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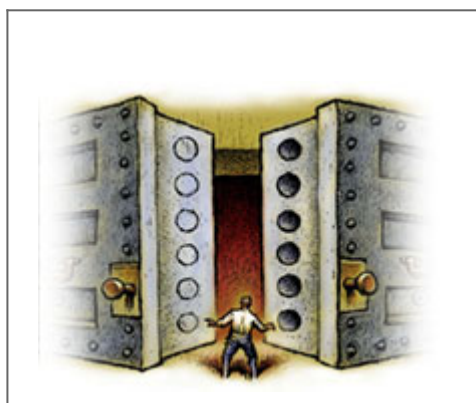
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The IP Conundrum

In late January, Intermec Technologies sent a letter to EPCglobal, the organization commercializing Electronic Product Code technologies, stating that it was no longer offering its RFID patents on a reasonable and nondiscriminatory (RAND) basis to other vendors making RFID tags and readers based on EPCglobal's Gen 2 standard. The move, while not surprising, has created lots of confusion in the marketplace.

Some believe Intermec's decision to negotiate royalties individually with companies that want to license its technology could threaten the industry. But before we get to that, we want to provide a little background and some perspective, which has been sorely lacking on this issue.

EPCglobal was established with the goal of creating an open standard for RFID tags that could be used to track goods within the global supply chain. EPCglobal wanted the standard to be made available on a royalty-free basis to companies that would make or use products based on the standard. In the end, EPCglobal agreed that if a company's



patents were needed for the Gen 2 standard, the company could choose to offer its patents either royalty-free or on a RAND royalty-bearing basis.

Intermec holds more than 100 UHF RFID patents. The company made five available royalty-free and offered the rest on a RAND basis (it claimed nine issued and five pending patents were used in the standard). Last August, Intermec spelled out the royalties it would charge under its RAND policy. It would require semiconductor manufacturers developing microchips based on the Gen 2 spec to make a royalty prepayment of \$750,000, which would be applied to a 5 percent royalty on unit sales. After royalties exceed the \$750,000 advance, manufacturers would be required to pay the 5 percent fee on unit sales for the life of the patent, with payments to be made quarterly.

When EPCglobal ratified the Gen 2 spec as a standard in December, it said the standard was royalty-free. Its position was that it was technically feasible to create Gen 2 tags and readers that did not infringe on any company's patents. They might not work well, but it was feasible. Intermec then wrote to EPCglobal in late January to say that since its patents were not part of the spec, it was under no obligation to offer them on a RAND basis.

Some commentators saw this as a big problem for the Gen 2 standard, believing that Intermec could put a gun to the industry's head and demand unreasonable royalties, which would make the technology expensive and therefore slow its adoption. Some vendors, who spoke to rfid journal on the condition of anonymity to avoid prejudicing negotiations with Intermec, said it was no big deal; technology companies are used to licensing intellectual property, and this was business as usual.

Clearly, end users would like the standard to be royalty-free, so the manufacturers' royalty costs aren't passed on to them. End users would also like to know they are not going to be sued for using technology that infringes on a company's patent. (Intermec stated that it has no intention of charging royalties to or suing end users.)

Even if Intermec had agreed to offer its patents on a RAND basis, that would not guarantee there would be no patent-infringement lawsuits. Patent policies created by standards-setting bodies are often vague about who must comply and for how long, which patents and patent applications are affected and the procedures for complying with the patent policy, according to Michael Farn, an associate at Fenwick & West, a law firm that deals with IP issues. Farn says that even if the policy isn't vague, most policies don't specify the remedy when obligations are breached, which means issues often wind up in court.

RAND licensing schemes don't guarantee that royalties will be low, either (see the box above). What RAND schemes do guarantee is that licensing fees are transparent—publishing the fees is usually a requirement—and that they are the same for everyone.

Now that Intermec feels it's no longer bound by the RAND requirements in EPCglobal's IP policy, two issues arise: how much manufacturers will have to pay to use Intermec's patented technologies, and which manufacturers will have access to those technologies. Intermec could choose to charge whatever it wants—and license its patents to whomever it wants.

But there might be benefits to some technology vendors if Intermec negotiates deals individually, rather than applying one policy to everyone in the industry. Small label makers, for instance, might find it hard to come up with the \$750,000 as a prepayment for royalties required under Intermec's RAND licensing plan, but they could potentially negotiate agreements with Intermec that exchange goods and services for the right to use Intermec's technology.

Perhaps the bigger question is whether Intermec might choose not to license its technology to some vendors. Intermec had sued Matrics, one of two original providers of EPC technology. Matrics was then bought by Symbol Technologies, which competes with Intermec in the bar code scanner market. In March, Symbol countersued Intermec. If Intermec wins the suit and chooses not to license its technology to Symbol, a major player would be shut out of the RFID market.

The fact is that patents are always a thorny issue for standards bodies, and RFID was never going to be an exception. There will be some uncertainty going forward, and there will likely be more lawsuits, if vendors decide to test Intermec's patents in court. But there's no reason to believe that the industry is significantly better or worse off now than it was when Intermec was offering its patents on a RAND basis.

What's Reasonable?

There's been a lot of discussion about reasonable and nondiscriminatory (RAND) licensing. Nondiscriminatory means that anyone who wants to can license the patents on the same terms as everyone else. That's clear. But what is reasonable?

Most patent laws around the world don't provide a definition. Sometimes standards bodies can work with vendors contributing their patents to a standard and agree in a dark, smoke-filled room what is reasonable. Sometimes two parties sue each other, and it's left to the courts to determine what's reasonable.

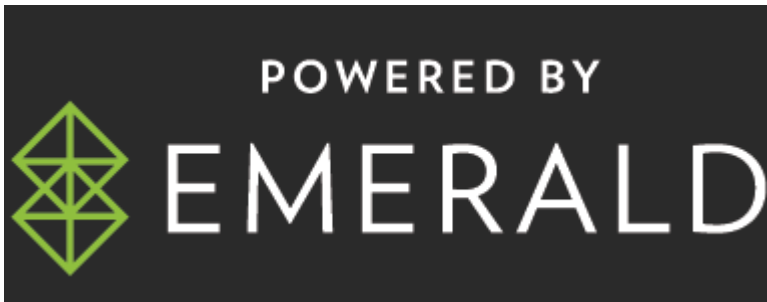
The licensing rates awarded by the courts differ from industry to industry. From 1990 to 2001, there were 21 cases in which U.S. district courts determined the appropriate licensing fee in disputes between computer and electronics manufacturers, and the average royalty was 10 percent, according to a report by PENTA Advisory Services, a consulting firm in Washington, D.C. The highest average royalty—14 percent—was in cases involving fabricated metal product manufacturers. The lowest was 3 percent, in food manufacturing.

In 37 of 93 cases where the courts awarded a reasonable royalty, the awards ranged from 6 percent to 10 percent. These cases all involved two parties. A patent attorney, who declined to have his name or firm identified, says that in cases where a standard is at stake, the courts will usually consider what impact royalty fees for patents in the standard might have on the market and end users. "If there is one patent holder, 10 percent might be a reasonable royalty," he says. "If there are five patent holders, giving each 10 percent would likely kill the standard."

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