

# Tackling unreasonable behaviour

**John H Choi** and **Changhun Lee** of **Shin & Kim** look at amended guidelines on the unreasonable exercise of IP rights

**T**he Korea Fair Trade Commission (KFTC) amended the Review Guidelines on Unreasonable Exercise of Intellectual Property Rights (IPR Guidelines) on December 17 2014. Although the IPR Guidelines lack binding force, they are meaningful in that they provide the specific illegality standards for the KFTC to decide individual issues, increasing clarity and consistency in its enforcement. The KFTC expects that the amended Guidelines will allow more effective regulation of non-practising entities (NPEs) and global companies' abuses of monopolistic power through patent rights, and greater protection of domestic companies from abuses of patent rights. The KFTC stated that it plans to actively monitor abuses of patent rights based on the amended IPR Guidelines.

## Basic principles

The basic principles of the IPR Guidelines have been substantially revised, and the regulation standards for the exercise of IPRs generally seem to have become stricter. There are several amendments to the basic principles, including the addition of the definition of 'the proper exercise of IPRs' (excluded from the application of the Monopoly Regulation and Fair Trade Act – MRFTA – under article 59).

## The regulation standards for the exercise of IPRs seem to have become stricter

While the previous version of the IPR Guidelines focused on unfair trade practices, the amended Guidelines limit the scope of their application to market dominant companies. The IPR Guidelines state that market dominant power is not automatically presumed for IPR holders and that an IPR holder's market dominant power does not automatically imply that their exercise of IPRs violates the MRFTA.

In determining whether the exercise of IPRs violates the MRFTA, the amended IPR Guidelines now use 'anti-competitive effects', instead of the previously used 'effect of impeding fair trade' (this included both anti-competitiveness and unfairness).

Further, the amendment clarifies that exercise of IPRs has both positive and negative effects (both pro-competitive and anti-competitive).

## Illegality standards

The previous version of the IPR Guidelines included unfairness as well as anti-competitive effects as the standard in determining unreasonableness. In the amended IPR Guidelines, the standard for determining unreasonableness of IPR use has been unified as anti-competitiveness. This is an important acknowledgement that the regulation of IPR use should be consistent with the fundamental purpose of antitrust law – protecting competition. Based on this amendment, the KFTC now, in principle, should prove that 'conducts at issue restricted competition', which is beyond the level of simply proving 'conducts at issue caused detriments to other companies'. This amendment is expected to substantially reduce the scope of IPR use subject to application of the IPR Guidelines.

The amended IPR Guidelines state that:

Anti-competitive effects of exercise of IPRs in the relevant market are determined by comprehensively considering whether the exercise of IPRs causes price increase or output reduction, restriction on the variety of products or services, hindrances to innovation, foreclosure effect, increase of competitors' expenses, or possibility of such effects being created in the relevant market. These consideration factors are examples of criteria that are important in determining anti-competitive effects, and it does not mean that a factor not included in the list cannot be considered in determination of anti-competitive effects.

## Package licensing and tying

The amended IPR Guidelines expressly refer to the pro-competitive nature (efficiency-enhancing effects) of package licensing, while also mentioning that package licensing can possibly constitute tying. In particular, the Guidelines provide the example of licensing standard essential patents (SEPs), on the condition of also licensing unnecessary non-SEPs, and state that in such case, the licensing is highly likely to constitute tying.

The amended IPR Guidelines state that:

Package licensing – in licensing one or more closely related patents, licensing multiple patents together – can have pro-competitive effects that enhance efficiency in the relevant market through, among others, reduction of search costs for relevant technologies, reduction of costs of negotiation with the patent holders, reduction of risks of patent infringement suits, and elimination of uncertainty regarding R&D investments. However, forcing licensees to also purchase unnecessary patents can constitute tying. In particular, when the licensee wants to obtain a license for subject non-SEP's substitute technologies from a third party, licensing unnecessary non-SEPs together with the SEP may be unreasonable.

## Standard technologies

The previous version of the IPR Guidelines included provisions regulating

the exercise of patent rights related to standard technologies. These included: in the standardisation process, unreasonably agreeing on conditions regarding the price, output volume, geographic regions, counterparties; unreasonably not disclosing information of patent applications or registrations to increase the possibility of being designated as the technical standard or to avoid prior consultation on licence conditions; unreasonably refusing to license; and unreasonably imposing discriminatory conditions or unreasonable level of royalties.

The amended IPR Guidelines include additional provisions to regulate the following conducts: (i) excluding competitors through evading or circumventing the fair, reasonable, and non-discriminatory (Frاند) commitments; and (ii) unreasonably restricting licensees' exercise of their patent rights or unreasonably requiring licensees to cross-license their non-SEPs.

## The amendment clarifies that exercise of IPRs has both positive and negative effects

### SEP holders' injunction claims

The IPR Guidelines state that the Frاند commitment imposes on SEP holders the duty to negotiate the licence agreement in good faith with the potential licensee in accordance with the Frاند terms.

The amended IPR Guidelines provide that when an SEP holder who made the Frاند commitment brings an injunction claim against a willing licensee (a potential licensee who is willing to receive the licence), the claim can be found anti-competitive and outside the scope of proper exercise of patent rights. In particular, if the SEP holder does not diligently satisfy the duty to negotiate and bring an injunction claim, such conduct may be unreasonable. However, when the injunction claim is the only means of relief or when the injunction claim is against an unwilling licensee (a potential licensee who is not willing to receive the licence), there is a low probability of the claim being found unreasonable.

To a significant degree, the new provision appears to reflect the Seoul Central District Court's decision from *Samsung Electronics v Apple Korea* of August 24 2012 (case 2011Gahap39552). The court upheld Samsung's patent infringement claim for its SEPs based on the fact that despite its knowledge of the SEPs, Apple used them without requesting the licence from Samsung.

It is also notable that a definition of SEP has been newly added to the Guidelines.

The amended IPR Guidelines state that:

SEPs are patents to implement standard technologies – the patents, licenses for which are essential in manufacturing products or providing services that requires standard technologies...

When SEP holders do not diligently satisfy the duty to negotiate and bring an injunction claim, the conduct may be found unreasonable. In determining whether an SEP holder diligently satisfied its duty to negotiate, the following factors can be considered:

whether the SEP holder officially made an offer to negotiate to the potential licensee, whether the negotiation period with the potential licensee was appropriate, whether the licence conditions offered to the potential licensee were reasonable and non-discriminatory, whether the parties agreed to go through the court or an arbitrator, if the parties failed to agree on the licence terms, etc.

If an SEP holder's injunction claim is not allowed against an unwilling licensee (a potential licensee who is not willing to receive the licence), the potential licensee may not diligently negotiate or delay or avoid payment of royalties (ie reverse hold-up). Also, in special circumstances, the injunction claim may be the only means of relief for the SEP holder. Therefore, in the following cases, there is a low probability of the SEP holders' injunction claims being found unreasonable:

(1) When the potential licensee refuses to follow the decision of the court or the arbitrator, or refuses to enter the licence agreement on Frاند terms even though objective Frاند terms have been found, such as in the process of the case at the court or the arbitrator.

(2) When the injunction claim is the only means of relief because it is difficult to expect compensation because, among others, the potential licensee is on the verge of bankruptcy.

### NPE's exercise of patent rights

Another noteworthy point in the amended IPR Guidelines is that new regulation provisions on NPEs' exercise of patent rights have been added (in the Guidelines, NPEs are called companies specialising in patent management). In defining an NPE, the Guidelines state that: (i) NPEs do not manufacture, sell or provide services using the patented technologies; and (ii) earn profits through the exercise of their patent rights against those using the patents.

The amended IPR Guidelines provide types of anti-competitive conducts of NPEs, including: imposing excessive royalties; for patent rights obtained from a third party, denying the application of Frاند conditions that were applied to the previous patent holder, while imposing unreasonable levels of royalty; using deceitful means to raise patent infringement suits; and, after a patent holder transfers its patent rights to an NPE, using the NPE to abuse the patent rights (privateering). For privateering, the patent holder is considered the subject of the violations, but at times NPEs can also be the subject of the violations.

The general assessment is that NPE activities have not been a significant problem in Korea, but it is possible that through the amendment, the KFTC may start to actively enforce the new regulation provisions on NPEs. Therefore, it would be necessary to pay greater attention to the KFTC's activities in this regard.

The amended IPR Guidelines state that a:

'Company specialising in patent management' is a company that does not manufacture or sell goods nor provide services using patented technologies but earns profits by exercising its patent rights against, among others, those implementing the patents...

The company specialising in patent management's main business model is building a strong patent portfolio by purchasing patent rights from third parties and earning profits using the portfolio by providing licences to other companies or using patent infringement suits. The company specialising in patent management purchases, manages etc patents of those who lack the ability to exercise their patent rights or do not have the intent to commercialise the patents

on their own – such as individuals, small- and mid-sized companies, research institutions – and through these means, ensure that they receive proper compensation and provide incentives to invent. Also, by playing the role of middlemen to ensure the patent rights are transferred to the party that needs the patents, the company specialising in patent management can vitalise the patent technology transactions and contribute to capitalisation of patent rights.

However, despite these pro-competitive effects, as the company specialising in patent management does not engage in manufacturing, there is no need to enter into cross-licence agreements with the counterparties and there is low risk of infringement suits by the counterparties. Therefore, there is higher risk of the company specialising in patent management abusing its patent rights, compared to the patent holders in general. In particular, the following conducts can be found outside the proper exercise of rights and to have concerns for anti-competitive effects.

A. The standards for abusing patent rights as set forth in these Guidelines basically apply to the company specialising in patent management's exercise of patent rights, just as the patent holders in general's exercise of patent rights. Therefore, besides the type of conducts listed below, if the company specialising in patent management engages in the conducts specified in sections III.1 through 6, the conduct may be outside the proper scope of exercise of patent rights. Also, if a patent holder other than the company specialising in patent management engages in the conducts below, it may be outside the proper scope of exercise of patent rights...

## The general assessment is that NPE activities have not been a significant problem in Korea

Because the company specialising in patent management does not engage in manufacturing, the company specialising in patent management, compared to regular patent holders, has the incentive or ability to impose excessive royalties. Therefore, the company specialising in patent management's conducts are more likely to be found unreasonable than those of regular patent holders. In determining whether the royalty level is reasonable, various factors can be considered including the objective technological value of the patent, the royalty the patent holder receives from other licensees, the amount of royalty licensees pay for similar patents, characteristics and scope of the licence agreements, duration of the licence, and profitability of the products manufactured using the patents.

In particular, in case of royalties for SEPs (including de facto standard) licensed on Frand terms as described in Section III 5 A, the conduct may be unreasonable.

B. With respect to patent rights obtained from a third party, denying the application of Frand conditions that applied to the previous patent holder, while imposing unreasonable level of royalty compared to the regular transactional practices

C. Agreeing with the multiple companies that established the company specialising in patent management through a consortium

to unreasonably reject licensing patents to the companies that did not participate in the consortium or to license on discriminatory terms

D. Raising patent infringement suits or sending warning letters for patent infringement through deceptive means, including concealing, omitting, or causing confusion regarding facts crucial for the counterparty to respond to the company specialising in patent management's exercise of patent rights.

An example of such conduct is sending identical demands for royalties to multiple parties through a shell company where it is impossible to know who the patent holder is, without providing specific details on the patents that have been allegedly infringed upon. In particular, when the company specialising in patent management does not own the patent rights, is not in the position to exercise the patent rights, or has expired patents, demanding royalties or threatening lawsuits is highly likely to be found unreasonable.

E. After the patent holder transfers patent rights to the company specialising in patent management, making the company specialising in patent management to take certain conducts, such as 7 A or B of these Guidelines, against other companies

In this case, the patent holder, in principle, is the subject of the violation. However, the company specialising in patent management can also be the subject of the violation comprehensively considering the relationship between the patent holder and the company specialising in patent management, the specific details of the unreasonable conducts, the level and type of participation by the company specialising in patent management in the unreasonable conducts.

### Other provisions

There are a few other significant provisions in the amended IPR Guidelines. For example, in the amended IPR Guidelines, the provisions regulating excessive royalties for licence agreements in general have been removed. There has been much criticism in Korea for the regulation of pricing abuses, with almost no cases of the KFTC's regulation of pricing abuses in the past 20 years or so. However, unlike licence agreements in general, the excessive royalty provisions still remain for the exercise of SEP rights and NPE's exercise of patent rights. Also, the MRFTA (as well as the Enforcement Decree) contains express provisions on excessive pricing.

The amended Guidelines also provide a definition of grantbacks, their pro-competitive and anti-competitive effects, and the standards to determine unreasonableness of grantbacks.

The amended IPR Guidelines state that:

Grantbacks refer to, in licence agreements, when the licensee improves technologies relevant to the licence, requiring the licensee to transfer or licence the improved technologies to the patentee. Grantbacks can be exclusive so as to transfer rights to use the improved technologies only to the patentee, and they can also be non-exclusive so that the improved technologies can be transferred to other companies in addition to the patentee. These grantbacks, particularly when they are non-exclusive, can have pro-competitive effects. Specifically, providing the patentee the compensation for grant of patents on improved technologies can expedite early-stage innovation, allows licensees and patentees to share the risk of improving technologies, and enables additional innovation based on the licensed technologies.

However, grantbacks can reduce the licensees' incentives to conduct R&D and restrict competition in the relevant market. In determining whether a grantback restricts competition and falls outside of the proper scope of rights, the following factors are relevant.

- (1) Whether the grantback is exclusive or non-exclusive;
- (2) If exclusive, whether the licensee has the right to use the improved technologies ;
- (3) Whether the scope of the grantback includes improvements that are not relevant to the licensed patented technologies;
- (4) Duration of the grantback;
- (5) Whether the grantback is royalty-free;

(6) Whether either party has market dominant power and whether they are competitors;

(7) The effect of the grantback on incentive to conduct R&D.

In relation to relevant markets for exercise of IPRs, the previous version of the IPR Guidelines only included the product market and technologies market, and the concept of innovation market was newly added through the amendment. Innovation market refers to relevant markets for specific R&Ds for new or improved products, technologies, or processes.

The KFTC expects that the addition of the concept of innovation market will facilitate the proper analysis of the effects of the exercise of IPRs on competition, which was formerly difficult in terms of product and technology markets.



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