might reduce downstream innovation
    • Products have fewer features
    • Fewer new products
  – Might reduce implementation of the standard
  – Final goods prices may be higher, variety may be lower, and consumers may find products implementing standards to be less valuable.
Injunctions and the Standard Setting

• Injunctions and FRAND
  – Seeking injunctions against willing licensees seems inconsistent with a FRAND commitment.
  – Seeking an injunction allows the patentee to exploit the market power conferred upon it when its technology becomes incorporated into a standard.
  – The patentee is able to obtain royalties that exceed the \textit{ex ante} value of the technology.
Injunctions and Standard Setting

• Standard setting is inherently collusion over technology choice
  – But technology competition *ex ante* to the adoption of the standard should result in lowest quality-adjusted cost technology.
  – Injunction threats may distort that competition.
Injunctions and Standard Setting

• Why do we care about the distortion of technology competition?
  – The exploitation of market power conferred by the standard is ancillary to the standard setting process.
  – SSO may have chosen a lower cost technology but for the deceptive FRAND commitment.
  – There may be reduced standard implementation and potentially reduced downstream innovation relative to undistorted technology competition.
Google/Motorola

• Objectionable conduct
  – Motorola sought injunctions (and exclusion orders) against RIM, Apple, and Microsoft on its SEPs relating to cellular, Wi-Fi, and video compression standards.

  – Google maintained the lawsuits after its acquisition of Motorola.
Google/Motorola

• Legal issues
  – Seeking injunctions against willing licensees of one’s SEPs violates FRAND and, consequently, violates section 5 of the FTC Act (unfair methods of competition and unfair acts or practices).
  – Proposed consent lays out what it means to be a willing licensee.
Google/Motorola

- Economic theory of harm
  - Absent a threat of injunction, negotiated royalties should approximate the additional value the patented feature contributes to the downstream product.
  
  - The threat of injunction may result in negotiated royalties which exceed the value of the patented feature.
Google/Motorola

• Injunction threat and SEPs
  – Licensee may be willing to pay entire margin in order to avoid the possibility of an injunction.
  – Higher downstream margins suggest higher negotiated royalties.
Google/Motorola

• Injunction threat and SEPs
  – Patentee is vertically integrated downstream
    • Patentee may be willing to accept a lower royalty to avoid successful defensive assertion.
    • Patentee may be less concerned about defensive assertions when its relative downstream presence is small (higher royalties).
    • Patentee may be more concerned about defensive assertions when downstream firm’s technology is more valuable (lower royalties).
Google/Motorola

• Google’s licensing conduct
  – Google’s SEP assertions related to smartphone and gaming consoles.
  – Relative sales of Google’s competitors were increasing.
  – Some evidence SEPs were asserted against high margin products.
Google/Motorola

• Effect of Google’s licensing conduct
  – Characteristics of licensees and Google’s licensing conduct are consistent with an injunction threat resulting in higher negotiated royalties.
  – Harm to Apple’s and Microsoft’s incentives to innovate and implement standards likely small given the size and resources of these firms.
  – Harm to smaller firms from Google’s conduct may have significant impact on incentives to introduce new features in their products and/or introduce new products.
PAE Activity

• Area FTC is beginning to examine
  – PAE workshop joint with DOJ last year
  – Still at understanding stage

• PAEs potentially address failure in patent markets
  – Difficult to value patents because they lack comparables
  – Value of individual patents is discounted due to portfolio effects
  – High search costs
  – Patents are a probabilistic property right
PAE Activity

• Open questions
  – Does PAE activity result in higher returns to individual and small inventors?
  – Does PAE activity reduce downstream innovation?
  – What is net effect on innovation?
PAE Activity

• Antitrust concerns
  – Patent transfers from operating companies to PAEs
    • Royalty stacking
    • Raising rivals’ costs
  – Assertions of SEPs
    • Greater hold-up concerns
    • Potential harms may not be mitigated by defensive assertions
  – Assertions of large portfolios
    • SEPs and commercially essential patents
    • Portfolio license may be necessary for freedom to operate
PAE Activity

• Consumer protection concerns
  – Deceptive assertions (i.e., nuisance suits)
    • No actual patents
    • Patents are invalid
    • Patents are expired
    • Patents are not infringed
    • Patents are exhausted
    • Patents apply to a different end use
PAE Activity

• FTC continues to study PAE activity as there are many other open questions/concerns.