



Are restrictions on patent law necessary and meaningful?

English Summary developed by 4iP Council

of the article by Prof. Dr. Klaus-J. Melullis, former judge at the Federal Court of Justice, Germany, "Zu Notwendigkeit und Sinnhaftigkeit von Beschränkungen des Patentrechts, Mitt. 2016, 433 ff."



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Are restrictions to patent enforcement necessary?

Executive Summary:

The public policy discussions on the value and importance of intellectual property rights (IPR) are increasing and in parallel policymakers are considering limiting the owner's rights to enforce their IPR. In Europe, the discussion started on copyrights, to allow users to have easier and free access to protected content on the Internet, to the disadvantage of the creator. Driven by patents, which are essential for a technical standard (SEP), IPRs have become more and more the focus of the discussion. And today's discussion on potential abuse of IPR is going beyond those SEP. The enforcement of any IPR by its owner is considered by some as abuse of the patent system, which is not in line with European Competition Law.

This article critically analyses the arguments put forward that the patent and its enforcement limit competition, differentiating between SEP and non-SEP. It further analyses the potential need for regulatory intervention in the litigation system and the expected consequences of such potential intervention on competition, investments, research and development activities and innovation.

The existing patent and litigation system in both Germany and Europe protects fair competition, fosters investment in research and development, and encourages innovation. It allows the inventor to protect his invention against free-riding. Potential abuse of the patent system happens sporadically and is controlled by the existing instruments of the German and European legislation. Courts have at their disposal sufficient instruments to avoid potential abuse of the patent system on the national and European level.

I. Underlying Issues

1.1 Standard Essential Patents

The more successful technologies are often global. At the same time, technology lifecycles are getting shorter and shorter and more complex, which requires co-creation, involving several partners. Consumers are benefitting from this situation, as global competition makes these complex technologies affordable and available. But co-creation and global use requires that standards are developed in order to make components and services compatible, and at the same time to avoid de facto monopolistic standards.

Patents protect most of the technologies included in 'hardware' technology standards. This creates a natural tension between the public interests of protecting individual rights and the public interest of getting access to the technologies at affordable prices, enabling free trade. To address this tension various instruments limiting the rights of patent holders, have been developed, and improved by national and European jurisdictions over the last decades. The FRAND (Fair Reasonable And Non Discriminatory terms) commitment obliges the patent holder to give direct or indirect access to the standard to everyone, including competitors. Because of the FRAND commitment, the patent holder may be limited in his rights to seek an injunction, if he makes an unreasonable offer under FRAND conditions.

Potential abuse might occur when patent holder refuses to license under FRAND conditions, but he existing instruments have been proven to avoid such potential abuse as shown by a variety of court decisions over the last years.

1.2 Non Standard Essential Patents

The rights of the patent holder of SEP are limited due to the exceptional circumstances created by the standardisation context. For non-SEP these types of exceptional circumstances do not apply. Nevertheless, the public discussion is driven by the request to limit the rights of a patent holder in general to a “Reasonable” use (and enforcement) of his rights, and to limit his rights to injunctive relief in particular.

This discussion is primarily caused by the fear that business models that aggregate patents and seek to enforce these rights abuse the patent system. Several aspects are systematically ignored in this discussion:

- (1) The function of the patent system is to enable the inventor to obtain a return on his investment and avoid free-riding of competitors, who did not invest in R&D and patent protection. The return should not only be the money invested in R&D and the patent protection, but also a profit margin that compensates the risk the inventor took. The system is designed to include risk for R&D failure, time to market and market failure.
- (2) In general, the aggregator compensates the inventor for his previous investments. In exchange the aggregator receives all rights resulting from the patent. This exchange may be beneficial in cases where the inventor (contrary to the aggregator) has neither the financial resources nor the expertise to exploit his rights, including enforcement against a more powerful infringer than himself.

In addition, whether the simple fear that aggregators might try to abuse their patent enforcement rights can justify the limitation of the rights for all patent holders should be seriously questioned. If ‘abusive’ behaviour is to be sanctioned or limited, abuse needs to be objectively defined. Otherwise these limitations will open opportunities for free-riders to abuse the system themselves, which would seriously slow down R&D activities and harm innovation.

II. Is there a need for intervention on the legal framework?

1.1 Do patents limit free and fair competition?

The discussion around SEP enforcement shows the debate is not driven by evidence of problems with the patent system or the underlying legal system, but rather the potential ‘abusive use’ of these systems. The primary argument is that the potential ‘abusive use’ of enforcement rights by patent aggregators or non-practicing entities (NPE) may unjustly increase prices by increasing costs to manufacturing entities. As patent enforcement occurs in all technical areas, one would expect to see such a negative impact on prices applying to all products based on patent protected technologies, not only to products based on SEP protected technologies, like i.e. mobile communication technologies. However, consumer prices show exactly the opposite: Even though the mobile communication sector is driven by intensive use of (essential and non-essential) patents and their enforcement, strong competition and short life cycles keep prices low and affordable. Therefore, the fear that patent holders might use their rights to gain extraordinary high profits cannot be proven for this sector.

Any limitation on enforceability of patents may put into question the patent system as a whole and may impact its very function as an innovation protector and enabler that fosters general social welfare. It seems to be important not to compare the prices of products with or without patent protection, but to question what the world would look like without patent effective protection. It can be assumed that:

- a) Less innovative products would be available as most of manufacturers would not be willing to invest in research and development without the fair chance to recoup the investment and gain market-conformed profit;
- b) Innovative products would only be offered by companies having a natural monopoly due to sheer size and financial resources, which would create a monopoly situation (and pricing) as such.

In case the patent holder tries to withhold a product from the market using the patent system, the German legal system foresees, in exceptional circumstances where that product is an essential facility, the possibility for compulsory licenses for non-standardised technologies. For SEP the FRAND commitment offers direct and indirect access to the technology.

1.2 Should enforcement be conditioned to certain characteristics?

a. Re-Investment in R&D

One of the major arguments used in the public policy discussion on potential abuse of patents by patent aggregators refers to the fact that those entities neither manufacture based on patent protected technologies nor invest in research and development activities. This argument fundamentally misunderstands the patent system and its function, i.e. the protection of innovation.

Even though the argument that royalties are re-invested into new R&D seems to be compelling as a justification to fully use the enforcement rights of patents, the patent system does not require this at all. The rationale is that the invention's protection and the inventor's scheme of the patent system is following an ex-post approach, meaning the inventor should be rewarded for the effort and investment he already did in the past. Any condition to future expenses would require the inventor always to be active and would disable him to retire at any time.

Also the patent system does not require that the reward assigned to the inventor is limited to his costs only. Such limitation probably would discourage potential new inventors to disclose their work, especially the most risky R&D, as it will not pay off. The result would be shrinking innovation activities to the disadvantage of the society.

There is no logical reason why these considerations should not apply for patent aggregators. Selling the patent to an aggregator is simply an extension of the value creation chain of the invention. The aggregator compensates the inventor when acquiring patents. In exchange for their investment they should obtain the same rights as the original investor. The same argument applies, if the aggregator buys patents from insolvency, as he satisfies the inventor's creditor.

b. Patent Quality

Another argument supporting the view that the patent system hinders innovation is that more and more trivial technology finds its way into patent protection. In general it must be stated that this is not an issue of the patent system as such, but a criticism against the work of the patent offices. Moreover this hypothesis has not been proven by any statistical evidence so far.

The test of 'obviousness' is mostly used to attack patents in nullity suits. Again, this underlines that the function of the patent system is ex-post, meaning that retroactively many inventions appear trivial, which has not been the case before the inventor worked on the technology challenge nor when the patent office granted the patent. The low total number of successful nullity suits, compared to the number of patents filed and compared to the number of successful infringement suits clearly shows that the majority of patents are strong and protect products and trigger a strong commercial interest from competition, because they are innovative (for details please see: Aloys Hüttermann, Mitt. 2016, 101 ff; Christoph Ann VPP Rundbrief 2016, 42 ff; ders. Mitt. 2016, 245, 247 ff)

c. Ability to Cross-Licence

In the public discussion it is often argued that full rights to enforce patents should only be granted to patent owners who practice their patents. The hypothesis behind this is that only practising companies are vulnerable themselves, meaning willing to grant cross-licenses on their own technologies to avoid damage on their own production and sales.

This argument obviously ignores the fact that the function of the law is to ensure law-abiding behaviour of all parties. Enforcement of rights granted by law cannot be sanctioned just because the patent owner wants to use them according to applicable law, no matter if the owner is a practising entity or not. Patent law does not discriminate against types of patent holders. Vice-versa the infringer is obliged to stop infringement, but is not entitled to claim a license. In practice, a practising entity might be more willing to agree on a cross license in order to create legal certainty and 'freedom of action' for itself, to minimise the tentative risk of infringing the other party's patents. But this situation triggers no need to change the system as such.

1.3 Is there a need for general regulation?

A detailed analysis of cases that claim a need for regulatory intervention indicates that the core accusation is a potential 'abuse' of legally granted rights, resulting from patent law.

Neither the patent system nor the underlying legislation is responsible for individualised abusive behaviour of patent holders. The nature of the patent system is to protect and foster innovation to the benefit and welfare of society at large. Therefore the system needs to have instruments that protect inventors and investors to ensure returns on investment for the risk taken and market-conformed profits. Exclusion of competitors is allowed and is only limited by law through existing regulation for compulsory licensing. Furthermore the legislation allows licensing and offers opposition and nullity actions to remove patent protection.

The above-mentioned calls for 'abusive uses' to be further restricted goes beyond existing European and national legislations. But the assessment between use and 'abusive use' cannot be done in the abstract or as a general rule. It has to be always a decision based on the facts of the individual circumstances at hand. The assessment needs to be done individually and in a timely manner by the courts. Therefore, a general regulatory intervention that restricts the courts' ability to adjudicate on fact-specific determination of rights is not applicable.

The courts involved need to consider all individual circumstances of the case, which includes not only the potential abuse of the patent rights, but in particular also the abusive behaviour of the infringer.

General regulations and intervention may unintentionally encourage the unauthorised use of protected technologies, meaning free-riders will be encouraged to disregard the rights of the patent holder and inventor and to infringe the patent rights. Limitations of the availability of injunctive relief would encourage infringers to abuse rights and merely await court action by the patent holder. During that time the infringer would be able to continuously use the protected technology, due to such limitations of the patent holder's rights and might benefit from the lack of financial resources of the patent holder to afford litigation.

Key words:

FRAND, enforcement, injunctive relief, innovation, regulatory intervention, return on investment, limitation, standard essential patents (SEPs), non-practicing entities (NPEs), patent aggregators.

Conclusion:

The demand for regulatory intervention based on potential abuse of patent rights ignores that such abuse happens only occasionally. Isolated cases should not be addressed through general regulations that affects all players but rather must be assessed by courts as they can consider all the individual circumstances of each particular case.

Any regulatory intervention that restricts the right of the patent holder, limits his chance to obtain a fair return on his investment for the risk of failure he has taken as well as a market-conformed profit. The right to get rewarded for the disclosure of an invention remains with the original inventor, who holds the patent, or in case he sells the patent, to whomever this right is transferred.

Co-creation and technology transfer would be negatively impacted by regulatory intervention. Innovation processes and product development would be retarded as free riders would be encouraged to infringe the patent and seek long lasting litigation while using the technology and earning profits without any timely and fair compensation.