EU High Court Sets Important SEP Precedent
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In a landmark judgment rendered July 16, 2015, the European Court of Justice has clarified when a holder of a standard-essential patent who has committed to the standard-setting organization to grant licenses to all implementers of the standard on fair, reasonable and nondiscriminatory terms is prohibited from seeking a court injunction against an alleged infringer of the SEP under the general EU law prohibition of abuses of a dominant position (Article 102 TFEU).

In essence, the court holds in Huawei Technologies Co. Ltd. v ZTE Corp., ZTE Deutschland GmbH[1] that an SEP holder who agreed to FRAND licensing cannot seek a court injunction without first taking specific steps with a view of reaching a license agreement with the alleged infringer, while also obliging the alleged infringer to negotiate in good faith. The court also clarified that the SEP holder cannot refuse to grant a license on the ground that the alleged infringer challenges the validity of the SEP, or the patent's essentiality for the standard, or whether its use of the SEP constitutes an infringement.

The judgment largely follows the advisory opinion of Advocate General Melchior Wathelet and is broadly in line with the substantive approach that the European Commission applied in its Motorola[2] and Samsung[3] decisions last year concerning cases raising similar issues. That also means that the approach set out by Germany's highest civil court, the Bundesgerichtshof, in the 2009 Orange Book[4] judgment, which allows greater scope for the SEP holder to seek an injunction, can no longer be applied in FRAND cases. However, the judgment makes clear that Article 102 TFEU becomes relevant only when the SEP holder seeks an injunction or a recall of the infringing products. Article 102 TFEU does not prevent the SEP holder from bringing actions for damages or for rendering of accounts.

The judgment addresses a hotly debated legal question of great commercial relevance, and it provided a significant amount of guidance, for the first time, from the EU's highest court on the issue. However, the judgment addresses only some of the legal questions that SEP holders and alleged infringers face in these situations, and even the questions addressed are in part expressed in very broad terms inviting different interpretations. Legal disputes will continue to arise in this field.

Background

The case resulted from a request for a preliminary ruling from the Regional Court in Dusseldorf made in the context of a patent enforcement action brought before it by Huawei. Huawei alleges that products commercialized by ZTE infringe an SEP held by Huawei regarding the Long Term Evolution (LTE) telecommunications standard adopted by the European Telecommunications Standards Institute (ETSI). As is required by the ETSI rules as a pre-condition for being included in the LTE standard, Huawei had committed to ETSI to grant licenses to the patent in question on FRAND terms to users of the standard. After negotiations between Huawei and ZTE regarding the granting of a license had broken down, Huawei filed a claim in the Dusseldorf court, seeking an injunction prohibiting the infringement, the rendering of accounts, the recall of products and an award of damages.

In defense, ZTE argued that Huawei's action was an abuse of dominant position in breach of Article 102 TFEU, given that ZTE was willing to negotiate a license on FRAND terms. The Dusseldorf court asked the court to clarify the conditions under which Article 102 TFEU prevents the holder of an SEP from seeking injunctions and other court remedies against alleged infringers of the SEP. In particular, the Dusseldorf court considered that...
the guidance provided by the highest German civil court in the 2009 Orange Book judgment, which placed significant obligations on an infringer seeking to avoid an injunction, could not be reconciled with statements made by the European Commission in interim press releases in the Samsung and Motorola cases, which suggested that a SEP holder no longer has the right to obtain an injunction under Article 102 TFEU once the alleged infringer shows itself to be a “willing licensee.”[5]

The Court’s Ruling

The judgment focuses on actions for injunctions and actions seeking recalls of infringing products, and finds both raise the same issues.[6] By contrast, the judgment finds that an SEP holder’s actions for damages or rendering of accounts do not raise abuse of dominance concerns.

The court emphasizes that injunctions prevent standard-compliant products manufactured by alleged infringers from appearing or remaining on the market, thus giving the SEP holder the possibility to reserve to itself the manufacture of the products in question.[7] While this is the normal consequence of the exclusionary rights granted under patent laws, the court considers it important that, by giving a FRAND licensing commitment to the standard-setting organization, the SEP holder has created a "legitimate expectation" for third parties that the SEP holder will generally seek to monetize its invention by granting licenses rather than by enforcing its right to exclude others from making use of the invention. The court explains that the application of Article 102 TFEU must create a "fair balance" between these legitimate expectations and the rights of the SEP holder conferred by the patent laws.[8]

The court explains that seeking injunctive relief in cases where the dominant SEP holder has committed to license on FRAND terms will be considered abusive if the SEP holder fails to first make a reasonable approach to the alleged infringer in order to try to reach a license agreement. An abuse also occurs if the SEP holder seeks an injunction after having made such an approach if the alleged infringer has responded in good faith. More specifically:

- **Requirements regarding the initial approach to be made by the SEP holder:** The court held that seeking an injunction will be abusive unless the SEP holder first (1) alerts the alleged infringer of the infringement by designating the patent and specifying the way in which it has been infringed, and (2) after the alleged infringer has expressed its willingness to conclude a licensing agreement on FRAND terms, presents to the alleged infringer a specific, written offer for a license on FRAND terms, specifying, in particular, the royalty and the way in which it is to be calculated.[9]

- **Requirements regarding the response of the alleged infringer:** The alleged infringer does not need to accept the license offer to avoid an injunction, but must "diligently" respond "in accordance with recognised commercial practices in the field and in good faith,"[10] which must be established on the basis of objective factors.

The court then articulates some of the relevant factors:

- The alleged infringer must not apply "delaying tactics."[11]

- If the alleged infringer disagrees with the offer made by the SEP holder, the alleged infringer must "promptly" make a specific written counter-offer based on FRAND terms.[12]

- If the SEP holder rejects the counter-offer and the alleged infringer is using the SEP, the alleged infringer must "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."[13]

- It is open to the SEP holder and the alleged infringer at that stage to agree to request that the amount of the royalty be determined by an independent third party without delay.[14] Although the court finds this to be a relevant factor, the court did not explicitly indicate that an injunction would be prohibited if the alleged infringer made such an offer, in contrast to the position taken by the advocate general.[15]

- The court also held that the alleged infringer "cannot be criticised" either for challenging the validity, essentiality or infringement of the SEP in parallel to the licensing negotiations or reserving its right to do so subsequently.[16] Therefore, such conduct by the alleged infringer cannot justify an injunction.

**Issues Not Addressed by the Judgment**

While the judgment addresses several important points, it does not address some other issues that are relevant in disputes between a SEP holder and an alleged infringer.

The judgment does not discuss the circumstances that must be present to support the conclusion that a SEP holder holds a dominant position. The question of dominance was outside the court’s reach in this case because in its request for the preliminary ruling, the Dusseldorf court did not ask any questions on the issue of dominance and simply stated that Huawei held a dominant position. However, both Advocate General Wathelet in his advisory opinion and the European Commission in its Motorola decision discussed arguments that have been brought forward by SEP holders in the past in an attempt to reject a finding of dominance.

Moreover, the Motorola decision discusses at length the effects that the seeking of an injunction by Motorola had on competition. In Huawei v ZTE, the court remained completely silent on the question of effects. Whether this means that the competitive effects brought about by seeking an injunction will in the future be irrelevant remains to be seen.

Finally, the judgment does not provide any guidance as to the legal standards that define whether the terms of a license offer constitute FRAND terms. This issue leads to frequent disputes between SEP holders and implementers of a standard, including, for example, the appropriate royalty percentages and the proper basis for calculating royalties.[17] The conclusions of the European Commission's consultation on patents and standards, which closed on Feb. 15, 2015,[18] as well as the efforts of standard setting organizations and national courts to formalize minimum requirements for FRAND terms, may shed further light on this issue.

**Comments**

The court seeks to hold the SEP holder to its FRAND commitment by requiring it to take certain steps to attempt to reach a license agreement with the alleged infringer before being allowed to seek an injunction. The court bases this position on what it describes as the legitimate expectations of third parties that the SEP holder created by making the FRAND commitment.

Interestingly, the court distinguishes its prior Volvo, Magill and IMS judgments[19] holding that abuses of dominance can only occur under "exceptional circumstances" when a dominant undertaking exercises exclusive rights linked to intellectual property rights.[20] The court emphasizes that the present case is different in that Huawei's patent was included in a standard set by a standard-setting body and that Huawei committed to FRAND licensing.[21] This leads the court to rely on the argument of legitimate expectations.[22] Also interestingly, the judgment does not mention the earlier ITT Promedia and Protege International "right of access to the courts" judgments of the General Court that defined very narrow circumstances under which a
company can be found to abuse a dominant position by seeking to enforce legal rights in court.

On the other hand, the court makes clear that an injunction must be possible if the alleged infringer reacts unreasonably to the offer made by the SEP holder and therefore shows itself to be unwilling to negotiate in good faith. The judgment avoids the term of a "willing licensee" that has been used by the European Commission in this context, but in substance the court shares the European Commission's general approach. By defining steps that the alleged infringer must comply with, the court shows that it seeks to address the reverse holdup problem that might arise if infringers were able to prevent injunctions by merely pretending to be negotiating.

On this point, however, the judgment provides some general guidance but little detail. It requires the alleged infringer to respond to the offer "diligently," "in accordance with recognised commercial practices in the field" and "in good faith." Moreover, the alleged infringer must not employ "delaying tactics." The judgment does not further describe or define any of these terms. It can be expected that disputes will in the future arise about these requirements before competition authorities and courts. The same can be expected to be true regarding the obligation on the alleged infringer to submit a counter-offer "promptly." Moreover, the court does not address the questions of whether or not the SEP holder can demand cross-licensing or portfolio licensing.[23]

In broad terms, the balancing act required by the judgment is broadly in line with the European Commission's infringement decision in Motorola, which found that Motorola infringed Article 102 TFEU by seeking court injunctions, and its commitment decision in Samsung, in which the European Commission rendered binding commitments offered by Samsung setting out a "licensing framework" that, if adhered to by the alleged infringer, shields it from actions for injunctions brought by Samsung (so-called "safe harbor"). It is not clear, however, if the court's approach is entirely congruent with the European Commission's approach in these cases. Notably, the European Commission placed significant emphasis on the notion that it is reasonable for the alleged infringer to offer that the royalty rates be set by a court or arbitration tribunal. The court judgment does not place such significant emphasis on this issue. However, it emphasizes the need for the alleged infringer to provide appropriate security in the form of bank guarantees or otherwise if the SEP holder rejects the counter-offer made by the alleged infringer.[24] This issue does not appear to have played a significant role in Motorola and Samsung.

The judgment also means that the approach set out by the German Bundesgerichtshof, the highest German civil court, in its 2009 Orange Book judgment does not apply with regard to SEP holders that have given FRAND commitments. Although the Orange Book case concerned a de facto standard (as opposed to a standard set by a standardization body), it was later applied by lower courts in Germany also with regard to the present type of situations. The German court practice is of particular relevance in this context because so many patent holders bring enforcement actions in Germany, where the bifurcated court system means a finding of infringement (and consequential injunction) can be handed down months or years before validity is considered.

**Outlook**

The court's judgment in Huawei v ZTE provides important guidance, but still leaves many questions open, and further questions are certain to arise as national courts seek to apply these guidelines in specific cases. Just as in other parts of the world, SEPs will continue to lead to significant questions under the abuse of dominance rules in Europe.

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[5] It is important to note, however, that the European Commission's actual decisions in Samsung and Motorola provided much more detailed guidance than the interim press releases.
[6] For simplicity, we mention only injunctions in the remainder of this advisory.
[16] Paragraph 69.
[17] This latter point has been the subject of recent policy discussions (e.g., the recent change of the policy of the IEEE, which now says that royalties should be calculated on the basis of the value of the smallest saleable unit, rather than the value of the final complete product, available here) as well as recent cases in the US (see for example cases 337-TA-613 and 337-TA-868 heard before Administrative Law Judge Essex).
[19] The Court does not reference here its Bronner judgment nor the Microsoft judgment rendered by the lower General Court.
[22] By contrast, the European Commission's Motorola decision argued that the inclusion in the standard and the FRAND commitment created exceptional circumstances in the meaning of the prior case law (see paragraphs 278 and following of that decision).
[24] In its advisory opinion, Advocate General Wathelet linked the two aspects: if the alleged infringer proposes that the terms of the licence (notably the royalty calculation) be fixed by a court or an arbitration tribunal and offers sufficient security of payment, then the SEP holder should be prevented from seeking an injunction. The Court did not follow this approach, creating room for discussion as to what role the offer to have the licensing terms fixed by a court or arbitration tribunal plays in assessing the reasonableness of the alleged infringer's response.