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Federal Jury Finds that Ericsson's Licensing Offer to HTC is FRAND

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On February 15, a Texas federal jury found that Ericsson did not breach its obligation to offer HTC licenses to its standard-essential patents (SEPs) on fair, reasonable and non-discriminatory (FRAND) terms. The verdict ended a nearly two-year dispute as to whether FRAND obligations preclude a licensing offer based on end products rather than components. Ericsson succeeded in convincing the jury that its FRAND commitment does not require it to base royalty rates for its SEPs on the value of smartphone chips rather than the phones themselves. The jury verdict suggests that other SEP holders may be able to successfully argue that basing royalty rates on end products rather than components does not violate their FRAND obligations.

Ericsson holds patents that the parties agreed are essential to the 2G, 3G, 4G and WLAN wireless communication standards, and made a commitment to several standard setting organizations to license those SEPs on FRAND terms. HTC makes smartphones that implement Ericsson's SEPs and brought suit against Ericsson in April 2017, alleging that Ericsson overcharges for its SEPs.

HTC argued that Ericsson's royalty rates are unreasonable on a number of grounds, including that they are based on the value of the smartphones HTC produces rather than the chips that incorporate the SEPs within the phones. HTC also alleged that Ericsson's rates do not account for "royalty stacking," whereby an SEP holder must pay royalties to multiple patent holders to comply with a standard. HTC brought antitrust as well as breach of contract claims. The court, however, severed the antitrust claims and sent them to arbitration prior to trial because they related to past license agreements with enforceable arbitration provisions. The court also severed HTC's other claims relating to alleged past overcharges, while leaving intact the portion of HTC's suit seeking licenses to Ericsson's SEPs on FRAND terms going forward.

Last October, Ericsson moved for a ruling that its FRAND commitment to the European Telecommunications Standards Institute (ETSI) does not require it to base its royalty rates on the "smallest salable patent-practicing unit" (SSPPU)—in this case, chips. The court held in a January ruling that ETSI's Intellectual Property Rights policy, adopted in 1994, does not *automatically* require SEP holders to use the SSPPU as a royalty base. Instead, what constitutes a FRAND royalty rate depends on the particular facts of the case.

HTC and Ericsson chose to proceed to trial and present their arguments to a jury. Prior to trial, the court ruled to exclude expert testimony put forward by HTC relating to patent hold-up, royalty stacking and antitrust economics. After five days of trial and three hours of deliberation, the jury returned a verdict largely in favor of Ericsson, finding that the company's licensing offers to HTC are on FRAND terms. The jury also found that HTC and Ericsson both breached their duty to negotiate in good faith with one another.

The jury verdict suggests that other SEP holders may have success in arguing that they can base their royalty rates on end products like smartphones without violating their FRAND obligations. US courts, however, have applied varied approaches to determining FRAND rates and only a few have undertaken extensive calculations. No court has set a universal approach to calculating FRAND rates and as the Texas court noted in its January ruling, what constitutes FRAND is a fact-specific determination and can vary from case to case. For example, the *HTC/Ericsson* case did not address whether requiring a *component* manufacturer to pay a royalty based upon

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the value of an end product such as a phone violates FRAND obligations. A court or jury could reach a different conclusion about what constitutes FRAND terms in this different factual scenario. Thus, while Ericsson's conduct may be instructive, SEP holders should not assume that that they are abiding by their FRAND commitments whenever they base royalty rates on end products.

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