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***Huawei*: Establishing the Legal Standard for a FRAND Defense as a Basis for Resisting Requests for Injunctive Relief for Infringements of SEPs Under Competition Law**

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I. INTRODUCTION

On July 16, 2015, the Court of Justice (“CJEU”) handed down the eagerly anticipated preliminary ruling concerning the circumstances in which a (presumptively dominant) standard essential patent (“SEP”) holder who has given a commitment to license on fair, reasonable, and non-discriminatory (“FRAND”) terms may seek injunctive relief without infringing Article 102 of the Treaty on the Functioning of the European Union (“TFEU”).²

Despite creating antitrust liability for a type of conduct which hitherto had not been considered as capable of producing anticompetitive effects, the judgment confirms that a SEP holder who has given a FRAND commitment does not abuse a dominant position by seeking an injunction against a recalcitrant implementer who refuses to negotiate a license on FRAND terms, employs dilatory tactics, or makes a licensing counter-offer that is not on FRAND terms.

The CJEU’s ruling relates to a reference, pursuant to Article 267 TFEU, from the Landgericht Düsseldorf (Germany) in April 2013 in the context of litigation between Huawei and ZTE.³ Huawei had sought an injunction in respect of alleged infringement by ZTE of a patent declared by Huawei as potentially essential to the 4G LTE standard and which, should it prove to be actually essential, Huawei had committed to license on FRAND terms.

The reference sought to resolve a perceived conflict between the relevant German case law (the *Orange-Book-Standard*⁴ ruling of the German Supreme Court) and the novel legal standard proposed by the Commission in its *Motorola* and *Samsung* decisions creating antitrust liability for SEP holders; more precisely, the proposed approach of the Commission as set out in the press release announcing that it had sent a statement of objections to Samsung (¶34). In this context, the CJEU was asked to explain:

[i]n what circumstances the bringing of an action for infringement, by an undertaking in a dominant position and holding an SEP, which has given an undertaking to the standardisation body to grant licences to third parties on

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² Preliminary Ruling of 16 July 2015 in *Huawei Technologies Co. Ltd. v. ZTE Corp., ZTE Deutschland GmbH*, Case C-170/13 EU:C:2015:477 (“*Huawei*”).

³ See Landgericht Düsseldorf, Beschluss vom 21. März 2013, Aktenzeichen: 4b O 104/12 / Regional Court of Düsseldorf, Decision of 21 March 2013, File No. 4b O 104/12.

⁴ Judgment of 6 May 2009, KZR 39/06.

FRAND terms, seeking an injunction prohibiting the infringement of that SEP or seeking the recall of products for the manufacture of which the SEP has been used, is to be regarded as constituting an abuse contrary to Article 102 TFEU (¶44).

II. TEST FORMULATED BY THE CJEU

The CJEU held that the “particular circumstances of the case,” i.e. when (i) the patent at issue is “essential ... rendering its use indispensable to all competitors which envisage manufacturing products that comply with the standard ...,” and (ii) the SEP holder has given an “irrevocable undertaking [...] to the standardisation body in question, that it is prepared to grant licences on FRAND terms,” “justify the imposition on the [(presumptively dominant) SEP holder] of an obligation to comply with specific requirements when bringing actions against alleged infringers for a prohibitory injunction or for the recall of products,” (¶59). Importantly, the CJEU also set out a number of obligations for implementers/infringers.

In these circumstances, the CJEU ruled that seeking (and presumably obtaining and enforcing) an injunction in respect of the alleged infringement of an SEP will not constitute an abuse of a dominant position “as long as” the following procedure is complied with:

- Prior to bringing an action for an injunction or product recall, the dominant SEP holder has “alerted the alleged infringer of the infringement complained about by designating that patent and specifying the way in which it has been infringed” (¶71).
- Where the alleged infringer has then “expressed its willingness to conclude a licensing agreement on FRAND terms,” the SEP holder has then to present a “specific, written offer for a license on [FRAND] terms,” specifying the royalty amount and calculation methodology.
- In the event that the alleged infringer does “not accept the offer made to it,” then “it may rely on the abusive nature of an action [...] only if it has submitted to the [SEP holder], promptly, and in writing, a specific counter-offer that corresponds to FRAND terms” (¶66).
- Where the alleged infringer “continues to use the patent in question,” it may not rely on the alleged abusive nature of the action if “has not diligently responded to that offer, in accordance with recognised commercial practices in the field and in good faith, this being a matter which must be established on the basis of objective factors and which implies, in particular, that there are no delaying tactics” (¶65).
- If the counter-offer does not lead to the conclusion of a license, “it is for [the] alleged infringer, from the point at which its counter-offer is rejected, to provide appropriate security, in accordance with recognised commercial practices in the field, for example by providing a bank guarantee or by placing the amounts necessary on deposit. The calculation of that security must include, inter alia, the number of the past acts of use of the SEP, and the alleged infringer must be able to render an account in respect of those acts of use” (¶67).
- In addition, “where no agreement is reached on the details of the FRAND terms following the counter-offer [...] the parties **may, by common agreement**, request that the amount of the royalty be determined by an independent third party, by decision without delay” (¶68, emphasis added).

III. DEPARTURE FROM SETTLED CASE LAW

The CJEU appears to have considered incorrectly that a request for an injunction is analogous to a refusal to license. In addition, the standard adopted by the CJEU is a departure from its well-established and settled case law (*Volvo*, *Magill*, *IMS Health*, etc.) in this regard, according to which, “the exercise of an exclusive right linked to an intellectual property right by the proprietor may, in exceptional circumstances, involve abusive conduct” (¶47). Presumably recognizing that the facts before it could not properly be considered as “exceptional,” the CJEU adopted a different standard of “particular circumstances” instead of concluding that there was no abusive conduct.

While the CJEU appears to have diluted, if not contaminated,⁵ the applicable test, it does so only in circumstances where: (i) prevention from using the patent at issue would “compromis[e] the essential functions of the product in question;” and (ii) through recourse to an injunction, the holder of the patent in question “can prevent products manufactured by competitors from appearing or remaining on the market and, thereby, reserve to itself the manufacture of the products in question.” Accordingly, the “particular circumstances” still require proof of the foreclosure of rivals. These particular circumstances apply only to a limited subset of SEPs and SEP holders, and would not be satisfied if the SEP holder was not also present on the downstream market for products that comply with the standard. In this context, the CJEU refers to the fact that the SEP holder “can prevent products manufactured by competitors from appearing or remaining on the market and, thereby, reserve to itself the manufacture of the products in question” (¶52).

Given that the conduct at issue concerns allegedly abusive use of the processes of EU national courts, it is disappointing that the ruling from the EU’s highest court ignores the established EU competition law standard on abusive litigation set out in *ITT Promedia* and *Protégé International*,⁶ even if only to overrule or distinguish it. It is curious that such seemingly relevant precedent was deemed implicitly not to apply in the “particular circumstances” of SEP litigation.

In this context, it would seem that the CJEU has also conflated the questions of when an injunction should be granted with when it would be abusive merely to seek injunctive relief from a national judge.

Departing from its established case law, the CJEU has designed a novel legal standard that firms involved in licensing will likely find both incomplete and divorced from reality, and which will result in significant uncertainty.

IV. THE CJEU’S FORMALISTIC AND STYLIZED TEST IS DIVORCED FROM REALITY

The stylized and formalistic negotiation process envisaged by the CJEU assumes that SEP holders assert, and infringer/implementer license, SEPs individually and, hence, ignores entirely

⁵ The CJEU distinguishes the present case from the *Volvo*, *Magill*, *IMS Health* etc. line of cases rather than recasting the applicable legal test.

⁶ Judgment of 17 July 1998 in *ITT Promedia v Commission*, Case T-111/96 EU:T:1998:183; and judgment of 13 September 2012 in *Protégé International v Commission*, Case T-119/09 EU:T:2012:421.

issues of portfolio and cross-licensing, both common and pro-competitive practices in the industry.

Equally, the CJEU presupposes, incorrectly, that the first offer will necessarily be made by the SEP holder and considers, naively, that offers and counter-offers are detailed and made in neat, written form.

In addition, the CJEU process entails a single offer/counter-offer, rather than an ongoing back-and-forth negotiation, and hence gives no clear guidance on the role of injunctive relief as a means to resolve a stalemate. The only relevant discussion is found at paragraphs 67 and 68, which refer to (i) the alleged infringer providing “appropriate security” such as a bank guarantee or payment into escrow; and (ii) the option of third party determination “by common agreement.” Yet, given the CJEU’s unequivocal statement that a (presumptively dominant) SEP holder “does not abuse its dominant position [...] as long as” the procedure set forth by the CEJU is followed, it surely cannot be the case that seeking injunctive relief at some later stage necessarily breaches Article 102 TFEU. Attaching antitrust liability to conduct by the SEP holder who has already made a FRAND offer seems unnecessarily harsh.

The CJEU’s ruling creates antitrust exposure for a SEP holder who mistakenly believes that its offer is FRAND, but not for an alleged infringer who makes the equivalent mistake. The fact that the risk is borne by only one party risks skewing negotiations and, in this regard, the ruling necessarily strengthens the position of implementers of standard-essential technology, upsetting the balance that has hitherto prevailed and incentivised investment in innovation.

The CJEU’s ruling has potentially serious implications for domestic civil proceedings. According to the CJEU, both offer and counter-offer must be made on FRAND terms. In these circumstances, national courts may be required to adjudicate on a substantive point at a preliminary stage of a dispute. However, the CJEU does not offer any guidance on how FRAND terms should be determined in this context. Concerning public enforcement, it is doubtful that the Commission or national competition agencies would be competent to determine whether an offer or counter-offer is or is not on FRAND terms,⁷ or crucial issues of validity, essentiality, and infringement.

V. THE CJEU’S RULING IS NOT AN ENDORSEMENT OF THE EUROPEAN COMMISSION’S MOTOROLA & SAMSUNG DECISIONS

The CJEU’s ruling is not an endorsement of the Commission’s *Motorola* and *Samsung* decisions. On a number of significant points, the CJEU either is silent, or diverges significantly from the Commission’s approach. Importantly, the CJEU imposes materially more obligations on alleged infringers than the Commission.

At the outset it is worth noting that, unlike the Commission’s decisions, the CJEU’s ruling did not consider issues of market definition and dominance: “the existence of a dominant position” was not contested before the Landgericht Düsseldorf and “[...] the questions posed by

⁷ In its *Motorola* and *Samsung* decisions, the Commission absolved itself of such a determination.

the referring court relate only to the existence of an abuse.” Accordingly, the CJEU’s analysis was necessarily “confined” to this criterion.⁸

Nonetheless, the ruling contains *obiter dicta* on the issue, which suggests that the CJEU may have had doubts about Huawei’s presumed dominance, and may be generally reluctant to consider that, in a licensing dispute involving two SEP owners, one party could be found to hold a dominant position. In this context, the CJEU recalls that the referring court recognized that Huawei and ZTE “have equivalent bargaining power” (¶37). The CJEU also notes, as a “preliminary point,” that both Huawei and ZTE “are holders of numerous patents essential to [the relevant standard i.e. LTE]” (¶40).

The CJEU’s ruling defines a “SEP” as “a patent which is essential to a standard established by a standardization body” (¶2), noting that “the patent at issue is essential to a standard ... rendering its use indispensable to all [suppliers of standard-compliant devices].” In contrast with the position taken by the Commission, the CJEU appears to accept that a (presumptively dominant) SEP holder who has given a commitment to license on FRAND terms can only be found to have committed an abuse where the SEP in question is confirmed as being valid and essential to the standard, and has been found to have been infringed. In reaching these conclusions, the CJEU may have overlooked the fact that (i) patents are generally only declared as potentially essential; and (ii) not all valid SEPs will necessarily be infringed by a standard-compliant product.

Importantly, by stating that there is no abusive conduct “as long as” a certain procedure is followed, the CJEU does not endorse the so-called “willing licensee” test proposed by the Commission in its *Motorola* and *Samsung* decisions, which effectively reversed the burden of proof onto the SEP holder seeking an injunction with the aim of providing a safe harbor for alleged infringers rather than SEP holders.

Applying the CJEU’s ruling, and assuming a FRAND offer has been made by the SEP holder, an alleged infringer is obliged to make a FRAND counter offer before it can raise an antitrust defense to an injunction request. The CJEU’s requirements that (i) alleged infringers act “diligently ... in accordance with recognised commercial practices,” “in good faith” and not employ “delaying tactics;” and (ii) third-party determination may be resorted to only if there is “common accord,” stand in stark contrast to the position adopted by the Commission, where an alleged infringer could avoid an injunction merely by indicating its readiness to have the terms of a license determined by a third party. Another point of divergence with the Commission’s approach is the obligation on alleged infringers to provide “appropriate security” (e.g. a bank guarantee or payments into escrow) “in accordance with recognised commercial practices in the field.”

In the light of the above, given the CJEU’s assessment, the Commission’s *Samsung* and *Motorola* decisions are of little, if any, significance going forward.

⁸ See ¶¶ 43, 28, and 44.

VI. CONCLUSION

In considering the questions referred to it by Landgericht Düsseldorf, the CJEU has (i) designed a novel legal standard that departs from the settled case law of the EU courts; and (ii) prescribed a process that is in stark contrast to that envisaged in the Commission's *Samsung* and *Motorola* decisions.

The CJEU ruling's formalistic and stylized test creates uncertainty and is divorced from the real world of licensing negotiations, not least because it does not engage with issues of cross-licensing and portfolio licensing.

This, coupled with the fact that the ruling: (i) does not directly address the important issues of dominance and market definition; and (ii) is ill-suited for national courts that do not apply an *Orange-Book-Standard*-type of test when assessing requests for injunctive relief, means that it is most unlikely that *Huawei* will be the final word on the debate concerning the application of competition law to SEPs. One can therefore anticipate further references from national courts trying to determine these outstanding issues and how the ruling would apply to disputes in other EU member states.

That said, the judgment confirms that a SEP holder who has given a FRAND commitment does not abuse a dominant position by seeking an injunction against a recalcitrant implementer who refuses to negotiate a license, employs dilatory tactics, or makes a licensing counter-offer that is not on FRAND terms.