

No. 12-35352

**IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT**

MICROSOFT CORPORATION,

Plaintiff-Appellee,

v.

MOTOROLA, INC., MOTOROLA MOBILITY, INC., and
GENERAL INSTRUMENT CORPORATION,

Defendants-Appellants.

On Appeal From The United States District Court
For The Western District of Washington
Case No. 2:10-cv-01823 (Judge James L. Robart)

***AMICUS CURIAE* BRIEF OF INTEL CORPORATION IN SUPPORT OF
APPELLEE MICROSOFT CORPORATION AND AFFIRMANCE OF THE
DISTRICT COURT'S ORDER**

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, *amicus curiae* Intel Corporation, a Delaware corporation, hereby declares and discloses that it is a publicly traded corporation with its stock listed on the National Association of Securities Dealers Automated Quotations (NASDAQ). Intel Corporation does not have a parent company nor does any publicly held company own 10% or more of Intel's stock.

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STATEMENT OF INTEREST OF *AMICUS CURIAE*

Intel Corporation develops, manufactures, and sells integrated digital technology products, primarily integrated circuits. Its products include computing and communications components for server and personal computers, such as microprocessors, chipsets, motherboards, wireless and wired connectivity products, platforms incorporating these components, and software products, among many other offerings. Intel holds thousands of patents, is a member of a number of standard-setting organizations (“SSOs”), and has contributed technology to a number of important standards. Many of Intel’s products also operate in accordance with industry standards that may incorporate patents held by other companies. Accordingly, Intel has a strong interest in the proper interpretation and reliable enforcement of contractual commitments that patentees make to SSOs.

All parties to this appeal have consented to the filing of this brief. No person other than Intel and its counsel authored this brief in whole or in part or contributed money that was intended to fund the preparation or submission of this brief.

INTRODUCTION

This case raises an issue of exceptional importance to the U.S. economy. Computing, networking, and communications products incorporate numerous interoperability standards promulgated by SSOs (“standards”)—technical specifica-

tions that ensure a common format for communicating between devices. These standards are often critical to further innovation and consumer choice, facilitating the rapid adoption of new products and services. Without such SSO-devised standards, consumers could not be assured that their devices would be able to communicate with devices made by other manufacturers. As a result, many consumers would delay purchases until the industry settled on a single technology through a process of attrition (thereby delaying the adoption of innovative new technologies), and early purchasers would be stranded with devices that cannot communicate with most other devices.

The expanding role of standards may exacerbate an already significant obstacle to innovation in the high-technology sector: the “holdup” problem, which arises when a patentee uses the threat of “an injunction, and the potentially serious sanctions arising from its violation” (e.g., contempt sanctions), as “a bargaining tool to charge exorbitant fees to companies that seek to buy licenses to practice the patent.” *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 396 (2006) (Kennedy, J., concurring). This problem is particularly acute when compliance with a standard requires the infringement of standard-essential patents (“SEPs”). Because it is commercially necessary for manufacturers to comply with interoperability standards that achieve broad acceptance, manufacturers of standard-compliant products are required to practice technologies that are subject to SEPs, which in

turn confers enhanced holdup power upon SEP holders who fail to honor their commitments.

Before a standard's adoption, the royalties that the patentee could demand from licensees reflect only the value of its patent relative to other methods of achieving the same technological objective. Once an SSO adopts an interoperability standard that incorporates a particular patent, however, viable substitutes for the technology no longer exist, which, absent RAND commitments, enables SEP holders to extract supra-competitive royalties from firms that must implement the standard. The consequence is that implementers may be forced to pay far more for licenses than can be justified by the economic value of the claimed inventions.

The holdup problem is exacerbated by the fact that standards typically incorporate numerous SEPs—often thousands—and complex products incorporate hundreds of standards. *See* Mark A. Lemley and Carl Shapiro, *Patent Holdup & Royalty Stacking*, 85 *Tex. L. Rev.* 1991, 1992 (2007); Brad Biddle et al., *How Many Standards in a Laptop? (And Other Empirical Questions)* 1 (2010), available at http://www.standardslaw.org/How_Many_Standards.pdf (identifying 251 interoperability standards implemented in modern laptop computer). Thus, numerous patentees may hold SEPs that read on standard-compliant components of a given product. If even a small fraction of them demand unreasonably high royalties, the aggregate royalty burden could amount to multiples of the product's price.

To address this problem, most SSOs ask SEP holders to commit to license all entities that employ the standard, on “reasonable and non-discriminatory” terms (“RAND”) or “fair, reasonable, and nondiscriminatory” (“FRAND”) terms.¹ Such commitments typically create contractual obligations that may be enforced by anyone practicing the standard. Despite these commitments, however, some SEP holders demand exorbitant royalties for use of their SEPs, and seek injunctions against firms that do not acquiesce. Because the SSOs are not enforcement bodies, it falls to courts to enforce compliance with RAND commitments under the ordinary rules of contract law.

This case involves RAND commitments that Motorola, Inc., made with respect to two standards. Although the specific issue on appeal is the propriety of the district court’s anti-suit preliminary injunction, that relief is intended to preserve Microsoft’s ability to enforce Motorola’s RAND commitment for one of the standards (ITU-T H.264), and is justified in part by the important policy interests in judicial enforcement of RAND commitments that would be frustrated absent such relief.

¹ The two terms are functionally equivalent. Thomas F. Cotter, *Patent Holdup, Patent Remedies and Antitrust Responses*, 34 J. Corp. L. 1151, 1191 n.200 (2009).

As discussed below, recognition of three important principles that flow from the specific contractual commitments that Motorola undertook will help to achieve the goals of RAND commitments and mitigate the potential harm to innovation and consumer welfare otherwise engendered by standard-setting. First, a RAND license must be available to all comers. Second, a “reasonable” royalty rate under such RAND commitments must be based on the value of the particular component of the product that practices the standard and the relative contribution of the patentee’s SEPs to that component, taking into account alternatives that were available before the adoption of the standard and the reasonable aggregate royalty level for all SEPs and other patents that read on the component. Third, a patentee that makes a RAND commitment may not obtain an injunction against an alleged infringer that is willing and able to pay a RAND royalty.

This Court will likely be the first federal appellate court to address the enforcement of a RAND commitment with respect to the reasonableness of a royalty rate and the propriety of injunctive relief. These issues are of pressing importance to the U.S. economy and the public interest. In a recent International Trade Commission filing in a related dispute between Microsoft and Motorola, the Federal Trade Commission (“FTC”) expressed “concern[.]” about SEP holders’ attempts to enjoin the sale of patent-compliant products by “seek[ing] an exclusion order for infringement of [a] RAND-encumbered SEP as a way of securing royalties that

may be inconsistent with that RAND commitment.” Statement on the Public Interest, at 1, No. 337-TA-752 (June 6, 2012). Permitting such relief, it said, “has the potential to cause substantial harm to U.S. competition, consumers and innovation.” *Id.* Accordingly, in reviewing the district court’s anti-suit injunction—and, in particular, in evaluating the forum’s interest in this dispute—this Court should enforce the strong U.S. policy in favor of precluding SEP holders from leveraging unearned market power to the detriment of the public.

ARGUMENT

I. Standard-Setting Creates Opportunities For Patentees To Exploit Unearned Market Power

A. Standard-Setting Has The Potential To Bestow Undeserved Market Power On SEP Holders

SSOs play a critical role in the technology field by enabling “companies to agree on common technological standards so that all compliant products will work together.” *Apple, Inc. v. Motorola Mobility, Inc.*, 2011 WL 7324582, at *1 (W.D. Wis. June 7, 2011). Interoperability standards spell out specific protocols that are incorporated into products to enable them to communicate with each other. These standards “lower costs by increasing product manufacturing volume” and “increase price competition by eliminating ‘switching costs’ for consumers who desire to switch from products manufactured by one firm to those manufactured by another.” *Id.* They do so by “facilitat[ing] the sharing of information among purchasers of products from competing manufacturers, thereby enhancing the utility of all

products and enlarging the overall consumer market.” *Broadcom Corp. v. Qualcomm Inc.*, 501 F.3d 297, 308 (3d Cir. 2007).

The standard-setting process enhances consumer welfare by bringing together industry participants to compare and evaluate competing technologies for inclusion in standards. Through this process, SSOs can “readily make an objective comparison between competing technologies, patent positions, and licensing terms before an industry becomes locked in to a standard.” *Broadcom*, 501 F.3d at 309. Organized standard-setting also “reduces the risk to producers (and end consumers) of investing scarce resources in a technology that ultimately may not gain widespread acceptance.” *Id.* Interoperability standards benefit consumers by creating an “ecosystem of products and services in which competition can thrive.” Richard J. Gilbert, *Deal or No Deal? Licensing Negotiations in Standard-Setting Organizations*, 77 Antitrust L.J. 855, 855 (2011).

A “complication with standards,” however, “is that it may be necessary to use patented technology in order to practice them.” *Apple*, 2011 WL 7324582, at *1. In this case, for example, Motorola holds a number of patents that it asserts are essential to the H.264 and 802.11 standards. Normally, “a patent does not necessarily confer market power upon the patentee.” *Ill. Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 45 (2006). There “will often be sufficient actual or potential close substitutes for” the patented product or process to “prevent the exercise of

market power.” U.S. Dep’t of Justice (“DOJ”) and FTC, *Antitrust Guidelines for the Licensing of Intellectual Property* § 2.2 (1995), available at <http://www.justice.gov/atr/public/guidelines/0558.pdf>.

When SSOs’ interoperability standards attain commercial acceptance, however, substitute technologies are effectively foreclosed. *Broadcom*, 501 F.3d at 314. This is because compliance with standards becomes commercially necessary, forcing firms to practice SEPs and preventing them from using what otherwise would be alternative technologies.

By effectively compelling implementers to use SEPs in order to compete, interoperability standards would (absent enforceable RAND commitments) empower SEP holders to extract unreasonably high royalties from suppliers of standard-compliant products and services. *Broadcom*, 501 F.3d at 314. There are often no substitutes for a SEP because an interoperability standard necessarily requires use of the patented technology, and alternatives are not viable once the standard has achieved broad acceptance. For example, it could be commercially impracticable to omit the H.264 standard from Windows, because it is critical to a large proportion of third-party video content.

B. Standards May Exacerbate The Problems Of Holdup And Royalty Stacking

Standards may aggravate the holdup problem that arises when patentees use the threat of an injunction as “a bargaining tool to charge exorbitant fees.” *Hynix*

Semiconductor Inc. v. Rambus Inc., 609 F. Supp. 2d 951, 966 (N.D. Cal. 2009) (quoting *eBay*, 547 U.S. at 396 (Kennedy, J., concurring)). Holdup typically occurs when a patentee threatens an injunction after the accused infringer has made a substantial investment to develop a product and bring it to market. It enables the patentee to “capture not just the value of the inventive contribution that they have made—something they ought to be entitled to—but also some greater amount of money than their invention is worth.” Mark A. Lemley, *Ten Things To Do About Patent Holdup of Standards (And One Not To)*, 48 B.C. L. Rev. 149, 152 (2007). In other words, in addition to the economic contribution of the patented technology, the royalty may capture sunk costs that the producer has invested in the development of the product.

As the federal antitrust agencies have explained, “[a] holder of IP incorporated into a standard can exploit its position if it is costly for users of the standard to switch to a different technology after the standard is set.” DOJ and FTC, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* 38 (2007), available at <http://www.ftc.gov/reports/innovation/P040101PromotingInnovationandCompetitionrpt0704.pdf>. For example, “developing an alternative standard could be costly and may delay the introduction of a new product.” *Id.* Companies that “have invested significant resources developing products and technologies that conform to the standard will find it prohibitively

expensive to abandon their investment and switch to another standard” and will “become ‘locked in’ to the standard.” *Broadcom*, 501 F.3d at 310. Patentees thus obtain a “unique position of bargaining power” in which they “may be able to extract supracompetitive royalties from the industry participants.” *Id.* Of course, holdup can occur even in the absence of standards. But “[s]tandard setting makes the holdup problem worse because it leads to the creation of *irreversible* investments.” Lemley, *supra*, at 154 (emphasis added).

The threat from holdup is compounded by the fact that a product often incorporates many standards. Lemley & Shapiro, *supra*, at 1992. One study estimated, for instance, that a modern laptop computer incorporates “*at least 251 interoperability standards*”—with “the actual number . . . certainly much higher.” Biddle, *supra*, at 1. Because each standard may, in turn, incorporate hundreds or even thousands of patents, any given product may be subject to tens of thousands of SEPs alone—in addition to numerous other patents and other intellectual property rights. In short, a “modern device can encompass thousands of useful technologies, each of which may be covered by a patent claim.” *Hynix Semiconductor*, 609 F. Supp. 2d at 966; *see also* S. Rep. No. 110-259, at 12 (2008) (“[M]any products comprise dozens, if not hundreds or even thousands of patents, and the infringed patent may well be one smaller part of a much larger whole.”); European Patent Office, *Scenarios for the Future* 9 (2007), available at [10](http://www.epo.org/news-</p></div><div data-bbox=)

issues/issues/scenarios/download.html (“[T]he once ‘virtuous circle’ [of the patent system] has become eroded by problems such as . . . patent thickets, increasing costs and complexity of technology.”).

This multiplicity of standards and SEPs, in conjunction with the threat of holdup, leads to a further problem: “royalty stacking,” whereby numerous patent holders each demand unreasonably high royalties on the same product. Lemley & Shapiro, *supra*, at 1993. This can result in a total royalty burden that renders the product commercially unviable. Demands by multiple SEP holders for supra-competitive royalties cause prices to rise and output to fall, to the detriment of consumers. Royalty stacking hurts consumer welfare by raising prices for goods and preventing some innovative products from reaching the market at all. Economic theory teaches that when different patentees control the price of SEPs, no single patentee has an adequate incentive to ensure that the cost of the product is low enough to make it commercially attractive. Carl Shapiro, *Navigating the Patent Thicket* 123, in *2 Innovation Policy and the Economy* (eds. Adam B. Jaffe et al. 2002).

C. RAND Commitments Help Mitigate The Anticompetitive Threat From Standards

SSOs have recognized the power that standards may confer upon SEP holders to exploit the market power created by the incorporation of their patents into standards. They have attempted to prevent the creation of unearned market power

by promulgating rules “to insure that standards do not allow essential patent owners to extort their competitors or prevent them from entering the marketplace.” *Apple*, 2011 WL 7324582, at *1. Among other measures, most SSOs ask holders of patents that may read on a standard to commit to offer licenses on “RAND” (or, in Europe, “FRAND”) terms to firms that implement the standard. *Id.*

The International Telecommunications Union (“ITU”), whose H.264 standard is implicated in this appeal, has adopted a Common Patent Policy (“ITU Policy”) that governs SEPs held by participants in the standard-setting process. *See* <http://www.itu.int/en/ITU-T/ipr/Pages/policy.aspx>. It provides that “a patent embodied fully or partly in a [standard] must be accessible to *everybody* without undue constraints.” ITU Policy, Preamble (emphasis added). It further states that a patent holder should file a statement with the ITU indicating that it is (1) willing to negotiate licenses free of charge, (2) “willing to negotiate licenses with other parties on a non-discriminatory basis on reasonable terms and conditions,” or (3) “not willing to comply with” either of those options, in which case the standard “shall not include provisions depending on the patent.” *Id.* §§ 2, 3. Consistent with those requirements, Motorola submitted declarations to the ITU with respect to the H.264 standard stating that it either “will grant” or “is prepared to grant” a “license to an unrestricted number of applicants on a worldwide, non-discriminatory basis and on reasonable terms and conditions to manufacture, use, and/or sell implemen-

tations of the [standard].” *Microsoft Corp. v. Motorola, Inc.*, 2012 WL 1669676, at *2 (W.D. Wash. May 14, 2012) (quotation marks omitted).

RAND commitments, such as the ITU’s, help to prevent holdup by establishing *ex ante* ground rules for licensing SEPs. They are intended to reduce “the potential for the exercise of ex post market power” by constraining the ability of SEP holders to make unreasonable license demands using injunction threats and other sharp tactics to extract unreasonably high royalties after a standard is adopted. *Gilbert, supra*, at 856. But because the ITU, like other SSOs, does not have the capacity to enforce those commitments, it falls upon the courts to do so.

II. This Court Should Uphold The District Court’s Anti-Suit Injunction Because It Furthers Important Policies Of This Forum And This Case Is Dispositive Of The Foreign Action

The district court’s injunction against Motorola’s attempt to exclude Microsoft’s products from the German market was necessary to enforce Motorola’s RAND commitments. Under the well-settled precedents of this Court setting forth the circumstances in which anti-suit injunctions may be issued, the district court’s injunction was proper and should be affirmed.

A touchstone of this circuit’s analysis of anti-suit injunctions is the evaluation of whether the foreign litigation threatens to “frustrate a policy of the forum issuing the injunction.” *Applied Med. Distrib. Corp. v. Surgical Co. BV*, 587 F.3d 909, 913 (9th Cir. 2009) (quotation marks omitted) (setting forth factors for anti-

suit injunction).² In *E. & J. Gallo Winery v. Andina Licores S.A.*, 446 F.3d 984 (9th Cir. 2006), for example, this Court ordered issuance of an anti-suit injunction to prevent foreign litigation that violated a contractual forum-selection clause, explaining that the United States has a policy of “encouraging enforcement of forum selection clauses,” and that “[w]ithout an anti-suit injunction in this case, the forum selection clause effectively becomes a nullity.” *Id.* at 991–92. “An anti-suit injunction,” this Court explained, “is the only way [the plaintiff] can effectively enforce the forum selection clause.” *Id.* at 993; *see also Applied Med.*, 587 F.3d at 918–19.

The same is true here. As explained below, Motorola’s RAND commitments require Motorola to offer reasonable license terms to all parties and to refrain from seeking injunctions against parties from which it is practicable to collect a royalty. Motorola has failed to make a RAND offer to Microsoft, and instead has obtained an injunction against Microsoft’s sales in Germany. Practically speaking, an injunction in Germany could (if enforced) compel Microsoft to settle for unreasonable license terms, not only in Germany but in the United States as well, before the district court can resolve its claims: Motorola’s ability to exclude Microsoft

² Insofar as Microsoft’s likelihood of success on the merits, the balance of the equities, and the public interest may be relevant, those factors also strongly favor injunctive relief for the reasons set forth below.

from the large German market will give Motorola powerful leverage to demand excessive royalties worldwide. This is precisely the exploitation of unearned market power that the RAND promises were designed to prevent. Accordingly, an “anti-suit injunction is the only way [Microsoft] can effectively enforce” the RAND obligation. *E. & J. Gallo Winery*, 446 F.3d at 993.

The federal government has made clear that it is in the interest of the United States to prevent the exploitation of a SEP through injunctive relief. As discussed above, the FTC has concluded that permitting Motorola to obtain injunctive relief “has the potential to cause substantial harm to U.S. competition, consumers and innovation” by enabling Motorola to “secur[e] royalties that may be inconsistent with that RAND commitment.” Statement on the Public Interest, *supra*, at 1. There can be little doubt, then, that allowing Motorola to enforce an injunction against Microsoft, which will likely force Microsoft to settle for a royalty that exceeds RAND terms, would “frustrate a policy of the forum issuing the injunction.” *Applied Med. Distrib. Corp.*, 587 F.3d at 913 (quotation marks omitted).

An additional important consideration in this Court’s evaluation of an anti-suit injunction is the question whether “the first action is dispositive of the action to be enjoined.” *Applied Med.*, 587 F.3d at 913 (quotation marks omitted). Motorola’s attempt to enjoin Microsoft’s sales in Germany on the basis of patents that Motorola admits are covered by its RAND commitments unquestionably “can

be resolved in the local action,” *id.* at 915, because this action will resolve Microsoft’s entitlement to a license on RAND terms, and a license will obviate any basis for an injunction in Germany or elsewhere. Accordingly, this “action is dispositive of the action to be enjoined” under this Court’s precedents.³

This Court should therefore hold that the necessarily overlapping issues and strong public-policy interest in enforcing RAND commitments justify an anti-suit injunction here. In reaching that conclusion, this Court should recognize three principles that follow directly from the text and purpose of Motorola’s RAND commitments. First, RAND licenses must be offered to all comers; this follows directly from the plain text of the commitment. Second, RAND royalty-setting must account for other patents that read on the product; thus, the “royalty base” taxed by RAND royalties must be based on the value of the component that implements the standard, taking into account *the ex ante* value of the SEPs (*i.e.*, before they were incorporated into the standard) and the reasonable aggregate royalty level, with due consideration for all of the technologies (patented or otherwise) in-

³ Motorola thus errs in suggesting that this case cannot resolve questions of German patent law pending in the German court. Appellants’ Br. 26–28, 32. As the parties agree, the interpretation and enforcement of Motorola’s RAND commitment presents a question of U.S. law (*see infra* note 4), and nothing in the text of the commitment suggests that its meaning would vary by jurisdiction. Because Microsoft is ready and willing to take a license on RAND terms, the determination of what constitutes a RAND royalty for Motorola’s SEPs worldwide will resolve the German action for injunctive relief.

corporated into the licensed component. Third, patentees that make RAND commitments may not seek an injunction where the infringer is willing and able to pay RAND royalties.

A. A RAND Commitment Requires A SEP Holder To License All Comers, Including Component Makers

The basic principles of contract interpretation are well-settled.⁴ In interpreting a contract, a court “attempt[s] to determine the parties’ intent by focusing on the objective manifestations of the agreement.” *Hearst Communications, Inc. v. Seattle Times Co.*, 115 P.3d 262, 267 (Wash. 2005) (en banc). “If relevant for determining mutual intent,” courts will examine “extrinsic evidence,” such as “(1) the subject matter and objective of the contract, (2) all the circumstances surrounding the making of the contract, (3) the subsequent acts and conduct of the parties, and (4) the reasonableness of respective interpretations urged by the parties.” *Id.* at 266.

As an initial matter, the foremost command of the RAND contractual obligation is that a SEP holder must grant a reasonable license to *all* comers—both sellers of completed products to consumers, such as Microsoft, and manufacturers of the components that go into those products. The plain text of the ITU Policy

⁴ The parties agree that Washington law applies here, although these basic principles do not vary materially by jurisdiction.

states that a SEP holder must be “willing to negotiate licenses with other parties on a non-discriminatory basis on reasonable terms and conditions” and that the express purpose of this requirement is to ensure that the standard is available “to everybody without undue constraints.” ITU Policy, Preamble, § 2.2 (emphasis added). The “sole objective” of the ITU Policy is to “meet this requirement.” *Id.*, Preamble (emphasis added). Further, Motorola’s RAND declarations commit Motorola to “license to an *unrestricted* number of applicants.” *Microsoft Corp.*, 2012 WL 1669676, at *2 (emphasis added; quotation marks omitted). Its RAND commitments thus guarantee that all implementers may incorporate the H.264 standard on reasonable terms, while also enabling it to obtain fair compensation for the use of its intellectual property.

Accordingly, Motorola must grant RAND licenses to any willing party, including, for example, manufacturers of the components used in Microsoft’s products.

B. For A Multi-Component Product, A RAND Commitment Generally Requires A Royalty To Be Assessed At The Component Level And To Take Account Of Other Patents That Read On The Component

Two related principles flow directly from the text and objective of the RAND commitments required by the ITU Policy, particularly in light of industry custom and practice. First, a RAND “royalty base” must be set at the component level. In other words, the royalty rate generally must be applied to the smallest

component that implements the standard, not to the value of the entire product. Second, in deriving a royalty rate, a court must take account of the contribution of the patent to the component—and, in particular, must consider how many patents (both SEP and non-SEP) read on that component.

These basic requirements are fundamental elements of a “reasonable” royalty rate because they ensure that the rate reflects only the incremental economic contribution of the SEP and not unearned market power that RAND commitments are designed to obviate. As a group of SSOs explained to the Third Circuit, the objective of RAND commitments is to “produce standards that any willing implementer can use and that will become widely adopted,” while “[a]voiding hold-up outcomes (with their exorbitant and exclusionary license demands).” *Amici Curiae Br. of the IEEE et al.* at 8, 27, *Broadcom Corp. v. Qualcomm Inc.*, No. 06-4292 (3d Cir. Dec. 19, 2006).

When hundreds or thousands of patents are incorporated into a standard, it would take only a handful of SEP holders demanding unreasonable royalties to render the standard commercially unviable. In interpreting RAND commitments, therefore, courts must ensure that each SEP holder receives a royalty that reflects only the contribution of its patent to the accused product, and not the unearned market power that it agreed through its RAND commitment to forego. That requires a determination of the *ex ante* value of a SEP—that is, the royalty that the

SEP holder could have obtained from the manufacturer in arms-length bargaining before the SEP was incorporated into the standard. That determination must account for the fact that, when a standard is incorporated into only one component of a multi-component product, royalties based on the value of the entire product tend to compensate SEP holders for numerous technologies and features beyond those covered by their patents, thereby overcompensating them and leading to royalty stacking. *See Uniloc USA, Inc. v. Microsoft Corp.*, 632 F.3d 1292, 1318–19 (Fed. Cir. 2011).

Industry practice confirms that a RAND royalty requires a component-level royalty base and a royalty rate that takes into account the total royalty burden on the component. For example, former IBM licensing chief Gerald Rosenthal, who has negotiated hundreds of licensing agreements involving various computer industry products, explained in trial testimony relating to the 802.11 Wi-Fi standards that in his two decades of licensing experience, “in lots of negotiations . . . with probably hundreds, if not many more companies,” a royalty base on the lowest-level component “was generally the case that both sides agreed to during the negotiations.” Trial Tr. 76:1–4, *Commonwealth Scientific & Ind. Research Org., Inc. v. Buffalo Tech., Inc.*, No. 6:06-cv-549 (E.D. Tex. Apr. 17, 2009).

Motorola itself has recognized that a RAND royalty should take into account the overall licensing burden for all the relevant technologies in the end product.

See Ericsson, Motorola, and Nokia, *Expanded Proposal for IPR Policy Reform 3* (ETSI GA/IPRR02(06)05, Feb. 4, 2006). According to Motorola, this requires examining “the *overall cumulative royalty costs* for a given standard and not just to assess whether the terms being offered by one particular licensor are fair and reasonable *in vacuo*.” *Id.* at 4 (emphasis added).⁵

Important SEP licensors have implemented these principles in their licenses. For example, MPEG-LA, a patent pool that licenses 2,339 H.264 SEPs, charges Microsoft an annual royalty that is capped at \$6.5 million for those patents. Mot. for Summ. J., Dkt. 237, at 1–2 (Mar. 30, 2012). The royalty rate advertised by MPEG-LA for all 2,339 SEPs is \$0.10 per unit for an operating system such as Microsoft’s Windows but is capped at \$6.5 million, reflecting a royalty rate of approximately *five one-hundredths of one percent* of the wholesale price of Windows software (assuming that the wholesale price of Windows is \$40 and that over three-hundred million personal computers are sold annually). See http://www.mpegla.com/main/programs/avc/Documents/AVC_TermsSummary.pdf. This practice of charging a tiny fraction of the price of a standard-compliant product for a large number of SEPs confirms the industry-wide expectation that RAND requires a

⁵ Intel does not endorse the overall approach urged by Motorola in this statement, but merely notes Motorola’s recognition of the need for RAND royalties to be proportionate in light of all the other patents that read on a given product or component.

royalty that accounts for the total royalty burden on the product to ensure its commercial viability.

Industry practice thus confirms two key elements of RAND royalties, each of which helps to achieve the objective of avoiding holdup and royalty stacking: the royalty base must be set at the component level and the royalty must account for all of the patents that read on that component. Those elements, in fact, have long been applied by U.S. courts in establishing a “reasonable royalty” in ordinary patent-infringement suits—a background legal practice that undoubtedly informed Motorola’s commitments here (which both parties agree are governed by U.S. law). *Caritas Servs., Inc. v. Dep’t of Soc. & Health Servs.*, 869 P.2d 28, 36 (Wash. 1994) (en banc) (“Parties are generally deemed to contract in reliance on existing law.”).

It is well-settled that in setting a reasonable royalty in a patent-infringement lawsuit, a court may utilize a royalty base equal to the entire value of an infringing product *only* “to the extent that the patent owner proves that the patent-related feature is *the* basis for customer demand” for the entire product. *Marine Polymer Techs., Inc. v. HemCon, Inc.*, 672 F.3d 1350, 1360 (Fed. Cir. 2012) (en banc) (emphasis added; quotation marks omitted). If the patented feature is not the basis for customer demand for the entire product, the royalty base must equal an apportioned share of the total value of the product reflecting the contribution of the rele-

vant component to consumer demand. *Uniloc*, 632 F.3d at 1318–19.⁶ Then, once a component is isolated and its value apportioned, the royalty *rate* applied to that royalty base must reflect the total number of patents that read on the component and the other cost inputs that are built into it. As the Federal Circuit has explained, courts must identify the “portion of the realizable profit that should be credited to the invention as distinguished from non-patented elements [or patents held by others], the manufacturing process, business risks, or significant features or improvements added by the infringer.” *Lucent Techs., Inc. v. Gateway, Inc.*, 580 F.3d 1301, 1332 (Fed. Cir. 2009) (quotation marks omitted).

These basic precepts of patent law provide clear standards for courts to employ in enforcing the principle that a RAND royalty must reflect the contribution of the SEP to the value of a multi-component product. To evaluate whether a license meets the RAND requirement, a court must ensure that the royalty base is equal to the economic contribution of the smallest component that incorporates the

⁶ Under this rule, it is not sufficient for a patentee to assert a purportedly low royalty *rate* applied to the entire market value to reflect the minor role played by the patented feature in the product. As the Federal Circuit has explained, “[t]he Supreme Court and this court’s precedents do not allow consideration of the entire market value of accused products for minor patent improvements simply by asserting a low enough royalty rate.” *Uniloc*, 632 F.3d at 1320. The danger is that royalties based on the value of the entire product will be set systematically at rates that are too high based on the contribution of the patented technology, precisely the problem that leads to royalty stacking. *Id.*

standard and that the royalty rate reflects the total royalty burden on that component.⁷

Motorola's offer in this case failed to meet these requirements and expectations for a "reasonable" royalty. Motorola demanded a royalty of 2.25% of the *end price* of each accused final product (in other words, the entire market value of the products). That is an excessively high royalty rate. Even if the H.264 standard were the *only* standard practiced by Microsoft's products and even if the SEPs in the MPEG-LA patent pool were the *only* other SEPs practiced by the H.264 standard, the total royalty burden would exceed the total price of the products if the patent pool charged a royalty proportionate to what Motorola demanded: The patent pool contains approximately 45 times as many SEPs as what Motorola claims to own, meaning that the total royalty burden under Motorola's 2.25% demand would equal 103% of the price of the product—which is self-evidently unreasonable. And in reality, of course, there are far more SEPs that read onto the H.264 standard

⁷ The royalty base should never include more than the "smallest salable unit[]" that incorporates the patented technology, unless the patentee can satisfy the entire market value rule with respect to a larger unit or product. *Cornell Univ. v. Hewlett-Packard Co.*, 609 F. Supp. 2d 279, 283–88 (N.D.N.Y. 2009) (Rader, C.J., sitting by designation). In some circumstances, such as integrated high-technology products that do not incorporate separately marketable components but practice numerous patented technologies, a more granular approach may be required, if the patented technology is not "the basis for customer demand for the entire [product] including the parts beyond the claimed invention." *Id.* at 286.

than those owned by Motorola and the MPEG-LA patent pool; far more standards are incorporated into Microsoft's products than just the H.264 standard; and Microsoft's products incorporate numerous other inputs, including other patented and non-patented technologies. Thus, an ITC administrative law judge recently concluded that Motorola's offer was not reasonable. *Certain Gaming & Entm't Consoles, Related Software, & Components Thereof*, Initial Decision 300-04, No. 337-TA-752 (Apr. 23, 2012).

Finally, Motorola errs in asserting that rather than enforcing RAND commitments, "a court should defer to bilateral negotiations between parties participating in good faith and be leery of interceding to impose its own terms except as a last resort." Motorola Br. 31. As explained above, the purpose of a RAND commitment is to prevent a SEP holder from exploiting unearned market power. That objective would be defeated if courts withheld relief and relegated prospective RAND licensees to a bilateral negotiation in which the SEP holder exerts leverage that stems not from the intrinsic value of its patents but from its exploitation of power that it had agreed to cede when it made the RAND commitment. This is particularly true when the SEP holder has further tilted the playing field by seeking an injunction against a willing prospective licensee, despite its commitment to grant a license to all willing applicants.

C. Injunctions Are Inappropriate To Enforce A SEP When The Infringer Is Willing And Able To Pay RAND Royalties

In addition to proposing license terms that far exceed what is permissible under its RAND commitments, Motorola has obtained an injunction that could (if enforced) bar the sale of Microsoft products into Germany. The RAND commitment, however, precludes a SEP holder from obtaining injunctions against alleged infringers that are willing and able to pay RAND royalties. Particularly where, as here, a SEP holder has failed even to offer RAND terms, issuance of an injunction at the request of the SEP holder violates its RAND commitment and utterly frustrates the important policy interests underlying the standard-setting process's insistence on such commitments. As the Director of the U.S. Patent and Trademark Office recently told Congress, "if later folks who have offered their patents under FRAND terms then are able to get exclusion orders or injunctions, you can certainly have some tremendously negative side effects." Hr'g Before the S. Judiciary Comm., "Oversight of the United States Patent and Trademark Office: Implementation of the Leahy-Smith America Invents Act and International Harmonization Efforts," 41:18 (June 20, 2012); *see also id.* at 90:06 (injunctions could "unravel

the incentives that lead people into this process of negotiating the standard essential patents”).⁸

The plain text of Motorola’s contractual commitment (and other RAND commitments) precludes patent-infringement injunctive relief against willing licensees. Motorola pledged to make its SEPs available to “*an unrestricted number of applicants.*” *Microsoft Corp.*, 2012 WL 1669676, at *2 (emphasis added; quotation marks omitted). It further promised to “negotiate licences with other parties on a non-discriminatory basis on reasonable terms and conditions” under a Policy that expressly has as its “sole objective” ensuring that the standard is “accessible to everybody without undue constraints.” ITU Policy, Preamble, §2.2.

Thus, Motorola’s RAND commitment constitutes a promise to license Motorola’s SEPs to all willing parties that incorporate the H.264 standard into their products. As a result, the RAND commitment effectively modified the scope of Motorola’s patent rights. A patent confers “a property right,” *Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co.*, 535 U.S. 722, 730 (2002), that ordinarily entitles the holder to exclude others from practicing the patent. But “[a]s with other property rights, patent-related rights can be contracted away.” *Deprenyl Animal Health, Inc. v. Univ. of Toronto Innovations Found.*, 297 F.3d 1343, 1357 (Fed.

⁸ <http://www.judiciary.senate.gov/hearings/hearing.cfm?id=d1d944e8c0b3e2a582633afaeb6ba43a>.

Cir. 2002). Once a patentee agrees to license SEPs, the scope of its property right is modified, and it may no longer seek injunctions against willing licensees. Motorola's contractual promise to accept RAND royalties as sufficient compensation from *all* users of its SEPs leaves no room for barring parties willing and able to pay RAND royalties from selling standard-compliant products. *See Slip op.* at 18–19, *Apple, Inc. v. Motorola, Inc.*, No. 1:11-cv-08540 (N.D. Ill. June 22, 2012) (Posner, J.) (“By committing to license its patents on FRAND terms, Motorola committed to license the ’898 to anyone willing to pay a FRAND royalty and thus implicitly acknowledged that a royalty is adequate compensation for a license to use that patent.”).

Traditional equitable principles underscore the impropriety of injunctive relief for SEP holders in these circumstances. In *eBay*, the Supreme Court held that patent-infringement injunctions are unavailable unless “remedies available at law, such as monetary damages, are inadequate to compensate for [the plaintiff’s] injury.” 547 U.S. at 391. A SEP holder that makes a RAND commitment is not expressing a mere “willingness to license its patents,” *id.* at 393 (quotation marks omitted), but rather pledging to license the patents to *all* parties on RAND terms. Thus, issuance of an injunction at the request of the SEP holder would violate its RAND commitment and utterly frustrate the important policy interests underlying the standard-setting process’s insistence on RAND commitments. *Apple, supra*,

slip op. at 21 (“A FRAND royalty would provide all the relief to which Motorola would be entitled if it proved infringement,” and “thus it is not entitled to an injunction.”).

The key purpose of RAND commitments—“[a]voiding hold-up outcomes” and “ensuring that a standard will be genuinely ‘open’ to implementation by all interested parties,” *Amici Curiae* Br. of the IEEE, *supra*, at 27—would obviously be frustrated by permitting SEP holders to obtain injunctions. As discussed, the “threat of injunctive relief allows a patent owner to capture a substantially greater share of a component invention in a settlement than it otherwise could have.” Lemley, *supra*, at 153. If, for example, a “patentee can get an injunction that effectively says that Intel, because it included this circuit in its microprocessor, has to stop selling that microprocessor immediately . . . [t]he negotiation value associated with that threat of injunctive relief is quite substantial.” *Id.*; see also Carl Shapiro, *Injunctions, Hold-up, and Patent Royalties*, 12 *Am. L. & Econ. Rev.* 280, 283 (2010) (“The right to obtain an injunction thus gives the patent holder the power to hold up an infringing firm The prospect of such hold-up affects the negotiating strengths of the two parties prior to the onset of litigation.”).

The very purpose of the RAND commitment is to thwart this sort of exploitation of unearned market power. If there are any circumstances in which it is inappropriate for a party to use “an injunction, and the potentially serious sanctions

arising from its violation,” as a “bargaining tool,” *eBay*, 547 U.S. at 396 (Kennedy, J., concurring), it is the standard-setting context, where there is little possibility of design-around and the patent holder has already agreed that a royalty is sufficient compensation for its SEPs.

Of course, if an accused infringer were judgment-proof and refused to pay a RAND royalty, the SEP holder might indeed suffer irreparable harm absent an injunction, making injunctive relief appropriate. But in this case, Microsoft is willing and able to pay a RAND royalty, so Motorola’s contractual commitment to accept such payments as full compensation for the use of its SEPs precludes it from enforcing a patent-infringement injunction against Microsoft with respect to those SEPs.

CONCLUSION

Important policies of nationwide significance would be frustrated if SEP holders were permitted to evade their RAND commitments by demanding unreasonable royalties backed up by threats of injunctive relief. Properly construed, RAND commitments mean that royalties must be assessed at the component level and that injunctive relief is ordinarily inappropriate. Judicial enforcement of those principles is vital, not only to implement the basic bargain of the parties and preclude SEP holders from unfairly leveraging the market power created by estab-

lishment of the standard, but also to maintain the viability of the standard-setting process for the benefit of consumers, innovation, and the Nation's economy.

This Court should affirm the district court's order barring Motorola from enforcing any injunctive relief obtained in the German court system relating to the patents at issue here.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that pursuant to FED. R. APP. P. 32(a)(7)(C) and Ninth Circuit Rule 32-1, the foregoing brief is proportionately spaced, has a typeface of 14 points, and contains 6,990 words.

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CERTIFICATE OF SERVICE

I, Thomas G. Hungar, a member of the Bar of this Court, hereby certify that on June 29, 2012, I electronically filed the foregoing brief with the Clerk of Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

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