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INTELLECTUAL PROPERTY AND STANDARD SETTING

-- Note by Germany --

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Introduction

1. Technical standards and competition are both important factors which contribute to innovation and thus economic growth. However, the relationship between standards and competition law bears potential for conflict. As companies are only willing to make investments in research and development if they can expect that their investments will pay off, intellectual property needs effective protection. However, the right balance must be maintained between the stimulation of innovative activity on the one hand and participation in technical advances on the other. One key area that has been highly disputed and is under the scrutiny of the courts is the question of how to deal with standard essential patents.

2. This contribution builds upon the earlier contributions by the Federal Republic of Germany submitted to the OECD Roundtable on Competition, Patents and Innovation of June 2009¹ and to the Roundtable on Standard Setting of June 2010². It will focus on the possible abuse of a dominant position based on a standard-essential patent (SEP) in the context of the claim for an injunction (below B). German case law dealing with this issue follows the approach developed by the Federal Court of Justice in its "Orange Book Standard" – decision which will be outlined under B.1.³ The latest developments in this regard are pointed out under B.2. Under C. the contribution illustrates a merger control proceeding that focussed on patents. The contribution ends with concluding remarks (D.).

1. Standards and abuse of dominance

3. A patent gives the patent holder an exclusive right; however, in using the right, the patent holder is bound to the principles of competition law. This is of particular importance with regard to products where innovations of different companies or even competitors build upon or complement each other in a way that the companies need licences for each other's patents to avoid possible infringements. Often this situation is solved by cross-licensing or offering royalty-free licences. Where companies negotiate licence contracts with royalty payments, conflicting interests about the terms and conditions may arise. This is particularly complex in the context of technical standards and SEPs.

4. Standards are established by standard setting organisations (SSOs)⁴ where the member companies of the SSO work together e.g. in committees or working groups.⁵ The advantage of agreeing on such standards is that they ensure interoperability and compatibility between related products which in many cases has great economic benefits.⁶ Once, however, a standard is agreed upon it confers a certain degree of market power to its participants. As it is not possible to develop around "essential" patents, anyone who

¹ German contribution to the Roundtable on Competition, Patents and Innovation of June 2009 <http://www.oecd.org/daf/competition/roundtables.htm#v2009>

² German contribution to the Roundtable on Standard Setting of June 2010 <http://www.oecd.org/daf/competition/47381304.pdf>

³ For overview in German cf. Thomas Kühnen, Der kartellrechtliche Zwangslizenzinwand und seine Berücksichtigung im Patentverletzungsprozess, Festschrift für Tilmann, p. 513 et seqq.

⁴ For SSOs in Germany cf. German contribution to the Roundtable on Standard Setting of June 2010

⁵ See for example ETSI, European Telecommunications Standards Institute <http://www.etsi.org/about/how-we-work>

⁶ Cf. European Commission, Horizontal Guidelines, OJ C 11, 14.1.2011, pp. 1–72, para. 263.

would like to use the standard depends on licences for the relevant SEPs. Possible scenarios that may raise competition concerns in this situation are, inter alia, that the holder of an SEP refuses a licence, thereby preventing competitors from having access to the standard. Alternatively, the SEP holder grants a licence only on restrictive or discriminatory terms and conditions. Without the right to use the SEP the potential licensee is prevented from using the technology and accordingly cannot compete with the patent holder.

5. SSOs have identified the risks described above (and others such as “patent ambushes”⁷) and integrated rules in their proceedings to minimize them. A company participating in the standard setting process has to disclose essential patents and declare whether it is willing to grant royalty-free licences or to make it possible for the other parties in the standardisation process and third parties to obtain a licence on fair, reasonable and non-discriminatory (FRAND) terms. If the patent holder refuses to grant royalty-free licences or licences under FRAND terms, the standardisation process is suspended and the standard is redesigned in order to circumvent the patent in question.

6. Against the background of disputes between mobile phone manufacturers, the question has come into focus whether the holder of an SEP can abuse a dominant position deriving from holding an SEP if he takes a company to court that uses the SEP without having agreed on a corresponding licence agreement and files for injunctive relief. The defendant can try to oppose this claim in various ways, inter alia by raising the “competition law defence”. The defendant would argue that he is entitled to a licence agreement under antitrust law and that the patent holder is abusing its dominant position by not concluding a patent licence agreement on non-discriminatory and non-restrictive terms and conditions. The competition law defence is based on the *dolo petit* - consideration, i.e. although a party using a patent without the consent of the patent holder acts unlawfully, the patent holder cannot sue the party because he would be asking for something he would have to give back immediately (in the form of the licence) and thereby violate the principle of good faith under German civil law. National courts within the European Union have reached different conclusions when dealing with this issue.

2.1 *The Orange Book Standard - decision*

7. In 2009 the Federal Court of Justice issued its landmark *Orange Book Standard* - decision (KZR 39/06).⁸ Philips was the owner of a patent that was *essential* for the production of recordable and rewriteable optical data carriers (CDR and CDRW). The patent was not standard-essential in the sense that it was the result of a standard setting process and Philips did not provide a FRAND declaration but it concerned a necessary part of a *de facto* standard. Philips had granted many companies a licence to the patent on the basis of a standard licence agreement. One company manufactured and marketed CDRs and CDRWs without such a licence. The company argued that the licence fees were excessive and also discriminatory because other companies had been granted more favourable conditions. According to the company, Philips had abused its dominant position. The Regional and Higher Regional Courts granted injunctive relief.

8. The Federal Court of Justice stated that the patent holder may not discriminate against a company wishing to conclude a licence agreement by charging this company higher licence fees than others would have to pay without any objective justification. However, according to the Orange Book ruling, the patent holder claiming for an injunction based on his patent abuses his dominant position only if two conditions are met:

⁷ See German contribution to the Roundtable on Standard Setting of June 2010

⁸ Cf. Federal Court of Justice, decision of 9.5.2000: <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&sid=7aacd183a773de293b2ba2910eb8354e&clien t=12&nr=22802&pos=0&anz=1> (German, translation into English: <http://www.ipeg.eu/blog/wp-content/uploads/EN-Translation-BGH-Orange-Book-Standard-eng.pdf>.) The Bundeskartellamt regularly engages in civil proceedings as *amicus curiae* and submitted its observations during the oral procedure of the Orange Book case.

9. Firstly, the potential licensee must show that he has made and remains bound by an unconditional offer (i.e. particularly not under the condition that a court affirms the infringement of the patent) to conclude a licence agreement which the patent holder cannot reject without violating the prohibition of discrimination or anti-competitive behaviour. The decision does not discuss what kind of terms and conditions such a licence offer has to include in detail.

10. Secondly, the potential licensee, if he already uses the patent before the holder of the patent has accepted his offer, has to fulfil the obligations defined in the proposed licence agreement. This means in particular, that the potential licensee has to pay the royalties resulting from the contract or ensure their payment. The licensee does not have to make payment to the patent holder, but can deposit the royalties.

11. Furthermore, the court stated that if the potential licensee considers the requested royalties to be excessive or the patent holder refuses to quantify the royalties it would be admissible to offer the holder of the patent an unspecified fee to be determined by the patent holder at his reasonable discretion, and to deposit an amount which at least corresponds to the objectively appropriate amount of the licence fee or possibly exceeds this level. The Federal Court of Justice held that, if necessary, the licensee could clarify in later proceedings whether the licence fee imposed was within the limits set by competition law.

12. Lower German courts and appeal courts which hear a considerable number of patent infringement cases of international significance have applied these criteria to many injunction requests, including those concerning SEPs.⁹ To give a few examples of the relevant case law: the Düsseldorf Regional Court found that the SEP holder is not obliged to make an offer on its own initiative to conclude a licence agreement;¹⁰ the Mannheim Regional Court found that the defendant has in principle to recognise the patent holder's entitlement to compensation if he applies the competition law defence after having started using the SEP (he can challenge the amount though)¹¹. Regarding the criterion "unconditional" the Mannheim Regional Court stated that the potential licensee may not question the validity of the patent.¹² In this case, the potential licensee added a termination clause to his offer which applies if the licensee challenges the validity of the patent. This dispelled the appeal court's concerns.¹³ Overall, the case law of the lower courts in SEP cases is considered patent holder friendly.¹⁴

2.2 *Latest developments: Samsung, Motorola, Huawei/ZTE*

2.2.1 *The European Commission: Samsung and Motorola*

13. On 29 April 2014 the Commission issued its first decisions concerning competition law enforcement in relation to SEPs. In 2011 Samsung started to seek injunctive relief before courts in various Member States including Germany against Apple based on claimed infringements of SEPs relating to the

⁹ Düsseldorf Regional Court 24.4.2012, 4b O 274/10 http://www.justiz.nrw.de/nrwe/lgs/duesseldorf/lg_duesseldorf/j2012/4b_O_274_10urteil20120424.html

¹⁰ LG Düsseldorf 24.4.2012, 4 B 274/10

¹¹ Mannheim Regional Court 9.12.2011 7 O 122/11, recital 89, http://lrw.juris.de/cgi-bin/laender_rechtsprechung/document.py?Gericht=bw&GerichtAuswahl=Landgerichte&Art=en&Datum=2011-12&nr=15103&pos=2&anz=5 (German)

¹² Mannheim Regional Court 9.12.2011 7 O 122/11, recital 91

¹³ OLG Karlsruhe (Appeal Court) 27.2.2012, 6 U 136/11, recital 31 http://lrw.juris.de/cgi-bin/laender_rechtsprechung/document.py?Gericht=bw&GerichtAuswahl=OLG+Karlsruhe&Art=en&Datum=2012-2&nr=15385&pos=2&anz=5

¹⁴ Cf. Alison Jones, Standard-essential patents: FRAND commitments, injunctions and the smartphone wars, European Competition Journal 2014, p. 11 et seqq.

3G UMTS standard. When this standard was adopted, Samsung had given a FRAND commitment. The Commission found that under the specific circumstances of the case seeking injunctions against Apple based on Samsung's SEPs may constitute an abuse of a dominant position. Samsung offered commitments which the Commission rendered legally binding on 29 April 2014.¹⁵ On 29 April 2014 the European Commission also adopted a decision which found that Motorola's seeking of an injunction against Apple before a German court on the basis of a smartphone SEP constituted an abuse of a dominant position prohibited by EU antitrust rules.¹⁶

14. The Commission pointed out that seeking injunctions before courts is generally a legitimate remedy for patent holders in case of patent infringements; but seeking an injunction based on SEPs may constitute an abuse of a dominant position if firstly an SEP holder has given a voluntary commitment to license its SEPs on FRAND terms and secondly where the company against which an injunction is sought is willing to enter into a licence agreement on such FRAND terms.

2.2.2 *Huawei/ZTE*

15. The press release of the European Commission concerning its issue of a statement of objections in its Samsung case¹⁷ prompted the Düsseldorf Regional Court (Landgericht Düsseldorf) to suspend proceedings in a dispute between Huawei and ZTE¹⁸ and to refer five questions to the European Court of Justice (C-170/13)¹⁹. According to Art. 267 Treaty on the Functioning of the European Union (TFEU) a court of a Member State of the European Union can refer questions to the Court of Justice about the interpretation of European Law.

16. Huawei and ZTE are two Chinese telecommunications hardware manufacturers. Huawei holds an SEP essential to the LTE (Long Term Evolution) standard used in mobile phone communication. Huawei notified the patent to the respective standard setting organisation (European Telecommunications Standards Institute – ETSI) and made a commitment to grant licences to third parties on FRAND terms. ZTE inter alia develops and markets base stations with LTE software in Germany. The companies unsuccessfully discussed the possibility of concluding a licence agreement. Huawei named a royalty; ZTE offered a cross-licensing agreement and proposed a royalty. However, ZTE did not make a payment. Huawei claimed an infringement and sued ZTE for injunctive relief.

¹⁵ Samsung committed not to seek injunctive relief before a court in the European Economic Area for the infringement of its SEPs in respect of a standard implemented in smartphones and tablets if the potential licensee agrees to a licensing framework according to which a third party sets FRAND terms in case the parties have not agreed on a licensing agreement within a period of 12 months. Case AT.39939 - Samsung - Enforcement of UMTS standard essential patents, http://ec.europa.eu/competition/antitrust/cases/dec_docs/39939/39939_1501_5.pdf

¹⁶ Apple proposed several licence agreements, one allowing Motorola to set the royalties according to its equitable discretion and on FRAND terms. Case AT.39985 Motorola - Enforcement of GPRS standard essential patents, http://ec.europa.eu/competition/antitrust/cases/dec_docs/39985/39985_928_16.pdf

¹⁷ http://europa.eu/rapid/press-release_IP-12-1448_en.htm “[...] While recourse to injunctions is a possible remedy for patent infringements, such conduct may be abusive where SEPs are concerned and the potential licensee is willing to negotiate a licence on Fair, Reasonable and Non-Discriminatory (so-called "FRAND") terms. [...]”

¹⁸ Düsseldorf Regional Court, 21.03.2013, 4b O 104/12 www.justiz.nrw.de/nrwe/lgs/duesseldorf/lg_duesseldorf/j2013/4b_O_104_12_Beschluss_20130321.html

¹⁹ Request for a preliminary ruling lodged on 5 April 2013, Huawei Technologies Co. Ltd v ZTE Corp., ZTE Deutschland GmbH, Case C-170/13. Questions referred in English. <http://curia.europa.eu/juris/document/document.jsf?text=&docid=139489&pageIndex=0&doclang=EN&mode=req&dir=&occ=first&part=1&cid=394895>

17. The Düsseldorf Regional Court decided to refer the case because of the importance of the questions raised and the large number of patent infringement litigations concerning SEPs in Europe.

18. The Court explained that if it had adopted the approach described in the Commission's press release to the Huawei/ZTE case, ZTE would be considered willing to negotiate and thus ZTE's competition law defence would apply. On the other hand, according to the Orange-Book criteria the defence would not apply because the offers made by ZTE were not unconditional, ZTE did not comply with the obligations defined in the licence agreement to be concluded as it did not make any payments or deposits and, finally, ZTE did not render an account for past acts of use.

19. In particular, the Court wanted to know whether an SEP holder is abusing his dominant market position if he brings an action for an injunction against a patent infringer although the infringer has declared that he is willing to negotiate such a licence (this reflects the Commission's approach described in the press release) or whether an abuse of the dominant market position is to be presumed only where the infringer has submitted to the SEP holder an acceptable, unconditional offer to conclude a licensing agreement which the patent holder cannot refuse without unfairly impeding the infringer or breaching the prohibition of discrimination, and the infringer fulfils his contractual obligations for acts of use already performed in anticipation of the licence to be granted (reflecting the criteria developed by the Federal Court of Justice in its Orange Book Standard - decision and applied to SEP cases by lower courts).

20. The Düsseldorf Regional Court itself tends to the opinion that it is not sufficient to demonstrate a willingness to negotiate.²⁰ One of the arguments is that willingness to negotiate is open to different interpretations. The potential licensee could declare that he is willing to negotiate but withdraw the declaration at any time. The court explains that in its experience not all patent users that try to put forward the competition law defence are seriously interested in concluding a licence agreement.²¹ The court points out that on the one hand an injunction should not be used as a threat allowing the patent holder to enforce royalties exceeding FRAND. However, on the other hand the negotiating position of the patent holder should not be weakened in a way that the infringer could achieve unreasonably low royalties which would be the case if the patent holder would not be allowed *per se* to file for an injunction.²² The court does not strictly follow the Orange Book approach, particularly regarding the requirement of an "unconditional" offer. In the court's view there is no urgent need for the agreement to be unconditional in that only those products are covered which (affirmed by a court) infringe the SEP. Furthermore, the court does not consider it imperative that the patent user may not make his offer conditional upon the validity of the patent, as this could lead to a situation where the validity of SEPs is not reviewed at all.²³

21. The Advocate General proposed answers to the questions of the Düsseldorf Regional Court to the Court of Justice on 20 November 2014.²⁴ The Advocate General draws a clear line between cases concerning SEPs where the patent holder was part of a standard setting process of an SSO, thus had impact on the standard and gave a FRAND commitment to the SSO (as Huawei and ZTW did) on the one hand

²⁰ Düsseldorf Regional Court, 21.03.2013, 4b O 104/12, recital 31 et seqq.

²¹ As Bo Vesterdorf puts it "It should not be forgotten that implementers very often either "forget" or use every trick in the book to avoid taking a licence or at least try to drag out negotiations for as long as possible; in practice sometimes for months and years, without paying anything in the meantime.", CPI Antitrust Chronicle, Antitrust Enforcement and Civil Rights: SEPs and FRAND Commitments, August 2014 (1).

²² Düsseldorf Regional Court, 21.03.2013, 4b O 104/12, recital 35 et seqq.

²³ Düsseldorf Regional Court, 21.03.2013, 4b O 104/12, recital 44 et seqq.

²⁴ Advocate General's Opinion, C-170/13, Huawei/ZTE <http://curia.europa.eu/juris/document/document.jsf?text=&docid=159827&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=5041> (English version)

and de facto standards (Orange Book, no FRAND commitment) on the other hand. In the Advocate General's view it is natural that the holder of a de facto standard that has not given any commitment to grant a licence under FRAND terms has greater negotiating power²⁵ than the patent holder who has given a FRAND commitment and thereby voluntarily restricted his right.²⁶ On this basis, the Advocate General argued that the Orange Book Standard cannot be applied by way of analogy to the Huawei/ZTW case. At the same time the Advocate General makes it clear that a vague and non-binding willingness of the patent user to negotiate cannot be a criterion on which a competition law defence can be based.

22. The Advocate General considers it necessary to find a middle course-. He believes that as a general rule a patent holder is free to use, inter alia, an injunction to enforce its right. The infringer, before using the patent, has to open negotiations in order to conclude a licence agreement. The situation is different if the patent holder has given a FRAND commitment. In this case he is obliged to take certain measures before bringing the infringer to court. If the infringer is not aware of the infringement, the SEP holder has to alert him and specify the infringement. The Advocate General argues that the infringer does not necessarily know that he is infringing a valid patent given the number of patents notified to SSOs as essential and the proportion of patents that are not valid or essential. The SEP holder has to offer the infringer a licence agreement on FRAND terms which has to indicate the amount of the licence fee. In the Advocate General's view it can be expected that the SEP holder prepared a draft offer when giving the FRAND commitment anyway.²⁷ The infringer has to show himself ready, willing and able to conclude a licence agreement. He has to respond in a serious manner and accept the offer or promptly present a counter offer. Referring to the concerns of the Düsseldorf Regional Court, the Advocate General points out that if the infringer acts purely in a tactical or unserious manner, an injunction would not constitute an abuse of a dominant position. The infringer is free to ask for the terms to be set by a court or an arbitration tribunal if the negotiations are not opened or unsuccessful without being regarded as unserious. In this case the SEP holder can ask for a bank guarantee or a deposit. Furthermore, the infringer should be free to challenge the validity, use and essential nature of the patent.

23. The opinion of the Advocate General is not binding on the Court of Justice.

3. Merger control and patents: Novell

24. The role of patents was also the subject of several merger control proceedings.²⁸ The creation of the joint venture CPTN by Microsoft, Oracle, Apple und EMC in 2011 is an example of merger control proceedings which focus primarily on issues relating to patents. The concentration was notified to the Bundeskartellamt and the US Department of Justice and the two authorities cooperated closely with each other, based on waivers provided by the parties.²⁹

25. Microsoft, Oracle, Apple and EMC created CPTN as a vehicle to acquire 882 software patents from Novell. CPTN would acquire the patents which would then be allocated and distributed to the four owners, each granting and receiving licences for all the respective patents. The acquisition vehicle CPTN would then be dissolved.

²⁵ Advocate General's Opinion, C-170/13, Huawei/ZTE, recital 48

²⁶ Advocate General's Opinion, C-170/13, Huawei/ZTE, recital 86

²⁷ Advocate General's Opinion, C-170/13, Huawei/ZTE, recital 86

²⁸ Cf. German contribution to the Roundtable on Competition, Patents and Innovation of June 2009.

²⁹ See US Department of Justice, Justice News of 20.04.2011, <http://www.justice.gov/opa/pr/cptn-holdings-llc-and-novell-inc-change-deal-order-address-department-justices-open-source>

26. The patents concerned inter alia the open source operating system “Linux”. The transaction raised concerns in respect of markets for operating systems and virtualization software in which Microsoft and EMC/VMware respectively held at least a powerful position. The Bundeskartellamt received a number of complaints that these positions might be further strengthened if the acquirer applied “Fear, Uncertainty, Doubt” - strategies (FUD) against smaller competitors by pursuing them by means of patent actions.

27. The parties altered their original plans in response to competition concerns expressed by both authorities which allowed the authorities to clear the transaction without an in-depth investigation.³⁰

4. Conclusion

28. Disputes about patents as described above are in most cases efficiently handled by specialized chambers of civil courts. Since 2009 the courts have applied the approach developed by the Federal Court of Justice in the Orange Book Standard - decision which in general leads to appropriate results.³¹ In light of the above, the Bundeskartellamt has never opened formal proceedings dealing with an alleged abuse of dominance related to a dispute about a standard-essential patent.

29. However, a further refinement of the case law dealing with the competition law defence must be welcomed. In particular with regard to complex products like mobile phones where standards are of utmost importance in order to guarantee interoperability there seem to be scenarios which highlight the possible limitations of the Orange Book approach which when established by the Federal Court of Justice did not target SEPs.³² With respect to some standards the sheer number of patents may make it difficult and uncustomary to enter into negotiations on every single SEP before applying the standard. The user of the patent may not in all cases know that he is infringing a patent. Furthermore, the patent holder and the potential licensee may become entangled in various court proceedings before different courts dealing with the licence agreements or the patents. Finally, the parties’ view on the appropriate amount of a licence fee can differ considerably.

30. While the legal nature of a FRAND commitment might not be clearly defined, the approach by the European Commission shows that if it is supposed to make any difference it has to oblige the owner of the patent to take some active role before claiming an injunction if the other party is willing to negotiate. Recalling the arguments of the Düsseldorf court it will have to be analysed in detail whether the decisions may risk shifting the balance of negotiating power too far to the patent infringer.³³ In view of this it will be even more interesting to see how the opinion of the Advocate General further refines the respective obligations with a view to a fair balance of negotiating powers. The decision of the European Court of Justice will be expected with great interest.

³⁰ For more details cf. Bundeskartellamt Activity Report 2011/2012 p. 94, <http://www.bundeskartellamt.de/SharedDocs/Publikation/DE/Taetigkeitsberichte/Bundeskartellamt%20-%20T%C3%A4tigkeitsbericht%202012.html?nn=3591134> (German)

³¹ Deichfuß, Die Rechtsprechung der Instanzgerichte zum kartellrechtlichen Zwangslizenzienwand nach „Orange-Book-Standard“, WuW 2012, 1146-1162 (1161).

³² In a recent interview Professor Joachim Bornkamm, Presiding Judge at the Federal Court of Justice until February 2014, pointed out that when ruling in the Orange Book case the Federal Court of Justice did not focus on SEPs. It rather aimed to define the conditions for a serious licence offer in a situation where the potential infringer had never applied for a licence but used the standard nonetheless. JUVE Rechtsmarkt 06/14 p. 62.

³³ According to Bo Vesterdorf, CPI Antitrust Chronicle, August 2014 (1), this might even discourage the patent holder from taking part in standard setting procedures, giving FRAND commitments or investing in R&D at all.