



# Standardization and competitive advantage

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..... Several commentators have suggested lately that negotiation of licensing terms (particularly royalty-free licensing) during the standards setting process was likely to violate the antitrust laws. Apparently, the theory was that the conduct amounted to a price-fixing conspiracy. However, in recently granting a business review clearance to the American Welding Society (AWS), the Antitrust Division of the US Department of Justice approved the practice of a standards setting organization securing a waiver of intellectual property rights before standardizing on some patented technology.

### Department of Justice business review procedure

The DoJ explains its business review procedure in 28 CFR (Code of Federal Regulations) section 50.6. The procedure

permits an organization to request from the Department of Justice “a statement of the Antitrust Division’s current enforcement intentions with respect to” a proposed course of action. If the agency considers that the proposed action will not violate the antitrust laws, it sends a *clearance letter* to the organization so stating. Sometimes, the process involves negotiations and requests for additional information. Although not necessarily binding the government to refrain from suing the organization, the letter provides considerable comfort because the DoJ almost never sues anyone who has obtained such a letter. However, the letters always close with the statement

This letter expresses the Department’s current enforcement intention. In accordance with our

normal practices, the Department reserves the right to bring any enforcement action in the future if the actual operation of any aspect of the proposed standard proves to be anticompetitive in any purpose or effect.

### Background: Robotic welding cell technology

The American National Standards Institute (ANSI) accredits AWS as a standards developer. AWS members are manufacturers and users of welding equipment and supplies. The development of technical codes, standards, specifications, guides, and recommended practices related to welding is one of AWS’ principal activities.

This case involved a standard that would set specifications for assuring the interoperability of various devices that make up a robotic welding cell (RWC). An RWC consists of several devices that work together to produce a weld on an automated basis. For the RWC to weld, the devices in the RWC must communicate. Most welding equipment communications currently use dedicated wires, one per message type, bundled into a cable. Cables connect to the equipment with connectors that are unique to each piece, and unique to individual vendors’ preferences. Therefore, to put together an RWC, someone must act as an integrator and ensure that interfaces of the various devices are compatible with each other. Once an integrator has developed a solution for a particular set of equipment, changing any compo-



ment becomes expensive because each component has a unique interface, and because comparable component devices from other vendors have different interfaces.

Integrators and users currently incur high costs when replacing one component device in an RWC with a device from a different vendor. Moreover, specialty welding equipment makers might be obliged to implement several interfaces for their devices to meet different integrators' requirements. An AWS technical committee has been trying for several years to develop a standard interface specification to overcome the problem of nonuniform interfaces.

Two specifications were available. One, the DeviceNet system, was already in wide use. The other, ArcLink, was not in use at all, and was patented. Moreover, those in the industry already using DeviceNet might be unwilling to switch to ArcLink. Nonetheless, the AWS technical committee determined that ArcLink was technically superior. The owner of the ArcLink patents agreed to waive all intellectual property rights in connection with the specification's use and also to provide technical assistance to anyone interested in using ArcNet to implement the standard.

### **AWS asks for clearance to proceed**

Users of the DeviceNet system argued that basing the standard on ArcLink would give ArcLink's proprietor an unfair competitive advantage. AWS therefore asked the Antitrust Division for a business review clearance, based on the following assumptions:

Assuming that AWS adheres to the ANSI-mandated procedures, and assuming AWS has a reasonable and good-faith basis to believe, from a technical standpoint, that ArcLink is preferable as the basis for the specification, we request a statement of the Antitrust Division's current enforcement intentions should the Society proceed with the development of an interface

specification based on ArcLink rather than DeviceNet, even if adoption of the specification would give Lincoln [ArcLink's proprietor] a competitive advantage and even if the technology within the specification is not currently widely used in the industry.

Although AWS did not explain the competitive advantage, this is what was presumably involved: When a given technology becomes the basis for a standard, a company already marketing a product (such as a chipset) for implementing the standard with that technology has a marketplace advantage over other companies that have yet to develop a comparable product. For example, you can see this in the choice of technology and technical specification for the IEEE 802.11 standard for wireless local area networks.

### **DoJ's response**

The DoJ said in its 6 October 2002 response letter that it was not going to "bless a standard," or decide whether one technology was better or worse than the other. All it cared about was process. That is,

we look to see whether the process of standard setting has been abused to seek an unfair competitive advantage and whether the proposed standard is the product of any anticompetitive conduct on the part of the organization or its members. [To be sure,] there is always a possibility that adoption of any standard, by private or public entities, could have some adverse effect on some competitors.

But standards are also procompetitive in that they reduce costs and facilitate competitive entry. Consequently, the DoJ says, you must examine standards under a rule-of-reason analysis in which the potentially anticompetitive effects of a standard are balanced against its poten-

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tially beneficial effects. An antitrust problem exists only if the potentially anticompetitive effects outweigh the potentially beneficial effects.

### **Factors to consider**

The Antitrust Division said that it lacked the facts to determine whether in this case the balance tipped one way or the other. But it was prepared to address the points that AWS raised, and its position on standard setting in general is as follows:

The fact that the proposed standard is based on technology that is not widely used does not by itself render the proposed standard unreasonably anticompetitive. ... Nor does the fact that adoption of the proposed standard might give some producers some advantage over others automatically compel a conclusion that competition will be unreasonably restrained in the future.

More specifically in the case of the AWS proposal, the Antitrust Division was disinclined to challenge AWS by an antitrust enforcement action, based on the following factors:

- The DoJ is unaware of "any evidence that would lead us to conclude that the proposed standard is the product

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of any anticompetitive conduct on the part of the Society or its members.”

- It is unlikely that AWS has organized a cartel to restrain competition in RWC interface technology, because its membership includes both producers and consumers of RWC systems. It is unlikely that consumers of RWC technology would agree to “knowingly deprive themselves of reasonable competitive options.”
- Furthermore, there is no reason to think that some member has duped the AWS into creating an unfair competitive advantage for that member.
- AWS has adopted “standard-setting procedures [that] are open and transparent and its Committee has carefully considered the technological and competitive implications of adopting a standard based on the contending technologies.”
- Finally, “the owner of the intellectual property rights to be incorporated by the proposed standard has agreed to waive such rights in connection with adherence to that standard.”

In these circumstances, the Antitrust Division said it would presume that AWS and its members correctly determined “that the proposed standard would best serve consumer interests,” or at least it would not presume the opposite.

**What does this mean?**

Certainly, it is clear from the letter that the Antitrust Division does not object to what some commentators had been claiming raised an antitrust problem: a standards setting organization negotiating with a patent owner and agreeing to incorporate its patented technology into a technical standard if the owner agreed to royalty-free licensing. That is not a problem and actually weighs on the favorable side of the balance in granting a clearance.

To be sure, this leaves unstated what is reasonable and nondiscriminatory (RAND)

licensing at a preset rate. But the DoJ has granted other clearances—notably those for digital video discs—on patent pools for a technical standard in which patent owners collectively specified royalties at an allegedly low rate (say, 4 percent).

Therefore, you must view with some skepticism the claim that antitrust concerns arise when a standards organization negotiates royalty-free licensing or RAND as part of the standards process. Perhaps, in some circumstances, problems can occur, but addressing royalty terms is surely not an automatic no-no.

The remaining factors in my earlier list identify, at least by implication, what not to do. That is, because the absence of this conduct led the Antitrust Division to approve the AWS process, it would seem to follow that engaging in such conduct would raise eyebrows.

However, the letter reflects a curious approach to antitrust enforcement. It states that the Antitrust Division does not have the facts needed to balance the respective weights of the potentially anticompetitive effects and the potentially beneficial effects. Then, the letter says that the DoJ is unaware of enough factual evidence on which to base a conclusion of anticompetitive intent or effect.

Finally, the letter says that the DoJ will not presume that AWS and its members made an incorrect judgment about what best serves consumer interests. On the basis of that general state of ignorance, the Antitrust Division then grants a clearance assuring no likelihood of enforcement.

In the past, a general state of ignorance and an inability to determine likely intent or effect would lead the Antitrust Division to do nothing. You would expect the Antitrust Division to require convincing one way or the other for it to take any action at all. It seems to make little sense for the Antitrust Division to now say that when it doesn’t know what’s going on it will grant a clearance.

**Going out on a limb needlessly**

To some extent, granting the clearance ties the Antitrust Division’s hands in the future, despite the disclaimer about

reserving the right to bring an enforcement action if an anticompetitive purpose or effect surfaces later. At the very least, it would be embarrassing to sue the AWS after granting it a clearance. It is fair to say that the clearance letter encourages the organization to go ahead with its proposal. How could the Antitrust Division later justify pulling the rug out from under AWS? At a minimum, the Antitrust Division would have to show a substantial, unforeseen change in circumstances.

Given that potential enforcement liability, the Antitrust Division should just have said that in its present state of knowledge it does not have a basis for taking enforcement action, and that the proposed conduct is not obnoxious on its face. It should have made no promises, one way or the other, about what would happen if something ever relieved the DoJ of its now pervasive ignorance. That would have been more protective of the public’s interest in effective law enforcement if anticompetitive problems later arise.

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