



IPR Policy as Strategy

The Battle to Define the Meaning of FRAND



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1. Introduction

The value of patents affects the performance of firms and the structure of markets, which in turn impacts the dynamic and static efficiency of the economy. Thus any discussion that impacts the value of patents through legislative reform, new judicial norms, or other regulatory or contractual regimes will have a systemic effect on the economy and thus must be informed by an understanding of the empirical evidence, the potential theoretical consequences of change, and the self-assertive interests of the parties that are lobbying for change. Without this holistic evaluation we are likely to initiate change that creates greater inequities, potentially lowering instead of raising aggregate social welfare.

One of the most high-stakes arenas where strong business interests are currently debating and defining the value of patents is within the telecommunication industry. While much of the attention in the popular press has focused on the smart phone war between Apple and Samsung, which is a relatively traditional industrial battle over competing products, a potentially more important intellectual property battle concerning the future of telecommunications in the knowledge economy has been ensuing in parallel. This is not a conventional battle over the market share of products between horizontal competitors on product markets, but a battle among vertical collaborators over the appropriation of value between upstream technology owners and downstream product implementers. As such, the current conflict in the context of telecommunication standards is part of a wider paradigm shift from an industrial to a knowledge economy characterized by an increasing number of actors that commercialize knowledge through intellectual property based business models. Thus market conflicts between vertical actors over royalties regarding technology standards can carry a greater systemic impact as it questions the viability of a new division of innovative labor in the economy.

This study addresses the ongoing battle to define the meaning of F/RAND as a key institution in determining the value of standard essential patents (SEPs) and the transformation of the telecommunication industry in the emerging knowledge economy. In particular, this study investigates the social construction of F/RAND and SEP value by deconstructing the key concepts and self-assertive interests of industry actors that have formed the basis for recent judicial, regulatory, and policy decisions. The primary goal is to unveil the normative game whereby actors seek to define reality from the perspective of their own self-interest, whether economic or ideological, in hopes that this will facilitate more objective research and more effective decision-making by standard-setting organizations, courts, competition authorities, and legislators. The full paper will be available in an academic journal in the near future. Below is a short summary of the preliminary findings.

2. Preliminary findings

- **Self-Interest and Heterogeneity in the Telecommunication Value Chain**

The telecommunication industry operates in a fragmented value chain where heterogeneous actors operate with both industrial and knowledge-based business models, and competition is conducted on both the technology and product market. This has resulted in that SEPs play a strategic role in determining bargaining power in vertical relationships as well as competitive advantage in horizontal relationships. A specific firms' view on F/RAND is aligned not with the position in the value chain, but instead depends on the type of business model and the relative strength of the SEP portfolio in relation to specific competitive relationships (e.g. not every chipmaker or end product supplier has the same view on F/RAND). The evidence suggests that as the competitive environment and strategy of firms change, so does their viewpoint on the definition of F/RAND and the value of SEPs.

- **The Social Construction of F/RAND**

The history of F/RAND in the telecommunication industry can be dated back to the 1956 AT&T consent decree. While, in this instance, F/RAND was seen as a remedy to facilitate technology access, there is now considerably disagreement as to whether F/RAND is institutionally sufficient to regulate license agreements in the telecommunication industry without anti-competitive effects. This has generated a rather intense battle over the meaning of F/RAND among market actors with divergent views. While there is general agreement that F/RAND should regulate both access to technology and incentives to innovate, there is a large disagreement (e.g. between 1-2 orders of magnitude) over what constitutes a F/RAND royalty rate. Relatively new concepts, such as royalty stacking and ex ante valuation have emerged together with new arguments related to well-known concepts such as injunction and royalty base. However, by far the most important issue relates to the social construction of the concept of patent holdup, especially the distinction between its contractual and antitrust dimensions. Despite the market success of F/RAND-enabled standards and the 2006 eBay ruling limiting injunctions, the use of the concept of patent holdup still remains at the core of the argumentation in defining the meaning of F/RAND in 2015.

- **Legitimizing Arenas and the Communicative Game**

Self-interests and normative concepts are not sufficient in of themselves to define the meaning of F/RAND without communicative actions on legitimizing arenas. This primarily includes influencing IPR policies in SSOs, filing amicus briefs and strategic use of litigation in the courts, filing complaints at the FTC and ITC, and participation in DOJ, FTC, and Congressional hearings. Additionally, indirect influence through academic research and media sources also impacts the decisions of legitimizing arenas. These communicative actions result in court orders, enforcement actions, policy statements, business review letters, exclusion orders, IPR policies, legislation, etc. all of which combine to ultimately influence the meaning of

F/RAND in general, but more importantly impact the actual negotiation of SEP licenses in market transactions.

While firms are expected to act in their own self-interest, the role of legitimizing arenas is to safeguard the interests of society as a whole. There are clear indications that market actors are strategically looking to alter the “rules of the game” in their favor by taking an active role in influencing policy decisions regarding F/RAND and the value of SEPs. Thus there is a genuine concern that strong financial interests can unduly affect the framework upon which open standards are developed and commercialized. By mapping the self-interests, the origin and use of normative concepts, and the communicative actions, actors on legitimizing arenas will be better able to deconstruct and understand the validity of the complex argumentation and evidence put before them and make better informed, systemic decisions.