



May 31, 2019

Judge Rules Qualcomm Licensing Practices Violate Antitrust Law

It has now become apparent, as Qualcomm learned last week in *Federal Trade Commission v. Qualcomm Incorporated*, 17-CV-00220-LHK, 2019 WL 2206013 (N.D. Cal. May 21, 2019), that it is not enough, in one's technology and IP licenses, to focus on the business terms and IP protective provisions. Rather, one must take into consideration the impact the licensing strategy will have on the vigor of competition in relevant markets. Perhaps an even more important lesson to be learned from the May 21, 2019 decision of U.S. District Judge Lucy Koh of the Northern District of California is to caution clients to tone down the rhetoric in internal correspondence about vanquishing the competition.

Judge Koh stopped just short of calling Qualcomm executives liars, but went out of her way to point out that the verbal testimony of the Qualcomm executives was consistently contradicted by internal email messages, memoranda, and hand-written notes. Qualcomm executives had to be admonished to slow down when telling their story, but fell silent under cross-examination by Federal Trade Commission (FTC) lawyers, answers needing to be painstakingly pried from the mouths of those same Qualcomm witnesses. Perhaps another lesson to be learned from the case is to spend significant time on witness preparation.

Judge Koh ordered that Qualcomm's licenses be renegotiated, an order Qualcomm says it will try to stay pending appeal. Given Qualcomm's poor showing in court, its resources would likely be better spent in negotiating fixes to its licenses to curb its potential damage exposure. The FTC wasn't after damages; that's not its mission. Licensees, customers, and competing chip makers, however, will be after blood – money damages. Plus, because of the Sherman Act's special provisions, those plaintiffs may well get those damages trebled – along with their attorney's fees. Apple Computers, however, is one potential plaintiff who won't be lining up, Apple having settled its own case against Qualcomm, literally, in the shadow of the FTC's trial.

Qualcomm's Chip-Related Licensing Policy

Qualcomm's chip-related patents had been designated in the standards setting process as standard-essential patents ("SEPs"). As such, they had to be licensed on fair, reasonable, and nondiscriminatory terms. Qualcomm's licensing terms, however, were anything but fair, reasonable, and nondiscriminatory, as Judge Koh found in her earlier ruling on a summary judgment motion. Still, it would be a mistake to conclude that violating one's obligations to standards setting organizations by employing sharp licensing practices is enough, standing alone, to violate the Sherman Act. That is not what the judge held.

It would also be a mistake to conclude that Judge Koh's opinion is limited to those few patent holders lucky enough to possess SEPs. Quite apart from its standard-essential patents, Qualcomm's licensing practices were questionable for anyone holding actual or potential market power. Patents, by definition, give the patent holder a limited monopoly, but when that monopoly, in effect, blocks the gateway into a market, IP policies can be nudged aside by antitrust policies. Thus, it is not a complete defense simply to rely on one's patent rights. So, not licensing to rival chip makers, something ordinarily permitted, was impermissible when Qualcomm's patents clog the gateway to the market. Then, Qualcomm didn't just sell its chips; it conditioned the sale of its chips on the presence of separate license agreements. Because of the First Sale Doctrine in copyright and the patent exhaustion doctrine for patents, once a product is sold, the number of controls that the seller may impose on the buyer is quite limited. If, however, there are separate licenses, more control is permitted; a legitimate

business practice. Qualcomm, however, used those licenses to restrict customers' dealings with competitors and to charge what the FTC called "exorbitant royalty rates."

Implications

One might ask why it was more improper for Qualcomm to exact its toll from royalties than to charge more for its chips. It probably isn't; it all comes down to Qualcomm's ability to use its gateway blocking patents to extract more than what Qualcomm deserved as a reward for its innovation. On top of all this, Qualcomm rewarded customers who agreed to buy exclusively from Qualcomm with rebates and exacted penalties from customers who did not. These and many of Qualcomm's other practices, if carried on outside the context of market power, would not have been unlawful.

Once market power, that ability to block the gateway to a market, is added in, those practices, especially when coupled with highly aggressive anti-rival rhetoric, become problematic. Therefore, as we said at the beginning, it is not enough to focus on business terms and IP protection provisions in ones licenses; one must also be cognizant of the potential impact of the licensing practices on the vigor of competition in the relevant markets. This calls for skills and expertise in both IP and antitrust.

Additional Information

If you have any questions regarding the recent Qualcomm decision, please contact one of the authors listed below. For more information concerning our intellectual property practice, please visit us at www.KutakRock.com.

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