What To Expect From An Appeal Of FTC V. Qualcomm

By **Kevin Post, Steven Pepe and Samuel Brenner** (June 5, 2019)

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On May 21, 2019, Judge Lucy Koh of the U.S. District Court for the Northern District of California issued a detailed, 233-page opinion in a closely watched case between the Federal Trade Commission and Qualcomm, one of the largest cellular chip suppliers in the world.[1]

As part of her order, Judge Koh issued a sweeping injunction that has the potential to affect dramatically the shape of the chip marketplace, as well as the licensing of large numbers of standard-essential patents owned by numerous third parties. For example, among other things, Judge Koh ordered that Qualcomm must abandon its "no license, no chips" policy and must renegotiate license terms with customers in good faith and without threats or discriminatory provisions.[2] Judge Koh also ordered that Qualcomm must make exhaustive SEP licenses available to modem-chip suppliers on fair, reasonable and nondiscriminatory terms.

Judge Koh's decision quickly generated extensive commentary, including a May 28, 2019, op-ed in The Wall Street Journal in which Christine Wilson, an FTC commissioner appointed by President Donald Trump, criticized the ruling as "both bad law and bad policy."[3]

Following the ruling, Qualcomm immediately vowed it would appeal, and on May 28, 2019, Qualcomm filed a motion seeking to stay Judge Koh's order pending that appeal.[4] In its motion, Qualcomm argued that complying with the injunction would fundamentally change how Qualcomm conducts business in a way that could not be easily reversed should the U.S. Court of Appeals for the Ninth Circuit overturn — even in part — Judge Koh's decision.

As the sweeping scope of Judge Koh's order and Qualcomm's stay motion make clear, any appeal will likely raise a number of interesting and potentially novel legal issues at the very intersection of antitrust and SEP/FRAND licensing. Some of these — such as whether the FTC's "tax" theory of antitrust is viable[5] — will likely be largely relegated to the area of antitrust.

But given the underlying facts of this case and Qualcomm's business model, however, other appellate issues will be particularly relevant to (and have a significant impact on) those most interested in SEP licensing and the question of what constitutes a FRAND licensing rate. Among such issues are both the scope of the injunction and whether Qualcomm has an antitrust duty to license its SEPs to rival upstream chip makers, rather than licensing only end-user products, like cell phones.

Notably, the key appellate issues could change depending upon whether Judge Koh, or the Ninth Circuit, agrees to stay any part of Judge Koh's order pending completion of the appeal. Should this injunction go into force, Qualcomm will need to enter new contracts that would be extremely difficult, if not impossible, to unwind should Judge Koh's order be overturned. (Though Qualcomm might try to build in escape clauses in new contracts in the event of an appellate victory, any such escape clauses might themselves might be viewed

as discriminatory, and thus as violating the injunction.)

The contracts Qualcomm is required to negotiate pursuant to the injunction would perhaps preclude Qualcomm from obtaining the same license rates in the future that it has thus far received for its SEP portfolio, might change what a FRAND rate is for Qualcomm's SEPs (and all SEPs related to, for example, 3G, 4G and 5G technology), and would almost certainly mean that Qualcomm's revenue from licensing would drop significantly.

Assuming that denial of a stay does not essentially moot this issue, one of the most important questions that will be addressed by the Ninth Circuit, at least from the perspective of those interested in using Qualcomm chips, is whether the injunction Judge Koh ordered was impermissibly broad, especially given the evidence proffered at trial. (That appears to be at least Commissioner Wilson's view, though she leaves it ambiguous whether she is suggesting that the injunction is wrong as a legal matter, or merely represents bad public policy.) Regardless, Judge Koh's injunction will have a significant and long-standing effect on Qualcomm, and will even subject Qualcomm to FTC monitoring for seven years.

Qualcomm suggests in its motion that it was improper for Judge Koh to issue an injunction at all in the absence of post-2018 evidence of market conditions, particularly given that Qualcomm's post-March 2018 licensing negotiations constitute "virtually the entirety of Qualcomm's new 5G SEP-only licensing program."[6]

Qualcomm also maintains that an injunction is inappropriate unless the FTC satisfies the factors required for a permanent injunction under eBay Inc. v. MercExchange LLC.[7] Qualcomm might argue on appeal that, in light of these issues with the record evidence, the sweeping scope of the injunction is not appropriate. One potential problem with such an argument is that, in order to prevail, Qualcomm may need to undermine the substantive judgment (and not just the remedy) as well.

A second important appellate issue from the perspective of those interested in SEP licensing and FRAND determinations — as well as any companies interested in manufacturing products that comply with 3G, 4G and 5G standards — is whether Qualcomm in fact has an antitrust duty to license its SEPs to rival chipmakers in the first place.

In her order, Judge Koh relied in part on Aspen Skiing Co. v. Aspen Highland Skiing Corp.,[8] in finding that Qualcomm had a "duty to deal" with its chip-maker competitors.[9] In that case, Judge Koh observed, there was "sufficient evidence to show that the defendant had refused to deal with the plaintiff only because of the defendant's anticompetitive intent to maintain its monopoly."[10]

Judge Koh then addressed those factors relevant in Aspen, concluding in part that Qualcomm had terminated a "voluntary and profitable course of dealing" (its standard licensing program) and was refusing to license rivals to its SEP portfolio "out of anticompetitive malice."[11]

Both Qualcomm and Commissioner Wilson have criticized Aspen, at least as applied to antitrust issues broadly, and the Ninth Circuit has signaled that courts should be cautious in concluding that companies have a "duty to deal" with their rivals. That said, Aspen was crafted in a context that did not involve SEPs, which — because they are essential — imbue the patent holder with significant market power.

In other words, while there is an argument that the "duty to deal" should be applied with particular caution by courts, the FTC will be able to argue that the duty to deal is especially

important when a company is licensing, or refusing to license, patents that it itself holds out as essential to critical technical standards.

These are not the only possible appellate issues that relate to the intersection of antitrust and SEP licensing/FRAND issues, and that have the potential to affect how SEP-holders and manufacturers craft and address FRAND offers in the future. As another example, at trial, in addressing what would be an appropriate royalty rate, Qualcomm used the entire handset device as the royalty base. In her order, Judge Koh concluded that this approach was inconsistent with Federal Circuit law concerning apportionment and the smallest saleable patent practicing unit.[10]

While that case law would likely govern were this appeal to go to the Federal Circuit, given that this appeal will instead go to the Ninth Circuit, even though it concerns SEPs, it is possible that this case could then lead to a circuit split on the appropriate method of determining cellular royalties in the FRAND context.

Although the trial phase of this dispute is winding down, the appellate phase has the potential to affect lasting change in the licensing of SEPs, particularly in the cellular space. But what is clear even now is that Judge Koh's order sets up a potential vehicle for raising and addressing issues that will significantly impact FRAND and SEP licensing approaches and litigation in a wide varieties of industries, including the internet of things.

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[1] See FTC v. Qualcomm Inc., No. 17-CV-00220-LHK, slip op. (N.D. Cal. May 21, 2019) ("Order").

[2] See Order at 227-29.

[3] Christine Wilson, "A Court's Dangerous Antitrust Overreach," Wall Street Journal, May 28, 2019.

[4] FTC v. Qualcomm Inc., No. 17-CV-00220-LHK, Dkt. No. 1495 (May 28, 2019) ("Mot.").

[5] See Mot. at 14-15.

[6] Mot. at 11-12.

[7] eBay Inc. v. MercExchange LLC, 547 U.S. 388 (2006)

[8] Aspen Skiing Co. v. Aspen Highland Skiing Corp., 472 U.S. 585 (1985)

[9] Order at 135-40.

[10] Order at 135.

[11] Order at 137-38.

[12] See Order at 172-73.