Update China Desk

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English Version

"Intellectual Property and EU Competition Law – a tight squeeze for Chinese telecommunication giants"

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On July 16th 2015 the European Court of Justice (ECJ) delivered its long awaited judgment in the Huawei Technologies v. ZTE Corp. case[1] on the infringement of standard essential patents (SEPs). The ECJ ruling alleviates discrepancies between European antitrust rules and (national) patent laws which have been a source of uncertainty in the past. This case highlights the rising importance of patent litigation to Chinese companies, as it pits the two rival behemoths of Chinese telecommunications against each other.

Patent litigation cases related to SEPs have proliferated around the globe in recent years[2], especially in the telecommunications sector with big names like Apple, Google, Microsoft, Motorola and Samsung seeking injunctive relief for patent infringements (the so called "patent wars").

Technical standards are set by standard setting organizations (**SSOs**) such as the European Telecommunications Standards Institute (**ETSI**), which ensure interoperability of the implemented technologies.

When a patent protected technology is *essential* to a certain standard it is called a SEP. Contrary to non-essential patents it is impossible for competing companies to invent alternative solutions because the SEP is a requirement of the set standard.

Considerable market power is thus conferred on the holder of a SEP when a standard is implemented throughout an industry.

Standard Essential Patents

[1] Case C-170/13 Huawei Technologies Co. Ltd v ZTE Corp., ZTE Deutschland GmbH.

[2] http://ec.europa.eu/growth/industry/intellectual-property/patents/standards/index_en.htm

While standardization agreements under SSOs generally do not infringe on EU competition law, they enable patent holders to extract excessive royalty fees or to "hold up" users of the standard by excluding competitors by means of injunction.

Therefore SSOs require their members to commit to licensing any patents deemed essential on FRAND[3] terms in order to prevent a holder of a SEP to obtain significant market power,

Huawei v. ZTE Background

Huawei, a leading telecommunication equipment manufacturer in the world, headquartered in Shenzhen, China holds a European patent declared essential to the Long Term Evolution (**LTE**) mobile telecommunications standard developed by ETSI.

ZTE – another Chinese telecommunications manufacturer – allegedly infringed upon Huawei's patent. A licensing agreement could not be reached and consequently Huawei applied for injunctive relief in Germany and other European countries based on its SEP. ZTE claimed Huawei was making use of its dominant position and that its application for injunctive relief was abusive.

The Düsseldorf Regional Court who handled the case was faced with two seemingly inconsistent precedents, one set by the German Federal Court of Justice in its *Orange-Book-Standard*[4] decision and the other set by the European Commission decision in the *Samsung*[5] case.

Orange-Book-Standard

The German Federal Court had held in its decision that a plaintiff abuses its dominant position by seeking injunctive relief on the grounds of a patent infringement if the defendant:

(1) unconditionally offers to enter into a license agreement with the plaintiff at a particular royalty rate or at a rate to be determined by the plaintiff and

(2) the defendant behaves as if it is an actual licensee, and pays royalties into an escrow account.

However this case differed from the Huawei v ZTE case as the patent in question was only *de facto* an essential patent, meaning it was essential due to market forces and not because it was deemed as such by a SSO.

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[3] **Fair, Reasonable and Non-Discriminatory**

[4] BGH KZR 39/06, 2009.

[5] http://europa.eu/rapid/press-release_IP-14-490_en.htm

The Commission on the other hand had found in the *Samsung* case that if a SEP holder had committed to

(1) license its SEPs and

(2) do so on FRAND terms,

it is anti-competitive to try to exclude competitors from the market by seeking injunctions on the basis of its SEPs if the licensee is willing to negotiate such a license.

Samsung

Since ZTE had allegedly been willing to negotiate a license, the court in Düsseldorf was faced with two contradictory decisions. It therefore stayed the decision and referred a series of questions to the EJC and requested a preliminary ruling.

The ECJ did not refute Huawei's dominant position conferred by its SEP and therefore limited its analysis on the issue of abuse.

In its judgement the ECJ found that seeking injunctive relief was not per se abusive but depended on certain actions on the side of the SEP holder and user as set out by the court.

ECJ Decision

(1) SEP holder must notify the SEP user of the infringement

(2) SEP user must indicate its willingness to conclude a license on FRAND terms

(3) SEP holder must present a written (initial) offer on FRAND terms

(4) SEP user must respond promptly, diligently, and in good faith

While the court established criteria which strike a balance between European competition law and (national) patent laws, it - deliberately – refrained from defining at what point a SEP holder has a dominant position and what constitute *fair, reasonable and non-discriminatory* terms. Therefore it is up to national courts to address these issues on a case-by-case basis.

The Huawei v. ZTE judgement provides for welcome clarity and will not only reverberate through Europe but also beyond, as this decision, in all likelihood, has been closely monitored by Chinese antitrust regulators.

SEP and Antitrust in China

In recent years China's telecommunications market has become one of the largest in the world. At the same time China

has also seen significant developments in antitrust enforcement, starting with the promulgation of the Anti-Monopoly Law (**AML**) in 2009.

Officials at the National Development and Reform Commission (**NDRC**), the Chinese competition authority charged with investigating abuses of dominance have recently announced that the NDRC will step up measures to combat anticompetitive behavior by SEP holders.

Qualcomm

In February 2015 the NDRC had fined Qualcomm, an American semiconductor company that holds several SEPs for certain telecommunication standards CNY 6.08 billion (approx. EUR 870m), one of the largest fines imposed by any antitrust authority in the world against a single company. The NDRC had charged Qualcomm with imposing excessive royalties on Chinese mobile device manufacturers.

As Chinese companies are slowly shifting from intellectual property (**IP**) users to IP creators with companies like Huawei and ZTE at the forefront, the protection of IP rights will play an ever more important role. Like their European counterparts Chinese regulators, competition authorities and courts will be faced with the complex interplay between IP and antitrust rules.

Conclusion

In conclusion the ECJ decision provides useful guidelines to SEP owners and implementers alike. However essential questions like when a company is deemed dominant and what constitute FRAND terms are left unresolved and will certainly be addressed in future cases.

As the Chinese government's national strategy aims to transform the Chinese economy from "Made in China" to "Created in China" it is faced with the same issues that challenge regulators around the world. China is moving ahead fast and it is encouraging to see that companies can fully defend their commercial interests.

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