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A Critical Analysis of the EC Proposal for SEP Regulation

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The proposal of the European Commission on the [Regulation of SEP's](#) (the “**Proposal**“) has elicited criticism from various sides, including patent attorneys and lawyers, law professors, the government of [the Netherlands](#) and [Finland](#), prominent UPC judges (see [here](#) and [here](#)), [the president of the EPO](#) and leading SEP holders (such as [Nokia](#) and [Qualcomm](#)). The proposal consists of two main components: the introduction of a SEP register, including essentiality checks for registered patents, and a procedure to determine FRAND conditions and aggregate royalties for use of a given standard. While it may sound only fair to be aiming for a fair, balanced, predictable and transparent licensing framework, the current draft's application may in fact very well have the opposite effect. Perhaps most controversial is how far the Commission seems willing to go in constraining the fundamental rights of patentees. Surprisingly, the recent endorsement by the [European Parliament's Committee on Legal Affairs](#) (“**JURI**“) seems to leave [key features that render the proposal controversial intact](#). This article sets out some of the more problematic aspects of the current Proposal.

Encroachment on Fundamental Rights

The primary concern about the Proposal revolves around the non-binding FRAND determination process. This process, initiated by either a SEP holder or an implementer, must be concluded within nine months (art. 39-40). Although the non-binding nature of the procedure may appear harmless enough, the problematic aspect lies in the fact that the patentee can only bring a claim in court *after* completion of the FRAND determination procedure (art. 34(1)(a)). This limitation on court actions is waived only if the responding party indicates that it does not want to participate (art. 38(3)(b)). However, an implementer lacks an incentive to expedite the FRAND determination procedure and may intentionally prolong it for the entire nine-month period, thereby securing an extended period of protection. It is argued that this delay unfairly benefits implementers, facilitating hold-out.

Courts have long acknowledged that denying a patentee access to courts, while an infringer continues to use its patented invention, harms the patentee. For example, in *Otis v. Apple* the High Court of Justice stated (para. 45): *‘To make the patentee wait for a year or more from infringement finding to FRAND trial would be almost like a compulsory licence, and that is not justified. It is not just a question of an interim position pending a further determination but a substantive loss of rights for the patentee in respect of an ageing property right.’*

The aforementioned limitation to enforce a patent could be deemed to infringe the fundamental

property rights of the SEP holder (art. 17(2) of the EU Charter) and the right of access to court (art. 47 of the EU Charter). Standing case law of the Court of Justice of the European Union (CJEU) confirms the principle that all EU acts must respect fundamental rights, which are an integral part of the general principles of law protected by the CJEU (*Internationale Handelsgesellschaft*). Only under strict conditions (see also art. 52(1) of the EU Charter) there is room to restrict these fundamental rights. The Commission justifies its proposed restrictions by citing CJEU case law (*Explanatory Memorandum*, p. 10), but the cited cases differ substantially from the restriction of access to courts as suggested in the Proposal. For instance, the case *Rosalba Alassini v Telecom Italia SpA* concerns an Italian regulation mandating non-binding dispute resolution before court action in consumer-telecommunications provider disputes. As noted by *Qualcomm* (p. 13-14), this ruling cannot be applied one-to-one to the situation here at hand. Most significantly, the maximum duration of this dispute resolution was thirty days, significantly shorter than the proposed nine-month FRAND determination procedure. Moreover, temporarily restricting court action for a past-due payment is distinct from limiting access to courts in cases involving ongoing infringement of intellectual property rights.

Furthermore, the limitation of court access does not align with the Commission's aim to provide uniform, open, and predictable outcomes for SEPs, especially when one party can unilaterally conduct the FRAND procedure without the other party's participation, leading to unreliable results. Additionally, the Proposal fails to expedite dispute resolution as the decision remains non-binding (as also explained by *Fabian Gonell*).

Moreover, the Commission has seemingly overlooked a fundamental aspect of patent rights – their core essence lies in the authority to prevent others from manufacturing, utilizing, or selling the patented invention. This is the reward granted to inventors for a) making the invention and b) sharing that invention with the general public. This is desirable behaviour that is stimulated by the patent system. If the reward is limited, so is the incentive that patent law aims to provide.

While a potential tension can exist between patent law and competition law, it is essential to recognize that '*competition and patents are not inherently in conflict*', as also asserted by the American FTC in their report (*To Promote Innovation*, p. 2). In fact, as noted by the US Court of Appeals for the Federal Circuit, patent and competition laws '*are actually complementary, as both are aimed at encouraging innovation, industry, and competition*' (*Atari Games Corp. v. Nintendo of America*). Nevertheless, according to the US Supreme Court, competition law can be invoked when patentees attempt to *overstep* the boundaries of their patent grants (*Carbice Corp. v. Patents Development Corp*). EU case law also adopts this premise, affirming that the exercise of exclusive rights linked to intellectual property is generally permissible. Only in exceptional circumstances may the enforcement of a SEP involve abusive conduct by an entity with a dominant position, which must be assessed on a case by case basis as outlined in *Huawei/TZE* (see para. 46-47). Essentially, the restrictions on the exclusive rights of the patentee as contained in the Proposal, imply that the Commission assumes that SEP owners both inherently possess and abuse dominance when initiating legal proceedings during this period. This contradicts standing case law and is contrary to essential principles of competition and intellectual property law.

Not 'FRAND'

It is also questionable whether the EUIPO should have the authority to determine exact FRAND royalty rates in the first place. Resolution of FRAND disputes by EU courts does not generally involve a judicial authority setting a certain royalty rate. In fact, most EU courts have been very cautious about setting exact royalty rates for the use of SEPs (e.g. see *Philips v. Wiko*, para. 4.177;

Sisvel v. Haier, para. 81). It seems likely that this hesitation of EU courts to set exact royalty rates indicates the complexity of the matter, raising concerns about the feasibility of assigning this responsibility to the EUIPO on a regular basis.

Furthermore, the Proposal seems to disregard the important dynamics of FRAND licensing negotiations. In the notable case of *Huawei v. ZTE*, the CJEU reaffirmed that the core of the assessment is whether a party has demonstrated its willingness to enter into a license agreement under FRAND terms. As aptly put by the High Court of Justice in *Unwired Planet v. Huawei* (para. 708): '[...] a willing licensee must be one willing to take a FRAND licence on whatever terms are in fact FRAND. Those terms might be settled by negotiation, by a court or by an arbitrator but to insist on any particular term runs the risk that that term is not FRAND. At best it could only amount to a form of contingent willingness.' The German Bundesgerichtshof holds a similar reasoning in *Sisvel v. Haier* (para. 81) by stating that (translated to English): 'Since appropriate conditions for a contractual relationship, in particular an appropriate price, are regularly not objectively determined, but only as a result of (possibly similar) negotiated market processes, the serious and purposeful participation of the undertaking willing to license in the negotiation of appropriate contractual terms is of decisive importance.'

The approach of setting FRAND royalty rates becomes even more problematic with the addition of a non-binding expert opinion on the total aggregate royalty (as outlined in art. 18), which is defined as 'the total amount of money paid or required to be paid to license all patents essential to a standard' (art. 2(10)). This procedure involves aggregating a sum and distributing it among individual SEP holders based on the size of their SEP portfolios, which is determined by dividing the number of declared SEPs within a portfolio by the total number of SEPs. Subsequently, this aggregate royalty rate can be taken into account to determine a FRAND rate under the previously mentioned FRAND determination procedure. Although this 'top-down' approach takes into account essential features, it overlooks the overall value of SEPs. Some SEPs significantly impact a standard, while others enhance interoperability or offer minor improvements. Relying solely on essentiality for aggregate royalties may be imprecise. In the *Optis v. Apple* case, the court could not find credible evidence to establish a universally applicable aggregate rate and, therefore, dismissed a single rate. The proposed "opinion" procedure is unlikely to yield different outcomes or reduce licensing disputes.

Questionable Legal Basis

Finally, it is unclear whether there is sufficient legal basis for the Commission's Proposal. The Commission bases its competence on Article 114 TFEU, which allows for the adoption of measures necessary to improve the functioning of the internal market. Utilizing this legal basis, the Commission seeks to address divergent national court approaches to SEP-related issues (*Explanatory Memorandum*, p. 4-5). Furthermore, the Commission asserts the Proposal is needed because self-regulation has not decreased the number of SEP licensing disputes and it seems likely that these conflicts will rise in the future. This is considered as undesirable, since it can cause more delays in negotiations and increase the parties' licensing costs (*Impact Assessment Report*, p. 23). By promoting more transparency and certainty the Commission seeks to address this.

Under settled case law, to which the Commission refers, although regulation under Article 114 TFEU is possible 'if the aim is to prevent the emergence of future obstacles to trade resulting from multifarious development of national laws, the emergence of such obstacles must be likely and the measure in question must be designed to prevent them' (*Germany v. Parliament and Council*, para. 38).

Whether diverse court rulings, if these indeed exist, necessarily constitute ‘future trade obstacles likely to emerge’ (see for a more extensive analysis what [Qualcomm has submitted in Consultation](#), p. 4-6) is debatable. The Commission itself acknowledges the prior absence of specific EU or national rules on SEPs and the fact that previous court rulings have not necessarily shown different results, despite perceived differences in approaches. The only observation the Commission shares on this subject is that *‘it is difficult for competent courts in the Member States to handle SEP-related cases and make detailed and consistent FRAND determinations’*.

The available evidence, moreover, does not indicate the existence of market failure, due to the burdens of SEP related litigation, that would justify intrusive market intervention (see also what [ICLE-affiliated scholars have explained in their comments](#), p. 5). In fact, the Commission’s own empirical evidence points to no systemic negative effects on SEP owners and implementers ([Empirical Assessment of Potential Challenges in SEP Licensing](#), p. 185). Besides that, there is a low incidence of SEP litigation, *‘with no discernible overall increasing or decreasing trend’*. ([Empirical Assessment of Potential Challenges in SEP Licensing](#), p. 108).

Furthermore, even if the Commission’s reasoning would be followed that potentially diverging court rulings constitute obstacles to trade within the internal market, it is doubtful whether the proposed measures will effectively take away such obstacles. Instead, they could exacerbate the situation by undermining the harmonization efforts of the UPC, which has been in operation as of 1 June 2023, and transferring authority to a non-judicial body within the EUIPO. Since all proceedings within this non-judicial entity are non-binding, the proposed essentiality checks, conciliation, and aggregate royalty procedures would moreover still require a court to make a final decision when parties fail to reach an agreement.

Lastly, it is questionable whether the Proposal satisfies the requirements of proportionality and subsidiarity, which are key pillars limiting the Commission’s competence to introduce legislation. After all, there is no evidence that the EUIPO is more competent than national courts or the UPC in determining FRAND conditions, and costs for SEP holders may increase unnecessarily for uncertain transparency gains. The president of the EPO, who has apparently not been consulted on the Proposal, voiced [similar concerns](#) to the European Parliament.

Conclusion

In short, the Proposal faces extensive criticism from various sides primarily for infringing on fundamental rights by restricting a patentee’s court access during the FRAND determination procedure. The suggested method for determining FRAND royalty rates furthermore not only deviates from the well-established and focused FRAND assessments carried out by the national courts, but also introduces an oversimplified top-down approach that risks undermining the true value of SEPs. Besides that, the legal foundation of the Commission’s competence under Article 114 TFEU is questionable, raising serious doubts about the necessity and effectiveness of the proposed measures.

Given the Proposal’s significant implications, the Commission would be well advised to reconsider the Proposal from a legal standpoint, giving due consideration to fundamental principles of intellectual property and competition law, as well as taking into account the potential adverse economic consequences.

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