



Huawei v ZTE – No More Need To Look At The Orange Book In SEP Disputes

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Industry standards are crucial for economic development – they reduce transaction and production costs; they increase efficiency; they ensure network interoperability. A number of industries, such as telecoms, IT and automotive heavily rely on standards. Once a standard has been adopted, standard-setting organisations usually require owners of patents found to be essential to the standard (Standard Essential Patents, or SEPs) to commit to charging a fair, reasonable, and non-discriminatory (FRAND) royalty to the users of the selected technology.

Given that standards covering equipment such as smartphones, games consoles, computers, DVD players and the like are implemented on a global basis, patents essential to those standards are a global issue and create global challenges (given the similarity in the products using them around the world). A number of patent disputes have developed between SEP holders and tech companies using the standardised technology. One major debate focuses on the conditions under which SEP holders can seek injunctions based on infringement of the patents for which a FRAND commitment has been given.

This article analyses the long-awaited judgment of the Court of Justice of the European Union (ECJ) in *Huawei v ZTE* which was handed down on 16 July 2015.² The judgment provides a structured framework for when EU competition law permits SEP holders who have given a FRAND commitment to seek an injunction.

The background: the contrast between the German Orange Book test and the EU Commission in *Samsung/ Motorola*

The *Huawei v ZTE* case was referred to the ECJ by the Düsseldorf District Court, which was hearing a patent dispute between two Chinese companies: Huawei Technologies (Huawei) and ZTE Corp (ZTE). Huawei was the holder of a patent, which it had declared to be essential to practise the Long Term Evolution (LTE) standard published by the European Telecommunications Standards Institute (ETSI). As part of the standard setting process, Huawei had agreed to license that patent on FRAND terms to parties seeking to implement the standard. ZTE was one such party. Huawei and ZTE had negotiations on the licensing terms and royalty rate, but did not reach agreement. Huawei then sought an injunction in Germany against ZTE for using its patent without a licence. ZTE raised a competition law defence, arguing that seeking an injunction was an abuse of Huawei's dominant position in the market for the licensing of the technologies as specified in the LTE standard technical specifications and was contrary to Article 102 TFEU.

The Düsseldorf court asked for guidance from the ECJ as to whether, when assessing whether Huawei's behavior was abusive, it should follow the well-established German practice (*Orange Book*) or the approach more recently advanced by the European Commission in its *Samsung* and *Motorola* decisions.³

The *Orange Book* judgment by the German Federal Court of Justice (Bundesgerichtshof)⁴ handed down in 6 May 2009 provides that a competition law defence may be relied on by the alleged patent infringer to prevent the grant of an injunction only in exceptional cases. In that case it was found that a claimant seeking an injunction on *de facto* essential patents (where no FRAND commitment had been given) only abuses its dominant position by seeking an injunction if the alleged infringer:

a) unconditionally offers to enter into a licence agreement with the SEP holder at a rate that is so high that the plaintiff cannot reasonably refuse or at a rate to be determined by the plaintiff but being subject to court review and adjustment; and

b) behaves as if it were an actual licensee, i.e. renders account of its acts for use of the patent and pays royalties (albeit in an escrow account for as long as the patent holder does not accept the licence agreement offer).

It is up to the defendant to prove that the two conditions are fulfilled. The “unconditional nature of the offer” means, in particular, that the offer should not be conditional on a court holding that the alleged infringer’s behaviour did in fact infringe the patent. In practice, this makes the competition law defence very unattractive, in particular because a number of lower German courts basically required the defendant to waive all defences with regard to non-infringement and invalidity of the patent.

The other alternative was the approach taken by the European Commission (EC) in its decisions against Motorola and Samsung adopted on 29 April 2014.⁵ In these decisions, the EC suggested a broader application of Article 102 TFEU to injunctions brought by SEP holders which had given a FRAND commitment (which was not the case in *Orange Book* itself). The EC concluded that a patent holder abuses its dominant position when, having given a FRAND commitment over a SEP to a standard setting body, it seeks an injunction against a “willing” licensee.⁶ The EC explained that if the alleged infringer agreed to take a licence and to be bound by a determination of the FRAND royalties by the relevant court or arbitration tribunal, it is considered a “willing licensee” and no injunction should be granted.⁷ The EC also clarified that a willing licensee remained free to challenge the validity of the patent, its alleged infringement, and the essentiality of the SEPs under licence,⁸ since “*it is in the public interest to allow challenges to the validity of patents and to ensure that royalties are not unduly paid.*”⁹

The Düsseldorf court found that applying the *Orange-Book-Standard* to the *Huawei v ZTE* case would lead it to issue the requested injunction, while applying the principles set out in the Samsung press release might lead it to dismiss Huawei’s action for injunction based on the competition law defence under Article 102 TFEU (depending on what was considered sufficient to be a willing licensee).

The ECJ judgment

The question of when a SEP holder is dominant was not addressed

At the outset of its analysis, the ECJ noted that the existence of Huawei's dominant position was not an issue before the Court. Finding whether a company holds a dominant position on a specific relevant market is a pre-condition for invoking Article 102 TFEU and the definition of the relevant market is of vital significance for the appraisal of dominance.¹⁰ However, the questions posed by the Düsseldorf court to the ECJ in *Huawei v ZTE* related only to the existence of an abuse.¹¹ The ECJ has jurisdiction only to give rulings on the interpretation or the validity of a provision of EU law on the basis of the facts put before it by the national court.¹² In this case the referring court stated that Huawei "unquestionably" holds a dominant position, without any request for the ECJ to clarify the approach it should take, meaning that the ECJ did not have the jurisdiction to examine that point.¹³

Thus the Court did not address an important issue – which was nonetheless raised by the Dutch government at the oral hearing and considered by Advocate General Wathelet in his Opinion – namely whether a SEP holder is *per se* in a dominant position by virtue of having a patent that is essential to a standard. In his Opinion on the case, the Advocate General, noted that the fact that an undertaking owned a SEP did not automatically mean that it held a dominant position. Rather in his view holding a SEP raised a rebuttable presumption of dominance, but that question needed to be examined by the national court on a case by case basis.¹⁴ This is in line with the Horizontal Guidelines¹⁵ and *Motorola* where the EC concluded that the mere holding of a SEP or the exercise of related rights does not confer dominance in and of itself.¹⁶ The Advocate General had also expressed caution about assuming that all SEP holders are dominant, in light of the special responsibility not to allow its conduct to impair genuine competition which a dominant position imposes on the undertaking concerned. He noted that a finding of dominance cannot therefore be based on hypotheses.¹⁷

In the *Samsung* case, the EC found that the company held a dominant position "*in the markets for the licensing of the technologies as specified in the UMTS standard technical specifications, on which each of its UMTS SEPs reads*" on the basis of a number of factors, including the widespread adoption of the UMTS standard and the fact that industry players were "locked-in."¹⁸ In *Motorola* the EC concluded that the company held a dominant position "*on the EEA market for the licensing of the technology, as specified in the GPRS standard technical specifications, on which Motorola's Cudak GPRS SEP reads,*"¹⁹ after assessing a number of factors, the most important being the indispensability of the GPRS standard, the industry "lock-in" to that standard.²⁰

Although the better view is that SEP holders should not *per se* be presumed dominant, given that the factors set out in *Samsung* / *Motorola* will apply to many SEPs, a SEP holder which

has given a FRAND commitment is likely to have to follow the steps set out in the Huawei judgment if it wishes to seek an injunction.

SEP holders who agree to license under FRAND create legitimate expectations

The need to maintain the right balance between competition rules and protection of intellectual property (IP) rights as well as the right to effective judicial protection is at the heart of *Huawei v ZTE*. The ECJ started its analysis by referring to the classic case law on compulsory licensing under which, the exercise of an IP right (e.g., by bringing an infringement action) cannot in itself constitute an abuse of a dominant position.²¹ Enforcement of IP rights violates competition rules only in exceptional circumstances.²² The ECJ focused on two main factors (the second of which distinguishes this case from the previous case law on compulsory licensing):

- the indispensability of the patent at issue, in the sense that it is essential to a standard established by a standardization body, rendering its use indispensable to all competitors that envisage manufacturing products complying with the standard to which the patent is linked;²³ and
- the fact that the SEP status was given in return for the proprietor's irrevocable undertaking to the standardization body that it is prepared to grant licences on FRAND terms, in conjunction with the fact that SEP status means that its proprietor can prevent products manufactured by competitors from appearing or remaining on the market and thereby reserve to itself the manufacture of the products in question.²⁴

These two circumstances “*create legitimate expectations on the part of third parties that the proprietor of the SEP will in fact grant licences on such terms,*” and therefore “*a refusal [...] to grant a licence on those terms*” may, in principle, constitute an abuse within the meaning of Article 102 TFEU and could be raised as a defence in actions for a prohibitory injunction or for the recall of products.²⁵

The reference in the judgment to “competitors” is intriguing. How to interpret it? Would we be going too far to read it as suggesting that a different legal standard may apply to a pure licensing entity, which is not a competing manufacturer, when it seeks an injunction? Probably – as such an interpretation is not borne out by the operative part of the judgment, which on its face applies to all SEP holders who seek an injunction. Perhaps the reference to competitors simply reflects the underlying facts of the case, i.e. it was between two companies that are competing manufacturers.²⁶

The requirements with which a dominant SEP holder needs to comply before seeking an injunction

The ECJ noted that SEP holders cannot be denied judicial protection and therefore should have recourse to legal proceedings to ensure effective enforcement of their exclusive rights.²⁷ Indeed, a SEP holder is not prevented from enforcing its patent, but only obliged to grant a licence on FRAND terms. However, in order to prevent an action for a prohibitory injunction from being regarded as abusive, a SEP holder must comply with conditions which seek to ensure “a fair balance of the interests concerned.”²⁸ As the ECJ put it, the irrevocable offer to grant licences on FRAND terms justifies “the imposition on that [SEP holder] of an obligation to comply with specific requirements when bringing actions against alleged infringers.”²⁹ The judgment sets out in detail these requirements and explains the legal framework under which FRAND licences of SEPs should be negotiated before an injunction is sought.

The requirements on the SEP holder as described below are cumulative and need to be fulfilled in the order presented by the judgment for the SEP holder legally to be able to seek an injunction.

First, the SEP holder must alert the SEP user, by giving notice or engaging in prior consultation, of the alleged infringement by designating the SEP at issue and specifying the way in which it has been infringed.³⁰ This criterion is justified because the SEP user may not be aware that it infringed a patent, due to the large number of SEPs which exist.³¹

Second, after the SEP user has expressed its willingness to take a FRAND licence, the SEP holder must present to the SEP user a specific, written offer for a licence on FRAND terms, specifying the amount of the royalty and the way that royalty is to be calculated.³² This requirement stems from the SEP holder’s commitment to limit its exclusive IP right by licensing it on FRAND terms. The SEP holder has also the necessary information to comply with the principle of non-discrimination, in particular, if it has already granted other licences. This requirement of a written offer as a prelude to discussion goes beyond the approach of the EC in *Motorola/Samsung*, i.e., it is an additional requirement. The ECJ did not explicitly address this issue, but presumably if the national court does not consider that the offer made by the SEP holder falls within the limits of what could be considered FRAND, then no injunction can be granted.

Once the SEP holder has fulfilled these requirements, it is up to the SEP user to take action if it is to be able to rely on a competition law defence to resist the granting of an injunction.

First, the SEP user must diligently respond to the SEP holder’s written offer, “in accordance with recognized 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.” Should the SEP user not accept the SEP holder’s offer, it has to submit, promptly and in writing, a specific counter-offer that corresponds to FRAND terms.³³

Second, if the SEP user is using the teaching of the SEP prior to the conclusion of a licensing agreement, it must provide appropriate security from the point at which its counter-offer is rejected, which must include the number of past acts of use of the SEP for which the SEP user must be able to render account.³⁴ Security can be provided by, for example, providing a bank guarantee or placing the necessary amounts on deposit.³⁵ The question of what would amount to “appropriate” security would be for a national court to determine.

The ECJ also added that if no agreement is reached after this round of offer and counter-offer, the parties “*may, by common agreement, request that the amount of the royalty be determined by an independent third party, by decision without delay.*”³⁶ It is not entirely clear whether this is a “requirement” to be fulfilled before an injunction could be issued. It appears that this is of less relevance than the four requirements listed above, given that this point is not included in the operative part of the judgment, which is the part that binds the national court. This is another difference in emphasis from the EC’s approach in *Samsung* and *Motorola*.

In addition, the ECJ clarified that a SEP user “*cannot be criticized*” for challenging, in parallel to the negotiations relating to the grant of licences, the validity of the relevant SEPs, their essential nature to the standard, or their actual use.³⁷ This is in line with the EC’s views expressed in the *Motorola* and *Samsung* cases as described above.

Finally, the ECJ made clear that the above requirements do not apply to actions seeking the rendering of accounts in relation to past acts of use of the SEP at issue or an award of damages in respect to those acts of use, because such actions do not directly affect competitors marketing products complying with the standard in question.³⁸

Implications of the judgment: in the EU, Germany and globally

The detailed guidelines set by the ECJ establish a procedural framework for SEP holders and SEP users seeking injunctive relief. SEP holders cannot go to court seeking an injunction against a willing licensee where the patent holder has committed to license its technology on FRAND terms unless specific requirements are fulfilled and specifically if they have not made an initial FRAND license offer. The judgment limits the possibility to use the threat of an injunction against users of a standardized technology, if the latter are prepared to take a licence under valid patents which they actually use. On the other hand, requirements are also imposed on SEP users which need to engage in specific steps before being able to argue that an injunction is abusive: the SEP user will have to present its own FRAND counter-offer. It seems that a declaration to be bound by a FRAND rate set by a court or arbitrator (which made a SEP user a “willing licensee” under the EC decisions) would have to follow the specific steps

(SEP user presents a counter-offer following SEP holder's offer) set out by the judgment. While the ECJ's test requires the SEP holder to present a FRAND offer to the SEP user, specifying the amount of royalty and the way the royalty is calculated, the ECJ did not define FRAND (indeed it was not asked to do so by the national court). The judgment does however suggest that there is not one single right view of FRAND in any particular licensing discussion, given that the SEP user is able to submit its FRAND counter-offer to a FRAND offer by the SEP holder. So FRAND is something that is negotiable and two different offers could be both FRAND. Accordingly, though the ruling is clear as to the procedures that have to be followed to obtain an injunction, it will not end, but only shift, the focus of the controversies in SEP cases pending before national courts.

Furthermore, the judgment, coming as it does on top of the EC's *Samsung* and *Motorola* decisions, will significantly change the balance of German SEP litigation and shift the burden of proof. So far, Germany has been a forum of choice for European patent litigation. German courts have been generous in granting injunctions for patent infringements and have taken the view that competition law defences generally do not bar an injunction, even if the litigation concerns a SEP. Accordingly, it was the defendant's burden to prove all the elements of a competition law defence. Under the ECJ's approach, the SEP holder seeking injunctive relief will be obliged to prove that he approached the infringer and offered him an agreement on FRAND terms. If the defendant contests the FRAND assertion, for example on the basis of its own FRAND royalty calculation, the court will have to appoint an expert to resolve this issue. This will likely be time-consuming and costly.

Finally, the judgment once again shows the global reach and driving role of EU competition law in the technology sector and, indeed, in all sectors where IP plays an important role. An interesting feature of the case is that no European companies are involved. It is a battle between two big Chinese tech companies, Huawei and ZTE. The choice of Europe for a tech dispute between global players is not new – Sun and Real Networks took their battle with Microsoft to Brussels over 15 years ago. However, it is perhaps a sign of changing times that a key EU decision is being set for the first time by Chinese tech giants rather than US ones.

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- ¹ Respectively, Partner and Associate in the Brussels office of White & Case LLP. The opinions expressed in this article are personal to the authors and do not necessarily represent the opinions of either White & Case LLP or any of its clients.
- ² C-170/ 13 *Huawei v ZTE*, EU:C:2015:477 (Judgment).
- ³ The details of the *Motorola* and *Samsung* decisions were not public at the time the Düsseldorf court made the reference to the ECJ. At the time only the EC press releases were available.
- ⁴ KZR 39/06.
- ⁵ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*; Commission decision of 29 April 2014, Case AT.39939 – *Samsung - Enforcement of UMTS Standard Essential Patents*.
- ⁶ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*, recital 427.
- ⁷ *Ibid.*, recital 437.
- ⁸ Commission decision of 29 April 2014, Case AT.39939 – *Samsung - Enforcement of UMTS Standard Essential Patents*, recitals 99 and 107. In particular, in *Samsung* the EC held that the applicable rules on burden of proof in litigation regarding challenges of the patent licensing agreement will not be altered and that “*the court will be requested by the parties, and the arbitration tribunal shall take into account issues of validity, infringement and essentiality.*”
- ⁹ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*, para. 491. This ensures that “*companies, and ultimately consumers, are not obliged to pay for patents that are not infringed.*” (see Commission MEMO of 29 April 2014, available at [http://europa.eu/rapid/press-release MEMO-14-322_en.htm](http://europa.eu/rapid/press-release_MEMO-14-322_en.htm))
- ¹⁰ C-6/72, *Continental Can v Commission*, EU: C:1973:2, para. 32; C-49/07, *Motosykletistiki Omospondia Ellados NPID (MOTOE) v Elliniko Dimosio*, EU:C:2008:376, para. 31.
- ¹¹ Judgment, para. 43.
- ¹² C-138/08, *Hochtief and Linde-Kca-Dresden*, EU:C:2009:627, para. 22.
- ¹³ AG Wathelet Opinion in C-170/ 13 *Huawei v ZTE* delivered on 20 November 2014 (AG Wathelet Opinion), para. 57 and footnote 20.
- ¹⁴ *Ibid.*, para. 57. See also footnote 26 where the Advocate General cites C-457/10 P *AstraZeneca v Commission*, para. 186 (“*although the mere possession of intellectual property rights cannot be considered to confer such a position, their possession is none the less capable, in certain circumstances, of creating a dominant position, in particular by enabling an undertaking to prevent effective competition on the market.*”)
- ¹⁵ Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements (Horizontal Co-operation Guidelines), para. 269: “*(...) even if the establishment of a standard can create or increase the market power of IPR holders possessing IPR essential to the standard, there is no presumption that holding or exercising IPR essential to a standard equates to the possession or exercise of market power. The question of market power can only be assessed on a case by case basis.*”
- ¹⁶ Commission decision of 29 April 2014, Case AT.39985 - *Motorola – Enforcement of GPRS Standard Essential Patents*, recital 211.
- ¹⁷ AG Wathelet Opinion, para. 58.
- ¹⁸ Commission decision of 29 April 2014, Case AT.39939 – *Samsung - Enforcement of UMTS Standard Essential Patents*, paras 45-51.

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- ¹⁹ Commission decision of 29 April 2014, Case AT.39985 - Motorola – Enforcement of GPRS Standard Essential Patents para. 269.
- ²⁰ *Ibid.*, para. 226.
- ²¹ Judgment, paras 42 and 47.
- ²² *Ibid.*, para. 46. See also C- 238/87 *Volvo v. Veng*, EU:C:1988:477, para. 8, C 241/91 P and C 242/91 P RTE and ITP v Commission, EU:C:1995:98, para 33; C 418/01 *IMS Health v. NDC Health GmbH*, EU:C:2004:257, para. 34.
- ²³ Judgment, paras 49-57.
- ²⁴ *Ibid.*, paras 51-52.
- ²⁵ *Ibid.*, paras 53-54.
- ²⁶ The EU Commissioner in a recent speech at the International Bar Conference in Florence on 11 September 2015 stated that the principles of the judgment should not be limited to manufacturers of devices using the essential technology, but also apply to companies at other levels of the distribution chain, for example telecom operators. In that context, it is understood that the EC has requested information from the parties involved in a patent dispute initiated by Saint Lawrence, a patent licensing company and subsidiary of US-based Acacia, against Deutsche Telekom for distributing (but not producing) handsets using Saint Lawrence’s technology.
- ²⁷ Judgment, paras 57 – 58.
- ²⁸ *Ibid.*, para. 55.
- ²⁹ *Ibid.*, para. 59.
- ³⁰ *Ibid.*, paras 60-61.
- ³¹ *Ibid.*, para. 62.
- ³² *Ibid.*, paras 63-64. This differs from AG Wathelet’s Opinion which opined that, after alerting the SEP user, the SEP holder had, “*in any event*,” to present a written offer for a license on FRAND terms (AG Whatelet Opinion, para. 85).
- ³³ Judgment, paras 65-66.
- ³⁴ This conclusion differs from the Advocate General’s Opinion, which did not consider that security should be proactively provided in order for the Article 102 TFEU defence to succeed.
- ³⁵ Judgment, para. 67.
- ³⁶ *Ibid.*, para. 66.
- ³⁷ *Ibid.*, para. 69.
- ³⁸ *Ibid.*, paras 72-76.