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Huawei v. ZTE A Deep Dive



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*Huawei Technologies: More
Certainty on SEP Injunctions, But
Not the End of the Story*

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***Huawei Technologies*: More Certainty on SEP Injunctions, But Not the End of the Story**

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I. INTRODUCTION

The issue of declared standard-essential patents (“SEPs”) and competition law has been a hot topic that has pitted holders of SEPs and users of SEPs against one another in a patent war game with Article 102 TFEU as ammunition. The long awaited judgment of the Court of Justice of the EU (“CJEU”) in *Huawei Technologies* (“*Huawei Technologies*”)² attempts to put an end to the war by striking a careful balance between protection for SEP holders on the one hand and undue delay for implementers in bringing their products to the market on the other.

The judgment builds on the previous decisions of the European Commission (“Commission”) in relation to previous cases involving Samsung and Motorola but provides more detailed guidance and welcome clarity to both SEP holders and implementers as to what steps each must take in order to retain either the right to request, or the right to object to a claim for, an injunction preventing use of an SEP. Significantly, it reaffirms that an alleged infringer cannot be criticized for challenging, or insisting on reserving the right to challenge, in any negotiations the essentiality or validity of the SEP(s) in question.

The judgment holds that an owner of SEPs who has given a fair, reasonable, and non-discriminatory (“FRAND”) undertaking may be abusing its dominant position by seeking an injunction against an alleged infringer, unless the SEP holder alerts the alleged infringer and provides a specific written offer for a license on FRAND terms. However, if the SEP holder follows these steps, it may seek an injunction if the other party continues to use the SEPs in question and fails to respond “diligently” to the SEP holder's offer “in accordance with recognised commercial practices in the field” and “in good faith.” If the alleged infringer adopts “delaying tactics,” then it will lose the right to object to a claim for injunctive relief as an abuse of a dominant position.

Furthermore, the alleged infringer may only allege that an action for a prohibitory injunction is an abuse of a dominant position once it has “promptly” submitted in writing a “specific counter-offer that corresponds to FRAND terms.”

Despite providing welcome clarifications, the *Huawei Technologies* judgment leaves a number of questions unanswered, however. Moreover, national courts (and eventually the Unified Patent Court (“UPC”)) will be required to apply the *Huawei Technologies* framework to the specific facts of each particular application for an injunction by a SEP holder. The possibility of further references to the CJEU therefore remains.

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² Case C-170/13.

II. WHAT ARE SEPS AND WHY ARE THEY IMPORTANT?

SEPs are patents declared by the patent owner as covering technologies which are essential components of products which comply with relevant industry standards agreed between manufacturers through standard-setting organizations (“SSOs”). The manufacture of any such products by a manufacturer which has not obtained a license from the SEP holder infringes the patent in question (assuming that the patent is valid, is actually essential to the standard, and it not the subject of a down-stream license or patent exhaustion). In principle, however, SEP holders undertake that if their patented technology is to be included in an agreed industry standard, they will license their SEPs to any third party on FRAND terms.

III. COMPETITION LAW ISSUES RELATING TO SEPS

It has been argued that holders of such SEPs may (i) have a dominant position in relation to the protected technology and (ii) be abusing their dominant position under Article 102 of the Treaty on the Functioning of the European Union (“TFEU”) by seeking, threatening to enforce, or actually enforcing an injunction against an alleged infringer who requires the technology to manufacture products that comply with the agreed standard and has shown willingness to negotiate a license on FRAND terms. The concern is that the threat of an injunction may enable the SEP holder to apply undue pressure on the alleged infringer and impose unduly onerous licensing terms (such as unfairly high royalties). Alternatively, if an injunction is obtained, there is a risk of the product disappearing from/not coming to the market.

IV. BACKGROUND TO HUAWEI TECHNOLOGIES

A. The Commission's Decisions in the Samsung and Motorola Cases

The Commission decisions in *Motorola*³ and *Samsung*⁴ of April 2014 were the first cases to provide some guidance from the Commission on the compatibility of SEP injunctions with the EU competition rules. The Commission opened its investigation into Samsung after Samsung had sought injunctive relief in the courts of various EU Member States against Apple based on alleged infringements of certain of its SEPs relating to 3G UMTS technology. The investigation into Motorola was opened after Motorola sought an injunction (also against Apple) in the German courts based on alleged infringements of its SEP relating to GPRS technology.

While recognizing that seeking an injunction is a legitimate remedy against an alleged patent infringer, the Commission held that applying for an injunction based on SEPs *may* be an abuse of a dominant position where the patent holder has given a voluntary commitment to license its SEPs on FRAND terms and where the injunction is sought against a licensee who is “willing” to enter into a license agreement on FRAND terms.

In *Samsung*, the Commission accepted binding commitments from Samsung, for a period of five years, not to seek injunctive relief in the European Economic Area (“EEA”) in relation to all its SEPs for technologies implemented in smartphones and tablets against any company that

³ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*.

⁴ Commission decision of 29 April 2014, Case AT.39939 – *Samsung - Enforcement of UMTS Standard Essential Patents*.

agrees to a particular licensing framework. The licensing framework consisted of a negotiation period of up to 12 months and a third-party (court or arbitrator) determination of FRAND terms.

In *Motorola*, the Commission concluded that Motorola had breached Article 102 TFEU by seeking and enforcing an injunction against Apple in Germany in relation to a smartphone SEP. The Commission also found that it was anticompetitive to force Apple, under threat of enforcement of injunction, to give up its rights to challenge the validity of Motorola's SEPs. However, it decided not to fine Motorola due to the lack of legal precedent.

These decisions provided a form of “safe harbor” for alleged infringers who are willing to submit to third-party resolution of FRAND disputes, and clarify that seeking to challenge the validity of a patent does not render an alleged infringer unwilling. However, they failed to provide any detailed explanation as to the criteria according to which it is to be judged whether an alleged infringer is, or is not, “willing.”⁵

B. Huawei Technologies' Application for Injunctive Relief Against ZTE in the German Courts and the "Orange Book" Standard

Huawei and ZTE are both holders of a number of declared SEPs covering aspects of the LTE (Long Term Evolution or “4G”) standard⁶ and had therefore made commitments within the ETSI framework to license those patents on FRAND terms.

In March 2013, the Regional Court of Düsseldorf made a preliminary reference to the CJEU in a case between Huawei, as the holder of certain SEPs covering aspects of the LTE/4G standard, and ZTE, as the alleged infringer of the patents. The reference to the CJEU in this case arose from the potential conflict between the approach taken previously by the German courts and the EU Commission's approach in the *Samsung* and *Motorola* cases.

The German decisional practice was based on what is known as the “*Orange Book*” case.⁷ The *Orange Book* case concerned a *de facto* standard for CD-Rs (recordable compact discs). The patent-holder, Philips, sought injunctive relief against several manufacturers and one of the defendants argued that, in doing so, Philips had abused its dominant position on the market for CD-Rs. However, the German Court found that this defense could only succeed in relatively limited circumstances and, in particular, only if the alleged infringer accepted the validity of the patent. The Orange Book Standard was therefore considered to be more friendly to SEP-holders than the Commission's approach in *Samsung* and *Motorola*, which found that the mere seeking of an injunction would constitute an abuse in many circumstances.

The German Court therefore decided to stay proceedings and ask the CJEU for clarification on the appropriate threshold for an abuse of dominance defense in the context of a SEP injunction and on the concept of a willing licensee.

⁵ More recently, the Commission carried out an industry wide consultation between October 2014 and February 2015 entitled “A modern framework for standardisation involving intellectual property rights, with the objective of gathering information and views on the interplay between standardisation and intellectual property rights (IPR) such as patents.

⁶ LTE/4G is a mobile network communication standard which is composed of more than 4,700 SEPs.

⁷ KZR 39/06, Orange Book Standard, Judgment of 6 May 2009. [Check reference]

V. THE CJEU'S JUDGMENT IN HUAWEI TECHNOLOGIES

A. *The Need to "Strike a Balance"*

The CJEU stated that it was required to "strike a balance between maintaining free competition...and the requirement to safeguard [the SEP-holder's] intellectual property rights and its right to effective judicial protection," both of which rights the Court noted to be protected under the Charter of Fundamental Rights of the European Union ("the Charter").

In terms of the extent to which these rights can be fettered by competition law, the CJEU clearly was not of the view that an application for injunctive relief by an SEP-holder constitutes abusive conduct *per se* under Article 102 TEFU; rather, it noted that it is

"settled case law that the exercise of an exclusive right linked to an intellectual-property right... forms part of the rights of the proprietor of an intellectual-property right, with the result that the exercise of such a right, even if it is the act of an undertaking holding a dominant position, cannot in itself constitute an abuse of a dominant position",

but also stated that

"it is also settled case-law that the exercise of an exclusive right linked to an intellectual-property right by the proprietor may, in exceptional circumstances, involve abusive conduct for the purposes of Article 102 TFEU."

B. *The Significance of the FRAND Undertaking by Huawei*

In considering how to strike this balance in the circumstances at hand, however, the Court noted, first, that the patent at issue was declared essential to a standard established by a SSO, meaning that Huawei could prevent products manufactured by competitors from appearing or remaining on the market and, thereby, reserve to itself the manufacture of the products in question. Second, the patent had been declared essential only in return for an irrevocable undertaking by Huawei to license it on FRAND terms, which created legitimate expectations on the part of third parties.

C. *The Framework With Which the SEP-holder Must Comply*

1. *Conduct of the SEP-holder*

According to the framework set out in the CJEU's decision, in order to avoid an infringement of Article 102 TFEU, SEP holders seeking injunctive relief must alert the alleged infringer to the infringement, designating the specific SEPs concerned and specifying the manner in which they have been infringed (due to the large number of SEPs composing a standard such as the one at issue, the CJEU considered it possible that the alleged infringer could be unaware that it was using technology protected by an SEP). No indication is given as to the level of detail required to be given, but it is assumed that, at the very least, examples of the alleged infringer's products said to infringe must be provided.

Whether details of exactly how it is alleged a product falls within the claims of the SEP must be provided is also unclear. The SEP-holder must also make a written licensing offer on FRAND terms, including the proposed royalty and an explanation of the way in which it is calculated. It must not seek to prevent the alleged infringer from challenging the validity and/or the essentiality of the SEPs in question or reserving the right to do so in future.

2. Conduct of the alleged infringer

As for the alleged infringer, if it continues to use the SEP concerned, then it is obliged to respond “diligently” to the SEP holder's offer “in accordance with recognised commercial practices in the field” and “in good faith.” This will be assessed objectively. However, the judgment does not give any criteria by which such an objective assessment should be conducted. The alleged infringer also must not adopt “delaying tactics.”

Furthermore, the alleged infringer may only allege that an action for a prohibitory injunction is an abuse of a dominant position once it has submitted a “specific counter-offer that corresponds to FRAND terms.” It is presumed that the alleged infringer may provide a counter-offer even if the SEP-holder's initial offer is within the FRAND range, although this is not explicit in the decision. It is also presumed that, as with the initial offer, any such counter-offer must also contain a proposed royalty and calculation methodology (though this is not stated expressly in the judgment).

A question in relation to this requirement is how it is intended that the alleged infringer judges what constitutes FRAND for these purposes, given the CJEU's reference in the decision to the opinion of the Advocate General, whose view was that the SEP-holder is better-placed to assess whether an offer complies with the FRAND requirement, particularly if it has already granted other licenses.

The judgment also suggests that, should the SEP holder reject such a counter-offer, then the infringer is obliged to provide appropriate security (e.g. a bank guarantee or deposit) in respect of past and future infringements, and render an account. The CJEU held that it cannot be abusive to seek damages or a rendering of accounts, since those remedies do not have a direct impact on products complying with the standard in question manufactured by competitors appearing or remaining on the market. The judgment does not, however, specify whether the amount of security should be calculated by reference to the royalty rate in the offer or the counter-offer. There is also a question mark as to whether this is a pre-requisite to avoiding injunctive relief; it does not feature in the operative ruling at the end of the judgment, but only earlier on in the text of the decision.

3. Determination by an independent third party if the SEP-holder and alleged infringer can't agree

The CJEU noted that the parties may “by common agreement” request that the FRAND royalty be “determined by an independent third party, by decision without delay.” However, it does not say anything about what happens to any ongoing litigation in the interim and, in particular, the availability of injunctions. Second, it is not clear whether this is optional or a mandatory requirement, given that the decision states that the parties “may” (rather than must) pursue this option, and it is not mentioned in the operative part of the judgment. It is also unclear what the implications would be if the parties could not reach agreement on a referral to a third party in principle, or on the identity of the third party.

VI. IMPLICATIONS AND FURTHER UNANSWERED QUESTIONS

A. *The CJEU Has Largely Endorsed the Commission's Approach in Samsung/Motorola Rather Than Orange Book*

As explained above, according to the Orange Book Standard, a competition law defense could only be relied on to prevent the grant of an injunction in relatively exceptional circumstances (in particular, if the alleged infringer waived its right to challenge the validity of the patent). In contrast, the CJEU in *Huawei Technologies* has broadly endorsed the findings of the Commission in *Samsung* and *Motorola* in holding that a SEP-holder will be viewed as abusing a dominant position simply by seeking an injunction if it does not adhere to the Court's framework.

However, it may not be correct to dismiss the Orange Book Standard as irrelevant post-*Samsung*, *Motorola* and *Huawei Technologies* because, as noted by the Advocate General in *Huawei Technologies*, there are significant factual differences between these cases. In particular, the patent at issue in *Huawei Technologies* was developed as a result of an agreement concluded between the undertakings (including Huawei and ZTE) involved in the standardization process within ETSI, whereas the standard at issue in the Orange-Book-Standard case was a *de facto* standard in relation to which the owner of the patent at issue had not given a FRAND licensing commitment.

B. *How Does Huawei Technologies Differ From the Principles Established in Samsung/Motorola?*

The CJEU's decision in *Huawei Technologies* is consistent with some of the key principles established in *Samsung and Motorola*. For example, (i) the SEP-holder can only be viewed as abusing a dominant position if the alleged infringer is not a willing licensee; (ii) where the parties are not able to agree on FRAND terms, the question may be decided by an independent third-party or court; and (iii) potential licensees of SEPs should remain free to challenge the validity, essentiality, or infringement of SEPs.

However, *Samsung* and *Motorola* provide very little practical guidance as to the ways in which the SEP-holder must conduct itself so as to comply with competition law and the criteria by which the alleged infringer should be judged to be “willing” (or not). As set out above, *Huawei Technologies* has gone some way to providing such guidance by setting out “specific requirements” with which the SEP holder needs to comply in order to be able to seek an injunction without abusing its dominant position. Equally, the CJEU has set out clear steps that an alleged infringer must take in order to show that it is a “willing” licensee.

C. *Key Commercial Implications of the Judgment*

SEP-holders may well consider that the framework set out by the CJEU limits their freedom to negotiate royalty rates freely. For example, they may feel that the requirement for their initial written offer to be FRAND goes against standard commercial practice—i.e. that the licensor would usually expect its first offer to be higher than the rate it ultimately expects to agree on. Similarly, alleged infringers may consider that they would normally expect their opening offer to be considerably lower than the amount that they expect to pay. However, this reflects the Court's desire to achieve a balanced approach. It should also be born in mind that it is inherent in

the CJEU's framework (simply by view of the fact that it envisages a counter-offer) that there would be a range of royalty rates which would be viewed as FRAND. Consequently, there is still scope for a negotiation.

It does, however, remain to be seen whether royalty rates for SEPs will decline significantly as a result of this framework (and, therefore, whether consumer prices will be affected). It is also unclear whether the threat of reduced royalty rates will have any sort of effect on incentives to innovate—in theory, this should not be the case in circumstances where SEP-holders were, in any event, happy to commit to licensing on FRAND terms.

In general, the ability to enforce intellectual property rights is crucial in order to incentivize innovation. It is important to remember that the CJEU found in *Huawei Technologies* that the seeking of an injunction by an SEP-holder will **not** constitute an abuse of dominance unless it fails to comply with the framework. It is, therefore, clear that the CJEU is not seeking to question the fundamental right of a patentee to enforce its rights; rather, it has sought to ensure that it does so in a way which addresses the legitimate concerns that injunctions can otherwise be used by SEP-holders to distort licensing negotiations, extracting excessively high royalties and thereby distorting competition on downstream markets. The decision therefore reduces the likelihood of products being blocked or withdrawn from the market in the EEA.

D. Key Questions That Remain Unanswered

A number of questions remain unanswered by the CJEU's judgment and some of the concepts built in to the CJEU's framework are clearly open to interpretation. There is therefore scope for Member States/national courts to interpret the decision differently. These questions include: Has the alleged infringer responded “diligently” to the SEP-holder's written offer, and was its counter-offer provided sufficiently “promptly?” What will happen if an alleged infringer does not respond at all to the offer by the SEP-holder? Will the court in question still need to assess whether the initial offer was on FRAND terms or can the application for an injunction be made in any event (e.g. because the alleged infringer is seen as “unwilling” or as using delaying tactics)? As set out in the following paragraphs, some more fundamental questions also remain unanswered.

1. Is a SEP-holder always dominant?

The question of a potential abuse under Article 102 TFEU only arises in circumstances where the party concerned is considered to be dominant. However, the referring German Court did not ask the CJEU whether, or in what circumstances, the SEP-holder should be viewed as dominant. The CJEU did not therefore express a view on this question. It is to be noted that in his opinion on the case, the Advocate General stated his view that

"If the fact that anyone who uses a standard set by a standardisation body must necessarily make use of the teaching of an SEP, thus requiring a licence from the owner of that patent, could give rise to a rebuttable presumption that the owner of that patent holds a dominant position, it must, in my view, be possible to rebut that presumption with specific, detailed evidence."

There is therefore clear scope for debate in future cases.

2. What does FRAND mean in the context of an SEP license?

Further, while the CJEU's framework accounts for the possibility for the parties to a negotiation to request that the FRAND royalty be determined by an independent third party, it does not provide any guidance as to definition of "FRAND" in this case or more generally. It may, therefore, be said that *Huawei Technologies* will not end the competition law disputes in relation to the seeking of injunctions in relation to SEPs; rather, it will simply change the nature of those disputes.

3. Can the CJEU's framework be applied to more complicated negotiations relating to patent portfolios and/or cross-licensing?

In many cases, negotiations relate to large numbers ("portfolios") of patents. The process and logistics of such negotiations can be particularly complex and it therefore remains to be seen whether it will be possible to meaningfully apply the CJEU's framework in such circumstances. Similarly, where the parties concerned are both intellectual property rights-holders and wish to enter into cross-licenses, the negotiation process will be even more complex, potentially raising further question marks over the practical utility of the CJEU's framework.

VII. HUAWEI TECHNOLOGIES IS NOT THE END OF THE STORY

It is, therefore, clear that there remains some scope for a divergence in the approach taken in different Member States. This risk may only exist until the Unified Patent Court is up and running, however (and the CJEU's decision in *Huawei Technologies* will give the UPC a helpful framework).

Further, the EU's Competition Commissioner stated recently that *Huawei Technologies* does not mark the end of the story on SEP licensing concerns under competition law, noting that the Commission has seen attempts to circumvent the decision; for example, where companies seek injunctions against companies active at other levels of the distribution chain (e.g. telecoms operators selling phones rather than the phone manufacturer).

In addition, it must not be forgotten that, while the CJEU has now set out a framework for SEP licensing negotiations, it will be up to the national courts to interpret and apply the CJEU's requirements. This will require case-specific and fact-intensive inquiries and leaves scope for diverging interpretations.

It seems that *Huawei Technologies* may be just a temporary truce in a war that is set to continue.



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The ECJ *Huawei–ZTE* Decision: En Route to Ending Hold-Out?

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The ECJ *Huawei–ZTE* Decision: En Route to Ending Hold-Out?

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I. INTRODUCTION

On July 16 2015, the European Court of Justice (the “ECJ”) issued its much-awaited decision in the *Huawei-ZTE* matter (“Decision”),² in reply to questions referred by the German Landgericht Düsseldorf court. The Decision involved a Standard Essential Patent (“Essential Patent”) dispute between two telecommunications companies manufacturing smartphones.³

The main questions addressed by the Decision focused on: (1) whether, or under what circumstances, an Essential Patent holder (“Licensor” or “Innovator”) who provided a Fair Reasonable and Non-Discriminatory (“FRAND”) access assurance may abuse a dominant market position, where it enjoys one, if it brings an action for injunction against an infringer who has declared itself willing to negotiate towards a license; (2) what are the particular qualitative and/or time requirements needed to substantiate the infringer’s “willingness to negotiate;” and (3) what are the particular requirements for the Essential Patent holder’s initial offer, if any.

Notably, these questions were raised against the background of the German *Orange-Book-Standard* decision,⁴ which focused only on the willingness of an infringer to conclude a license on FRAND terms in considering whether an “abuse of dominance” defense is available. However, the ECJ chose not to adopt the *Orange-Book* standard. Instead, the Decision provides a new procedural framework that looks at both the Essential Patent Holder and the infringer’s behavior. On the one hand, where infringers fail to comply with the new ECJ framework, they lose the opportunity to allege a Licensor’s injunctive relief action is potentially abusive. On the other hand, the Decision creates a “safe harbor” in which Licensors may freely seek injunctive relief without potential competition concerns if they comply with the procedural framework. This new framework aims to prevent an increasingly prevalent practice known as patent hold-out, which involves lucrative long-term infringement of Essential Patents by calculated technology users who are unwilling to take a license under FRAND terms.

This note identifies the underlying principles and boundaries of the Decision. It then highlights certain circumstances that are highly specific to the Decision, before examining the

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² Case C-170/13 Huawei Technologies Co. Limited v. ZTE Corp. (Fifth Chamber, 16 July 2015) *available at* <http://curia.europa.eu/juris/document/document.jsf?jsessionid=9ea7d2dc30ddec4f949241db44d296cc9739f41099c5.e34KaxiLc3qMb40Rch0SaxuRa3j0?text=&docid=165911&pageIndex=0&doclang=EN&mode=req&dir=&occ=first&part=1&cid=747013>.

³ Fair, reasonable and non-discriminatory terms (FRAND) are a licensing obligation that is often required by standard setting organizations for members that participate in the standard-setting process.

⁴ KZR 39/06 Orange-Book-Standard (Federal Court of Justice of Germany, May 6 2009).

constructive guidance and safe harbor framework that the Decision establishes. We conclude by expressing cautious optimism that the ECJ's new framework may diminish the patent hold-out problem.

II. UNDERLYING PRINCIPLES AND BOUNDARIES OF THE DECISION

Under EU competition law, the assessment of whether an undertaking has abused its dominant position under Art. 102 TFEU requires a *rule of reason* test comprised of three elements: (1) evaluating whether the undertaking holds a dominant position also known as “market power;” (2) finding of an anticompetitive foreclosure; and, where the two preceding elements are found (3) the target may demonstrate that its conduct is “objectively necessary” or produces substantial efficiencies which outweigh any anticompetitive effects on consumers.⁵

The emphasis of the Commission's enforcement activity in this area “is on safeguarding the competitive process ... and ensuring that undertakings which hold a dominant position do not exclude their competitors.”⁶ In light of this competition analysis context it is useful to note the following.

A. Essential Patents Do Not Necessarily Convey Market Power

The Commission has made it clear that “there is no presumption that holding or exercising IPR essential to a standard equates to the possession or exercise of market power” noting that “[t]he question of market power can only be assessed on a case by case basis.”⁷ This approach is consistent with U.S. antitrust law.⁸ The Decision explicitly avoids delving into this matter because, in the referred case, the existence of a dominant position was not contested.⁹

B. Right to Seek Injunctive Relief is a Fundamental Right

The Decision recognizes that European Law “provides for a range of legal remedies aimed at ensuring a high level of protection for intellectual-property rights” and for “the right of

⁵ 2009/C 45/02 Communication from the Commission — Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, 2009 OJ C 45/7 (24 February, 2009) available at [http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0224\(01\)&from=EN](http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0224(01)&from=EN), §§ 9-18, 19-26, and 28.

⁶ *Id.* at §6.

⁷ EC Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements, 2011 OJ C 11/1 (14 January 2011), §269, available at [http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52011XC0114\(04\)&from=EN](http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52011XC0114(04)&from=EN).

⁸ Under U.S. antitrust law, patents and other intellectual property rights should not be viewed as necessarily conveying market power. See *Illinois Tool Works Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006); U.S. Dep't of Justice & Fed. Trade Comm'n, *Antitrust Guidelines for the Licensing of Intellectual Property* (April 6, 1995) §2.2. In the context of Essential Patents, there is similarly no presumption that they create market power but, rather, market power must be established in each case basis, see *ChriMar Systems, Inc. v. Cisco Systems*, 72 F.Supp.3d 1012, 1019 (N.D. Cal. 2014) (rejecting the argument that “to the extent that the...Patent is essential to the 802.3af and the 802.3at standards, no viable technology substitutes exist and ChriMar has monopoly power over the [relevant] [t]echnology Market”; explaining instead that there are other necessary elements that need to be proven “in order to prove market power”).

⁹ Decision at § 43 (“As the referring court states [...] the existence of a dominant position has not been contested before it by parties[.]. Given that the questions posed by the referring court relate only to the existence of an abuse, the analysis must be referred to the latter criterion”).

access to a tribunal.”¹⁰ In particular the ECJ notes that “[T]he proprietor of the essential patent at issue has the right to bring an action for a prohibitory injunction or for the recall of products.”¹¹ Consequently, the ECJ found that this right can only be limited in particular circumstances. Indeed, the ECJ ensures that it is for the national court to assess whether a claim for an injunction gives rise to an antitrust defense, but that the Essential Patent holder should not be barred from bringing the claim in the first instance. Effective prohibitions on the ability to seek a judicial remedy are not recognized by the ECJ.

C. The Decision Does Not Define What is FRAND

While interested parties may attempt to interpret the Decision as applying to the meaning of the term “FRAND,” such attempts are not supported by the Decision. Rather, the Decision is clearly limited to potential Art. 102 TFEU analysis of actions seeking injunctions for the infringement of Essential Patents.¹²

III. SPECIFIC CONTEXT OF THE DECISION

The case referred to the ECJ by the German Landgericht Düsseldorf court was fact-specific. It remains unclear to what extent the Decision will be applicable to cases whose facts would be distinguishable. Important case-specific aspects include the following.

A. The Decision Involved Two Direct Competitors

The Decision reiterates, in multiple places,¹³ that its competition analysis refers to a scenario where the innovating Essential Patent holder tries to prevent standard compliant products that are “manufactured by **competitors** from appearing or remaining on the market.” Since, as noted by the Commission, Art. 102 TFEU enforcement focuses on attempts to exclude **competitors**, it is unclear what the analysis would be where the parties to an Essential Patents licensing dispute are not competitors. Potential competitive harm is always a greater concern where the scenario is a horizontal one, i.e. one in which a party has an interest in excluding a competitor from the market, and less of a concern otherwise.

Notably, a June 2015 decision by Brazil’s competition agency (CADE) that involved an Essential Patent owner who sought an injunction against a strategic opportunistic infringer, and where such injunction was granted, made it clear that one of the many reasons CADE did not find competitive harm and therefore closed the competition case, was the fact that the parties to the dispute were not competitors.¹⁴

¹⁰ *Id.* at § 57.

¹¹ *Id.* at § 52.

¹² *Id.* at § 39.

¹³ *Id.* at §§ 49, 52, 64 and 73-74.

¹⁴ Decision No. 08700.008409/2014-00, TCT v. Ericsson (1 June, 2015), § 20 available at <http://goo.gl/2tZozo>; Appeal denied on July 7 2015 and available at http://sei.cade.gov.br/sei/institucional/pesquisa/documento_consulta_externa.php?CBqAUEI9nI3CEI9rjzOScrVPZyHJe9UNqzDNROL8OzOf3qPrlowO7tQcfSQqwRPQcjDUI3vfpNISFSbhjDDGxw.

B. The Decision Concerned One Single Essential Patent

This is relevant because many Essential Patent licensing disputes involve sizeable global portfolios of multiple patents. That is the context in which the prevalent problem of patent hold-out often materializes; for example, through attempting to force licensors to litigate the merits of each patent in its extensive portfolio on a patent-by-patent basis as a prerequisite to taking a FRAND license.

Such opportunistic behavior exploits the fact that litigation is very expensive and takes years to consummate, and hence it is practically impossible for a significant contributor of standardized technology to timely and cost-effectively litigate its entire global Essential Patents portfolio through national courts. As a result, such calculated infringers attempt to force Essential Patent holders to license their Essential Patents on sub-FRAND terms, which in turn chills incentives to invest in R&D and in participation in and contribution of proprietary technology to open standards. Because only a single Essential Patent was asserted in the referred case, the ECJ did not specifically address this important and concerning aspect of patent hold-out.

IV. THE FRAMEWORK OF THE DECISION: CURBING HOLD-OUT AND GAMESMANSHIP

The importance of the Decision lies in the procedural framework it provides for licensing negotiations. In light of increasing attempts to free-ride on the FRAND-assured Essential Patents, the Decision aims to curb the success of such opportunistic strategies. It references “reverse hold-up”¹⁵ and clarifies repeatedly that the ECJ will not tolerate infringers’ “delaying tactics.”¹⁶ Thus the Decision imposes an obligation on the alleged infringer to respond to the Essential Patent holder’s license offer “diligently,” “in accordance with recognized commercial practices in the field,” “in good faith,” and with “no delaying tactics.”¹⁷ In this way, the CJEU has sought “to ensure a fair balance between the interests concerned.”¹⁸

The Decision then sets out a concrete framework to prevent patent hold-out as follows:

1. An Essential Patent owner must first give notice to an infringer by designating the infringed Essential Patent(s) and the way in which it/they have been infringed;¹⁹
2. It is then up to the infringer to express its willingness to conclude a licensing agreement on FRAND terms;²⁰
3. Only if and once an infringer has expressed its willingness to license on FRAND terms, the Licensor must present the infringer with a written licensing offer;²¹
4. After being presented with the Licensor’s offer, the infringer is under tight deadlines to either accept the offer or present a FRAND counter-offer (“promptly” and “in accordance

¹⁵ Decision at § 38.

¹⁶ *Id.* at §§ 65-66 and 71.

¹⁷ *Id.* at § 65.

¹⁸ *Id.* at § 55.

¹⁹ *Id.* at § 61.

²⁰ *Id.* at § 63.

²¹ *Id.* at § 63.

with recognized commercial practices in the field and in good faith”). “[D]elaying tactics” are explicitly mentioned as a key factor for that evaluation;²² and

5. The Decision imposes a duty on the infringer to deposit an “appropriate security” as soon as its counter-offer is rejected;²³ the infringer cannot argue that a motion for an injunction against it is abusive until such security deposit is in place.²⁴

Where the infringer fails to comply with the ECJ framework, i.e. where it fails to negotiate in good faith or uses delay tactics, it then can no longer successfully raise allegations of abuse of dominance by the Innovator as a defense against the seeking of injunctive relief. The Licensor also continues to enjoy broad access to injunctive relief free from potential Art. 102 TFEU liability in all cases where the infringer makes a counter-offer that is not FRAND.²⁵

In recognizing technology users' duty to negotiate in good faith, the Decision is consistent with U.S. case law, such as the *Ericsson v. D-Link* decision.²⁶ It is also in line with the increasing recognition of patent hold-out as a serious problem. For example, in the *Apple v. Motorola* decision,²⁷ Chief Judge Rader commented that “hold out is equally as likely and as disruptive as a hold up.” The FTC has also acknowledged the existence of problematic scenarios in which “the patent-holder is forced to license the patents at less than fair market value,”²⁸ and the ITC has, in its 2013 *Samsung v. Apple* decision, addressed hold-up as an “expensive litigation” scenario under which “an implementer utilizes declared-essential technology without compensation to the patent owner under the guise that the patent owner’s offers to license were not fair or reasonable.”²⁹

Notably, the Decision consciously avoids use of a “hold-up” framework. Although Advocate General Wathlet’s Opinion (“Opinion”) stated:

it should be ensured that SEP-holders cannot, for example, impose excessive royalties in breach of their commitment to grant licences on F/RAND terms, thereby engaging in conduct which has become known as ‘patent hold-up.’³⁰

However, the Decision did not see a need to frame the discussion in terms of “hold-up” or “excessive or unfair royalties” that could result from the threat of exclusion due to the seeking of an injunction. This is notable, because “hold-up” is the context in which the current FRAND debate is often set and these very points were indeed made to the ECJ in both written pleadings and at the oral hearing. Therefore the ECJ conspicuously chose not to take on board these

²² *Id.* at §§ 65 and 66.

²³ *Id.* at § 67.

²⁴ *Id.* at § 67.

²⁵ *Id.* at § 66.

²⁶ Memorandum Opinion and Order, *Ericsson v. D-Link*, No. 6:10-00473, 2013 WL 2242444 (Aug. 6, 2013).

²⁷ U.S. Court of Appeals for the Federal Circuit (April 25, 2014).

²⁸ Quote taken from the Prepared Statement of the Federal Trade Commission before the U.S. Senate Committee on the Judiciary, concerning “Standard Essential Patent Disputes and Antitrust Law” (July 30, 2013).

²⁹ Commission Opinion, *In re Certain Electronic Devices, Including Wireless Communication Devices, Portable Music and Data Processing Devices, and Tablet Computers*, Inv. No. 337-TA-794 (Int’l Trade Comm’n June 4, 2013), at 63.

³⁰ § 41 of the Opinion. The theory of “royalty stacking” was also put before the ECJ and referred to in the European Commission’s pleadings to the ECJ. *See* footnote 14 of the Opinion.

arguments and rejected the opportunity to endorse the various supra-FRAND “hold-up” theories.

V. WHAT ARE “DELAYING TACTICS”?

There are multiple scenarios that calculated infringers can play out as a delay tactic—the possibilities are endless. One such scenario can be a situation whereby, in the context of a sizeable Essential Patents portfolio, an infringer insists on patent-by-patent licensing. A standard-compliant product, such as a smartphone, is often covered by hundreds or even thousands of individual patents often owned by a single patent holder. Hence, the prevailing efficient industry practice is portfolio licensing due to significant savings in transaction costs and time. Notably, standard implementers need to take a license to all relevant Essential Patents, not just a few individual ones, to obtain freedom to operate.

By insisting on patent-by-patent licensing, however, an infringer can significantly delay and obstruct licensing negotiations. It forces Licensors to unnecessarily provide licensing terms and detailed proof of validity and essentiality for hundreds or thousands of individual patents, which is an extremely costly and time-consuming exercise. Throughout all this time, the Licensor would receive no compensation for its significant investment in R&D and in the standard, while the infringer continues to lucratively sell products that free-ride on others’ technology. In addition to obviously compromising the commercial interests of the Innovator, such behavior also gives the infringer a competitive advantage over legitimate market participants that did take a license on FRAND terms and pay licensing fees.

VI. SAFE HARBOR FOR ESSENTIAL PATENT HOLDERS

The ECJ framework also creates a safe harbor for Essential Patent holders. In cases where such holders hold a dominant position, they cannot be accused of abusing their position under Art. 102 TFEU where they act as “willing licensors” under the framework. More specifically, Licensors do **not** abuse their dominant position if seeking injunctive relief after having (1) given the infringer notice of its infringement³¹ and, after the infringer expressed its willingness to conclude a license on FRAND terms, (2) provided the infringer with a written licensing offer on such terms.³²

This Licensor safe harbor applies **regardless** of the conduct of the infringer. In other words, it also applies where the infringer has complied with all the procedural framework requirements, i.e. where it has negotiated in good faith, provided the Licensor with a FRAND counter-offer, and provided adequate security. After all, abuse of a dominant position is a defense to patent infringement claims, and in such a case the infringer would not be able to demonstrate an abuse by the Licensor.

In addition, as established above, such a defense would only be available where the infringer itself complies with the framework (i.e. is a “willing” party). Thus, an infringer can only allege an abuse of a dominance defense where it has itself complied with the procedural framework, while the Licensor did not. Note that even when such defense is raised, the infringer

³¹ *Id.* at § 60.

³² *Id.* at § 63.

must still successfully prove that, under the circumstances, the Licensor's behavior constitutes an Art. 102 violation under the three-element rule of reason described earlier.

The ECJ safe harbor is not a common rigid set of rules that all Licensors must comply with in order to be sheltered from potential Art. 102 TFEU liability. Rather, the Decision provides one example of a possible safe harbor for Licensors, as is evident by its negative phrasing: "the proprietor of a patent essential to a standard (...) does not abuse its dominant position as long as (...),"³³ and by the fact that the court's overall approach leaves broad discretion to national courts to analyze the parties' willing/unwilling mindset under the circumstances that come before them.³⁴

Indeed, it is conceivable and even likely that there are many other safe scenarios for Innovators, as the ECJ made it clear that injunctive relief is a fundamental right that can only be limited in specific, exceptional circumstances. Legitimate injunctive relief for infringement of Essential Patents is the rule, not the exception.

For example, where parties have already engaged in prolonged licensing negotiations, it makes little sense for the Licensor to provide the infringer with separate *de novo* notice of infringement. Also, where, during licensing negotiations for a portfolio of Essential Patents, the infringer has made it clear that it is not interested in individual licensing terms, it will later be difficult to successfully argue that the Licensor has abused its dominant position by not specifying individual patents and the way in which those patents are infringed.³⁵ The fact that a Licensor has, under such circumstances that are different from the *Huawei-ZTE* ones, not complied with the criteria of the framework, does not necessarily mean that it is an "unwilling licensor" under the framework, let alone that it abused its dominant position within the meaning of Article 102 TFEU.³⁶

The above analysis is illustrated in the table below which shows, in green font, the scenarios under which Licensors cannot be subject to Art. 102 TFEU liability when seeking injunctive relief for breach of Essential Patents:

³³ *Id.* at § 77.

³⁴ *Id.* at § 70: "It is for the referring court to determine whether the abovementioned criteria are satisfied... **in so far as they are relevant, in the circumstances**, for the purpose of resolving the dispute in the main proceedings." If the ECJ gave the referring court that type of discretion where the facts of the case were known, it is clear that it left broad discretion to future courts where the facts are unknown, to consider all the relevant circumstances.

³⁵ *Id.* at § 61.

³⁶ See also the International Competition Network (ICN) Unilateral Conduct Working Group Recommended Practices on DOMINANCE/SUBSTANTIAL MARKET POWER ANALYSIS PURSUANT TO UNILATERAL CONDUCT RULES, §5 available at <http://www.internationalcompetitionnetwork.org/uploads/library/doc317.pdf> (demonstrating the general antitrust approach according to which being outside a "safe harbour" is generally necessary but **insufficient** for finding a problem).

| | Licensors complies with ECJ framework – ‘Safe Harbor’ | Licensors does not comply with ECJ framework |
|--|---|--|
| Infringer complies with ECJ framework (and not otherwise “unwilling”) | ✓ | If willing licensor (under other circumstances – fact specific): ✓ |
| | | If “unwilling” licensor - ? (depends on whether Art. 102 TFEU rule of reason analysis criteria are proven) |
| Infringer appears to comply with ECJ framework but “unwilling” under other circumstances/tactics | ✓ | ✓ |
| Infringer does not comply with ECJ framework | ✓ | ✓ |

VII. CONCLUSION

The ECJ confirms that Essential Patent holders, like all patentees, are entitled to injunctive relief and recall of products where their rights are infringed. This right may only be limited in specific, exceptional circumstances.

In particular, the Decision provides a procedural framework for licensing negotiations that aims to prevent patent hold-out strategies by “unwilling” infringers. First, the Decision obligates infringers to respond to the Innovator’s licensing offer “diligently, “in accordance with recognized commercial practices in the field,” “in good faith,” and with “no delaying tactics.” If infringers fail to do so, they lose the defense of alleging that the action for an injunction against them was abusive.

Furthermore, the ECJ decided that as long as the Licensor provides the infringer with due notice of infringement and—provided that the infringer has subsequently declared itself willing to license on FRAND terms—a licensing offer on FRAND terms was rejected by the infringer, the Licensor is then free to pursue infringement actions and injunctions, regardless of any further conduct of the licensee (a one-sided “safe harbor”).

It remains to be seen whether this new framework will suffice for resolving the problem of patent hold-out. Time will tell as national courts begin to apply the Decision. The economic incentive for infringers to pursue hold-out strategies remains high, especially where large Essential Patent portfolios are involved. There is always the risk that infringers will test the boundaries of the Decision’s framework through creative sophisticated hold-out strategies in which delay tactics are obscured as good faith negotiations. But the Decision also warrants cautious optimism, because it provides Innovators with a concrete and flexible framework to effectively weed out such behavior.



Huawei v ZTE – No More Need To Look At The Orange Book In SEP Disputes

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Industry standards are crucial for economic development – they reduce transaction and production costs; they increase efficiency; they ensure network interoperability. A number of industries, such as telecoms, IT and automotive heavily rely on standards. Once a standard has been adopted, standard-setting organisations usually require owners of patents found to be essential to the standard (Standard Essential Patents, or SEPs) to commit to charging a fair, reasonable, and non-discriminatory (FRAND) royalty to the users of the selected technology.

Given that standards covering equipment such as smartphones, games consoles, computers, DVD players and the like are implemented on a global basis, patents essential to those standards are a global issue and create global challenges (given the similarity in the products using them around the world). A number of patent disputes have developed between SEP holders and tech companies using the standardised technology. One major debate focuses on the conditions under which SEP holders can seek injunctions based on infringement of the patents for which a FRAND commitment has been given.

This article analyses the long-awaited judgment of the Court of Justice of the European Union (ECJ) in *Huawei v ZTE* which was handed down on 16 July 2015.² The judgment provides a structured framework for when EU competition law permits SEP holders who have given a FRAND commitment to seek an injunction.

The background: the contrast between the German Orange Book test and the EU Commission in *Samsung/ Motorola*

The *Huawei v ZTE* case was referred to the ECJ by the Düsseldorf District Court, which was hearing a patent dispute between two Chinese companies: Huawei Technologies (Huawei) and ZTE Corp (ZTE). Huawei was the holder of a patent, which it had declared to be essential to practise the Long Term Evolution (LTE) standard published by the European Telecommunications Standards Institute (ETSI). As part of the standard setting process, Huawei had agreed to license that patent on FRAND terms to parties seeking to implement the standard. ZTE was one such party. Huawei and ZTE had negotiations on the licensing terms and royalty rate, but did not reach agreement. Huawei then sought an injunction in Germany against ZTE for using its patent without a licence. ZTE raised a competition law defence, arguing that seeking an injunction was an abuse of Huawei's dominant position in the market for the licensing of the technologies as specified in the LTE standard technical specifications and was contrary to Article 102 TFEU.

The Düsseldorf court asked for guidance from the ECJ as to whether, when assessing whether Huawei's behavior was abusive, it should follow the well-established German practice (*Orange Book*) or the approach more recently advanced by the European Commission in its *Samsung* and *Motorola* decisions.³

The *Orange Book* judgment by the German Federal Court of Justice (Bundesgerichtshof)⁴ handed down in 6 May 2009 provides that a competition law defence may be relied on by the alleged patent infringer to prevent the grant of an injunction only in exceptional cases. In that case it was found that a claimant seeking an injunction on *de facto* essential patents (where no FRAND commitment had been given) only abuses its dominant position by seeking an injunction if the alleged infringer:

a) unconditionally offers to enter into a licence agreement with the SEP holder at a rate that is so high that the plaintiff cannot reasonably refuse or at a rate to be determined by the plaintiff but being subject to court review and adjustment; and

b) behaves as if it were an actual licensee, i.e. renders account of its acts for use of the patent and pays royalties (albeit in an escrow account for as long as the patent holder does not accept the licence agreement offer).

It is up to the defendant to prove that the two conditions are fulfilled. The “unconditional nature of the offer” means, in particular, that the offer should not be conditional on a court holding that the alleged infringer’s behaviour did in fact infringe the patent. In practice, this makes the competition law defence very unattractive, in particular because a number of lower German courts basically required the defendant to waive all defences with regard to non-infringement and invalidity of the patent.

The other alternative was the approach taken by the European Commission (EC) in its decisions against Motorola and Samsung adopted on 29 April 2014.⁵ In these decisions, the EC suggested a broader application of Article 102 TFEU to injunctions brought by SEP holders which had given a FRAND commitment (which was not the case in *Orange Book* itself). The EC concluded that a patent holder abuses its dominant position when, having given a FRAND commitment over a SEP to a standard setting body, it seeks an injunction against a “willing” licensee.⁶ The EC explained that if the alleged infringer agreed to take a licence and to be bound by a determination of the FRAND royalties by the relevant court or arbitration tribunal, it is considered a “willing licensee” and no injunction should be granted.⁷ The EC also clarified that a willing licensee remained free to challenge the validity of the patent, its alleged infringement, and the essentiality of the SEPs under licence,⁸ since “*it is in the public interest to allow challenges to the validity of patents and to ensure that royalties are not unduly paid.*”⁹

The Düsseldorf court found that applying the *Orange-Book-Standard* to the *Huawei v ZTE* case would lead it to issue the requested injunction, while applying the principles set out in the Samsung press release might lead it to dismiss Huawei’s action for injunction based on the competition law defence under Article 102 TFEU (depending on what was considered sufficient to be a willing licensee).

The ECJ judgment

The question of when a SEP holder is dominant was not addressed

At the outset of its analysis, the ECJ noted that the existence of Huawei's dominant position was not an issue before the Court. Finding whether a company holds a dominant position on a specific relevant market is a pre-condition for invoking Article 102 TFEU and the definition of the relevant market is of vital significance for the appraisal of dominance.¹⁰ However, the questions posed by the Düsseldorf court to the ECJ in *Huawei v ZTE* related only to the existence of an abuse.¹¹ The ECJ has jurisdiction only to give rulings on the interpretation or the validity of a provision of EU law on the basis of the facts put before it by the national court.¹² In this case the referring court stated that Huawei "unquestionably" holds a dominant position, without any request for the ECJ to clarify the approach it should take, meaning that the ECJ did not have the jurisdiction to examine that point.¹³

Thus the Court did not address an important issue – which was nonetheless raised by the Dutch government at the oral hearing and considered by Advocate General Wathelet in his Opinion – namely whether a SEP holder is *per se* in a dominant position by virtue of having a patent that is essential to a standard. In his Opinion on the case, the Advocate General, noted that the fact that an undertaking owned a SEP did not automatically mean that it held a dominant position. Rather in his view holding a SEP raised a rebuttable presumption of dominance, but that question needed to be examined by the national court on a case by case basis.¹⁴ This is in line with the Horizontal Guidelines¹⁵ and *Motorola* where the EC concluded that the mere holding of a SEP or the exercise of related rights does not confer dominance in and of itself.¹⁶ The Advocate General had also expressed caution about assuming that all SEP holders are dominant, in light of the special responsibility not to allow its conduct to impair genuine competition which a dominant position imposes on the undertaking concerned. He noted that a finding of dominance cannot therefore be based on hypotheses.¹⁷

In the *Samsung* case, the EC found that the company held a dominant position "*in the markets for the licensing of the technologies as specified in the UMTS standard technical specifications, on which each of its UMTS SEPs reads*" on the basis of a number of factors, including the widespread adoption of the UMTS standard and the fact that industry players were "locked-in."¹⁸ In *Motorola* the EC concluded that the company held a dominant position "*on the EEA market for the licensing of the technology, as specified in the GPRS standard technical specifications, on which Motorola's Cudak GPRS SEP reads,*"¹⁹ after assessing a number of factors, the most important being the indispensability of the GPRS standard, the industry "lock-in" to that standard.²⁰

Although the better view is that SEP holders should not *per se* be presumed dominant, given that the factors set out in *Samsung* / *Motorola* will apply to many SEPs, a SEP holder which

has given a FRAND commitment is likely to have to follow the steps set out in the Huawei judgment if it wishes to seek an injunction.

SEP holders who agree to license under FRAND create legitimate expectations

The need to maintain the right balance between competition rules and protection of intellectual property (IP) rights as well as the right to effective judicial protection is at the heart of *Huawei v ZTE*. The ECJ started its analysis by referring to the classic case law on compulsory licensing under which, the exercise of an IP right (e.g., by bringing an infringement action) cannot in itself constitute an abuse of a dominant position.²¹ Enforcement of IP rights violates competition rules only in exceptional circumstances.²² The ECJ focused on two main factors (the second of which distinguishes this case from the previous case law on compulsory licensing):

- the indispensability of the patent at issue, in the sense that it is essential to a standard established by a standardization body, rendering its use indispensable to all competitors that envisage manufacturing products complying with the standard to which the patent is linked;²³ and
- the fact that the SEP status was given in return for the proprietor's irrevocable undertaking to the standardization body that it is prepared to grant licences on FRAND terms, in conjunction with the fact that SEP status means that its proprietor 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.²⁴

These two circumstances “*create legitimate expectations on the part of third parties that the proprietor of the SEP will in fact grant licences on such terms,*” and therefore “*a refusal [...] to grant a licence on those terms*” may, in principle, constitute an abuse within the meaning of Article 102 TFEU and could be raised as a defence in actions for a prohibitory injunction or for the recall of products.²⁵

The reference in the judgment to “competitors” is intriguing. How to interpret it? Would we be going too far to read it as suggesting that a different legal standard may apply to a pure licensing entity, which is not a competing manufacturer, when it seeks an injunction? Probably – as such an interpretation is not borne out by the operative part of the judgment, which on its face applies to all SEP holders who seek an injunction. Perhaps the reference to competitors simply reflects the underlying facts of the case, i.e. it was between two companies that are competing manufacturers.²⁶

The requirements with which a dominant SEP holder needs to comply before seeking an injunction

The ECJ noted that SEP holders cannot be denied judicial protection and therefore should have recourse to legal proceedings to ensure effective enforcement of their exclusive rights.²⁷ Indeed, a SEP holder is not prevented from enforcing its patent, but only obliged to grant a licence on FRAND terms. However, in order to prevent an action for a prohibitory injunction from being regarded as abusive, a SEP holder must comply with conditions which seek to ensure “a fair balance of the interests concerned.”²⁸ As the ECJ put it, the irrevocable offer to grant licences on FRAND terms justifies “the imposition on that [SEP holder] of an obligation to comply with specific requirements when bringing actions against alleged infringers.”²⁹ The judgment sets out in detail these requirements and explains the legal framework under which FRAND licences of SEPs should be negotiated before an injunction is sought.

The requirements on the SEP holder as described below are cumulative and need to be fulfilled in the order presented by the judgment for the SEP holder legally to be able to seek an injunction.

First, the SEP holder must alert the SEP user, by giving notice or engaging in prior consultation, of the alleged infringement by designating the SEP at issue and specifying the way in which it has been infringed.³⁰ This criterion is justified because the SEP user may not be aware that it infringed a patent, due to the large number of SEPs which exist.³¹

Second, after the SEP user has expressed its willingness to take a FRAND licence, the SEP holder must present to the SEP user a specific, written offer for a licence on FRAND terms, specifying the amount of the royalty and the way that royalty is to be calculated.³² This requirement stems from the SEP holder’s commitment to limit its exclusive IP right by licensing it on FRAND terms. The SEP holder has also the necessary information to comply with the principle of non-discrimination, in particular, if it has already granted other licences. This requirement of a written offer as a prelude to discussion goes beyond the approach of the EC in *Motorola/Samsung*, i.e., it is an additional requirement. The ECJ did not explicitly address this issue, but presumably if the national court does not consider that the offer made by the SEP holder falls within the limits of what could be considered FRAND, then no injunction can be granted.

Once the SEP holder has fulfilled these requirements, it is up to the SEP user to take action if it is to be able to rely on a competition law defence to resist the granting of an injunction.

First, the SEP user must diligently respond to the SEP holder’s written offer, “in accordance with recognized commercial practices in the field and in good faith, a point which must be established on the basis of objective factors and which implies, in particular, that there are

no delaying tactics.” Should the SEP user not accept the SEP holder’s offer, it has to submit, promptly and in writing, a specific counter-offer that corresponds to FRAND terms.³³

Second, if the SEP user is using the teaching of the SEP prior to the conclusion of a licensing agreement, it must provide appropriate security from the point at which its counter-offer is rejected, which must include the number of past acts of use of the SEP for which the SEP user must be able to render account.³⁴ Security can be provided by, for example, providing a bank guarantee or placing the necessary amounts on deposit.³⁵ The question of what would amount to “appropriate” security would be for a national court to determine.

The ECJ also added that if no agreement is reached after this round of offer and 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.*”³⁶ It is not entirely clear whether this is a “requirement” to be fulfilled before an injunction could be issued. It appears that this is of less relevance than the four requirements listed above, given that this point is not included in the operative part of the judgment, which is the part that binds the national court. This is another difference in emphasis from the EC’s approach in *Samsung* and *Motorola*.

In addition, the ECJ clarified that a SEP user “*cannot be criticized*” for challenging, in parallel to the negotiations relating to the grant of licences, the validity of the relevant SEPs, their essential nature to the standard, or their actual use.³⁷ This is in line with the EC’s views expressed in the *Motorola* and *Samsung* cases as described above.

Finally, the ECJ made clear that the above requirements do not apply to actions seeking the rendering of accounts in relation to past acts of use of the SEP at issue or an award of damages in respect to those acts of use, because such actions do not directly affect competitors marketing products complying with the standard in question.³⁸

Implications of the judgment: in the EU, Germany and globally

The detailed guidelines set by the ECJ establish a procedural framework for SEP holders and SEP users seeking injunctive relief. SEP holders cannot go to court seeking an injunction against a willing licensee where the patent holder has committed to license its technology on FRAND terms unless specific requirements are fulfilled and specifically if they have not made an initial FRAND license offer. The judgment limits the possibility to use the threat of an injunction against users of a standardized technology, if the latter are prepared to take a licence under valid patents which they actually use. On the other hand, requirements are also imposed on SEP users which need to engage in specific steps before being able to argue that an injunction is abusive: the SEP user will have to present its own FRAND counter-offer. It seems that a declaration to be bound by a FRAND rate set by a court or arbitrator (which made a SEP user a “willing licensee” under the EC decisions) would have to follow the specific steps

(SEP user presents a counter-offer following SEP holder's offer) set out by the judgment. While the ECJ's test requires the SEP holder to present a FRAND offer to the SEP user, specifying the amount of royalty and the way the royalty is calculated, the ECJ did not define FRAND (indeed it was not asked to do so by the national court). The judgment does however suggest that there is not one single right view of FRAND in any particular licensing discussion, given that the SEP user is able to submit its FRAND counter-offer to a FRAND offer by the SEP holder. So FRAND is something that is negotiable and two different offers could be both FRAND. Accordingly, though the ruling is clear as to the procedures that have to be followed to obtain an injunction, it will not end, but only shift, the focus of the controversies in SEP cases pending before national courts.

Furthermore, the judgment, coming as it does on top of the EC's *Samsung* and *Motorola* decisions, will significantly change the balance of German SEP litigation and shift the burden of proof. So far, Germany has been a forum of choice for European patent litigation. German courts have been generous in granting injunctions for patent infringements and have taken the view that competition law defences generally do not bar an injunction, even if the litigation concerns a SEP. Accordingly, it was the defendant's burden to prove all the elements of a competition law defence. Under the ECJ's approach, the SEP holder seeking injunctive relief will be obliged to prove that he approached the infringer and offered him an agreement on FRAND terms. If the defendant contests the FRAND assertion, for example on the basis of its own FRAND royalty calculation, the court will have to appoint an expert to resolve this issue. This will likely be time-consuming and costly.

Finally, the judgment once again shows the global reach and driving role of EU competition law in the technology sector and, indeed, in all sectors where IP plays an important role. An interesting feature of the case is that no European companies are involved. It is a battle between two big Chinese tech companies, Huawei and ZTE. The choice of Europe for a tech dispute between global players is not new – Sun and Real Networks took their battle with Microsoft to Brussels over 15 years ago. However, it is perhaps a sign of changing times that a key EU decision is being set for the first time by Chinese tech giants rather than US ones.

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- ¹ Respectively, Partner and Associate in the Brussels office of White & Case LLP. The opinions expressed in this article are personal to the authors and do not necessarily represent the opinions of either White & Case LLP or any of its clients.
- ² C-170/ 13 *Huawei v ZTE*, EU:C:2015:477 (Judgment).
- ³ The details of the *Motorola* and *Samsung* decisions were not public at the time the Düsseldorf court made the reference to the ECJ. At the time only the EC press releases were available.
- ⁴ KZR 39/06.
- ⁵ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*; Commission decision of 29 April 2014, Case AT.39939 – *Samsung - Enforcement of UMTS Standard Essential Patents*.
- ⁶ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*, recital 427.
- ⁷ *Ibid.*, recital 437.
- ⁸ Commission decision of 29 April 2014, Case AT.39939 – *Samsung - Enforcement of UMTS Standard Essential Patents*, recitals 99 and 107. In particular, in *Samsung* the EC held that the applicable rules on burden of proof in litigation regarding challenges of the patent licensing agreement will not be altered and that “*the court will be requested by the parties, and the arbitration tribunal shall take into account issues of validity, infringement and essentiality.*”
- ⁹ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*, para. 491. This ensures that “*companies, and ultimately consumers, are not obliged to pay for patents that are not infringed.*” (see Commission MEMO of 29 April 2014, available at [http://europa.eu/rapid/press-release MEMO-14-322_en.htm](http://europa.eu/rapid/press-release_MEMO-14-322_en.htm))
- ¹⁰ C-6/72, *Continental Can v Commission*, EU: C:1973:2, para. 32; C-49/07, *Motosykletistiki Omospondia Ellados NPID (MOTOE) v Elliniko Dimosio*, EU:C:2008:376, para. 31.
- ¹¹ Judgment, para. 43.
- ¹² C-138/08, *Hochtief and Linde-Kca-Dresden*, EU:C:2009:627, para. 22.
- ¹³ AG Wathelet Opinion in C-170/ 13 *Huawei v ZTE* delivered on 20 November 2014 (AG Wathelet Opinion), para. 57 and footnote 20.
- ¹⁴ *Ibid.*, para. 57. See also footnote 26 where the Advocate General cites C-457/10 P *AstraZeneca v Commission*, para. 186 (“*although the mere possession of intellectual property rights cannot be considered to confer such a position, their possession is none the less capable, in certain circumstances, of creating a dominant position, in particular by enabling an undertaking to prevent effective competition on the market.*”)
- ¹⁵ Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements (Horizontal Co-operation Guidelines), para. 269: “*(...) even if the establishment of a standard can create or increase the market power of IPR holders possessing IPR essential to the standard, there is no presumption that holding or exercising IPR essential to a standard equates to the possession or exercise of market power. The question of market power can only be assessed on a case by case basis.*”
- ¹⁶ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*, recital 211.
- ¹⁷ AG Wathelet Opinion, para. 58.
- ¹⁸ Commission decision of 29 April 2014, Case AT.39939 – *Samsung - Enforcement of UMTS Standard Essential Patents*, paras 45-51.

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- ¹⁹ Commission decision of 29 April 2014, Case AT.39985 - Motorola – Enforcement of GPRS Standard Essential Patents para. 269.
- ²⁰ *Ibid.*, para. 226.
- ²¹ Judgment, paras 42 and 47.
- ²² *Ibid.*, para. 46. See also C- 238/87 *Volvo v. Veng*, EU:C:1988:477, para. 8, C 241/91 P and C 242/91 P RTE and ITP v Commission, EU:C:1995:98, para 33; C 418/01 *IMS Health v. NDC Health GmbH*, EU:C:2004:257, para. 34.
- ²³ Judgment, paras 49-57.
- ²⁴ *Ibid.*, paras 51-52.
- ²⁵ *Ibid.*, paras 53-54.
- ²⁶ The EU Commissioner in a recent speech at the International Bar Conference in Florence on 11 September 2015 stated that the principles of the judgment should not be limited to manufacturers of devices using the essential technology, but also apply to companies at other levels of the distribution chain, for example telecom operators. In that context, it is understood that the EC has requested information from the parties involved in a patent dispute initiated by Saint Lawrence, a patent licensing company and subsidiary of US-based Acacia, against Deutsche Telekom for distributing (but not producing) handsets using Saint Lawrence’s technology.
- ²⁷ Judgment, paras 57 – 58.
- ²⁸ *Ibid.*, para. 55.
- ²⁹ *Ibid.*, para. 59.
- ³⁰ *Ibid.*, paras 60-61.
- ³¹ *Ibid.*, para. 62.
- ³² *Ibid.*, paras 63-64. This differs from AG Wathelet’s Opinion which opined that, after alerting the SEP user, the SEP holder had, “*in any event*,” to present a written offer for a license on FRAND terms (AG Whatelet Opinion, para. 85).
- ³³ Judgment, paras 65-66.
- ³⁴ This conclusion differs from the Advocate General’s Opinion, which did not consider that security should be proactively provided in order for the Article 102 TFEU defence to succeed.
- ³⁵ Judgment, para. 67.
- ³⁶ *Ibid.*, para. 66.
- ³⁷ *Ibid.*, para. 69.
- ³⁸ *Ibid.*, paras 72-76.



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HUAWEI v ZTE: Judicial Conservatism at the Patent-Antitrust Intersection

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HUAWEI v ZTE: Judicial Conservatism at the Patent-Antitrust Intersection

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I. INTRODUCTION

At its core, the preliminary ruling of the Court of Justice of the European Union (“CJEU”) in *Huawei v ZTE* explains whether, and if so how, holders of FRAND-pledged Standard-Essential Patents (“SEPs”) abuse a dominant position under Article 102 TFEU when they apply for an injunction and/or product recall against unlicensed implementers of their technology.²

Huawei v ZTE has several specific features. First, it is a judgment of the upper court of the European Union. Only this Court can provide a definitive interpretation of Article 102 TFEU. Once affirmed, CJEU-made law applies to all stakeholders in Europe.³ With this, *Huawei v ZTE* can be expected to set an EU-wide antitrust standard on the question of injunctive relief for FRAND-pledged SEPs.

Second, judgments issued under the preliminary rulings procedure relate to questions of law, not facts.⁴ Neither their reasoning, nor their operative parts, lend themselves to much distinguishing on grounds of case-specificity, beyond the factual framework delineated in the question addressed to the Court. In *Huawei v ZTE*, the questions referred to the Court were phrased in large terms and concerned the conduct of holders of FRAND-pledged SEPs generally. *Huawei v ZTE* can thus be deemed to talk of principles.

This short paper contends that *Huawei v ZTE* is a conservative judgment. It only extends by a razor-thin margin the zone of antitrust liability for patent owners. The *Huawei v ZTE* Court is reluctant to relax its traditional case-law that affirms antitrust liability on patent owners only in

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² See CJEU, *Huawei v ZTE*, 16 July 2015, not yet reported. To put things in context, Article 102 TFEU allegations have been raised before national patent courts as a shield to infringement proceedings by unlicensed implementers. Article 102 TFEU allegations have also been made as a sword against SEP holders before and by competition agencies across the world.

³ It must therefore be observed by all subordinate courts, antitrust agencies, and natural and legal persons subject to their jurisdiction, including foreign firms. See CJEU, Joined cases 28 to 30-62, *Da Costa en Schaake NV, Jacob Meijer NV, Hoechst-Holland NV v Netherlands Inland Revenue Administration*, ECR, 0031 p.69.

⁴ See CJEU, Recommendation to national courts and tribunals in relation to the initiation of preliminary ruling proceedings, (2012/C 338/01), ¶ 7: “As stated above, under the preliminary ruling procedure the Court’s role is to give an interpretation of European Union law or to rule on its validity, not to apply that law to the factual situation underlying the main proceedings. That is the task of the national court or tribunal and it is not, therefore, for the Court either to decide issues of fact raised in the main proceedings or to resolve any differences of opinion on the interpretation or application of rules of national law.”

“exceptional circumstances.” To be sure, the Court admits that SEPs covered by a FRAND pledge generate “particular circumstances,” which justify an extension of antitrust liability.⁵ But on close read, the Court only expands antitrust liability in relation to a slice of cases of injunctions on FRAND-pledged SEPs that lead to exclusionary leveraging.

In contrast, *Huawei v ZTE* does not seem to contemplate any antitrust liability against firms that use injunctions on FRAND-pledged SEPs to extract “unfair” licensing terms, a problem mundanely described as “patent hold-up.”⁶ This is significant, because the Court was perfectly free to frame Article 102 TFEU liability in terms both of abusive exclusion and exploitation, as the Commission did in its *Motorola* and *Samsung* enforcement initiatives which actually prompted the *Huawei v ZTE* reference of the German Court in the first place.

After *Huawei v ZTE*, the basis for antitrust liability against FRAND-pledged SEPs holders is thus very thin. With this, the judgment may also have ramifications on ongoing antitrust cases, in particular those started against a subset of upstream licensing entities—also often referred as Non Practicing Entities (“NPEs”) or Patent Assertion Entities (“PAEs”)⁷—for those firms do not generally purport to, and cannot, engage in anticompetitive leveraging.

II. FROM EXISTENCE OF ABUSE, TO ABSENCE OF ABUSE

The referring German court questioned the CJEU on the “existence of an abuse,” and the conditions thereof.⁸ Instead, the CJEU reverses the perspective. It proceeds to explain, throughout the judgment, the circumstances in which an application for an injunction and/or product recall does not constitute an abuse. The reasoning of the CJEU could not be less clear. At paragraph 55, the Court talks about how “the proprietor of an SEP” can “prevent an action for a prohibitory injunction or for the recall of products from being regarded as abusive.”⁹ After setting out a long list of “conditions” relating to the SEP holder’s conduct, the Court repeats, at paragraph 71, that a SEP holder that complies with those prescriptions “does not abuse its

⁵ See CJEU, *Huawei v ZTE*, ¶ 48.

⁶ For an early formulation, see Mark A. Lemley & Carl Shapiro, *Patent Holdup and Royalty Stacking*, 85 TEXAS L. REV. (1992).

⁷ As noted in the European Commission JRC Science and Policy Report, Innovation in the Digital Single Market: The Role of Patents, 17 March 2015: “The preliminary ruling is also expected to have ramifications for the future of Patent Assertion Entities (PAE) practices. In particular, concerns are voiced over possible abuse of the enforcement system and the UPC procedure by PAE.” See also, *Management Plan 2015, DG Competition*, at 34-35 [2015], available at http://ec.europa.eu/atwork/synthesis/amp/doc/comp_mp_en.pdf: “The Commission further observes that a phenomenon coming with the proliferation of IT patents and patent litigations is the emergence of so-called non-practising entities (NPEs). There are companies which are not involved in R&D activities or in the manufacturing or sale of goods or services, but whose business is limited to the acquisition and enforcement of patent and patent portfolios. In Europe, it is expected that NPEs will become more active with the installation of the new unitary European patent and the new Unified Patent Court which will allow for European-wide enforcement of patents. Competition law obligations with regard to patents, and in particular SEPs, apply in the same way to NPEs as to any other company”; A. Italianer, Director-General for Competition, European Commission, “Shaken, not stirred. Competition Law Enforcement and Standard Essential Patents” (Apr. 21, 2015): “We will remain on guard in our antitrust enforcement. Because holders of SEPs find new ways of challenging alleged patent infringement. In a recent case before the [German] Mannheim district court, the SEP-holder sued not the *producer* of the phone, but the *distributor* of the phone: Deutsche Telekom. This is a new development and we are watching it closely”.

⁸ *Id.*, ¶ 43.

⁹ *Id.*, ¶ 55.

dominant position ... by bringing an action for infringement.”¹⁰ Finally, the operative part of the judgment, which is the response to the German court, is again worded in terms of the conditions under which Article 102 TFEU can be deemed inapplicable.

In plain words, the German court asked the Court: Can you tell me when there is abuse? And the Court responded: No, I will tell you when there is no abuse. This is subtle, and as a result *Huawei v ZTE* is not primarily about antitrust liability. It is predominantly about antitrust immunity.

III. LIABILITY FOR PRACTICING ENTITIES, IMMUNITY FOR UPSTREAM LICENSING ENTITIES

Huawei v ZTE only finds antitrust liability against SEPs holders that manufacture or sell products on the basis of the licensed technology. Paragraph 52 of the judgment explains the sort of antitrust concerns which the Court finds are raised by injunctions on FRAND-pledged SEPs: a SEP owner “can prevent products manufactured by competitors from appearing or remaining on the market and **thereby reserve to itself the manufacture of the product in question** (emphasis added).”¹¹ Actions for injunctions and/or product recall are problematic because SEP owners with a certain degree of vertical integration can monopolize the manufacturing market.

Readers well versed in antitrust law will recognize here the classic anticompetitive leveraging scenario for Article 102 TFEU liability.¹² An actual or potential degree of vertical integration in manufacturing by the SEP holder is necessary to trigger a finding of abuse. The practical implication of this is that upstream licensing entities remain immune from Article 102 TFEU liability for this type of conduct.

In the antitrust field, some stakeholders contend that the Court’s holding in *Huawei v ZTE* is much broader.¹³ They argue that the FRAND commitment generates antitrust liability in itself, *vis-a-vis* an indefinite number of third parties, and regardless of whether the SEP owner who gave the commitment is or not vertically integrated. Their argument is based on paragraph 53 of the judgment, which says that “an undertaking to grant licences on FRAND terms creates legitimate expectations on the part of third parties” such that a “refusal by the proprietor of the SEP to grant a licence on those terms may, in principle, constitute an abuse within the meaning of Article 102 TFEU.”¹⁴

This reading is specious. Paragraph 53 opens with “In those circumstances.” It is thus safe to assume, given our numeral system, that paragraph 53 chimes with paragraph 52, and that the “circumstances in which FRAND terms create legitimate expectations” are those in which a vertically integrated SEP owner initiates infringement proceedings.

¹⁰ *Id.*, ¶ 71.

¹¹ *Id.*, ¶ 52.

¹² For an early formulation, see Aaron Director & Edward Hirsch Levi, *Law and the Future: Trade Regulation*, 51 NORTHWESTERN UNIV. L. REV. 281 (1956): “The doctrine of abuses sees them as exclusionary devices useful for getting a monopoly, or expanding it, or for moving from one monopoly to the creation of another. Thus when vertical integration is concerned, the inquiry is often as to the “leverage” of the device.”

¹³ See speech of Commissioner Vestager, 11 September 2015, 19th IBA Conference, Florence, *available at* https://ec.europa.eu/commission/2014-2019/vestager/announcements/intellectual-property-and-competition_en

¹⁴ *Id.*, ¶ 53.

IV. ANTITRUST LIABILITY VIS A VIS COMPETITORS

Like it or not, the other implication of the anticompetitive leveraging theory of liability endorsed in *Huawei v ZTE* is that it is only abusive for a SEP holder to seek an injunction and/or product recall against an implementer with whom it does (or will) compete in a market. This, in turn, implies that a SEP owner with upstream manufacturing activities (e.g., a networking equipment provider) remains free to start injunction and/or product recall proceedings against an unlicensed downstream manufacturer (e.g., a handset manufacturer) with whom it does not compete. And this makes perfect sense, because as is well-known, only a relevant market is worth monopolizing.

V. ANTITRUST LIABILITY FOR EXCLUSION OF COMPETITORS, NOT EXPLOITATION

Though this is a subtle nuance, the *Huawei v ZTE* Court's antitrust concern is one of anticompetitive exclusion, not exploitation. The Court is silent on the alleged risk that SEPs owners resort to patent litigation to charge unFRAND licensing terms from rival implementers. Instead, it is vocal on risks of anticompetitive foreclosure.

At first glance, this omission looks mysterious. The patent hold-up/royalty stacking theory has fueled many antitrust initiatives, including the Commission's *Motorola* decision which devoted 15 of the 17 pages on "anticompetitive effects" to its discussion.¹⁵

Did the patent hold-up theory fall through the cracks of judicial proceedings? This is unlikely. The question of patent hold-up (and hold-out) had been placed front and center before the CJEU, which mentions it in its ruling.¹⁶ And even before this, patent hold-up was mentioned in the December 21, 2012 Press Release which prompted the reference from the German court,¹⁷ at the oral hearing, and in the Opinion of Advocate General Wathelet.¹⁸

All this confirms that the question of hold-up had entered the scope of the proceedings brought before the CJEU. And it kills for good the argument that *Huawei v ZTE* was not a case about hold-up, so that the Court could not allegedly reason the case in terms of abusive exploitation.

Against this background, the Court's silence conveys a message, but which one? Does it repudiate the hold-up/royalty stacking theory? Maybe. Is it reluctant to let antitrust enforcers interfere with the price system, and believe that the national courts system adequately deals with such issues in the context of FRAND setting proceedings? This is more likely.

¹⁵ See Commission Decision, Case AT.39985 – Motorola – Enforcement of GPRS Standard Essential Patents, 29 April 2014.

¹⁶ See CJEU, *Huawei v ZTE*, *supra* note 2, ¶ 38.

¹⁷ See EU Commission, Press Release, Brussels, 21 December 2012, Antitrust: Commission sends Statement of Objections to Samsung on potential misuse of mobile phone standard-essential patents: "Standards bodies generally require members to commit to license patents that they have declared essential for a standard on FRAND terms. This commitment is designed to ensure effective access to a standard for all market players and to prevent "hold-up" by a single SEP holder, since access to those patents which are standard-essential is a precondition for any company to sell interoperable products in the market."

¹⁸ See AG Wathelet Opinion under *Huawei v ZTE*, FN 50.

VI. PATENTEE (ANTITRUST) OR IMPLEMENTER (IP) LIABILITY FOR NEGOTIATION BREAKDOWN

The *Huawei v ZTE* Court ascribes procedural courtesy obligations to a FRAND pledge. Interestingly, those rules of conduct apply both to the SEP holder and to the infringer.

The Court seems to use the threat of antitrust (abuse) and IP (injunction) liability as backstops, to discipline both SEP holder and infringer in order that they converge towards a mutually agreeable FRAND royalty level (a process denoted by the inverted trapezoid figure below).¹⁹ This leads the CJEU to map out the negotiation process that should be followed by SEPs holders who have given a FRAND commitment if they wish to stay clear of the strictures of antitrust enforcement, and by unlicensed infringers who wish to resist actions for injunctions and product recall.

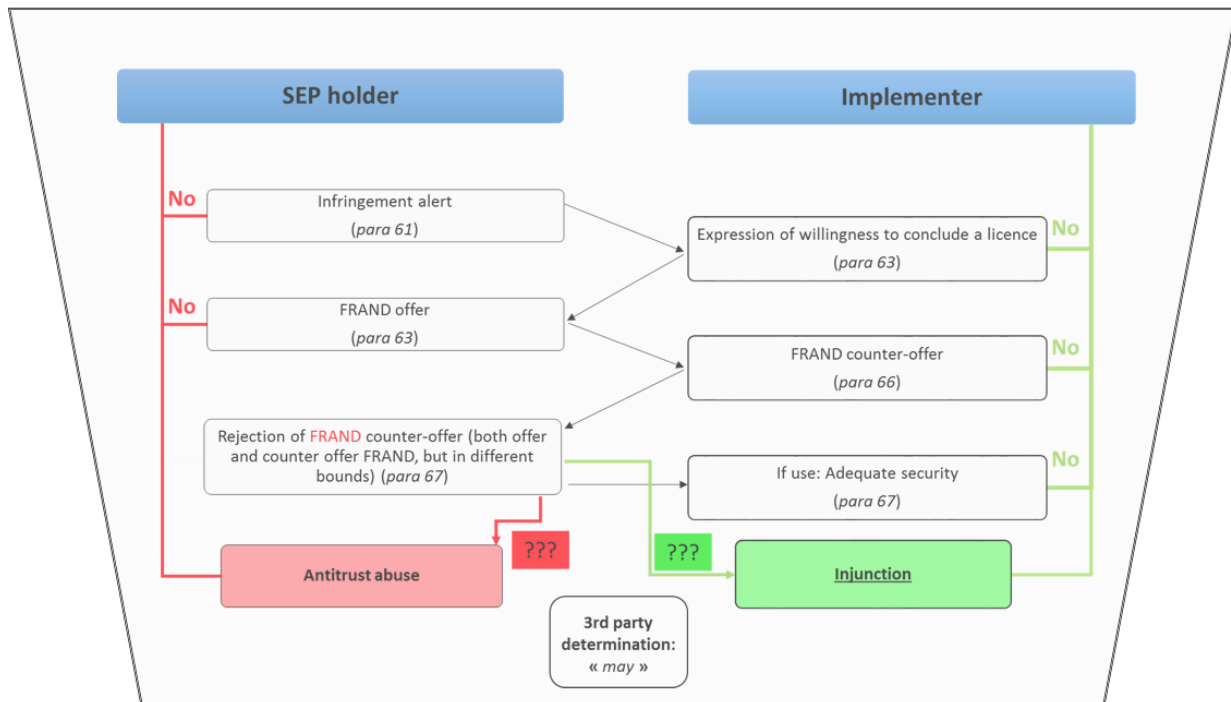
From an antitrust standpoint, this is interesting, because the SEP holder retains at several junctures the freedom to start injunction/product recalls actions, “as long as” he observes a certain procedural courtesy.²⁰ Instead of reciting the process, let us identify the circumstances in which injunctions relating to FRAND-pledged SEPs remain available: if in response to a notice of infringement, the implementer does nothing; in response to the initial FRAND offer of the SEP holder, the implementer does not submit a FRAND counter offer, or submits an UNFRAND counter offer, or submits a FRAND counter offer but practices the SEP without putting royalties into escrow; in case the offer is on the higher bound of the FRAND range and the counter-offer is in the lower bound, though this conclusion remains unclear from the judgment (see question marks in the figure below). Conversely, a finding of antitrust liability can arise when the SEP holder starts infringement proceedings: without prior alert; before making a FRAND offer

Moreover, the Court steers clear from laying down detailed FRAND pricing principles. In fairness, this was not unexpected. The referring Court had not queried the Court on the meaning of FRAND. That said, the Court suggests that it is not an UNFRAND counter-offer, or UNFRAND behavior, for the licensee to challenge the validity or essentiality of the SEP.²¹

¹⁹ Figure reproduced and adapted from N. Banasevic, *The Implications of the ECJ's Huawei/ZTE Judgment*, BRUSSELS MATTERS, (17 September 2015).

²⁰ See CJEU, *Huawei v ZTE*, *supra* note 2, ¶ 71.

²¹ *Id.*, ¶ 69.



VII. FRAND IS A RANGE, NOT A PIXEL PRICE

Even though the *Huawei v ZTE* Court does not address FRAND pricing, it acknowledges that both parties can make FRAND offers and counter-offers and, in spite of this, remain in disagreement.

This gives currency to the view that there is not a pixelized FRAND point, and that several distributional prices exist that are FRAND. In particular, if the SEP holder makes a FRAND offer in the upper bound, and the implementer makes a FRAND counter-offer in the lower bound, the parties “may” submit their dispute to third-party determination. But if they disagree over this, the ultimate question is what happens. And on this, the Court gives no guidance.

VIII. CONCLUSION

Huawei v ZTE does not address comprehensively all issues related to standards, patents, and antitrust policy: e.g. dominance, standards competition, countervailing buyer power among SEP holders, portfolio licensing, Non-SEPS, *De facto* standards, FRAND pricing, valuation techniques, etc.

It suggests, however, that beyond competitor exclusion, there is little space for antitrust policy in disputes relating to FRAND-pledged SEPs. Advocate General Wathelet had recognized the existence of distributional, bargaining, and revenue-sharing problems among Standard

Setting Organizations (“SSOs”) participants.²² His Opinion urged SSOs to address those problems internally, and to use only antitrust law as a “last resort.”²³

The *Huawei v ZTE* Court goes further. In the context of FRAND-pledged SEPs, the law on abuse of dominance applies only to the exclusion of rivals.²⁴ Its reach is limited, and does not encompass the conditions at which SEP licenses are granted, unless they amount to a refusal to license. Disputes over such conditions seem left to the wisdom of national courts.

The Court could have sought to address the alleged hold-up problem. An obvious route, for instance, would have been to tell the German judge that an injunction or product recall action is abusive when it leads to “unfair selling prices,” within the meaning of Article 102 (a) TFEU. It did not. And this contrasts with the judicial activism of the Court in other areas, where it has resorted to Article 102 (a) TFEU of its own motion, to establish antitrust liability.²⁵

After *Huawei v ZTE*, it is predictable that some stakeholders with an iron in the fire—in particular those who have railed and taken steps against so-called “patent trolls”—will contend that Article 102 TFEU remains applicable to the conduct of NPEs on the ground that the case referred to the CJEU concerned competing firms, and that the Court could not possibly talk of NPEs conduct. This does not only ignore the nature of preliminary rulings. It also obfuscates that the question referred by the German court drew no distinction between the conduct of upstream licensing entities and practicing entities, and talked of owners of FRAND-pledged SEPs generally. Moreover, the implicit repudiation of the hold-up theory, which is the main type of harm allegedly caused by NPEs, corroborates that Article 102 TFEU does not—in the Court’s view—apply to NPEs.

One could attempt to dwell on the reasons underpinning the Court’s lack of consideration of upstream licensing entities conduct as a possible source of abuse. A tentative one is that the Court believes that hold-up is an issue of less concern than anticompetitive exclusion. Another plausible explanation is the Court’s trust in the national courts to deal with revenue-sharing disputes among industry players.

Unfortunate as it may be for some policy makers, the solution given by the Court of Justice is crystal clear. *Dura lex, sed lex...*

²² See AG Wathelet Opinion under *Huawei v ZTE*, ¶ 11.

²³ *Id.*

²⁴ It also remains arcane on the test of anticompetitive foreclosure that ought to apply to admissible antitrust defenses. Indeed, if the grant of an injunction leads to the removal of products from a given geographic market, it does not flow that large firms with multi-market operations will necessarily be excluded by a simple request for an injunction or product recall. Moreover, EU law connoisseurs know all too well that the notion of “legitimate expectations” is subject to a case-by-case, strict assessment, and that if this is the test to be used, then the first question to address is whether, in the proceedings at hand, the FRAND commitment was likely to generate such expectations.

²⁵ See for instance, in Case C-52/09, *Konkurrensverket v TeliaSonera Sverige AB*, [2011] ECR I-00527, ¶ 25.

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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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***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**

Miguel Rato, Collette Rawnsley, & Mark English¹

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.