Policy Paper PP10/11

Cabinet Office Procurement Policy – Use of Open Standards

Introduction

The Federation represents IP intensive companies in the United Kingdom – a list of members is attached. Our member companies are extensively involved with IP in Europe and internationally. Not only do our companies own considerable numbers of IP rights, both in Europe and elsewhere, but they are affected by the activities and IP rights of competitors. They may be either plaintiffs or defendants in IP related court actions, here and elsewhere.

The Government's policy

The Government has indicated that open standards should be sought whenever it is procuring IT equipment, according to the recent Procurement Policy Note on Use of Open Standards when specifying ICT requirements dated 31 January 2011. The note reads:

> When purchasing software, ICT infrastructure, ICT security and other ICT goods and services, Cabinet Office recommends that Government departments should wherever possible deploy open standards in their procurement specifications.

The advice applies to all Government departments, their agencies, and non-department bodies, and any other bodies they are responsible for.

IP Federation comments

1. The IP Federation shares the view that open standards can help to promote eGovernment interoperability and support responsive services for citizens and businesses. However, the Procurement Policy Note defines "open standards" in a manner inconsistent with market realities and industry practices. The policy thus threatens to undermine interoperability, impede innovation, and restrict the Government's ability to procure many of the most innovative ICT solutions. We believe that this preference could have negative effects on our members' businesses, particularly if NHS-operated hospitals copy this policy. Further, it seems in conflict with EU law.
2. The decision to define open standards as those in which IPRs are made irrevocably available on a royalty-free basis is misguided. The vast majority of recognised open standards developers require contributors to license IP on FRAND terms (with or without payment of a royalty). It has been demonstrated over and again that FRAND licensing policies enable and encourage innovative companies large and small to contribute their valuable IP to specifications, while at the same time ensuring those who want to implement standards can do so on reasonable terms.

3. By adopting this overly narrow definition of open standards, the UK policy will leave public authorities unable to procure many leading ICT products and services. A wide range of popular products implement standards widely viewed as open (i.e. FRAND-based), but that fail to meet the Policy Note criteria of irrevocably available IP. One recent study[1], for example, found over 250 standards implemented in a single laptop – three-quarters of which were developed under FRAND terms.

4. The UK preference also runs counter to fundamental principles of European procurement law. European procurement law is premised on ensuring that all equivalent solutions can compete in the marketplace and that decisions are made on best whole-life cost. To date, however, the UK has adduced no evidence to suggest that standards in which IP is made irrevocably available always offer best whole-life cost. Indeed, a recent study[2] from the Dutch Court of Audit concluded that the costs and benefits of open standards vary case by case.

5. Ultimately, the UK policy will distort the ICT marketplace in the UK. Currently, consumers – including Government users – use technologies that implement a mix of standards (open, royalty-bearing and royalty-free, proprietary) to achieve their interoperability goals. The UK policy will distort this vibrant ecosystem by discriminating against standards development models that permit innovators to charge a reasonable fee providing that their technology is made available on FRAND terms. This leaves innovators with two choices: contribute their valuable IP to standards free of charge, or opt out of standards setting. Unquestionably, some innovators will choose the latter option – resulting in less innovative specifications and, ultimately, less interoperability. At the same time, technology developers will move away from solutions that implement a mix of standards and toward solutions that rely on a smaller universe of "Government-endorsed" technologies – leading to reduced consumer choice.

6. The UK policy also sets a dangerous precedent for third countries. UK law and policy have long recognised that patents and other IPRs provide the market-based incentives and rewards necessary to drive investment in R&D and fuel the development of new technologies. The UK has consistently encouraged its trading partners to respect these principles as well. The Policy Note approach is inconsistent with this tradition – and unquestionably serves as an unhelpful model for third countries (like China) keen on utilising the innovations of UK industry without respect for IPRs.

   The UK policy also deviates from the corresponding EU policy to improve electronic cooperation among public administrations in EU Member States. This programme – known as ISA for "Interoperability Solutions for European Public Administrations" – takes a very practical approach in

[1] http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1619440

[2] http://www.courtofaudit.com/english/News/Audits/Introductions/2011/03/Open_standards_and_open_source_software_in_central_government

supporting administrations across Europe to communicate more easily. The relevant part of the EU policy[3] defines openness as follows in paragraph 5.2.1 (footnotes are as given in the EU document):

> If the openness principle is applied in full:
>
> - All stakeholders have the same possibility of contributing to the development of the specification and public review is part of the decision-making process;
> - The specification is available for everybody to study;
> - Intellectual property rights related to the specification are licensed on FRAND[4] terms or on a royalty-free basis in a way that allows implementation in both proprietary and open source software[5].

The EU policy thus explicitly allows for FRAND terms.

7. Many other EU policies also endorse the use of FRAND, including the Commission's ESO Guidelines[6], requiring ESOs (European Standards Organisations) to –

> ensure that standards, including any IPRs they might contain, can be used by market operators on fair, reasonable and non-discriminatory conditions (FRAND).

and DG Enterprise's communication, The Way Forward[7]:

> IP essential to the implementation of standards is licensed to applicants on a (fair) reasonable and non-discriminatory basis ((F)RAND), which includes, at the discretion of the IPR holder, licensing essential IP without compensation.

The UK policy runs in the exact opposite direction.

8. We encourage the Cabinet Office to revisit the policy in its upcoming Government Strategy on ICT – and, specifically, to bring the open standards definition in line with industry and EU understandings. More broadly, UK departments should be encouraged to make procurement decisions on the basis of merit.

9. At a minimum, the UK should conduct a broad stakeholder consultation and thorough Impact Assessment of the policy. The Policy Note was adopted without consultation with industry and, contrary to Government policy, without any analysis of its economic impact. Such an analysis should be undertaken immediately, and should set out the economic rational for the proposed policy (including the costs and impact of the new policy on UK industry and its impact on the Government's ability to procure from among the full universe of ICT solutions) and any evidence behind the assumption that a return on IPRs is incompatible with interoperability.

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[3] http://ec.europa.eu/isa/strategy/doc/annex_ii_eif_en.pdf
[4] FRAND: Fair, reasonable and non discriminatory.
[5] This fosters competition since providers working under various business models may compete to deliver products, technologies and services based on such specifications.
[6] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52008DC0133:EN:NOT
[7] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2009:0324:FIN:EN:PDF

Some further arguments

1. According to the BIS website[8], the Government wants -

   > to make sure that Britain is the best place in the world to run an innovative business or service - this is critical to the UK's future prosperity, our quality of life and future job prospects.

   We agree with the sentiment, but a precondition for achieving this objective is that investing in innovation makes sense: one must be able to collect benefits from innovation investments. Imposing royalty-free licensing does not help in getting a return on innovation investments and is thus at odds with the Government's own policies.

2. The Government wants to go for the lowest cost, which is indeed a primary object in procurement. However, as the total costs of ownership (TCO) in ICT are formed by two components, viz. acquisition costs and service costs, it does not make sense to only control the acquisition costs by imposing royalty-free licensing.

   Suppose two software packages A and B that are equally attractive as regards functionality:

   - If software package A has £100 acquisition costs and 5 years service costs of £100 each, the TCO = £600.
   - If software package B has zero acquisition costs because of royalty-free licensing but £150 yearly service costs, after 5 years the TCO = £750.

   Obviously, package A is the better choice, but it will not be selected because the ICT procurement specifications do not allow for package A to be selected.

3. If interoperability was a consideration behind prescribing royalty-free standards, there is another fundamental misunderstanding, as royalty-bearing licensing has not prevented the GSM standard and the CD standards from becoming enormously popular, so that royalty-bearing licensing is apparently no obstacle at all if the conditions are reasonable.

Conclusion

The members of the IP Federation trust that the Government will review this policy for using open standards whenever it is procuring IT equipment. It is essential that purchasing decisions should be based on merit and best whole-life cost, and that UK innovators who seek to license their IPR on fair, reasonable and non-discriminatory (FRAND) terms are not prejudiced in UK public procurement.

IP Federation
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[8] http://www.bis.gov.uk/policies/by/themes/innovation

IP Federation members 2011

The IP Federation (formerly TMPDF), represents the views of UK industry in both IPR policy and practice matters within the EU, the UK and internationally. Its membership comprises the innovative and influential companies listed below. It is listed on the European Commission's register of interest representatives with identity no: 83549331760-12.

ARM Ltd
AstraZeneca plc
Babcock International Ltd
BAE Systems plc
BP p.l.c.
British Telecommunications plc
British-American Tobacco Co Ltd
BTG plc
Delphi Corp.
Dyson Technology Ltd
Eli Lilly & Co Ltd
ExxonMobil Chemical Europe Inc
Ford of Europe
Fujitsu Services Ltd
GE Healthcare
GKN plc
GlaxoSmithKline plc
Hewlett-Packard Ltd
IBM UK Ltd
Infineum UK Ltd
Merck Sharp & Dohme Ltd
Nokia UK Ltd
Nucletron Ltd
Pfizer Ltd
Philips Electronics UK Ltd
Pilkington Group Ltd
Procter & Gamble Ltd
QinetiQ Ltd
Rolls-Royce plc
Shell International Ltd
Smith & Nephew
Syngenta Ltd
The Linde Group
UCB Pharma plc
Unilever plc
Xerox Ltd