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FTC Secures Partial Victory Requiring SEP Holder to License to All Comers in Antitrust Case

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Summary

Recently, a federal district court in California granted partial summary judgment for the US Federal Trade Commission (FTC) in an important intellectual property and antitrust case involving standard essential patents (SEP). The court's decision requires an SEP holder to license its SEPs for cellular communication standards to all applicants willing to pay a fair, reasonable and non-discriminatory (FRAND) rate, regardless of whether the applicant supplies components or end-devices. The decision represents a significant victory for the FTC in enforcing its views of an SEP holder's commitments to license patents on FRAND terms.

IN DEPTH

On November 6, a federal district court in California granted partial summary judgment for the US Federal Trade Commission (FTC) and ordered Qualcomm, Incorporated to license its intellectual property for cellular communication standards to all willing applicants. *FTC v. Qualcomm, Inc.*, No. 17-cv-00220, 2018 US Dist. LEXIS 190051 (N.D. Cal. Nov.6, 2018). The decision requires Qualcomm to license its alleged standard essential patents (SEP) to all comers, regardless of whether they make component products or end-devices, and represents a significant victory for the FTC in enforcing its view of an SEP holder's commitments to license patents on fair, reasonable and non-discriminatory (FRAND) terms.

The FTC sued Qualcomm in January 2017 alleging that the company violated Section 5 of the FTC Act by refusing to license its alleged SEPs to other modem chip suppliers in violation of industry agreements, thus ensuring customers had to rely on Qualcomm for their modem chip supply. According to the FTC, Qualcomm then used its position as a "dominant supplier" of modem chips to require customers to license Qualcomm's alleged SEPs for "elevated royalties." In June 2017, Judge Lucy Koh of the US District Court for the Northern District of California denied Qualcomm's motion to dismiss. The FTC filed a motion for partial summary judgment in August 2018 on a discrete legal question: whether two agreements with industry standard-setting organizations (SSOs) required Qualcomm to license its alleged SEPs to all comers on FRAND terms.

The FTC brought this action, in part, under Section 5 of the FTC Act, which prohibits “unfair methods of competition in or affecting commerce.” 15 USC § 45(a)(1). The “elusive” standards of Section 5 declare as unlawful those acts and practices that “contravene the spirit of the antitrust laws” in addition to those that may violate the Sherman or Clayton Acts. *See* FTC, *Statement of Enforcement Principles Regarding “Unfair Methods of Competition” Under Section 5 of the FTC Act* (Aug. 13, 2015); *see also FTC v. Brown Shoe, Inc.*, 384 US 316, 321 (1966) (“This broad power of the Commission is particularly well established with regard to trade practices which conflict with the basic policies of the Sherman and Clayton Acts even though such practices may not actually violate these laws.”).

Notably, Section 5 does not enumerate specific acts or practices that may be deemed as unfair methods of competition. Those standards have instead developed over time through the FTC’s administrative practice. Although the FTC’s use of Section 5 as a standalone mechanism of enforcement has fluctuated over time, more recently the FTC has trended toward expanding the standalone reach of Section 5. While the FTC’s motion for partial summary judgment against Qualcomm did not seek to determine that Qualcomm violated Section 5, the case provides an example of licensing behavior that may raise concerns about dampening competition and trigger the FTC to bring a standalone enforcement action under Section 5.

Qualcomm holds several patents that facilitate cellular connectivity through networks that implement cellular communication standards and that are alleged as SEPs. Industry SSOs develop and manage these standards. SSOs in a variety of industries, including the telecommunications industry, often incorporate patented technology into the standards they adopt. To avoid conferring market power on the patent holder, SSOs have intellectual property rights (IPR) policies that require members to make assurances that any SEPs will be licensed to all applicants on FRAND terms.

In the instant case, Qualcomm is a member of two telecommunications SSOs—the Alliance for Telecommunications Industry Standards (ATIS) and the Telecommunications Industry Association (TIA) —both of which maintained IPR policies stating that the organization would adopt a standard that required the use of an essential patent only if the patent holder committed to license the patent on FRAND terms. The parties did not dispute that Qualcomm made several such commitments to both SSOs and that those commitments constituted binding contracts. Rather, Qualcomm asserted that the SSO IPR policies only required it to license its SEPs to suppliers of end-devices like cellular handsets—not those who manufactured a component such as a modem chip.

In deciding the issue, the court considered not only Qualcomm’s statements to the SSOs, but also the language in the SSO IPR policies. Here, however, the written assurances of the patent holder mirrored the language in the policies. The court rejected Qualcomm’s contention that the policies contained limitations that did not require it to license its alleged SEPs to component manufacturers. Instead, the court found that the plain text of the policies required patent holders to license SEPs to “all applicants” or “any applicant" who commit(s) to paying a FRAND rate. The policies did not contain any clear limitations as to which entities could receive a license. *See Microsoft Corp. v. Motorola, Inc.*, 696 F.3d 872, 884 (9th Cir. 2012) (emphasizing the policy "admits of no limitations as to who or how many applicants could receive a license"). Nor did the TIA or ATIS policies specify that only applicants who "practice" or "implement" *whole* standards could receive licenses. In fact, the policies contemplated that an applicant could receive a license to practice "any portion" of a standard (TIA IPR at 8), "or for the purpose of implementing a standard" (ATIS IPR at 10). Qualcomm was unable to put forth any other precedent limiting the scope of an SEP holder's FRAND commitments.

The court also reasoned that companion guidelines that explain the intent behind an SSO's policies are relevant to demonstrating whether the policy's language is susceptible to a particular meaning. The TIA's guidelines explained an SEP holder's FRAND commitments prevent an SEP holder from "securing a monopoly in *any* market" as a result of including patented technology in a standard. Thus, the court concluded that if a patent holder could discriminate against component suppliers like modem chip makers, it could achieve a monopoly in the component market and limit competing implementations of those components in direct contravention of the SSO's policies and stated purpose to "enable competing implementations that benefit manufactures and ultimately consumers." TIA IPR at 6. Moreover, the court found that Qualcomm had licensed its alleged SEPs to another component supplier and Qualcomm itself had received licenses to supply components. Therefore, the court found that as a matter of law, the SSO IPR policies required Qualcomm to license its alleged SEPs to component modem chip suppliers.

The decision is notable because it could affect how SEP holders license their patents. Going forward, SEP holders must review any FRAND commitment and ensure they are adhering to their agreed willingness to license their SEPs to any potential implementer. Judge Koh's ruling may also impact royalty structures by restructuring licensing negotiations from the end-device level to the components level, resulting in a proliferation of licenses from the SEP holder throughout the supply chain. Both end-device product manufacturers *and* component manufacturers will have to ensure they have sufficient license coverage to ensure they may produce products (end-devices or components) without infringing any SEPs. Finally, the decision underscores the importance of ordinary course documents in government investigations and litigation. The FTC and the court repeatedly relied on Qualcomm's own documents and statements to emphasize the importance of modem chip components to cellphones and industry standards. Government enforcers often use ordinary course documents to reinforce allegations and companies should be mindful of how ordinary course documents regarding SEPs, licensing strategies and industry SSOs could bear on the outcome a government investigation or complaint.

The case now proceeds to trial in early 2019. The scope of the trial will be to determine whether Qualcomm's conduct regarding licensing of its alleged SEPs, as well as whether certain exclusive dealing arrangements harmed competition in violation of Section 5.