Microsoft Loses Big In MP3 Patent Suit
$1.52 Billion Penalty Could Be Harbinger

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A federal jury in San Diego yesterday ordered Microsoft to pay $1.52 billion to Alcatel-Lucent for violating two patents for a technology used by hundreds of companies that allows users to play digital music on computers, cellphones and other portable devices.

The judgment, which lawyers from both sides called the largest patent award ever, raised the prospect that scores of other companies could now be financially liable for using the popular MP3 format.

"Any of the companies that have licensed and implemented that technology have to have great concern about this verdict," said Thomas W. Burt, a Microsoft vice president and deputy general counsel.

Alcatel-Lucent argued that it held the rights to the technology because it was developed at Bell Laboratories, which later became part of Lucent. Alcatel bought Lucent last year. The company successfully argued that Microsoft infringed on the patents by including the digital music technology in its Windows operating system starting in 1998. The same technology later was used in Microsoft's Windows Media Player and is included in the Windows Vista operating system, which was released to the public last month.

Microsoft countered that it had properly licensed the technology from Germany's Fraunhofer Institute, which was involved with Bell Labs in developing aspects of the MP3 format. Only after Microsoft and other companies made licensing agreements with Fraunhofer did Alcatel-Lucent raise its claim, Microsoft argued.

"As a result of the verdict today, the jury determined the patents were developed by Bell Labs and not in conjunction" with Fraunhofer, said Joan Campion, a spokeswoman for Alcatel-Lucent. "We've made strong arguments supporting our view and we are pleased by the court's decision."

Alcatel-Lucent said it would ask for a larger judgment against Microsoft. The $1.52 billion in damages was determined by calculating 0.5 percent of all sales of computers equipped with Windows and lacking the proper licensing from mid-2003 through 2005. John Desmarais, Alcatel-Lucent's lead trial lawyer, said the company would ask that 2006 sales be included.

Burt said Microsoft not only would appeal the jury's findings of patent infringement but also would challenge the amount of the damages. He said it was improper to calculate damages based on the value of computer sales rather than the lesser value of sales of the Windows operating system. He also said that the jury improperly included overseas sales of computers in the calculations.

The issue of whether U.S. patent law can be extended to products made abroad figured prominently this week in arguments before the U.S. Supreme Court in a separate case pitting Microsoft against AT&T.
The verdict yesterday came in one of several patent lawsuits that Alcatel-Lucent brought against Microsoft. Others involve video-file, color graphics and computer interface technologies. Several billion dollars of additional damages could ride on the outcome of these suits, lawyers said.

The judgment surprised industry experts, who said they had not been following the case closely.

"Most of us thought this was going to go bye-bye," technology analyst Rob Enderle said. He said he expected Alcatel-Lucent to approach other companies using MP3 technology and use the verdict "like a club" to collect fees.

About 400 companies have similar licensing agreements with Fraunhofer, according to Thomson Technology, a San Diego company that identifies itself as the "licensing representative of MP3 patents and software of the Fraunhofer Institute." Those companies include Apple, Creative Technology, Real Networks, Palm and Samsung.

Alcatel-Lucent and its lawyers would not say whether they plan to target more companies, but Desmarais signaled that others using the audio-file technology could be vulnerable.

"For anyone who implements the standard, the same arguments would apply," he said.

*Staff writer Mike Musgrove contributed to this report.*

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