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THE SURVEY SAYS: TIFFANY IS NOT GENERIC FOR A RING SETTING

By Jennifer Lee Taylor and Sabrina Larson

Last month, the Southern District of New York granted summary judgment to Tiffany & Co. on its trademark infringement claim against Costco Wholesale Corporation for selling rings advertised under the TIFFANY mark. *Tiffany & Co. v. Costco Wholesale Corp.*, No. 1:13-cv-01041 (S.D.N.Y. Sept. 8, 2015).

Tiffany had sued Costco after learning that it was displaying rings next to signs reading "Platinum Tiffany .70 VS2" and "Platinum Tiffany VS2.1." Costco counterclaimed, asserting that "Tiffany" is a generic term for a type of ring setting. Costco also raised fair use as an affirmative defense.

Tiffany unsuccessfully filed an early summary judgment motion on Costco's genericness counterclaim. The court denied that motion, holding that factual disputes existed as to the meaning of the terms "Tiffany" and "Tiffany setting" in the minds of the general public.

Tiffany later filed another summary judgment motion for infringement and counterfeiting, and on Costco's genericness counterclaim and fair use defense. With its motion, Tiffany presented a survey with 464 respondents. When shown the word "Tiffany" in materials similar to Costco's point-of-sale signage, nearly 4 out of 10 consumers believed that "Tiffany" was being used as a brand name. Another 3 out of 10 said they thought it was both a brand name and a descriptive word.

To oppose Tiffany's motion, Costco challenged Tiffany's survey methodology. It also proffered the testimony of several experts that "Tiffany" is the sole word in the English language to describe a particular style of ring setting. The experts further opined on the long history of the generic use of "Tiffany" to describe such settings. Costco additionally offered dictionary definitions and expert testimony from a senior consultant to Dictionary.com.

The court held as a matter of law that Costco's sale of rings advertised as "Tiffany" rings satisfied all of the factors giving rise to a likelihood of confusion, especially bad faith. It also rejected Costco's arguments that "Tiffany" is a generic term and that Costco was entitled to claim fair use.

continued on page 2

The court noted that Costco proffered no evidence raising a material issue of fact regarding whether "the primary significance of the Tiffany mark to the relevant public is as a generic descriptor or a brand identifier." The court explained that the "question of 'primary significance' is the key to a determination of genericism." Relying on Tiffany's survey, the court granted summary judgment on Costco's genericness counterclaim.

The court's decision is a good reminder that survey evidence can be extremely helpful in establishing whether a term is perceived as a trademark, a descriptive term, or a generic product category. It can also be helpful in establishing whether trade dress is protectable. Although surveys can be very expensive to conduct and are frequently susceptible to attack on a variety of grounds, they may make the difference between winning and losing trademark and trade dress cases. Had Tiffany conducted a survey before filing its first summary judgment motion on genericness, it might have prevailed the first time, rather than needing to renew its summary judgment motion on that issue.

A WIN FOR KYLE BASS'S HEDGE FUND AS THE PTAB DISMISSES CELGENE'S SANCTIONS MOTIONS

By Cary Miller and Matthew I. Kreeger

The Patent Trial and Appeals Board (PTAB) dismissed Celgene Corporation's ("Celgene") motions for sanctions against the Coalition for Affordable Drugs ("the Coalition").

As we previously reported (here and here), the Coalition is an entity affiliated with a Kyle Bass hedge fund that filed several inter partes review (IPR) petitions against Celgene and other biotech companies. Bass's hedge fund apparently has shorted the shares of those companies, such that it stands to profit if their stock prices drop. The PTAB authorized Celgene to file a motion for sanctions for "abuse of process" against the Coalition.

In its sanctions briefing, Celgene had argued that the Coalition's IPRs were an abuse of the IPR process. It asserted that IPRs were not designed to achieve the "primary purpose" of the Coalition and Mr. Bass's other companies, which is to generate profit through short sales of pharmaceutical stocks after filing IPR petitions. "[I]f the Board permits this strategy to continue," Celgene contended, "it will be inundated with similar petitions." Celgene viewed these types of IPR petitions as "an unwarranted burden on the [PTAB] . . . and on innovators like patent owner Celgene Corporation . . . and its shareholders."

In response, the Coalition countered that profit is "at the heart of nearly every patent and nearly every IPR."

The PTAB dismissed Celgene's motions for sanctions. It stated that "Congress did not limit inter partes reviews to parties having a specific competitive interest in the technology covered by the patents." The PTAB agreed with the Coalition that profit is at the center of "nearly every inter partes review" and stated that having "an economic motive for challenging a patent claim does not itself raise abuse of process issues."

This dismissal of Celgene's sanctions motion means that the IPR proceedings will continue. The PTAB must decide whether to institute the IPR proceedings in October 2015.

PROPOSED AMENDMENTS TO THE IPR PROCESS

Congress is considering amendments to the IPR process. H.R. 9, the Innovation Act of 2015, would preclude institution of IPR petitions unless the petitioner certifies (1) that it does not own a "financial instrument . . . designed to hedge or offset any decrease in market value of an equity security of the patent owner or an affiliate" and (2) that it has not demanded payment from the patent owner or an affiliate in exchange for foregoing filing an IPR, unless the petitioner or any real party in interest has been sued for infringement under the patent at issue. If enacted, this amendment could moot IPR challenges by hedge funds.

VERSATA: THE FEDERAL CIRCUIT EXPLAINS THE PARAMETERS AND APPEALABILITY OF CBM PROCEEDINGS

By Richard S.J. Hung and Barbara N. Barath

On July 9, 2015, the Federal Circuit decided its first appeal of a covered business method (CBM) patent review. In *Versata Development Group Inc. v. SAP America, Inc. et al.*, Case No. 14-1194 (Fed. Cir. July 9, 2015) ("*Versata I*"), the

continued on page 3

court addressed four issues relating to CBM proceedings generally: (1) the scope of judicial review; (2) the definition of a "CBM patent"; (3) the applicable claim construction standard; and (4) whether 35 U.S.C. § 101 arguments are available. The court ultimately affirmed the decision of the Patent Trial and Appeal Board (PTAB) that a product-pricing patent was invalid as claiming only abstract ideas.

In a separate decision issued on July 13, 2015, the Federal Circuit further held that a patentee may not file a lawsuit in federal district court to challenge the PTAB's initial decision to institute CBM review. *Versata Development Group Inc. v. Lee*, Case No. 2014-1145 (Fed. Cir. July 13, 2015) ("*Versata II*").

BACKGROUND

In 2007, Versata Software Inc. sued SAP America, Inc., for allegedly infringing U.S. Patent No. 6,553,350 ("the '350 patent"). After a 2011 trial, a jury found that SAP infringed the '350 patent and awarded Versata $391 million in damages. In May 2013, the Federal Circuit affirmed the jury verdict.

While the initial appeal was pending, SAP petitioned for CBM review of Versata's patent under AIA Section 18. In granting SAP's petition, the PTAB concluded that the '350 patent qualified as a CBM patent and that Section 101 applied during CBM proceedings. In June 2013, the PTAB issued a final written decision, holding the patent invalid under Section 101 as covering only the abstract idea of calculating a product price.

In March 2013, Versata separately sued the U.S. Patent Office (PTO) in the Eastern District of Virginia, seeking to set aside the PTAB's decision to institute. The district court dismissed the case for lack of subject matter jurisdiction and for failure to state a claim. It did so because "the decision to institute post-grant review is merely an initial step in the PTAB's process to resolve the ultimate question of patent validity, not a final agency action." *Versata Dev. Corp. v. Rea*, 959 F. Supp. 2d 912, 915 (E.D. Va. 2013). The court further noted that Congress clearly intended "to preclude subject matter jurisdiction over the PTAB's decision to institute patent reexamination [*sic*] proceedings." *Id.*

Versata appealed both the PTAB's final decision and the district court's decision to the Federal Circuit. The cases were consolidated for argument but decided separately in *Versata I* and *II*, respectively.

THE FEDERAL CIRCUIT'S HOLDINGS REGARDING CBM PROCEEDINGS

In the *Versata I* and *II* cases, the Federal Circuit addressed four key issues relating to CBM proceedings generally.

COMING IN HOT!

We'd like to extend our congratulations to our colleagues on recent awards and recognitions:

- *Best Lawyers* named 18 MoFo IP attorneys as recommended in the areas of Litigation: Intellectual Property, Litigation: Patent, Patent Law, Biotechnology Law, Commercial Litigation and Bet-the-Company Litigation.
- MoFo partners **Rachel Krevans**, **Catherine Polizzi**, and **Mika Mayer** were all included in *The Recorder*'s 2015 list of Women Leaders in Tech Law.

1. Scope of Judicial Review

35 U.S.C. § 324(e) bars the appeal of the PTAB's determination as to whether to "institute" CBM review. Accordingly, a preliminary question on appeal was whether Versata could challenge the PTAB's conclusions that (1) the '350 patent is a CBM patent and (2) Section 101 applies during CBM proceedings. The PTO took the position that, because the determination that the '350 patent is a CBM patent was made at the institution stage, it was immune from judicial review under Section 324(e). SAP argued that the same was true of the PTAB's decision to apply Section 101, which the PTAB also made at the institution stage.

In *Versata II*, the Federal Circuit agreed that Section 324(e) "barr[ed] judicial review of the initial decision to institute." *Versata II* at 5. For this reason, the court affirmed the district court's dismissal of Versata's lawsuit challenging the PTAB's initial decision to institute CBM review.

In *Versata I*, however, the Federal Circuit confirmed that it *can* review the PTAB's *final written decision*, including whether the '350 patent is a CBM patent and whether Section 101 applies during CBM proceedings. This is true even though Section 324(e) precludes appeals of the PTAB's *institution decision*. The court reasoned that it "may review issues decided during the PTAB review process" – "regardless of when they first arose in the process, if they

continued on page 4

are part of or a predicate to the ultimate merits." *Versata I* at 57. Judge Hughes dissented on this point, arguing that the majority was impermissibly expanding the Federal Circuit's jurisdiction and scope of review.

2. Definition of Covered Business Method Patent

Section 18(d)(1) of the AIA defines a CBM patent as one "that claims a method or corresponding apparatus for performing data processing or other operations used in the practice, administration, or management of a financial product or service . . . ." In *Versata I*, the Federal Circuit held that the definition of a CBM patent "is not limited to products and services of only the financial industry, or to patents owned by or directly affecting the activities of financial institutions such as banks and brokerage houses." *Id.* at 35.

The court further wrestled with Section 18(d)'s exception to the definition of a CBM patent. Under Section 18(d), a CBM patent "does not include patents for technological inventions." PTO regulations attempt to clarify that a "technological invention" is one in which the claimed subject matter as a whole (i) "recites a technological feature that is novel and unobvious over the prior art" and (ii) "solves a technical problem using a technical solution." 37 C.F.R. § 42.301(b).

As the court noted, these clarifications are unhelpful. The first requirement is itself "rather obvious, and not novel," and the second requirement "defin[es] a term in terms of itself" in a way that "does not seem to offer much help." *Id.* at 37.

The court ultimately concluded that the '350 patent "does not fall within the exception for technological innovations" – "whatever that exception may otherwise mean." *Id.* at 39. It explained that the claimed invention is "not a technical solution, but more akin to creating organizational management charts." *Id.* Although Versata argued that all claims require the use of a computer, the court emphasized that the "presence of a general purpose computer to facilitate operations through uninventive steps does not change the fundamental character of an invention." *Id.* at 38 (citing *Alice Corp. Pty. Ltd. v. CLS Bank Int'l*, 134 S. Ct. 2347 (2014)).

3. Claim Construction Standard in CBM Proceedings

Noting that the "broadest reasonable interpretation" claim construction standard applies in post-grant proceedings, the Federal Circuit saw "no basis for distinguishing between the two proceedings for purposes of the PTAB's use of BRI in claim construction here." *Id.* at 41. The court commented, however, that it was "less than clear" that the outcome would have changed even under a different claim construction regime. *Id.*

4. Availability of Section 101 in CBM Proceedings

The court affirmed that Section 101 challenges are available in CBM proceedings. *Id.* at 45.

THE FEDERAL CIRCUIT'S DECISION REGARDING VERSATA'S PATENT

While recognizing that each abstract idea case "requires separate analysis," *id.* at 56, the court concluded that the PTAB correctly invalidated Versata's patent as claiming only the abstract idea of determining a price using a computer. The court held that the claims do not improve an existing technological process, as they are directed to improving the performance of price determination – not the performance of a computer. *Id.* at 54.

CONCLUSION

The *Versata* cases together confirm the extensive authority of both the PTAB and the Federal Circuit. *Versata II* confirms that a patentee may not challenge the PTAB's decision to institute CBM proceedings via parallel district court proceedings. After the PTAB has rendered its final written decision, however, the Federal Circuit may review the PTAB's underlying determinations (*e.g.*, whether a patent qualifies as a CBM patent and whether Section 101 is an available ground for invalidity) on appeal of that final decision.

THE EUROPEAN COURT OF JUSTICE ON ENFORCEMENT OF FRAND PATENTS: *HUAWEI V. ZTE*

By Rufus Pichler and Wolfgang Schoenig*

The European Court of Justice (ECJ) rendered its highly anticipated ruling in *Huawei v. ZTE*[1] on the enforcement of standard essential patents (SEPs) which are subject to a FRAND commitment. SEPs play a significant role in the mobile communications sector and patent owners have widely asserted them to try to enjoin their competitors' standard compliant products (in what is often referred to as the "smartphone wars"). With its latest decision, the ECJ requires that a specific process be followed when

continued on page 5

seeking injunctive relief in the EU based on the alleged infringement of FRAND-committed SEPs in order to balance the interests of the patent owner and the implementers of standards.

THE GERMAN PROCEEDINGS

After unsuccessful licensing discussions, Huawei sued ZTE for patent infringement in the Higher Regional Court of Düsseldorf, Germany, seeking injunctive relief and damages. The patent in suit has been declared to ETSI[2] as essential to the LTE standard, and Huawei committed to ETSI to license the patent on FRAND terms[3] to any third party in accordance with ETSI's policies.

The Düsseldorf Court was confronted with conflicting German precedent, on the one hand, and evolving EU legal standards, on the other hand, on when it is proper for an owner of a FRAND-committed SEP to seek injunctive relief against a potential infringer.

In its leading *Orange Book* decision[4], the German Federal Court of Justice (BGH) held that seeking injunctive relief under SEPs against a potential infringer amounts to an anticompetitive abuse of the SEP holder's dominant position only under very narrow circumstances. It placed the burden on the alleged infringer to take specific steps in order to avoid an injunction. Specifically, under the *Orange Book* standard:

- The alleged infringer must make an unconditional and binding offer to license the patent;
- The offer may, specifically, not be subject to the condition that the patent is, in fact, found to be infringed by the alleged infringer's actions.
- The alleged infringer must account for all past and ongoing acts practicing the patent at issue and pay to the patent owner or into escrow all sums that would be owed under the license agreement on account of such use.
- If the amount of a reasonable license fee is disputed, the alleged infringer must offer to pay a license fee to be determined by the patent owner in its reasonable discretion (which is subject to court review).

The European Commission took a markedly different approach in its antitrust decisions in *Samsung v. Apple* and *Motorola v. Microsoft*.[5] Both decisions suggest a much lower threshold for finding an abuse of a dominant position under EU law[6] where holders of FRAND-committed SEPs are seeking injunctive relief against potential infringers. In *Samsung*, the Commission indicated that the "willingness" of the potential infringer to negotiate a license will render it unlawful for the patentee to pursue an injunction. Samsung's commitments to the Commission to avoid a fine indicate that the Commission considers a prospective licensee to be "willing" where it commits to a negotiation period of up to 12 months and, if no agreement is reached, to a binding third-party determination of FRAND terms.

Similarly, in *Motorola*, the Commission found that Motorola abused its dominant position by insisting, among other things, on certain anticompetitive licensing terms, including a requirement to make payments for SEPs that may not actually be infringed; prohibiting the licensee from challenging the licensor's patents or providing for a termination right upon challenge; and insisting on a reciprocal cross-license.

The Düsseldorf Court found that, when applied to the instant case, the BGH's *Orange Book* standard and the Commission's approach in *Samsung* and *Motorola* would lead to opposite results. The Court stayed the proceedings and referred several questions to the ECJ, all focusing on when seeking an injunction under SEPs which are subject to a FRAND commitment is improper and constitutes an abuse of a dominant position.

THE ECJ'S DECISION

The ECJ held that seeking an injunction against an alleged infringer of a FRAND-committed SEP is an abuse of the patent owner's dominant position where the SEP holder fails to comply with certain requirements before initiating the action. The specific requirements and sequence are as follows:

- Before bringing an action, the SEP holder must alert the alleged infringer of the infringement by designating the SEP in question and specifying the way in which it has been infringed.
- If the alleged infringer expresses a willingness to take a license, the SEP holder must provide a written licensing offer on FRAND terms, specifying, in particular, the royalty and how it is to be calculated.
- Only if the alleged infringer continues to use the SEPs in question and fails to respond diligently to the SEP holder's offer in accordance with recognized commercial practices in the field and in good faith (and in particular without delaying tactics) may the SEP holder seek an injunction.

The Court emphasized that the exercise of an intellectual property right does not in and of itself constitute an abuse of a dominant position, but can be abusive under "exceptional circumstances." The Court found these exceptional circumstances in the standard-essentiality of the patent at issue, including the fact that competitors do not have the option of avoiding the patent with respect to

continued on page 6

standard-compliant products, and in the patentee's FRAND commitment, which "creates legitimate expectations on the part of third parties that the proprietor of the SEP will in fact grant licenses on such terms."

With respect to the notice requirement, the Court agreed with the Advocate General's observation that, given the large number of SEPs (here 4700), it cannot always be assumed that the alleged infringer is aware of its use of the SEP.[7] Moreover, given the SEP holder's FRAND commitment, the burden should be on the SEP to provide a specific licensing offer to the alleged infringer. In this regard, the Court emphasized that the SEP holder, in the absence of a standard license agreement or a publicly accessible prior agreement with another competitor, is in a better position to propose non-discriminatory licensing terms.

If the alleged infringer does not accept the SEP holder's licensing offer, an abuse of dominant position defense is available only, if the alleged infringer has promptly submitted a written counter offer on FRAND terms. If the counter offer is rejected, the alleged infringer must also provide appropriate security with respect to its past and continued use until an agreement is concluded, *e.g.*, by providing a bank guaranty or paying amounts into escrow.

If the parties continue to fail to agree on what terms constitute FRAND terms, the Court indicated that the parties may, by common agreement, request that the amount of the royalty be determined by an independent third party.

The Court provided little substantive guidance on what terms would or would not meet the FRAND requirement, except for the important clarification that the alleged infringer must remain free to challenge, during the negotiations and in the future, the validity and the essential nature of the SEPs at issue as well as the alleged infringer's actual use of the SEPs.

IMPLICATIONS AND OPEN QUESTIONS

The ECJ chose a middle ground between the *Orange Book* standard established by the BGH and the Commission's position in *Samsung*. While seeking to establish a process that limits room for stalling and delay tactics by the alleged infringer, overall the approach favors the alleged infringer, when compared to the *Orange Book* approach, by shifting the burden of making the first FRAND offer to the SEP holder and leaving the option open for the alleged infringer to challenge the validity, essentiality, and infringement of the SEP during and after the licensing discussions. It will presumably be much more difficult now, especially in Germany, to obtain injunctions under FRAND-committed SEPs.

No Guidance on FRAND Royalty

Many important issues remain open, however. Most importantly, the Court provided little substantive guidance on when licensing terms are FRAND, and no guidance at all with respect to the setting or reasonableness of FRAND rates.

Several U.S. courts have discussed FRAND rate-setting issues over the last couple of years, including the district court decisions in *Microsoft v. Motorola* (appeal currently being heard in the 9th Circuit),[8] *In re Innovatio IP Ventures*,[9] *Realtek Semiconductor v. LSI*,[10] *CSIRO v. Cisco*,[11] and the Federal Circuit's decision in *Ericsson v. D-Link*.[12]

The U.S. approach is still evolving. Courts have considered various (and sometimes different) factors, including that a "reasonable" royalty should (1) be consistent with the relevant "SSO's goal of promoting widespread adoption of their standards"[13]; (2) "mitigate the risk of patent hold-up"[14]; (3) "address the risk of royalty stacking"[15]; (4) ensure that "holders of valuable intellectual property will receive reasonable royalties on that property,"[16] such that innovators "have an appropriate incentive to invest in future development and to contribute their inventions to the standard-setting process"[17]; and (5) "be based on the incremental value of the invention, not the value of the standard as a whole or any increased value the patented feature gains from its inclusion in the standard."[18] The Federal Circuit, however, has declined to endorse any one set of factors that should be used for all FRAND-encumbered patents.[19] Although the Federal Circuit recognized that "SEPs pose two potential problems that could inhibit widespread adoption of the standard: patent hold-up and royalty stacking,"[20] it held that, in order for these potential problems to be considered as part of a FRAND damages analysis, the accused infringer must present "actual evidence of hold-up or stacking," stating that "[c]ertainly something more than a general argument that these phenomena are possibilities is necessary.[21] The Federal Circuit did reiterate, however, that apportionment is often required with respect to the royalty base, holding that unless the "entire value of a machine as a marketable article is 'properly and legally attributable to the patented feature,' courts must insist on a more realistic starting point for the royalty calculations by juries—often, the smallest salable unit and, at times, even less."[22]

No such guidance exists in Germany or elsewhere in the EU. The Mannheim District Court was asked to set the FRAND rate in a dispute between Motorola and Apple.[23] In the course of those proceedings, the Mannheim court asked the Commission for its opinion on a number of questions concerning the application of EU competition rules relevant to the setting of FRAND rates, and requested the Commission's opinion with respect to the exact method it should employ to set the FRAND royalty rate in compliance with EU competition law.[24] The specific questions that the court posed are not public, but in *Motorola* the Commission quotes one of the questions: "Is it sufficient to comply with the FRAND industry standard in view of Article 102 TFEU that the

continued on page 7

fact that usually a number of patents of a portfolio are not valid or upon review turn out to be non-essential is taken into account by other means than a judicial review of each and every patent, for instance through sampling and/or general reduction as regards the royalties or something similar?"[25] As it stands, no response by the Commission to any of the questions has been published, and the Mannheim proceeding was settled and dismissed following the Commission's *Motorola* decision.

Whether a licensing offer or counter offer was consistent with FRAND terms, including with respect to the royalty base and royalty rate, is going to be a crucial question when applying the ECJ's *Huawei* rules. This issue will remain one for national courts to resolve on a case-by-case basis.

Other Open Questions

Other open questions that national courts will need to address over time include the following:

- What are the guidelines for determining whether the alleged infringer has "diligently responded to [the initial FRAND offer], in accordance with recognised commercial practices in the field and in good faith"? The ECJ's guidance on this point is vague, stating only that "this [is] a matter which must be established on the basis of objective factors and which implies, in particular, that there are no delaying tactics."
- Whether it is mandatory for the alleged infringer to provide "appropriate security" if the counter offer has been rejected, and whether appropriateness should be determined based on the SEP holder's initial offer, the alleged infringer's counter-offer, or on some other standard, in order to avoid an injunction?
- Whether a party can unilaterally satisfy the requirements for a FRAND offer by deferring the determination of the FRAND rate (and possibly other terms) to an independent third party. The ECJ suggests that this is a possible path to resolution if the parties so request "by common agreement."
- Whether injunction proceedings are to be stayed pending any resolution (by an independent third party or by the court) of the parties' disagreement as to what is FRAND.

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* Robert Grohmann provided valuable assistance in the preparation of this client alert.

1 European Court of Justice, judgement of 16 July 2015, case no. C-170/13 – *Huawei*.

2 The European Telecommunications Standard Institute.

3 Fair, reasonable, and non-discriminatory.

4 German Federal Court of Justice, judgment of 6 May 2009, case no. KZR 39/06 – *Orange Book*.

5 European Commission, case no. AT. 39939 – Samsung v. Apple; European Commission, case no. AT. 39985 – *Motorola v. Microsoft*.

6 Article 102 of the Treaty on the Functioning of the European Union (TFEU).

7 Advocate General, opinion of 20 November 2014, case no. C-170/13 – *Huawei*.

8 2013 WL 2111217 (D. Wash. 2013).

9 2013 WL 5593609 (N.D. Ill. 2013).

10 2014 U.S. Dist. LEXIS 81673 (N.D. Cal. 2014).

11 2014 U.S. Dist. LEXIS 107612 (E.D. Tex. July 23, 2014).

12 773 F.3d 1201 (Fed. Cir. 2014).

13 *Microsoft*, 2013 WL 2111217 at *12 (involving ITU, ISO/IEC, and IEEE policies).

14 *Id.; see also Innovatio*, 2013 WL 5593609 at *9 (involving IEEE policy and stating "one of the primary purposes of the RAND commitment is to avoid patent hold-up"); *Ericsson*, 773 F.3d at 1234.

15 *Microsoft*, 2013 WL 2111217 at *12; Innovatio, 2013 WL 5593609 at *9; Ericsson, 773 F.3d at 1234.

16 *Microsoft*, 2013 WL 2111217 at *12.

17 *Innovatio*, 2013 WL 5593609 at *9.

18 *Ericsson*, 773 F.3d at 1235; *Microsoft*, 2013 WL 2111217 at *12 ("a reasonable royalty on the economic value of its patented technology itself, apart from the value associated with incorporation of the patented technology into the standard").

19 *Ericsson*, 773 F.3d 1201.

20 *Id.* at 1209.

21 *Id.* at 1234.

22 *Id.* at 1227. *See also VirnetX, Inc. v. Cisco Sys.*, 767 F.3d 1308, 1327 (Fed. Cir. 2014) ("Where the smallest salable unit is, in fact, a multi-component product containing several non-infringing features with no relation to the patented feature …, the patentee must do more to estimate what portion of the value of that product is attributable to the patented technology.").

23 LG Mannheim, case no. 7 O 122/11 – *Motorola v. Apple*. The European Commission, case no. AT. 39985 – *Motorola v. Microsoft*, at (167) et. seq., provides a detailed summary of the initial stages of the rate-setting proceeding.

24 European Commission, case no. AT. 39985 – *Motorola v. Microsoft* at (174).

25 European Commission, case no. AT. 39985 – *Motorola v. Microsoft* at (302).

CHINA'S SAIC ISSUES COMPETITION RULES REGULATING ABUSE OF INTELLECTUAL PROPERTY RIGHTS

By Sherry Yin and Lei Ouyang

On April 7, 2015, China's State Administration of Industry and Commerce of the PRC (SAIC) issued the long-anticipated *Provisions on the Prohibition of the Abuse of Intellectual Property Rights to Eliminate or Restrain Competition* (关于禁止滥用知识产权排除、限制竞争行为的规定; the "IP Guideline"), which will come into effect on August 1, 2015. The IP Guideline marks the end of a six-year-long legislative process for the SAIC that began in 2009

continued on page 8

and for the first time, specifically addresses issues with respect to intellectual property rights (IPR) in China's competition law area.

Among other things, the IP Guideline restricts horizontal and vertical monopolistic agreements relating to IPR, requires IPR owners with market dominance to license their patents under the "essential facility" doctrine, regulates conduct during standard setting processes, and prohibits patent pool members from undertaking certain activities.

SCOPE OF APPLICATION

The IP Guideline addresses two categories of IPR-related anticompetitive conduct: monopolistic agreements and abuse of market dominance. The IP Guideline expressly indicates that it will not apply to any price-related monopolistic conduct, which is under the jurisdiction of China's National Development and Reform Commission of the PRC (NDRC). Accordingly, issues related to charging excessive licensing fees by licensors will still be handled by the NDRC.

PROHIBITION AGAINST MONOPOLISTIC AGREEMENTS

The IP Guideline prohibits operators from entering into horizontal and vertical monopolistic agreements when exercising their IPRs. Such prohibition is twinned with a safe-harbor provision. Such safe-harbor provision:

- permits a horizontal agreement, if either the aggregate market share of the operators concerned is no more than 20 percent or at least four substitutable technologies with reasonable costs in the same relevant market are available; and
- permits a vertical agreement, if either the respective market share of each operator concerned is no more than 30 percent or at least two substitutable technologies with reasonable costs in the respective upstream or downstream relevant market are available,

in each case, so long as evidence does not show that the agreement has the effect of eliminating or restricting competition.

Interestingly, the IP Guideline is silent on whether agreements falling outside of the safe harbor provisions are "*per se*" illegal under China's Anti-Monopoly Law (the AML) or whether they might be defensible following a "rule of reason" analysis. Therefore, how the SAIC will exercise its enforcement authority in respect of IPR-related monopolistic agreements in practice remains to be seen.

PROHIBITION AGAINST THE ABUSE OF DOMINANCE

Overview

The IP Guideline includes more detailed guidance in regard to the abuse of dominance by operators when exercising IPRs, addressing practices such as forcible bundling, restrictive trading, refusal to license IPRs that constitute an essential facility, imposition of unreasonable restrictive conditions, and differentiated treatment towards counterparties with the same conditions.

It is worth noting that several prohibitions specified in the IP Guideline seem to mirror practices of Qualcomm that were recently penalized by the NDRC, such as requiring an exclusive cross-license of improvements, prohibiting licensees from questioning patents' validity, and restricting licensees' right to utilize expired IPRs. This may indicate more integrated interagency coordination among the three Chinese competition authorities than has been seen before.

Essential Facility Doctrine

Despite some objections, the SAIC introduced a tough compulsory licensing requirement on essential facilities that requires patent owners with market dominance to mandatorily license their IPR when the underlying IP constitutes an "essential facility," also known as *de facto* SEP (as defined below). Factors that suggest that IP does constitute an "essential facility" include:

(i) if the underlying IPR has no reasonable replacement and is essential for other operators to compete in the relevant market;

(ii) if refusal to license could have an adverse impact on competition and innovation and could impair consumers' welfare and the public interest; and

(iii) if licensing such IPR would not cause an unreasonable damage to the licensor.

Although the SAIC stated that the application of "essential facility" doctrine will require strict conditions in order to strike a balance between encouraging innovation and protecting competition, the broad language will raise tremendous uncertainties in practice. For example, criteria for determining whether the compulsory licensing would cause "an unreasonable damage to the licensor" remain unclear. This will likely pose a threat to multinational corporations in patent-heavy sectors, such as the IT and pharmaceutical sectors. Coupled

continued on page 9

with the SAIC's ongoing investigation against Microsoft, the NDRC's recent penalty against Qualcomm and its suspended investigation against InterDigital, issuance of the IP Guideline is a clear sign of heightened scrutiny of antitrust enforcement in China's IP field.

Standard Setting

The IP Guideline addresses anticompetitive issues during the standard setting process and prohibits a dominant operator from the following: (a) deliberately not disclosing its patent information to standard setting organizations during the standard setting process, or explicitly waiving its right during the standard setting process, but claiming its patent rights afterwards;

(b) after its patent becomes a standard essential patent (SEP), carrying out refusal to license, tying, and imposing other unreasonable trading conditions in violation of the fair, reasonable and non-discriminatory principle, also known as the FRAND principle.

PROHIBITION ASSOCIATED WITH PATENT POOLS

The IP Guideline defines a "patent pool" as an agreement arrangement under which two or more patentees jointly license the patents they own to a third party in a certain manner, such as through establishing a special joint venture for this purpose and through entrusting a member of a patent pool or an independent third party to administrate. It regulates the activities of patent pools' members by prohibiting them from exchanging sensitive information and reaching monopolistic agreements. The IP Guideline also prohibits members of patent pools in a dominant market position from abusing their dominance. The IP Guideline provides a list of abusive behaviors, including, but not limited to, restricting patent pools' members from licensing their patents to parties outside of the patent pools, imposing an exclusive cross-license of improvements, restricting patent pools' members or licensees from developing competing technologies, and forbidding licensees from challenging patents' validity. Further, it grants the SAIC the authority to exercise its discretion to determine any other types of abuse by patent pools.

Although patent pools have not been popular in China, they have been widely adopted in Western countries for years. With the reality that China is a large technology import country, the IP Guideline will likely target foreign owners of patent pools at least in the near future.

PENALTIES

Consistent with the AML and rules issued by the NDRC, the IP Guideline appears to grant the SAIC a large degree of discretion to determine penalties, which include monetary

continued on page 10

fines within a range from 1 percent to 10 percent of violators' annual sales in the previous year, orders to stop the illegal act, and confiscation of the illegal income. Again, it does not specify whether the sales refer to those in China or globally.

UNRESOLVED ISSUES

Certain important issues in the IP Guideline remain unclear. For example, the "essential facility" doctrine requires further clarification on its scope of application to avoid being misused. In addition, it remains to be seen how the SAIC will tackle the use of injunctions by dominant operators. For its part, the NDRC has so far focused its enforcement efforts on companies that seek to impose injunctions against willing licensees of SEPs.

WHERE TO FIND US

- **October 10, 2015**
  Chinese BioScience Association, Foster City, CA – **Janet Xiao**
- **October 13, 2015**
  Kairos Global Summit, Burbank, CA – **Michael O'Donnell**
- **November 11, 2015**
  Practising Law Institute: Trial By Jury 2015, New York, NY – **Michael Jacobs**