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Ex Ante Rate Disclosure In Tech Standards, A Decade Later

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In January 2007, the VITA Standards Organization made history — and stirred up a lot of controversy — by voting to adopt a patent policy that mandates "ex ante" royalty rate disclosures. Specifically, the VITA intellectual property policy requires its members to not only disclose all patents that are likely to be essential to implement the standard (a common practice among standards development organizations, or SDOs, around the world), but also to declare "the maximum royalty rate" they will seek for their disclosed patents, and to do so during the members' debate over which technologies to include in the standard (i.e., ex ante to standard publication).[1] VITA remains the only SDO to ever adopt a mandatory maximum royalty rate disclosure policy.[2]

I recently had an in-depth discussion with Ray Alderman — the then-executive director at VITA who conceived of and pushed the new policy through implementation — to get his 10-year retrospective on the disclosure policy, including the challenges he faced at the time, the factors that have made the policy a success for VITA over the past decade, and the reasons why such a policy is unlikely to ever emerge at another SDO.

What Spurred the Policy Change?

In the years leading up to its dramatic change in IP policy, VITA had wrestled with a handful of problematic patent holders. The worst were firms that failed to disclose that they held patents essential for a VITA standard, waiting until after the standard was finalized and implementers had begun commercialization before seeking high royalties, a strategy known as "patent ambush."[3] As the executive director, it was Alderman who bore the brunt of VITA members' complaints regarding other members' ambush tactics.

After suffering through the time and expense involved in dealing with two separate instances of patent ambush, Alderman sought a more permanent solution. He engaged Robert Skitol and Ken Vorrasi of Drinker Biddle & Reath LLP and the three hatched the plan to revise VITA's IP policy to include ex ante maximum rate disclosure. To give the new policy teeth, they also inserted terms spelling out that any failure to adequately declare maximum rates in a timely fashion (meaning within 30 days of the working group meeting implicating the member's patents) would result in the member having to license its patents on a royalty free basis. In other words, disclose it or lose it.

The Road to Adoption

Because most SDOs are composed of members that compete with one another in downstream markets — and VITA is no exception — Alderman, Skitol and Vorrasi sought antitrust review from the U.S. Department of Justice for VITA's tentative new IP policy terms. That process entailed the DOJ spending over 25 hours with Alderman and interviewing several VITA members, which took around six months. After conducting its due diligence, the DOJ required only modest changes to VITA's policy proposal, and in late 2006 VITA had a positive business review letter in hand.[4]

With the antitrust hurdle cleared, Alderman next had to gain approval from VITA membership. While VITA allowed the executive director to draft the policy on his own (with legal assistance), for the new policy to be implemented a majority of VITA's members had to approve it. Some members did indeed object to the policy change — after all, it was a significant move away from the former (and widely accepted) policy of committing to license standard-essential patents on fair, reasonable and nondiscriminatory, but otherwise unspecified, terms and conditions. After discussion, however, a majority of members did approve the change and the new policy was adopted in early 2007, a few months after the DOJ business review letter issued.

The approval process was still not complete, though. After VITA members voted to adopt the new policy, VITA then had to obtain approval from the American National Standards Institute. ANSI is the American SDO accreditation agency. With a new IP policy in place, VITA had to seek reaccreditation from the ANSI Executive Standards Council to confirm that the new policy conformed to ANSI guidelines on patent disclosure and licensing. Here, Alderman reports that the battle was more pitched, with a number of ANSI members opposed to any specific ex ante royalty rate disclosure. VITA managed to garner majority support at ANSI's Executive Standards Council, but the council's positive vote was appealed three times — the maximum allowable under ANSI rules — before VITA finally achieved reaccreditation in the spring of 2007.

VITA's Unique Characteristics Underlie the Policy's Decade of Success

The implementation process was clearly rocky, but Alderman reports that once in place the maximum rate disclosure policy has worked smoothly for VITA's members, with no further changes to the IP policy needed and no violations from members over the past decade. The policy's success appears to be due in large part to a number of factors that set VITA apart from other technology SDOs — and that also explain why VITA still stands alone in mandating ex ante royalty rate disclosure.

First, VITA is a relatively small SDO. It had a total of 120 members in 2017 and works on three to four new standards in a typical year, with less than 90 standards in total emerging over the past decade. In contrast, the Institute of Electrical and Electronics Engineers, the SDO that oversees the development of the Wi-Fi standard, has roughly 400,000 members, over 1,100 active standards, and over 600 standards under development in 2017.[5] Being small reduces the diversity of interests and objectives among VITA members, and makes trust and compromise easier to achieve.

Second, VITA has a relatively narrow technology focus. It concentrates on computing standards used in mission critical settings, such as configuring electronics to survive radiation in space for use in military satellite systems. This too diverges from the other SDOs that have made headlines with IP disputes. For example, IEEE covers a wide range of electrical engineering areas, from consumer electronics to nuclear power. Reinforcing the effects of its smaller size, VITA's targeted technology focus strengthens its members' shared goals and facilitates cooperation.

VITA's technology focus extends to implementer applications of its standards as well. Take Wi-Fi as an example once again. That standard is incorporated into a wide range of assorted products, including smartphones, tablets, laptops, desktop computers, and smart appliances like refrigerators and washing machines. VITA standards, on the other hand, tend to have one application only. This has important implications for royalty rate disclosure: the fewer the implementer applications, the more likely a single royalty rate will appropriately capture the value of using the patented technology. In contrast, standards with lots of diverse applications are more likely to require a different royalty rate for each application in order to be consistent with FRAND principles, making maximum rate disclosure both more complicated for patent holders and less informative for implementers. (As an added benefit, VITA's one-application, one-royalty-rate environment has enabled it to avoid the heated debate over component versus end product licensing that has engulfed much of today's SDO FRAND policy discussion.)

Next consider that the commercial markets for VITA standards are smaller than many other high profile SDOs, like IEEE or the European Telecommunications Standards Institute. Alderman estimates that VITA standards impact global markets on the order of $3 to $5 billion, whereas ETSI's mobile telecom standards implicate revenues of over $550 billion globally.[6] With that kind of money at stake, it is not surprising that mobile telecom firms fight hard over any IP with the potential to affect profitability.

Finally, the primarily military markets affected by VITA standards generally are not "patent rich." Alderman estimates that VITA has seen around nine to 10 patent disclosures over the decade that the maximum rate disclosure policy has been in place. He explains that most VITA members cross license any relevant patents they hold with other members as needed and do not rely heavily on IP to drive revenues. The limited reliance on patents stems in part from the fact that patent licensing can create major complications for the fixed-bid U.S. Department of Defense contracts that comprise the bulk of demand for many VITA standard implementations. This is again in sharp contrast to other industries with highly public technology standard disputes, like Wi-Fi and mobile telecom. For example, in a prior academic study I calculated that ETSI's 3G mobile telecom standard had over 14,000 unique patent declarations by the end of December 2010, and many of those declarations listed multiple patents.[7] But with less emphasis on patent licensing and more emphasis on end product revenues, the ex ante rate disclosure regime fits well into VITA members' business models and industry practices.

VITA IP Policy Limitations Are Key

Even with a relatively small group of relatively homogenous firms developing a relatively narrow set of technologies and operating in a largely cross-licensing oriented marketplace, there were still risks to VITA adopting a maximum royalty rate disclosure policy. That's where the specific limitations of VITA's policy come in.

One important safeguard is VITA's strict confidentiality rule. Only VITA members can view drafts of VITA standards while they are under development. VITA also uses digital watermarking technology so that any draft copy that does slip out can be traced back to the member that released it. And this year VITA expanded its draft standards documents to bind nonmembers as well, adding language along the lines of "if you read this document and you are not a member of VITA, you are still bound by all VITA policies." While these steps reduce VITA's standards development transparency, they work to limit the risk that an external third party could use a VITA draft standard document to write an ex post patent application tailored to technologies already under consideration.

Lastly, members' maximum royalty rate disclosures are also restricted to VITA members' eyes only. Members obtain disclosed maximum rates through a written request, which includes a commitment not to release or disseminate the rates to any other party. Furthermore, the disclosed maximum rate solely applies to the specific standard named and cannot be used to argue for a lower rate for any other standard, even when the underlying patents are the same. To that end, disclosed licenses include scope limitations noting that the licensing terms only apply to licensees making products compliant to a specific VITA standard. Nor can a VITA member's patent and maximum rate disclosure be used to force it to license any nonessential patents, trade secrets, or tacit knowledge. Alderman views these limitations as important safeguards ensuring balance between implementers and patent holders, protecting the former from patent ambush and ensuring that the latter can earn reasonable compensation for their patented inventions contributed to VITA standards.

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[1] For a copy of the policy, which has remained unchanged since it was adopted in 2007, see http://www.vita.com/resources/Documents/Policies/vso-pp-r2d8.pdf.

[2] Observe that VITA places no restrictions on the rates (or any other license terms) that any member discloses, only requiring that the firm announce its chosen maximum rates for rights to its patents as applied to the standard at issue. IEEE had a voluntary, but little used, rate disclosure policy.

[3] In the late 1990s and early 2000s, a number of antitrust matters involved patent ambush, the most famous being the FTC's long-running case against Rambus, first filed in 2002; see https://www.ftc.gov/news-events/press-releases/2002/06/ftc-issues-complaint-against-rambus-inc.

[4] https://www.justice.gov/atr/response-vmebus-international-trade-association-vitas-request-business-review-letter.

[5] As reported by IEEE-SA, IEEE Standards Association Announces Virtual Reality (VR) and Augmented Reality (AR) Standards Projects In Advance of Participation at Augmented World Expo, (May 9, 2017), available online at http://standards.ieee.org/news/2017/ieee_p2408.html.

[6] https://www.statista.com/topics/1147/mobile-communications/.

[7] Layne-Farrar, Anne, "Assessing IPR Disclosure Within Standard Setting: An ICT Case Study", in Modern Trends Surrounding Information Technology Standards and Standardization Within Organizations, Kai Jakobs ed., IGI Global, 2014.