

## Ruling In FTC's Qualcomm Case Could Upend SEP Licensing

By **Matthew Perlman**

*Law360 (May 22, 2019, 11:17 PM EDT)* -- A California federal judge dealt Qualcomm a huge blow Tuesday by ruling that its model for licensing cellular modem chips is illegal, issuing a strongly worded opinion that dampens prospects for a likely appeal and could lead other players in the cellular industry to revisit their licensing practices.

The Federal Trade Commission, which challenged Qualcomm's licensing practices, scored a big win with the ruling, as U.S. District Judge Lucy Koh found that Qualcomm's licensing scheme for standard-essential patents covering cellular technology violated the Sherman Act.

The agency targeted the company's policies of not licensing to rival chip manufacturers and of requiring phone makers to purchase licenses separately from the chips themselves, which the FTC said allowed it to wrench exorbitant royalty rates for its SEPs.

The FTC also took aim at the methods Qualcomm used to reinforce its scheme, including rebates for phone makers that agreed to exclusivity and penalties for those that didn't.

The lengthy opinion focused heavily on business documents produced by Qualcomm that Judge Koh found showed that the goal of the company's licensing practices was to hurt competition. While Qualcomm staked its defense largely on testimony from its executives, the judge said the documents contradicted their statements in nearly every instance.

She also compared the responses executives gave while being questioned by Qualcomm's attorneys, when they had to be asked on several occasions to slow down, to their answers to the FTC on cross-examination, when they were "very reluctant and slow to answer."

"Therefore, the court largely discounts Qualcomm's trial testimony prepared specifically for this litigation and instead relies on these witnesses' own contemporaneous emails, handwritten notes, and recorded statements to the IRS," the opinion said.

### Appeal Faces Uphill Battle

David Reichenberg, an antitrust litigator with Cozen O'Connor, told Law360 that courts frequently make determinations about the credibility of witnesses, but that what was surprising about the Qualcomm case was Judge Koh's "across-the-board rejection of any degree of credibility or merit to any Qualcomm

witness."

"The testimony on the [FTC] side was almost universally credited," Reichenberg said.

Experts say these types of credibility findings are generally given a lot of weight by appellate courts since the trial judge was in the courtroom and had the opportunity to assess things such as a witness' demeanor. Qualcomm has vowed to appeal Judge Koh's ruling, and while it remains to be seen what issues the company will attack, it could face an uphill battle.

"The more credibility determinations you make at the trial level, the more protected you are in your analysis," Reichenberg said of the judge's ruling.

With the witness testimony largely negated by the district court's findings, Constantine Cannon partner Ankur Kapoor told Law360 an appeal will have to rely on the expert evidence that Qualcomm has produced to try and show the conduct did not have an impact on the competitive process.

But considering Judge Koh's damning view of the business documents, that could be difficult, too, he said. "The findings on the documents are quite strong, and if the expert testimony is equivocal, or there's a tie, then the documents are going to carry the day," Kapoor said.

In addition to its planned appeal, Qualcomm said it intends to seek an immediate stay of the injunction requiring it to renegotiate many of its existing license agreements.

Judge Koh noted in the opinion that it "made little sense" for the court to leave the licenses in place after finding they're the product of anti-competitive conduct. George A. Hay, a professor of law and economics at Cornell University Law School, told Law360 the company may start reevaluating its existing licenses anyway, while it pursues its other options.

"Since she has ruled that what they're doing is illegal, and is ongoing, that would mean damages are accruing," Hay said, noting that the ruling also gives Qualcomm's customers a fair amount of leverage. "One could imagine that Qualcomm might say, 'Well, I'm not sure we're going to win on this on appeal, maybe we better simply limit our loses.'"

### **Implications for Other Players**

The Qualcomm case has been closely watched because it deals with conflicts between antitrust policy and intellectual property rights, namely what lengths owners of critical IP must go in order to fulfill their duty to make sure others can license their technology. Since Qualcomm's patents have been included in industry standards — helping technology operate across equipment made by various manufacturers — the company has an obligation to license its SEPs on fair, reasonable and nondiscriminatory, or FRAND, terms.

But courts have not yet seen the breach of these obligations, or the alleged breach, as an antitrust problem in itself. Many, including the head of the U.S. Department of Justice's Antitrust Division, believe the issue is more of a contract dispute than anything else.

While Judge Koh's ruling doesn't specifically find that a FRAND breach alone constitutes an antitrust violation, Kapoor said the opinion brings the issues together. This means other companies that own SEPs should be reviewing their licensing models to make sure they don't run into any problems.

"This is the first case to have held breach of FRAND obligations to form the basis, along with other things, of Sherman Act violations," he said. "I think holders of standard-essential patents have to look very carefully at their licensing practices to see whether those practices somehow exclude competition, significantly or not."

On a summary judgment motion earlier in the case, Judge Koh ruled that Qualcomm had breached its commitments to two standard-setting organizations by refusing to license its SEPs to rival chip makers. But her opinion on the merits of the case didn't go any further, which Lisa Kimmel, a senior counsel in Crowell & Moring LLP's antitrust group, told Law360 suggests the ruling may not have much of an impact industrywide.

"She did not come out and say anything about any other specific [standard development organization] policies, and I think that's an important takeaway for this case," Kimmel said.

Kimmel also said that the judge's opinion does not rely on those FRAND breaches as the primary reason for finding an antitrust violation. Instead, she said, it focused more on "garden variety" antitrust problems, such as exclusive dealing and rebate policies for its chips.

"I think she always tied it back to that," Kimmel said. "Nowhere did she say that a breach that just led to a higher price was the basis for the antitrust findings."

Apple had been embroiled in a tangle of litigation with Qualcomm over its licensing practices until the sides reached a settlement last month. The agreement ended patent disputes in the U.S. and abroad as well as an antitrust case brought by Apple in California. While Qualcomm later said the deal was worth at least \$4.5 billion in licensing fees, details have not been disclosed.

This means it remains unclear if that licensing agreement conforms with the injunction ordered by Judge Koh. The order also calls for a monitor to ensure Qualcomm's compliance with the injunction, and that monitor could be tasked with reviewing the deal.

But Hay said the companies both knew that there was a possibility that the FTC could prevail in its case, and likely structured the deal with that in mind.

"The settlement was negotiated in the shadow of this case," he said.

### **Implications for the DOJ**

Another remaining issue is the DOJ Antitrust Division's role in the case. The agency filed a statement of interest in early May asking the court to take input and hold a hearing before ordering any remedies if Qualcomm was found liable. The division said it was concerned that an "overly broad remedy" could harm the cellular market, including by impacting the development of 5G, the next-generation cellular standard.

In her opinion Tuesday, Judge Koh dispatched with those concerns, saying that the case already included testimony and evidence about the "feasibility of requiring Qualcomm to license its SEPs to rival modem chip suppliers, and on other issues related to the scope or nature of the remedy."

The DOJ's antitrust chief, Makan Delrahim, has been an advocate for the rights of patent holders in the

standard-setting process since taking over the helm of the division, saying on several occasions that the concerns should be focused on the implementers of the standards — the licensees — rather than the patent owners.

But the agency's statement of interest in the Qualcomm case didn't attack the company's alleged liability; it focused only on the court's remedy. Reichenberg also noted that the ruling does not find that the FRAND breach alone was an antitrust violation, just that it was a part of a broader anti-competitive scheme.

Hay said the DOJ's bid to intervene could have politics behind it since the Trump administration has made 5G development in the U.S. a priority and wants to ensure that an American company such as Qualcomm holds on to its market-leading position.

"There's an element of a national champion about this," he said, adding that the DOJ's stance also makes it difficult to discern when and to what extent it might weigh in on Qualcomm's appeal.

"Nothing they've said so far says that the FTC was wrong on liability," Hay said. "So, at what point are they going to weigh in?"

The case is *FTC v. Qualcomm Inc.*, case number 5:17-cv-00220, in the U.S. District Court for the Northern District of California.

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