

European Court of Justice's Judgment in Case C-170/13 *Huawei v ZTE*

July 21, 2015

Competition

On July 16, 2015, the Court of Justice of the European Union ("CJEU" or "the Court") issued its long-awaited [judgment](#) in *Huawei Technology Co. Ltd v ZTE Corp., ZTE Deutschland GmbH*. The CJEU found that the holder of a standard essential patent ("SEP") may, in certain circumstances, abuse its dominant position in seeking to enjoin the implementation of technology reading on its SEPs by an alleged infringer.

On April 5, 2013, the Landgericht Düsseldorf referred five questions to the CJEU in connection with Huawei's action against ZTE in Germany for allegedly infringing one of its Long-Term Evolution SEPs. As a result, the CJEU has, for the first time, considered whether, and in what circumstances, the holder of a SEP (who has committed to grant licences on fair, reasonable and non-discriminatory ("FRAND") terms) may abuse a dominant position under Article 102 of the Treaty on the Functioning of the European Union ("TFEU") in seeking to enjoin the implementation of technology reading on its SEP.

SEP holders may abuse their dominant position when seeking injunctions against the unlicensed use of their SEP

As a preliminary note, the CJEU points out that, in assessing the lawfulness of an action for infringement of a SEP, it must "*strike a balance between maintaining free competition [...] and the requirement to safeguard that proprietor's intellectual property rights and its rights to effective judicial protection*". While enforcing intellectual property rights ("IPR") generally does not amount to an abuse of dominance by a patent holder, the Court noted that this may be the case in exceptional circumstances.

The existence of exceptional circumstances

The Court distinguishes the present situation from previous cases relating to the balancing of these interests on the basis that (i) the patent concerned is a SEP; and (ii) the patent is a SEP because Huawei gave an irrevocable undertaking to a standardisation body to grant licences on FRAND terms. This undertaking "*creates legitimate expectations on the part of third parties that the proprietor of the SEP will in fact grant licences on such terms*". In those circumstances, the refusal by the SEP holder to grant a licence on FRAND terms "*may, in principle, constitute an abuse*".

Conditions under which a SEP holder does not abuse its dominant position

The Court clarifies the conditions under which an action by a dominant SEP holder against an alleged infringer to enjoin the implementation of a technology (including through an import ban or for the recall of products that implement that technology) will not be regarded as abusive.

- **Prior to bringing an action, the SEP holder must give notice or consult with the alleged infringer, i.e., the SEP holder must "alert the alleged infringer of the**

infringement complained about by designating that SEP and specifying the way in which it has been infringed." This requirement stems from the observation that, because of the large number of SEPs composing a standard, the alleged infringer may not be aware of the possibility of infringement.

- **Once the alleged infringer has expressed its willingness to conclude a licensing agreement on FRAND terms, the SEP holder must present a written offer for a licence on FRAND terms, specifying the amount of the royalty and the calculation methodology.** The Court took the view that, because of the undertaking given to the standardisation body, there is an expectation that the SEP holder would make such an offer. This approach can be contrasted with that of the Advocate General, who did not require that the alleged infringer first express its willingness to conclude an agreement on FRAND terms. He simply recommended that the proprietor of a SEP "*must, in any event, present to the alleged infringer a written offer for a licence on FRAND terms*".
- **The alleged infringer should then "diligently respond to that offer".** The Court specifies that this should be done "*in accordance with recognised 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.*" While this may raise questions as to what constitutes a diligent response, the Court can be read as setting out a standard of conduct for alleged infringers that balances their interests against those of SEP holders:
 - If the alleged infringer decides to reject the SEP holder's offer, to be considered to have responded diligently, **the infringer must submit to the SEP holder "promptly and in writing, a specific counter-offer that corresponds to FRAND terms"**. Otherwise, the alleged infringer will not be allowed to claim that the SEP holder's action is abusive.
 - **If the alleged infringer uses the teachings of the SEP before an agreement is concluded, the alleged infringer must provide commercially appropriate security "from the point at which its counter-offer is rejected"** (such as a bank guarantee or funds in escrow). "*The calculation of that security must include, inter alia, the number of past acts of use of the SEP.*"
- If no agreement is reached, the parties **may request that the amount of the royalty be determined without delay by an independent third party.**

Merely initiating legal proceedings and seeking damages for infringement do not constitute an abuse of dominant position. These considerations only apply to actions that aim to prevent products from entering or remaining on the market (actions brought to prevent products being placed on the market or to recall products). They do not apply to actions by a SEP holder with a view to obtaining the rendering of accounts or an award of damages in relation to past acts of use of that SEP, since such actions do not directly impact on products appearing or remaining on the market.

The alleged infringer can contest the validity of the patent. An alleged infringer "*cannot be criticised either for challenging, in parallel to the negotiations relating to the grant of licences, the validity of those patents and/or the essential nature of those patents to the standard [...] or for reserving the right to do so in the future.*" The latter point echoes the views expressed by the Advocate General when he suggested that the alleged infringer should be entitled to reserve the right, after entering into a licence agreement, to challenge the infringement, essentiality and validity of the SEP before a court or arbitration tribunal. He characterised the right to appeal validity as a matter of public interest.

The Court's approach significantly differs from the approach taken by the German Courts under the so-called *Orange Book Standard*. The German Federal Court of Justice considered that seeking an injunction may only be abusive if the alleged infringer has made an unconditional and binding licence offer. The CJEU places the burden on the SEP holder (i) to alert the alleged infringer of the infringement and (ii) then to make an initial fair offer. However, as explained above, the CJEU also requires the alleged infringer to satisfy some strict conditions. For example, the alleged infringer's willingness to negotiate cannot merely be presumed on the basis of its oral statement that "*in a general way [...] it is prepared to enter into negotiations*" to avoid being enjoined (as some have interpreted the Commission's approach in the *Samsung* commitments). The Court made it clear that the alleged infringer must respond "*diligently*", "*in good faith*", and "*that there [be] no delaying tactics*". However, the determination of what indicates "willingness" has been left to national courts.

However, some uncertainties remain. First, **the Court does not address the question of whether ownership of a SEP necessarily confers dominance.** It merely indicates that "*the existence of a dominant position has not been contested before [the referring court] by the parties to the dispute in the main proceedings*" and that "*[g]iven that the questions posed by the referring court relate only to the existence of an abuse, the analysis must be confined to the latter criterion.*" While he did not provide a clear answer, the Advocate General noted that the fact that a company holds an SEP does not necessarily mean that it holds a dominant position – this is a matter to be decided on a "case by case" basis.

Second, **while this judgment provides legal clarity on certain competition obligations relating to SEPs, its scope is limited to a particular set of facts, i.e., the patent concerned is a SEP.** Therefore, the situation remains unclear with regard to *de facto* standards and non-standard essential patents, whether or not the patent holder has undertaken unilaterally to license on FRAND terms, for example.

In sum, the judgment makes it clear that a SEP holder bears much of the burden in seeking to reach terms with an unlicensed implementer. Many have observed that the SEP holder is better placed to assess the value of its patents, and the Court's requirement that the SEP holder make the first offer could be construed as displaying some sympathy for that view in circumstances where the alleged infringer has indicated a willingness to negotiate to enter into an agreement on FRAND terms.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Antitrust practice group:

Miranda Cole	+32 2 549 52 64	mcole@cov.com
Peter Camesasca	+32 2 549 52 38	pcamesasca@cov.com

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