CLEARY GOTTLIEB

ANALYSIS

Our Analysis of the Ninth Circuit Panel Decision Reversing FTC v. Qualcomm

August 27, 2020

On August 11, 2020, a Ninth Circuit panel reversed the District Court for the Northern District of California's judgment in *FTC v. Qualcomm, Inc*. The panel held that Qualcomm's conduct—(a) refusing to license its standards essential patents (SEPs) to rival chipset manufacturers; (b) refusing to supply chipsets to OEMs unless they first executed a license to its SEPs ("no license, no chips"); and (c) making exclusivity payments to Apple—was not anticompetitive. The panel did not disturb the District Court's conclusions that Qualcomm had monopoly power in the markets for code division multiple access (CDMA) and premium long-term evolution (LTE) cellular modern chipsets.

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The panel's opinion had several key holdings:

- A duty to deal requires a short-term sacrifice of profits and a previous profitable course of dealing *while* the monopolist has monopoly power.
- Violating a commitment to license SEPs on fair, reasonable, and non-discriminatory (FRAND) terms is the exercise of lawful monopoly power and does not give rise to antitrust liability, at least absent intentional deception that led to the SEP holder's selection into the standard.
- Once the question of Qualcomm's royalties being FRAND is set aside, Qualcomm's licensing scheme was "supplier neutral," as the licensee must pay them no matter whether it uses Qualcomm's or rivals' chipsets.
- Qualcomm's "no license, no chips" policy—under which it refuses to sell its chips to any company that has not taken a license to its patents—was justified to avoid patent exhaustion.

The FTC may now seek a rehearing *en banc* with the Ninth Circuit. Given the messy history of the litigation, in which the District Court adopted an unusual theory different from the FTC's and the DOJ intervened to oppose the FTC, the FTC may not wish to do so. But with some tension between the panel opinion and several precedents, including some that impact broader antitrust law, the FTC may still feel compelled to appeal.

Background on the standard setting and antitrust law

Modern electronics are the result of contributions by many inventors creating ever-more complex devices that must be interoperable with products created by others. To enable this interoperability, standard-setting organizations (SSOs) seek convergence on a common technology. SSO members include companies that develop competing technologies and which lobby to have their methods incorporated into the standard, to the exclusion of other competing alternatives, in exchange for a pledge to license their technology on FRAND terms. This combination results in wider adoption of essential technology and enables interoperability among devices. In essence, standard setting involves trading competition between alternative technologies for competition between interoperable implementations of a single technology.

Courts have long grappled with the role of antitrust in policing abuses related to standard setting. Early cases, such as *American Society of Mechanical Engineers*, took a dim view of potential competitors agreeing to standards, noting that an SSO "can be rife with opportunities for anticompetitive activity."[1] As time passed, however, courts began to appreciate the benefits that standard setting could bring. For example, in *Allied Tube*, the Supreme Court noted that "[w]hen, however, private associations promulgate [] standards based on the merits of objective expert judgments and through procedures that prevent the standard-setting process from being biased by members with economic interests in stifling product competition…those private standards can have significant procompetitive advantages."[2]

The most recent and active debate, however, has been over the use of antitrust to police licensing of SEPs. On the one hand, the Third Circuit in *Broadcom v. Qualcomm* recognized that, absent enforcement of contributors' FRAND promises, the exclusion of alternative technologies could result in SEP holders exercising the market power that flows from being part of the standard, rather than only that which comes from the value of SEP holder's own invention.[3] The Third Circuit therefore viewed preventing the exercise of market power through violations of the FRAND commitment as a core concern of antitrust, at least when the SEP holder's commitment had been an important attribute in the selection of its technology into the standard.[4]

The Federal Circuit, on the other hand, took a different view. In *Rambus v. FTC*, it observed that a core requirement of anticompetitive conduct is the exclusion of competition.[5] In that case, the FTC had made no findings about what technology the relevant SSO would have selected had Rambus's intent to violate its FRAND commitment been known, and so it could not say that the deception had excluded another competitive alternative.[6] The court emphasized that antitrust law is not meant to police high prices alone, absent evidence that those prices flowed from a reduction in competition, and is therefore not a proper mechanism for enforcing FRAND commitments.[7]

The FTC's theory: shifting profits from chipsets to SEP royalties to hamper entry

The FTC accepted that Qualcomm was instrumental in the development of early mobile baseband technology. For the purposes of litigation, the FTC also accepted that Qualcomm had lawfully acquired monopoly power in the supply of CDMA chipsets and premium LTE chipsets and that Qualcomm's SEPs were valid.

Nonetheless, the FTC argued that Qualcomm's conduct had allowed it to block the entry of rival

1 *Am. Soc'y of Mech. Engs., Inc. v. Hydrolevel Corp.*, 456 U.S. 556, 571 (1982).
2 *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 501 (1988).
3 *Broadcom Corp. v. Qualcomm Inc.*, 501 F.3d 297, 314 (3rd Cir. 2007).
4 *Id.*
5 *Rambus Inc. v. Fed. Trade Comm'n*, 522 F. 3d 456, 464 (Fed. Cir. 2008).
6 *Id. at* 466. By contrast, the European Commission, which also investigated Rambus, expressly found that the conduct did exclude other alternatives.
7 *Id.*

suppliers, unlawfully maintaining these monopolies in violation of Section 2 of the Sherman Act.[8]

The "standard" licensing model allows collection of lawful monopoly rents, but the monopoly erodes over time as rivals enter

The FTC had noted that, in the typical industry licensing model, a firm in Qualcomm's position would earn its profits in two streams. First, the firm would sell its product, which through a principle called "patent exhaustion" implicitly includes a license to any of the firm's IP that is substantially embodied in the product.[9] Second, the firm would license its SEPs to rival sellers, with royalties subject to the firm's FRAND commitment.

This licensing model allows the firm to exploit its lawfully acquired monopoly in the chipsets and earn a reasonable return on its SEPs. However, it has the disadvantage that the high price of the chipset would stimulate entry by rival chipset suppliers, eventually eroding the firm's monopoly.

The Qualcomm licensing model is able to extract monopoly rents without drawing entry

To avoid attracting entry, the FTC alleged, Qualcomm came up with a new licensing model.[10] The model would transfer some of its profits from the chipset price—which only Qualcomm customers pay—to the royalties for its SEPs—which the purchaser of any chipset must pay. By transferring profits to the royalty, the price to use Qualcomm's chipsets would stay the same, but either the price to use rivals' chipsets would have to rise or rivals' profits would have to fall, reducing either the attractiveness or sustainability of any challenge to Qualcomm's chipset business.

The primary obstacle standing in the way of Qualcomm's licensing model was its commitment to SSOs to license its patents on FRAND terms. Absent further steps, anyone purchasing from a Qualcomm rival would simply refuse to pay the inflated royalty, either suing to enforce the FRAND commitment as a matter of contract law or invoking the FRAND commitment as a defense in a patent infringement suit.

Qualcomm took two actions to prevent that outcome:

- Qualcomm refused to license its SEPs to rival chipset makers. Instead, it prevented them from making a claim by agreeing not to assert its patents against the chip suppliers in exchange for information from these competitors about market developments, while reserving the right to assert claims against any rival's OEM customers.
- Then, Qualcomm refused to supply chipsets to OEM customers unless they first signed a license to Qualcomm's SEPs ("no license, no chips") that covered both the use of the SEPs in Qualcomm's chipsets and in rival's chipsets. As Qualcomm was a monopolist in the supply of chipsets, OEMs had no choice but to agree.

By taking these two actions, the FTC alleged, Qualcomm was successfully able to prevent any party from invoking a contract or patent remedy against its inflated royalties.

The effect was to suppress entry, which Qualcomm compounded by paying exclusivity rebates to a key customer, Apple

The FTC alleged that the overall effect of Qualcomm's conduct was to create a tax on purchases from rivals, suppressing rivals' incentives to enter. The FTC analogized this conduct to the *Caldera v. Microsoft* case, in which Microsoft had required OEMs to pay it license fees on all processors the OEM shipped, whether they included Windows or not.[11]

8 As a technical matter, the FTC alleged a violation of Section 5 of the FTC Act, which prohibits "unfair methods of competition," but which also encompasses violations of Sections 1 and 2 of the Sherman Act.

9 A commonly heard argument for separate IP licensing is that patents practiced only by the end device (often called "system-level patents") are entitled to royalties that are a share of the price of the end device. But it is relatively common, for example, to charge less for processors that are used in less expensive devices reflecting the share of the end device price.

10 *Ninth Cir. Opinion* at 37.

11 *FTC Response Brief* at 37–38.

Notwithstanding Qualcomm's conduct, key OEM customers such as Apple continued to encourage rivals to enter. Several attempted to do so, including Broadcom and Intel, although they struggled to attract sales given the inflated royalties OEMs had to pay to Qualcomm to use their chipsets.

Ultimately, all of those potential rivals decided to abandon their entry plans, other than Intel, which continued to pursue business with Apple. Although Apple was keen to support Intel's plans for entry, Apple was also not willing to risk all of its iPhone inventory on a new supplier.

Qualcomm, the FTC alleged, thus determined to leverage Apple's need for some Qualcomm chips to foreclose any supply from Intel by offering Apple exclusivity payments. The FTC cited documents from Intel employees showing that in 2014 Intel had been close to a deal with Apple to supply a portion of baseband chips for the new iPhone. Intel employees then testified that the deal fell apart once Apple realized they would lose an exclusivity payment from Qualcomm valued at approximately $1 billion. The FTC argued that these royalties did not ultimately benefit OEM customers, because they only served to offset the inflated royalties Qualcomm imposed.

The FTC made similar allegations regarding offers to other large OEMs, such as Samsung and Huawei.

The District Court's theory: an antitrust duty to deal with rivals

On May 21, 2019, the District Court granted the FTC's request for a permanent injunction. But, surprisingly, the District Court did not adopt the FTC's primary theory of harm with respect to Qualcomm's refusal to license to rivals. Instead, the District Court predicated its decision on the grounds that Qualcomm had a duty to deal with its rivals under the Supreme Court's decision in *Aspen Skiing*.

In an earlier procedural motion, the District Court had granted partial summary judgment for the FTC, holding that Qualcomm's FRAND commitments required it to license its SEPs to rival modem chip suppliers.[12] Under the terms of its declarations to two SSOs (TIA and ATIS), Qualcomm had a contractual obligation to license "to all comers," including rivals.[13]

Following from this earlier holding, the District Court held that Qualcomm had an antitrust duty to license its SEPs to rival chipset makers. Citing *Aspen Skiing* and a number of follow-on appellate cases, the court found that Qualcomm:

- terminated a voluntary and profitable course of dealing when it stopped licensing rival chipmakers;
- was motivated by anticompetitive malice; and
- there is an existing retail market for licensing modem chip SEPs.

The court cited evidence that Qualcomm had licensed rival chip suppliers in the past and that it ceased doing so in order to protect its chipset business.[14] This evidence was, however, quite dated.

The District Court then cast the "no license, no chips" policy as enabling Qualcomm to impose unreasonably high royalty rates that resulted from its "leverage" of the chip supply against OEMs,[15] and that it could not charge the same royalty rates if it licensed rival chip suppliers.[16] It characterized this excess royalty as reflecting the value Qualcomm's monopoly chip market share rather than the value of Qualcomm's patents.[17] The District Court thus found this "surcharge" disproportionately harms rivals by controlling the "all-in" price of any modem chip sold and preventing rivals from underbidding Qualcomm.[18]

Finally, as the FTC had argued, the District Court concluded that Qualcomm's use of exclusivity agreements and so-called "incentive funds" wrongfully

12 *District Court Opinion* at 125.
13 *Id.*
14 *Id.* at 137–40.
15 *Id.* at 159.
16 *Id.* at 133.
17 *Id.* at 161.
18 *Id.* at 183–85.

foreclosed Qualcomm's rivals from selling modem chips.[19]

The court ordered Qualcomm to license rival chipmakers and to renegotiate existing licenses to OEMs without the threat of withdrawing chip supply.[20] The Ninth Circuit stayed that order pending appeal.

Qualcomm's and the DOJ's response: legitimate licensing practices to avoid patent exhaustion and legitimate discounts to key customers

Qualcomm argued that the District Court erred in holding that it had a duty to license its rivals and none of the required elements of *Aspen Skiing* were met. In that case, the Supreme Court had held that a monopolist's refusal to deal with a competitor could violate Section 2 of the Sherman Act where there was (1) a prior voluntary and profitable course of dealing with the rival; and (2) the monopolist was willing to sacrifice the short-term benefits of that course of dealing in exchange for a long-run impact on its rival.[21] Qualcomm denied that it had ever engaged in a "course of dealing" with rivals, because it had never granted chip-level rivals exhaustive licenses. Moreover, Qualcomm's argued that its decision not to license rival chipmakers was profitable in the short term, and therefore did not sacrifice short term profits for the sole purpose of eliminating a rival, as had been the case in *Aspen Skiing*.[22]

Qualcomm also argued that its "no license, no chips" policy was justified as a way to avoid patent exhaustion.[23] It suggested that the policy was supplier neutral: OEMs paid the royalties no matter whether they purchased chips from Qualcomm or one of its rivals.

Even if the policy enabled Qualcomm to maintain "unreasonably high" royalty rates by evading the type of negotiation process envisioned under FRAND terms, and harmed OEMs, Qualcomm argued, this did not exclude competition and therefore is not an antitrust issue.[24]

Separately, in an unprecedented move, the DOJ also intervened in the appeal in support of Qualcomm and against the FTC. The DOJ's arguments largely echoed Qualcomm's, adding the DOJ's view that it was critical to the national security of the United States that Qualcomm remain the dominant supplier of cellular baseband chipsets.[25]

The panel's opinion: antitrust has no place in policing FRAND commitments, Qualcomm's conduct was supplier neutral

The panel largely adopted Qualcomm's arguments in reversing the District Court ruling.

Qualcomm has no duty to deal because none of the elements of *Aspen Skiing* are met

On appeal, the FTC had declined to defend the District Court's decision on the ground that Qualcomm had a duty to deal with—that is, to license—its rival chipset suppliers. The panel agreed, but went further in a number of respects, agreeing with Qualcomm that none of the required elements for the *Aspen Skiing* exception was met:

First, the panel held that Qualcomm did not terminate a "voluntary and profitable course of dealing" because it had never granted rival chipmakers exhaustive licenses. Additionally, the panel noted that the FTC offered no evidence that Qualcomm licensed chipmakers from the time it first gained monopoly power in the modem chip market.[26] The panel's requirement that the change to the course of dealing must occur while the firm has monopoly power is, however, in some tension with the facts of *Aspen Skiing*: In that case, the course of dealing long predated Ski Co. obtaining monopoly power through acquiring a rival operator and then opening a new

19 *Id*. at 83, 105.
20 *Id*. at 227–29.
21 *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 610–11 (1985).
22 *Qualcomm Opening Brief* at 48–49.
23 *Id*. at 17.
24 *Id*. at 100–01.
25 *See Brief of the United States of America as Amicus Curiae* at 6.
26 *Qualcomm Opening Brief* at 33–34.

resort, which kicked off a series of demands and threats that ultimately culminated in the termination several years later.[27] It is also difficult to understand the rationale for imposing such a requirement—presumably the behavior pre-acquisition of market power was motivated by efficiency, and all else equal a change resulting only from acquiring market power would suggest an anticompetitive motive.

Second, the panel found that Qualcomm's rationale for changing to OEM-level licensing was in response to a change in patent-exhaustion law and was lucrative in both the short and long term.[28] The panel found that Qualcomm in fact declines to enforce its patents against rival chipmakers, instead offering them indemnification agreements.[29]

The panel thus held that the District Court had erred in holding that Qualcomm was otherwise under an antitrust duty to license rival chip manufacturers.[30]

Qualcomm's refusal to license rivals was not anticompetitive under the FTC's "traditional Section 2 standards," because antitrust has no role in policing FRAND commitments to SSOs

The panel also found wanting the FTC's alternate theory that "Qualcomm entered into a voluntary commitment to deal with its rivals as part of the SSO process, which is itself a derogation from normal market competition, and (2) Qualcomm's breach of this contractual commitment satisfies traditional Section 2 standards [in that] it tends to impair the opportunities of rivals and . . . does not further competition on the merits."[31]

The panel first expressed doubt that, even if Qualcomm had breached its FRAND commitment by refusing to license rivals, that the FTC had shown how that refusal impaired those rivals' competitive opportunities, because Qualcomm did not collect royalties from them ("no license, no problem").[32] The panel was not persuaded that entry and investment by rivals were deterred because the "no license, no problem" agreements with rivals functioned as *de facto* licenses.[33] The panel also noted that MediaTek and Intel had entered while these policies were in force.[34] Moreover, the panel found that Qualcomm had a procompetitive justification for not licensing rival chipset makers, because licensing at the OEM and chip-supplier levels simultaneously would require the company to engage in "multi-level licensing," leading to inefficiencies and less profit.[35] The panel did not explain what those inefficiencies were or whether the refusal was reasonably necessary to avoid them.

The panel also declined to apply *Broadcom v Qualcomm*, because the FTC had not alleged "intentional deception of SSOs on the part of Qualcomm nor that Qualcomm charged discriminatorily higher royalty rates."[36] That finding is however at odds with the District Court's factual findings that Qualcomm internally understood the FRAND commitment it had made to SSOs to require it to license rival chipset makers, and that it had purposefully refused to do so.[37] Rather, what seems to have driven the panel is that it was persuaded by the policy arguments of several *amici* that contract and patent remedies are better equipped to handle FRAND disputes than is antitrust law.[38]

Qualcomm's "no license, no chips" was supplier neutral and at best an unsuccessful "margin squeeze" claim

The panel also disagreed that the "no license, no chips" policy enabled Qualcomm to impose an anticompetitive surcharge on rivals' modem chip sales, as both the FTC and District Court had urged.[39] That

27 *Aspen Skiing*, 472 at 587–95.
28 *Ninth Cir. Opinion* at 34.
29 *Id*. at 35.
30 *Id.* at 31–36.
31 *Id.* at 36.
32 *Id*. at 35–37, 48.
33 *Id.* at 37.
34 *Id*.
35 *Id*. at 37–38.
36 *Id*. at 38–39.
37 *District Court Opinion* at 752 (e.g., "Qualcomm's 'commitment to the industry to license on fair and reasonable terms free from unfair discrimination would make it difficult to argue that we have the right to refuse to license [Intel].'").
38 *Ninth Cir. Opinion* at 39–40.
39 *Id*. at 45.

theory relied primarily on an analogy to *Caldera Inc. v. Microsoft Corp.*, in which Microsoft had required OEMs to pay license fees for sales of any machine, whether it was loaded with Windows or a rival's operating system. The panel distinguished *Caldera* on the basis that Qualcomm was entitled to charge OEMs a royalty where its SEPs were practiced in conjunction with a rival's chipset, whereas Microsoft had no such entitlement for machines that did not carry its software.[40]

Given that Qualcomm was entitled to charge *a royalty*, the panel then cited *NYNEX Corp. v. Discon, Inc.* to dismiss any challenge to *the level of the royalty*, noting there is no Sherman Act violation where "consumer injury naturally flowed … from the exercise of market power that is lawfully in the hands of a monopolist," even if the pricing effects of its market power were exacerbated by deception.[41] In doing so, the panel noted the Supreme Court's statement in *Trinko* that the opportunity to charge monopoly prices "is an important element of the free-market system" and "is what attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic growth."[42] The panel also held that the royalty rate applied regardless of chip supplier, and so together this entitlement to charge something and supplier neutrality did not have the "practical effect of exclusivity."[43]

The FTC had argued that the facial neutrality of Qualcomm's royalty was meaningless, because when purchasing from Qualcomm the customer would only care about the sum of the chip price and royalty, and thus Qualcomm could set an arbitrarily high royalty by simply lowering the chip price.[44] The panel also dismissed this argument, characterizing it as analogous to arguing a "margin squeeze"—too high a price for the license to rivals given the price of Qualcomm's chip—noting that under the Supreme Court's *linkLine* case such a claim requires either a duty to deal in the input (the license) or predatory pricing of the output (the chip).[45]

Even if a surcharge theory were valid, Qualcomm's royalties were not unreasonably high

The panel also rejected the District Court's predicate finding that Qualcomm's royalties were high, holding that there is no principle under competition law requiring that patent royalties be based on the Smallest Saleable Patent Practicing Unit (SSPPU).[46] The panel held that antitrust law does not require that royalties "precisely reflect a patent's current, intrinsic value and are in line with the rates other companies charge for their own patent portfolios."[47] The panel did not discuss any of the existing case law on the setting of FRAND rates in patent litigation.

Qualcomm did pay Apple exclusivity rebates, but they did not result in anticompetitive foreclosure

Finally, the panel concluded that "Qualcomm's 2011 and 2013 agreements with Apple have not had the actual or practical effect of substantially foreclosing competition in the CDMA modem chip market."[48] The court relied on the fact that only Intel was found to have been foreclosed, and that because it was not shown to have been viable during much of the relevant period, it was only foreclosed from competition for one year, as it was later selected by Apple as its main chip supplier.[49] The Court did not address the FTC's allegations that other competitors had been foreclosed previously, and that Apple had to acquire Intel's baseband chipset product in order to continue the development of an alternative to Qualcomm's chips, after Intel had announced immediately after Apple's settlement with Qualcomm that it could not continue developing 5G chips as a result of the impact of Qualcomm's anticompetitive policies.

40 *Id*. at 45–46, 48.
41 *Id*. at 45. More specifically, in *NYNEX* the deception was not directed at market participants, but instead was intended to prevent the relevant regulatory agency from imposing a lower price cap.
42 *Id*. at 51.
43 *Id*. at 46.
44 *Id*.
45 *Id*. at 47.
46 *Id*. at 42–43.
47 *Id*. at 43.
48 *Id*. at 51-54.
49 *Id*. at 49, 52–53.

…

Although the panel opinion parsed each of the items of anticompetitive conduct on its own, the FTC had urged the panel to view them a series of interconnected and mutually reinforcing measures. There is a long history of so-called "course of conduct" monopolization claims under Section 2 of the Sherman Act, sometimes successful, sometimes not.[50] The panel, however, did not address this argument from the FTC.

The panel also made two other, somewhat detached points that do not seem necessary to sustain its holding, but which contradict existing case law. First, the panel criticized the District Court for focusing on harm to OEMs, holding that because OEMs are customers and not competitors, this harm was outside of the relevant market for cellular modem chipsets.[51] This is difficult to square with past decisions characterizing harm to customers of the relevant product market is the classic example of antitrust injury.[52]

Rather, this section of the panel's opinion is probably better read as making a *NYNEX*-type argument: high prices to OEMs are not anticompetitive unless they are the result of excluding competitors.[53] That, however, seems dissonant with the FTC's argument, which had not been that Qualcomm's royalty being too high caused OEMs to pay too much. Instead, the FTC had focused on Qualcomm's decision to condition the sale of its monopoly chipsets on OEMs agreeing to pay a particular royalty rate for competitors' chips, conduct that distorted the competitive process in which either the OEM or the rival would have freely bargained with Qualcomm over that royalty rate, and then which in turn made is less attractive to purchase rivals' chips.[54] It is possible that this conditioning might have been clearer had the FTC analogized it to a tying arrangement, but the FTC did not do so.

Second, the panel also noted early in the opinion that courts apply burden-shifting frameworks to claims under Sherman Act Section 1 (agreements in restraint of trade) and Section 2 (monopolization).[55] It then leapt from this similarity to the conclusion that the standards under Section 1 and Section 2 are the same.[56] But that is in significant tension with a long line of case law holding the opposite; for example, that "a monopolist's use of exclusive contracts, in certain circumstances, may give rise to a Section 2 violation even though the contracts foreclose less than the roughly 40% or 50% share usually required in order to establish a Section 1 violation."[57]

The likely consequence of the decision will be a greater role for contract- and patent-law remedies, at least in the United States

Whether antitrust does or does not have a role to play in dealing with standard-setting abuses has been and will remain a hotly-debated topic. The panel's opinion takes a clear stand on the side of excluding antitrust remedies for FRAND violations, pointing parties to seek contractual or patent remedies for these harms. Implementers seeking to rely on antitrust would therefore be well-advised to steer their claims to the Third Circuit, where they can rely on *Broadcom v. Qualcomm* and potentially seek to extend it. And SEP holders seeking to avoid antitrust liability would be well-advised to do the opposite, to steer their cases to

50 *See e.g.*, *City of Anaheim v. Southern Cal. Edison Co.*, 955 F.2d 1373, 1373 (9th Cir. 2007); *City of Mishawaka v. Am. Elec. Power Co.*, 616 F.2d 976, 986 (7th Cir. 1980) *Free Freehand Corp. v. Adobe Sys.*, 852 F. Supp. 2d 1171, 1180 (N.D. Cal. 2012).

51 *Ninth Cir. Opinion* at 30.

52 *See United States v. Microsoft Corp.*, 253 F.3d 34, 58 (D.C. Cir. 2001) (Anticompetitive conduct must "harm the competitive *process* and thereby harm consumers."); *Associated General Contractors v. Cal. State Council of Carpenters*, 459 U.S. 519, 530 (1983) ("Congress was primarily interested in creating an effective remedy for consumers who were forced to pay excessive prices."); *Reiter v. Sonotone Corp.*, 442 U.S. 330, 343 (1979) (describing the Sherman Act as a "consumer welfare prescription.") (*quoting* ROBERT H. BORK, THE ANTITRUST PARADOX 66 (1978)).

53 *Ninth Cir. Opinion* at 30.

54 *FTC Response Brief* at 34–35, 45–48.

55 Specifically, that the plaintiff must demonstrate likely anticompetitive effect, then the defendant must offer a procompetitive justification, then the plaintiff must prove the anticompetitive effect outweighs the procompetitive justification. *Ninth Cir. Opinion* at 28.

56 *Id.*

57 *Microsoft*, 253 at 70.

the Ninth Circuit or Federal Circuit (by filing a primary patent infringement claim).

Bringing a standalone antitrust case of this magnitude, however, is difficult, expensive, and takes a long time. Thus, apart from circuit shopping, we expect to see more implementers pursue arguments under contract law that they are third-party beneficiaries of FRAND promises to SSOs and under patent law about exhaustion and the level of reasonable royalties as the measure of damages.

These remain viable arguments.[58] Contract arguments along these lines have been successful in a number of recent cases, including *Ericsson v. TCL*[59] and *Microsoft v. Motorola*.[60] Similarly, FRAND commitments have been successfully raised as patent defenses in other cases, such as *Apple. v. Motorola*,[61] *Realtek v. LSI*,[62] and *Ericsson v. D-Link.*[63]

At the same time, the panel did not seem to recognize that Qualcomm's strategy effectively blocked both rivals and OEMs from actually being able to invoke those contract and patent remedies. We therefore also expect to see other SEP holders who have market power in downstream markets for the products implementing those SEPs attempt to replicate the Qualcomm licensing model to achieve the same effect.

If those models are to be challenged, that will likely require one of two things, either (a) rival product producers pushing the law forward on their standing to receive a fully-exhaustive license, even when they have received a non-assert covenant; or (b) OEMs developing the capacity to self-supply key components so that they cannot be subject to a similar "no license, no chips" practice and have the freedom to invoke those remedies. With respect to the latter, Huawei already has its HiSilicon division; and Apple similarly acquired the previous Intel baseband business.[64] One result of the decision may therefore be further consolidation among the OEMs to support the fixed costs of investing in component self-supply.

The panel's opinion, on its own, has no effect outside the US. For instance, the European Court of Justice has held that EU competition law applies to refusals to license SEPs to willing licensees.[65] Nonetheless, courts in EU member states have also lately moved to limit the impact of these past decisions. For example, the recent German Supreme Court judgment in *Sisvel v Haier*, and the Mannheim judgment in *Nokia v Daimler*, both applied high standards to be considered a "willing licensee."[66] The UK Supreme Court in *Unwired Planet v Huawei* broadened SEP owners' discretion to discriminate between implementers.[67] The European Commission's "Expert Group" on FRAND matters[68] will likely issue its report in Late September or early October this year, and given the group's composition we expect that report to be hostile to antitrust playing any meaningful role.

58 The panel vacated the District Court's summary judgment order finding that Qualcomm did have such a contractual obligation as moot, given its holding that Qualcomm's antitrust liability did not depend on that fact, without reaching its merits. *Id*. at 20.

59 *Ericsson Inc. v. TCL Commc'n Tech. Holdings, Ltd*., 2018 WL 2149736 (E.D. Tex. May 10, 2018) (currently on appeal to the Supreme Court on other grounds).

60 *Microsoft Corp. v. Motorola Inc.*, 854 F.Supp. 2d 993 (W.D. Wash. 2012).

61 *Apple Inc. v. Motorola Inc.*, 757 F.3d 1286 (Fed. Cir. 2014).

62 *Realtek Semiconductor Corp. v. LSI Corp.*, 946 F.Supp. 2d 998 (N.D. Cal. 2013).

63 *Ericsson v. D-Link*, No. 6:10-CV-473, 2013 WL 4046225 (E.D. Tex. Aug. 6, 2013).

64 Press Release, *Apple to Acquire the majority of Intel's smartphone modem business* (July 25, 2019).

65 *See Huawei Technologies Co., Ltd. v. ZTE Corp.*, C-170/13 (16 July 2015); *Motorola*, No. AT.39985 (29 April 2014); *Samsung Electronics*, C-3/39.939 (3 February 2014); *see also* Cleary Gottlieb Alert Memorandum, *Enforcing Standard-Essential Patents-The European Court of Justice's Judgment in Huawei v ZTE* (Aug. 3, 2015).

66 *Sisvel v Haier*, docket No. KZR 36/17 (FCJ May 5, 2020); *Nokia v. Daimler*, case no. 2 O 34/19 (Mannheim Regional Court August 17, 2020).

67 *Unwired Planet v Huawei*, [2020] UKSC 37, 26 August 2020, on appeals from: [2018] EWCA Civ 2344 and [2019] EWCA Civ 38

68 Group of experts on licensing and valuation of standard essential patents (E03600), https://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetail&groupID=3600.

We may therefore see further movement away from the use of antitrust to resolve SEP licensing in the near future, even though, due to differences in the underlying regimes, we do not expect it to directly influence pending proceedings elsewhere, for instance in the Korean Supreme Court (*Qualcomm v KFTC*).[69]

Future appeals

The FTC may request rehearing *en banc*. The Ninth Circuit typically rehears cases *en banc* as a panel consisting of the chief judge and ten other randomly selected judges from the circuit. The overall composition of the Ninth Circuit is more likely to be favorable to the FTC than were the panels that heard Qualcomm's motion to stay the District Court judgment and the merits.

Up to this point in the appeal, the FTC's staff lawyers had been litigating this case without further direction from the Commission itself, because the FTC was deadlocked 2-2.[70] However, since May, Chairman Joe Simons is no longer recused, because the recusal resulted not from his personal involvement but that of his previous firm, and sufficient time had passed.[71] As a result, it is highly likely that the full Commission will make the ultimate decision about the appeal.[72]

Apart from the direct issues in the case, the FTC may want to seek a rehearing in order to clean up some of the opinion's statements about general antitrust principles: for example, the elements of the panel's opinion regarding what counts as "harm to competition" versus customers or competitors, or the conflation of standards under Section 1 and Section 2 of the Sherman Act.

On the other hand, because of these types of issues, the FTC may believe that the opinion's reasoning is sufficiently vulnerable that it may not be followed by other Courts of Appeals. And it may fear that if it were to prevail in an *en banc* rehearing, Qualcomm might successfully petition for US Supreme Court review. Given the Supreme Court's views as expressed in other recent antitrust decisions, such as *Amex*, the FTC may view that as a losing proposition that would end the argument permanently.

The FTC could of course also theoretically directly seek *certiorari* from the US Supreme Court itself, in lieu of first asking for a rehearing *en banc*. We view that outcome as even more unlikely for the same reasons—that the FTC will want to contain the damage and reserve the right to fight another day.

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69 The FTC focused solely on the level of royalties paid by OEMs. Other antitrust authorities, notably the Korean FTC, also considered the competitive impact of other terms, such as royalty-free cross-licenses. In the KFTC's view, those terms extracted greater value from OEMs by failing to compensate them for their own patents. It also allowed Qualcomm to ensure its chipsets would be free of third-party SEP claims and to charge OEMs for that benefit, further allowing it to avoid loss of revenue from the chip price. The KFTC regarded this arrangement as an infringement of Qualcomm's FRAND promise and characterized it as a "patent umbrella" that sustained higher chip pricing. KFTC Judgment (January 31, 2019), *aff'd in part Qualcomm v. KFTC*¸ 2017 Nu 48 (Seoul High Court 4 December 2019). The decision was upheld in part and annulled in part by the Seoul Court of Appeals, and is currently on appeal to the Korean Supreme Court.

70 Matthew Perlman, *Will the FTC Change Its Tune On Qualcomm Licensing?*, LAW360 (Aug. 17, 2020), https://www.law360.com/articles/1301245.

71 Victoria Graham, *FTC's Simons No Longer Recused in Qualcomm Antitrust Case*, BLOOMBERG LAW (Aug. 13, 2020), https://news.bloomberglaw.com/mergers-and-antitrust/ftcs-simons-no-longer-recused-in-qualcomm-antitrust-case.

72 Although the rules are not entirely clear, FTC litigation counsel could theoretically decide whether or not to appeal on its own. That said, with a Commission that has a working majority such a decision would almost certainly be made through consultation between litigation counsel, the Director of the Bureau of Competition, and the Chairman.