

# Report on Issues Relating to Open Standards

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## Executive Summary

1. The adoption of open standards promotes competition in the market for software which uses those standards. The critical effect on competition in this regard being openness, rather than standardisation.
2. Standardisation and openness are separate concepts and should be dealt with separately. Openness alone should be sufficient to satisfy competition concerns.
3. Government purchasing decisions for data formats, or of applications which are locked to specific data formats, have impacts on the broader community. “Value for money” criteria have the potential to be biased towards an incumbent monopolist if:
  - (a) applied in relation to software locked to a closed standard; and
  - (b) no account is taken of the wider impact of the acquisition;and, in these circumstances the criteria can even be self defeating in the long run.
4. “Value for money” criteria can be sensibly applied on a purchase-by-purchase basis if the underlying data format is open, at least after a competitive environment has been established.
5. If the use of open standards is a means to the end of Government policy to promote competition then it is not appropriate for procurement to subvert that policy. Any failure to adopt an open standard must demonstrate consistency with the Government’s competition policy objectives. Therefore, any failure to adopt open standards should be accompanied by an alternative, funded, plan which achieves the desired policy objectives. A business case, compelling or not, should never be sufficient.
6. As a failure to adopt an open standard causes costs as a result of the impact on competition, those costs should be priced and charged to the infringing vendor.
7. Governments should prefer data formats in the following order (highest to lowest): open standards, open formats, closed standards, closed formats.
8. One way of achieving a migration to open standards is to require that vendors who fail to support open standards pay a migration fee as a percentage of the value of the contract awarded, that fee going towards migration of the vendors’ closed formats to open standards.
9. The use of agreements or covenants not to sue for the implementation of standards is the wrong way around. They require implementers to break the law, subject to an assurance that they will not subsequently be sued. For obvious policy reasons no Government should itself break the law, nor should it ever require its citizens to break the law, whether or not consequences follow. There are other problems with such covenants, such as: a failure to bind successors in title to the underlying rights; and that such covenants do not apply to criminal sanctions which might apply (particularly for copyright infringement). Governments should insist on positive licences in favour of implementers of standards.
10. Experience indicates that even the most seemingly difficult migrations of data formats are comparatively easy to achieve with the support of the relevant vendors. Such vendors must be given strong incentives to assist in such migrations.
11. Variants of RAND licensing are inappropriate. Such licences have historically discriminated against open source in the past, and *ad hoc* variations (eg free or zero fee) are not adequate. A licensing baseline should be established. That baseline should, at a minimum, permit any open source implementation.

## About the Author

Brendan is the principal of Open Source Law, a boutique legal practice based in Sydney Australia specialising in technology law, with a special focus on open source and free software. Brendan was entered on the roll of barristers and solicitors of the High Court of Australia in 1993. He worked as an employed solicitor for a little under 10 years, first at the Sydney offices of Mallesons Stephen Jaques, then at Gilbert + Tobin before establishing Open Source Law. Brendan is a past president of the NSW Society for Computers and the Law, and spent several years as an editor of its journal Computers and the Law. Brendan was a founding member and director of Open Source Industry Australia Limited and served as the chair of its board for its first five years of operation. Brendan is on the editorial panel of the Internet Law Bulletin and the International Free and Open Source Software Law Review. Brendan has spoken at international conferences on free and open source software and has provided advice to Government in relation to open source issues. In the course of the creation of version 3 of the GPL, Brendan provided advice to the Software Freedom Law Center on Australian law as it



applied to the proposed revisions. Brendan provides *pro bono* legal advice to the Software Freedom Conservancy and has been involved in GPL compliance work within Australia.

### **About this Report**

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## 1. Introduction

- 1.1 Open standards are beginning to receive attention from governments around the world. In the past, purchasing authorities have been content to adopt standards by default based on the functionality of the applications that were being acquired. This meant, in effect, that the choice of application dictated the storage format being adopted for the retention of government data. Invariably these formats were closed formats and, in a great number of cases, closed formats which were not standards.
- 1.2 Only after many years of accumulation of data in these closed, non-standard formats have governments begun to realise that the adoption of closed standards comes at a cost to interoperability. The use of closed standards has two immediate consequences: there is a lessening – or a total absence of – competition for the applications which rely on those formats with that lessening of competition resulting in higher prices and less innovation; and the adoption of closed formats is proxy for a mandate that citizens acquire specific third party software in order to deal with government. Such formats are also a roadblock towards government “open data” initiatives – any reworking of the data stored in a closed format requires a format-specific application. The requirement to use such applications adds cost but, more importantly, implicitly limits what reworking can be carried out to the capabilities of that application.
- 1.3 In this report we identify and comment on a small number of issues commonly encountered in discussions relating to open standards, particularly in the context of government. We assume for the purposes of this report that the promotion of competition is an end in itself. In this report we use storage formats as an example, but the arguments here may be equally applied to other means of data exchange or interchange such as APIs and protocols.

## 2. Competition Issues

- 2.1 Storage formats are subject to network externalities. That is to say, the more people using the storage format, the more valuable the storage format is to people. The presence of network externalities in respect of a good tends to preference first movers in the market. Later comers will always start at a disadvantage because even a small network of the first mover is more valuable than no network. Other things being equal, if two storage formats are equivalent, the first to market can be expected to dominate in the long term.
- 2.2 Where a customer specifies a storage format for a deliverable, the ability to deal with that customer becomes dependent upon the ability to provide the deliverable in that storage format. Where the mandated format is only implemented by one software suite, then the customer is, in effect, mandating the software that its suppliers must use in order to deal with it. Such mandates are bad because:
  - (a) they run the real risk of substantially lessening competition in the market for related software; and
  - (b) the functional limitations of the chosen software suite limit the value that the customer can derive from its procurement.
- 2.3 Mandating a closed format is equivalent to mandating the software which reads and writes that format. If an agency specifies that data is to be submitted in a closed format which is only implemented by a single vendor, the agency is, in effect, mandating that it will only accept bids from resellers in one form or another of that vendor. Mandating of an open format has no such impact on the software used because, by definition, an open format does not require that implementers have to deal with any particular person. Indeed, open standards can ensure full competition among suppliers for a technology despite a natural monopoly for that technology emerging.<sup>1</sup>
- 2.4 Mandating a closed format has a particularly adverse effect on Small and Medium Enterprises (SMEs) because they may lack the market power to force the format's gatekeeper to deal with them, or to do so on reasonable terms. As the format is closed, any SME will need to first negotiate in order to access it. However, the cost of negotiation has a disproportionate adverse effect on SMEs. For example, if they do not have in house counsel, they must hire negotiators at much higher spot rates, an often tenuous cash position means they have less tolerance for longer sales cycles (so a drawn out negotiation is harder) than large organisations.

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1 Ghosh, *An Economic Basis for Open Standards*, Report by FLOSSPOLs Project under the Sixth Framework Programme of the European Union



2.5 I note it is particularly important to recognise that the competition benefits arise primarily as a result of the availability of the format's related specification and the licensing terms which attach to it than other factors. For example, there are many formats which are standardised, yet are anti-competitive (video formats such as MPEG-2, for which there are no legal open source implementations are an example). We discuss competition issues relating to standards in the section on licensing of standards below.

### 3. What is Open

3.1 The question of whether a format is open or not ought to be determined by its effect in practice.<sup>2</sup> In the context of public procurement this means that the effect of the use of the format must be consistent with the procurement rules relating to non-discrimination and the promotion of competition. Storage formats which tend to advantage particular potential bidders should not therefore be considered "open".<sup>3</sup>

3.2 In my view, a format for which there exist potential implementers who must secure knowledge, data or permission directly or indirectly from a person or class of persons is not "open" in the sense used in paragraph 3.1. This is because if the format is mandated then a potential bidder must secure an agreement with a competitor in order to bid on the relevant work. This preferences the competitor, not only because they have what is, in effect, a veto right on the bidder's bid, but also because the negotiation process gives them information (being aware of bidder's position) and timing (not having to negotiate saves negotiation time) advantages. These advantages can be entrenched in any contract which is finalised. The entrenchment can occur through seemingly uncontroversial provisions tying fees to units sold, and then requiring sales reporting data, potentially in advance of the bidder's sale.

3.3 A format might otherwise be considered open, but the actual characteristics of the format may give such an advantage to one bidder as to be effectively closed. An example might be a seemingly open format which is of overwhelming size. Such a format might, as a matter of practice, only be able to be implemented by one large vendor. Another example might be a format which is specified in such detail as to be inextricably tied to the data representation strategy of a specific, complex application. While such a format might be openly licensed, again, as a matter of practice it might only be able to be implemented by the vendor of that specific application. Such formats should not be considered open.

3.4 These effects are independent of any cost charged for the ability to implement the standard and can still be present if there is no fee charged for the implementation. If the competitor refuses to deal there is no effective recourse for the bidder until such time as the competitor has sufficient market power to found a legal action. Ironically therefore, the absence of a right of action creates the incumbent's position. That said, if a per unit fee is chargeable for implementing the standard, it should not be considered open.

### 4. About "Value for Money" and its Misapplication

4.1 Government procurement can both create and reinforce a monopoly in goods and services which it is acquiring. Anecdotal evidence suggests that bureaucrats look at "value for money" type formulae and assess them against the cost to government on a purchase-by-purchase basis. This approach is acceptable in respect of goods and services which are easily substitutable (such as hammers, screws, cars etc). However in respect of goods which are specifically designed to prevent substitutability – eg closed storage formats it is an extremely hazardous approach, particularly given that they tend to be a natural monopoly. The reasons should be obvious:

- (a) the vendor of a product, when tendering to government can almost always underprice offerings which are subject to competitive effects – even when competitors are loss leading;<sup>4</sup>

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2 Ghosh, *An Economic Basis for Open Standards*, Report by FLOSSPOLs Project under the Sixth Framework Programme of the European Union

3 An argument about what constitutes advantage might be made, but would be unhelpful. A particular bidder might be "advantaged" because they have made use of an opportunity to skill up in the standard when others haven't. "Advantage" here needs to be considered within the broader context of competition policy and whether a particular advantage might reasonably be overcome by other potential bidders.

4 That is to say, if the supplier of another product is subject to competition they will not be able to price differently to government and the public. Any loss leading will only be effective in respect of the particular purchase. However, in the case of a closed format vendor, the benefits from loss leading continue to accumulate.



- (b) the government, bound by its bureaucrat's incorrect understanding of the value for money policy is required to purchase the vendor's product;
  - (c) government begins accumulating files in a closed storage format locked to the product;
  - (d) over time network effects enable the vendor to crowd out competitive offerings – in order to read government data, third parties must buy the vendor's product, in order to submit data to government third parties must buy the vendor's product;
  - (e) the vendor, now a monopolist, can charge what it likes to the rest of the community safe in the knowledge that, because of the preponderant use by government others have no choice but to acquire the product;
  - (f) ironically, over time the monopolist will even be able to charge the government more because of the its huge installed base and the previous elimination of competition.
- 4.2 Any “value for money” type criteria will be ultimately self-defeating if applied on a tender-by-tender basis to closed storage formats, or to software which uses closed storage formats. At best, a value for money approach in this way is a shifting of cost from government to a subset of the public, other than through the tax system (see Figure 1).
- 4.3 Value for money in this context needs to be calculated by reference to the broader impact of the acquisition on the community – or, more realistically, the likely impact on the broader community of a pattern of similar acquisitions (eg further purchases by government in order to read documents stored as a result of the initial purchase). If the storage format is open, then the presence of competition justifies a purchase-by-purchase consideration as there are no lock-in effects.



## Government Purchasing as a Form of Indirect Taxation

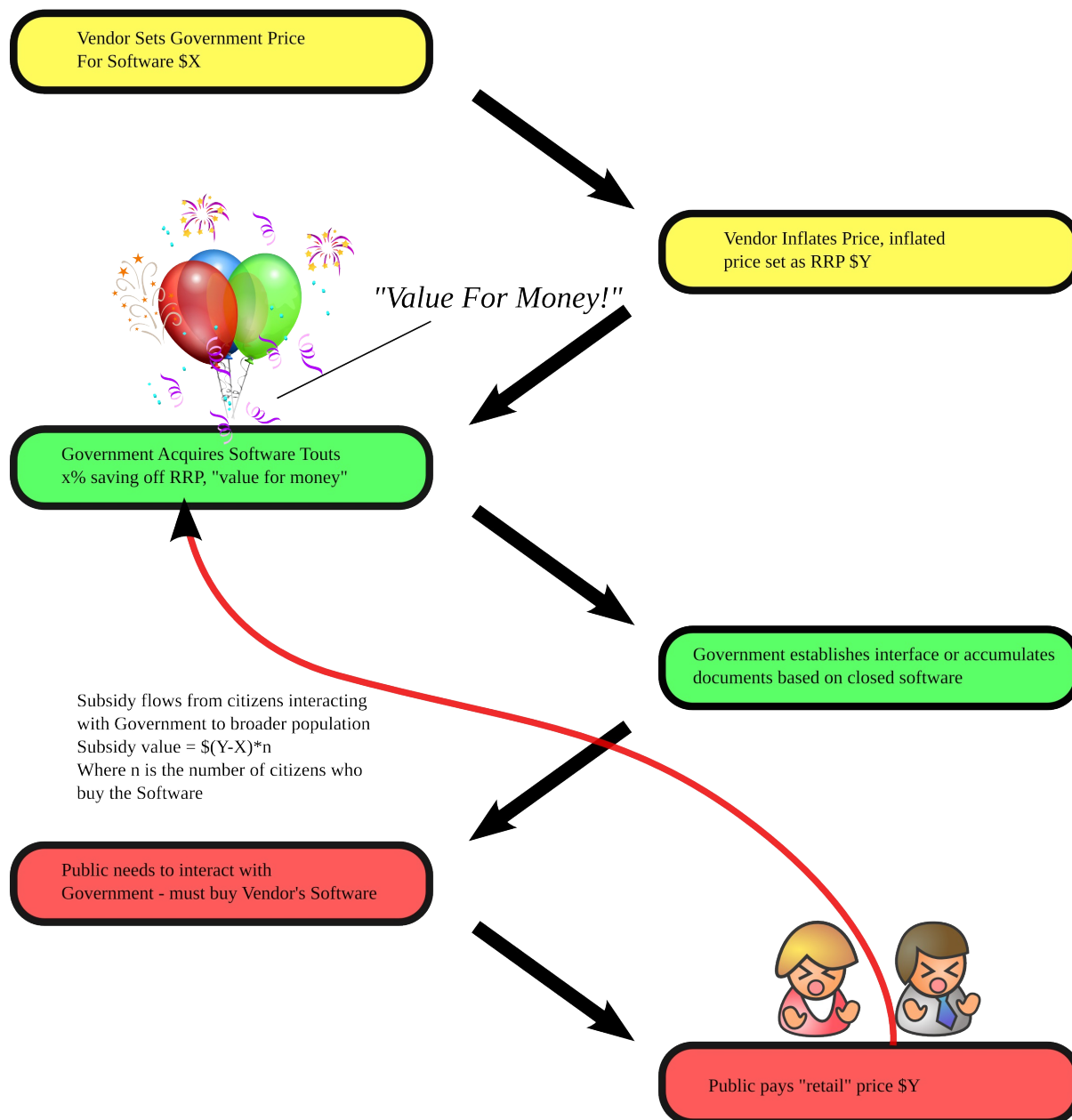


Figure 1: Broader Effects of Government Purchasing

### 5. About Formats and Data Standards

- 5.1 Open standards and open formats are often discussed together, sometimes being used interchangeably. However, whether a format is open and whether it is a standard are separate questions and ought to be treated separately. Requirements such as the forum in which the format is adopted and/or standardised do not go to whether the format is open *per se*. Nevertheless, these requirements will be very relevant in deciding whether to choose to adopt the format: formats which have the stewardship of a recognised standardisation body are more likely to be stable; those which have a transparent development process are more likely to cover expected use cases.
- 5.2 That said, as a matter of fact, government has historically adopted formats which have not been standardised (for example Word “.doc” files). All governments should acknowledge that, while open



standards are a desirable goal, practicalities will require the adoption of formats which are not standards from time to time. Where a policy proposes the use of open standards, but makes no provision for the case where there is no open standard, that policy will be implicitly promoting a lessening of competition.

## File Format Feedback Loop

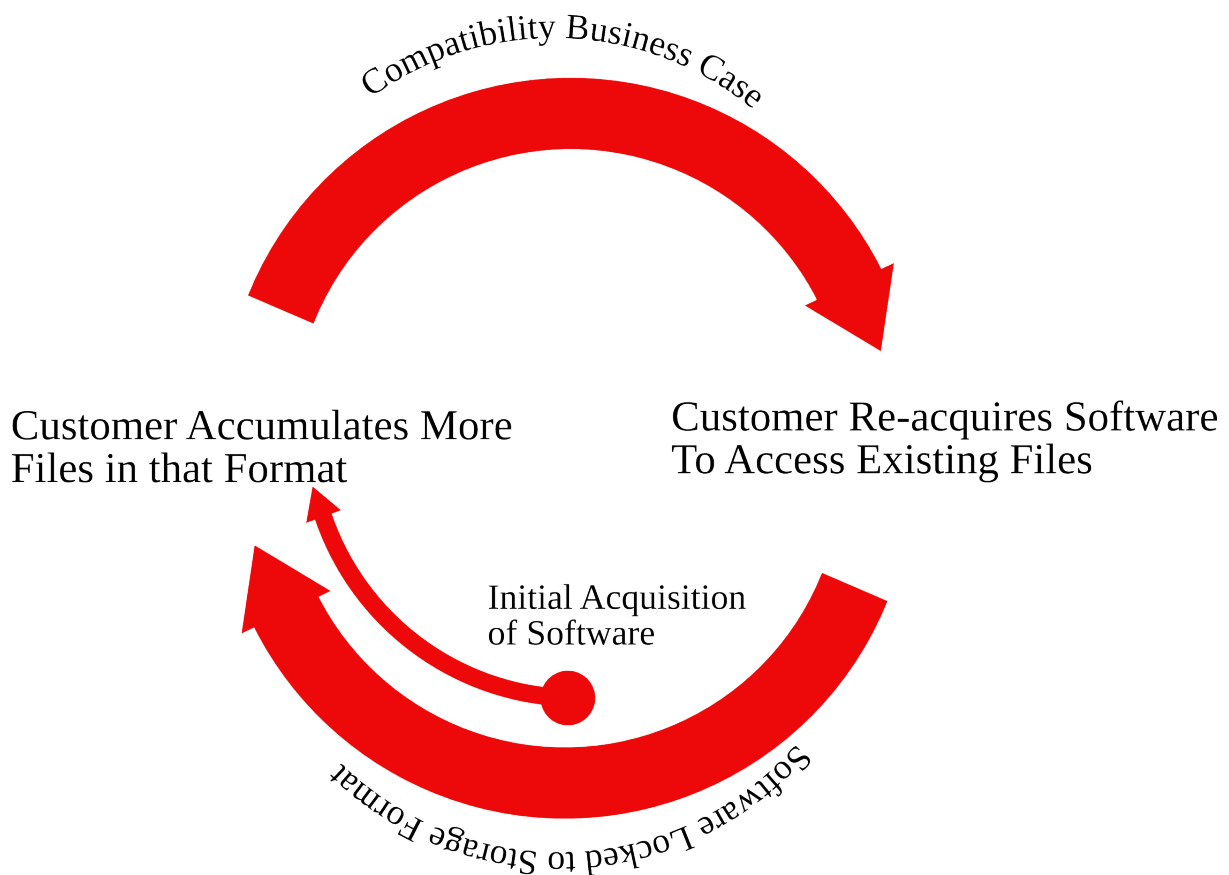


Figure 2: File Format Feedback

- 5.3 This arises because standards for data formats face a chicken and egg problem. Achieving standardisation is a comparatively long process which involves non-trivial commitment of time and money. In the absence of an application or applications which are saving data it is unlikely that there will be support for establishing a standard for that data format. In most cases then, any standard must be preceded by one or more applications. A corollary is that whenever any new application is created, it is very likely that the data format used by that application will not be a standard. Being aware of the anti-competitive effects of closed formats, applications providers will tend to prefer closed formats that they are able to control, especially if they have power in the market for that software or software of that type. However, this is only a decision by the vendor. A government acquiring the software could influence the vendor to make the format open. Therefore a failure to prioritize open over closed formats will tend to lead to a failure to implement open formats. This, of itself, reduces competition. However, there is also a knock on effect in that it reduces the pool of open formats which can be submitted to a standardisation process.
- 5.4 Thus, for any relatively new application which uses a closed format there will be a self evident business case to the effect that, because the application is new there is no standard data format. Therefore, there is no open standard and thus the relevant agency will be justified in adopting the application and its associated closed format. The government will acquire the software using the closed format and begin accumulating data in the closed format. When it comes time to renew the contract, even if there are competing applications which implement an open standard the need for continued access to those files





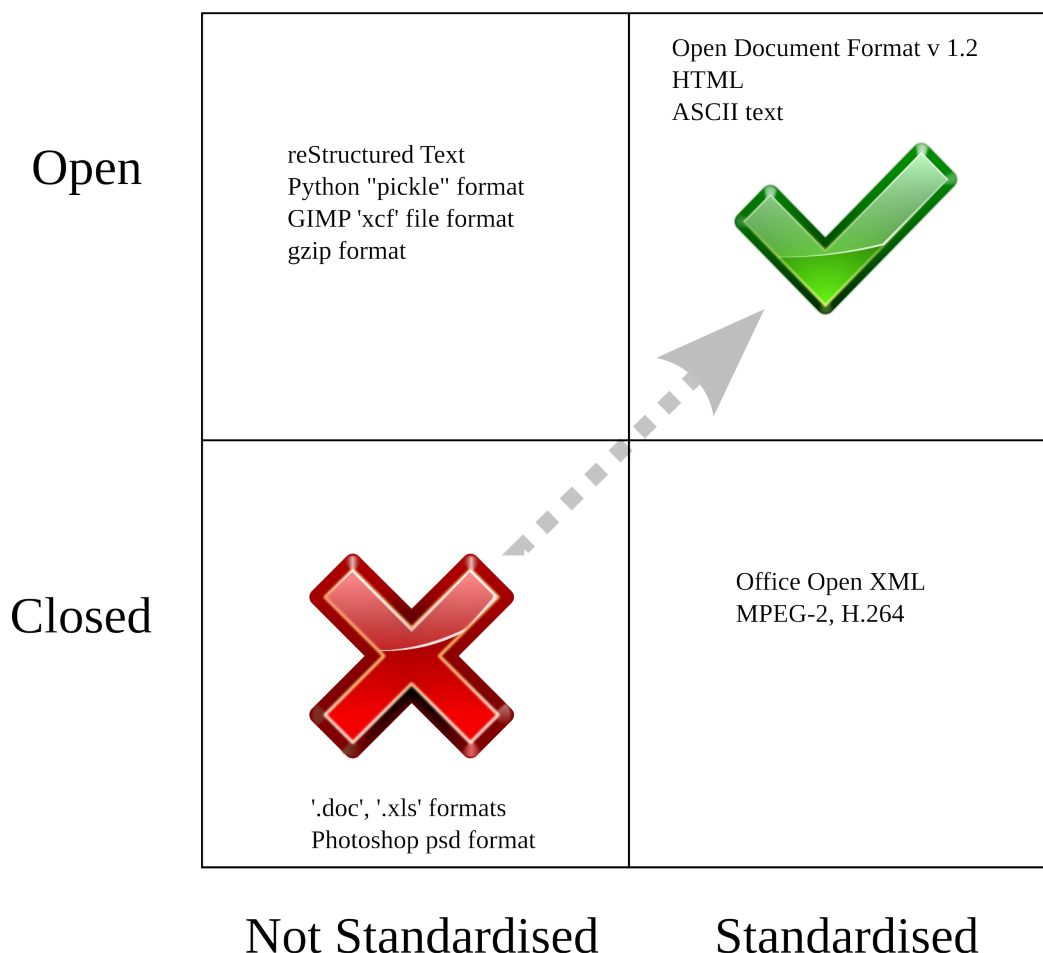
already accumulated in the closed format will still provide a compelling business case to again avoid the open standard. The adoption of the closed format will create a self-perpetuating feedback. The only time that the government will force a move from the closed format is when the costs become unbearable. In the meantime the government, and any who have to do business with government, will be paying higher prices and having lower functionality as a result of the lack of competition that comes from lock in.

## 6. Exceptions to Open Standards Recommendations

- 6.1 Government recommendations to use open standards are not an end in themselves. Rather, they are a means to the end of implementing government competition policy. It follows therefore that any failure to adopt the recommendation in a particular instance must still remain consistent with government policy. Thus, for example, provision of clear business reasons for not following such a recommendation cannot, of itself, be justification for avoiding the recommendation. That there may exist a business case against the use of open standards or open formats is not to the point. There can be no business case for overriding government competition policy. On the contrary, if the use of open standards as a means is not appropriate in the circumstances, then a different means must be proposed.
- 6.2 In my view a tiered approach to data formats is a better solution, with preference for data formats of the following types in order (see Figure 2):
  - (a) open standard
  - (b) open format (not standardised)
  - (c) closed standard
  - (d) closed format (not standardised)
- 6.3 In each instance, a case would need to be put why the preferred level could not be achieved. More importantly, a price should be put on the damage done to competition from the adoption of the format. This can be achieved by requiring that any use of a format other than an open standard should have a **migration plan, a budget and a funding plan** in place to migrate the application to an open standard. Such migrations could (and probably should) be coordinated at a whole of government level.



## Data Formats Grid



\*Note: open formats which are not formally standardised nevertheless may be informally standardised through mailing lists etc

Figure 3: Migration Path from Closed to Open

- 6.4 Migrations could be funded by implementing an earmarked migration fee for procurements involving a non-open or non-standard format. If a vendor tenders to government with an application which does not support open standards, the procurement agency tasked with running the relevant tender would add a migration fee, payable by the vendor to the procurement agency, to be applied in the migration of data formats from closed non-standards to open standards. Such a fee would be applied on a sliding scale as a percentage of the acquisition cost. Thus, a procurement of software which used a closed format might pay a larger percentage of the acquisition cost as a migration fee, while software which used a closed standard might pay a lesser percentage. The vendor would also need to agree to implement a plan to migrate off its closed format.
- 6.5 Ideally a migration fee will be priced to reflect the additional cost to the government and to the community as a result of the use of the closed format. Thus, for example, if a vendor provides a low cost version of their application to government in the knowledge that it will be able to charge higher fees to the general community who want to exchange data with government, then the migration fee ought to be greater than that extra cost to the community.
- 6.6 A mere requirement, for example, to provide a clear business case imposes only the most negligible of costs on the non-complying vendor (that is, the cost of preparing the business case). This bears no relationship to the damage to the community from the loss of competition as a result of the use of the format, nor the increased cost to government from that lessening of competition, nor of the migration



costs that will be incurred by the government in maintaining data in that format. Such a requirement will have no noticeable effect on increasing competition.

- 6.7 I acknowledge that, realistically, a government is unlikely to impose the real cost of adopting a closed format on a vendor. Nevertheless, the government ought to explicitly acknowledge that cheap pricing for government departments is not always in the interests of the broader community if those cheap prices are, in effect, a form of cost shifting from government to the private sector.

## 7. Covenants not to sue

- 7.1 It has been argued that implementation rights can be adequately addressed by a promise of non-assertion from relevant rights holders. Such an approach is unacceptable for three reasons:

- (a) first, government cannot be endorsing illegal acts. Patent and copyright legislation makes it clear that doing any of the acts comprised in the patent or copyright without the permission of the rights holder is an infringement and, therefore, an illegal act.<sup>5</sup> Legal structures of the form of “non assertion” or “covenant not to sue” assume that there is an infringement for which civil action will not be taken. This effectively assumes that breaking the law is justified if no consequences follow. This is not the case. Breaking the law is bad whether or not you get sued. Moreover, the government itself would be breaking the law. However pragmatic it seems, it would raise obvious ethical issues for a solicitor, as an officer of the court, to give advice to break the law. The government should not be requiring or endorsing illegality as a condition of dealing with government. It is relevant to note that where exceptions seemed relevant, the legislation<sup>6</sup> specifically establishes compulsory licences in favour of government rather than merely absolving government of liability;
- (b) second, licences are typically binding on successors in title to the relevant rights.<sup>7</sup> Such binding effects are specifically established under the legislation and will not apply to “covenants”, “agreements” or “promises” not to sue. Therefore, being rights *in personam* they will not bind successors in title. For example, if someone sells a patent covering a standard, people implementing the standard may be exposed to patent suits from the new owner.<sup>8</sup> While we are familiar with the use of the word “covenant” to establish a right *in rem* which runs with real property, we are not aware of any law which would have that effect in respect of the word “covenant” when used in respect of patent and copyright rights.
- (c) third, rights holders are not competent to give such an assertion in respect of criminal actions. Criminal actions can be brought even against the express wishes of the property holder whose rights have been infringed. While patents legislation typically doesn't include offences for “mere” infringement, it does not follow that this is the case in other jurisdictions, nor that offences won't be introduced into the legislation in the future, particularly given the legislative history and IP rhetoric of the past decade. Further, the copyright legislation contains many offences relating to the infringement of copyright which can apply to the implementation of a standard.

- 7.2 Non assertion promises and covenants not to sue are entirely unacceptable in this context. There is a perfectly viable solution in the provision of a licence by the relevant rights holder.

## 8. Document Migration is Easy, but Vendor Commitment is Crucial

*“Hamlet: Madam, how like you this play?”*

*Queen: The lady doth protest too much, methinks.”*

*Hamlet,<sup>9</sup> Act III, Scene II*

- 8.1 Much has been said from time to time of the difficulty posed by accumulated files in closed formats. These files are used as a justification for continuing to buy the same software that created them because the need to have continued access to them is important and migration to a new format is presumed to be overwhelmingly difficult.

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5 See, for example section 60 of the Patents Act 1977 (UK),

6 Eg: the *Patent Act 1977* (UK) and *Copyright, Designs and Patents Act 1988* (UK).

7 See, for example section 196(4) of the *Copyright Act (Cth) 1968*.

8 The previous holder has promised not to sue, but the new holder has made no such promise.

9 <http://www.gutenberg.org/ebooks/1524>



- 8.2 While application vendors may present as if migration of legacy files provides insurmountable obstacles, experience provides obvious counterexamples. The obvious candidates in this regard are the transitions between the storage formats used by Microsoft Word, the first occurring with Word 97 (a version of the doc format which was not backwards compatible)<sup>10</sup> and the second with the release of Microsoft with Word 2007 (to .docx/OOXML). In each case, with a willing vendor, the transition was achieved with minimal disruption despite having perhaps the largest, most widespread store of files in the legacy format across a vastly heterogeneous pool of users.
- 8.3 In each case the most recent version of the program stored its documents in a format which earlier versions of the program could not read. Thus, a user of Word version 6 could not read a document saved by a user of Word 97. Migration problems were largely solved by the vendor:
- (a) providing converter and viewer applications for earlier versions; and
  - (b) setting the default format for saving in their application.
- 8.4 For any large scale migration, the per user cost of providing converter and viewer applications will be small. Similarly, there is negligible cost involved in varying a program so that a certain format is used as the default format when saving (even if only eg for those customers which request it).
- 8.5 The sheer scale of the migration achieved in these cases dwarfs, by several orders of magnitude, any migration that any individual government might choose to undertake. Despite these migrations being of such magnitude, they were achieved with no substantial difficulty. To argue that a format migration on the scale of only a single government, even the whole of that government, would be a substantial problem is not credible.
- 8.6 There is one and only one roadblock to any format migration. That roadblock is the reticence of the incumbent vendor. Vendors in the past have used their own market position as a reason to not assist in any such migration arguing, for example, that there is no “market demand” for the support of alternative formats. The irony of such claims should not be lost on us.
- 8.7 Unfortunately, any incumbent vendor is aware that assisting in a migration will break the advantage gained from the format lock in. They are therefore in a position to be willing to “bet the farm” on refusing assistance. Government will therefore be put in a position of brinkmanship in order to implement an open format. If Government is honest about moving to an open format it must be in a position to stare down such brinkmanship. This includes being willing to adopt an alternative application, possibly of sufficient, but lesser, functionality, if the incumbent vendor will not assist in migrating to an open format.
- 9. Licensing Conditions for Standards**
- 9.1 In some quarters there are suggestions that the adoption of standards subject to Reasonable and Non-Discriminatory (RAND), Fair, Reasonable and Non-Discriminatory (FRAND) or Reasonable and Non-Discriminatory, Zero fee (RANDZ) terms for the implementation of a standard will be acceptable. Under such schemes the relevant rights holder chooses the licence terms which apply to the standard, subject to the reasonable and non-discriminatory requirements.
- 9.2 Such arrangements are bad in general because they are, at best, meaningless and possibly misleading. The most obvious example is that of “RAND” licensed standards which carry a per unit fee, the instances of which are manifold. Such standards cannot be implemented as open source because open source licences preclude the payment of a licence fee. Despite being canonical examples of “reasonable and non discriminatory” terms, such terms clearly discriminate against open source implementations.
- 9.3 This is not a problem that can be solved by adding a “zero fee” rider to the licensing terms. Such riders are an *ad hoc* solution to a particular instance of discrimination and provide no redress in respect of other forms of discrimination. Indeed, such riders are bad in that they validate the core discrimination. The means of discrimination are manifold and a full taxonomy is impossible. However, they can include licence terms which:
- (a) require implementation of the whole or large parts of the standard for validity (if the standard is large, this discriminates against small implementers which may only have a niche need);

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10 Now called the “Word 97-2003 Binary File Format”



- (b) become invalid if the standard changes or only apply to the most recent version of the standard (discriminates against pre-existing implementations);
  - (c) require notice of licensees or other downstream accounting requirements (open source implementations cannot comply with this requirement);
  - (d) have purpose based restrictions or fees, eg: fee payable for commercial use, but free for web or personal use (open source implementations cannot comply with this requirement);
  - (e) have procedural requirements for validity such as clicking an accept box (again, an open source implementation does not necessarily have control of the user interface).
- 9.4 There is an additional problem in that the formats might be standardised, but the terms are not. Thus there is no baseline for what a person seeking to implement the standard can expect of the terms.
- 9.5 Allowing RAND/FRAND/RANDZ standards not only fails to resolve the issue but shifts the non-discriminatory argument onto the implementers who may not be in a position to take the point (eg open source implementers). Permitting RAND/FRAND/RANDZ terms is not sufficient. To be acceptable, there must be a baseline for the licensing terms. At a minimum that baseline should be that the licensing terms applying to a standard must permit all open source implementations of that standard.