

## Results Are In: Year of the Horse Ends with a Record Fine of USD 975 Million for Qualcomm

On 10 February 2015, China's National Development and Reform Commission (NDRC) announced that it was imposing fines of RMB 6.088 billion (approximately USD 975 million) on Qualcomm for abusing its dominant position in the CDMA, WCDMA and LTE wireless communication standard essential patents (SEPs) licensing market and the baseband chip market. The NDRC's decision marked the conclusion of a 15-month investigation which commenced in November 2013.

Given the significance of this record-breaking fine and decision, the NDRC posted a public statement on its website and simultaneously held a press conference both of which provided some preliminary details of its investigation and decision. The complete Administrative Sanctions Decision will be published on a later date.

### Background

The NDRC first received complaints and reports from two US companies with regards to Qualcomm's abusive behaviour as early as 2009. The NDRC did not at this point initiate investigations, most likely due to the infancy of the Anti-Monopoly Law (AML) and its limited experience in dealing with the complexity of the interaction between the AML and intellectual property law. However, with the

substantive developments in 2012 and 2013, including Huawei/InterDigital and the drafting of the first guidelines for anti-monopoly enforcement in the intellectual property right (IPR) related area, the NDRC commenced investigations against Qualcomm following complaints and reports from a number of Chinese and foreign smart mobile device manufacturers in 2013.

### Qualcomm's abusive behaviour

According to the NDRC's public statement, Qualcomm was found to have a dominant position in (1) the markets for the licensing of CDMA, WCDMA and LTE wireless communication SEPs and (2) the market for the supply of baseband chips. The public statement does not provide details on how the relevant markets were defined nor market shares held by Qualcomm or how the NDRC established dominance. However, it is understood from a televised interview with an NDRC official that in the SEPs licensing market, Qualcomm was found to have 100 percent market share for each individual SEP, and over 50 percent market share for the supply of baseband chips.<sup>1</sup>

The NDRC concluded that Qualcomm abused its dominance in the two relevant markets as follows:

<sup>1</sup> Interview with NDRC available at <http://tv.cntv.cn/video/C10316/a3fea407396f408fab2037e9c8739875>.

MARKETS FOR CDMA, WCDMA AND LTE WIRELESS COMMUNICATION SEPs	MARKET FOR THE SUPPLY OF BASEBAND CHIPS
<p>Qualcomm charged unfairly high royalties by:</p> <ul style="list-style-type: none"> <li>refusing to provide to licensees a patent list for which they were charged royalties resulting in customers being charged royalties for expired patents;</li> <li>requiring licensees to grant cross licenses to it for free and refusing to deduct royalties or provide other consideration for such cross licenses; and</li> <li>charging royalties on the basis of the net wholesale selling price of an overall device.</li> </ul>	<p>Qualcomm attached unreasonable conditions to the sale of its baseband chips requiring, as a condition of supply, baseband chip customers to sign patent licensing agreements which contain no-challenge clauses. In the event a licensee did not sign Qualcomm's patent licensing agreement or disputed and brought suit against the licensing agreement, Qualcomm would refuse to supply its baseband chips.</p>
<p>Qualcomm tied non-SEP licenses to SEP licenses without justifiable reasons by refusing to separately license its SEPs and non-SEPs, forcing some of its licensees to buy the non-SEPs from Qualcomm.</p>	

Qualcomm was therefore found to have abused its power by engaging in excessive pricing, imposing unfair terms and bundling. The NDRC in its public statement concluded that Qualcomm's abusive behaviour eliminated and restricted market competition, impeded and stifled technology innovation and development, and harmed consumer interests. When released, the complete Administrative Sanctions Decision should provide valuable insights on the NDRC's interpretation of these provisions and procedural issues.

### Fines and rectification plan

Pursuant to section 47 of the AML, a company who abuses its dominance can be subject to a fine of between 1 percent to 10 percent of its annual revenue. According to the NDRC's public statement, Qualcomm's fine was 8 percent of its revenue in China in 2013 and was determined by considering a range of factors including the serious nature and extended duration of Qualcomm's abusive behaviour, its cooperation in the investigation and the voluntary rectification plan offered to the NDRC.

In addition to the fine imposed, which Qualcomm stated it will not contest, Qualcomm agreed to implement a rectification plan approved by the NDRC, the key terms of which are as follows:

- Qualcomm will offer licenses to its current 3G and 4G Chinese SEPs separately from licenses to its other patents and will provide patent lists during the negotiation process. If Qualcomm seeks a cross license from a Chinese licensee as part of such offer, it will negotiate with the licensee in good faith and provide fair consideration for such rights.
- For licenses of Qualcomm's 3G and 4G Chinese SEPs for branded devices sold for use in China, Qualcomm will charge royalties of 5 percent for 3G devices<sup>2</sup> and 3.5 percent for 4G devices<sup>3</sup> that do not implement CDMA or WCDMA, in each case using a royalty base of 65 percent of the net selling price of the device.
- Qualcomm will give its existing licensees an opportunity to elect to take the new terms for sales of branded devices for use in China as of 1 January 2015.
- Qualcomm will not require, as a condition of sale, customers of baseband chips to sign a license agreement containing unreasonable terms or prohibiting customers from challenging the license agreement.<sup>4</sup>

The fine imposed and the rectification measures suggest that the NDRC only imposed penalties on

<sup>2</sup> Including multimode 3G/4G devices

<sup>3</sup> Including 3-mode LTE-TDD devices

<sup>4</sup> However, this does not require Qualcomm to sell chips to any entity that is not a Qualcomm licensee, and does not apply to a chip customer that refuses to report its sales of licensed devices as required by its patent license agreement.

Qualcomm's abusive behaviours in China. This appears to be in contrast to the Huawei/InterDigital case, where the courts took the view that InterDigital's licensing practices in respect of its US SEPs had substantial, material and reasonably foreseen impact on the domestic production, export opportunity and export trade of Huawei and other Chinese companies, thus applying the AML to InterDigital's US SEPs licensing practices.

## Implications

The Qualcomm case is a milestone in Chinese AML enforcement. The enforcement approach should be of particular interest to antitrust authorities in other jurisdictions (e.g., EU, US and South Korea) which are reportedly investigating Qualcomm for similar abusive practices. Additionally, the decision may also impact other IPR holders (including SEPs and IPRs which constitute *de facto* standards) as the results set a precedent on what may be considered reasonable royalty rates and licensing practices in China. Furthermore, although the NDRC investigation has ended, there may be follow-on civil suits against Qualcomm in China by Chinese companies and consumer groups.<sup>5</sup>

The Qualcomm case demonstrates NDRC's willingness to impose significant fines in abuse of dominance cases, in contrast to its approach in the China Unicom/China Telecom case and the InterDigital case. It also confirms the NDRC's growing sophistication with its ability to tackle the complexity of the interplay between competition principles and intellectual property law.

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<sup>5</sup> The amended Consumer Rights and Interests Protection Law in China has provided the consumer groups with facility to bring suits on behalf of Chinese consumers who purchased over 320 million units of smartphones in 2013.

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