GCR USA NEWS

Out of Sync?: DOJ's Policy Reversal Towards SEPs Lacks Legal Support

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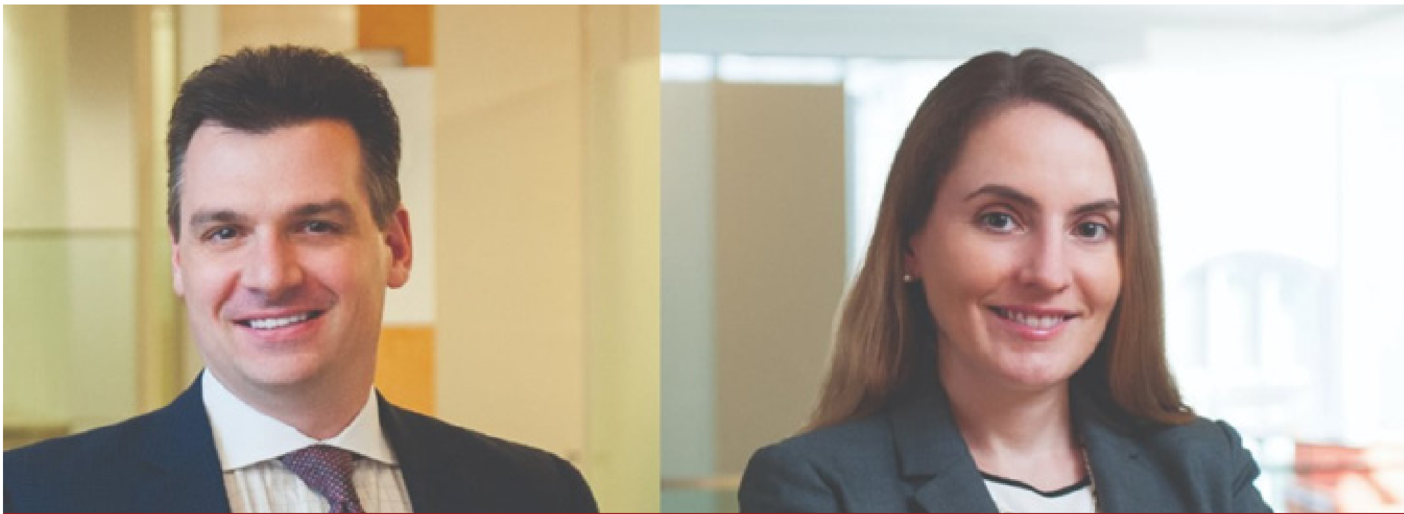

Jay Jurata and Emily Luken of Orrick

*In a series of recent statements, the US Department of Justice's antitrust division has expressed an apparent policy shift regarding the application of competition law to the assertion of standard-essential patents subject to a commitment to license on fair, reasonable, and non-discriminatory terms. Orrick Herrington & Sutcliffe partner **Jay Jurata** and associate **Emily Luken** say the seeming reversal is troubling because it is out of sync with a large and growing body of US case law.*

Prior to an apparent change in position in recent months, US antitrust authorities recognised that competition law plays an important role in preventing potential anti-competitive behaviour by owners of standard-essential patents. SEPs are patents that a standard-setting organisation has formally incorporated into a particular technological standard. Standardisation enables interoperability and connectivity among different technological devices; it also has the effect of eliminating potential competitors for alternative technologies.

To address the potential competition problems that arise with respect to standardisation, many standard-setting organisations require that the patent holder commit to license its SEPs on fair, reasonable and nondiscriminatory terms. Absent the FRAND commitment, there is a significant risk that the patent holder would unfairly wield its strong bargaining position vis-à-vis the licensee to extract royalties beyond the incremental value of the technology, a problem known as "hold-up."

Both the US Department of Justice's antitrust division and the Federal Trade Commission previously have said antitrust law can be applied to address hold-up and other potential anti-competitive behaviour by SEP-holders. For example, in 2013, the DOJ and US Patent & Trademark Office issued a policy statement acknowledging the harms to consumers that could result from seeking royalties at a level higher than FRAND and leveraging the threat of injunctions. Two years later, Antitrust Division head Bill Baer reaffirmed that position by declaring that "hold up concerns are real," and harms both the competitive process and innovation. And last year, the FTC sued Qualcomm for alleged anti-competitive SEP licensing practices, which the district court agreed sufficiently pled violations of the Sherman Act.

During the past six months, however, the DOJ has retreated from those prior positions. Instead, in a series of speeches, the Antitrust Division has espoused that patent hold-out – also known as reverse hold-up, whereby an implementer allegedly prolongs accepting a SEP licence until its royalty demands are met – is a bigger problem than hold-up. Similarly, it has stated that antitrust law should not be used to police the FRAND commitments of SEP-holders, which can be more properly addressed by contract and other common law remedies. Finally, the Antitrust Division has endorsed the view that holders of FRAND-encumbered SEPs should be able to seek injunctions as a legitimate means of enforcing their IP rights, and limiting these rights runs the risk of transforming FRAND into a "compulsory license".

Spirited debate on important industry developments, and the role of antitrust, is a time-honoured tradition and improves the development of competition policy. In furtherance of that debate, the DOJ's recent statements have received scrutiny from academics and former government officials as well as industry representatives who have expressed concern over the theoretical justifications and practical impact of the DOJ's position. Moreover, the recent DOJ statements are out of step with numerous, comprehensive and well-reasoned US court decisions that have carefully examined these issues.

Hold-up is, and remains, a problem

Multiple US appellate and district court decisions recognise that hold-up is a real risk. This includes decisions from the US Court of Appeals for the Third Circuit, the Ninth Circuit and the Federal Circuit, as well as the US District Courts for the Central District of California, the Northern District of California, the Northern District of Illinois and the Western District of Washington. Indeed, in the most recent case adjudicating a FRAND rate, *TCL v Ericsson*, the court explained its rationale for the methodology it employed for the precise purpose of mitigating against hold-up: it "provides the ceiling for a FRAND rate, because increasing the royalty rate after the standard has been adopted, without showing that the increase is due to additions to the standard, is the definition of hold-up."

Moreover, when courts have been forced to adjudicate an appropriate FRAND royalty or to rule on a jury's evaluation, in every case the adjudicated rate has been orders of magnitude smaller than the offer the SEP-holder made prior to judicial proceedings.

In *Microsoft v Motorola*, Motorola claimed that one of its SEP portfolios was worth up to $4.50 per unit. Ultimately, the court held that the portfolio was worth less than $0.04 per unit, a difference of over 100 times less than what was initially sought.

In *In re Innovatio*, a patent assertion entity demanded a royalty rate of more than $16 per unit for tablets. After trial, the court determined that an appropriate royalty should be less than $0.10 per unit and based on the component chip – a reduction of 160 times less than what was demanded.

In *Realtek v LSI*, LSI sought an ITC exclusion order against Realtek and demanded, according to Realtek, a royalty exceeding the selling price of Realtek's products. The appropriate FRAND rate was ultimately determined to be about 0.19% of the price of the chips implementing LSI's SEPs, a difference of 500 times less than what was sought.

In *TCL v Ericsson*, the rates that TCL would have been required to pay Ericsson for mobile phones, for some technologies, would have been 10 times higher than what the court ultimately found.

Some have suggested that hold-up is less of a problem than hold-out because some licensees may require a patent owner to prove infringement before entering into a licence. But the Federal Circuit, when addressing that very issue in *Apple v Motorola*, held that requiring a SEP owner to go to court to prove infringement does not make an alleged infringer an "unwilling licensee" justifying an injunction. As discussed further below, this is consistent with other US court decisions acknowledging that injunctions on FRAND-encumbered SEPs should be rare.

Not adhering to a FRAND commitment is a competition concern

In 2007, the Third Circuit recognised in *Broadcom v Qualcomm* that a SEP-holder's breach of a FRAND commitment can violate section 2 of the Sherman Act. In that case, the court held that the allegation – that Qualcomm induced an SSO into adopting a standard incorporating its SEPS based upon false FRAND promises, and later, after implementers were locked in, reneging on that promise by demanding non-FRAND royalties – was actionable anti-competitive conduct. One year later, a court in the Northern District of Texas similarly agreed that making a false FRAND promise could constitute unlawful monopolisation.

More recently, the District of Delaware followed Broadcom when confronted with similar allegations regarding conduct by Interdigital. The federal district court held that such apparent deception before an SSO, coupled with a FRAND breach, sufficiently stated a claim for monopolisation under section 2 of the Sherman Act.

And in the FTC's case against Qualcomm, **Judge Lucy Koh** in the Northern District of California held that the FTC had alleged claims under sections 1 and 2 of the Sherman Act sufficient to survive a motion to dismiss. Qualcomm, among other things, allegedly had a "no license, no chips" policy, which combined with its apparent refusal to license to its competitors, effectively foreclosed the possibility of any FRAND challenge. In denying the motion to dismiss, Judge Koh relied on Broadcom for the point that a voluntary FRAND commitment creates an exception to the general antitrust rule that there is no duty to deal with one's competitors.

Injunctions for SEPs should be rare

Finally, multiple US court rulings establish that seeking injunctions on FRAND-encumbered SEPs should be the limited exception, not the rule. In *Microsoft v Motorola*, the Ninth Circuit interpreted Motorola's FRAND commitment, under the specific language of the SSO, to "at least arguably, [provide] a guarantee that the patent-holder will not take steps to keep would-be users from using the patented material, such as seeking an injunction, but will instead proffer licenses consistent with the commitment made." And although the Federal Circuit made clear in *Apple v Motorola* that there is no *per se* ban against issuing injunctions on SEPs, it also indicated that injunctions should only occur under rare circumstances where monetary damages will not suffice as adequate compensation for infringement. Without evidence that monetary damages are insufficient, an SEP holder will otherwise have difficulty establishing the requisite irreparable harm for an injunction.

Recognising the potential anti-competitive effect of an injunction, some courts have taken steps to prevent SEP holders from enforcing injunctions obtained in other proceedings or jurisdictions. For example, in *Realtek v LSI*, the district court prohibited the SEP-holder from enforcing any exclusion order it might obtain in a related section 337 proceeding at the US International Trade Commission precisely because the "act of seeking an exclusion order or injunctive relief by the ITC is inconsistent with defendants' RAND obligations." The same concerns led to the anti-suit injunctions issued in *Microsoft v Motorola, TCL v Ericsson* and *Huawei v Samsung*. Similarly, when Samsung obtained an exclusion order from the ITC based upon a finding of infringement on a SEP, the US Trade Representative vetoed the exclusion order.

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The immediate impact of this disparity between recent DOJ policy statements and US legal precedent remains uncertain. It is possible DOJ could initiate legal proceedings against one or more implementers due, in part, to a belief that hold-out presents a greater risk to competition than hold-up. However, in that event, DOJ will have sparse legal support for its position.

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