

## **Questions for the Record for Professor Thomas F. Cotter**

### **In relation to the December 18, 2024 Hearing Before the United States House of Representatives Subcommittee on Courts, Intellectual Property, and the Internet of the Committee on the Judiciary: “IP and Strategic Competition with China: Part IV — Patents, Standards, and Lawfare”**

Below are my responses to the Questions for the Record I received via e-mail on January 9, 2025, from Representatives Issa, Fitzgerald, and Cline:

#### **Questions for the Record from Representative Darrell Issa**

1. What are the potential benefits and risks to the United States taking a more robust role in the international standards and SEP systems?

*My response:* In my view, there could be benefits for the United States in coordinating with other countries on SEP-related issues that are in our mutual interest. For example, although I am somewhat agnostic on the overall merits of the European Commission’s Draft SEP Regulation, which is the subject of one of Representative Cline’s questions below, if policymakers in the United States and other allied nations conclude that the draft Regulation, as proposed, would not be in their common interest, it might make sense for these nations to engage in coordinated diplomatic efforts to oppose the draft Regulation’s enactment, at least in its current form. Another possibility, if policymakers believe it would be in the interest of the United States, might be to coordinate efforts to encourage standard-setting organizations (SSOs) to change some of their policies in regard to certain matters that other panelists discussed at the December 18 hearing, such as voting rights. Also, as I note in my response to one of Representative Fitzgerald’s questions below, it might be worth considering whether the U.S. and other nations should encourage SSOs to consider requiring the mandatory arbitration of FRAND disputes, to alleviate forum shopping. A third possibility might be, as one of the panelists at the December 18 suggested, to coordinate in developing common positions before the World Trade Organization in an effort to make proceedings there more effective. On the other side of the coin, one thing I would perceive as a possible risk would be unilateral action by the U.S. government that might be perceived as interfering with the independent judiciaries of our close allies, for example by threatening the U.K. with economic consequences if its courts continue to set global rates in FRAND litigation. I would be cautious, at any rate, about the potential for such actions to generate more costs than benefits for the United States. Finally, I believe it is important for Congress to be mindful that patents present both benefits and costs for U.S. innovators. Patent rights need to be sufficiently strong to induce investment in innovation, but at the same time policymakers should be mindful that, as many economists will agree, if rights are too strong they can inhibit other innovators from accessing the technology they need to engage in their own innovation.

2. A great deal of attention has been devoted to the availability (or lack thereof) of injunctive relief in SEP cases. Does the availability of injunctive relief tend to have any impact on the outcome of licensing negotiations? If so, in what way?

*My response:* If the SEP owner and the implementer do not expect a U.S. court to grant injunctive relief for the infringement of a FRAND-committed SEP, but rather for a court to determine the amount of damages or a FRAND royalty for both past and future infringement, I would expect this to affect licensing negotiations in the following ways. First, because the implementer may have little or no choice whether to use the FRAND-committed SEP or SEPs at issue if it wishes to compete, a SEP owner who can credibly threaten to enforce an injunction against an implementer may be able to negotiate an above-FRAND royalty—that is, a royalty that reflects not only the economic value of the SEP or SEPs at issue, but also some portion of the implementer’s non-redeployable sunk costs, its higher ex post switching costs, and/or its lower ex post network benefits. For discussion, see Thomas F. Cotter, Erik Hovenkamp & Norman Siebrasse, *Demystifying Patent Holdup*, 76 WASH. & LEE L. REV. 1501, 1531-32 (2019). The expected unavailability of injunctive relief against a willing licensee would decrease this risk of what is referred to as patent “holdup.” Second, however, the expected unavailability of injunctive relief might, in theory, encourage implementers to engage in strategic delay, sometimes referred to as “holdout,” if for example a damages award, including prejudgment interest, would not fully compensate the SEP owner for the time value of money or if, as Mr. Justice Meade opined in *Optis Cellular Tech. LLC v Apple Retail UK Ltd.*, [2021] EWHC 2564, [236]-[244] (Pat.) (Eng.), delay could induce SEP owners to “discount the royalties/damages for past acts” or encourage other implementers to hold out. (That said, in cases in which implementers have refused to negotiate in good faith, U.S. courts would have the discretion under *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388 (2006), to award injunctive relief, or in an appropriate case to award enhanced damages for willful infringement.) In short, the expected availability of injunctive relief strengthens the SEP owner’s bargaining position, and the expected unavailability of injunctive relief strengthens the implementer’s bargaining position. The goal, in my opinion, should not be to unduly strengthen either side but rather to craft rules and standards that result in the parties negotiating, or when necessary courts awarding, royalties that are in fact FRAND.

There are two additional complications to consider. First, if a dispute between a SEP owner and an implementer proceeds to trial in the United States, and the trier of fact is tasked with determining the amount of a FRAND royalty, it could be a judge, or it could be a jury, who ultimately decides that amount. Given the complexity involved, the possibility of a jury determination may add some further degree of uncertainty to the mix. Second, if injunctive relief is expected to be unavailable in the United States but available in some other jurisdictions (such as Germany or the Unified Patent Court), some SEP owners may have an incentive to focus their efforts on obtaining injunctive relief in one of the latter forums to compel a favorable, and perhaps global, settlement.

- a. Many commentators assert that injunctive relief is no longer available for patent infringement in the United States. Is that true, and does it matter if the patent at issue is an SEP? If so, why?

*My response:* In my opinion, it is an overstatement to conclude that injunctive relief is no longer available for patent infringement in the United States. Statistics indicate that practicing entities who request injunctive relief still have a very good chance of obtaining it—as they generally should, when their business models depend on excluding competitors rather than

nonexclusive licensing. By contrast, patent owners whose business models depend on nonexclusive licensing often face difficulty, under *eBay*, in demonstrating that injunctive relief is necessary to avoid irreparable harm, or that monetary damages would be inadequate, in view of the court's ability to determine an ongoing royalty in lieu of injunctive relief. Patent owners falling into this second category include nonpracticing entities who license on a nonexclusive basis, as well as SEP owners. In addition, SEP owners also may have difficulty showing that the balance of hardships favors injunctive relief, if access to the standardized technology is necessary for the implementer to compete and a court-determined royalty would adequately compensate the patentee. Conceivably, a court also may view the fourth *eBay* factor, the public interest, as favoring the implementer, if an injunction would threaten to deprive consumers of the ability to use an important product; and public interest considerations also can be important for purposes of determining whether to enter an exclusion order in a proceeding before the International Trade Commission. Again, though, depending on the specific circumstances at issue (e.g., if the implementer is an unwilling licensee or the public interest is not likely to be significantly affected), injunctive relief and exclusion orders may be appropriate remedies under U.S. law.

## Questions for the Record from Representative Scott Fitzgerald

1. The UK Supreme Court decided two landmark cases in the last few years in which it made FRAND determinations on a worldwide basis – *Unwired Planet v. Huawei* and *Interdigital v. Lenovo*. In those cases, the court articulated a framework for making FRAND determinations. What do you think of the decisions in those cases?

*My response:* Just to be clear, the UK Supreme Court has issued one decision, in 2020, addressing this issue, in the joined cases of *Unwired Planet International Ltd. v. Huawei Technologies (UK) Co. Ltd., Huawei Technologies Co. Ltd. v. Conversant Wireless Licensing SÀRL, and ZTE Corp. v. Conversant Wireless Licensing SÀRL*, [2020] UKSC 37. The other decision referred to in the question above, *InterDigital Tech. Corp. v. Lenovo Group Ltd.*, [2023] EWHC 539 (Pat.) (Eng.), *modified*, [2024] EWCA Civ. 743, is not a Supreme Court decision but follows the precedent set in *Unwired Planet*, as do other lower court decisions including *Optis Cellular Tech. LLC v. Apple Retail UK Ltd.*, [2023] EWHC 1095 (Pat.) (Eng.). At the time the trial court decided the *Unwired Planet* case in 2017, I expressed concern that the English court’s decision—to present the infringers with a choice between being enjoined from the U.K. market, or agreeing to the court’s determination of the terms of a global FRAND license—was overreaching, given the territorial nature of patent rights. (The infringers in the UKSC decision also were Chinese companies, and their sales in China were much greater than their sales in the U.K., which made me wonder whether, under the principle of *forum non conveniens*, if any country were to determine the terms of a global license in this particular instance, it should be China. The English court concluded otherwise, however, in part because it was unclear at the time whether a Chinese court would exercise authority to determine global FRAND rates.) Moreover, one predictable consequence of *Unwired Planet* was that courts in other countries, such as China, would come to emulate the English practice of setting global rates, and I and other expressed concern that this would only exacerbate forum shopping. On the other hand, I also recognized at the time that there are potential efficiency gains from having one court determine global rates, rather than proceeding on a country-by-country basis, something the trial judge in *Unwired Planet* referred to as “madness.” (That said, it may be that few if any FRAND disputes would proceed all the way to judgment in numerous countries, as opposed to settling after the first decision or two or three were rendered.) In any event, I still have those concerns, though I also recognize that there is a certain logic to the *Unwired Planet* framework. If, as a matter of industry practice, a FRAND license would be global in scope, a willing licensor and licensee would agree to a global license; and in default of their ability to reach a voluntary agreement, the infringer must either accept a U.K.-wide injunction resulting from its infringement of a U.K. patent, or agree to let the court set the terms of such a license (which could include a mechanism for adjusting rates as need be, if for example any of the patents covered by the license subsequently were to be invalidated in their countries of issuance). In addition—although I am not enough of a business person to have a firm opinion, one way or the other, whether the rates the English courts have set in cases noted above have accurately reflected the terms of a FRAND license—I have been impressed with the U.K. judges’ thoughtful, painstaking analysis and evaluation of the complex evidence before them in these cases. Further, although some observers initially thought that the *Unwired Planet* decision would make the U.K. a forum of choice for SEP owners, the other two decisions referenced above

are viewed as having been, if anything, more favorable to the defendants (Lenovo and Apple) than to the owners.

2. Despite being on multiple U.S. sanctions lists, Huawei utilizes its massive patent portfolio to collect licensing revenue from U.S. companies, which generated the sanctioned company more than \$560 million in 2022. Should the United States continue to allow sanctioned companies, like Huawei, to circumvent U.S. sanctions through the licensing of U.S. patents to U.S. companies?

*My response:* To the extent the answer to this question hinges on questions of national security, it is somewhat beyond my area of expertise. I would suggest, however, that before enacting legislation that would preclude companies such as Huawei from collecting licensing revenue from U.S. companies, Congress consider whether such a measure would invite retaliation by China, and if so what the impact of such retaliation might be on U.S. companies. It also may be advisable to solicit input from the United States Trade Representative and/or the USPTO regarding whether any such legislation would potentially raise issues under the Takings Clause, the TRIPS Agreement, or other existing legal obligations of the United States.

3. If you ask five people to define what constitutes fair, reasonable, and non-discriminatory (FRAND) licensing terms, you are likely to get five different answers. What do you think is the best method to determine FRAND terms, and who should ultimately be the arbitrator of that decision?

*My response:* I agree that there is a wide range of views concerning how FRAND royalties should be calculated; indeed, I mentioned some of the areas of potential disagreement in footnote 55 of my written testimony. That said, there are two principal general approaches, both of which I think are potentially helpful. One is to rely primarily, as courts often do in non-SEP patent infringement actions, on comparable licenses. To be sure, this is sometimes easier said than done. As in patent infringement actions generally, courts may need to ensure that the allegedly comparable licenses offered in evidence or considered by the parties' experts in forming their opinions are, in fact, sufficiently comparable to the license the court or jury will be constructing. Experts or courts may need to make adjustments based on material differences in circumstances, including the differences in the licenses' scope; apportionment of the patent rights at issue in the dispute from other patents and intellectual property rights included within an allegedly comparable portfolio; and the comparability of the parties to the license, e.g. in terms of their business models and scale, to the parties to the dispute. This may not be simple, but courts engage in this sort of inquiry all the time in everyday patent infringement actions, and the rules and standards that apply in those cases are largely transferrable to the FRAND context. Of course, that doesn't ensure that two different courts' decisions about what evidence to admit, or what conclusions to derive on the basis of that evidence, would be identical, and it would be fanciful to assume that FRAND determinations necessarily would be either. But when thoughtfully applied, the standard evidentiary framework for assessing royalties for patent infringement can narrow the gap.

The other methodology courts sometimes use, either primarily or as a "check" on the royalty derived from the use of comparables, is the "top-down" approach. In brief, this method involves estimating the aggregate royalty payable for the use of all SEPs reading on a particular

standard (e.g.,  $x\%$  of the value of a smartphone), and then apportioning that royalty based on the number of these SEPs which the plaintiff owns and would be licensing to the implementer—with adjustments, as may be appropriate, for the estimated number of SEPs that are likely to be invalid, non-essential in fact, or non-infringed, and (perhaps) for the strength of the owner's SEPs in comparison with the average SEP reading on the standard. U.S. and U.K. courts sometimes view the top-down approach as a secondary methodology, however, and that might make sense if there is reason to question the accuracy of the estimates needed to carry out the approach.

As for who should be the arbitrator or decisionmaker, I believe most economists considering the matter would agree that, ideally, it is preferable for the parties, who presumably have better information about the value of the relevant technology to their businesses, to work things out for themselves, rather than leaving it to a third-party court or arbitrator. But the reality is that voluntary negotiations are not always successful, in part because of the difficulty, even for the parties themselves, of valuing technology. SEP owners may have good reasons for believing they are entitled to  $x$ , and implementers may have good reasons for believing they should only have to pay  $y$ ; and both parties are accountable to shareholders who expect that firms will negotiate a favorable deal. For that reason, some subset of negotiations fail and wind up in court or before an arbitrator; and my own view is that it is important for courts to be ready and able to determine FRAND royalties when the parties cannot do so on their own. As for *which* courts should do this—and whether they should set global rates even if one or the other party would prefer that rates be set for the domestic portfolio only, as discussed above—those are difficult questions, though based on the cases to date I would be confident of the ability of both U.S. and U.K. judges to do a thorough and professional job. Alternatively, it might be worthwhile to consider whether private entities or governments should encourage standard setting organizations to give serious consideration to proposals, such as one floated by Lord Justice Arnold of the Court of Appeal for England and Wales (see footnote 66 of my written testimony), to require mandatory arbitration of FRAND disputes. I do not at this time have a firm opinion on the merits of this or other such proposals, but one advantage would be to reduce parties' ability to forum-shop their disputes to the venues they expect will be most favorable to their case. Of course, much would hinge on the quality of the arbitrators and the methodology they would employ to decide these cases.

## Questions for the Record from Representative Ben Cline

1. How can the draft EU SEP Regulation address concerns about Chinese or PRC-backed entities leveraging European courts to hold American manufacturers hostage?

*My response:* I am not altogether sure how to answer this question, in part because the draft SEP Regulation is just that—a draft—and it is not clear to me what the final version will look like, if and when it is enacted. What I understand to be the current version, as amended and approved by the European Parliament, is available at [https://www.europarl.europa.eu/doceo/document/TA-9-2024-0100\\_EN.html](https://www.europarl.europa.eu/doceo/document/TA-9-2024-0100_EN.html), but the proposal is now before another E.U. body, the European Council. For a brief update on the status of the draft, see Katharina Pehle, *The EU's SEP regulation: key changes and outlook*, MANAGING IP (Nov. 29, 2024), <https://www.managingip.com/article/2e354jfef8sjq0zxnqz9c/sponsored-content/the-eus-sep-regulation-key-changes-and-outlook>; see also footnote 38 of my written testimony, noting one commentator's report that the draft Regulation could be “stuck” in the Council for a long time. Broadly speaking, though, the draft has some features that, if enacted, may shed some light on the question posed above.

First, the Regulation would apply only to SEPs in force in any E.U. member state after the date of the Regulation's enactment.<sup>1</sup> Subject to some exceptions for micro and small enterprises, owners of these patents would be required to submit information about them to the European Union Intellectual Property Office (EUIPO), which would maintain a SEP registry and would conduct random essentiality checks. If, as one or more of the panelists at the December 18, 2024 hearing opined, Chinese firms in particular over-patent and over-declare for strategic reasons, then at least in principle these essentiality checks might be a useful response to that conduct.

Second, articles 15-18 set out a procedure under which owners of the SEPs covered by the Regulation may reach agreement on an aggregate royalty cap for standards. In theory, this might help reduce the risk of “royalty stacking,” and might facilitate use of the “top-down” approach I note above in my response to one of Representative Fitzgerald's questions—though I would also note, without necessarily either endorsing or rejecting, one commentator's concern that setting royalty caps would “encourage ‘patent counting,’ and “may generate incentives for companies to over-populate the Commission's proposed SEP Register, and undermine the important goal of producing greater transparency.” Justus Baron, *The Commission's Draft SEP Regulation—Focus on Proposed Mechanisms for the Determination of ‘Reasonable Aggregate Royalties’*, <https://ssrn.com/abstract=4537591>.

Third, the draft contemplates that, subject to some exceptions, either a SEP owner or an implementer may request a nonbinding FRAND determination—and indeed must do so before

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<sup>1</sup> See art. 1(2) of the current mark-up by the European Parliament (“This Regulation shall apply to patents that are in force in one or more Member States and that a SEP holder claims to be essential to a standard that has been published by a standard development organisation, after entry into force of this Regulation regardless of whether the SEP holder has or has not made a commitment to license its SEPs on fair, reasonable and non-discriminatory (FRAND) terms and conditions”).

pursuing litigation before a competent court of an E.U. member state.<sup>2</sup> They could avoid the nonbinding determination, however, by litigating elsewhere.<sup>3</sup> So, if the question is premised on the concern that Chinese firms that own E.U. SEPs might demand above-FRAND royalties from U.S. firms, or that Chinese implementers might hold out for below-FRAND royalties for E.U. SEPs owned by U.S. firms, I suppose the nonbinding determination envisioned by the draft Regulation could ameliorate these concerns, if the determination is sound—though perhaps only to the extent that it nudges the parties to agreement on the terms established in the nonbinding determination, rather than simply to reject that determination and proceed to litigation before an E.U. member state court or the Unified Patent Court, or to avoid the determination altogether by initiating litigation outside the E.U.

2. Can you please explain whether standard development organizations actually evaluate whether patents are essential to the standard, or whether instead the owners of the patents are the ones who make those assessments in their declarations?

*My response:* My understanding is that standard development organizations do not conduct such evaluations. It is a matter for the patent owner themselves. For example, the European Telecommunications Standards Institute (ETSI) Rules of Procedure, Annex 6 Rule 4 (Nov. 29-30, 2022), <https://www.etsi.org/images/files/IPR/etsi-ipr-policy.pdf>, titled “Disclosure of IPRs,” reads as follows:

4.1 Subject to Clause 4.2 below, each MEMBER shall use its reasonable endeavours, in particular during the development of a STANDARD or TECHNICAL SPECIFICATION where it participates, to inform ETSI of ESSENTIAL IPRs in a timely fashion. In particular, a MEMBER submitting a technical proposal for a STANDARD or TECHNICAL SPECIFICATION shall, on

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<sup>2</sup> *See id.* art. 34(1):

The FRAND determination in respect of a standard and implementation for which an entry in the register has been created, shall be initiated by any of the following persons:

- (a) SEP holder, prior to any initiation of a SEP infringement claim before a competent court of a Member State;
- (b) an implementer of a SEP prior to any request for the determination or assessment of FRAND terms and conditions of a SEP licence before a competent court of a Member State.

The FRAND determination shall not apply to existing licensing agreements during their application term.

*See also id.* art. 38(6) (“The FRAND determination shall concern a global SEP licence, unless otherwise specified by the parties in case both parties agree to the FRAND determination or by the party that requested the continuation of the FRAND determination. SMEs and start-ups that are parties to the FRAND determination may request to limit the territorial scope of the FRAND determination”).

<sup>3</sup> *See id.* art. 47(2) (“Where a parallel proceeding has been initiated before or during the FRAND determination by a party, the panel of conciliators, or where it has not been appointed, the competence centre, shall terminate the FRAND determination upon the request of the other party”).



a bona fide basis, draw the attention of ETSI to any of that MEMBER's IPR which might be ESSENTIAL if that proposal is adopted.

4.2 The obligations pursuant to Clause 4.1 above do however not imply any obligation on MEMBERS to conduct IPR searches.

4.3 The obligations pursuant to Clause 4.1 above are deemed to be fulfilled in respect of all existing and future members of a PATENT FAMILY if ETSI has been informed of a member of this PATENT FAMILY in a timely fashion. Information on other members of this PATENT FAMILY, if any, may be voluntarily provided.

Note that the second sentence of Rule 4.1 uses the phrase “*might be* ESSENTIAL” (emphasis added). Rule 15, in turn, defines the word “ESSENTIAL” to mean “that it is not possible on technical (but not commercial) grounds, taking into account normal technical practice and the state of the art generally available at the time of standardization, to make, sell, lease, otherwise dispose of, repair, use or operate EQUIPMENT or METHODS which comply with a STANDARD without infringing that IPR. For the avoidance of doubt in exceptional cases where a STANDARD can only be implemented by technical solutions, all of which are infringements of IPRs, all such IPRs shall be considered ESSENTIAL”. It defines “IPR” to mean “any intellectual property right conferred by statute law including applications therefor other than trademarks. For the avoidance of doubt rights relating to get-up, confidential information, trade secrets or the like are excluded from the definition of IPR”.

To my knowledge, the empirical evidence is consistent with the widespread belief that firms tend to “overdeclare” patents that are not, in fact, standard-essential. One reason may be that SSO members wish to avoid running afoul of the above Rule by *not* disclosing a patent that “might be” essential, which otherwise could have negative consequences (e.g., under antitrust law). Another, suggested by at least one panelist at the hearing if I understood correctly, is that firms sometimes may have an incentive to overdeclare for strategic reasons, e.g., to inflate the perceived value of their portfolios.