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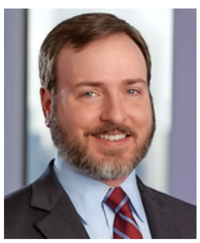
INSIGHTS: Emerging Global Trends in Standard-Essential Patent Litigation, Part II

SEP Litigation

In Part I of this two-part series, Regina Penti, Kevin Post, and Beibei Sun of Ropes & Gray discussed the availability of injunctions in Fair, Reasonable, and Non-Discriminatory (FRAND) cases. This second and final installment discusses trends relating to global licenses and the role of competition law in FRAND cases.



By Regina Penti, Kevin Post, and Beibei Sun

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In many Fair, Reasonable, and Non-Discriminatory (FRAND) cases, the crux of the dispute boils down to: (1) the appropriate scope of the license; and (2) the royalty level — and by extension, the royalty computation methodology. On scope issues, most courts now agree that, generally, a standard essential patent owner does not violate a FRAND commitment by offering or seeking a worldwide license, and also agree that a SEP owner violates its FRAND commitment by bundling SEP and non-SEPs, unless both parties agree. For example, in 2017's *Unwired Planet v. Huawei*, Justice Colin Birss concluded that Unwired Planet's insistence on a worldwide license was reasonable because the vast majority of licenses in the mobile communications industry, including all the comparable licenses used in the case, were granted on a worldwide basis, and that Huawei's markets and Unwired Planet's SEP portfolio were commensurate in their worldwide scope. Thus, he found that a worldwide license would reflect the economic realities of the parties and their industry, while a country-by-country license would be ''madness.'' The European Commission later endorsed this position in its SEP guidelines, noting: ''For products with a global circulation, SEP licenses granted on a worldwide basis may contribute to a more efficient approach and therefore can be compatible with FRAND.'' Similarly, in *TCL v. Ericsson*, Judge James Selna of the U.S. District Court for the Central District of California required that the parties conclude a global license with specified terms, although the decision was likely aided by the fact that both parties requested that the court issue a global license. In *Huawei v. Samsung*, the first major decision from China focusing on an international standard, the Shenzhen court entered an injunction against Samsung subject to the parties successfully negotiating a global cross-license. Like *TCL*, no party in *Samsung* disputed that a global license would be appropriate in a dispute between two global giants. On bundling, the European Commission guidelines note that rights holders cannot require a licensee to accept non-SEPs to license SEPs, and the Shenzhen court recently faulted Samsung for requiring that a global cross-license agreement with Huawei cover both SEPs and non-SEPs.

Despite these points of convergence, there is no settled consensus on FRAND royalty calculations. To date, the four U.S. cases that have set FRAND rates have all used different techniques and made assumptions. In *Microsoft v. Motorola*, Judge James Robart of the U.S. District Court for the Western District of Washington applied a modified *Georgia-Pacific v. U.S. Plywood Corp.* framework to set a FRAND rate, which he then checked using comparable licenses. In *Innovatio IP Ventures*, the court largely followed the *Microsoft* approach, yet determined a royalty rate that was about three times that of the *Microsoft* case for the same standard. In *Ericsson v. D-Link*, reversed and remanded on appeal, the royalty rate was determined by a jury that was instructed to apply an unmodified *Georgia-Pacific* framework. And most recently in *TCL*, Judge Selna applied a ''top-down'' approach, in which a court begins with an aggregate royalty attributable to the standard as a whole, and then allocates a portion of that total to an individual SEP owner based on their proportional contributions to the standard. FRAND cases outside of the U.S. have not clarified matters. For example, in *Unwired Planet*, Justice Birss, after declaring that there can be only a single FRAND rate in any particular circumstance, set out to compute that worldwide rate. He initially analyzed comparable licenses, then checked the computed rate using a top-down approach. Following *Unwired Planet*, the European Commission endorsed a top-down approach in its guidelines, noting that ''an individual SEP cannot be considered in isolation. Parties need to take into account a reasonable aggregate rate for the standard, assessing the overall added value of the technology.'' However, both the European Commission and Judge Selna in *TCL* disagreed that FRAND means a single rate as opposed to a range. And more recently, in *Huawei v. Samsung*, the Shenzhen court applied the top-down approach to determine whether the parties' initial offers were FRAND. However, the Shenzhen court used the number of technical proposals accepted from each party by the standard-setting organization (SSO) as a proxy for the relative strength of the parties' patent portfolios. Judge Selna in *TCL* rejected such an approach.

The result of these varied approaches is, predictably, starkly different royalty rates. For example, although *Unwired Planet* and *TCL* were both directed to the same standards (2G, 3G, and 4G), Judge Selna concluded that there are about twice as many total SEPs for each of these standards as did Justice Birss. Each judge also disagreed with the numbers provided by the parties before it. As a result, the rates produced in *Unwired Planet* were seen as largely favorable to the SEP owner, while the rates in *TCL* were seen as largely favorable to the alleged infringer. In nearly all FRAND cases in the U.S., the rates determined by the courts were lower, sometimes orders of magnitude lower, than the rates demanded by the SEP owners. These differences among courts that purport to resolve a global dispute without consultation with other courts can give rise to tactical behaviors by the parties. For example, given the different outcomes in the U.K.'s *Unwired Planet* and Judge Selna's *TCL*, will we now see patent owners head to the U.K. in pursuit of similar judgment, while conversely, implementers file claims in California? Forum-shopping is not new in litigation, but one wonders whether the possibility of obtaining worldwide rates from any forum, even those with only an arguably tenuous nexus to the dispute, raises the stakes in the race to be first to the courthouse, and could derail the very negotiations these cases are intended to promote.

Indeed, global licensing and enforcement efforts can be further complicated when an offer to license a worldwide portfolio of SEPs is made in the U.S. In two cases involving antisuit injunctions, an implementer has sought to prevent an SEP owner from pursuing litigation involving one or more of those SEPs in jurisdictions other than the U.S. In a 2012 decision in *Microsoft v. Motorola*, the Ninth Circuit affirmed a decision by Judge Robart barring Motorola from pursuing litigation in Germany while Microsoft's breach-of-contract case was pending in district court. There, a German court had found several Motorola SEPs infringed and was preparing to issue an injunction (that was not self-enforcing). In a lengthy opinion, the Ninth Circuit analyzed the factors surrounding anti-suit injunctions and found that the district court's narrow injunction was appropriate, despite the comity concerns raised by Motorola. ''However elusive it may be, comity is not, of course, to be contemplated lightly. Foreign anti-suit injunctions should not be issued routinely. But the record makes clear that the district court gave thoughtful consideration to the importance of international comity and nevertheless determined that under the unique circumstances of this case, an anti-suit injunction was proper.'' More recently, Samsung requested that the U.S. District Court for the Northern District of California enjoin Huawei from enforcing an injunction granted in China that would prevent Samsung from making or selling 4G devices in the Chinese market. Judge William Orrick granted Samsung's request. ''In the absence of an anti-suit injunction, Samsung faces the risk of significant harm, not just in China, but with impacts percolating around the world,'' the judge found. ''The Chinese injunctions would likely force it to accept Huawei's licensing terms, before any court has an opportunity to adjudicate the parties' breach of contract claim.'' These decisions demonstrate that U.S. courts are willing to exercise jurisdiction over a worldwide dispute to adjudicate breach-of-FRAND claims pending in the U.S.

The complexity of these global jurisdictional issues was recently reaffirmed in *Conversant Wireless Licensing v. Huawei, ZTE and Ors*. There, Huawei challenged the jurisdiction of a U.K. court to set a global FRAND license where the U.K. accounts for only 1 percent of Huawei's sales and 0.6 percent of ZTE's sales over which royalties are claimed, and China, where another suit is pending, accounts for the majority of the sales. Rejecting defendants' argument, the U.K. court found that Chinese courts have no jurisdiction to set a global FRAND rate, and that the case was properly characterized as claims for infringement of U.K. patents, notwithstanding that the object of the proceedings was either a global FRAND license or FRAND injunction. It remains to be seen whether other courts will respect each other's independence in such instances. At least in the cases of *Microsoft v. Motorola* and *Huawei v. Samsung*, U.S. courts did not.

Shifting Role of Competition Laws

Antitrust concerns loom large in FRAND cases because of the power-shifting dynamics that come into play when technology is mandated by a widely adopted technical standard. Governmental agencies and private parties routinely claim abuses of power in these cases. Across the globe, however, the antitrust norms and rules regarding SEPs are difficult to assess because of fragmented regulatory schemes that often put multiple agencies in charge of policing them. For example, prior to the consolidation of antitrust enforcement power in the newly formed State Administration for Market Regulation in March 2018, several agencies had a role in policing standards in China, including the Standardization Administration of China, the State Administration for Industry and Commerce, and the National Development and Reform Commission. In the U.S., both the Federal Trade Commission and the Antitrust Division of the Department of Justice have an active policing role in standardization, and seem to disagree on how to police them.

Because the FTC and DOJ are both headed by political appointees, it is not unusual for a policy shift to follow each change in administration. Indeed, an obvious shift in antitrust policing of SEPs in the U.S. appears to be underway. After pursuing a policy aimed at curbing patent hold-up for many years under the previous administration, the current administration seems more concerned with policing the problem of holdout, or at least taking a more hands-off approach. Assistant Attorney General Makan Delrahim, who heads the Antitrust Division of the DOJ, expressed a general preference for contract remedies over antitrust remedies for FRAND violations in public remarks in November 2017, noting that ''excessive use of the antitrust laws rather than other remedies can overlook and undermine the magnitude of investment and risk inventors undertake for the chance at being included in a standard.'' He also indicated that the DOJ would focus on potential antitrust violations by SEP implementers and the SSOs. ''When implementers act together within a standard-setting organization as the gatekeeper to sales of products including a new technology, they have both the motive and means to impose anticompetitive licensing terms. At the extreme, they can shut down a potential new technology in favor of the status quo, all to the detriment of consumers.'' To resolve these issues, he suggested that the Antitrust Division will pay special attention to ''rules that SSOs impose that appear designed specifically to shift bargaining leverage from IP creators to implementers, or vice versa'' or any action that ''appears to be cartel-like anticompetitive behavior among SSO participants, either on the innovator or implementer side.'' For many observers, these comments appear directed to the recent rule changes by the Institute of Electrical and Electronics Engineers, which were largely seen as favoring implementers over SEP owners. In an apparent pushback, FTC Commissioner Terrell McSweeny has emphasized the need for federal agencies to combat patent hold-up and other anticompetitive conduct, noting, ''It would be unfortunate if the antitrust agencies were to unlearn the lessons of over 15 years of scholarship and bipartisan study and question their longstanding support for combating holdup based on vague concerns about over-deterrence.''

The European Commission attempted in its recent guidelines to provide safe harbors that will clarify which behaviors will run afoul of competition law. The new EU guidelines, though not legally binding, adopts safe harbors or defenses that will reduce the antitrust emphasis in SEP cases, which may ultimately reduce the role of competition law in future SEP cases in the EU. In particular, the communication clarifies that an SEP holder, including a nonpracticing entity, does not violate competition laws by seeking an injunction against an unwilling licensee of a FRAND-encumbered patent, although insistence on bundling SEPs and non-SEPs would be anticompetitive. But in *Unwired Planet*, Justice Birss distinguished a deviation from the FRAND rate from a competition law violation: ''there is no reason why the [FRAND] undertaking should entitle either party subsequently to challenge agreed terms as being non-FRAND absent competition law considerations.'' He further notes that an abuse of dominance will not be found unless an offer ''is so far above FRAND rate as to act to disrupt or prejudice the negotiations themselves.'' Meanwhile, the Japan Fair Trade Commission (JFTC) published guidelines regarding the treatment of SEPs under the Antimonopoly Act. These guidelines include criteria for determining when an SEP owner may seek an injunction. Indeed, the JFTC framework appears to align closely with the European Court of Justice's positions in *Huawei v. ZTE*.

It is not clear whether any of these shifts will produce significant change in the licensing and litigation of SEPs. The shift in tone has not yet been followed by any action in the U.S. However, if regulatory agencies that are tasked with policing standards diverge in their approach to SEPs, that could lead to significant confusion and counterproductive angst among implementers and SEP owners who need clarity to assess risks and opportunities involved in investing in major projects that are affected by standards, such as the deployment of 5G.

Conclusion

Although recent decisions have harmonized aspects of the treatment of these patents across certain jurisdictions, differences remain on several important issues. In particular, questions remain regarding situations in which injunctive relief may be sought or awarded, the proper method for calculating royalties, and the role of competition law in these cases — all crucial issues that can change the balance of power during licensing negotiations. As standards take on increasingly important roles in digitized economies, the need to streamline SEP litigation and licensing becomes more urgent. To that end, it is crucial that the terms are fair and reasonable to both sides. And although SEP owners and implementers may have conflicting views on what qualifies as FRAND, they agree that this area is badly in need of clarity. Courts and agencies charged with SEP oversight should take steps to limit opportunities for tactical behavior that can undermine good-faith negotiations.

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