PREU BOHLIG & PARTNER

The ECJ's *Huawei v. ZTE* Decision and its Implementation in Practice

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Overview

I. Introduction

Standards, SEP and FRAND

- **A standard-essential patent** protects a technology,
  - which is the subject matter of a standard
  - which must be used to implement the standard.
- **Industry standard** (*de facto* standard)
  - Defined by companies.
  - Implemented because it is technically or economically superior.
- **Codified standard** (established or *de jure* standard)
  - Standard set by a standard-setting organization (SSO).
- **Declaration of willingness to license**
  - Exemption criterion under Art. 101(1), (3) TFEU.
  - Irrevocable.
  - **FRAND** terms (*Fair Reasonable And Non-Discriminatory*).

Prohibition on the Abuse of Market Power

Art. 102 (1) of the Treaty on the Functioning of the EU (TFEU)

*"**Abuse of a dominant position in the internal market** or a significant segment thereof by one or more companies is prohibited as incompatible with the internal market to the extent this can result in an impairment of trade between Member States."*

- Patent protection alone does not establish market dominance
  - ECJ GRUR Int. 1995, 490, 492 – *Magill.*
- **There is no market dominance** unless
  - an SEP must be used to implement the standard,
  - there is no alternative to the standard, and
  - products are unsaleable without the implementation of the standard.

The Defense of Compulsory License under Antitrust Law

- **Legal consequences of a violation of Art. 102 TFEU**
  - If there is a general refusal to grant licenses => legal obligation to grant licenses
  - After licensing becomes a practice =>
    - Prohibition on discrimination
    - Prohibition on unfair impediments, e.g.
      - Excessive license fees
      - Licensing of “unnecessary” intellectual property rights

} = License on FRAND terms

Specific Cases

Unlicensed patent, no willingness to grant a license, no FRAND declaration
=> ECJ GRUR 2004, 524 – ***IMS Health***

- There is a violation of Art. 102 TFEU if (cumulatively)
  - There is a dominant market position;
  - There are unusual circumstances:
    - The license is indispensable to the license seeker;
    - New product;
    - No factual basis for refusal;
    - Exclusion of any competition in the downstream market

Specific Cases

Out-licensed patent; *de jure* or *de facto* standard, no FRAND declaration.

=> German Federal Court of Justice [BGH], dec. of 6 May 2009, KZR 39/06 – ***Orange-Book-Standard***
= GRUR 2009, 694.

- **There is an abuse of market power** and a violation of § 242 of the German Civil Code [BGB] (*dolo petit defense*) **only** if the defendant makes a license offer that is
  - unconditional and
  - acceptable;
  - and complies with and fulfills the obligations under the license agreement (in advance).

Specific Cases

SEP with FRAND declaration

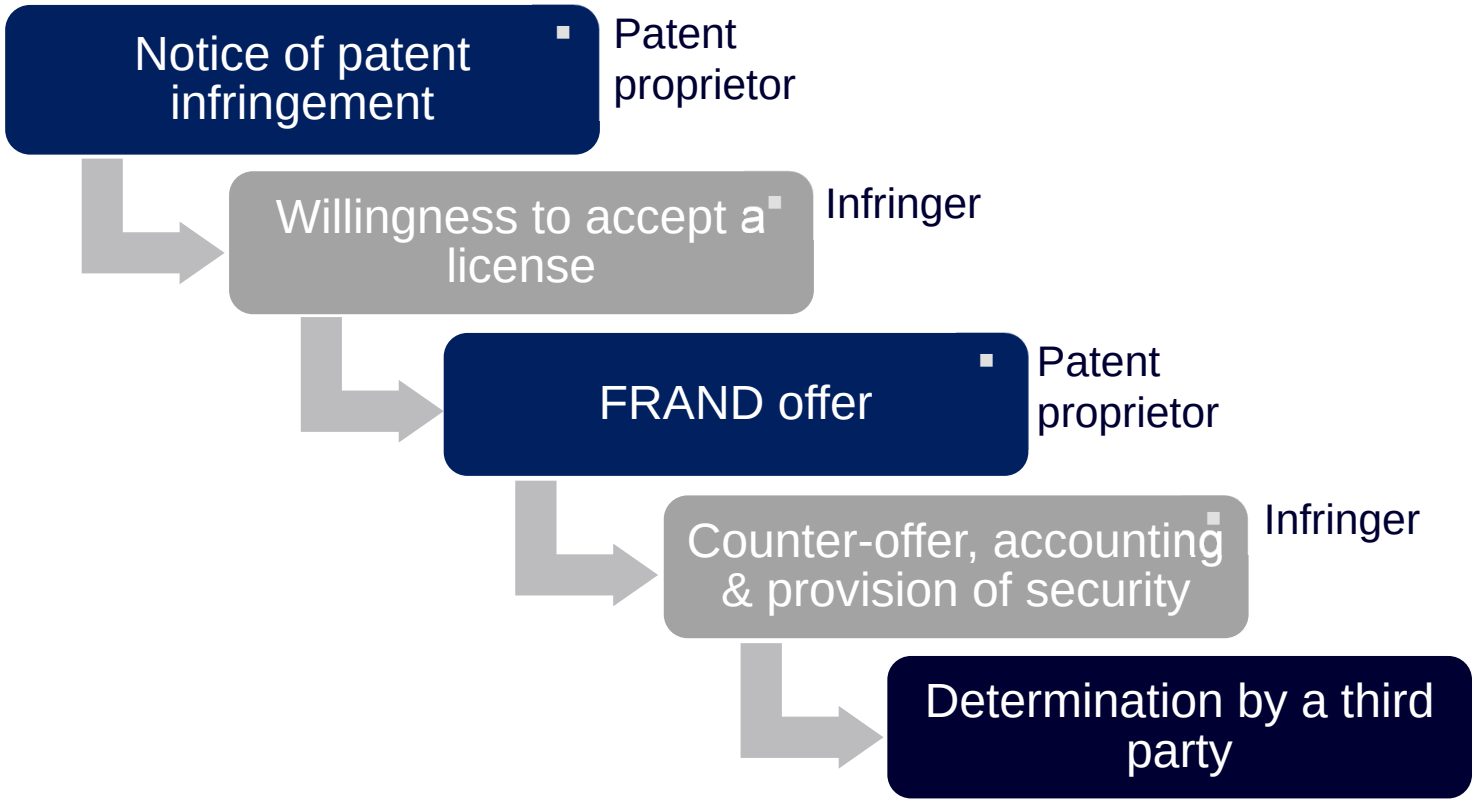
=> Commission in the ***Motorola,*** C(2014) 2892, and ***Samsung,*** C(2014) 2891 decisions of 29 April 2014.

- "**Safe Harbor**" for the infringer willing to accept a license:
  - If the SEP proprietor has made a **FRAND declaration**,
  - the infringer will be protected against prohibitive injunctions as long as he shows a **readiness to accept a license**.
  - Example of sufficient willingness to accept a license: Agreement to having the FRAND license **determined by a third party**

=> ECJ Mitt. 2015, 449 – ***Huawei v. ZTE***

II. The ECJ's *Huawei v. ZTE* Decision

The *Huawei* procedure <u>before filing an action</u>



Dominant Market Position and Abuse

- Does the SEP automatically establish a **dominant market position**?
  - Not answered in *Huawei v. ZTE* or *Orange-Book-Standard*.
  - In *Motorola v. Apple,* the Commission found:
    - Subject-matter of the industrial property right = relevant product market, since SEP = own technology market.
    - SEP proprietor holds a 100% share of the relevant market.
    - The standard is indispensable to the product market because there is no substitute.
  - Advocate Gen. Wathelet in re: *Huawei v. ZTE*, C-170/13, Marg. no. 58:
    - If every use of the standard necessarily realizes the teaching of an SEP => simple **presumption** of a dominant position (see also Regional Court (LG) of Düsseldorf, dec. of 24 April 2014 – 4b O 273/10).
    - But: **The presumption can be rebutted** (by the SEP proprietor).

Dominant Market Position and Abuse

- Regional Court of Düsseldorf, dec. of 26 Mar. 2015, regarding the NFC (Near Field Communication) standard :
  - Advocate General Wathelet's presumption does not apply to every standard-essential patent.
  - The dominant market importance in an individual case based on the content of the patent and the actual importance in the market must be examined.
  - Not every standard-essential patent (SEP) imparts significant market power. Many functions in a standard are of secondary importance to the market.
  - **The burden of presentation and proof is on the defendant**, who invokes the defense under antitrust law (disputed).

Dominant Market Position and Abuse

- Commission in re *Motorola*: The willingness to grant a license under FRAND terms encouraged market participants to use the standard and invest in its infrastructure (“*locked-in”).*
- Advocate General Wathelet agreed in his opinion of 20 Nov. 2014 in re: *Huawei v. ZTE,* C-170/13.
- ECJ – *Huawei v. ZTE*, Marginal no. 53 et seq.:
  - An undertaking to grant licenses on FRAND terms creates legitimate expectations on the part of third parties that the proprietor of the SEP will, in fact, grant licenses.
  - But: Under Art. 102 TFEU, a patent proprietor is only required to grant a license on FRAND terms.

Importance of the FRAND Declaration

- Art. 102 TFEU, and not the FRAND declaration itself, establishes the patent proprietor's obligation to offer a license.
  - But: The existence of a FRAND declaration can establish abuse of a dominant market position.

- **Problems:**
  - No FRAND declaration was made for the SEP (*Orange-Book-Standard* cases)?
  - A patent was granted to a third party who is not a member of the standardization organization.
  - The SEP was transferred to a third party who did not make a FRAND declaration.
    - German legal precedent: The FRAND declaration is merely contractual and does not inhere in the patent.
    - Contrary opinion of the Commission (in re: *Rambus*): "*The FRAND declaration travels with the patent.*"

The Infringer's Defenses

"[69] Finally, an alleged infringer cannot be criticized […] for challenging **the validity of the patents** and/or the **essentiality** of the patents to the standard […] **and/or their actual use,** in parallel to the negotiations relating to the grant of licenses, or for reserving the right to do so in the future*."*

(ECJ – *Huawei v. ZTE*, Marginal no. 69)

- Therefore, the defendant may
  - challenge the validity of the patent,
  - raise the defense that there has been no infringement and
  - dispute that the patent must be used in the application of the standard (standard-essentiality).

Rendering of Accounts and Damages

- **Actions for rendering of accounts and damages**
  - According to the ECJ, such actions have no direct effect on market entry by standard-conforming competing products.
  - Consequently, they **must not be abusive** within the meaning of Art. 102 TFEU.
- **But:**
  - Can a patent proprietor who does not fulfill his FRAND obligations demand full damages (according to the three types of calculations) or only license fees?
  - Is his claim to damages, and thus his accessory claim to information, limited to the FRAND license fee?
  - Yes, otherwise a patent proprietor who conformed to antitrust law would be placed in a worse position than one who violated antitrust law. The breach of duty results in a limitation on the patent proprietor’s claims.

III. Implementation in Practice

Notice of Patent Infringement

"[61] **Prior to initiating judicial proceedings on such claims**, **the proprietor** of the SEP in question must first **notify the alleged infringer of the infringement** […] **by identifying the SEP** and **specifying the way in which it has been infringed**…*"*

(ECJ – *Huawei v. ZTE*, Marginal no. 61)

- **When?**
  - Generally before filing the action
  - **Old cases** (i.e. upon the filing of an action before 16 July 2015): It was possible to make up for this lapse in the course of litigation (Regional Court of Düsseldorf, dec. of 03 Nov. 2015, Case No. 4a O 144/13).

Notice of Patent Infringement

- **New cases:** Can the patent proprietor make up for the lapse in the course of litigation?
  - As long as the *Huawei* procedure is not completed or prevented/delayed by the infringer => obstacle to implementation (*Kühnen/*Maimann, lecture of 20 Nov. 2015).
  - Defense of compulsory license under cartel law => estoppel defense under § 134 BGB. A claim for injunctive relief is not “ripe” as long as the assertion of the SEP constitutes abuse of a dominant market position.
  - Therefore: The patent proprietor can make up for the lapse until the close of the oral hearing.
  - Otherwise: The action will be dismissed as unfounded at the present time.

- In exceptional cases, **notice may be unnecessary** if it is certain that the defendant is aware that he is using the patent in suit.

Notice of Patent Infringement

- **What content?**
  - Identification of the patent in suit (publication number or the like)
  - Statement
    - of which act of infringment (offering, manufacturing, etc.)
    - infringes which challenged embodiment of the patent in suit.
  - No further substantiation (of the complaint) is necessary (contrary opinion, Advocate General *Wathelet*, in re: *Huawei v. ZTE,* C-170/13, Marginal no. 84).
    - No need to threaten legal action.
    - The usual request-to-show-authorization or warning suffices (Cordes/Gelhausen, Mitt. 2015, 426, 432); a complaint should be filed in any event (cf. Regional Court of Düsseldorf, dec. of 03 Nov. 2015, Case No. 4a O 144/14).
  - No need to mention all patents for which the patent proprietor regularly demands licenses => subject matter of the license terms.

The Infringer's Request for a License

- **How?**
  - Any (informal, even implied) request is sufficient -- even in the answer to the complaint!

- **What content?**
  - Willingness to license the patent in suit under FRAND terms.
  - Recommendation: No advance exclusion of certain terms
  - Make sure that the attorney has authorization to receive service of process!

- **When?**
  - **Soon after receiving the notice** of patent infringement (cf. ECJ – *Huawei v. ZTE*, Marginal no. 66 = general requirement to expedite the proceedings).
  - **Four weeks!** Three months can be too long (Regional Court of Mannheim, dec. of 27 Nov. 2015 – 2 O 106/14)

FRAND Licensing Offer

*"[63] Secondly, [...] it is for **the proprietor of the SEP to present to the alleged infringer a specific, written offer for a license on FRAND terms**, in accordance with the undertaking given to the standardization body, **specifying, in particular, the amount of the royalty** and the **way in which that royalty is to be calculated**."*

(ECJ - *Huawei v. ZTE*, Marginal no. 63)

- **To whom?**
  - Potential patent infringers.
  - Making an offer to an affiliate can be sufficient if
  - there is an interest in a license for the corporate group,
    - license agreements are generally centrally coordinated, and
    - one can assume that the group parent and the defendant subsidiary communicate (Regional Court of Düsseldorf, dec. of 03 Nov. 2015, Case No. 4a O 144/14, Marginal no. 193)

FRAND Licensing Offer

- **What content?**
  - License agreement with the usual provisions (=> reversed *Orange-Book-Standard* constellation).
    - The patent proprietor has the right to determine the price, § 315 BGB, mutatis mutandis
    - If available: the patent proprietor's standard license agreement.
    - Special right of termination in the event a nullity suit?
      - (-), according to the ECJ – *Huawei v. ZTE*, Marginal no. 69, an attack on the validity of the patent is permissible. In addition, under Art. 5 (1) lit. b TTR 2014: There is a special right of termination only for exclusive licenses.
  - License fee and manner of its calculation
    - License fee = reference value + royalty rate
    - Method of calculation, possibly staggered reduction.

What is FRAND?

- **Method of calculation**
  - What is the market rate?

- **Portfolio license** => main point at issue
  - No portfolio containing different technologies (Commission finds a antitrust law violation)
  - Only SEPs?
  - Only the patents being used?
  - Foreign countries?

The Infringer's Response

- If a FRAND licensing offer is made (and only then):
  - The infringer has a general **duty to respond**,
    - With due care
    - In good faith, and
    - Especially **without delaying tactics** (ECJ – *Huawei v. ZTE*, Marginal no. 65)

- If the patent proprietor's FRAND licensing offers is rejected:
  - Specific **counter-offer** (on FRAND terms)
  - Within a short period of time (ECJ – *Huawei v. ZTE*, Marginal no. 66)
    - "Short period of time" < 1 month (cf. Regional Court of Düsseldorf, dec. of 03 Nov. 2015, Case No. 4a O 144/14, Marginal no. 215).

The Infringer's Response

If the **SEP is already being used**:

*"[67] Furthermore, where the alleged infringer **is using the SEP** before a licensing agreement has been concluded, the alleged infringer must **provide appropriate security** […] **from the point on at which its counter-offer is rejected** […]. The calculation of that security must include, inter alia, the number of past acts of use of the SEP […]."*

- After the rejection of the (first) counter-offer by the patent proprietor
  - **Disclosure** of the number of past acts of use
  - **Provision of appropriate security** (ECJ – *Huawei v. ZTE*, Marginal no. 67).
    - Under the duty to expedite the proceedings, the accounting and the security must be provided quickly (cf. Regional Court of Düsseldorf, dec. of 03 Nov. 2015, 4a O 144/14, Marginal no. 208 et seq.)
  - No duty to provide security **until two FRAND offers** have been made (patent proprietor's offer + infringer's counter-offer) (disputed, contrary opinion Regional Court of Mannheim, dec. of 27 Nov. 15, 2 O 106/14)

The Infringer's Response

- **Amount of security to be provided?**
  - Appropriate license fee => patent proprietor's FRAND offer?

- **For what period of time?**
  - Only for the future, until the expected determination of the FRAND license by a third party?
    - Arg.: ECJ – *Huawei v. ZTE*, Marginal no. 67: "from the time the counter-offer is rejected."

  or

  - also for the past, until the expected determination of the FRAND license by a third party?
    - Arg.: ECJ – *Huawei v. ZTE*, Marginal no. 67: disclosure of "past" acts of use.

Determination by a third party

*"[68] In other respects, where **no agreement** has been reached on the details of the FRAND terms **following the counter-offer** by the alleged infringer, the parties **may**, by mutual agreement, request **that the amount of the license fee be determined by the decision of an independent third party,** issued without delay."*

- ***When?***
  - After the counter-offer, i.e. when two FRAND offers have been made.

- **Who?**
  - Arbitration tribunal or arbitrator.
  - State court if both parties waive the right of appeal (Kühnen/Maimann, lecture of 20 Nov. 2015).
  - Not the infringement court.
  - Any party who does not consent is not willing to conclude a license agreement (Kühnen/Maimann, lecture on 20 Nov. 2015).

Remedy of Errors/Loss of the FRAND Defense

*"[62] **Prior to initiating judicial proceedings** on such claims, the proprietor of the SEP in question must first notify the alleged infringer of the infringement.*

[64] […] if the proprietor of an SEP promises the standardization organization that he will grant licenses on FRAND terms, he is expected to make such an offer."

- Notification by filing the complaint?
- FRAND offer in the reply?
- Willingness to conclude a license agreement in the answer to the complaint?

- In practice, the plaintiff can cure many errors.
- The defendant can easily lose the FRAND defense by making an error (disclosure, security) (cf. Regional Court of Düsseldorf 4a O 144/14).

- **Caution: Liability!**

Circumventing the FRAND Defense

- NPEs sue dealers to reach manufacturers. The NPEs expect that dealers will not be willing to accept licenses and, therefore, the *Huwawei* procedure will fail.
- **But:** Higher Regional Court (OLG) of Karlsruhe, 6 U 44/15, dec. of 23 April 2015
  - **The willingness of the manufacturer to conclude a license agreement** is sufficient for the defense of compulsory license
  - The patent proprietor must make a FRAND offer to the manufacturer.
  - **License negotiations** between the manufacturer and the SEP proprietor **are** more **skewed** if the injunction is directed at the customer.
  - **Customers have less of an interest in a dispute** with the SEP proprietor. However, there is an existential threat to the manufacturer‘s relationship with its customers.
  - An SEP proprietor who enters into license agreements with other manufacturers, places himself **at odds with his own licensing practice**.

Thank you for your attention!

Contact

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