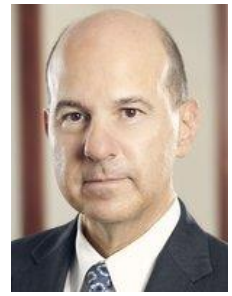
US Should Learn From German Courts Balancing SEP Rights

By **David Kappos and Daniel Etcovitch** (March 9, 2021)



David Kappos

Daniel Etcovitch

In a recent decision involving standard-essential patents, the German Federal Court of Justice, or FCJ, set a productive tone in balancing the rights of patentees and implementers in SEP disputes.

In the November Sisvel International SA v. Haier Deutschland GmbH decision,[1] the FCJ explicitly considered what obligations the parties have in fraught negotiations over FRAND licenses in the SEP context, giving clarity and guidance to parties going forward.

The FCJ demonstrates a refreshingly pragmatic understanding of the same motivations evident to every New York merchant: The hot dog sellers always want the mustard to be free.

Restated in the more staid terms of patent licensing: SEP implementers will find every possible reason to delay or avoid paying for access to innovators' creative output, absent rules that motivate real dialog. If, as a matter of policy, we attach no consequences to delay, it's just good business sense for them to take without paying for as long as possible.

We American capitalists should have picked this up about a decade ago, but, instead, we have spent years questioning the motives of the innovators, only recently coming to appreciate the precarious fate of innovators who pour resources into risky research and development, then contribute it to a standard, hoping to someday be compensated if the technology is adopted and the standard proves successful, only to find out after running that gauntlet that implementers will happily walk off with the goods under their arms and refuse to pay until and unless they are taken to court.

The German approach to disputes over standard-essential patents licensed on fair, reasonable and nondiscriminatory terms starts with the baseline FCJ finding that a court should assess whether the patentee abused a dominant market position, and, if so, the implementer has grounds to avoid significant liability for infringement. This is fair and pragmatic as always; one who seeks equity must practice equity.

In this case, the FCJ importantly recognized a key component of FRAND negotiations: An SEP owner, unlike patentees in most other contexts, cannot completely block access to the patent, by virtue of its FRAND obligation. This means that an SEP owner's only effective method to prevent recalcitrant implementers from illicitly using its patent is by requesting an injunction from a court.

As the FCJ recognized, ignoring that important distinction when evaluating whether a patentee has abused a dominant market position by suing for an injunction would create a market distortion, giving implementers an unfair advantage over competitors who actually negotiated and paid for a license. A patentee's agreement to a FRAND commitment does not change the fundamental fact that implementers must negotiate and pay for a license to use the SEP.

Next, the FCJ provided explicit analysis of the conduct required of each party in negotiations for FRAND terms. For a patentee to qualify for the safe harbor laid out in the Court of Justice of the European Union's 2015 Huawei Technologies Co. v. ZTE Corp. decision, the patentee must notify the implementer of the patents existence and the requirement to license.

From there, the implementer has an affirmative duty to show, clearly and unambiguously, that it is willing to negotiate a license, and that behavior must be exhibited throughout the entire negotiation process. For both the patentee and the implementer, the standard is fundamentally about behavior: Both parties must, at all times, be constructively engaged with one another.

The FCJ recognizes that this is a business negotiation, specifying that the patentee's first offer is not required to be FRAND in all respects, and abuse of a dominant market position is only present if the patentee outright denies the articulated interests of the implementer, making it impossible to negotiate a license.

By the same token, the implementer is required to react productively and provide a counteroffer. Simply stonewalling is not an option. In a marketplace in which implementers believe that their use of SEPs will be protected by courts relying on the FRAND commitments of patentees, this standard requiring the implementer to constructively engage and negotiate provides much-needed balance.

The FCJ is simply recognizing what New York merchants understand — consumers will delay paying as long as possible, unless presented with motivation to be reasonable.

On the subject of remedies, the FCJ is clear that restricting damages to the amount of a FRAND royalty should only occur in a case where there is abuse of a dominant market position.

The implication of this finding is critical: If there is no such abuse because the patentee did demonstrate a willingness to negotiate FRAND terms, the damages must be higher than if a license had been negotiated proactively, given the infringement by the implementer and/or its unproductive behavior during negotiations.

Any other result simply rewards infringement and free-riding, gives implementers a ready excuse to hold out against good-faith licenses, and causes unnecessary disputes.

The FCJ's ruling, which is based on the realities of negotiation dynamics in the SEP context, exhibits another pragmatic recognition by the German courts that the patent rights of innovators must be respected in the first instance and that implementer behavior designed to delay or avoid paying for its use of SEPs can come in many subtle forms.

A request from a patentee for an injunction after prolonged negotiations is not a sign of exclusionary behavior, especially given that the patentee has already broadly bound itself to offer FRAND terms. It is more often the result of an implementer playing New York hardball in an effort to delay or avoid paying for a license to use the property it has appropriated.

The FCJ's analysis demonstrates two practical dynamics at play in FRAND disputes. First, implementers are quick to adopt hard-won innovations embodied in standards for their own gain, taking for granted the expense and risk borne by patentees.

Second, there must be consequences for implementers who do not proactively come clean and constructively seek a license. If there are no such consequences, implementers will not engage productively and the result will be endless litigation couched under the guise of SEP wars, when the litigation is actually the result of systemic lawbreaking by implementers refusing to pay what they owe.

No New York merchant would accept someone walking into its store and taking products without paying, daring the shopkeeper to sue. Why should users of SEPs be treated differently? We Americans should take a lesson from the practical approach of the German courts in this most recent SEP case.

David J. Kappos is a partner at Cravath Swaine & Moore LLP. From August 2009 to January 2013, he served as undersecretary of commerce and director of the U.S. Patent and Trademark Office.

Daniel J. Etcovitch is an associate at the firm.

[1] Sisvel International S.A. v. Haier Deutschland GmbH & Haier Europe Trading SRL, Bundesgerichtshof [BGH] [Federal Court of Justice], Nov. 24, 2020, KZR 35/17 (Ger.).