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The EC SEP Regulation Proposal: New Rules To be FRAND?

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On 27 April, about a month after an [unofficial leaked version](#), the European Commission published the highly-contentious [Standard Essential Patents \(SEPs\) Regulation Proposal](#). The Proposal aims to facilitate SEP licensing by increasing transparency over SEPs, reducing information asymmetries between SEP licensors and implementers and facilitating the agreement on Fair, Reasonable and Non-Discriminatory ('FRAND') licenses. Such a regulation would innovate the legal framework for licensing SEPs in Europe that so far rested on Arts. 101 and 102 of the TFEU, particularly on the [Horizontal Cooperation Guidelines](#), currently under review, and the [Huawei v ZTE](#) abuse of dominance case law.

As for other EU laws harmonising intellectual property rights across Member States (such as the [Intellectual Property Rights Enforcement Directive](#)), the Commission uses Art. 114 of the TFEU to remove obstacles to the proper functioning of the internal market. If enacted, the Proposal would impose the registration of patents deemed standard-essential in an electronic register held by the [EU Intellectual Property Office \(EUIPO\)](#) for the patentee to enforce its rights in the EU. Furthermore, it would entrust the EUIPO to administer non-binding procedures to assess the essentiality of registered SEPs, establish global aggregate royalty rates for standards implementations, and determine actual FRAND licenses. In practice, SEPs validated in Member States would become a special type of patent subject to a *sui generis* intellectual property rights system with substantial extra-territorial effects.

The Regulatory Problems

Since the [2017 Communication on SEPs](#), the EC acknowledged [two opposing issues](#) in the technology markets for licensing SEPs for Information, Communication Technology (ICT) standards: patent hold-up and hold-out. In essence, patent hold-up refers to situations where a SEP holder can exploit its market power over standard implementers that cannot design around or substitute the technology claimed by the SEP. Such a lock-in situation occurs because compliance with the standard is indispensable for product market competition. In a patent hold-up situation, the SEP holder can obtain supra-FRAND remuneration thanks to the threat of an injunction that would exclude the SEP infringer from standard-compliant product markets. Instead, patent hold-out consists of standard-implementers wilfully free-riding, not seeking licensees for the SEPs they practice knowing infringement will not be pursued or offering SEP holders to abide by below-FRAND licensing conditions unless being mandated otherwise in court. Together, patent hold-up

and hold-out undermine confidence in, and incentives to join, standard-development organisations' open innovation efforts, tilting the balance towards closed innovation models such as *de facto* proprietary standards and platform ecosystems.

The Road to the EC SEP Proposal

The CJEU, when asked to reconcile the tension between dominant SEP holders' exclusivity and implementers' access to industry standards in *Huawei v ZTE*, focused on the [good faith negotiating path](#) to conclude bilateral FRAND licenses. It balanced the opposing interests by recognising that if they meet certain conditions, dominant SEP holders do not abuse their position by seeking injunctive relief against implementers showing their unwillingness to take a FRAND licence. The *Huawei v ZTE* negotiating framework enhances legal certainty, especially in traditional ICT sectors where FRAND licensing disputes have emerged historically. Nonetheless, parties still disputed standard-essentiality, invalidity, infringement, FRAND terms and conditions and abuses of dominance before their preferred jurisdictions [globally](#), trying to achieve favourable rulings to influence licensing negotiations in their favour.

After its [2020 IP Action plan](#), mentioning possible reforms to clarify and improve the framework for the declaration, licensing and enforcement of SEPs, the [2021 SEP Expert Group Report](#) and multiple [consultations in 2022](#), now the Commission advances a concrete regulatory proposal. Specifically, the Commission looks at nascent [Internet of Things markets](#) with many SMEs that might be put off by the need to conclude an unpredictable number of FRAND licenses for an unknown price. The Proposal inserts itself in the foreground of the *Huawei v ZTE* negotiating framework and seeks to reduce frictions of SEP licensing that could impair participation by European firms in standardisation processes and the roll-out of standards in the EU's [fair green and digital transitions](#) or Single Market value chains.

The Scope of the Proposed Regulation

Subject-wise, the Proposal would apply to patents granted in Member States that are essential to standards subject to FRAND licensing commitments (art. 1(2)). Patent applications, utility models and non-EU patents are outside the scope of the Proposal (Art. 2(1)), as well as EU SEPs for standards subject to royalty-free or open-source licensing commitments.

Timing-wise, the Proposal would catch all those standards published after its entry into force. However, the Commission has the delegated power to impose specific obligations retroactively on already-existing standards whose licensing severely distorts the internal market (Art. 66(4)). It can also exclude individual use cases for new standards that '*do not give rise to significant difficulties or inefficiencies affecting the functioning of the internal market...*' (Arts. 1(4)).

Such flexibility in application is desirable not to complicate well-functioning SEP licensing markets and to catch old yet critical standards but also necessary, given the sheer amount of industry standards continuously developed. However, legal certainty would call for clearer indicators of what difficulties or inefficiencies in SEP licensing would justify the inclusion or exclusion into the regulatory framework. How many SEP litigation instances are enough to bring a standard implementation into the purview of the EUIPO? Can a patent pool with an incomplete

SEP coverage for a standard implementation avoid the need for regulatory oversight?

A Star is (Re)Born: The EUIPO As the EU SEP Authority

The real star of the Proposal is the EUIPO (Art. 3). The Alicante-based EU agency would host a new competence centre, most notably to maintain a SEP electronic register and database and administer non-binding procedures for assessing standard-essentiality, aggregate royalties and FRAND licensing terms and conditions. Although the EUIPO would need to build SEP-related skills from scratch, it already has extensive experience in IPR registration, enforcement databases and ADR Services, precisely thanks to its [Observatory](#) and [Boards of Appeal](#). Furthermore, the EUIPO would rely on external consultants, admitted to its rosters of essentiality evaluators and aggregate royalty or FRAND conciliators, to carry out the non-binding regulatory procedures (Art. 26).

The EUIPO SEP Register and Database

The least controversial function of the EUIPO would be to maintain a SEP register and database insofar as this improves the property notice functions of SEPs. On the one hand, the SEP register (Art. 4) would collect basic data such as patent number, country of validation, relevant standard and technical specification, owners' contact details, public standard FRAND licenses, licensing availability through patent pools and outcomes of essentiality checks. On the other hand, the database (Art. 5) would gather added value data such as granular patent bibliographic data (e.g., priority date, family members, grant date), known implementations of the SEP, standard FRAND terms and conditions, information on essentiality, FRAND and aggregate royalty determination. Intuitively, the SEP register would be publicly accessible free of charge, whereas access to the database would require prior registration and possibly a fee.

[Patent pools](#) (Art. 9), courts (Art. 10) and ADR service providers (Art. 11) must feed SEP-related information to the EUIPO too. Competition lawyers most likely have low expectations regarding information reporting by national courts given the unenforced precedent of Art. 15 of [Regulation 1/2003](#). Patent lawyers might be sceptical, too, given the existing but ineffective [requirements to record patent ownership changes and licenses](#) before the European and national patent offices.

Notifications of New Standards and Global Aggregate Royalties

The first step in the regulated framework is a joint obligation for SEP holders (Art. 14) to notify the EUIPO about a new standard (and new technical specifications for existing ones). Failure to notify the existence of a new standard by the SEP holders jointly within 30 days from its publication or individually within 90 days would entitle any implementer to do the notification. By 120 days from the publication of the standard, or the awareness of a new use for an existing standard, all or some SEP holders can notify a possibly global aggregate royalty for the applicable SEPs (Art. 15). Global rates have a clear extra-territorial effect that contradicts the SEP registration requirement limited to SEPs validated in the Member State and directly follows suit to the global FRAND rate determination by non-EU courts.

Apart from international comity issues, the possibility of fixing SEP prices after a standard is set goes even beyond the competition law benevolence of paras. 473 and 500 of the [draft new Horizontal Cooperation Guidelines](#) to the *ex-ante* disclosure of maximum accumulated royalty rates by SEP holders. It also ignores the competitive safeguards for operating patent pools of paras. 248ff of the [Technology Transfer Guidelines](#), currently under review. First, it is unclear how SEP holders might agree on a global aggregate royalty rate shortly after a standard is set when the standard implementations have unclear value while not running afoul of Article 101(1) TFEU. Second, without an explicit option to record multiple aggregate royalty rates by different groups of SEP holders, one might wonder how vertically integrated SEP holders and non-practising SEP holders can find an agreement over a common price even through a EUIPO-appointed conciliator (Art. 17).

Moreover, holders of 20% of SEPs for the relevant standard, together with either 10 SMEs or implementers representing at least 10% of the relevant market share for the standard-compliant product, can ask the EUIPO to appoint a three-people panel as a last resort to pinpoint an aggregate royalty. Building on input by any stakeholder, the expert panel of conciliators would provide by majority a non-binding expert opinion on the aggregate royalty within 8 to 14 months from appointment. All participants to such an expert opinion would pay its costs, whereas SEP holders would bear the conciliators' fees when just facilitating the agreement on an aggregate royalty (Art. 63(3)).

SEPs As Special Patents Subject to Registration Requirements

Within six months from the publication of a new standard on the EUIPO website or the later patent grant, SEP holders must register their SEPs in force in at least one Member State and pay a registration fee (Art. 20). The EUIPO conducts a formal check on a sample of registrations and eventually asks for corrections (Art. 22). Third parties and the EUIPO, upon data sent by national courts or patent offices, may also request formal and substantial corrections to SEP holders (Art. 23). Failure to amend registrations within two months from the request would trigger their suspension until the error is remedied. SEP holders can also seek a suspension review before the EUIPO Boards of Appeal.

Most notably, failure to register SEPs within the six months deadline precludes enforcement against the relevant standard implementation and bars compensation for infringement acts occurring from the due time for registration until its late performance (Art. 24). Accordingly, EU SEPs would officially become a unique type of patents whose exclusive rights would be subject not only to examination by patent offices but also to registration before the EUIPO. Although the Proposal would impose on national courts the duty to verify registrations before ruling on SEP issues (Art. 24(5)), more realistically, the opposing parties driven by self-interest would inform courts about the registrations or lack thereof.

Large SEP holders have a way out from a full-blown registration requirement with a sort of patent portfolio safe harbour. Indeed, Art. 24(3) would exclude that the limitation on the enforcement of non-registered SEPs invalidates clauses in broad portfolio licenses that shield royalty rates from individual SEPs' invalidity, non-essentiality or unenforceability. Besides uncertainty on what constitutes "*a broad portfolio of patents*" and how many SEP registrations are enough to keep intact portfolio royalty rates, this safe harbour might raise [exploitative competition law](#) concerns.

For example, large SEP holders could select what SEPs to register for enforcement purposes while imposing portfolio licenses tying the registered SEPs to unregistered ones and charging for invalid, non-infringed or non-essential patents.

The Expected Essentiality Check System

Since the 2017 SEP Communication, an EU system of essentiality checks has been in the air, even more so after two studies ([here](#) and [here](#)) funded by the Commission. The key features of the EUIPO essentiality assessment would be:

- Analysis limited to the essentiality of just one national SEP out of a family of SEPs sharing a common priority application (even if patent claim construction can result in [different outcomes depending on the jurisdiction](#));
- Analysis limited to a representative sample of all SEPs registered for a standard;
- Each SEP holder can propose annually up to 100 of its registered SEPs for each standard to be checked;
- Any implementer can also pinpoint up to 100 registered SEPs for each standard to be checked, which opens the door to collusion risks among implementers coordinating their proposals anti-competitively;
- The appointed evaluator has six months to issue his non-binding reasoned opinion, considering observations filed by any stakeholders;
- SEP holders may request the peer review by another evaluator of a *prima facie* negative essentiality check, which should take an additional three months;
- EUIPO publishes in its register the outcome of the essentiality check or peer review, essentiality ratios per SEP holder and per standard, while in the database the underlying reasoned essentiality opinion;
- The party that requests the essentiality check would pay its fees.

FRAND Determination: The Bulk of the Proposal

25 out of 72 articles of the Proposal set a [mandatory first-step, non-binding FRAND determination procedure](#). Mandatory attempts and incentives for alternative dispute resolution (ADR) before going to court are not a novelty in Europe. Since the 2008 [Mediation Directive](#), some [Member States](#) have introduced mandatory first-step ADRs in civil and commercial disputes. Now, SEP holders or implementers of standards registered by the EUIPO would need to request (and pay) a FRAND determination before raising SEP-related issues before the just-starting [Unified Patent Court](#) or Member States' courts (Art. 34). Such an attempt would specify by default a global FRAND licence with clear extra-territorial impact. Parallel court or administrative proceedings in non-EU countries between the same parties concerning the same SEP licensing issues may run together with the EUIPO FRAND determination, but each party may ask for the termination of the procedure before the EUIPO (Art. 47). Interestingly, there is no FRAND determination requirement before lodging complaints to competition authorities for abuse of dominance by SEP holders, which implementers can use as a hold-out strategy. The only available remedy against SEP infringement without a FRAND determination would be provisional injunctions of a financial nature, with which many [EU jurisdictions are likely unfamiliar](#).

The EUIPO would notify the relevant counterparty (the so-called responding party) about the request for a FRAND determination. If the responding party does not reply in time, decides not to participate or does not commit to abiding by the outcome, then it is up to the requesting party to either let the FRAND determination terminate or continue it unilaterally. If the responding party accepts the FRAND determination and commits to its outcome, the ball returns to the requesting party. This latter may determine the start of the FRAND determination by also undertaking to abide by its outcome. If the requesting party relinquishes its initial request, the responding party may terminate the procedure or continue it unilaterally.

Parties have a solid incentive to commit to the FRAND determination outcome since failure to do so precludes an effective right of confrontation, such as by selecting the conciliator that would administer the procedure and deliver the FRAND determination (Art. 39) or by submitting reasoned FRAND determination proposals (Art. 52). Failure to commit to the FRAND determination also unleashes court actions over the same subject matter by the abiding party.

The procedure, which should take nine months, during which national statutes of limitation would be suspended (Art. 37), can terminate positively or negatively. Positive outcomes would include the parties' settlement or a joint declaration to accept the conciliator's FRAND determination. Negative results would consist of a party's refusal to accept the conciliator's FRAND determination or a party's failure to reply to the conciliator's FRAND determination (Art. 56). For negative outcomes, the conciliator provides the parties with a report including a confidential assessment of the FRAND determination (Art. 57(1)). A non-confidential version of the report stating the conciliator's methodology and assessment of the FRAND determination is included in the EUIPO database (Art. 57(3)). Moreover, the EUIPO provides the parties to the joint procedure or the party to the unilateral procedure, respectively, with notice of termination or commitment stating the subject matter, a summary of the procedure and the reasons for its termination. Both the conciliator's report and the notice could be used under the *Huawei v ZTE* framework to demonstrate **one's good faith and the counterparty's bad faith** in negotiations to influence rulings on injunctive relief and FRAND terms and conditions. This possibility makes the UPC and Member States' patent judges one of the main beneficiaries of the Proposal since it would significantly ease their adjudicating burdens in SEP disputes.

First Impression

To increase transparency over SEP licensing in favour of both SEP licensors and implementers a single registration system before the EUIPO makes sense to determine one-stop-shop efficiencies compared to fragmented and incomplete patent registers. However, it is more questionable to give a legal monopoly to the EUIPO over the (non-binding) resolution of substantive SEP licensing issues. Multiple ADR centres with IP expertise (such as ones of **WIPO** and **UPC**) are already in place and could be eligible to provide the services set out by the Proposal in competition with each other and the EUIPO.

Further, the Proposal has a major competition law deficiency when it comes to the possibility to fix a global aggregate royalty for a standard implementation. At least, the competitive safeguards of the Technology Transfer Guidelines applicable to the formation and operation of patent pools, such as transparency, open participation and limits to sensitive information exchanges should apply to any global aggregate royalty discussion.

Overall, the Commission SEP Proposal is just the beginning of the uncertain EU legislative procedure that might well come to a dead end or U-turn particularly due to the [European elections of 2024](#). EU policymakers should strive not to tilt the balance between SEP holders and implementers enshrined by the CJEU in *Huawei v ZTE* if their goal is to facilitate SEP licensing. For the sake of open innovation through collective standardisation, any regulation should take care not to facilitate patent hold-ups as much as hold-out.

* *Join the discussion on the SEP Proposal at the webinar by the EUI Center for a Digital Society of May 19th. Register [here](#).*

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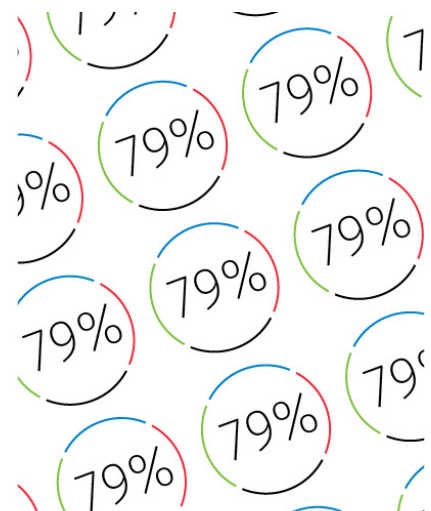
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