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District Court Creates Roadmap for Determining RAND Licensing Rates for Standard Essential Patents

For the first time, a federal District Court has set the terms of a reasonable and non-discriminatory (RAND) licensing rate for standard essential patents. On April 25, 2013, the court in *Microsoft v. Motorola* issued an order establishing the RAND royalty rate for Motorola's patent portfolios, determining the patents were essentially worth pennies per unit, in contrast to Motorola's demand of approximately $4.50 per unit.[1] This determination may save Microsoft billions of dollars—having to pay approximately $1.8 million as opposed to the $4 billion Motorola demanded.

This decision is important because it provides a framework for future courts to determine a RAND rate. Central to the court's analysis was determining "the contribution of the patent to the technical capabilities of the standard and also the contribution of those relevant technological capabilities to the implementer and the implementer's products."[2] This analysis basically boils down to asking: (1) are the patents essential to any portion of the standards; (2) how much of a technical contribution do the patents make to the standard; and (3) how will the patentee's contributions to the standard be used by the implementer's product?

The *Microsoft* court, after extensive testimony by economics experts, created a "modified" RAND *Georgia Pacific* licensing analysis. In developing its modified *Georgia Pacific* factors, the court focused on three prevailing RAND issues:

- **Reducing the risk of patent hold-up.**[3] The court specifically noted Motorola could not claim the value of the standard/technology as a whole, only the incremental value its patents provided to the standard;

- **Mitigating royalty stacking.**[4] The court stated that hypothetical bilateral negotiations should not be conducted in a vacuum; they must take into account other licenses for similar standardized technology so that the licensee is not overburdened by "stacked" royalty rates;

[1] *Microsoft Corp. v. Motorola, Inc*., No. C10-1823JLR, Doc. No. 681 (W.D. Wash. April 25, 2013).

[2] *Id.* at 37.

[3] "Hold-up" is the patent holder demanding more than the value of its patented technology in an attempt to capture the value of the standard itself.

[4] "Royalty stacking" is where an implementer pays royalties to multiple standard essential patent holders on the same product.

- **Ensuring patent holders receive reasonable royalties on their intellectual property.** The patent holder still needs to be fairly compensated for its technology to incentivize future inventors into submitting their technology for adopting in a standard.

In this case, the court saw little value in Motorola's patents due to their limited contributions (if any) to the standards and their limited use by Microsoft's products. The minimal value the patents contribute to the standards drove the royalty rate offered by Motorola down from the dollars per unit to pennies per unit range.

In setting the actual value, the court relied heavily on patent pool royalty rates as comparable licenses. The court noted that pools try to strike a balance between setting a royalty high enough to get patent holders to join and low enough to ensure adoption of the standard. Finding that these characteristics aligned with the purposes of the RAND commitment, the court concluded the patent pools identified in this case were a strong indicator of a RAND royalty rate. In contrast, the court rejected Motorola's prior licenses as comparable because they were not generated under RAND principles.

Although the court's decision may act as a roadmap for future RAND rate disputes, it is likely to endure criticism by standard essential patent holders. Patent holders may believe the court's approach sets the royalty rate too low to provide a monetary benefit for the contribution of their patented technology to a standard. Nevertheless, the court's new factors, and explanation of those factors, provide potential licensees ammunition in challenging high royalty rate offers for standard essential patents. Further, by setting a specific roadmap for calculating RAND rates, licensors need to be wary of this framework or be subject to potential claims that it has breached its RAND obligations.

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