MAY 2008, RELEASE ONE

GCP
THE ONLINE MAGAZINE FOR GLOBAL COMPETITION POLICY

Standards and Market Power

Cecilio Madero Villarejo and Nicholas Banasevic

European Commission

WWW.GLOBALCOMPETITIONPOLICY.ORG

Standards and Market Power

Cecilio Madero Villarejo and Nicholas Banasevic*

I. INTRODUCTION

Standards play an increasingly significant role in the modern economy, in particular in the high-tech sector. They ensure that products in an increasingly inter-connected world can work together properly, and therefore allow companies to concentrate on producing innovative products to the benefit of consumers. However, standardization may also confer market power on an essential patent holder which he may not otherwise have possessed. This paper therefore examines what the associated antitrust implications are, and what lessons antitrust regulators and standards bodies might draw.

II. DO STANDARDS CONFER MARKET POWER?

Many of the standards cases currently in competition authorities' agendas center on the issue of whether standardization has "illegitimately" conferred market power on a company, or whether such market power can be unfairly exploited as a result of a company having its technology incorporated in a standard.[1]

* Cecilio Madero Villarejo is Director, Markets and Cases II: Information, Communication and Media, DG Competition, European Commission. Nicholas Banasevic is Deputy Head of Unit, Antitrust: IT, Internet and Consumer Electronics Unit, DG Competition, European Commission. The views expressed in this paper are the authors' personal views, and do not necessarily represent the position of the European Commission.

[1] For example, the Commission has issued a Statement of Objections in the *Rambus* case, in which it has been preliminarily concluded that Rambus is charging an ex post price that absent its prior deceptive

Standardization can confer market power on a company, but we do not believe that being included in a standard *in itself* does so. In our view, whether or not standardization confers market power depends on two main factors:

- First, it is important to look at whether it is commercially indispensable to comply with a particular standard. It may be the case for example that there are several standards in the market competing to gain commercial pre-eminence. In such a scenario, it is unlikely that an essential patent holder for any one of the standards in question would possess market power.
- Second, it is important to examine whether there is lock-in to the standard in question—in other words, whether it is realistically feasible to switch away from a standard to another technology.

Therefore, we would submit that standardization can confer market power on a company whose patent has been incorporated in a standard when it is commercially indispensable to comply with the standard in question, and when there is lock-in to the standard.

A related question is whether standardization confers an *incremental* degree of market power on an essential patent holder, in other words a degree of market power which absent the standard, an essential patent holder would not possess. If so, this would allow the essential patent holder to charge higher prices than he would otherwise be able to absent the standard.

---

conduct in a standards body, it would not have been able to charge. *See* Press Release, European Commission, Commission confirms sending a Statement of Objections to Rambus (Aug. 23, 2007), *available at* http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/07/330&format=HTML&aged=1&language=EN&guiLanguage=en.

Our view is that to determine this, it is important to examine the hypothetical ex ante competitive situation (i.e., before the standard was agreed). By way of illustration, imagine a standardization process where there are five technologies of roughly equal quality competing to be incorporated in a standard. If competition can occur on the basis of both technology and price, then the ex ante situation would be one where one of the five technologies is chosen with the price having been competed down to the competitive level. Now, imagine where competition on the price parameter had not been possible, as is primarily the case in most standardization bodies. In such a scenario, the essential patent holder of the technology that is chosen can be said to hold a degree of incremental market power as a result of the standard. This is because he is able to charge an artificially inflated ex post monopoly price as a result of being included in the standard that he would not have been able to charge ex ante. Conversely, one can also imagine a situation where, ex ante, there is a unique, pioneering, and innovative technology which has no alternatives. In such a scenario, the price that the patent holder can charge is the same ex ante and ex post, and hence there is no incremental market power conferred by the standard.

III. WHAT CAN STANDARDS BODIES DO?

Preventing companies from unfairly exploiting incremental market power that they have obtained as a result of a standard has been a challenge for standards bodies over the years. The most common tool has been the RAND (reasonable and non-discriminatory terms) commitment. In other words, companies that have their

technologies incorporated into a standard are obliged to give a commitment that they will license such technology on reasonable and non-discriminatory terms. The aim of such a commitment is laudable; conceptually, we see it as precisely aiming to constrain the charging of an artificially inflated ex post price by the essential patent holder simply by virtue of his being included in a standard. As such, the obvious benchmark for what is a "reasonable" price is what would have been the hypothetical ex ante situation.

However, because there may be practical difficulties in discerning what such a hypothetical ex ante situation would have been, there have recently been attempts by some standards bodies[2] to pre-empt the problem by allowing ex ante price competition for the standard. In other words, in addition to requiring ex ante disclosure of essential technology during the standardization process, companies are *also* required to disclose the (maximum) price they will charge for such technology if it is selected for the standard. As we have already highlighted above, this type of scheme can be beneficial, since it allows for competition between rival technologies on both quality *and* price. As such, the price is auctioned down to the competitive level before the standard is selected, and the problem of artificially inflated ex post pricing as a result of the standard is avoided.

We note that opposition to such schemes has been mooted in some quarters on the grounds of supposed antitrust concerns (e.g., because "discussing" price in such a collective standards forum should be taboo). We believe that such criticisms should not be used as a smokescreen to hinder the uptake of ex ante type schemes. In a scenario

[2] *See, e.g.*, VITA, *at* http://www.vita.com/vso-stds.html (last visited May 15, 2008).

where there are a number of substitute technologies competing to be chosen, we cannot see how "price-fixing" can be a relevant factor. Quite the contrary, since the schemes introduce a parameter of competition (i.e., on price) that has up until now not been present in standards bodies. Of course, if a certain scheme in question is simply a cover for some kind of cartel, then that would obviously be a problem, but that is then nothing to do with the nature of the scheme in itself.

IV. CONCLUSION

We have outlined how in certain circumstances, standards can confer on essential patent holders a degree of market power which absent the standard, they would not possess. In such situations, cases may naturally come under antitrust scrutiny, since a company may be able to charge artificially inflated prices. The ideal scenario is one where standards bodies adopt rules that prevent such issues coming to the fore. However, while we see clear potential benefits in the type of ex ante scheme that some standards bodies have recently adopted or are considering, we do not believe that it is the role of an antitrust regulator to prescribe a specific type of scheme to standards bodies. While it is of course imperative that a standards body's rules comply with competition law, industry knows itself best, and therefore should responsibly draw up the rules that are most appropriate to its needs.