

Supersize Me: Damages Claims in Patent Litigation

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I. WHAT YOU SHOULD ALREADY KNOW

A. Statutory Basis for Patent Damages

35 U.S.C. § 284 provides the basis for patent damages. It states:

Upon finding for the claimant the court shall award the claimant damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court.

Under section 284, the court also has the authority to increase damages by an amount up to three times that awarded as compensatory damages. In addition, attorneys' fees may be awarded in certain circumstances that the court determines are exceptional.¹

B. Case Law

1. Reasonable Royalties

Most of the law of damages is found in case law.² As noted in the statute, the minimum amount to be awarded is a reasonable royalty when infringement is found. The seminal case of *Georgia-Pacific* is still the most often-cited authority for determining a reasonable royalty, despite being 40 years old.³ *Georgia-Pacific* provides a 15-factor test that is often relied upon in determining a reasonable royalty. The laundry list of factors laid out in *Georgia-Pacific* includes the following elements:

1. The royalties received by the patentee for the licensing of the patent in suit.
2. The rates paid by the licensee for licenses on comparable patents.
3. The nature and scope of the license, as exclusive or non-exclusive, and size of territory covered.
4. The licensor's established policy to grant licenses or retain a proprietary position in the marketplace.
5. The commercial relationship between the licensor and licensee, such as, whether they are competitors.
6. The effect of selling the patented specialty in promoting sales of other products of the licensee—i.e., ability to enjoy conveyed sales.
7. The duration of the patent and the term of the license.
8. The established profitability of the product made under the patent, its commercial success, and its current popularity.

¹ 35 U.S.C. § 285.

² See, e.g., *Compensatory Damages Issues in Patent Infringement Cases: A Handbook for Federal District Court Judges*, available at www.nationaljuryinstructions.org/damages.

³ *Georgia-Pacific Corp. v. United States Plywood Corp.*, 318 F. Supp. 1116 (S.D.N.Y. 1970), modified and aff'd, 446 F.2d 295 (2d Cir. 1971), cert. denied, 404 U.S. 870 (1971).

9. The utility and advantages of the patent property over the old modes or devices.
10. The nature and benefits of the patented invention.
11. The extent to which the infringer has made use of the invention.
12. The portion of the profit or of the selling price that may be customary in the particular business or in comparable businesses to allow for the use of the invention or analogous inventions.
13. The portion of the realizable profit that should be credited to the invention as distinguished from non-patented elements, the manufacturing process, business risks, or significant features or improvements added by the infringer.
14. The opinion testimony of qualified experts.
15. The amount that a licensor (such as the patentee) and a licensee (such as the infringer) would have agreed upon (at the time the infringement began) if both had been reasonably and voluntarily trying to reach an agreement; that is, the amount which a prudent licensee—who desired, as a business proposition, to obtain a license to manufacture and sell a particular article embodying the patented invention—would have been willing to pay as a royalty and yet be able to make a reasonable profit and which amount would have been acceptable by a prudent patentee who was willing to grant a license.

Commentators in the field have studied the number of times that reasonable royalties are awarded in patent cases, and have determined that a reasonable royalty is the most-often awarded remedy in patent cases.⁴

There are two primary factors that drive the amount of reasonable royalties: the royalty *rate* and the royalty *base* to which the rate is applied. The major wrinkle in determining the royalty base is whether the dollars associated with the entire sale are to be included, or whether only a portion of the sale is to be used in the royalty base. There are a number of cases that provide guidance on the size of the royalty base, as discussed below.

2. Lost Profits

In certain cases, a patent holder who demonstrates infringement may be entitled to its lost profits as its remedy. It is also possible to have a mixed award, and receive lost profits on some portion of the lost sales and a reasonable royalty on the remainder.

The most commonly cited test for determining what the patent holder would have made in the absence of infringement is set forth in the *Panduit* case. *Panduit* teaches that, to obtain lost profits, the patentee must demonstrate the following:

1. demand for the patented product;

⁴ See, e.g., *PriceWaterhouseCoopers 2009 Patent Damages Study*, FTC Panel Discussion at 4 (February 11, 2009), available at www.ftc.gov/bc/workshops/ipmarketplace/feb11/docs/alevko.pdf.

2. absence of acceptable non-infringing substitutes (or apportionment of the infringer's market share amongst the players who offer acceptable substitutes);
3. capacity to meet the demand (includes manufacturing and marketing capability); and
4. the amount of lost profits.⁵

3. The Entire Market Value Rule

The entire market value rule is a concept that concerns whether only the value of the patented invention should be included in the damages calculation, or whether a broader scope of sales applies. The entire market value rule applies both to damages calculations made under a reasonable royalty basis (in terms of sales of which products should be included in the royalty base) as well as lost profits (in terms of which sales should be used as a basis for determining the lost profits).

The concepts underlying the entire market value rule were explored in detail by the Federal Circuit in the *Rite-Hite* case.⁶ In *Rite-Hite*, the Court explained that where the patented feature is the basis for consumer demand of the entire product or process, then damages should be based on the full value of the product or process.⁷

4. Willfulness and Damages Multipliers

Under section 284, the Court is also granted the power to increase damages by an amount up to three times that awarded as compensatory damages. In addition, attorneys' fees may be awarded in certain circumstances that the Court determines are exceptional.⁸ Generally, cases were found to be exceptional only where willful infringement or other egregious behavior existed. In 2007, the Federal Circuit decided *In re Seagate*, in which the Court determined that for willful infringement to exist, the patent holder must demonstrate by clear and convincing evidence that the infringer acted with objective recklessness.⁹

C. Proposed Legislation on Patent Reform and Potential Effect on Damages

Proposed legislation on Patent Reform has been percolating through the system for the past three years. Initially introduced in April, 2007, S. 1145 (Senate) and H.R. 1908 (House) have undergone a number of revisions. The current proposed Patent Reform Bill (S.

⁵ *Panduit Corp. v. Stahlin Bros. Fibre Works, Inc.*, 575 F.2d 1152 (6th Cir. 1978).

⁶ *Rite-Hite Corp. v. Kelley Co., Inc.*, 56 F.3d 1538, 1549 (Fed. Cir.) (*en banc*), *cert. denied*, 116 S. Ct. 184 (1995).

⁷ The corollary rule to the entire market value rule is the concept of apportionment. Where the patented product or process is not the entire basis for consumer demand, then damages must be apportioned between the value of the patented feature and the remained, with damages being awarded only on the value that the patented feature provides.

⁸ 35 U.S.C. § 285.

⁹ *In re Seagate Tech.*, 497 F.3d 1360, 1371 (Fed. Cir. 2007).

515) was published by the Senate Judiciary Committee on March 4, 2010 (to amend the March 2009 version of S. 515).

Relevant provisions in the currently pending legislation that would affect the determination of compensatory damages include the following:

1. A requirement that the parties state at the time of the final pretrial order the methodologies and factors the parties propose to have the court instruct the jury on with respect to damages;
2. The ability of the court to determine, *sua sponte*, or on motion of either party, whether one or more of a party's damages claims lacks a legally sufficient evidentiary basis (the purpose of the inquiry being to limit the introduction of any evidence on damages which is deemed to lack a sufficient evidentiary basis); and
3. The ability of either party to request that the trial be sequenced so that the trier of fact decides the issues of infringement and validity before the issues of damages and willful infringement (the court is instructed to grant such request absent good cause to reject it).¹⁰

A previous version of the bill also contained a provision that essentially overturned the entire market value rule as enunciated in the *Rite-Hite* case. Such language is no longer in the present draft of the bill.

Relevant provisions in the currently pending legislation that would affect the determination of willfulness include the following:

1. Codification of the "objectively reckless" standard of *In re Seagate*;
2. Codification that willfulness be pled with particularity under Rule 9(b);
3. Creating heightened standards with respect to notice of infringement, including a statement that an infringer's knowledge of a patent alone is insufficient to invoke willfulness and requiring pre-suit notice to include the identification of the patent, the product or process that is accused, and an explanation with particularity as to how the product or process infringes the patent; and
4. Directing the court not to increase damages if the court determines the case is close on issues of infringement, validity, or enforceability.

II. LATEST DEVELOPMENTS

The following section provides a summary of the key damages verdicts and decisions in the last year.

¹⁰ Note, however, that the sequencing of a trial is not to affect the timing of discovery.

A. Federal Circuit Decisions

1. Lucent

The Federal Circuit provided substantial guidance on patent damages in September of 2009 when it decided *Lucent Technologies, Inc. v. Gateway, Inc.*, and vacated a jury’s \$358 million damages award as based mainly on “speculation or guesswork.”¹¹ The court explained that if a patentee relies on previous license agreements for evidence of a reasonable royalty, the evidence must demonstrate how the previous license agreements are comparable.¹² With respect to the entire market value rule, the Federal Circuit reiterated that a patented feature must be the basis for demand, but explained that it is not error to use the market value of the entire product to determine a royalty as long as it accounts for the proportion of the product represented by the infringing feature.¹³

In that case, Lucent sued several companies in the Southern District of California for infringement of its ’356 patent, which is directed to a method of entering information into fields on a computer screen without using a keyboard (“the date-picker”).¹⁴ Lucent alleged that Microsoft indirectly infringed the patent by selling approximately 110 million units of Microsoft Outlook, Microsoft Money, and Windows Mobile for about \$8 billion.¹⁵ At trial, Lucent argued that it was entitled to a running royalty of 8% of the sales revenue for the accused products, or \$561.9 million.¹⁶ Microsoft countered that a lump-sum payment of \$6.5 million was the correct amount.¹⁷ The jury awarded a \$357,693,056.18 lump-sum for damages.¹⁸ The Southern District of California declined to award Microsoft a new trial or judgment as a matter of law on damages.¹⁹ Microsoft appealed.

The Federal Circuit agreed with Microsoft that the damages calculation lacked sufficient evidentiary support by focusing on the Outlook product and evaluating the relevant *Georgia-Pacific* factors. The court considered the eight license agreements that were admitted at trial in connection with *Georgia-Pacific* factor two—rates paid by the licensee for the use of other patents comparable to the patent in suit—but found that the previous license agreements did not support the damages award.²⁰ The court explained that the previous license agreements were created from events very different than the one in the *Lucent* case (one licensed IBM’s entire patent portfolio protecting its dominance in the personal computer market and there was little evidence regarding the other three), and that

¹¹ 580 F.3d 1301 (Fed. Cir. 2009).

¹² *Id.* at 1328.

¹³ *Id.* at 1339.

¹⁴ *Id.* at 1308-17.

¹⁵ *Id.* at 1324.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.* at 1333.

¹⁹ *Id.*

²⁰ *Id.* at 1325-32.

there was little evidence of how previous running-royalty licenses would be probative of a lump-sum payment.²¹

With respect to factors 10—nature of the patented invention—and 13—portion of the realizable profit that should be credited to the invention—the court concluded that the patented invention was only a “tiny feature” and that it is “inconceivable to conclude, based on the present record, that the use of one small feature, the date-picker, constitutes a substantial portion of the value of Outlook.”²² Instead, “numerous features other than the date-picker appear to account for the overwhelming majority of the consumer demand and therefore significant profit” and “Outlook’s date-picker feature is a minor aspect of a much larger software program and that the portion of the profit that can be credited to the infringing use of the date-picker tool is exceedingly small.”²³

With respect to factor eleven—extent to which the infringer has made use of the invention—the Federal Circuit agreed with Lucent that post-infringement evidence is probative in certain circumstances, but held that the “evidence of record is conspicuously devoid of any data about how often consumers use the patented date-picker invention.”²⁴ The court reasoned that “[t]he damages award ought to be correlated, in some respect, to the extent the infringing method is used by consumers. . . . because this is what the parties to the hypothetical negotiation would have considered.”²⁵ The court explained that the remaining factors tended to offset each other and concluded that it had the “unmistakable conclusion” that the jury’s damages award was not supported by the evidence and was instead based on guesswork.²⁶

The court next considered Microsoft’s argument that the jury erroneously applied the entire market value rule, which allows for the recovery of damages based on the value of an entire apparatus containing several features when the patented feature constitutes the basis for customer demand.²⁷ Although the jury indicated on the verdict form that its damages award was a lump-sum reasonable royalty, the court agreed with Microsoft that it appeared the jury applied a royalty percentage to the total sales of the software.²⁸ The court explained that it would have been error for the jury to apply the entire market value rule to the value of the software because Lucent did not prove that the patent-related feature was the basis for

²¹ *Id.* at 1326-32 (“Second, the jury heard little factual testimony explaining how a license agreement structured as a running royalty agreement is probative of a lump-sum payment to which the parties would have agreed. Third, the license agreements for other groups of patents, invoked by Lucent, were created from events far different from a license negotiation to avoid infringement of the one patent here, the Day patent.”).

²² *Id.* at 1332.

²³ *Id.* at 1332-33.

²⁴ *Id.* at 1333-34.

²⁵ *Id.* at 1335.

²⁶ *Id.* at 1336.

²⁷ *Id.* at 1337-39.

²⁸ *Id.* at 1335.

customer demand, as the evidence demonstrated that no one bought the product for the patented feature.²⁹

But the court held that it is appropriate to calculate a royalty amount using the value of the entire commercial embodiment “as long as the magnitude of the rate is within an acceptable range.”³⁰ For example, the court explained, it would have been an acceptable methodology for calculating damages if the jury had awarded Lucent less than \$6.5 million—the amount Microsoft proposed—using a 0.1% royalty on the entire market.³¹ The court held that “[t]here is nothing inherently wrong with using the market value of the entire product, especially when there is no established market value for the infringing component or feature, so long as the multiplier accounts for the proportion of the base represented by the infringing component or feature.”³² The court then vacated the jury’s damages award and remanded the case for a new trial.³³

Microsoft filed a petition for certiorari in February of 2010, but did not touch on the damages award.³⁴

2. i4i

In another recent damages case, the Federal Circuit affirmed a jury’s award of \$200 million in damages against Microsoft, although it suggested that the outcome might have been different if Microsoft had moved for judgment as a matter of law before the trial court.³⁵ In that case, i4i sued Microsoft in the Eastern District of Texas, asserting that Microsoft Word’s XML editing capabilities infringed i4i’s ’449 patent.³⁶ At trial, i4i relied on the testimony of Dr. Wagner, who opined that the reasonable royalty rate was \$98 for the 2.1 million infringing word products—an estimate of business users who “really needed” XML per Microsoft’s survey expert Dr. Wecker—for a total damages amount of \$200 million.³⁷ Dr. Wagner selected the \$98 proposed reasonable royalty by looking at the “benchmark” product of XMetaL, which sold for \$499, and Microsoft’s profit margin of 76.6%.³⁸ He asserted that any licensing fee would be a fraction of the profits on the benchmark product and that 25% of Microsoft’s profits, were it selling the \$499 benchmark and making a 76.6% profit, would be \$96.³⁹ He then applied the *Georgia-Pacific* factors to that rate, asserting that the royalty should be between \$96 and \$98.⁴⁰ Microsoft countered that the rate was

²⁹ *Id.* at 1336-39.

³⁰ *Id.* at 1338-39.

³¹ *Id.* at 1339.

³² *Id.*

³³ *Id.*

³⁴ *Microsoft Corp. v. Lucent Technologies, Inc.* (Sup. Ct. Feb. 19, 2010).

³⁵ *i4i Limited Partnership v. Microsoft Corp.*, 589 F.3d 1246 (Fed. Cir. 2009).

³⁶ *Id.* at 1256.

³⁷ *Id.* at 1268, 1270.

³⁸ *Id.* at 1298.

³⁹ *Id.*

⁴⁰ *Id.* at 1268-69.

exorbitant, as it had sometimes sold Word for as little as \$97 and paid \$1 million to \$5 million to license other patents, much less than the \$200 million i4i proposed.⁴¹

Before the case was submitted to the jury, Microsoft moved for judgment as a matter of law on several issues, but not on damages.⁴² The jury determined that the patent was valid, that Microsoft's Word infringed, that the infringement was willful, and awarded \$200 million in damages.⁴³ After trial, Microsoft renewed its motions for judgment as a matter of law and moved for a new trial on those issues and on damages and the court's evidentiary rulings. The district court denied those motions and awarded \$40 million in enhanced damages.⁴⁴

In December of 2009, the Federal Circuit affirmed the district court's decision.⁴⁵ The court rejected Microsoft's challenges to the admissibility and methodology of Dr. Wagner's testimony, acknowledging that there were weaknesses in Dr. Wagner's calculations, but explaining that Microsoft's issues were with his conclusions and not his methodology.⁴⁶ The court concluded that the testimony was sufficient under Rule 702 and the district court did not abuse its discretion in allowing him to testify.⁴⁷ The court also found that the survey expert i4i relied on to calculate the number of infringing business users who "really needed" XML was sufficient under Rule 702.⁴⁸ The court determined that the survey expert's methodology met the minimum standards of relevance and reliability, as both of Microsoft's experts opined that it underestimated the amount of infringing use.⁴⁹ Thus, the court concluded, the district court did not abuse its discretion in admitting the survey.⁵⁰

The court next considered Microsoft's challenge to the reasonableness of the damages award. The court first explained that although Microsoft objected to the size of the damages award, the Federal Circuit could not reach that question because Microsoft did not file a pre-verdict judgment as a matter of law on damages pursuant to Rule 50.⁵¹ The court suggested that if Microsoft had filed such a motion, "it is true that the outcome might have been different."⁵² The court concluded that Microsoft was not entitled to a new trial under the "narrower standard" and "more searching review" of a request for a new trial because the jury's damages award did not exceed the maximum amount calculable from the evidence at

⁴¹ *Id.* at 1268.

⁴² *Id.* at 1256.

⁴³ *Id.*

⁴⁴ *Id.* at 1257.

⁴⁵ *Id.* at 1268, 1270.

⁴⁶ *Id.* at 1269.

⁴⁷ *Id.* at 1270.

⁴⁸ *Id.* at 1270.

⁴⁹ *Id.* at 1271-72.

⁵⁰ *Id.* at 1272.

⁵¹ *Id.*

⁵² *Id.*

trial.⁵³ The court explained that while the damages award was high, it was supported by the evidence at trial, including the testimony of Dr. Wagner and Dr. Wecker.⁵⁴

Microsoft sought rehearing and en banc review, appealing, among other issues the damages award.⁵⁵ The court granted a rehearing in March of 2010, but only amended its injunction decision.⁵⁶ The court denied Microsoft's request for en banc review on April 1, 2010.⁵⁷

3. ResQNet

Another recent Federal Circuit decision addressing damages is *ResQNet.com, Inc. v. Lansa, Inc.*⁵⁸ In that case, ResQNet sued Lansa in the Southern District of New York, accusing Lansa's NewLook software of infringing ResQNet's '075 patent and another patent.⁵⁹ At a bench trial, ResQNet relied on its damages expert, Dr. Jesse David, who focused on the first *Georgia-Pacific* factor—royalties received by the patentee from existing licenses.⁶⁰ He relied on seven previous ResQNet licenses, five of which did not include the patents-in-suit or claimed technology and instead provided finished software products and source code as well as services such as training, maintenance, marketing, and upgrades.⁶¹ In the five “re-branding” licenses that did not include the patents-in-suit, the companies reserved the right to re-brand ResQNet's products before resale, for rates up to 25% to 40% (the exact amounts were under a protective order).⁶² The remaining two licenses arose out of litigation over the patents-in-suit.⁶³ One of those licenses was a lump-sum payment, and another was a straight rate-based license for “substantially less than” 12.5% (the court did not provide the exact amounts).⁶⁴ Dr. David considered some of the remaining *Georgia-Pacific* factors, but opined that “[f]or the most part, the other factors have no real impact here.”⁶⁵ Dr. David proposed a reasonable royalty rate of 12.5%, explaining that his proposed rate was “somewhere in the middle” of the “re-branding” licenses and the straight rate-based licenses.⁶⁶ Lansa did not offer a damages expert in response.⁶⁷

⁵³ *Id.* at 1273.

⁵⁴ *Id.*

⁵⁵ Microsoft's Combined Petition for Panel Rehearing and Rehearing En Banc, 2010 WL 387922 (Jan. 8, 2010).

⁵⁶ *i4i Ltd. P'ship. v. Microsoft Corp.*, No. 09-1504, ___ F.3d ___, 2010 WL 801705 (Fed. Cir. Mar. 10, 2010).

⁵⁷ *i4i Limited Partnership v. Microsoft Corp.*, No. 09-1504 (Apr. 1, 2010).

⁵⁸ *ResQNet.com, Inc. v. Lansa, Inc.*, 594 F.3d 860 (Fed. Cir. 2010).

⁵⁹ *Id.* at 868.

⁶⁰ *Id.* at 869-70.

⁶¹ *Id.*

⁶² *Id.* at 870.

⁶³ *Id.*

⁶⁴ *Id.*

⁶⁵ *Id.*

⁶⁶ *Id.* at 870.

After a bench trial, the court found that ResQNet’s ’075 patent was valid and infringed and awarded \$506,305 for past infringement based on a hypothetical royalty of 12.5%.⁶⁸ Lansa cross-appealed the damages award, challenging the methodology used by ResQNet’s damages expert.⁶⁹

On February 5, 2010, the Federal Circuit—per curiam—vacated the district court’s damages award and remanded for a determination of damages.⁷⁰ The court concluded that the district court’s award relied on speculative and unreliable evidence “divorced from proof of economic harm linked to the claimed invention” and was inconsistent with the court’s damages law.⁷¹ The court explained that the majority of the licenses were problematic for the same reasons as those in the *Lucent* case, as Dr. David used licenses “with no relationship to the claimed invention” to justify his proposed double-digit license rate.⁷²

The court specifically criticized two parts of Dr. David’s analysis: (1) the “extremely” high rates in the re-branding licenses compared with the license on the claimed technology and (2) the unconvincing reasons he gave for considering the bundling licenses.⁷³ The court explained that Dr. David offered “little or no evidence of a link between the re-branding licenses and the claimed invention” and that the district court “made no effort to link certain licenses to the infringed patent.”⁷⁴ The court asserted that Dr. David did not attempt to show that the re-branding agreements embodied the claimed technology or to show demand for the patented technology.⁷⁵ Instead, the court found that Dr. David’s downward shift from the re-branding licenses was “an admission that his calculations are speculative without any relation to actual market rates.”⁷⁶

The court also noted that the district court appeared to be influenced by Lansa’s decision not to use a damages expert, but explained that it was ResQNet’s burden—not Lansa’s—to persuade the court with legally sufficient evidence regarding the reasonable royalty.⁷⁷ The court also explained that the most reliable evidence in the case was the litigation straight-rate license on the patents-in-suit, and stated that “[o]n other occasions, this

⁶⁷ *Id.* at 872.

⁶⁸ *Id.* at 863.

⁶⁹ *Id.*

⁷⁰ *Id.*

⁷¹ *Id.*

⁷² *Id.* at 869-70 (“The inescapable conclusion is that Dr. David used unrelated licenses on marketing and other services—licenses that had a rate nearly eight times greater than the straight license on the claimed technology in some cases—to push the royalty up into double figures.”).

⁷³ *Id.* at 870.

⁷⁴ *Id.* at 871.

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ *Id.* at 872.

court has acknowledged that the hypothetical reasonable royalty calculation occurs before litigation and that litigation itself can skew the results of the hypothetical negotiation.”⁷⁸

In a dissent, Judge Newman criticized the majority’s decision, asserting that it created a new rule that no licenses involving the patented technology could be considered if the patents themselves were not directly licensed or if the licenses included subject matter in addition to that which was infringed.⁷⁹ She argued that the district court recognized the differences between the re-branding licenses and the facts of the case, and took those differences into account in its decision.⁸⁰ She also asserted that Lansa did not dispute the licenses that the majority found to be considered in error.⁸¹ Judge Newman also repeatedly criticized Lansa for failing to offer evidence or testimony in support of damages.⁸²

After the Federal Circuit’s decision, ResQNet sought rehearing or en banc review.⁸³ The court denied that request on March 31, 2010.⁸⁴

B. District Court Decisions

1. Cornell

The March 31, 2009 decision in the *Cornell University v. Hewlett-Packard Co.* case is notable not only because the jury awarded \$184 million in damages, but also because that decision was vacated by the district judge—Federal Circuit Judge Randall Rader, sitting by designation in the Northern District of New York.⁸⁵

In that case, Cornell accused 31,000 HP processors of infringing Cornell’s ’115 patent.⁸⁶ The ’115 patent is directed to a method for instruction issuance within a computer processor.⁸⁷ The court explained that there was no dispute that the ’115 patent covered just one component of the instruction reorder buffer (“IRB”), which was part of a computer processor, which is itself only a component the CPU module, which is a part of a “brick,” which is part of the larger server.⁸⁸ While HP sold primarily servers and workstations

⁷⁸ *Id.*

⁷⁹ *Id.* at 876 (Newman, J., dissent).

⁸⁰ *Id.* at 877 (Newman, J., dissent).

⁸¹ *Id.* at 878 (Newman, J., dissent).

⁸² *Id.* at 879, 881 (Newman, J., dissent).

⁸³ ResQNet’s Combined Petition for Rehearing and Suggestion for Rehearing En Banc, 2010 WL 974653 (Mar. 5, 2010).

⁸⁴ Resqnet.Com, Inc., et al. v. Lansa, Inc., Nos. 08-1365, 08-1366, 09-1030 (Mar. 31, 2010).

⁸⁵ *Cornell University v. Hewlett-Packard Co.*, 609 F. Supp. 2d 279 (N.D.N.Y. 2009).

⁸⁶ *Id.* at 283.

⁸⁷ *Id.*

⁸⁸ *Id.*

containing infringing processors, it also sold 31,000 infringing processors during the relevant time period.⁸⁹

At trial, Cornell sought damages on the revenue from HP's sales of its entire server and workstation systems in spite of a warning that the court would "scrutinize" the damages proof if Cornell sought such damages.⁹⁰ After it was clear Cornell was seeking such damages, the court interrupted the trial to conduct a *Daubert* hearing to determine whether Cornell's damages expert, Dr. Marion Steward, properly applied the entire market value rule "or had improperly expanded the rule to claim damages far in excess of the contribution of the claimed invention to this market".⁹¹ After the hearing, the court excluded Dr. Stewart's testimony that the entire market value of HP's servers and workstations should be used as the royalty base because neither Cornell nor Dr. Stewart offered credible and sufficient economic proof that the patented invention drove demand for HP's entire server and workstation market.⁹² The court allowed Cornell to instead offer testimony that took into account the fact that the claimed invention was not the entire system but only a component of a component of the system.⁹³ After the *Daubert* hearing, Dr. Stewart testified that the royalty base was \$23 billion, based on a calculation of what HP's sales of CPU bricks would have been.⁹⁴ The jury awarded \$184 million to Cornell, applying a 0.8% royalty rate to a \$23 billion royalty base.⁹⁵

The court vacated the award, finding that Cornell did not prove entitlement to the entire market value of HP's CPU brick products.⁹⁶ The court explained that the entire market value rule permits damages on technology beyond the scope of the claimed invention "only upon proof that damages on the unpatented components or technology is necessary to fully compensate for infringement of the patented invention."⁹⁷ The court explained that in this case Cornell did not provide such proof that it was entitled to a royalty base that was based on the sales of the unpatented technology as well as the patented technology.⁹⁸ The court reasoned that an over-inclusive royalty base from the sales of non-infringing components "is not permissible simply because the royalty rate is adjustable."⁹⁹

The court reasoned that the \$23 billion royalty base was not based on market transactions, but on a calculation of what HP would have earned if it had sold the infringing processors in conjunction with the CPU bricks.¹⁰⁰ The court was especially critical of

⁸⁹ *Id.*

⁹⁰ *Id.*

⁹¹ *Id.* at 283-84.

⁹² *Id.* at 284.

⁹³ *Id.*

⁹⁴ *Id.* at 284, 287.

⁹⁵ *Id.* at 282.

⁹⁶ *Id.*

⁹⁷ *Id.* at 284-85.

⁹⁸ *Id.* at 285.

⁹⁹ *Id.* at 286 (citing *Rite-Hite Corp. v. Kelley Co.*, 56 F.3d 1538, 1549 n.9 (Fed. Cir. 1995)).

¹⁰⁰ *Id.* at 287.

Cornell's damages methodology in light of the court's warnings before and after the *Daubert* hearing.¹⁰¹ The court suggested "[w]ithout any real world transactions, or even any discernable market for CPU bricks, less intrepid counsel would have wisely abandoned a royalty base claim encompassing a product with significant non-infringing components. The logical and readily available alternative was the smallest salable infringing unit with close relation to the claimed invention - namely the processor itself."¹⁰²

The court rejected Cornell's argument that any error in the choice of royalty base was irrelevant because the jury took the size of the royalty into account in calculating the final damages award.¹⁰³ The court suggested that the large royalty base obviously mattered, as Cornell fought hard throughout trial to advance it.¹⁰⁴ Citing *Rite-Hite*, the court suggested that the issue of whether a patentee is entitled to include the entire market value of a system incorporating the patented invention is separate from the effect of conveyed or collateral sales on the royalty rate.¹⁰⁵ The court noted that the methodology used to determine the proper royalty base is falls within the discretion of the district court.¹⁰⁶ While the court recognized that the Federal Circuit permits estimates in the damages context, it concluded that it was the court's duty to ensure that those estimates were tied to proper economic methodologies.¹⁰⁷ The court thus excluded Dr. Stewart's testimony.¹⁰⁸

The court then granted HP's motion for judgment as a matter of law that the proper royalty base was the hypothetical processor revenue of \$8 billion, and awarded Cornell \$54 million in damages based on the jury's 0.8% royalty rate.¹⁰⁹ The *Cornell* decision is currently on appeal.¹¹⁰ The Federal Circuit heard oral argument in the case on April 6, 2010.¹¹¹

¹⁰¹ *Id.* at 287-88.

¹⁰² *Id.*

¹⁰³ *Id.* at 289.

¹⁰⁴ *Id.*

¹⁰⁵ *Id.*

¹⁰⁶ *Id.*

¹⁰⁷ *Id.* at 290.

¹⁰⁸ *Id.*

¹⁰⁹ *Id.* at 293. The hypothetical processor revenue was then decreased over a billion dollars due to an implied license. *Id.*

¹¹⁰ See Defendant-Appellant's Initial Brief, 2009 WL 3044561 (Aug. 31, 2009); Plaintiffs-Cross Appellants Principal and Response Brief, 2009 WL 3867599 (Oct. 27, 2009); Defendant-Appellant's Response and Reply Brief, 2009 WL 5434698 (Dec. 23, 2009); Plaintiffs-Cross Appellants Reply Brief, 2010 WL 543373 (Jan. 22, 2010).

¹¹¹ See <http://www.cafc.uscourts.gov/calendar.html>. Interestingly, the panel included Judges Prost, Moore, Guilford. Judge Guilford is a district judge for the United States District Court for the Central District of California.

2. Uniloc

In *Uniloc USA, Inc. v. Microsoft Corp.*, a jury in the District of Rhode Island awarded Uniloc \$388 million—the fifth largest patent verdict in history—for Microsoft’s infringement of Uniloc’s ’216 patent, which covered a product activation system (“PA”).¹¹² But the district judge reversed the jury’s infringement verdict, and stated that it would have granted a new trial on the jury’s damages verdict.¹¹³

At trial, Uniloc’s damages expert, Joseph Gemini, proposed a reasonable royalty of \$2.50 per activation for a total damages award of \$564,946,803.¹¹⁴ He suggested that this amount was a “mere” 2.9% of the total dollar volume of sales of the accused products (\$19.27 billion).¹¹⁵ After hearing the testimony, the court warned Uniloc to “stay away” from the \$19 billion number, but the number “continued to rear its head” throughout trial, including when Uniloc challenged Microsoft’s proposed damages amount of \$7 million by suggesting that anyone who would accept a 0.00003% royalty rate “is nuts.”¹¹⁶ The court explained that this reliance on the \$19 billion sales of the accused products ran “afoul” of the entire market value rule.¹¹⁷ The district court noted that Uniloc conceded that customers did not buy Office or Windows because of PA and asserted that it would not seek a royalty based on the entire market value rule.¹¹⁸ The district court rejected Uniloc’s argument that the \$19 billion number was a “check” on the reasonableness of Microsoft’s damages expert’s opinion, explaining that references to numbers as a “gut-check” encourages what the rule seeks to prevent—awarding damages in excess of the contribution to the patented invention.¹¹⁹ The court reasoned that it was impossible to know how the evidence affected the jury’s damages award, but concluded that should the need for a new trial arise, Microsoft was entitled to a new damages determination without consideration of the \$19 billion amount.¹²⁰

The decision is currently on appeal at the Federal Circuit, although the damages issue is not on appeal.¹²¹

3. Centocor

In *Centocor Ortho Biotech, Inc. v. Abbott Laboratories*, a jury in the Eastern District of Texas determined that Abbott infringed Centocor’s ’775 patent, and awarded

¹¹² *Uniloc USA, Inc. v. Microsoft Corp.*, 640 F. Supp. 2d 150 (D.R.I. 2009).

¹¹³ *Id.*

¹¹⁴ *Id.* at 184.

¹¹⁵ *Id.*

¹¹⁶ *Id.*

¹¹⁷ *Id.*

¹¹⁸ *Id.*

¹¹⁹ *Id.* at 185.

¹²⁰ *Id.*

¹²¹ See Brief for Uniloc USA, Inc. and Uniloc Singapore Private Limited, Nos. 10-1035, 10-1055, 2010 WL 783511 (Fed. Cir. Feb. 04, 2010).

\$1,168,466,000 in lost profit damages and \$504,128,000 in reasonable royalty damages.¹²² With interest, the final award was \$1,848,235,661—the largest patent damages verdict ever.¹²³ Without any discussion, the district court denied Abbott’s motions for judgment as a matter of law or new trial on the lost profits award.¹²⁴

The case is currently on appeal at the Federal Circuit.¹²⁵ Among other things, Abbott is appealing the damages verdict, claiming that the jury’s award of lost profits is incorrect because there were non-infringing alternatives.¹²⁶

4. IP Innovation

In the March 2, 2010, *IP Innovation LLC v. Red Hat Inc.* decision, Judge Rader, sitting in the Eastern District of Texas, granted defendants’ motion to exclude the testimony of plaintiff IP Innovation’s damages expert, Mr. Joseph Gemini.¹²⁷ The court explained that Rule 702 requires it to exclude unreliable evidence.¹²⁸ In his expert report, Joseph Gemini invoked the entire market value rule in determining the royalty base in the case, including 100% of defendants’ revenues from the accused systems.¹²⁹ The court concluded that this methodology did not show a sound economic connection between the claimed invention and the broad royalty base, as the claimed invention was a “relatively small component” of the accused systems, and was one of over a thousand components in the accused systems.¹³⁰ The court noted that the claimed invention played a “small role” in the overall product and was “often-unused.”¹³¹ The court concluded that the expert’s use of the revenues from all accused products for the accused product was a “stunning methodological oversight” and made it difficult for the court to give any credibility to the expert’s assertion that the claimed feature was the basis for customer demand.¹³²

The court also found that the expert’s testimony should be excluded because he arbitrarily picked a royalty rate based on studies instead of relying on non-litigation licenses

¹²² No. 07-139, slip op., Doc. No. 332 (E.D. Tex. Dec. 18, 2009).

¹²³ *Id.* at 2.

¹²⁴ *Centocor Ortho Biotech, Inc. v. Abbott Laboratories*, No. 07-139, Doc. No. 325 (E.D. Tex. Nov. 1, 2009).

¹²⁵ Brief for Defendants-Appellants, No. 10-1144, 2010 WL 1180226 (Fed. Cir. March 08, 2010).

¹²⁶ *Id.* at *64-65.

¹²⁷ *IP Innovation L.L.C. v. Red Hat, Inc.*, No. 07-447, 2010 U.S. Dist. LEXIS 28372, at *2-3 (E.D. Tex. March 2, 2010).

¹²⁸ *Id.* at *4.

¹²⁹ *Id.* at *5.

¹³⁰ *Id.* at *5-6.

¹³¹ *Id.* at *6-8.

¹³² *Id.* at *8.

to the patents-in-suit.¹³³ The court explained that although the licenses were entered into more than a decade before the hypothetical negotiation, they are “far more relevant than the general market studies” that the expert relied on.¹³⁴ The court noted that it was plaintiff’s burden to prove damages and excluded the expert’s testimony because of these errors.¹³⁵

III. THE FUTURE OF DAMAGES AWARDS AND PRACTICE TIPS

Are patent damages awards really trending higher? What is driving the Federal Circuit’s recent activist stance on damages? What will become of the pending legislation in this area? What can we glean about the future of damages jurisprudence based on what is happening today?

Enormous damage awards certainly are good fodder for attention-grabbing headlines, and billion dollar verdicts have topped the news in recent years. But are damages awards really running amuck? Some commentators think not. For example, in response to hearings on intellectual property held by the Federal Trade Commission in December, 2008, a damages expert studied damages awards to determine whether there was a significant increase in size of awards in recent years. She concluded, “I don’t find much evidence of run-away awards in the 2000s.”¹³⁶ Of course the case discussion above demonstrates that some patent damages verdicts are still quite high, including the more than a billion-dollar verdict in the *Centocor* case—the largest patent damages verdict ever.

Whether there is or is not accurate evidence to support the notion that damages awards have been on the rise in recent years, there certainly is movement to modify the treatment of damages evidence in the courtroom. The pending legislation on Patent Reform has multiple provisions relating to the nature and type of damages evidence that likely will be acceptable in future cases. Recent Federal Circuit and district court decisions indicate the court is willing, as never before, to dig into damages verdicts and review the supporting evidence for sufficiency. In the past, review of the evidence in patent trials more typically was limited to issues of liability, not damages.

Indeed, the Federal Circuit does appear to be slashing damages awards on the basis of sufficiency of evidence, as seen in many of the recent decisions reported in this paper. In *Lucent*, the court vacated an award of nearly half a billion dollars against Microsoft, finding it did not meet the “substantial evidence” standard for proving damages. In *Cornell*, Judge Rader, sitting by designation at the Northern District of New York, decreased the damages that had been awarded by the jury by over 70%. In *ResQNet*, Judges Lourie and Rader

¹³³ *Id.* at *9-11 (“At least two of these agreements were entered into outside of the context of litigation and thus appropriate as touchstones for determining the appropriate royalty rate in this case.”).

¹³⁴ *Id.* at *11.

¹³⁵ *Id.* at *8-12.

¹³⁶ *Public Hearing Concerning the Evolving Intellectual Property Marketplace – Evidence of Problems in Estimation of Patent Damages in Recent Times*, Gauri Prakash-Canjels, Ph.D, available at www.ftc.gov/os/comments/iphearings/540872-00036.pdf.

vacated an award of more than \$500,000, finding that it was not supported by sufficient evidence. (Judge Newman dissented in this opinion.)

So how is a prudent practitioner to proceed in these changing times? For patentees, there is no substitute for presenting a solid damages case substantiated by appropriate evidence at the district court level. Doing so is the best measure of protection against having a large award overturned on appeal, or subject to attack based on changes in the law. Damages models are highly fact dependent. Care should be had to ensure that the evidence presented at trial mirrors the marketplace dynamics in which the patented products or processes are marketed and sold. Whether the measure of damages is lost profits or a reasonable royalty, in seeking to create the hypothetical world that would have existed without the infringement, great attention must be given to the real-world dynamics of the given marketplace. Overly aggressive assumptions that inflate damages figures are not likely to stand up to the heightened evidentiary scrutiny being applied by the Federal Circuit and being suggested in the pending Patent Reform legislation.

For accused infringers, damages experts and verdicts appear to be under greater scrutiny than ever, as can be seen from the cases discussed above. Accused infringers should monitor both the proposed royalty base and royalty rate closely and challenge damages evidence throughout the case—starting with the damages expert’s methodology, to summary judgment motions on damages, to motions in limine to limit evidence at trial, to judgment as a matter of law after the patentee’s case-in-chief, to post-trial requests for judgment as a matter of law, remitter, and/or new trial.

It is the view of the authors of this paper that large patent damages awards can continue to be obtained in certain circumstances. Large awards depend on the facts of your case, including whether the marketplace dynamics legitimately support the large damages sought and whether you are able to marshal evidence in your client’s favor to present a well-reasoned and compelling damages model to the judge or jury.