

## 1 FEDERAL TRADE COMMISSION

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FEDERAL TRADE COMMISSION

HEARING ON: ) Matter No.  
THE EVOLVING IP MARKETPLACE ) P093900  
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WEDNESDAY, FEBRUARY 11, 2009

Conference Center  
Federal Trade Commission  
601 New Jersey Avenue, N.W.  
Washington, D.C. 20580

The above-entitled hearing was held, pursuant  
to notice, at 9:00 a.m.

## P R O C E E D I N G S

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1  
2  
3 MS. MICHEL: We're going to go ahead, and we  
4 will get started now since we have so much to cover this  
5 morning.

6 Good morning. Welcome to the Federal Trade  
7 Commission, and our second in a series of hearings on  
8 the evolving marketplace. I am Suzanne Michel. I am  
9 the Assistant Director for Policy in the Bureau of  
10 Competition. I'm going to give you a couple of brief  
11 announcements, and then we will dig right in.

12 The first one is a security announcement. In  
13 the case of fire, if the building is evacuated, please  
14 go across the street, and we'll try to check off and  
15 make sure that everyone is out of the building.  
16 Hopefully that won't happen.

17 This project, the evolving IP marketplace, is  
18 our attempt to look at the operation of markets for  
19 patents and technology and how different legal doctrines  
20 impact the operation of those markets. Today we're  
21 going to be focusing on patent damages. Tomorrow we  
22 will be focusing on permanent injunctions in the wake of  
23 *eBay*.

24 We will be having future hearings on March 17 -  
25 I'm sorry, March 18, right? March 18, March 19, April

1 17 in D.C., and May 4 and 5 in Berkeley. We will be  
2 issuing a press release in the next couple of days  
3 announcing that and giving an indication of what those  
4 hearings will be about.

5 In terms of comments, our initial comment period  
6 closed February 5. I understand the web site was down  
7 around that time. It is back up now, so please, if  
8 anyone has comments, please submit them.

9 In the upcoming press release, we will also be  
10 announcing we will be reopening the comment period. We  
11 do not want to turn away any good input, and in  
12 addition, we wanted to give everyone an opportunity to  
13 comment on the discussions that you will be hearing in  
14 this series of hearings. We will close the comment  
15 period on May 15, because at some point you need to  
16 buckle down and start writing.

17 With that, I am going to turn the floor over to  
18 Bill Adkinson, who will introduce what we are doing  
19 today and the great program that we have lined up.

1 patent proceedings, in particular reasonable royalties.

2 We hope that this panel will help move the  
3 debate forward by focusing on the legal standards  
4 governing reasonable royalties and especially how those  
5 standards are implemented in judicial proceedings.

6 It's our great good fortune that we'll be  
7 hearing today from practitioners and economic policy  
8 experts who have an extraordinary array of experience in  
9 patent damage litigation. Their insights will provide a  
10 foundation for an assessment of whether there are  
11 problems in either the legal standards or the way  
12 they're implemented and also whether there are various  
13 reforms that might improve matters. This afternoon  
14 we're going to have a roundtable discussing the same  
15 issues.

16 I'm going to be real brief in introducing the  
17 panelists. Their very distinguished bios are on the web  
18 site, but I must mention that I wince when I think that  
19 the bill we would be running up if they were here on a  
20 paying matter. We're very grateful that they've taken  
21 the time from their work to come here and help us better  
22 understand these matters, especially in these really  
23 difficult economic times.

24 We're going to have lead off presentations on  
25 data on patent damages, the most current data available

1 on damage awards and related aspects of patent  
2 litigation. That's going to take a half hour or so.

3 We're going to take a short break then, and then  
4 we're going to dive into our panel, and we won't have  
5 any further breaks for the rest of the morning. So I'll  
6 introduce the two presenters right now.

7 Professor Paul Janicke is a professor of law at  
8 the University of Houston Law Center. He's also the  
9 founder of the Law Center's Institute for Intellectual  
10 Property and Information Law. He previously was a  
11 senior litigation partner at Arnold, White and Durkee.  
12 He's authored numerous articles on IP subjects and a  
13 case book entitled "Modern Patent Litigation."

14 His research activities include empirical patent  
15 law studies, particularly a web site called  
16 patstats.org, which I think we'll hear about a little  
17 more.

18 Then we're going to here from Aron Levko. Aron  
19 is the principal and founder of the intellectual asset  
20 management practice from PricewaterhouseCoopers in the  
21 Americas. He has extensive experience in dispute  
22 resolutions, intellectual asset transactions, business  
23 valuations and IP portfolio management.

24 He also has extensive expert testimony  
25 experience. He's published and spoken frequently on



1           Three quarters of them, by my reckoning, are for  
2 the patentee, and it is now down to about 1 and a half  
3 percent judgments on bench trials, so you can see trials  
4 are becoming, year by year, less and less the  
5 disposition tool of choice for contested patent cases  
6 and summary judgment becoming more and more the tool.

7           The Federal Circuit hears only about half of the  
8 400 patent appeals that are lodged there every year. I  
9 checked this just last week with the Court, and they say  
10 that about 200 cases are decided by panels that actually  
11 have law issues, not always patent law issues but some  
12 law issues to decide, and the rest of them, the other  
13 cases are dismissed perhaps due to settlement, perhaps  
14 because the appellant just gives up. It's kind of hard  
15 to tell.

16           So we really only get every year about 90  
17 Federal Circuit cases, including the Rule 36 summary  
18 affirmances, that are rulings in the patent law sense  
19 that we would call who wins and who loses.



1           Now, understand, we're not telling you the final  
2 judgment dollar numbers in these stats. We are telling  
3 you only what the jury foreman announced and only since  
4 2005. So Aron's data are much more comprehensive time  
5 wise than mine.

6           I am only looking at January 1, 2005, because  
7 that is around the time when people started to say,  
8 There's run-away freight trains in patent cases, these  
9 juries are just acting crazy. So we decided to take a  
10 look and to periodically monitor all the jury verdicts  
11 we could find, and we collect them not only from Westlaw  
12 but also from newspaper articles, word of mouth,  
13 wherever we can get the information. And we go online to  
14 Pacer and pull the actual verdict form.

15           So that's how we assemble it, so a lot of  
16 times, the ending judgment of course is going to be  
17 higher than the jury verdict because of enhancement due  
18 to willfulness, prejudgment interest. Other times the  
19 final judgment is going to be a lot lower because of  
20 remittitur and JMOL problems the patentee has to face.

21           So we're just looking at what the foreman  
22 announces. Those are the numbers, and if you look at  
23 those numbers since January of 2005, and this is current  
24 till January '09, in the last month, verdicts are not  
25 run-away freight trains usually.

1           Here I've got them organized from top to bottom  
2 over the four-year period. The biggest one was a billion  
3 and a half dollars. I might say it got set aside for  
4 other reasons, so just telling you what came out of the  
5 jury foreman. Then \$431 million, \$360 -- these are the  
6 runs that spur the filing of patent litigation, hundreds of  
7 millions of dollars -- but it doesn't take long before you  
8 drop down.

9           By the time you get down to the 101st or so --  
10 we're under a million dollars by the 100th row of this  
11 spreadsheet, and then it continues down from there, and  
12 then there's a bunch of zeroes at the bottom. The  
13 zeroes are of course where the jury came in for the  
14 accused infringer. There's about 25 percent of those  
15 cases.

16           So the patentee wins about 75 percent, if he can  
17 get to trial; that is, if he can get past the summary  
18 judgment hurdle that is the usual track, and for all  
19 that period the median is right here, \$5,290,000, the  
20 median of the winning patentee cases, not counting any  
21 zeroes. So if you just say, If I win, if I get past  
22 summary judgment and if I win at the jury, what's that  
23 foreman going to say, and in this period of time of four  
24 years, it looks like the median is just off over \$5  
25 million.

1           You know, median statistics are a small comfort  
2 to people who lost up here, and I understand that.  
3 There's some of you from this company, for example, you  
4 might have an interest in -- oh, here's the same company  
5 again, look at that, so their views on the whole subject  
6 might be diametrically opposed, and they're not going to  
7 be real happy or comforted by the fact that the median  
8 is way down here.

9           So some people say, Well, that's the median of  
10 all cases, but it really depends on where you sue. So  
11 we said, Okay, let's take a look district by district,  
12 in the heavy patent litigation districts, so I just  
13 picked a few and color coded them for convenience.

14           Let's look at this first one, Central District  
15 of California, lots of filings there, God only knows  
16 why. The results are very bad for patentees on summary  
17 judgment. You don't get to trial that fast, but still a  
18 lot of people file there. Notice how few trials there  
19 have been, jury trials and verdicts, just a handful in a  
20 four-year period. What are the numbers? Well, the  
21 highest one in that district is \$53 million, and it  
22 jumps down to \$19, \$12 and so on.

23           So the median is somewhere around here \$6  
24 million or so, \$7 or maybe \$8 million, not very different  
25 from the overall median, and the highest one is only \$53.

1 Well, since apparently it costs according to AIPLA  
2 survey about \$5 million per side to get to judgment --  
3 they don't measure until trial anymore because that's  
4 disappearing but cost to judgment, \$5 million a side, any  
5 verdict down here in the three and six million dollar  
6 range is probably not going to be considered a victory  
7 by the client.

8           So what about Northern California? A small  
9 number of cases there too. They seem to be a little bit

1 good too, only one loss at the jury level, and medians  
2 in the \$45-65 million range, but again not that many cases.

3 I put in New Jersey just because everybody seems  
4 to be wanting to sue there lately. They're the number 4  
5 district in the recent -- last year or so. I haven't  
6 any real feeling for why. The numbers certainly don't  
7 justify going to New Jersey. It takes a long time to  
8 get to judgment, not very favorable to the patentee when  
9 you get there, so it must be a high settlement rate for  
10 pharmaceutical companies I guess, so it's driving that.

11 Now, here is the big gorilla, the Eastern  
12 District of Texas, and here there is a lot of cases.  
13 The win rate is about the same as everywhere else, but  
14 the median of the wins is substantially higher and  
15 similar to Delaware. It's somewhere in the \$34-41  
16 million range, so naturally, lots of people file in the  
17 Eastern District of Texas, and it is not hard to see  
18 why.

19 There are a lot of trials there because summary  
20 judgment in the Fifth Circuit culturally and  
21 traditionally was not done very often, so your chances  
22 of getting to trial are better in the Eastern District,  
23 and I believe that's what's driving the large number of  
24 suits there at the minute. The future of that district  
25 is another matter for patent cases.

1           The Eastern District of Virginia, just a  
2   handful, not really enough to address, and Western  
3   District of Wisconsin because apparently it was a rocket  
4   docket. A lot of people seemed to want to file there

- 1 acceptable non-infringing substitute. That's gone now.
- 2 You can still get some lost profits even if there are





1 like what is win, what is a non-practicing entity, our  
2 definitions that we have used to compile the data.

3           Okay, just to kind of  
4 set the context up, the patents being issued, the  
5 grants, have increased markedly from at least -- we're  
6 looking at here in 1991 through about 2003. The  
7 increase was about, oh, 4 percent or so a year. But  
8 since 2003, a funny thing has happened -- grants have  
9 leveled off. And so we have an overall growth rate of  
10 3.5 percent over these 18 years or so, but  
11 really it's been almost zero for the last five years.

12           Meanwhile, patent trials, which had been  
13 increasing at over 6 percent a year through about 2004,  
14 themselves have leveled off. Now, I don't have data yet  
15 for 2008, but over the past three years, it really has  
16 declined slightly, so what does that mean?

17           Well, it means that maybe a lot of these  
18 disputes are being resolved outside of trials, in  
19 settlements or some sort of licensing with a little bit  
20 of a hammer, but that kind of sets the stage for now  
21 what is happening when a case is filed.

22           We're focusing now on the period 1995 through  
23 2008. We selected that because we saw that prior to  
24 1995, there was a general increase in damages, not year-  
25 by-year but a trend up. from say 1983 when the Circuit

1 Court was put in play or 1982.

2 Since 1995, as you will see in the preceding  
3 charts, the median damages -- I say median because it  
4 kind of smooths out some of the volatility -- has stayed  
5 fairly constant. Just to break apart a little bit what  
6 we have in our database during this period, we looked at  
7 something like 1,562 cases, and of those, about half or  
8 so are resolved at summary judgment, the other half  
9 going to trial.

10 At summary judgment, the vast majority are ruled  
11 in favor of the alleging infringer. I've split this  
12 really just between patent holder and infringer rather  
13 than plaintiff and defendant because I think that's a  
14 more reasonable or appropriate way of looking at.

15 Professor Janicke came up to me before the  
16 meeting here and said, Your summary judgment wins for  
17 the patentee seem a little bit high. I looked at the  
18 data. That's what it looks like, at least over 14  
19 years, but it's still very -- the patentees seem to make  
20 out much better at trial, and you will see, when we split  
21 it apart, why.

22 They prevail about 56 percent of the time at  
23 trial, only about 19 percent of the time at summary  
24 judgment, but that number may be higher for different  
25 reasons at summary judgment.

1           A win, by the way, is defined as any beneficial  
2 interest that the patentee derives. It may not be what  
3 they've asked for, but if they receive beneficial  
4 interest, we've categorized that as a win.

5           Here are some key findings before I get too  
6 heavily involved in the data. First of all, as I had  
7 mentioned, median damages have stayed fairly constant,  
8 although I will say, and you will see, that the juries  
9 have awarded much higher damages from those trials,  
10 particularly in the last several years, in this decade,  
11 and we are getting higher trends in these damages  
12 recently.

13           Non-practicing entities are also getting  
14 slightly higher damages recently, although this is kind  
15 of a time lag in terms of the rulings that are currently  
16 taking place in the Supreme Court and elsewhere  
17 regarding jurisdiction, venue, and so forth, so perhaps  
18 in the future we might see non-practicing entities have  
19 damage awards tailing off a bit. But there is great  
20 disparity between districts, and we've got a chart kind  
21 of looking at that.

22           The use of juries have increased markedly in  
23 this decade. Reasonable royalty has now become the more  
24 prevalent measurement of damages. We have a chart that  
25 looks at how you split apart the damage awards between

1 lost profits, reasonable royalty and price erosion. But  
2 what it doesn't do so much is the frequency of  
3 measuring damages. You look at that.

4 Patentees' success rate is 36 percent overall,  
5 dragged down by the summary judgments, but when we  
6 get to trial, it's at 56 percent. When you get to  
7 juries, Professor Janicke's 75 percent may be a little  
8 low, at least looking over that seven or eight years, but  
9 right around in the same ball park.

10 Finally there's three districts that seem to  
11 stick out a bit in terms of patentee success rate: The  
12 Eastern District of Virginia, Pennsylvania Eastern and  
13 Texas Eastern, and those three districts, out of some 90  
14 districts, make up 25 percent of all non-practicing  
15 entity filings, and we'll take a look at that, okay.

16 Into the data. Over the years again from 1995  
17 through 2008, you can see that it's been relatively  
18 constant. In the years 1996, 2001 and 2005 we see the  
19 spikes in the bars, and the reason why the medians have  
20 been up that high is because the lower damage award  
21 cases, of less than \$2 million, are less in those years.

22 There weren't any more higher-value damages,  
23 just less of the lower-value damages, so it's kind of an  
24 anomaly. It's a statistical measure. We've tried to

1 if you look at damages of greater than \$10 million.  
2 Again all of these numbers have been corrected to 2008  
3 dollars -- the earlier years have been inflated so  
4 that we have a real look at the dollars and not simply a  
5 nominal look.

6 Taking that into account, there are some 122  
7 cases over these 14 years that were greater than \$10  
8 million, and something like 30 percent of them have  
9 occurred in the last three years. Then if we look at  
10 cases at \$100 million or greater over 14 years, we  
11 see -- what is it, I have the number here, something  
12 like 22 cases.

13 Of those 22 cases, almost half have occurred in  
14 the past three years, and I will say 2008 has been a  
15 record year for both over \$10 million and over \$100  
16 million cases, six in fact of 22 just in 2008 alone.

17 So something is happening to the damages. They  
18 are increasing. If you look at averages or if you look  
19 at large cases, they have increased markedly in the past  
20 few years, although the medians have been staying fairly  
21 constant, so you have to look under those calm waters a  
22 bit.

23 We split that information now between juries and  
24 bench trial. Bench trial is in the dark blue. The jury  
25 trials are in the light blue. You can see a great

1     disparity, and it's growing. Just to put it in  
2     perspective a bit, you can see that the median jury award  
3     is now over ten times -- over  
4     ten times greater than the median bench trial award over  
5     the past several years.

6             If you look at it by decade, in the '80s and  
7     '90s, juries awarded about one and a half times what a  
8     bench trial might award. In the decade of the 2000s, it  
9     is almost ten times. So something is happening, and  
10    that is what's driving some of these not only the  
11    success rates but the damage awards.

12            We split it apart between practicing and non-  
13    practicing entities. It's volatile. The practicing  
14    entities being the dark blue, the non-practicing being  
15    the light blue. There are times when the non-practicing  
16    entities have done very well, and they seem to have a  
17    slight trend upward where the practicing entities have  
18    been fairly consistent.

19            We tried to again smooth the data so that you  
20    could really see what's happening. If we try to do this  
21    on averages, it would be all over the place, but there  
22    is an upward trend of non-practicing entities. Again  
23    this is kind of a time lag because what's happening over  
24    the past year won't be really reflected for a year or  
25    two down the road.

1           The use of juries, back in 1995, only about 16  
2 percent of all trials were jury trials, and now we're up  
3 42, 43 percent the past few years, so it's almost  
4 tripled.

5           Now, if we look at the measurement of damages,  
6 and we did this by decade, again this is by dollars  
7 awarded, back in the 1980s, the reasonable royalty, the  
8 middle bar, the mid-blue, was about 44 percent. It's now  
9 grown to 54 percent as an allocation of the damage  
10 dollars.

11           If you look at the occurrence, the number of  
12 times that measurement of damage has been used, back in  
13 the 1980s, it was most likely in the 30 percent, and now  
14 it's over 60 percent. So it has occurred almost twice in  
15 terms of frequency, and the dollar amounts haven't grown  
16 quite the same, so definitely it's the measure and the  
17 choice, and there's reasons for it.

18           One is this capacity issue, non-practicing  
19 capability issue. The non-practicing entities, not  
20 having the manufacturing or distribution capabilities, are  
21 becoming more prevalent, and that tends to be the driving  
22 force for the measurement of damages.

23           Then you have a cost issue. It does cost more  
24 to do a lost profits calculation, and there's more  
25 involved with having to look at the market, look at

1 alternate substitutes and so forth.

2           You get into confidentiality issues of company's  
3 themselves not wanting to disclose such key information  
4 like their product costs, their profitability, what  
5 pricing schemes they use by customers. And then finally,  
6 we've got a competitive issue. There is a more global  
7 market, and it is becoming more difficult to niche a  
8 dispute into just two companies. Even though there is a  
9 lot of splitting between the lost profits and the  
10 reasonable royalty. Just the competitive angle, the  
11 distribution channels, the demographics and the  
12 customer.

13           It's hard to really say only the patent holder  
14 and the infringer are the only ones competing. It's  
15 just -- that's what's happening, and that's what's  
16 driving this kind of movement.

17           Now, if we take a look again over the overall  
18 win rates beyond the damage awards, and I would look at  
19 success rate, overall, over 14 years, the patentees have  
20 prevailed 36 percent of the time, 19 percent at summary  
21 judgment, 56 percent at trial, but there's a trend, and  
22 let's look at some of the trends.

23           First of all, let me split them apart between  
24 practicing and non-practicing entities. The practicing  
25 entities are much more successful, in any



1 measure -- overall, summary judgment and trial.

2 Success rates year-by-year, you can see the  
3 median line at 36 percent. There is an upward trend.  
4 It dropped off a little bit in 2008, but really in the  
5 last four years, it's been above the median over the 14  
6 years, and so the success rates are happening. Why are  
7 they happening? Let's split that data up a little bit.

8 First of all, if we split it up between  
9 practicing and non-practicing entities, the practicing  
10 entities prevail much more often, but the non-practicing  
11 entities in the recent past have been a little more  
12 successful. There's a trend upward with that.  
13 Practicing entities have always been higher, but their  
14 medians have been fairly stable in terms of success  
15 rate.

16 The big change is when you look at trials. At  
17 trials now we're looking at 56 percent being the  
18 median, but there's a general slight upward trend in  
19 terms of success rates with really out of the last,  
20 what, seven years, five of the seven years -- or actually  
21 six of the eight years -- being above the median.

22 Why? Well, if you look at jury trials, again  
23 the bench trials are in the dark blue, the jury trials  
24 being the light blue, jury trials were always more  
25 successful for a patentee than bench trials, but even

1 more so in the past few years, and it's growing, that  
2 disparity.

3           You can see a year-to-year anomaly, but what we  
4 can see is over 14 years, patentees prevail at jury  
5 trials 79 percent of the time, only 44 percent of the  
6 time at bench trials, and the trend is moving. It seems  
7 that recently it's moving up, but it's been higher going  
8 back.

9           Again, this is data coming from Westlaw,  
10 publicly available and so forth. There may be other  
11 factors involved.

12           If we look at the success rate of practicing and  
13 non-practicing entities at trials, again we see the  
14 practicing entities generally more successful than the  
15 non-practicing entities. However, the non-practicing  
16 entities in the recent years have moved up markedly, and  
17 again there's a time where that may come back down  
18 again.

19           So all of these factors, increasing use of  
20 juries, the non-practicing entities filing more  
21 frequently, jurisdictional strategies and venues and so  
22 forth, all play a part in increasing success rates and  
23 increasing damages.

24           Very quickly the top three as I mentioned,  
25 Eastern Virginia, Eastern Pennsylvania, Eastern Texas,

1 we rated them based on median damages, trial success,  
2 summary judgment success. We didn't have the time, and  
3 we do this in our report, we do time to trial and  
4 include those in the rankings too, but you can see how  
5 they sort down.

6 The 21 that we show here are where we had  
7 districts with the at least 20 decisions over the 14  
8 years, so we don't look at all 90. We look at the 21  
9 that have at least 20, what we feel are some statistical  
10 significance in the numbers.

11 Finally, if we look at the non-practicing  
12 entities filings, New York Southern, Illinois Northern,  
13 Texas Eastern are the three most prevalent. They make  
14 up 25 percent of the non-practicing entity filings again  
15 over this 14 year period. The top 10 over half, I guess,  
16 10 out of 90 that we have.

17 And so quickly, the concluding thoughts are  
18 patent litigation is still a good, effective protection.  
19 It may not be a cost benefit. There are some issues  
20 with that, but it is a way to monetize the patents.

21 The forum and venue, very important. Juries are  
22 awarding patentees higher damages and have higher  
23 success rates, and there's a great disparity between the  
24 districts. The patentees are winning more often  
25 recently at trial, although these are trends, and

1 damages are also trending higher.

2 Finally, non-practicing entities, although  
3 they're not as successful as practicing entities, have  
4 had some recent increases in the damage awards.

5 Thank you.

6 MR. ADKINSON: Thank you very much. I should  
7 emphasize that there is more data available in Mr.  
8 Levko's annual assessment of damages and also at  
9 Professor Janicke's web site, patstats.org.

10 We are going to take a very brief break now.  
11 Shall I first introduce the speakers? We'll take a  
12 break, but it's going to be a very short break as we  
13 assemble the panel, and we're going to come back and  
14 introduce the speakers. Thanks.

15 (Whereupon, a brief recess was taken.)

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1 PANEL 1:

2 MODERATORS:

3 SUZANNE MICHEL, FTC

4 BILL ADKINSON, FTC

5 PANELISTS:

6 BRUCE BURTON, Senior Manger Director, FTI

7 TOM COTTER, Briggs and Morgan Professor of Law,  
8 University of Minnesota Law School

9 ANNE LAYNE-FARRAR, Director, LECG, LLP

10 PAUL M. JANICKE, HIPLA Professor of Law, University of  
11 Houston Law Center

12 DR. GREGORY K. LEONARD, Senior Vice present, NERA

13 GAIL LEVINE, Assistant General Counsel, Verizon  
14 Communications, Inc.

15 ARON LEVKO, Principal, PricewaterhouseCoopers

16 EDWARD R. REINES, Partner, Weil, Gotshal & Manges, LLP

17 JOHN SKENYON, Principal, Fish & Richardson, P.C.

18

19 MR. ADKINSON: I would like to introduce the  
20 rest of the panel. You've already been introduced to Mr.  
21 Levko and Professor Janicke. In addition, we have Bruce  
22 Burton, who is senior managing director at FTI. FTI  
23 Consulting, Inc., is a leading expert witness and  
24 consulting company. He is leading FTI's technology and  
25 intellectual property management practice.



1 presentations in court.

2 Gail Levine is assistant general counsel at  
3 Verizon Communications where she handles a wide array of  
4 high-tech intellectual property and competition policy  
5 strategy issues. She recently co-edited the ABA's  
6 handbook on antitrust intellectual property.

7 Antitrust has been one of her main fields, and  
8 among her positions has been work here at the FTC, where  
9 she was attorney advisor to Chairman Majoras, and also  
10 deputy assistant general counsel during which time she

1 Damages, Law and Practice."

2 So without further adieu, we'll go to the panel.

3 I greatly regret that I forgot to mention the  
4 person who wrote the first article in this field that  
5 I read, Tom Cotter. Tom hails from the  
6 University of Minnesota and participated in our December  
7 5th hearings and has written widely on this subject,  
8 including a book that he coauthored with Roger Blair.

9 MS. MICHEL: All right. Thank you. For any of  
10 you who missed the morning presentation, it is being --  
11 this whole day is being web cast, and the web cast will  
12 stay up on the FTC web site. You can go back and catch  
13 it later. We're generating a transcript, which will be  
14 posted on the FTC web site, as is the transcript from our  
15 December 5 hearing.

16 We are very fortunate to have this group of  
17 panelists today. Bill and I will be posing questions to  
18 which they will respond. If any panelists would like to  
19 respond, just please turn up your table tent, and we  
20 will call on you, and we'll see how that progresses.

21 I want to start with the big question of: Why  
22 does it matter? Why is it important to get the damages  
23 calculation right? What are the problems with over-  
24 compensation and under-compensation?

25 Ed, first on the draw there? Go ahead.



1           MR. REINES: Well, I think the important thing  
2 to keep in mind, especially when reviewing the  
3 statistical charts that we saw, is how many of the cases  
4 never get to complaint and never get to trial, so that  
5 you really have a magnification process where the  
6 anomalous outcomes at trial or fear of anomalous  
7 outcomes at trial can drive a whole range of  
8 decision-making that's all the way upstream, and the  
9 numbers start virally replicating.

10           So I think the short answer is it's important  
11 because not just the outcome of trial for trial's sake  
12 but also payments that go on throughout the system.

13           MS. MICHEL: Tom?

14           PROFESSOR COTTER: There's a sense in which we  
15 can never really know whether patentees are over- or  
16 under-compensated. It depends in large part on whether  
17 the substv2hdover- or

1 inadequate. The other side of the coin is that if  
2 damages are too generous, if they make patentees better  
3 off ultimately as a result of infringement and then  
4 obtaining damages at trial, they're taking a substantial  
5 risk of over-deterrence as well, that companies that want  
6 to use technologies may wind up investing more than is  
7 socially optimal in designing around.

8 They may be reluctant to engage in innovation  
9 that might inadvertently wind up infringing some  
10 existing patent or patents, so I think there are dangers  
11 from both over-and under-deterrence that we would like  
12 to avoid.

13 MS. MICHEL: Aron?

14 MR. LEVKO: Yeah. Some of the things that have  
15 been mentioned. Regarding the effects of over-  
16 compensation, first of all, you've struck freedom to  
17 practice and reduced the business flexibility. Second  
18 of all, you increase the investment costs, and just  
19 because of the investment costs, the return on  
20 investment is reduced in that regard. Third, as Tom had  
21 mentioned, you deter competition. These are over-  
22 compensation issues.

23 Fourth, you increase litigation. That's the  
24 honey pot that draws these cases, especially in certain  
25 jurisdictions, and finally from an economic standpoint,

1 you just move resources to less productive means, which  
2 is more money going after -- in an over-compensation  
3 sense, not going to the highest use.

4           Regarding under-compensation, as mentioned, you  
5 reduce innovation, but it's even more than that. You  
6 reduce particularly small business formation which is  
7 the job growth in the country. You also reduce return  
8 on investment, because you reduce the returns for making  
9 those investments on innovation.

10           Finally you encourage infringement. If an  
11 infringer feels that they're going to get a better shake  
12 at trial, although there's a lot of cost to that, they may  
13 not agree to a commercial license. So extremes on both  
14 parts are not good, and so that I think the focus here is  
15 to strike a balance.

16           MS. MICHEL: Bruce?

17           MR. BURTON: Just to add a few minor points and  
18 really focus a little bit on alternatives. If you're  
19 being under-compensated for your infringement, you will  
20 tend to seek other remedies or other remedies become  
21 more important, so you might think in terms of a  
22 trade-off between damages and injunctions, injunctions  
23 will become more important.

24           You might find that you'll do more with trade  
25 secrets. You will make an effort not to invest in the

1 lawsuit but rather you'll keep this technology secret,  
2 and you will lose the social benefit of the sharing of  
3 the knowledge and information from making it public.

4 Also, with decreased damages, not only  
5 domestically, but you will encourage infringement  
6 internationally. It's less onerous if you're a foreign  
7 competitor coming in and you infringe on a U.S.  
8 technology if the penalty is smaller.

9 MS. MICHEL: The patent statute talks about  
10 damages adequate to compensate for the infringement, so  
11 what are the goals of patent damages? Is it just to  
12 compensate the patentee for the infringement in the  
13 sense of the but-for world, or should we have some other  
14 goal in terms of deterring infringement? Anne?

15 MS. LAYNE-FARRAR: I think it cannot just be to  
16 make the patentee whole in terms of providing a  
17 reasonable royalty, because, of course, not all  
18 infringements are detected, so you already have a  
19 situation where some infringements will go by unnoticed.  
20 And if the reward then is simply to put back what a  
21 license would have achieved, you're going to increase  
22 that number of people trying to infringe, trying to get  
23 under the radar of not being detected.

24 So it has to have some element of deterrence to  
25 i00 0.shere so00 0.0000 cm0.00 0.0gtelolem3t0000radar of not bein

1 speakers talked about, so that we get the right amount

1 of course I mean the value of the patent as against its  
2 next best alternative, it's next best non infringing  
3 substitute, and that reasonable royalty damages should  
4 never include the hold-up value of the patent.

5 MS. MICHEL: Tom, your thoughts on deterrence  
6 versus straightforward compensation?

7 PROFESSOR COTTER: Well, I think the two are  
8 interrelated. As far as I can see this, the goals of  
9 patent damages law should be dual: One, to maintain the  
10 patent incentive, and secondly, to deter infringement but  
11 also to avoid the risk of over-deterrence.

12 I think as a first approximation, putting to one  
13 side the issue of when injunctions are appropriate and  
14 when damages are appropriate, just focusing on the  
15 damages aspect of the question, I think as a first  
16 approximation, compensatory damages, but-for damages,  
17 probably serve both goals reasonably well.

18 If the patentee is assured that he will  
19 obtain -- that he will be restored to the position that  
20 he would have occupied but for the infringement, that  
21 maintains the patent incentive and should be sufficient  
22 to deter infringement once we factor in the litigation  
23 costs that a potential infringer would have to incur if  
24 it uses the technology that it was found to have  
25 infringed.



1 the option of applying one or the other.

2 But one, and the one that I think is reflected  
3 in Professor Janicke's slides toward the very end that  
4 we didn't really get to during the first part of the  
5 program and also reflected in Gail's comments -- one  
6 approach to reasonable royalties would be to award the  
7 patentee the value of the patented invention ex post.

8 And so John Schlicher, for example, has argued  
9 that reasonable royalties should be based upon the  
10 profits the infringer made with the patented invention  
11 minus our best estimate of what those profits would have  
12 been without the patented invention. That's the  
13 economic value of the invention ex post.

14 The other alternative, which is I think somewhat  
15 easier to shoehorn into existing law, is to focus on the  
16 ex ante hypothetical bargain between the patentee and  
17 the infringer and ask: What bargain would the parties  
18 have struck ex ante if they were trying to negotiate a  
19 license?

20 I think either measure of damages has its  
21 benefits and its disadvantages. One possible problem  
22 with the ex post or restitutionary measure of damages is  
23 that after the fact, the infringer may be locked into a  
24 particular technology, and so if we're asking what  
25 profits would the infringer have made, using the next



1 best alternative, well maybe that next best alternative  
2 really never got developed because the infringer,  
3 perhaps inadvertently went down a particular  
4 technological path. So I think there's a risk of  
5 exacerbating patent hold-up to the extent that it  
6 happens, whether it's common or uncommon, if we use the  
7 ex post approach.

8           If we try to replicate the bargain the parties  
9 would have made ex ante, that's obviously a very  
10 speculative sort of enterprise as well, but in some  
11 rough sense, it does restore the parties, as best as we  
12 can do this, to the position they would have occupied  
13 but for the infringement.

14           So I think there's something to be said for  
15 using the hypothetical negotiation technique but trying  
16 to make it more closely reflect what those negotiations  
17 really would have looked like in the real world.

18           MS. MICHEL: Thank you. Tom has done a great  
19 job of laying out I think the majority of issues that  
20 we'll be covering through the morning, as he always  
21 does, and I highly recommend what I think to be one of  
22 the seminal articles in this area, his *Rethinking*  
23 *Patents Damages* article for anyone interested in this  
24 topic.

25           So Tom has really laid out for us the importance

1 of creating a but-for world when you're thinking about  
2 compensatory damages.

3 Paul, let's go to you next in the sense of: Is  
4 creating that but-for world a sufficient means to create  
5 both the compensation for the patentee that we want and  
6 the deterrence effect and what are the goals of the  
7 patent system here in the sense of how to create that  
8 deterrent effect also?

9 PROFESSOR JANICKE: The goal is in the  
10 Constitution, and if I were king, I would tell the jury  
11 only that, that the progress of the useful arts is the  
12 keystone, and the value added by a particular patent is  
13 what they should be looking at.

14 And just to make clear, I don't claim to have  
15 invented or originated this formulation. Lots of people  
16 have proposed it, but my idea is to tell the jury that  
17 some portion of the value added is what they ought to  
18 award in light of the Constitutional purpose.

19 It's hard to argue when it's in the  
20 Constitution, and I would throw out everything else.

21 MS. MICHEL: All right. Aron?

22 MR. LEVKO: Yeah. Well, first of all, if you're  
23 talking a but-for world, that pertains primarily to lost  
24 profits sort of damages. When you get into reasonable  
25 royalty, you get into all these analyses and factors and

1     so forth, but I guess the thing that is -- I guess  
2     there's a disconnect here, is if we're focusing on  
3     reasonable royalty damages, which I think is the focus  
4     primarily of the discussion this morning, connected to  
5     economic thought, you really need to connect it more to

1 commercialization has taken place.

2           So even though you're trying to set up a  
3 hypothetical negotiation, that hypothetical  
4 negotiation's based on both known and knowable facts,  
5 and some of the knowable facts is the patent is somewhat  
6 been commercialized, so that risk factor has been  
7 reduced.

8           And I guess what you need to take a look at is  
9 valuation principles. If you're going to bring the  
10 legal concept into damage calculations and get past  
11 the attempt at trying to frame this up in the form of  
12 either *Georgia-Pacific* factors or *Panduit* factors or but  
13 for, valuation concepts such as like Revenue Ruling  
14 5960, which is used for business valuation, a ruling  
15 like that that frames intangible asset valuation like  
16 Ruling 5960 frames for tangible asset or business  
17 valuation might be invoked here.

18           And that's how law can give us a proper ball  
19 park to play within rather than simply playing with no  
20 boundaries, which is what's happening today.

21           MS. MICHEL: I would like to spend a little time  
22 on lost profits before we dive more in-depth into  
23 reasonable royalties. We've done an excellent job of  
24 laying out the ground work there.

25           Greg, any thoughts on this concept of

1     compensating the patentee in trying to recreate the but-  
2     for world?

3             DR. LEONARD: Well, in lost profits, yes, I  
4     think the idea of the but-for world is to return the  
5     patentee to the financial position it otherwise would  
6     have been had the infringement hadn't occurred.

7             The interesting thing I think about that is a  
8     lost profits award actually has the ability to do some  
9     amount of deterrence as well, although it's primarily  
10    meant to be compensatory, whereas a reason reasonable  
11    royalty award, by its very nature, actually can't be  
12    deterrent at all in some sense, aside from the  
13    litigation cost.

14            The reason for that is that if you're a  
15    potential infringer and there's some action you could  
16    take to avoid infringing, in other words, design around,  
17    you're only going to take that action if the probability



1           So they've done a public service, and yet it is  
2 a public good because if I'm the one to pay to challenge  
3 the patent, that benefit runs down to other companies as  
4 well, so I think we want to be very careful about  
5 deterring the testing of patents through the over-  
6 compensation or any kind of deterrence.

7           Would you like me to just comment on lost  
8 profits in general?

9           MS. MICHEL: Sure.

10          DR. LEONARD: I think the problems in lost  
11 profits, and actually I think the problem is true of  
12 reasonable royalty as well, is what the law provides for  
13 right now is sort of a list of factors, so in the lost  
14 profits side, it's the *Panduit* factors, and on the  
15 reasonable royalty side, it's the *Georgia-Pacific*  
16 factors, and this is just sort of a list of ideas.  
17 Somebody mentioned it was a grab bag, and that's  
18 essentially what it is.

19          What we really need is a framework, conceptually  
20 sound and coherent framework that lays out this is how  
21 you do it, and the valuation principles or for my point  
22 of view the economic principles of supply and demand and  
23 other things, if that was really codified and people  
24 were held to it, experts were held to it by judges using  
25 for instance their *Daubert* gatekeeping ability, I think

1 we would be in much better shape.

2           So on lost profits, I think the problem is that  
3 the *Panduit* factors, they're stated as sort of necessary  
4 conditions. Well, actually they're not necessary at  
5 all, you can have lost profits, even if one or more of them  
6 aren't satisfied. And the way the language is used is  
7 ambiguous, it doesn't really match up well to economic  
8 principles.

9           So really what I would like to do is throw them  
10 out and replace it with a basic coherent economic  
11 framework that really would correspond well to what's  
12 done in an antitrust damages case or a commercial  
13 damages case, and we can go through the details of what  
14 that would be, but that's my basic thought on that.

15           MS. MICHEL: I was wondering about panelists'  
16 responses to two points raised by Greg. One is that we  
17 want to be careful in creating too much deterrence, and  
18 also responses to his point that perhaps we should throw  
19 out economic



1 Federal Trade Commission have authority to bring suit  
2 challenging bad patents? If we're talking about  
3 deterrence, if it's a bad patent that's causing trouble  
4 out there, can you fix it or do you not have authority  
5 to do that?

6 MS. MICHEL: It would be a very difficult  
7 antitrust theory. I would say authority, that's a  
8 harder question. As a matter of policy, I think we  
9 would not do that. We would bring an antitrust or  
10 unfair competition challenge to perhaps a patent  
11 acquired by fraud and asserted.

12 PROFESSOR JANICKE: So you don't bring  
13 declaratory judgment actions just to get rid of what you  
14 think is a troublesome patent?

15 MS. MICHEL: No, I would say that there was not  
16 authority to do that. That would be my own personal

1 don't think permits punitive effects from reasonable  
2 royalty or lost profit, and I think that's correct.  
3 Like I said, I think the statutory scheme just be back  
4 with compensatory damages in the form of lost profits  
5 and reasonable royalty, and punitive damages in the form  
6 of willful infringement or exceptional case otherwise. And  
7 I think that's the right way to think about it.

8 Picking up on Greg's point, you know, there is a  
9 cost to having to litigate just in all the witnesses,  
10 all the time of management, and in the cost, so even if  
11 you lose, there's sunk costs, unless you can prove an  
12 exceptional case the other way. And on Aron's point, in  
13 terms of what's the role within the reasonable royalty  
14 analysis for some sense of, you shouldn't just be back  
15 where you would be anyway if you're the patentee.

16 I think the legal certainty that you have is  
17 taken into account in the current damages model, which  
18 is the patent is assumed valid, enforceable and  
19 infringed in the negotiation, which is never the case in  
20 the real world.

21 So, I mean, I think that that's where you get world.

1     have all the overhead of having to deal with that, if  
2     they're vindicated, but they also have this risk of sort  
3     of being punished with all the ambiguity that's in the  
4     system.

5             And as we all know in the courtroom and the jury  
6     system, there's a lot of ambiguity. That itself I think  
7     is going to prevent people from just infringing



1 reflects the value that the patented technology  
2 contributes, and then if you're going to add something  
3 to that for deterrence factors, be clear and make that a  
4 separate element. So that in using those awards and  
5 damage awards and reasonable royalties on a going  
6 forward basis, first of all, the implementer is paying  
7 something reasonable going forward that doesn't count in  
8 some kicker factor, but also so that other parties  
9 looking at those rates may be wanting to use them as  
10 comparables can use the appropriate level too, so that  
11 there's a clean split between the ex ante/ex post  
12 reasonable and damage's deterrent component.

13 MS. MICHEL: I want to go to Jack next.

14 MR. SKENYON: Just a couple things based on what  
15 I've heard so far. I feel like I am in a Presidential  
16 debate here. I am the candidate from the Greenpeace  
17 organization, who got here because the ACLU won some  
18 court case.

19 But a couple things that I've heard here are  
20 very interesting and things I have really never thought  
21 of quite from that perspective before. And one is this, is  
22 Is that I think, what I just heard from Anne hit on, the  
23 reason that some damages awards seem inordinately high  
24 here, and that's how the case is tried.

25 She was talking about factors that deal with not

1 actually the infringement issue or the invalidity issue,  
2 but factors that deal with the willfulness issue, what  
3 did they do when? What did they do before? Did they  
4 get clearance? Did they do these things?

1 think you get into an area of unfairness here because  
2 the cases could be quite different dealing with the same  
3 patent, and I'll give one example, and then I'll stop  
4 here, but it would be this.

5 We had a case that involved a medical device,  
6 and the market -- think of the market as divided up in  
7 pie, three slices of the pie. The infringer's in one  
8 slice, not in ours. We're in one slice, and we have  
9 another competitor in the third slice. We're not  
10 competing with the other competitor in the third slice.  
11 There was a lawsuit -- there was a litigation, and there  
12 was a damages award, but we're not head-to-head  
13 competitors with them. That's one damage amount to us -  
14 that they were using our patent.

15 The other aspect of this dealt with the first  
16 competitor, who's not in our area, but comes in to our  
17 area with the infringing device, takes over our area and  
18 precludes us from marketing new products. Same patent,  
19 but totally different situations in terms of damages  
20 here. We're much more highly damaged, the numbers being  
21 the same, from the second guy than the first guy.

22 So if you're looking at assessing damages based  
23 on the contribution of the patent, you're actually  
24 eliminating the differences between or could be  
25 eliminating the differences between potential

1 infringers, and the position that they stand in can be  
2 quite different in the marketplace and quite different  
3 in terms of damage to the patentee in individual cases.

4 MS. MICHEL: Jack, have you seen a change in the  
5 way willfulness is litigated since the Federal Circuit's  
6 decision in *Seagate*?

7 MR. SKENYON: Not in terms of how it's actually  
8 presented at trial, but in many cases, you don't -- I  
9 think now what has happened is more times than not the  
10 willfulness case is thrown out by the Judge at the end  
11 of testimony as a directed verdict. I never saw that  
12 before, but that happens now, but it doesn't matter to  
13 the patentee.

14 The patentee has already put in the bad stuff,  
15 the bad evidence, and basically the jury has all heard  
16 it, and it will factor into the jury's decision on all  
17 the issues.

18 MS. MICHEL: Gail?

19 MS. LEVINE: I wanted to go back to some of the  
20 comments we were talking about earlier in terms of  
21 reasonable royalties.

22 MS. MICHEL: Can we come back to that actually?

23 MS. LEVINE: That's fine.

24 MS. MICHEL: Tom, any comments on lost profits?  
25 I want to bring out -- we'll bring out a couple more





1 damages enhancements really ought to really play a small  
2 role as well.

3 MS. MICHEL: Bruce?

4 MR. BURTON: You asked for comments about lost  
5 profits. I just wanted to share some information from  
6 doing a lot of cases and see what the panels' experience  
7 is as well.

8 Essentially what seems to be happening in the  
9 lost profits cases is there -- although there's still  
10 the pro forma addressing of the *Panduit* factors -  
11 essentially what goes on is a determination of whether  
12 the patent owner would have made the sales, infringing  
13 sales, and essentially you can almost collapse it all  
14 down to: Can you go into court and prove that you would  
15 have made those sales.

16 And if you can do that -- you are reconstructing  
17 the marketplace, if you can do that, you're going to be  
18 entitled to your lost profits.

19 MS. MICHEL: In that sense, the apportionment  
20 issue has arisen in the case law, areoe, thc5lly to the

1 profits? How should the law respond? Aron?

2 MR. LEVKO: First of all, the question of  
3 apportionment of lost profits, *Panduit* factors are fine  
4 as a pro forma as has been pointed out by several folks,  
5 and maybe even useful. The but-for situation should  
6 take into account really not just the market definition,  
7 but the market size and segmentation.

8 Oftentimes an infringer comes into the market,  
9 and I'm not pro infringer or patentee because I have  
10 testified about equally for both, but I have had several  
11 instances where the alleged infringer comes into the  
12 market and enlarges the market through advertising,  
13 through reputation, through service levels that don't  
14 deal specifically with the functionality of the product.  
15 Another aspect -- and that isn't reflected all the time  
16 in this litigation.

17 The other thing is that pricing mechanisms need  
18 to be taken into account. A slightly different price,  
19 lower price or creative pricing might indeed again  
20 enlarge the market or get to certain customer  
21 demographics that the patent holder didn't have  
22 initially.

23 *Crystal Semiconductor* is a case in point where  
24 just doing an elasticity sort of economic analysis could  
25 skew exactly how many units really could be claimed as

1     lost profits.  And then finally the infringer, if they  
2     didn't have that infringing product in the market, might  
3     have another product.  
4

1 terms of frequency or amount.

2 But that's some reflection of at that time  
3 whether there was an independent opinion and the  
4 behavior of the parties during litigation and so forth,  
5 just to put some thought into different aspects of it.

1 offering, we have to decide what small means, first of  
2 all, but the way to do that is just say what would the  
3 defendant have done in the but-for world where it didn't  
4 infringe.

5           Now, that may be as Aron was saying -- maybe  
6 they had an older product they could have offered.  
7 Maybe there's a different way to offer that infringing  
8 feature. Maybe the infringing feature could just be  
9 dropped from the product, and you offer a somewhat  
10 inferior product.

11           The first thing you have to do is figure out  
12 what to do there, and then you say: How would consumers  
13 have responded to that, and some consumers are going to  
14 have decided not to buy the alternative product or maybe  
15 there's no product at all in which case they would all  
16 have to switch to something else, but you figure out how  
17 many of them would have gone to the patented product.

18           And again in antitrust we're doing something  
19 similar all the time, and so in a merger analysis, we're  
20 interested in how close the two merging companies

1           So it's very straightforward, and you don't have  
2   to get into apportionment or you don't have to worry  
3   about the entire market or the entire product. It's  
4   simply what would have happened, and I think by actually  
5   using these terms and these concepts that really don't  
6   have a good economic basis, it actually confuses things,  
7   and that's one of the problems that we face when we're  
8   in a real one of these cases.

9           MS. MICHEL: Bruce?

10          MR. BURTON: Well, I actually took my tent down  
11   because you said at the end exactly what I was going to  
12   try to summarize, what would have happened, and Aron did  
13   a wonderful elaboration of all the challenges, but  
14   essentially it boils down to, considering all these  
15   factors, what would have happened? What sales would  
16   they have made and at what price and to whom?

17          Those are the type of questions that you have to  
18   answer, and that's part of the reason why you're seeing  
19   reasonable royalty becoming more prominent than lost  
20   profits. It's getting to be a real tough calculation.

21          MS. MICHEL: Paul?

22          PROFESSOR JANICKE: I agree completely with what  
23   Greg said, and I think where that comes out in terms of  
24   your question is the entire market value is really a  
25   meaningless cliché that we should get rid of. It

1 doesn't do anything to help with any calculation on lost  
2 profits.

3 MS. MICHEL: Jack?

4 MR. SKENYON: First of all, I know there's a lot  
5 of interest in this entire market value analysis, but  
6 quite frankly it doesn't occur in that many cases to  
7 begin with, so I'm not sure how big a problem it is by  
8 any stretch of the imagination, but in terms of the lost  
9 profits analysis to begin with, I think in any of these  
10 damages cases, we are running into more and more  
11 problems because of the tendency to go further and  
12 further into fantasy land as to what could have  
13 happened, what might have happened, what should have  
14 happened, and it's endless. It's an endless stream of  
15 things.

16 I think it's better to look at the lost profits  
17 cases from the point of view of the infringer sold some  
18 products. Their customers bought the products. What  
19 would those customers have bought instead, assuming the  
20 infringing product is off the market?

21 And one of the strange things that I don't see  
22 in too many patent cases is that the infringer is in a  
23 unique position to respond to that. It's their  
24 customers, but you rarely see situations where  
25 they're introducing survey evidence of their customers



1 as to what they would have bought instead or anything or  
2 any legitimate hard evidence along that line. In fact,  
3 the only survey evidence that was ever attempted to be  
4 introduced against me in a case, and it was very, very  
5 powerful evidence was something that the other side  
6 withheld and didn't get it in procedurally.

7 That at least is concrete. Where we're dealing  
8 with the fantasy land issue about what could the  
9 infringer have done instead, what could the other people  
10 have done instead. I think that -- if you want  
11 something that's going to be difficult for juries to  
12 grasp or figure out or sort through, I think that's what  
13 you're talking about.

14 MS. MICHEL: Tom?

15 PROFESSOR COTTER: Mostly I would just want to  
16 echo what some of the other panelists have said, that I  
17 think that patent damages insofar as lost profits are  
18 or something really ought to be administered procedurally.

19 I think that the type of analysis that I  
20 have seen in the cases that I have seen is that I  
21 think that the type of analysis that I  
22 have seen in the cases that I have seen is that I  
23 have seen in the cases that I have seen is that I  
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28 have seen in the cases that I have seen is that I  
29 have seen in the cases that I have seen is that I  
30 have seen in the cases that I have seen is that I

1 and there's really no getting around that. We do the  
2 best we can, but we're never going to know for certain  
3 what the state of the world would have been but for the  
4 infringement.

5           But one possible thing if you think about in  
6 this context, and Mark Lemley has raised this in one of  
7 his papers on damages, maybe there are some cases in

1 and any other comment you were going to raise?

2 DR. LEONARD: I think on that, I would just use  
3 the same standard that you use in an antitrust case.  
4 Again, I'm not a lawyer but as I understand it, you are  
5 allowed some amount of latitude because you wouldn't be  
6 in that situation if the defendant hadn't done what they  
7 had done, so it's sort of the same thing here I think.

8 I just wanted to go back just for a minute to  
9 the entire market value rule because I think there are  
10 two other additional points that are worth raising.

11 One is how it relates to so-called convoyed  
12 sales and how that's changed over time. I think the  
13 Court has made it hard to -- the CAFC has made it hard  
14 to get lost profits on convoyed sales, even if that  
15 convoyed product was sold directly because of the sales  
16 of the product that for which you lost sales directly  
17 due to the infringement, and I think that is sort of too  
18 bad because that is an under-compensation.

19 Now, I agree, you have to show that there's a  
20 causal link, that you would have made the convoyed sales  
21 if you had made the other sales. There's no question  
22 there's an element of proof you have to make there, but  
23 if you can make it, it seems to me that that should be  
24 allowed.

25 And then the second thing is just going back to

1 that idea of what a small component is, I think two  
2 extreme examples help demonstrate this and again how if  
3 you look at things from an economic point of view, you  
4 don't have to worry about defining something as small or  
5 not.

6 So if you have a product -- I had a case where  
7 basically the product was a piece of material wrapped  
8 around a metal cage, if you will. It was a stent graft,  
9 and the basic idea was if -- the patent addressed the  
10 combination of the two -- and so if you didn't have that,  
11 the material outside, you really didn't have a product  
12 that anyone was going to use.

13 Yet the other side was arguing, Well, there  
14 shouldn't be any lost profits here or it should somehow  
15 be apportioned because the metal part of it wasn't  
16 really part of what was covered by the patent. Again  
17 that's in a way just silly, because the point is if, in  
18 the but-for world, you would have had no product, those  
19 customers would have had to go somewhere else.

20 It doesn't matter that the material was only  
21 half the product. The point remains that from the  
22 supply side, those customers wouldn't have had any  
23 product to buy, and so they would have had to switch to  
24 something else.

25 So now there are other cases where maybe

1 removing the infringing feature would leave a saleable  
2 product, and in that case, a lost profits analysis  
3 should again just look at the customers who would have,  
4 because of the inferior product, switched to something  
5 else.

6 So the apportionment really works through  
7 looking at what consumers would have done given the set  
8 of available alternatives, and it really requires  
9 looking at both the supply and the demand sides, and I  
10 think that's another deficiency that comes up when  
11 people do lost profits analysis.

12 MS. MICHEL: Aron?

13 MR. LEVKO: Yes, just to comment on some of the  
14 other folks. Regarding the Court imposing restrictions  
15 on lost profits, a lot of that can be gotten around if  
16 you get into specific customer information, and Jack had  
17 mentioned that he sees a lack of survey evidence. It  
18 doesn't take a lot. You don't have to have a survey,  
19 but if you talk do a couple, three main customers to  
20 find out what they would have done, particularly in an  
21 industrial sales setting or a distributor, and to see if  
22 indeed they would have tried at least to get two  
23 suppliers or would they have stuck to one supplier or  
24 whether they've ever bought from this infringer before.

25 That often reveals some not broad landscape as

1 to what everybody would do, but certainly enough  
2 persuasive measures, one way or the other, as to what  
3 their alternatives would have been. Oftentimes you will  
4 find that buyers, particularly if they're large  
5 industrial buyers, don't want one supplier. They want  
6 two suppliers, and so that makes it more difficult to  
7 have a lost profits case.

8 On the other hand, if the infringer really had  
9 not been in that distribution channel before or had not  
10 had the relationship with the customers before, how can  
11 they say that they would have made a sale with something  
12 else because they haven't been successful?

13 So I think plowing the ground a little more  
14 deeply, along the lines with what a number of people  
15 have said, will get into the economic aspects of whether  
16 lost profits indeed are relevant here.

17 When you're dealing with the entire market value  
18 rule, as Greg points out, I've been involved in both  
19 sides of that, both in terms of medical instruments,  
20 which indeed where you put a notch here or a drug  
21 coating there or a slight design change oftentimes gives  
22 you a new product, and in fact the patent then really  
23 more or less encompasses the entire product.

24 When you get into other industrial product uses,  
25 telecommunication uses, oftentimes the patent itself may

1 be just a portion of the product. It may be a new  
2 wiring harness or it may be some component or accessory  
3 to an automotive vehicle. You have to take it case by  
4 case.

5 So the entire market value rule, I mean we're  
6 kind of downplaying it a little bit. There is a basis  
7 for it, but it's based on really what does that patent  
8 do in terms of transforming the product, and if it makes  
9 a brand new product like maybe a fuel injection in an  
10 engine, makes it a brand new model, well that's the  
11 entire product. If it's a notch on a catheter or a drug  
12 coating on the stent yes, that's a new product.

13 But if you're talking about an intermittent  
14 windshield wiper or a new type of coating on a component  
15 for less rusting, I don't know if that constitutes the  
16 entire product contribution. That's a very tough thing,  
17 and it may not be manufacturing costs. The  
18 manufacturing costs may be fairly limited or even the  
19 investment.

20 It's how if it really economically distinguishes  
21 that product in the market to define the market. You're  
22 back to that concept of defining the market.

23 MS. MICHEL: Related to this point of whether  
24 courts are too hesitant to award lost profits, under  
25 what circumstances should a patentee who makes the

1 patented product receive a reasonable royalty instead of  
2 lost profits? Are there such circumstances? Any  
3 thoughts? Jack?

4 MR. SKENYON: Well, the court actually I think  
5 addressed that in the *Rite-Hite* case because that was a  
6 case where the patentee made a patented -- used the  
7 patent to make one of the dock levelers that it made. I  
8 think it was -- I probably get them mixed up, but it had  
9 an automatic one with a motor, and I think the patent --  
10 that was the patented one that the patentee was selling,  
11 and it made another one that was a manual one that was  
12 not covered by the patent.

13 The infringer actually made only a leveler that  
14 was manual that competed with the manual one of the  
15 patentee, for which it got -- the patentee got some lost  
16 profits damages. The rest becomes reasonable royalty.

17 So the net effect of that was that the patentee,  
18 practicing its invention, because of the facts of the  
19 case and how the market divided with the products, was  
20 entitled to a reasonable royalty in the circumstances,  
21 so I think that's a case, and there are others, that  
22 fall in that category.

23 MS. MICHEL: When talking about reasonable  
24 royalties, is the hypothetical negotiation the right  
25 construct, the right approach? Is it just the best



1 thing we can come up with, even though it's not great?  
2 Gail, we'll hear your thoughts.

3 MS. LEVINE: Well, I think the hypothetical  
4 negotiation is a useful tool, but there may be better  
5 tools out there. Professor Cotter highlighted one  
6 earlier this morning where I think you called it the ex  
7 post test, right? And as I understand it, the test, the  
8 crux of that test, which makes a lot of economic sense, is  
9 the test asks for the technological value of the patent,  
10 what's the patent value over the next best alternative  
11 that the infringer could have used? What's really  
12 important if you're applying that test properly is the  
13 timing.

14 After lock in, after switching -- after the  
15 infringer has incurred a whole lot of switching costs,  
16 if that's present in this case -- the  
17 infringer may have a lot fewer substitutes to turn to in  
18 an economic sensible way. So it's important to ask,  
19 sometimes -- not at the date of infringement necessarily --  
20 whether there were next best alternatives and look to  
21 the delta between the next best alternative and the  
22 infringing option then.

23 It's important instead to go back before the  
24 switching costs were incurred and ask at the time -- it  
25 may be, for example, at the time the product was

- 1 designed, then what next best alternatives were
- 2 available, what non-infringing substitutes were then
- 3 available. on 2 8ilabilable, what non-infringing substitutes were

1 MS. MICHEL: Focusing for a minute on the  
2 concept of the hypothetical negotiation and what we  
3 might call an alternative of the value of the  
4 alternatives, do we need a new legal rule to talk about  
5 the value of the alternatives, or as in *Grain*  
6 *Processing*, is that just the maximum the infringer would  
7 have paid in a hypothetical negotiation?

8 I'll throw that question out along with any  
9 other comments you might have on the hypothetical  
10 negotiation. Anne?

11 MS. LAYNE-FARRAR: Well, I think this follows up  
12 on a point made just a minute ago about the value of the  
13 patent having a great deal of difference depending on  
14 who's using it, so you really can't say what is the  
15 value, the economic value of a particular patented  
16 technology.

17 That value depends a what use it's going to be  
18 put to and some uses may be highly valuable and others  
19 may be trivial, and those two parties shouldn't have to  
20 pay the same in reasonable royalties. What's reasonable  
21 for those two parties differs a great deal.

22 If I can just expand a little bit on what Gail  
23 said, I agree that when you set these hypothetical  
24 negotiations, you want to eliminate the ability of a  
25 patent holder to act opportunistically and exploit the

1 switching costs, but you also want to think about why  
2 the license didn't happen before.

3           And over time, I think this was also raised  
4 earlier this morning -- over time, lots of kinds of  
5 risks change. When a technology is brand new, you don't  
6 know whether it's going to be commercially successful.  
7 There's a lot of uncertainty around whether it can

1 first of all, it's really exciting to hear new proposals  
2 and different ways to go about calculating damages, but  
3 one of the challenges that I see with most any of the  
4 proposals that puts a single factor first or makes that  
5 the primary one of which then you're going to do some  
6 other kind of judgmental adjustment up or down is that  
7 it doesn't really recognize the differences in  
8 circumstances of the patent, of patent litigation.

9 I think everyone here has worked on hundreds if  
10 not more, thousands of cases, and one thing that I'm  
11 continually struck by is they're different, and it's  
12 really important to be flexible in your analysis, hold  
13 true to some principles but to have the full array of  
14 tools available to you as an analysis in order to assess  
15 the situation and assess the views of the plaintiff,  
16 assess the views of the defendant, look at the  
17 hypothetical negotiation, look at the information  
18 available to them, the date of the hypothetical,

1 say. If you're going to compensate for the damage,  
2 well, essentially you're reconstructing a negotiation  
3 with slightly different assumptions, valid, infringed,  
4 enforceable. You're reconstructing that negotiation,  
5 and then having factors played out to put the patent  
6 owner in a situation very similar to what they would  
7 have been in.

8 MS. MICHEL: Paul?

9 PROFESSOR JANICKE: I just want to clarify  
10 because apparently I gave several speakers the  
11 impression that my value added single factor proposal  
12 lacked flexibility. I want to emphasize that I wasn't  
13 implying that the number or percentage or whatever  
14 should be the same for all defendants.

15 Of course it shouldn't. The value added for the  
16 defendant in the particular case is what I meant to  
17 indicate by value added, not to say that there was some  
18 universal value number attached to a given patent.

19 Secondly, I get worried about integrating as  
20 many factors as Bruce has just outlined, even though  
21 they're logically sensible factors that should be  
22 integrated, because we're asking 12 people off the  
23 streets of Marshall, Texas, to do this. There's really  
24 a limit to what juries can focus on in a case.

25 So that's another reason why I prefer my highly

1 flexible value added factor, single factor.

2 MS MICHEL: Greg?

3 DR. LEONARD: I would just like to briefly say  
4 that ex ante versus ex post, ex ante has the virtue of  
5 returning the parties to where they would have been if  
6 they had agreed that the patent was valid and infringed,  
7 and as a result of that, instead of having to proceed  
8 forward with litigation, had decided to settle the  
9 matter right then and there.

10 I think that has certain virtues because among  
11 other things, it avoids a sort of ex post sample  
12 selection problem, which is you would only get lawsuits  
13 in cases where the patent -- the defendant turned out to  
14 have a very successful product, which I think is not  
15 necessarily a good thing.

16 So if there was a lot of uncertainty at the time  
17 of the date of the hypothetical negotiation, then that  
18 would have led to a much discounted royalty rate. I  
19 think that's something to take into account to set up  
20 the incentives properly for litigation and for  
21 settlement.

22 MS. MICHEL: Aron?

23 MR. LEVKO: I guess going to the framework of  
24 the hypothetical negotiation, I think it's appropriate  
25 from the standpoint it sets up the right valuation

1 principles, and if indeed we're trying to tie this  
2 exercise into some more rigorous framework and  
3 potentially have it within policy of law, I think it  
4 should be adhere more to valuation principles, which  
5 means that you do need a date of which to agree upon.

6           Given that date, I agree with some of the  
7 speakers that the ransom, or the fact that there's some



1 big differences should lie between compensating a non  
2 practicing entity and a practicing entity.

3 A non-practicing entity doesn't really bear a  
4 lot of risk out there, other than having the bare patent  
5 rights. When you enter into competition in a  
6 negotiation, less has been made it seems in the  
7 *Georgia-Pacific* factors, for instance, which one of the  
8 assumptions are it's a willing buyer, willing seller,  
9 and it kind of just blows right past that.

10 That's not true. That's a big, big factor in a  
11 real-life negotiation, and I think it should be a big  
12 factor in a reasonable royalty determination in a  
13 litigation. If indeed you're dealing with a competitive  
14 aspect at risk of losing sales, even though you can't  
15 identify the lost profits, it should have a profound  
16 impact in the damages part of the valuation calculation.

17 So going back, there should be a hypothetical  
18 negotiation. It should be constructed along the  
19 valuation principles. It should be prior to sunk costs  
20 because the valuation principle wouldn't reflect that in  
21 going forward, and if you're looking forward, you do  
22 have some benefit because you're in a litigation sense  
23 rather than a real-life negotiation, and that there is a  
24 difference between a non-practicing and a practicing  
25 entity because of the willingness to license and the

1 competitive factor.

2 MS. MICHEL: Ed?

3 MR. REINES: So as implemented in courtrooms  
4 around the country, the hypothetical negotiation is  
5 basically a free for all. It sounds like there's pretty  
6 much a consensus that that's so, and I think part of the  
7 cause of that is the entire market value rule being  
8 applied in the reasonable royalty context, because it's  
9 sort of displaced or atrophied Federal Circuit law  
10 development in the area of: How do we put some  
11 boundaries around the hypothetical negotiation? How do  
12 we prioritize factors that matter? So there's sort of  
13 an absence of law and guidance, and that's especially  
14 true on what the base should be.

15 I mean, you can -- the numbers were 90 appeals a  
16 year on patents. I don't think that there is very  
17 little damages law for many other reasons other than the  
18 fact that there's not a lot of legal boundaries that are  
19 being placed on that. I realize that that opens a whole  
20 other kettle of fish, so to speak, so I think right  
21 now as implemented, the hypothetical negotiation is  
22 deeply flawed because there's no real boundaries for how  
23 it's been.

24 One of the things, the projects I've been  
25 involved with, Chief Judge Michel put a group together

1 to put jury instructions together, and one of the steps  
2 we've taken is to create a damages instruction that  
3 attempts to modernize *Georgia-Pacific*. It's not a cure-  
4 all for the weakness of that test, but it at least  
5 attempts to try to bring it to the modern age in terms  
6 of the obtuseness and the repetitiveness that can be  
7 quite tedious when you're in a trial situation.

8 So that's one step that's been taken, but I  
9 think there needs to be some real legal improvement for  
10 how it's done.

11 MS. MICHEL: Tom?

12 PROFESSOR COTTER: Yeah. I agree with much of  
13 what the preceding speakers have said, and I guess  
14 here's how I would think of or frame the hypothetical  
15 negotiations. What we want the hypothetical negotiation  
16 framework to focus on, make it more rational and more  
17 predictable, is to ask: What is the projected economic  
18 value to the defendant of using this technology in  
19 light of the other possible alternatives they could have  
20 used before they incurred the switching costs?

21 I think that's really the question we ought to  
22 be focusing on in trying to replicate the hypothetical  
23 negotiations, and that raises two issues that I just  
24 want to briefly point out.

25 One is: Should there be a discounting then for

1 the legal risk, as I think Aron and maybe Greg mention  
2 indeed? I think that actually is not a good idea, and  
3 here is one area where I think the existing case law is  
4 actually - I won't say surprisingly rational, but I  
5 think the existing case law actually gets it right.

6 The existing case law says in trying to  
7 reconstruct the hypothetical negotiations, we will  
8 assume that the parties were negotiating based on the  
9 assumption that the patent was valid and infringed.

10 That actually makes sense, and this was actually  
11 pointed out in a paper by Steven Callas and Jonathan

1 the amount we would expect the parties to divide up in  
2 these hypothetical negotiations.

3 Now, if the defendant were to walk away and uses  
4 the technology and plaintiff files suit, goes to trial,  
5 the plaintiff in going to trial recognizes that there's  
6 a 56 percent chance that they'll prevail at trial. So  
7 if at trial the plaintiff prevails and we award  
8 \$560,000, the plaintiff's expected earnings from going  
9 to trial is only 56 percent of \$560,000. We're under-  
10 compensating the plaintiff. We're discounting twice for  
11 the legal risk.

12 So to prevent that, the law currently,  
13 rationally says, When we do the hypothetical negotiation  
14 calculation, we'll assume patent validity and  
15 infringement. The legal risk is already taken into  
16 account by the fact that the plaintiff had to go to  
17 trial to vindicate its rights.

18 The other issue, the entire market value rule, I  
19 agree that there's a sense in which it's just a complete  
20 category mistake to apply that in the reasonable royalty  
21 context. But I think it could potentially play a role in  
22 the following sense. If we really are trying to  
23 replicate what the parties would have done ex ante, one  
24 methodology they mi.00 g0oar metid ea ante, is ao ap rgatdnWf., eh

1 based on actual sales of some final product.

2 So if that's the methodology that best  
3 replicates how the parties themselves would have valued  
4 a patent license, I don't think there's anything  
5 particularly offensive about using the end value of the  
6 product as the royalty base in this context.

7 The problem comes in the application where  
8 courts and juries are not exercising much judgment in  
9 determining what the royalty rate is. The royalty rate  
10 based on the -- the royalty rate that you would be  
11 multiplying by the end value of the product might be  
12 very, very small, and that is something that I think we  
13 need to provide some guidance on: What's the applicable  
14 royalty rate, if we're going to use the entire value of  
15 the product as the royalty base.

16 MR. REINES: Suzanne, I just want to say  
17 something real quick on that. Just in the world that I  
18 see and dwell in, there's a lot of products where the  
19 revenue numbers can be so huge, \$50, \$60, \$70 billion, even  
20 annually, and to expect someone to say if something is the  
21 twig on the twig on the twig on the twig on the twig of  
22 a multi-featured box, to expect a jury to sort of  
23 embrace sort of a .00000001 rate and still make a  
24 hundred million dollars or whatever it is is not - that  
25 is not really the real world that I see.

1           You really have to control the base if you want  
2 a rational outcome in those situations. Once \$80 billion  
3 goes up -- and a lot of times the cards on which the  
4 patent inventions are sold separately, so it's not  
5 like you don't have an invoice price that you could  
6 say is, which is a small fraction of it. So I really  
7 think that exaggerated base can be a very big problem  
8 for a rationale outcome for the reasons I just stated.

9           MS. MICHEL: How should we go about determining  
10 what the base is then? Gail, and any other comment you  
11 were planning to offer?

12           MS. LEVINE: It's a good question. I think the  
13 more important question though should be what the base  
14 times rate equals, right? If you start by looking at  
15 that number, you're going to be I hope coming up with an  
16 economically sensible result, so the question as we've  
17 been talking about before is: What's the value added?  
18 What's the economic value of the patent for this  
19 defendant over against the next best alternative?

20           If this patented technology allows the defendant  
21 to sell the product for a dollar more than he otherwise

1 question to start with isn't what's the base. The  
2 question to start with is: What is the economic value  
3 of the patent? Once you've got your economic witnesses,  
4 once you've got the jury all focused in that direction  
5 instead, not on the question of what's the base, I think  
6 you're going to come up with a lot more -- less  
7 unpredictable, more economically rational jury verdicts.

8 MS. MICHEL: Ed, your thoughts on how this would  
9 work in court?

10 MR. REINES: I mean, I just don't see the system  
11 rejecting the whole concept of rate multiplied times  
12 base, which is sort of -- in a sense you're proposing  
13 everything will be lump sum, that there's an assigned  
14 dollar value which keys off of a margin, which in your  
15 case is a dollar in your hypothetical, and certainly one  
16 side can argue that. The other side is not going to  
17 argue that.

18 The plaintiff is always going to attempt to put  
19 the huge revenue number up on the screen, and it really  
20 is unringing the bell. There's just a lot of smart  
21 people. If you get a number up on there that's \$60  
22 billion and someone says, if you give them a hundred  
23 mon anddIch kttdvging thoiEi4lely any of it. It



1 hundred cards and that doesn't include the whole other,  
2 that's just a card going into the big box, and  
3 plaintiffs will routinely -- I've never seen a plaintiff  
4 not claim entitlement to the overall box as the revenue  
5 amount.

6 And you just can't un ring the bell, so the right  
7 question is Suzanne's, which is, OK, how do you -- unless  
8 we come up to a different -- where someone says, you're  
9 absolutely prohibited from doing that, you just assign a  
10 dollar value, which I don't think that's a world on the  
11 horizon.

12 What's the base? How do you regulate that? I  
13 think there's two flaws there. The first flaw, and I'm  
14 glad to see there's been discussion on this in Congress  
15 and elsewhere is having some sort of gatekeeping, some  
16 meaningful gatekeeping so that people are looking at  
17 these questions flexibly: Is this reasonable? Is  
18 this within the range of reason pretrial? Because once  
19 you get that situation, you will get the development of  
20 law.

21 There's sort of an absence or there's a total  
22 absence of law, and so one of the benefits that I see of  
23 a gatekeeping, like a real procedural teeth in to say --  
24 to have a judge make findings and conclusions just like  
25 they would in other situations, not the conclusion but

1 is this reasonable? Does this get past the court to  
2 go to trial? Then you generate law and get sort of in  
3 this situation you can't do this, and in this situation  
4 you can't do this and we start creating boundaries which  
5 are much needed. There are also needs to be I think  
6 substantive law change accompanying that because of the  
7 absence of substantive law.

8 But in terms of base, it seems to me that there  
9 needs to be some sense of the closest unit that's  
10 priceable in the vicinity of the claimed invention. I  
11 don't purport to have magic how that's doable. I think  
12 what defendants aren't as effective at doing as they  
13 should be is finding invoice prices for components.

14 So if the accused infringer is buying a sub-  
15 component, there will be a price associated with it,  
16 right, because the big problem is if you're just selling  
17 a whole big box for one price, you start having an  
18 absence of alternatives for base. There either is no  
19 base or it's this big over-sized base. How do you deal  
20 with that?

21 I think looking at the cost side more often,  
22 just to give yourself a base, which is when they source  
23 this or when they source that: What are the numbers? But  
24 it's a challenge, and I think we need just more case-by-  
25 case decision-making and substantive change to help fuel

1 this.

2 MS. MICHEL: We will come back to the  
3 gatekeeping issue and explore that in-depth. It's a  
4 critical one.

5 For this round of questions, I would like the  
6 panelists' response to how to go about this reasonable  
7 royalty calculation. What is the role of the entire  
8 market value rule? How do we look at the base? How  
9 should we get the royalty rate or do we do a lump sum?

10 MS. LEVINE: Just to be clear, I'm not saying  
11 that all verdicts forevermore must always be lump sum.  
12 The idea though was though that the base should depend  
13 less on considerations, and I think Ed raises some very  
14 practical considerations.  
15 Just putting out  
16 big numbers for the sake of big numbers isn't what we're  
17 aiming for here.

18 The goal should be instead to look for a base  
19 that makes economic sense. You can have fights between  
20 experts as to what happens. It happens, as Greg  
21 points out, in antitrust cases all the time. What the  
22 relevant market definition is is a very similar question  
23 here, and we can have debates about it, but at least  
24 let's all work under the same economically sensible  
25 rubric in trying to figure that question out.

1 MS. MICHEL: Anne?

2 MS. LAYNE-FARRAR: Yeah. I would like to start  
3 with the discussion of the base and point out that I  
4 think you need more than just the invoice price. You  
5 need a price that's easily observable by the patentee  
6 and that cannot be manipulated.

7 So, for example, if a potential infringer is  
8 purchasing multiple components from the same source and  
9 those prices can be shifted so that the overall package  
10 is the same, they could make a deal, let's lower this  
11 price on this component, and then I have less to pay in  
12 royalties. So you need to think about how the firms are  
13 going to respond to: If this price is used as the  
14 base, what is their reaction going to be?

15 I think that's one of the things that drove the  
16 use of let's just look at the whole box because that's  
17 the price that's set by the market that the consumers  
18 are willing to pay.

19 I recognize the problems of putting the big  
20 number up. Certainly from an economic or a mathematical  
21 standpoint, as long as that component is used in a fixed  
22 proportion in the good, the base is irrelevant. You can  
23 always adjust the royalty.

24 If from a practical standpoint juries don't like  
25 to see those small numbers, maybe we need to work on

1 better instructions for them to understand that those  
2 aren't under-compensating, those little tiny royalties,  
3 because it is far easier, and certainly from an  
4 enforcement standpoint this is a big issue, particularly  
5 internationally where you have manufacturers say in Asia  
6 who under report on a regular basis.

7           And it's easy to under report if the prices  
8 aren't transparent, aren't posted in some public forum,

1 that makes sense as a base issue. That's one way to  
2 look at it.

3 Just a comment on sort of the best method of  
4 determination. I perhaps am a traditionalist because I  
5 see a lot of merit in a hypothetical negotiation,  
6 *Georgia-Pacific* approach. I think the flexibility in  
7 the gathering of data points is really central to doing  
8 a thorough and complete job, and perhaps the focus is:  
9 Why does that go astray? And there are some reasons it  
10 seems historically that sort of jump up that says:  
11 Here's some challenges you have to be alert to.

12 I'm not saying that these things are wrong. I  
13 think there is a place in a reasonable royalty entire  
14 market value. I think there are times when that is the  
15 right base to use, and you'd be unwise to view that. But  
16 there's also a lot of room for abuse in an entire market  
17 value rule. There's a lot of room for abuse in  
18 comparables.

19 A lot of comparables just plain aren't  
20 comparable, but it's hard for a jury to really see that.  
21 They don't work with technologies day in and day out,  
22 and even judges often don't, and it's very challenging  
23 to understand when someone puts forward something that's  
24 a comparable, why it is and isn't, and that can be an  
25 area of significant abuse, particularly if you haven't

1 matched your base, your royalty base, with your rates, so  
2 you're seeing comparables at 5 percent when you should  
3 be 1/10th of 1 percent on this particular base.

4 Rules of thumb, dangerous. It's only  
5 happenstance and luck if a rule of thumb is right in a  
6 particular circumstance, and yet people put rules of  
7 thumb forward as if they're gospel. It can be very  
8 misleading to rely on a rule of thumb that is not  
9 particularly -- that rule of thumb, again just like the  
10 entire market rule, could be right, but boy show us  
11 right by connecting to the product and the economics of  
12 that situation.

13 Then I would also posit that it's a challenge  
14 when people don't consider all the factors, and I don't  
15 mean factors in the sense of *Georgia-Pacific* factors,  
16 but all the relevant economics, because people will hone  
17 in on a particular aspect, totally ignoring the greater  
18 environment, in which that data should be interpreted,  
19 and by doing that you can get very misleading results  
20 that can be hard to refute without a lot of work and a  
21 lot of explanation.

22 So I'll just leave it with that, that it's not  
23 so much in my mind the methodology as some of the ways  
24 some of the tools within the methodology are applied.

25 MS. MICHEL: Paul?

1                   PROFESSOR JANICKE: Yeah. I think the reason we  
2 got into the whole issue of base is because we got into



1           PROFESSOR JANICKE:  It's supposed to, according  
2 to case law anyway, and real life changes the style of  
3 negotiations and what people would really do if they  
4 were willing, then what we do in the courts should  
5 change to match that.

6           MS. MICHEL:  Why is the unit not the base if it  
7 came within a few cents of a unit?

8           PROFESSOR JANICKE:  Base only matters if you're  
9 going to do a rate times base calculation.  If you're  
10 going to do it five cents a unit, there is no base.  
11 There is no rate.  They agreed on five cents a unit or  
12 \$2 a unit, and base drops out of the calculation in the  
13 real license negotiation.

14           I'm told various numbers, but some people say 40  
15 percent of real licenses now are not based on rate.  
16 They are fixed amount of money per unit.  I don't know.  
17 It is certainly growing rapidly though.

18           My second point on this was:  Are you going to  
19 ask today anything about the problem of royalty  
20 stacking in the software industry?  Because that is an  
21 especially difficult problem for reasonable royalty  
22 thinking.  And by stacking, I mean the problem that if  
23 you come out with a software product of any considerable  
24 size, you are going to have to deal with 50 to 150  
25 patents.

1 MS. MICHEL: Can the hypothetical negotiation  
2 take that into account and should it?

3 PROFESSOR JANICKE: I'm at a loss as to how,  
4 because in an actual case, frequently the defendant  
5 doesn't know how many other hammers are out there about  
6 to fall on him and so on, but experience of the software  
7 companies seems to be uniform, that you come out with  
8 anything, and you're besieged with -- I'm assuming  
9 everyone is in good faith on both sides.

10 So they didn't know about these patents. They  
11 didn't see how they would apply to their product, which  
12 is what they say in court also, and the plaintiffs say,  
13 we're not particularly arguing about willfulness, but  
14 when we saw your product, we saw, Ah-ha, one of the  
15 routines in your software is covered by my claim 7, so  
16 nobody's trying to do anything underhanded at all.

17 It just turns out seemingly all the time that  
18 there is a huge number of patents to cope with, and if  
19 you start giving 1 percent to each one, the products  
20 will lose profitability in no time, and yet you can't  
21 account for all of the other ones in a given litigation.

22 I find it an exceedingly unsolvable problem.

23 TD( 22 u3 22 Eant)TjEs mi200 0.i-m.

1           PROFESSOR JANICKE: That wouldn't sell too well,  
2 and they wouldn't know about a lot of them, but from the  
3 settlement, since 86 percent of the cases are going to  
4 settle, they've got to be thinking, what else am I going  
5 to have to deal with on this product, so that the  
6 product can remain profitable?

7           And there is a large unknown that they have to  
8 deal with, but frequently a company like Microsoft, by  
9 the time they have to make this decision on whether to  
10 settle the case, they're aware of maybe 25 other patents  
11 that are a problem or that their owners of those patents  
12 say are a problem and probably another 25 percent that  
13 haven't surfaced yet, so what are they to do in a  
14 reasonable hypothetical negotiation world?

15           I think that is the main reason that's driving  
16 the Business Software Alliance to try to get probably an  
17 overly-specific definition into the patent reform  
18 statute. I don't think that's a particularly good  
19 solution, but I confess, I don't have a good solution.

20           MS. MICHEL: Jack?

21           MR. SKENYON: A couple things on this issue.  
22 First of all, the hypothetical negotiation scenario is,  
23 first of all, not the only way that you can compute a  
24 reasonable royalty damages. The Federal Circuit has  
25 approved at least one other way that's entirely

1 different or almost entirely different, and what Tom had  
2 proposed here, that could be asserted too, calculating  
3 of damages that way.

4           The risk you would run would be that the Federal  
5 Circuit has not approved that way of calculating  
6 damages, so if you're faced with that at trial, and it  
7 was \$10 million either way, you would probably go with  
8 the *Georgia-Pacific* factor knowing that wouldn't be an  
9 issue on appeal since the Federal Circuit's familiar  
10 with that and has proved that.

11           That said, I think the hypothetical negotiation  
12 scenario is looked at generally in the wrong way, and  
13 the way it is is this: Is that the statute itself sets  
14 the minimum value of damages as a reasonable royalty.  
15 That's the only mention of reasonable royalty that there  
16 is in the statute.

17           I think that legitimately is the royalty that  
18 you would pay if you sat down with someone who wanted to  
19 license your patent, there's no threat of litigation,  
20 and just came to some agreement. I think that's the  
21 minimum.

22           What I think that is is factor 15 of  
23 *Georgia-Pacific*, and I think the other factors in  
24 *Georgia-Pacific* can be used to drive up that rate, and I  
25 think that's how you should look at it. Once you've

1 driven the rate up, you can use some of the other  
2 factors to drive it down again.

3           Basically I don't think it's proper to look at  
4 the hypothetical negotiation scenario from the view of:  
5 Well, what could have happened, what should have  
6 happened, what might have happened, what we could do. I  
7 think that's where we run into some problems here, and  
8 one of the problems I think that Ed pointed out, which  
9 is a very important one, at least in some industries is  
10 the base problem here on this, is that if you approach  
11 it this way and you come up with a royalty number, the  
12 question is, not the royalty number. The question is  
13 the base it's applied for.

14           *Georgia-Pacific* is really setting the royalty  
15 rate, not the base necessarily. The base, if you stop  
16 and think about it, is supposed to be what the  
17 infringing product is, and in Ed's scenario, which is a  
18 fairly common one where the problem lies is, is that  
19 suppose in one case the patent covers the little circuit  
20 he mentioned, but suppose in another case they've gotten  
21 a claim that deals with the whole system, of which that  
22 patented circuit is part.

23           So now what's the base? If it's the infringing  
24 product, we're talking about the whole system, even  
25 though only a little part of it is really important in

1 terms of patentability, so I think my suggestion would  
2 be here is that, first of all, keep in mind what the  
3 hypothetical negotiation is really supposed to be about.  
4 Don't put too much into it.

5           There are *Georgia-Pacific* factors, I do not know  
6 what they mean. There are *Georgia-Pacific* factors that  
7 I cannot find a case anywhere at any time that has  
8 turned on that particular factor.

9           So all it is is just a general guideline, and  
10 there are other ways to do this here, some have been  
11 approved by the Federal Circuit, that might be more  
12 appropriate in a particular case. And if you wanted to  
13 approach this from that point of view here, that the  
14 answer on this base question may be that you want to  
15 install a rule, if you will, that maybe the  
16 *Georgia-Pacific* application is not to be used in certain  
17 cases, or to have the judge formulate which one is,  
18 because otherwise I think the problem is absolutely  
19 insoluble on this base issue, which is a critical issue  
20 I think, as Ed pointed out in some industries.

21           It doesn't come up in other industries but it  
22 does in the software and electronics field.

23           MS. MICHEL: It is interesting that you say  
24 there are *Georgia-Pacific* factors for which -- you have  
25 never seen come up. How common is it then to include in

1 the jury instructions just a list of all 15 factors, and  
2 if we do that, do we risk not giving the jury good  
3 guidance?

4 MR. SKENYON: : I think the reason the factors  
5 are all listed is because there's a propensity for the  
6 district courts to adopt form jury instructions, and  
7 each form jury instruction on damages that I've seen  
8 that deals with *Georgia-Pacific* will include all the  
9 factors. Because potentially all the factors could be in  
10 there -- very little interest in crossing out ones that  
11 don't seem to apply when you get to that stage in the  
12 litigation.

13 But I'm not sure that the jury actually makes  
14 a decision on damages in any case by going through all  
15 the *Georgia-Pacific* factors. I just don't believe it.  
16 I think when the jury makes a decision on damages, it has  
17 actually very little to do with the damages presentation  
18 to begin with.

19 What I think happens is this: Is that you have  
20 a verdict form that includes -- there's an infringement  
21 question, and there's multiple claims usually that you  
22 have to decide, and then there's probably maybe a  
23 willfulness question. Maybe there's invalidity issues  
24 on various things, and my belief is that as soon as the  
25 jury starts deciding against the defendant in one, it's

1 easier for them to rule against them going down the  
2 line.

3 So by the time you get to the damages question,  
4 which is the last question, they're not rowing in the  
5 defendant's boat any more. They are firmly in the  
6 plaintiff's camp, and if the plaintiff put down a number  
7 of \$15 million based on the moon being made of green  
8 cheese, I think the verdict is going to be \$15 million.

9 In most cases, I think that's what happens is  
10 they spend very little time, I'm being a little bit  
11 flippant as to what the juries will do -- but I don't  
12 think they spend very much time on the damages issue at  
13 all. I don't think it's a question of guidance of the  
14 jury.

15 I think it's a question of pre-loading with the  
16 judge some limitations on the damages that can be  
17 presented in a particular case, because I think once you  
18 get to the jury, I think if they're going for the  
19 patentee, it's hopeless, and in a lot of defendants'  
20 cases, I don't even put on a defense on the numbers  
21 simply because I think it's a waste of my time.

22 PROFESSOR JANICKE: *Georgia-Pacific* factor 16.

23 MR. SKENYON: Nothing I say is intended to amend  
24 *Georgia-Pacific* and associate me with it.

25 MS. MICHEL: We have two very significant issues



1 on the table at this point. One is how to think about  
2 the base. The other is how to deal with the  
3 *Georgia-Pacific* factors, how to deal with juries and the  
4 fact that perhaps the jury is not doing the complete  
5 analysis there.

6 Greg, let's go to you.

1 base if the plaintiff's expert is allowed to get up and  
2 say 1 percent.

3 So it seems to me that's where the judge has to  
4 step in and not allow that kind of testimony, and at  
5 that point the jury, unless they go off on their own,  
6 which I guess they're allowed to do that, but if they  
7 only hear two numbers that are very small, my guess is  
8 they're going to choose one of those numbers or something  
9 in between.

10 So I think in the end the base problem is going  
11 to be solved by essentially constraining experts to  
12 testify about things that actually make economic sense.  
13 And if the jury doesn't hear outrageous numbers, then  
14 they're not going to award an outrageous number.

15 MS. MICHEL: Aron?

16 MR. LEVKO: Since we've heard a lot about  
17 economics, let me add in there auditability, and we've  
18 kind of not touched on that point.

19 Regarding the base, if this is supposed to --  
20 that is, litigation, the hypothetical negotiation is  
21 supposed to simulate real life negotiations in a  
22 license agreement, you've got to have that to be  
23 auditable, and so on a basis of accounting. That's why  
24 oftentimes it does go to a unit basis rather than a base  
25 dollars which can be manipulated.

1           So in that regard, it does make a difference how  
2 you call unit or dollars or time or whatever. Those are  
3 all bases. The numerator, I guess the rate could be a  
4 dollar per unit or certain a dollar per time or levels  
5 to be reached upon which lump sums are provided. All  
6 those things are auditable, so let me just clarify that.

7           If it's going to emulate and simulate a real-  
8 life negotiation, that's how those contracts take  
9 place. Now, also a lot of them take place, if you're  
10 going to do a lump sum, you need to do discount rates if  
11 you're going to do that. That hasn't even been  
12 discussed.

13           Discount rates are going to have all sorts of  
14 fanciful factors to be considered because take a look at  
15 business commercial litigation, all the discount factor  
16 gyrations that go in front of juries.

17           So we haven't even addressed that in lump sums.  
18 I don't want to begin to do that, but that needs to be  
19 reckoned as well if we're going to do a hypothetical  
20 negotiation.

21           The issue of stacking is one part of what I call  
22 the broader context of the dynamic marketplace; that is,  
23 is it one patent out of 10 that really drives the  
24 products? Then at what point do you lose any  
25 profitability? That is part of the market definition

1 and part of what indeed is the incremental margin  
2 approach towards a royalty calculation, be that on a  
3 rate basis or a dollar or unit basis, so that fits in  
4 nicely with what we've been talking about, but it's all  
5 a component thereof.

6 Okay. Regarding the *Georgia-Pacific* factors,  
7 let me clue you in. When I do -- and I have testified a  
8 lot, I'm into the triple digits, *Georgia-Pacific* factors  
9 are influencers on the rate. They don't have anything  
10 to do with the base. And I don't do a calculation on  
11 rate based on *Georgia-Pacific* factors.

12 I use basic valuation and economic principles  
13 called market, income and cost and variations thereof to  
14 determine a royalty or to determine a damages amount.  
15 Now, where the *Georgia-Pacific* factors come into the  
16 analysis is what are the various factors that either  
17 drive up or down the rate? And they can go either way.  
18 Those factors can go either way, and there are a number  
19 of factors that are not included in the *Georgia-Pacific*  
20 factor analysis that should be included.

21 We've already touched on a few of them today,  
22 one being the financial positions of the parties,  
23 whether they're practicing, non practicing entity,  
24 competitor, non competitor. Even though there's a  
25 discussion somewhat in *Georgia-Pacific* factor analysis,

1 it's not the bargaining positions that are truly  
2 addressed, although that has a profound influence both  
3 on real-life negotiations and should be in the  
4 litigation.

5 The business plans, that is, most businesses  
6 look at a patent or a product or a development as a  
7 ticket to the next stage of development in their  
8 business, and so what are those business plans? How are  
9 they accounted for in terms of doing a royalty  
10 negotiation? Is it a potential option for them to get  
11 to the next stage in development?

12 That's not reflected in the *Georgia-Pacific*  
13 factor analysis, and then we've talked about already the  
14 fact that just because you get into a royalty situation  
15 doesn't mean there isn't any lost profits. You just  
16 can't prove it conclusively.

17 So if you do get involved into a negotiation,  
18 there could be a risk of losing sales by licensing  
19 someone, and that's not reflected really in the  
20 *Georgia-Pacific* analysis.

21 So what I'm going to say is you need to have, in  
22 terms of determining a royalty -- whether to hi00 0.0000 0ls 20



1     circumstance, hopefully you avoid that the vast majority  
2     of the time.

3             Then it's sort of, Well, the standard is whether  
4     the jury had any basis for doing this, and I might as

1 allowed to touch the concept that there's a lot of  
2 patents in the general field. But no judge is going to  
3 let you get into the fact of -- here's other patents that  
4 actually cover this -- because of the sense that that's  
5 satellite litigation. What do you do, *Markman*  
6 hearings on 15 other patents?

7           So you can't really ever demonstrate that, and  
8 then of course I think maybe the central problem in  
9 distorting the situation, not in every product in every  
10 field, but in the problem area, is you spend two weeks  
11 of these jurors' time pulling them out of their  
12 day-to-day life and you focus them only on this one  
13 feature, and everyone is talking about the prior art to  
14 this feature and all the attempts at solving the  
15 feature.

16           And even though the alleged infringer's counsel  
17 will have a full opportunity to say, but it's marginal,  
18 but it's minor, you spend two weeks talking about  
19 something, and there's just no way to undue the fact  
20 that it's going to have an exaggerated impact on people.

21           So I think you need to have a flexibility such  
22 that it's not one size fits all, but you need to have  
23 real rules so that it's not whatever some of these great  
24 expert witnesses that are up here say: You know, the way  
25 I look at it, it's like antitrust. There needs to be



1    some filtering of that.

1           It is not that simple. That is why when you're  
2   trying to legislate something, you're getting into some  
3   very dangerous grounds. That's why I get employed on  
4   these things.

5           MR. ADKINSON: John. Or Jack. I'm sorry?

1 number of licenses if you can get them, that you could  
2 possibly rely on, so I don't think that usually is an  
3 effective factor at all, and generally speaking, I don't  
4 see it too much in too many cases.

5 MR. ADKINSON: Paul?

6 PROFESSOR JANICKE: Jack just said if you can  
7 get them, and in my other life as a litigating patent  
8 lawyer -- this is old-time stuff because I've been on  
9 the law faculty 16 years now, but in my other life,  
10 perhaps due to a lack of talent or imagination, I could  
11 never get the licenses that I wanted to collect.  
12 Everybody brought all kinds of protective orders and  
13 motions to quash the subpoenas, and it became a battle  
14 unto itself.

15 So getting that kind of -- I agree it would be  
16 great, but getting hold of it for me at least was a very  
17 difficult chore, and I was very unsuccessful at it.

18 MR. ADKINSON: Anne?

19 MS. MICHEL: Anne?

20 MS. LAYNE-FARRAR: I was actually going to talk  
21 about some other things.

22 DR. LEONARD: I was just going to say I actually  
23 do see it maybe more than you might, either the  
24 comparable license -- I mean, I was just involved in a  
25 case a couple months ago where the other side's expert

1 had a list of supposedly comparable licenses from a four  
2 digit SIC code or something and then took the average  
3 and said: Well, this is the right number.

4 My analogy for that is nine and a half is the  
5 average men's shoe size, so I think what I'll do is I'll  
6 open up a store, and I'm only going to sell size 9 and a  
7 half shoes, let's see how well I do. It's totally  
8 ludicrous.

9 I think actually all the damages experts sitting  
10 up here agree with that, but I think even more dangerous  
11 though are the rules of thumb because there you have  
12 this claim that that's what people actually do, which I  
13 actually think is not true, and there's this unfortunate  
14 published paper that maybe soon I will be addressing,  
15 but that the claims that, oh, this really looks well and  
16 that sort of thing.

17 So I think it is very dangerous, and I think  
18 *Daubert* should be used to get rid of it, and I think

1 brought. I think the judges and just trial management --  
2 this is just my anecdotal, this isn't like the good  
3 professor, a systematic empirical analysis -- but is that  
4 the judge's feel they'll let it go, they'll see what  
5 happens at trial.

6 So the first thing is, okay, I don't really have  
7 to make this decision now, let's see if it all turns out  
8 as bad at trial. An then you're at trial, it's reined  
9 in in it's worse excesses, but still flows in, and  
10 getting something out like industry averages is  
11 basically -- I mean, that's so far from anything you  
12 would be ever able to get out of -- you would be able to  
13 strike.

14 And then it's sort of, well, we'll see what the  
15 jury does, and if the jury is a runaway, then I have my  
16 ability for remittitur and all, kinds of post-trial  
17 tools and it's just this creep that happens.

18 Then you have the creep phenomenon, which is:  
19 Okay, the jury just spent two weeks of their lives  
20 working on this, who am I really to second guess what  
21 the value is? There was sort of a lot of information  
22 thrown up there, and the Federal Circuit can fix it if  
23 it's really abusive.

24 And you just get that sort of a creep. That's,  
25 A, and then B, you have a lot of justifiably nervous,

1 one might say paranoid, in-house counsel who don't want  
2 to have to live through the jury seeing \$60 billion up on  
3 the screen for one millisecond because of their  
4 reporting requirements and everything else, and they  
5 don't want to have to worry about a post-trial motion -  
6 no really don't settle it now because the judge is going  
7 to fix it all.

8 I mean, it's just -- that's not real, that's not  
9 real, so that doesn't -- that's the structural -- to  
10 answer, that's the structural things that I see. I  
11 don't know if Jack may have similar or different  
12 experience.

13 MR. SKENYON: Pretty much the same I think with  
14 that.

15 MR. LEVKO: We've done an empirical study on  
16 *Daubert* motions. We don't have it specifically for an  
17 IP cases, but we have it for financial experts, and we  
18 do this every year. We also have another report that we  
19 released on that, and it seems -- I'm trying to recall  
20 the numbers, but something less than 50 percent of these  
21 cases have *Daubert* motions.

22 I think it's something like the high 30s or 40  
23 percent or something like that, and then we have  
24 eliminations that are around one-third, 30 percent or 33  
25 percent. It's below 30 percent. The plaintiffs are

1 limited more often than defendants. They're up I think  
2 probably closer to 40 percent, and the reasons  
3 primarily -- there's three basic screens, one being the  
4 qualifications of the experts, the second being the  
5 reliability of information, the third being the  
6 relevance of the information.

7           And it's the reliability of the information thation.





1 talking about compensating a patent holder for the  
2 contributed value, then you don't have to worry about  
3 all the other components because you're just getting the  
4 value of that one component that's being contributed.

5 Yes, it can be difficult to get to that  
6 contributed value, but that gives you more impetus then  
7 to strive for that kind of framework. And also we should  
8 recognize that within an industry where you have  
9 patent holders, who are long-term market players that are  
10 in this industry, they have every bit as much interest  
11 in solving the royalty stacking problem as do the  
12 manufacturers. If the market collapses because of a  
13 stacking problem, those patent holders aren't getting  
14 paid anything.

15 So it's very much in their interest as well.  
16 It's only these sort of short-termers, maybe people  
17 leaving the market, the bad actors, if you will, who  
18 have more of a short run view that that becomes more of  
19 an issue.

20 The long term industry players, even if they're  
21 non-practicing entities and only have upstream R&D very  
22 much care about solving the royalty stacking problem.

23 Which brings me to the final point I would like  
24 to make, and that's on the non-practicing entity. I  
25 think it's dangerous to say all these are willing

1 licensees. We should only give them reasonable royalty.  
2 They don't face any risk. I think if you're talking  
3 about an R&D firm who's chosen to specialize upstream,  
4 they very much face risk.

5           They're putting a lot of dollars on the line in  
6 their R&D, and if they don't get compensated for it,  
7 that could remove a valuable player from a market who  
8 maybe has a comparative advantage in doing the R&D and  
9 the upstream stuff as opposed to implementing it  
10 downstream.

11           So I think it's dangerous to view them too  
12 dismissively. And also in the context of a dynamic  
13 market, if you restrict them entirely say with a  
14 category rule, no injunctions, they only get reasonable  
15 royalties, no damages, that kind of thing, you can  
16 hinder that player's ability to negotiate reasonable  
17 royalties in the future with other parties because they  
18 say: Aw, you're a non-practicing entity, I know that if  
19 I bring you to trial, you'll be treated differently and  
20 I'm going to be okay.

21           So I just wanted to follow up on those few  
22 points.

23           MR. ADKINSON: Thank you 12           So I just wanted to f

1 is another area in what is demonstrated in court is if  
2 you're not using the licenses and you need more of the  
3 analytic approach, we could go to considering the value  
4 of the component or the value of the patented item.

5 What I want to ask first is how the panel --  
6 what the panelists can say about how difficult it is to  
7 present in court the sorts of evidence that will enable  
8 a jury to get a handle on what is itself another  
9 difficult question, trying to understand perhaps an  
10 unusual technology, advanced technology, and how perhaps a  
11 component of that technology contributes.

12 So from your experience, how do you go about  
13 trying to present to a jury how -- what the value of the  
14 particular technology is, and is there a mechanism you  
15 think is especially useful?

16 MS. LAYNE-FARRAR: I would say -- briefly, I'm  
17 sorry. I would say yes, it is a useful mechanism in  
18 that one of the things you can do is try and put things  
19 in context. You don't want to go down the 150 patents  
20 that are in all the cards in the box. That's  
21 overwhelming and mind numbing and too difficult for  
22 anyone to comprehend, but you can talk about basic  
23 components: This product is divided into three areas,  
24 and the patent reads on area one, and if we focus on  
25 area one, it's a big or a little piece of that, so in a



1 way is another factor that's not reflected in the  
2 *Georgia-Pacific* factors, that goes towards I would think  
3 strengthening, the arguments, if not the economic  
4 analysis and valuation, for patents because that shows a  
5 track record of success and from a valuation standpoint,  
6 reduces some of the risk factors that I've previously  
7 discussed.

8           The second thing is in regards to how to  
9 allocate on the base or the value, the royalty on a  
10 particular feature or patent within a total product. I  
11 think we've been dwelling a lot -- and I'm going to take  
12 it from real-life experience -- on functionality, that  
13 is, what does this patent do, how does it improve over  
14 the prior art, how may it be used by the user and so  
15 forth?

16           I think what I have found useful, besides the  
17 functionality, is looking at the sales history of  
18 products before and after the patent's introduced,  
19 taking into account the potential degradation of sales  
20 without the innovation. Levels of investment, to what  
21 extent any rational business would want to invest in  
22 these additional features and wanting to have a certain,  
23 at least minimum, return on investment.

24           Oftentimes that additional investment on this  
25 feature on that patent or that whole functionality is a

1 way of looking at the incremental benefit to be derived  
2 because that's rationally how capital expenditures get  
3 approved. I was a controller in a business, and that's  
4 how we do things.

5 You look at profitability; that is, how does  
6 that change the profitability or contribute to  
7 profitability overall by adding this feature of this  
8 patent and so forth? How is it sold? How is it  
9 advertised? How is it promoted? Is it a feature among  
10 several features? And we can take a look at the  
11 materials and so forth and see if it's even mentioned.

12 Then finally, is it a platform for business  
13 growth? This is the option concept. Does it get you  
14 into a ticket to the next generation? And oftentimes a  
15 value has to be something more than simply a  
16 straightforward valuation but needs to take into account  
17 some option of use as that. So those are some other  
18 thoughts regarding how to develop a component.

19 MS. MICHEL: Greg?

20 DR. LEONARD: I was going to add to that. That  
21 was a great list of ways to go about doing it. Another  
22 way from an economist's point of view, we're pretty good  
23 at relating consumer demand for product to the  
24 particular attributes that the product has.

25 So what you can do, for instance, is say well,

1 if the infringer had to change the attributes of its  
2 products in order not to infringe, we can use one of  
3 these models of consumer demand to estimate what the  
4 demand would have been in the but-for world, but again  
5 if you have to offer an inferior product, your demand  
6 for the product will fall, you would sell less, and that  
7 will be part of the incremental value that the patented  
8 technology gives you as the infringer.

9 I also want to mention this briefly, but there  
10 also could be a price effect too, so if you're offering  
11 an inferior product, you might not only sell less but  
12 you might also have to lower your price, but these are  
13 the kinds of things again that economists are really  
14 good at doing. And there are other ways, in addition to  
15 the ones that Aron mentioned, of looking at and trying  
16 to place a value on the actual incremental effects on  
17 the infringer of having access to the patented  
18 technology.

19 MS. MICHEL: Paul?

20 PROFESSOR JANICKE: Suzanne, your question was  
21 very perceptive about claims and how in patent law terms  
22 almost all claims realistically are comprising-type  
23 claims. And if we proceeded in the way as you suggest,  
24 where the real thing devised, let's call it, is the  
25 circuit and that's claimed in claim one, and then claim





1           So the question is how to solve that, right,  
2 given the time of day we need to do that and especially  
3 with your question? I think it's a really twin  
4 approach. So there needs to be a substantive rule, and I  
5 think value over the prior art or value over the  
6 alternatives -- seems to be some coalescence around some  
7 form of that and there's fine tuning and flexibility  
8 necessary in that, but something along those lines -  
9 coupled with some procedural reform.

10           I think you need both, so that you actually get  
11 the decision. You force decision points which forces  
12 the development of a body of law that can say when  
13 you're in a pharmaceutical situation, you don't apply --  
14 it's okay to do it this way.

15           When you're in this software circumstance -- and  
16 obviously you don't do it necessarily by technology per  
17 se, but just normal case law development, in this  
18 situation you would never be permitted to do that. And  
19 so I think we've talked a little bit about gatekeeper,  
20t00 but something where you have a pharmaceutical judge in person's appay

1 category, but Chief Judge Michel put together this  
2 committee with Judge Ward from Texas and Judge White  
3 from the Northern District of California, Judge Saris  
4 from Boston and Judge McKelvey from Delaware, and we've  
5 put together these modern rules, and they're not a cure-  
6 all for anything, but there are improvements attempted,  
7 especially in the royalty factors and other areas.

8           And those are available in the Federal Circuit  
9 bar association web site, and they're in the comment  
10 period right now. The comment period closes on February  
11 20. With such a great audience that we have here, I use  
12 this to solicit further input into that as an attempt to  
13 modernize the damages analysis.

14           MS. MICHEL: Thank you. Tom?

15           PROFESSOR COTTER: Yeah. Just to echo I think  
16 what Aron and Greg were saying, I think the real focus  
17 ought to be on the economic realities and not the  
18 vagaries of claim drafting.

19           So if we're trying to either estimate lost  
20 profits or to reconstruct this hypothetical bargain  
21 relating to the reasonable royalty, we ought to be  
22 focusing on what would have motivated people in the real  
23 world to reach a certain figure or what the actual  
24 consumer demand for the product with and without the  
25 patented feature might have been. None of this really

1 hinges or bears any necessary correlation to the way the  
2 claims are drafted because that's so manipulable -- how  
3 narrowly or broadly the claims are drafted.

4 I do think, however, the Patent Reform Act that  
5 didn't get through, but that portion of it that focused  
6 on comparing the patented -- the contribution over the  
7 prior art and estimating royalties based on that, I'm  
8 not sure that's really the way to go.

9 I think it's Schlicher again I think that made  
10 the point -- maybe it's really a timing issue here  
11 because that really focuses on what the potential value  
12 of the invention was at the time the application was  
13 filed, and I think really the timing issue we've mostly  
14 focused on today is what is the economic value of the  
15 invention at the time the defendant choose to go down a  
16 particular technological path.

17 That could be fairly wide gap, so I'm not sure  
18 that we ought to be focusing on the contribution over  
19 the prior art in estimating damages or royalties. I  
20 just don't think that's the right fit.

21 MS. MICHEL: Gail?

22 MS. LEVINE: I agree with a lot of that, and in  
23 fact I will never again speak after Professor Cotter  
24 because he always says everything I'm thinking. Maybe  
25 if I can amplify one or two points.

1           The economic test, the test about the  
2 technological value, it's value over alternatives, takes  
3 a lot of pressure off the claim game, right. It doesn't  
4 reward clever claiming as much as perhaps other tests  
5 would, and that's an attractive feature of it because  
6 it returns us to the economics, what a business person  
7 actually thinks and does.

8           Bill, you asked earlier: How can a test like  
9 the economic test, the technological value of the patent  
10 test, the value over alternatives test can be actually  
11 implemented in the courtroom? And I think that's a very  
12 good question. All of these things are in varying  
13 degrees difficult to prove, but what's the alternative?

14           The alternative is this grab bag of factors,  
15 this very unfocused determination. That's untenable,  
16 and we don't have to wait for a test that can be  
17 executed with mathematical precision, right, just  
18 something that returns courts -- and returns parties to  
19 a test that is more economically sensible is what we're  
20 aiming for.

21           And frankly the test for looking for the next  
22 best alternative, figuring out the difference between  
23 the non-infringing substitute and the patented  
24 technology isn't so dissimilar to what courts already do  
25 in the lost profits.



1 alternatives that were very significant. Maybe they  
2 were on the verge -- this is just made up of course, but  
3 on the verge of an alternative license that got  
4 precluded because of that. They lost tens of millions,  
5 okay.

6 If you have a perspective that restricts  
7 your ability to broadly look at the circumstance, that's  
8 my only concern is I don't want us to lose this ability  
9 to be flexible, to look at multiple points and make  
10 judgments.

11 MR. ADKINSON: Thanks. Greg?

12 DR. LEONARD: Yeah, I was going to raise  
13 something similar because there can be, in a situation  
14 where the patentee has not, for whatever reason, made a  
15 lost profits award but is concerned at the time of the  
16 hypothetical negotiation about competition from the  
17 infringer. It can very well be the case that sort of  
18 minimum royalty that a patentee would have been willing  
19 to accept exceeds the maximum royalty that the infringer  
20 would have been willing to pay. That does come up  
21 occasionally in cases, and it is a bit vexing to try to  
22 decide what to do.

23 Although my own personal answer is that the  
24 reasonable royalty should be set to the licensor's  
25 minimum willingness to accept in that situation for the

1 compensation purposes.

2 MR. ADKINSON: Jack?

3 MR. SKENYON: Just a quick comment on the idea  
4 of getting away from the claim language itself. Dealing  
5 with a claim that has computer, all its parts and the real  
6 key pieces of that little circuit that's in the claim.  
7 In terms of the litigation, you would have to have a  
8 *Markman* hearing that would deal with a number of the  
9 limitations in the claim. You would have to go to trial  
10 and prove infringement, that all the limitations were  
11 met by the accused product.

12 The invalidity case would have to be based, if  
13 it's an anticipation case or obviousness case based on  
14 all of the limitations in the claim, and then when  
15 that's all decided and it's all decided in favor of the  
16 patentee, then you get to the damages issue for the  
17 infringement, and we're deciding it based on something  
18 else. We're deciding on some little piece of thing or  
19 why it was issued from the patent office to begin with.

20 So I think there's some philosophical problems  
21 with that. I think there's practical problems with  
22 making that element of proof here of why it was issued  
23 from the patent office and what it is, so I see some  
24 difficulty with that approach.

25 MS. MICHEL: Ed?

1           MR. REINES: I just want to make a minor point  
2 on Greg's situation, which is when you have, for very  
3 good factual reasons, no overlap in what the  
4 hypothetical licensor or licensee would agree to because  
5 of external things to their particular reality. One  
6 argument I have seen from accused infringers is we make  
7 almost no profit, so therefore we wouldn't possibly give  
8 away more than our profit.

9           And to me that's sort of one of those spurious  
10 arguments because obviously if someone is losing money  
11 but they're taking market or they're using your  
12 intellectual property it doesn't create a zero.

13           So I think one of the challenges is: How do you  
14 deal with the situation where the ends don't meet? And  
15 that shows how difficult the process can be.

16           MS. MICHEL: Aron?

17           MR. LEVKO: I have a case. I testified and went  
18 through the CAFC, the Golight case -

19           MS. MICHEL: Yes.

20           MR. LEVKO: -- in which I was the expert, and in  
21 fact the patentee got more in royalty than the selling  
22 price of the defendant and that's because of the  
23 circumstances. That's the difficult thing, I can go  
24 through that, of trying to prescribe a certain  
25 procedure, law, what have you, because as Bruce pointed





1 please respond.

2 MR. REINES: This is very short to that, which  
3 is another frontier of this whole area is open source  
4 software now, but Lord knows what else will be open  
5 sourced where there's no -- there's no base. There's no  
6 revenue, and I think my sense is we're seeing more and  
7 more where people are open sourcing other people's  
8 things and saying: Aren't we great, we give this away to  
9 everybody by our services and support and whatever else?  
10 So that presents a whole series of issues around base,  
11 so I agree on the flexibility.

12 MS. MICHEL: Anne?

13 MS. LAYNE-FARRAR: Also very briefly, in the  
14 open source you may open source the component that has  
15 the patent in it and get your money off of the  
16 complimentary goods, like a service and say, well, the  
17 patent doesn't read on my service. Well, you priced it  
18 that way precisely to get around the patent licensing.

19 And another scenario would be like an  
20 intermediate good where the intermediate manufacturer  
21 indemnifies follow-ons, so in that case you may want to  
22 charge more than the price of that wholesale good  
23 because that person is passing on rights to others,  
24 perhaps additional rights than he or she is using.

25 MS. MICHEL: Any final comments from our

1 wonderful panelists?

2 Well, thank you very much. This has been an  
3 excellent panel. We will break for lunch now and return  
4 at 1:45. We have Judge Sue Robinson from the District  
5 Court of Delaware, who is well known as a patent jurist,  
6 will be here for a keynote speech, and then we will have  
7 an industry round panel, and we will see you then, I  
8 hope.

9 (Applause.)

10 (Whereupon, at 12:23 p.m., a lunch recess was  
11 taken.)

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## 1 AFTERNOON SESSION

2 (1:49 p.m.)

3 MS. MEYERS: Welcome back. Thank you for coming  
4 back this afternoon. We'll go ahead and get started  
5 now. We're doing the afternoon panel on damages law as  
6 part of the FTC's series on the evolving IP  
7 marketplace where we will have our industry roundtable,  
8 but before that, we will have Judge Robinson talk.

9 So it is now my distinct pleasure to introduce  
10 The Honorable Sue L. Robinson, District Court Judge of  
11 the United States District Court for the District of  
12 Delaware.

13 Judge Robinson has been a member of that court  
14 for 20 years now. She served as Chief Judge of the  
15 court from 2000 to 2007, and she also served on the  
16 Judicial Conference of the United States from 2002 to  
17 2003.

18 The District of Delaware is noted for hearing a  
19 large number of patent cases and other complex  
20 commercial cases. Judge Robinson has presided over many  
21 patent cases and has been at the forefront of patent  
22 jurisprudence. She has developed thoughtful and  
23 engaging opinions and demanded high standards from those  
24 practicing before her.

25 If you will indulge a shameless plug for

1 tomorrow's topics, among her opinions include several  
2 post *eBay* opinions that demonstrate this level of both  
3 theoretical and practical vigor and have taken great

1 a knowledgeable audience today.

2 When I was first asked to participate in this  
3 proceeding, I wasn't sure what I could contribute to a  
4 discussion on the standards for assessing patent damages  
5 and their implementations by courts, although I've been  
6 on the bench actually since 1991, I was a magistrate  
7 judge before that, and during my tenure, I have  
8 marshaled hundreds of patent cases and tried 65 at last  
9 count.

10 Nevertheless, my experience with damages is  
11 limited, and let me explain why. Starting in the mid  
12 1990s, the number of patent filings in the District of  
13 Delaware began to grow exponentially. At about the same  
14 time, judges had been directed by Congress, through the  
15 guise of the Civil Justice Reform Act, to set firm trial  
16 dates at the outset of each civil case.

17 As a result, it became apparent that the  
18 traditional ways of scheduling and trying cases would  
19 not accommodate our docket of no fewer than 20 multiple  
20 week patent trials a year.

21 In order to maintain a firm trial date for all  
22 of our cases, patent as well as our other civil and  
23 criminal cases, we could not allow patent trials to last  
24 indefinitely. We had to impose limits on lawyers so  
25 that trials would start and end predictably. My

1     colleague, Judge Farnan, began the experiment of timed  
2     trials in 1991, and we have never looked back.

3             In this regard, however, it stood to reason that





1 were proximately caused by defendant's negligent  
2 conduct.

3 Similarly, a plaintiff pursuing antitrust claims  
4 must prove injury in fact, that the injury was  
5 proximately caused by the defendant's violation of the  
6 antitrust laws, that the defendant's illegal conduct was  
7 a material cause of plaintiff's injury, and that  
8 plaintiff's injury was an injury of the kind that the  
9 antitrust laws were intended to prevent.

10 Because the fact of injury is not an essential  
11 element of the cause of action of patent infringement,  
12 but is presumed once infringement is proven, a jury in a  
13 patent case can determine all issues related to  
14 liability, infringement and validity without ever  
15 hearing a word about injury or the resulting damages.

.00 rg 16 8 plaintiff's injury was a substantial factor in causing the injury but

1     which are just as likely to obfuscate as clarify the  
2     issues to be tried. The temptation to inappropriately  
3     use evidence on damages to sway a jury's view on  
4     liability is certainly not unheard of, and I think it  
5     was referred to today in this morning's panel.

6             Indeed, like the claim construction exercise,  
7     and I have the feeling some of you have heard me say  
8     this before, a patent trial involves science, distorted  
9     by the limitations of language, further distorted by the  
10    trial tactics of aggressive members of the patent bar  
11    fighting over their client's market share. Bottom line,  
12    whenever you mix science with business and legal issues,  
13    all seen through the prism of litigation, the end  
14    product is bound to be complex.

15            Then think about the hypothetical negotiation  
16    and whether that artificial, legal construct really  
17    resonates to a typical juror, who has no information  
18    about the m.000s m o theimarket sith n tbc0.00er their client's m

1           If liability can be determined without the added  
2 complexities of damages within the context of a timed  
3 trial, it follows that damages should be bifurcated and  
4 the judgment on liability entered for purposes of appeal  
5 pursuant to Federal Rule 25) Federal Rule of Civil Procedure and 3e b

1 order to discuss settlement intelligently. Moreover, if  
2 the patentee is seeking a preliminary injunction,  
3 damages discovery is required at the outset.

4           Regardless of when damages discovery proceeds,  
5 it is beyond dispute that discovery in a patent case  
6 imposes a tremendous burden on the parties. Document  
7 production, especially electronic discovery, and  
8 depositions of employees can cost businesses millions of  
9 dollars in terms of lost hours of productivity and  
10 professional fees.

11           As a trial judge, I am cognizant of these costs  
12 and at least try to take into consideration when I make  
13 decisions that impact the litigation -- and at least try  
14 to take these costs into consideration when I make  
15 decisions that impact the litigation and trial  
16 processes.

17           For example, I have imposed limits on when  
18 document production can proceed and on when motions for  
19 summary judgment can be filed so that clients stop  
20 pursuing unreasonable expectations and lawyers stop  
21 turning hourly fees.

22           The tension between cost and reasonable  
23 litigation goals is reflected best in what I call the  
24 *Daubert* epidemic relating to the Supreme Court's opinion  
25 of that same name issued in 1993. I have to say I had

1 some prepared remarks, but after the remarks this  
2 morning, at lunch, I wrote down some more on my table  
3 cloth, so I might not be as polished here.

4 In my view, *Daubert* was supposed to protect the  
5 litigation process against bad science, not to determine  
6 which expert's analysis fits the economic realities of  
7 any particular case best. I've had cases where the  
8 parties have exchanged *Daubert* motions on every single  
9 expert witness, witnesses who have impeccable  
10 credentials, and whose analysis reflect fairly  
11 unremarkable principles.

12 Nevertheless, because the experts disagree  
13 substantively, motions are filed to have the judge  
14 preclude the experts from testifying at all, as opposed  
15 to testing the merits of the expert's opinions through  
16 the rigors of cross examination.

17 Now, this is especially true with damages  
18 experts, generally economists who build their expert  
19 opinions on a series of assumptions based on the  
20 evidence of record. Arguably if one assumption is  
21 incorrect, their theory falls apart like the veritable  
22 house of cards.

23 In this regard, however, and my apologies to any  
24 economists who are still here, but my view is that  
25 economic theory is basically all relative, that there

1 are very few absolutes that can be applied, and the  
2 economic landscape in my view looks very different from  
3 the perspective of a patentee versus the perspective of  
4 the infringer.

5 To have a judge shape that landscape based on  
6 lawyer arguments without hearing any of the evidence  
7 from the people who have the evidence to me undermines  
8 the right to a jury trial, and I truly believe that --  
9 well, I also find it interesting that the lawyers expect  
10 the Court to make these determinations. They don't say  
11 anything about their clients who actually know the  
12 economic realities putting any self restraint on the  
13 experts that they've hired.

14 So in my view, with due respect to the  
15 litigators who spoke about how -- and I know I've  
16 heard -- it's never happened in my court, I've heard

1 complex jury trial, it follows that damages should never  
2 become the tail that wags the dog in trial. Again, let  
3 me explain. Although the owner of a valid patent has  
4 substantive legal rights, it generally takes a business  
5 dispute to generate patent litigation.

6 Now, I respect the fact that patent cases are  
7 really business cases and that litigation is but one  
8 weapon in a company's arsenal of competitive armaments.  
9 Nevertheless, when business decisions are driving a  
10 party's litigation strategy, a case can spin out of  
11 control for the simple reason that the court is rarely  
12 informed of the business parameters in which its  
13 operating.

14 Both aspects of a patent dispute, the legal and  
15 the business, need to be resolved. In reality, however,  
16 the court is better equipped to resolve the former. It  
17 follows that the court should use its limited resources  
18 to do just that. After all, businesses generally have  
19 the means to resolve their disputes. However, they need  
20 the motivation a court decision affords to focus their  
21 means on an amicable solution.

22 Of course, having judicial officers available  
23 for mediation, both before and after the trial on  
24 liability, leads to the best results. In the settlement  
25 arena, unlike the courtroom, the issue of damages is and

1 should be the engine that drives the exercise. Unless a  
2 patent owner is seeking only injunctive relief, a good  
3 settlement officer can generally fashion creative ways  
4 to honor the patent owner's substantive rights while  
5 accommodating the parties' business needs, depending on  
6 the dynamics of the market and of their business  
7 relationship.

8           A jury can't do that, and indeed neither can the  
9 trial judge who does not have access in the normal  
10 course to the type of business information made  
11 available to a settlement officer. And that's how it  
12 should be. If parties to a business dispute cannot  
13 resolve their business problems without resorting to  
14 litigation, let the courts do what they do best, finally  
15 determine substantive legal rights.



1 the focus of most of these opinions.

2 Before I close, let me say a few words about  
3 injunctions. Since the Supreme Court's 2006 decision in  
4 *eBay*, it is much more difficult in my view to justify  
5 granting an injunction at all, let alone prior to the  
6 Federal Circuit's final say on liability.

7 Starting with the premise that injunctive relief  
8 is not meant to be penal in nature, I have come to  
9 conclude that injunctions are really about market share  
10 and are best suited to protect those patentees in two-  
11 party markets, most often emerging markets where they  
12 compete head-to-head with the infringer.

13 I find the imposition of injunctive relief more  
14 problematic when a patentee does not compete in the  
15 market at all or when the infringer is one among many  
16 competitors in a market, the point being that if the  
17 patentee's market share will not be substantially  
18 affected by enjoining the infringer, then surely the  
19 patentee is not suffering irreparable harm by allowing  
20 the infringer to continue its business pursuits. Under  
21 those circumstances, money damages may well constitute  
22 an adequate and appropriate form of compensation for  
23 infringement.

24 My final thoughts for today: I recognize that I  
25 have talked more about process than about substance. I

1 suggest that there is good reason for my doing so. As a  
2 trial judge, I write on water. My legal analysis is not  
3 correct unless and until the Federal Circuit says it is,  
4 but the Federal Circuit's decision is only as good as  
5 the record upon which it is based, and that is my  
6 primary job as a trial judge, to make sure that the  
7 litigation record reflects a fair, efficient and  
8 predictable process so as to engender confidence in the  
9 outcome by the business community.

10 This is especially challenging in times like the  
11 present when market forces are driving business disputes  
12 to litigation, but the third branch is receiving neither  
13 the resources it needs nor the respect it deserves for  
14 its role in maintaining a healthy, competitive business  
15 environment.

16 I suggest that the separation of issues,  
17 especially of damages, is an effective way to use the  
18 Court's expertise without undue burden on its limited  
19 resources.

20 I thank you for your time and attention.

21 (Applause.)

22 MS. MICHEL: Thank you, Judge Robinson, for

1                   (Pause in the proceedings.)  
2    PANEL 2:  INDUSTRY ROUNDTABLE DISCUSSION  
3    MODERATORS:  
4    BILL ADKINSON, FTC  
5    SUZANNE MICHEL, FTC  
6    PANELISTS:



1 Group.

2 Gary Loeb is Genentech's vice president for  
3 intellectual property.

4 Bryan Lord is vice president, finance and  
5 licensing and general counsel, at Amberwave.

6 Taraneh Maghame - is that close?

7 MS. MAGHAME: Close enough, Taraneh Maghame.

8 MR. ADKINSON: Thank you, sorry not that close,  
9 but Taraneh serves as vice president, patent policy and  
10 government relations counsel at Tessera.

11 Kevin Rhodes is chief intellectual property  
12 counsel at 3M Innovative Properties.

13 Dave Simon works as Intel's chief patent  
14 counsel.

15 Marian Underweiser works at IBM where she is  
16 intellectual property law counsel.

17 Thanks very much. We look forward to the panel.

18 MS. MICHEL: All right. Let's dig in. I know  
19 this group has a lot to say on this topic. They were  
20 invited because they've all been very involved in the  
21 issue over the last couple of years.

22 Let's start with the big picture. Why is this  
23 issue of patent damages important to your company, and  
24 you can turn up your table tent, and I'll call on you,  
25 but this might be something that most people would like

1 to comment on, and I'll just remind panelists to speak  
2 into the mike, and we'll pick it up on our transcript.  
3 Thank you.

4 Would anyone like to go first? Marian, I'm  
5 looking over there, sorry.

6 MS. UNDERWEISER: Okay. Well, thank you, first  
7 of all, for having the panel and having me here.

8 MS. MICHEL: And as part of --

9 MS. UNDERWEISER: I appreciate it.

10 MS. MICHEL: If it works as part of this issue,  
11 you can address why over-compensation and under-  
12 compensation might be problems.

13 MS. UNDERWEISER: Sure. Well, IBM's perspective  
14 on this is a balanced one. We look at reasonable  
15 royalty damages both from the perspective of  
16 patent holder, who has a significant IP licensing  
17 business. We make over a billion dollars a year  
18 licensing our IP. We also make a hundred billion  
19 dollars a year selling products and services, and so  
20 we're subject to a lot of adverse assertions of patents.

21 So for us, it's really more of a question about  
22 the whole IP market, the licensing market. We  
23 don't want to have to litigate. We would like to be  
24 able to have an efficiently running licensing market,  
25 and what does that mean?

1           Well, the court-awarded damages are effectively  
2 providing a benchmark for licensing and settlement  
3 negotiations, and collectively they're making up this  
4 marketplace. And for the marketplace to work, there has  
5 to be efficiency there. There can't be friction. There  
6 can't be a whole lot of transaction costs, or what you  
7 end up having is a problem getting -- your products are  
8 going to cost more than they need to cost.

9           Collaborations may not occur, and you won't have  
10 the innovations making their way into products, and in  
11 the case where parties decide to go forward but they  
12 can't agree, then they end up litigating and litigating  
13 is very costly and diverts funds away from where they can  
14 productively be used.

15           So what do we see? We see a problem in our  
16 industry where there is this sustained high level of  
17 patent litigation. There is the opportunity for  
18 inflated awards, and this to us means that there is too  
19 much diversion away from where things should be  
20 operating efficiently in the licensing market into  
21 litigation.

22           And at the same time, the parallel conclusion  
23 you can draw from that is that the standard and  
24 reasonable royalty damages is not providing the kind of  
25 certainty that parties need to be able to negotiate

1 those deals upfront.

2           So what we think would be a good way to approach  
3 this is to focus the damages analysis in a way that is  
4 somewhat more objective, right? And that would be --  
5 and a number of the panelists touched on this this  
6 morning, but that would be to focus on the economic  
7 value of the invention: What did the inventor really  
8 contribute? What's that economic value, and that's fair  
9 to the patentee? It compensates the patentee for what  
10 was contributed. It doesn't over- entee les tat





1 refuses generally to work for a contingency fee. For  
2 some strange reason we haven't been able to get anybody  
3 to do that. Similarly, when we have to produce  
4 documents, we're talking about literally, electronic  
5 document production now for us is millions of dollars in  
6 every single case, frequently the same documents, but  
7 every single case, huge costs. And many of the entities  
8 shows up, Here's my document. It's the file wrapper.  
9 It's the patent, and that's about it.

10 They're of course on contingency fee, and there  
11 has been a whole phenomenon capitalizing on that as, A,  
12 shown by, if you look at the statistics we saw  
13 this morning and you sort them by industry, it's clear  
14 that, for want of a better term, I'll use the term tech  
15 industry because that's what people tend to use, the  
16 damages are significantly higher, between four and six  
17 times higher.

18 And in addition to which what we're seeing is  
19 that's where the non-practicing entity litigation tends  
20 to be. Where they're very much viewing it as this is a  
21 way to -- if I get, if I'm lucky I strike it rich, and  
22 that creates a whole bunch of incentives, disincentives  
23 in the system, which just aren't frankly benefitting  
24 innovation.

25 It's even getting to the point that getting 30

1 or 40 million dollars out of one company can be rather  
2 hard in litigation, but what we now have is the number  
3 of defendants has gone up dramatically in the last few  
4 years where you now have 5, 10, 15, even 30 or 40  
5 defendants in a patent case, and in some districts  
6 you get -- I understand why the judges do this, you are  
7 getting 40 hours total trial time in a week or two week  
8 period.

9           Trying to try a case with that many defendants  
10 is of course unmanageable, and the thinking is not that  
11 they're going to take that many defendants to trial, but  
12 the thinking is they're going to get a couple million  
13 dollars from each of the defendants until they get down  
14 to a manageable number, and then those last two or three  
15 or four unlucky souls are going to be the ones that go  
16 to trial.

17           And it becomes a very economical situation to do  
18 this from a plaintiff's standpoint, so as a result, what  
19 we see patents that are supposed to be -- being  
20 used for innovation are actually being used for lots of  
21 other purposes, and I think it's because at least in our  
22 industry, the system tends to over compensate the  
23 patentee.

24           MS. MICHEL: Thank you. Kevin?

1 for inviting me to participate this afternoon. A little  
2 bit different perspective. First of all, 3M is balanced  
3 on this issue as well. On the patent owner's side, we  
4 currently own about 6,000 U.S. patents used to protect  
5 our investment in research and development, which  
6 totaled nearly 1.4 billion last year so we have a long-  
7 standing commitment to the patent system.

8 Now, why do we disclose our inventions in order  
9 to get a patent or I should say try to get a patent? We  
10 do that because we think they will provide meaningful  
11 protection for the investment in R&D that leads to those  
12 inventions, for the following investments and  
13 commercialization for those inventions that we  
14 commercialize, and to protect the commercial products  
15 that we put on the market from infringement.

16 So in my view, the damages award is part and  
17 parcel of that protection. Typically when we go into a  
18 patent infringement litigation, and we have a steady diet  
19 of plaintiff-side cases, in fact more cases are on the  
20 patent owner's side than defense cases, we don't get  
21 preliminary injunctions.

22 Preliminary injunctions are rare, and so you  
23 have a situation where you have two or three years of  
24 infringement before hopefully you can get that permanent  
25 injunction, and in the post-eBay world, I think on

1 Professor Janicke's web site, 69 percent now of cases in  
2 which permanent injunction is asked for, it's entered.

3 So hopefully we're going to get that permanent  
4 injunction, but even if that doesn't come for two or  
5 three years into the litigation, we want to have some  
6 type of meaningful compensation, and let's not lose  
7 sight of the fact that damages is compensatory in  
8 nature, some type of compensation for that infringement,  
9 whether it be reasonable royalty or lost profits or most  
10 commonly a combination of the two.

11 So I do believe that there's a compensatory  
12 aspect. I also believe, from firsthand experience, that  
13 damages too low eliminate the deterrent function of  
14 meaningful remedies for patent infringement litigation.

15 We have seen -- over 60 percent of our sales are  
16 outside of the U.S. We've litigated patents all over  
17 Europe and Asia, and we see what happens in legal  
18 systems where there aren't effective remedies for  
19 infringement. Essentially infringement becomes a cost  
20 of doing business. It's cheaper to free ride on someone  
21 else's R&D and pay the slap on the wrist penalty than it  
22 is to do your own R&D.

23 So there is a deterrent feature to damages that  
24 I would not want to see undermined if we start taking  
25 away remedies one by one, permanent injunctions and then

1 lowering damages.

2 On the other hand, we market over 50,000

3 products and services. Despite our efforts to clear

1 said is apt, and that is that then we just have experts  
2 on either side arguing over what the proper economic  
3 value is. I think it's Pyrrhic to think that by changing  
4 from a flexible test to a less factored test, if you  
5 will, that we get added certainty.

6 I was also struck by some of the statistics this  
7 morning. We heard this morning the median damages  
8 awards have remained remarkably consistent over the past  
9 15 years and declined in 2008 to what looked to me like,  
10 from just looking at the graph, was maybe the lowest  
11 level since 1998.

12 So it strikes me, I wonder when we're talking  
13 about changing damages laws, if we're talking about a  
14 solution in search of a problem here.

15 MS. MICHEL: Okay.

16 MR. RHODES: But the awards are very erratic.  
17 Well, erratic is another way of saying there's some big  
18 numbers on those slides, right, but we don't know  
19 anything about those cases. What were the inventions?  
20 What were the accused products? What were the sales of  
21 the accused products? You look at any body of law and  
22 you will see a disparity in awards of damages, so I  
23 don't think patent law is unique.

24 I don't think any alternative system is going to  
25 give us added certainty, and I don't think the case has

1     been made by data that damages awards are out of control  
2     or that juries aren't looking at the proper economic  
3     factors in making damages awards.

4             MS. MICHEL: Thank you.

5             MR. RHODES: So in my view, there is no need to  
6     abandon the body of law that's been developed over  
7     decades in favor of new rules. Especially in this time,  
8     those new rules have unsupported justification and just  
9     unknown economic ramifications, and I think that is  
10    not -- this is not the time to be making those kind of fffffff



1 the packaging in order to be able to put them in our  
2 very small kind of handhelds and other consumer  
3 electronics.

4 So our customers were really one of the main  
5 reasons why we turned our business into a licensing  
6 model. They needed additional sources for this  
7 technology. They needed us to license it to others who  
8 could more efficiently manufacture and who had more  
9 capacity to manufacture.

10 So basically there was a shift in our business.  
11 We took our home-grown technology. We sold off our  
12 manufacturing plant and we turned our business into a  
13 licensing business, and since that time, we have signed  
14 up over 50 companies, major companies, as licensees.

15 Now, that accounts for a certain percentage of  
16 the market. Now our technology is widely adopted, and  
17 there are still companies out there that are not willing  
18 to pay our standard royalties. And our royalties are not  
19 -- it's not a situation where we have to establish a  
20 value, we don't establish economic value. We don't  
21 establish kind of what is the incentive feature here.

22 There's over 50 licensees already. We've  
23 been -- we've built over a billion dollar company, a 1.2  
24 billion dollar company using this licensing model. So  
25 we are forced into litigation. If we cannot negotiate

1 licenses with people that are holding out on us, if we  
2 can't take our repeatedly-tested patents that have been  
3 tested in the courts, tested in the ITC and say: You are  
4 infringing because you use the same technology all our  
5 licensees do and you need to pay us -- there isn't another  
6 choice other than to litigate.

7           So we keep hearing about these outrageous costs  
8 of litigation for companies -- what we call the megatech  
9 companies who are pushing for this kind of reform, 50  
10 million a year, 60 million a year. Well, I think I can  
11 tell you that last year, we spent more than that on our  
12 litigation, so our little company has to spend more than  
13 that while we're still in litigation.

14           So the costs are not one-way, but one thing that  
15 strikes me is that in all of this discussion, first of  
16 all, we don't talk about what that amount of money for  
17 the megatechs means in terms of their revenues and their  
18 profits. I can tell you, like I said, we're a 2 billion  
19 dollar company, 1 billion dollar company. Spending 60,  
20 70, 80 million dollars in litigation in one year is a  
21 heck of a lot higher percentage than the \$50 million that  
22 a company spends defending itself on the number of  
23 patent litigations they may have in any given year.

24           But the other thing that I don't hear about is,  
25 for example, IBM, big licensing company, a lot of cross

1 licenses. Do we ever put a value on those cross  
2 licenses because if you have two what people like to  
3 call practicing entities going at it, and they end up  
4 settling, what do they do? They take cross licenses.  
5 What is the value of those cross licenses? Has anyone

1 really know what those other problems are, but when  
2 we're talking about deterrent effects, we're talking  
3 about willfulness.

4           When someone has been found to infringe and the  
5 patent's been found valid, that's when we're talking  
6 about enhanced damages so we need to keep in mind at  
7 what stage we're talking about this. It is necessary to  
8 deter willful infringement, and if that's what's being  
9 done -- and we even saw from the numbers this morning,  
10 that that's not really occurring on a regular basis.

11           I think the average was that there was maybe  
12 12 percent of cases where enhanced damages were given,  
13 and that was one and a half times, perhaps even though  
14 they're allowed to be trebled.

15           So again I keep coming back to this question of:  
16 Where do we see the over-compensation and where is the  
17 data that shows that we need to do something about this  
18 quote, unquote, problem? From our perspective, we need  
19 to have the ability to obtain appropriate royalties for  
20 our technology that we've spent hundreds of millions of  
21 dollars developing.

22           The only way we can do that is through  
23 litigation, if we cannot come to an agreement with folks  
24 that are using that technology, and having the  
25 flexibility to determine the amount of damages is

1 absolutely necessary.

2 The other thing that struck me this morning --

3 MS. MICHEL: Actually, why don't we move on  
4 because we'll come back, and we'll have an interactive  
5 discussion on a number of topics.

6 Bryan, could you tell us why for your company  
7 Amberwave, the issue of damages is important?

8 MR. LORD: Sure. First of all, a little bit of  
9 background on Amberwave. It's probably the case that  
10 most people at this table have a legal department that is  
11 larger than the size of my entire company. We're a 25-  
12 person research and development company in Salem, New  
13 Hampshire. We were spun out of MIT back in 1999.

14 We've raised 91 million dollars in venture  
15 capital to basically bring to market a suite of  
16 technologies that are in the domain of  
17 hetero-integration of advanced materials. That's a  
18 mouthful, but essentially what that means is you take  
19 different elements that are on the periodic table, all  
20 of which have different semiconductive properties, and  
21 you put them together in special ways.

22 Those special ways can help semiconductor chips  
23 run faster, use less power. They can make solar cells  
24 more efficient. They can make LADs that some day will  
25 replace light bulbs above us more efficient and

1 brighter and more pleasing to the eye.

2           So what we did in contrast to Tessera is raise  
3 this venture capital dollars. It really was the classic  
4 university professor and a frat brother turned venture  
5 capitalist who got together over coffee and decided to  
6 found the company based on this material science  
7 technology.

8           And unlike Tessera, we actually decided from the  
9 outset that the flexibility of the licensing business  
10 model made a lot of sense for the company. Being a  
11 venture-backed company, it made no sense to raise the  
12 500 million dollars or the 5 billion dollars to actually  
13 go into production and manufacturing.

14           And instead, as our world is becoming  
15 increasingly disaggregated, not aggregated, we're  
16 actually disaggregating in our economy, it made sense  
17 for us to stick to our knitting and focus on being a  
18 research and development shop.

19           So for us, damages really is the fallback that  
20 the venture capitalists asked about when they decided  
21 whether to make an investment in Amberwave, so we get  
22 that your technology has got some promise. We get that  
23 you've got some smart Ph.D.s. We get that we've got  
24 money.

25           What happens if you bring a product to market

1 and your sales guys do their job and somebody on the  
2 other side of the table says, in the licensing business  
3 model, thank you for teaching us about your technology,  
4 we're going to go ahead to use it and don't call us,  
5 we'll call you? That's what damages really relates to.  
6 It's really what is the -- as some people in the field  
7 call it a BATNA, what's the best alternative to a  
8 negotiated agreement.

9           And if you think about the Amberwave story, it  
10 really matters to everything, from that entrepreneur,  
11 that scientist at MIT deciding whether this was a risky  
12 enough or safe enough pursuit for him to go forward,  
13 whether those venture capitalists really had enough  
14 confidence in the intellectual property that was going  
15 to be generated to put that capital to work, and frankly  
16 whether those employees, me being one of which, said is  
17 this the place where I'm going to dedicate a hundred  
18 percent of my human venture capital to this enterprise?

19           So patents really matter. Patents really  
20 protect that joint investment, and I think we ought to

1 just the IBMs and Amberwaves as well, I think it's  
2 worthwhile for us to take note of where we stand as a  
3 society. This debate really started back a couple  
4 Congresses ago at least, 2005, and it's been portrayed  
5 as tech versus pharma, as tech versus trolls, as good  
6 guys versus bad guys and whatnot.

7 And there is a very, very serious economic  
8 debate going on that's trying to pour billions, if not  
9 trillions of dollars into the economy, to get people  
10 back to work, to get people to take risks and to bring  
11 new technologies to the marketplace, and it seems crazy  
12 to me that we are also having a conversation about how  
13 to reduce the negotiated value of intellectual property  
14 in today's day and age.

15 So I would encourage all of us also to think  
16 about the counter-incentives, the disincentives that I  
17 think we might be perpetuating by really continuing the  
18 debate that happened and started a long time ago and  
19 quite frankly ought to take place in a different context  
20 today.

21 MS. MICHEL: Thank you, and Gary, why are  
22 damages important?

23 MR. LOEB: Well, damages are important on both  
24 sides of the equation for Genentech. We're the target  
25 of IP lawsuits about 60 percent of the time, and we are



1 the enforcer of IP about 40 percent of the time. So I  
2 guess like some of the panelists, we actually feel like  
3 we're sort of a little bit in between the two camps that  
4 Bryan talked about a little bit, that have sort of  
5 dictated the patent reform debate.

6 We're sympathetic to the concept of patent  
7 hold-ups because there are a variety of cases that have  
8 bubbled through the system on things like research tools  
9 or such where either the patentee is trying to claim a  
10 reach-through royalty on a product that doesn't actually  
11 practice the patent, or somehow the patentee has gotten  
12 claims to sort of a reach-through claim -- where they've  
13 covered the entire product by expanding the scope of  
14 their claim, but really focusing on the inventive step in  
15 their invention.

16 And actually one of the key biotech cases that  
17 went to the Supreme Court dealt a little bit with the  
18 issue, the *Merck v. Integra* case, where you ultimately had  
19 what was deemed by the Federal Circuit opinion that was  
20 ultimately -- that is no longer in force -- what was  
21 deemed as a reasonable royalty of \$15 million that was  
22 essentially approved in the Judge Newman dissent where  
23 you had -- against Merck which had never gotten a  
24 product to the market, had never made a sale, had just  
25 had investment in development of tens of hundreds of

1 millions of dollars in a product, and so you had debate.

2           Ultimately that damages award of \$15 million, I  
3 think was reduced to \$6 million, but still that's a  
4 pretty hefty sum when even today, five years, four years  
5 after the fact there's still no product from Merck out  
6 on the market, so who knows if there will ever be a  
7 product out on the market by the time that the patent  
8 expires.

9           So we're sympathetic to the concept of patent  
10 hold-ups, but at the same time we're very invigorated  
1000 0tent

1 they've actually launched because the whole process of  
2 clinical trials is insulated from infringement, so you  
3 have a period where maybe you know someone has a very  
4 similar product that's potentially practicing your IP,  
5 and you're both sort of in development. Maybe you  
6 launch, but you can't find out until they launch if they  
7 really infringe your IP because you don't have a ripe  
8 case or controversy because there's no actual  
9 infringement.

10 So we definitely think that once you actually  
11 have a case with someone who hasn't taken a license, you  
12 need to be able to enforce your patents and be able to  
13 get appropriate damages with respect to them.

14 So therefore we're very concerned about some of  
15 the proposals on the patent reform front with respect to  
16 inventive contribution or essential features or  
17 predominant feature, particularly predominant feature.  
18 Because you look at a biotech product, we just have a  
19 product. It's not a computer that's preloaded with  
20 software that comes with a screen.

21 I mean, we just have a product, and it's often  
22 very difficult to say that a very important  
23 contribution -- that maybe the main reason you got FDA  
24 approval -- is the predominant feature of the product.  
25 It's not a particularly meaningful analysis with respect

1 to a lot of pharma and biotech products, so we worry  
2 about a tailoring of the economic value rule or the  
3 reasonable royalty analysis that sort of excludes a  
4 whole area of technology.

5 And then the other thing, we worry about just in  
6 general is trying to over-tailor the whole approach to  
7 damages. I think I largely agree with Kevin that the  
8 *Georgia-Pacific* factors are working reasonably well, and  
9 maybe with apologies to Judge Robinson, I think  
10 sometimes it does involve more oversight by a judge to  
11 make sure that they continue to work well.

12 And just before I close, I just want to bring up  
13 one case where we actually faced a theory that was going  
14 to the jury where a very reputable economics damages  
15 expert was going to say that every time you have a  
16 negotiation, the parties will always meet in the middle,  
17 and you should always get 50 percent of the profits of  
18 the party based on the total number of licenses taken at  
19 the time.

20 That almost made it to the jury, and it was  
21 based on a sort of obscure theory of the mathematician  
22 from *A Beautiful Mind*, and coincidentally, *A Beautiful*  
23 *Mind* had just won the academy awards, so it was on all  
24 the jurors' minds, so we brought the *Daubert* motion to  
25 try to get that theory stricken.

1           Ultimately we didn't have to go there because we  
2   invalidated the patent, but I do think that damages  
3   experts, maybe more than some other types of experts,  
4   are willing to go out on pretty extreme lines and that a  
5   lot of money is wasted in the whole damages expert  
6   battle, and often they have very little or not very  
7   recent real-world negotiation experience.

8           And you would think that that would be a key  
9   component of a true damages expert, not economics  
10  degrees from Oxford, but I've actually negotiated these  
11  licenses, and you don't find a lot of those people  
12  because those people don't really want to take sides.

13           So with all that said, I think we continue to  
14  feel that flexibility is crucial, and we worry about



1 the way you determine lost profits in appropriate cases,  
2 the ability historically to have injunctive relief in  
3 most cases, all of those together permit inventors, have  
4 permitted inventors to capture the full economic value  
5 of their inventions.

6 In turn that has allowed us as venture  
7 capitalist to provide capital to those inventors to  
8 develop the inventions. If you do not allow inventors  
9 to capture the full economic value of their invention  
10 but some hypothetical, arbitrary amount less than that,  
11 which nobody has ever been able to actually adequately  
12 describe, the amount of venture -- the amount of things  
13 that will qualify for venture capital financing -- will  
14 decrease.

15 Somebody said on the first panel there are very  
16 few actual laws of economics. I agree with that. There  
17 are almost no good laws of economics as we have learned  
18 recently, but one of the real laws of economics is that  
19 if you decrease returns, you will decrease investments.  
20 I mean, that I can guarantee.

21 So the reason that damages are so critical as  
22 one of the elements of the innovation system is that it  
23 does, together with other components -- injunctive  
24 relief I can tell you is arguably even more important in  
25 many cases, and the fact that injunctive relief is less

1 available is a huge issue for us. It is a major factor  
2 for us now in the way we think about funding companies  
3 as compared to how we thought before eBay. But damages,  
4 injunctive relief and other things are simply absolutely  
5 critical.

6 Bryan made a point before, told the story about  
7 his frat brother meeting with the scientist. I always  
8 tell this story. I mean, my experience is that when I  
9 meet an entrepreneur, there are usually three people at  
10 the table. There's the entrepreneur, the business  
11 person. There's a scientist and an engineer, and  
12 there's a venture capitalist. There's Bob Swanson and  
13 your founder. There's Bob Noyce and Arthur Rock. The  
14 entire semiconductor industry was created by venture  
15 capital. The entire biotechnology industry was funded  
16 by venture capital.

17 And you know, then there's the venture  
18 capitalists, and we talk about the -- there are two  
19 pieces of paper. There's a business plan that talks  
20 about the transistor and integrated circuit or splicing  
21 genetic engineering or something else, and there's a  
22 market and all that. And we go through all of that, and  
23 inevitably, the next question is: Is there another  
24 piece of paper on the table? And the other piece of  
25 paper is a patent.



1           If you don't have a patent or some other way to  
2           enforce your IP -- and IP broadly defined, trade secrets  
3           are IPs, but we're talking about patents. As much as I  
4           love the idea, my answer is 99 percent of the time going  
5           to be, I can't finance that. There's just there's no  
6           way to protect me from the enormous asymmetric power  
7           that other competitors have in the market versus my  
8           little pip-squeak start-up. I'm sorry. Some of these  
9           pip-squeaks grow up to be big companies. Anyway, that's  
10          what it matters to us.

11           MS. MICHEL: Thank you. Phil, why are damages  
12          important to Johnson & Johnson?

13           MR. JOHNSON: First by way of introduction, and  
14          maybe you know this, hopefully you're all wearing  
15          Band-Aid brand adhesive strips or use baby shampoo,  
16          Johnson & Johnson baby shampoo or Roc or Neutrogena or  
17          some of those other consumer products of ours.

18           But actually we're much more than a consumer  
19          products company. Collectively our 200 companies are  
20          the largest medical device manufacturer in the world.  
21          We're the largest healthcare company in the world. Our  
22          companies collectively are the third or fourth largest  
23          biotech company in the world and the fourth or fifth  
24          largest pharmaceutical company in the world.

25           We are plaintiffs and we're defendants more or

1 less in equal numbers, but unlike many companies that  
2 you hear in this debate, if you pick up our 10-K and you  
3 look, we have material patent litigations that are  
4 listed both as plaintiffs and as defendants.

5 We have litigated and do litigate against people  
6 at this table. Some of them, Kevin, we've paid damages  
7 many times the sales of our product to. Thank God  
8 that's dropped off the top ten list by now.

9 MR. RHODES: Thank you. Yes, unfortunately.

10 MR. JOHNSON: But I find myself thinking about  
11 our business as being very much like Jack's discussion  
12 of venture capitalists. We have more products to  
13 develop throughout our businesses and our different  
14 industries than we can afford to fund.

15 Right now, this is a time -- and we're not  
16 immune from the economic realities of what's going on.  
17 This is a time when there are a lot of reasons not to  
18 take risk. There are always a lot of reasons not to  
19 take risks, but there are especially now a lot of  
20 reasons not to take risks.

21 The patent system is the reason that we invest  
22 7.7 billion dollars a year in R&D, and when we sit down,  
23 we're very much like what Jack says, yes, we listen and  
24 we hear about the technology too. It happens to be  
25 maybe an internal team, but sometimes it's not.

1 Sometimes it's someone like Julio Palmaz who came to us  
2 with the idea for the first coronary stent, or sometimes  
3 it's a venture capitalist, or sometimes it's a  
4 pip-squeak company that's now substantial.

5 But in any event, we're looking at a number of  
6 things. We're looking at technical feasibility and  
7 technical risk, and in some of our areas, especially  
8 pharmaceuticals but not just pharmaceuticals, they're  
9 huge risks.

10 Then we're looking of course at the ability, if  
11 we go out into the market, to have exclusivity. In some  
12 areas like in pharmaceuticals, if we come out with a new  
13 drug, we might have five years of data exclusivity, but  
14 you can't begin to finance a billion dollar drug  
15 development project over 12 or 14 years on five years of  
16 exclusivity.

17 So it's all about the patents, and then we look  
18 at what's happened in the marketplace over the last --  
19 or in the legal community. It's harder to get patents,  
20 much harder to get patents, much harder to enforce  
21 patents, much harder to get injunctions if you're  
22 successful, and finally you come down to whether if you  
23 do win, are you going to collect damages?

24 And then let's assume that you are wildly  
25 successful, and after six or eight or ten years of



1 million dollars in R&D in order to produce a patent, on  
2 average. Where does that go? We're not building Taj  
3 Mahal research labs. It's necessary to have research  
4 labs, but R&D money is mostly jobs.

5 They're good jobs. They're jobs of Ph.D.s and  
6 highly trained people and ancillary people, and they're  
7 jobs, and there are a lot of jobs, and then when you get  
8 a patent and if the patent is enforceable and worthy of  
9 having more capital invested in it, it's more jobs, and  
10 if it produces a business, it's more jobs than that, and  
11 eventually one day you grow up to be Intel, like David's  
12 company did or like Gary's company did, and you have a  
13 real growing economy.

14 We're talking in patent damages about whether  
15 we're going to put the brakes on people who might take  
16 risks, and I think this is exactly the wrong time to be  
17 talking about putting on the breaks. I think we ought  
18 to be hitting the gas.

19 MS. MICHEL: Okay. And, Keith, why patent  
20 damages are important to your company?

21 MR. AGISIM: Sure. I'm with Bank of America, a  
22 very popular company these days. Despite that, I think  
23 we also take a very balanced approach to patents and  
24 damages in general. We do a substantial amount of  
25 research and development internally, hundreds of millions

1 of dollars a year. Most people don't realize, but the bank  
2 employs tens of thousands of engineers to develop the  
3 technology internal to the bank.

4 So not only do we have our own IP, the bank has  
5 relationships with 99 percent of the S&P 500. One in  
6 two consumers have some sort of banking relationship  
7 with the bank, so for us, the patent system has to both  
8 work for us in our industry, but it also has to work for  
9 our clients, the people that bank with us and have  
10 financial relationships with us.

11 So when we look at the damages issue, you know,  
12 it's an important issue, but I think it's important to  
13 put in context with a lot of the things we saw this  
14 morning -- in terms of forum shopping and venue and some of  
15 the quality issues we have seen at the PTO and some of  
16 these damages numbers we've seen. It's a holistic  
17 probable with the patent system, in that damages is an  
18 important and essential feature, something we'll talk  
19 about more today, but it's not the entire issue. It's  
20 one piece in a larger puzzle of overall patent reform  
21 that's needed.

22 Let's turn to damages itself. I think we've  
23 heard a lot here about needing proper incentives and  
24 investments, and I think it's important to keep in mind  
25 that the damages, at least as it relates to reasonable

1 royalties and lost profits, are supposed to be  
2 compensatory. It's going to compensate for your harm,  
3 no more, no less.

4 There are other mechanisms in the law to deal  
5 with punitive damages, to try to create and modify,  
6 incentivize people of certain behavior, injunctions and  
7 maybe that's the place that needs to be looked at.  
8 There's attorneys fees, costs and there are other  
9 mechanisms within the law to deal with that, but the  
10 damages themselves are supposed to be compensatory.

11 When you look at what's happening there, from  
12 the bank's perspective, we see a system that's broken.  
13 We saw this morning that non practicing entities on  
14 average get more money in damage than competitors do.  
15 That doesn't seem to make a lot of economic sense.

16 We also see -- which is a big issue for us -- is  
17 that we often get sued as an end user, something that  
18 someone else makes, we incorporate into online banking  
19 so people can log on, not have their identify stolen.  
20 We get sued on that feature.

21 The damages against the end user are subst15t.aa be compe

1           So you talk about what's the effect of at least  
2 in our view what are large excess damage awards? Well, I  
3 think we heard this morning -- I think the panel this  
4 morning had a consensus that you don't see a substantial  
5 increase in litigation. If people are over-compensated,  
6 that's going to drive more litigation, and that's  
7 exactly what we see in the financial services world.

8           A professor at Harvard Business School, the  
9 professor did some studies. He found that financial  
10 patents are 27 times more likely to be asserted than non-  
11 financial patents. Those numbers are orders of  
12 magnitude more than some of the most litigious areas of  
13 patent law such as pharma and biotechnology, so we far  
14 exceed the number of lawsuits.

15           If you look at growth rates for our cases in the  
16 financial services world, we're two times sort of the  
17 growth rate in technology, about four times the growth  
18 of overall patent litigation in the United States.

19           So if you ask in terms of: Is over-compensation  
20 happening? Again if you go by what the experts, the  
21 economists say this morning, if there's over-  
22 compensation, you'll see an increase in lawsuits. We're  
23 seeing it in the financial services world. Just look at  
24 the proliferation of non-practicing entities. If it  
25 wasn't a viable business model or you didn't get an out-



1 sized return for it, you do something else, it's a  
2 proliferation.

3 So to give more perspective, I think damages  
4 law, at least as it relates to financial services is  
5 broken and needs to be fixed. We talked a lot about --  
6 people have talked about jobs and the role innovation  
7 plays in that. I think it's important to keep in mind  
8 too that with increase in cost, with increased  
9 innovation, that's less products that we can introduce  
10 or any company can introduce. You have a lot of over-  
11 compensation.

12 That doesn't normally affect the bank, but again  
13 we're an aggregator of technology. We're an end user of  
14 technology. We develop our own, so that is a huge  
15 cascade effect of the entire economy, thousands of  
16 suppliers. If we don't bring a product to market, that  
17 affects thousands of suppliers and thousands of jobs.

18 I think the other just closing remark here, the  
19 last thing I would point out is that speaking about  
20 banks in general, not Bank of America per se, but  
21 banks -- certain capital ratio, which again is -- it's  
22 something to learn about in the banking industry lately,  
23 but so just as a ball park rough industry average, for  
24 every dollar that gets paid to non-practicing entity,  
25 that's \$10 that they can't lend out to businesses and

1 consumers to help the economy grow.

2 MS. MICHEL: I thank you all for very much for  
3 giving us this perspective to understanding the  
4 importance of patents in your companies.

5 We will now go to the system where I would ask  
6 you to turn up your name cards if you would like to  
7 answer. We talked a lot this morning about the role of  
8 damages as being compensatory to put the patentee in the  
9 position he would have been in had there been no  
10 infringement.

11 Any comments on whether that is the goal of the  
12 damages system, whether the goal stretches beyond that,  
13 and if so, depending on what you think the goal is, how  
14 should law approach it?

1           MR. LASERSOHN: So I generally agree with that,  
2 but I would add that if you go a layer below that, when  
3 you say to put the -- that is compensatory, to put the  
4 patent holder in the position he would have been in had  
5 the infringement not occurred, that is another way to  
6 look at the question of economic value; that is, what  
7 economic -- what has that cost the patent holder from an  
8 economic value point of view because ultimately those  
9 are two sides of the exact same coin? And I think that  
10 the answer to one is in fact the answer to the other.

11           They're the same answer effectively. Whether  
12 you call it compensatory or some other word, that is in  
13 fact what you're attempting to seek to find in both of  
14 those cases.

15           MS. MICHEL: Okay. Kevin?

16           MR. RHODES: Yes. I do believe generally that  
17 the goal of damages law should be to be compensatory. I  
18 don't think it is. I don't think whether its lost  
19 profits is determined under *Panduit* or reasonable  
20 royalty under *Georgia-Pacific*, I don't think by the time  
21 there's a remedy for infringement, even in the best  
22 case, even in the case where the patent holder gets a  
23 permanent injunction, gets lost profits for maybe some  
24 kind of market-based analysis of lost profits plus a  
25 reasonable royalty, you're ever put back into the

1 position as if the infringement had never occurred.

2 By the time of a final judgment and a damages  
3 award and an injunction, the infringement has changed  
4 the marketplace, whether it's reputational for the  
5 patent holder, customer relationships, pricing structure.  
6 You're never put in a fully compensatory position as if  
7 the infringement had never occurred.

8 So when people talk about over compensating or  
9 under compensating the patent holder, I come back to:  
10 Compared to what and based on what facts? It's very  
11 factually specific. I do think the goal ought to be  
12 compensatory with one additional layer on that. I think  
13 that we do run the risk if we take away too many  
14 remedies from patent holders, so permanent injunctions,  
15 decrease damages, you do lose part of the deterrent  
16 affect against infringement.

17 It's something that Professor Cotter was talking  
18 about this morning, especially in the context of  
19 undetected infringement. Is there going to be more  
20 incidents of undetected infringement if the remedies  
21 available to patent holders are too low?

22 MS. MICHEL: Bryan?

23 MR. LORD: I want to touch just a little bit on  
24 the over-compensation issue. It's been put forth that  
25 if there's over-compensation, we'll see an increase in

1 litigation, and the logical then conclusion that we're  
2 supposed to make is that: Well, therefore if there is  
3 an increase in litigation, then there must be over-  
4 compensation.

5           The two don't -- as all us I think as logicians  
6 might know that that's not necessarily a truism. In  
7 fact, there's certainly other explanations for that  
8 phenomena that may be the case. One might be the fact  
9 that there's more infringement. If there's more  
10 infringement, there might be more litigation.

11           In fact, as we know in some industries, and  
12 there's a famous situation where a Microsoft attorney  
13 was found to have been instructing his internal clients  
14 to say: Do not look at patents it, do not read patents.  
15 In fact, ignorance is bliss is the quote that I recall.

16           Well, if that's the case, it's likely to be the  
17 case that infringement increases in situations  
18 where you're training your people to ignore and be  
19 blissful about your ignorance of patents, so that  
20 certainly is a possibility. The other possibility is  
21 that we could have increases in patents which might call  
22 for an increase in litigation, and in fact, we know that  
23 that's been the case.

24           And frankly for all of us who believe in, as I  
25 think all the panelists do, innovation, we ought to

1 celebrate the fact that we have more patents in our  
2 system rather than less. We would be having a very  
3 different panel discussion if we were trying to figure  
4 out how to resurrect an innovation economy where there  
5 was not a lot of patents being filed, so that's a good  
6 thing, and we might expect then some litigation to  
7 flow -- to proportionately increase with that.

8 In fact, that's the last point on a  
9 proportionately case when we can look at all kinds of  
10 numbers, and of course statistics can be manipulated as  
11 you like, but if you actually look at the number of  
12 lawsuits per patent, it has roughly been the same  
13 amount -- 1.5 percent of all patents that have been  
14 issued over the last 20 years have been the amount of  
15 litigation that's ensued.

16 So we've seen actually a very flat amount of  
17 litigation for patents that have been issued over the  
18 course of the last 20 years, and that actually suggests,  
19 as I think Kevin said, that we might be looking for a  
20 solution in search of a problem here.

21 MS. MICHEL: Marian?

22 MS. UNDERWEISER: Thank you. What I think I've  
23 heard from a lot of people on the panel are issues  
24 surrounding speculation generally speaking, that what  
25 people are concerned about is the ability -- I mean, to

1 answer your question, yeah, absolutely. Reasonable  
2 royalties and lost profits, trying to compensate the  
3 patentee, and that's what they should do. They should  
4 be compensatory.

5 And I think that we're all recognizing that in  
6 patent litigation, there is risk. There's risk and  
7 there's cost, and so you don't want to end up having to  
8 litigate because there's uncertainty associated with  
9 what you end up with from either side of the equation.

10 And so part of the problem is to push the  
11 disputes to be resolved before you get there. So in order  
12 to do that, I think what you want to avoid is issues  
13 within the context of litigation that are speculative  
14 and are hypothetical and that are unknown. And that's  
15 why it's helpful to have something of a more objective  
16 standard, because I think that from what I'm hearing from  
17 the panelists -- if we could all agree somehow upfront,  
18 licensor-licensee, on what the value is and actually  
19 come to an agreement to where both sides of the table  
20 know that if they do end up in court, that this is where  
21 the valuation is going to go, they have an idea about  
22 that, they're more likely to agree up front. That would be  
23 better.

24 You wouldn't worry about how do I get my  
25 interest and how do I make sure that I really was

E0 rgBT3risk and

1       compensated and how do I figure out all these other  
2       contingencies to make sure that I really am compensated?

3               So the point of having more objectivity is  
4       avoiding that.

5               MS. MICHEL:   Dave?

6               MR. SIMON:   Yes.   So that is precisely the  
7       issue.   I don't think anybody disagrees that this is  
8       about adequate compensation.   Sometimes the disagreement  
9       is about what is adequate compensation, but we have a  
10      really serious issue of you have a test that is in  
11      essence a grab bag for whatever -- that frequently comes  
12      pretty close to whatever a jury comes back can be  
13      supported under because you can choose all, some or none  
14      of those 15 factors.

15              And then the Federal Circuit has told us that  
16      they won't overturn a jury verdict unless it's  
17      monstrous, which creates an additional problem for the  
18      District court judges who, I know they want to do  
19      justice.   On the other hand, I know the last thing most  
20      district judges want to do is to re-try a patent case.  
21      I could be wrong on that, but that's --

22              THE HONORABLE JUDGE ROBINSON:   That's wrong.

23              MR. SIMON:   I won't say his name, but I once had  
24      a District Court Judge threaten to whip out a gun if we  
25      brought the case back to him, and I know he kept one





1 said -- we stopped counting at 1,500 of our own patents  
2 in our product, and yet when you go to trial with this  
3 grab bag of factors, the trial, as Ed Reines has said  
4 this morning, is about the patent in suit.

5           You get at best, depending on the district, 40  
6 to 80 hours to try the case. You're going to be talking  
7 about the patent that's in suit, about the validity, the  
8 infringement, the damages, and maybe you'll get to spend  
9 a little bit about the atmospherics of your business,  
10 but the result is you have a huge over-emphasis on that  
11 patent in many instances.

12           So what you've done is you've created a huge  
13 amount of uncertainty, and whether you're looking at the  
14 threat of an injunction or not looking at the threat of  
15 an injunction, when you're looking at the huge  
16 potential damages theories, and we've had people come in  
17 with 5, 10 billion dollar damages theories, you have to  
18 take a step back and say, what's the rational act here.

19           The rational act is that you will try to settle  
20 these things, and you will try to settle these things in  
21 my view at what's -- if you really had to do a negotiated  
22 a bargain between the parties of what we would have  
23 paid at the time. If we had a choice to pay this much to  
24 use this patent, and we almost invariably have another  
25 option at the time we were doing our design decision, we



1 discussion around who owns that patent.

2 If it's a NPE, does that make that patent less  
3 valuable? Did less work possibly go into that patent  
4 because it's now being held by an NPE? I'm not sure  
5 that that's the way we should be looking at it.

6 The patents should be looked at with respect to  
7 whether they're good patents, bad patents, valid,  
8 invalid, infringed, not infringed. The owner of that  
9 patent is not a part that equation. Now, we talk about  
10 the increased litigation by NPEs and the fact that  
11 they're getting these larger damages awards.

12 I think it's pretty much well accepted that  
13 there's been a large number of entities that have been  
14 created recently that are able to assist individual  
15 inventors who, by the way, based on statistics that were  
16 discussed at the last hearing, they get -- 60 percent of  
17 the patents are given to individual inventors. They're  
18 able to help them monetize those patents.

19 They don't have and we don't have the billions  
20 of dollars to establish the types of plants that David  
21 was talking about, so because you have more avenues for  
22 the NPEs to be able to monetize those patents, you are  
23 seeing more of those patents out there. You are seeing  
24 more litigation around those patents.

25 The numbers go up. To the extent that the

1 patents are in industries where there are a large  
2 volumes of products, you're going to see larger numbers  
3 of products, so there's really nothing surprising about  
4 the trend now. And if our goal is to say we want to  
5 reduce the amount of litigation so we're not going to  
6 want these NPEs to enforce those patents -- rather than  
7 determining whether those are actually good patents that  
8 read on these products -- that's not the right way to go,  
9 and there's no over-compensation or under-compensation  
10 or compensation at all. We're just basically valuing a  
11 patent based on who the holder is.

12 MS. MICHEL: Okay. Jack?

13 MR. LASERSOHN: So just with respect to the  
14 point about how risky litigation is, again the risks in  
15 litigation are wildly asymmetric. The risk to a small  
16 company is not only that it loses the actual litigation,  
17 but that it never makes it through a litigation. It  
18 doesn't have the money. It cannot raise money while  
19 it's litigating very often, so innovator companies will  
20 do almost anything to avoid litigation.

21 The obvious thing that all of our companies,  
22 venture-backed companies do, and every venture capitalist  
23 will tell you this, is we desperately try to negotiate  
24 deals with larger companies either to acquire our  
25 companies or to pay a royalty.



1 a lot of obfuscation about what should be and what  
2 shouldn't. It's really a question of: Let's reduce  
3 damages. The proposals about different standards is  
4 let's reduce damage awards.

5 The effect of that is -- will be for certain to  
6 reduce the amount of investment which, by the way,  
7 creates jobs. 12 percent of the current employment in  
8 the United States, 19 percent of the GDP, are venture-  
9 backed companies. Most of the new jobs being created in  
10 the United States come from small companies, not from  
11 large companies, with notable exceptions. So that will  
12 ultimately -- absolutely damages will ultimately affect  
13 job creation and investment and innovation.

14 MS. MICHEL: Is anyone arguing that damages  
15 should have a kicker, some sort of going beyond making  
16 the patentee whole for these reasons?

17 Okay. I'll take that as a no. Phil, your  
18 comment?

19 MR. LORD: In seriousness, unfortunately that's  
20 not the context of this overall debate. You could have  
21 a debate. This is part of my opening comments about  
22 saying which way should be move the lever. Increase  
23 awards for damages, decrease awards for damages, and  
24 there would be very rationale economic justification for  
25 increasing the awards for damages as well.

1           So I'll pipe up. I understand unfortunately  
2 this agenda has been set in a context that says take it  
3 as stipulate that damages are too high, let's figure out  
4 what to do in order to reduce it, as Jack just talked  
5 about, and I think that's too narrow of just a  
6 description of the economic realities that we all are in  
7 this innovative economy.

8           MS. MICHEL: Phil?

9           MR. JOHNSON: Ed mentioned this this morning,  
10 but didn't really go into it. It's very hard to figure  
11 out what's happening by looking at the cases that are  
12 selected to go to trial. I mean, there are thousands of  
13 cases and probably over 20,000 cases in that sample that  
14 we saw this morning.

15           We have very few that actually ended up in high  
16 damage awards either way. What we did see is if you're  
17 a patent owner and you go to trial or you press your  
18 case, you have a two-thirds chance of getting zero, and  
19 then if you do win it's a little less likely than  
20 average that you won't get enough to cover your  
21 attorneys fees.

22           So that's not all that exciting, but there's so  
23 many cases out there and so few go to trial that what's  
24 happening is defendants and plaintiffs are collectively  
25 deciding which ones to try. What's surprising to me is



1 that the damages numbers have stayed relatively flat  
2 because over that same period of time -- well, that was  
3 15 years. I think back everybody thinks about their own  
4 company, our company's revenues are twice -- more than  
5 twice what they were ten years ago.

6 So you would be expecting if they had grown  
7 simply with the growth of business, and business has  
8 grown in the last 10 or 15 years, you would be expecting  
9 the amounts of the awards to go up at least in  
10 proportion with the inflation or the GDP or whatever,  
11 and that to me suggests that something is at work that  
12 is actually diminishing the relative value of awards  
13 rather than enhancing them.

14 MS. MICHEL: Keith?

15 MR. AGISIM: Thanks. I just want to respond to  
16 a couple points that have been raised in this  
17 discussion. The first one relates to some comments  
18 about the person, the patent holder isn't relevant to the  
19 damages discussion, and I think that that really  
20 illustrates part of the problem, that damages are not  
21 based on economic realities but this mythical  
22 negotiation.

23 Defendants and defendant's economic conditions,  
24 the size of the company, their profits, those are sort  
25 of the favorite tactics you see from patent holders,

1 explaining why -- what one penny per unit or one penny  
2 per transaction is perfectly reasonable. I think if  
3 you're going to look at the economics of the defendants,  
4 you also have to look at the economic position of the  
5 patent holder.

6           And I think some of these start-ups that we've  
7 been talking about are different than sort of the true  
8 non-practicing entity. Their whole business is the  
9 business of infringement. They don't want people to not  
10 infringe their patents as a start-up company may.  
11 Start-up company doesn't want the infringement. They  
12 want to build their own market, create their company and  
13 create jobs.

14           Your typical non-practicing entity wants you to  
15 infringe. If you're not infringing, they go out of  
16 business. So I think it's a completely different  
17 dynamic that needs to really be addressed as we're  
18 looking at what appropriate measure of damages are.

1 specific, but there's a whole -- there's scores and  
2 scores of companies that basically go out and buy up  
3 patents from bankrupt companies or individuals, and they  
4 try to go and find people to assert against, so that's  
5 largely what I'm talking about.

6 MS. MICHEL: All right. Oh, let's -- okay. I  
7 want to move into a more substantive discussion -- I  
8 didn't mean that -- a discussion of the substantive  
9 legal rules is what -- but please don't take the tents  
10 down, and work in any comments you want to make there,  
11 but trying to understand how important lost profits  
12 damages versus reasonable royalty damages are to  
13 your company and whether -- let's start with lost  
14 profits, you think that lost profits -- if it's  
15 important in your industry and being done appropriately? Is  
16 it working? Are the right kinds of damages being  
17 awarded? Okay.

18 Phil? Thank you.

19 MR. JOHNSON: When I'm collecting, absolutely  
20 not. No, the fact of the matter is you're talking about  
21 competitor lawsuits with lost profits damages, and they  
22 are always extremely important on both sides, whether  
23 youn18don1Nf rg 0.00 0ron1Nfplinstiff and tct ully ga

1 people will default over to a reasonable royalty, where  
2 you can prove them, they usually are amongst the most  
3 accurate of the damages.

4           Frequently you have good data from both sides of  
5 the equation because the infringer will have -- one  
6 thing that every business does is they keep track of how  
7 much money they're making, how much profit they're  
8 making with what they're doing. You frequently get a  
9 good look at both sides of the equation as a result of  
10 the discovery, and it isn't -- while there isn't a wild  
11 disparity, margins are what they were and sales are what  
12 they are, and there can be disputes over the  
13 contribution.

14           But frequently I think that generally -- I mean,  
15 actually generally we settle quite a few, as Judge  
16 Robinson indicated, against competitors where liability  
17 is clear and where the market share information is clear  
18 so I think they're very important. But let me go on to  
19 say that it's a rare case where you have a two-supplier  
20 market, where you don't also have reasonable royalties in.  
21 Because when there's a three supplier market and you're  
22 suing one of your competitors or four or five or six  
23 supplier market, then reasonable royalties are always a  
24 component of your case.

25           And it's always a component of your case as a

1 back up because you can never be sure that your lost  
2 profits case is actually going to be sustained, and you  
3 give it to the jury, and if the jury decides you're not  
4 entitled to lost profits, then it defaults to reasonable  
5 royalty.

6 MS. MICHEL: Yeah. Gary?

7 MR. LOEB: I agree with Phil wholeheartedly that  
8 in competitor situations, the last profit analysis is  
9 working well. We're starting to see the lost profits  
10 analysis abused a little bit in sort of non-practicing  
11 entity situations where the lost profits analysis  
12 g70002 gETts 1.0mFp removed: Well, if you had  
13 entered into a license agreement back then, that would  
14 have given us more legitimacy and we would have got more  
15 profits as a company and could have got more investment.

16 So it'2 gETtthis causal chainETtlost  
17 profits inEa non competitor setting. I think that'2 a  
18 little troubles000 and should be s gETTavoided, and  
19 we're starting to see allegations like that, but just in  
20 the general realm where you have a competitor, I think  
21 everyys 1.agrees that'2 gETtthe heart and souleTta  
22 logETtthe patent disputes that we have and that you  
23 need to be able to be fully compensated, whether or not  
24 a reasonable royalty, lost profit, s000 combinationET  
25 both, especially in sort of a post-eBay rule.

1           MS. MICHEL: All right. And is lost profits  
2 available in a three or four supplier market? Phil,  
3 what's your experience with that?

4           MR. JOHNSON: Yeah. It's available but to a  
5 lesser extent because you have to show that you've  
6 actually lost the sales and therefore lost the profits,  
7 and when there's another or several other suppliers in  
8 the market, you have to deal with the issue that first  
9 of all, you probably won't collect more than your market  
10 share because the defendant will say: Well, if we hadn't  
11 infringed, these sales would have gone to the other  
12 suppliers and they would have purchased the other  
13 technologies.

14           So you have to fight it out. It becomes an even  
15 harder case. The more suppliers there are, the more  
16 substitutes there are, the more interchangeability there  
17 is, the less likely it is you end up with a good lost  
18 profits case.

19           MS. MICHEL: Jack?

20           MR. LASERSOHN: Yeah, and I would add to that  
21 actually, while I think lost profits works up to a  
22 point, for many of our companies, they are always making

1 tiny, and there's always the argument: Well, you  
2 couldn't have been in the business anyway for the list  
3 of 15 different reasons, or as Phil just said, nobody's  
4 going to -- the other competitor took your share because  
5 nobody wants to buy from a pip-squeak company in the  
6 sector, et cetera, et cetera.

7 So actually in our part of the world it is  
8 difficult in many cases to make a lost profits case  
9 stick.

10 MS. MICHEL: And in your world, do many of the  
11 parties you're dealing with have products? Isn't that  
12 the reason that there's no lost profits?

13 MR. LASERSOHN: I'm sorry?

14 MS. MICHEL: Do they have a product? Do you  
15 need to have a product to have a lost profit?

16 MR. LASERSOHN: Yes, but you don't need just a  
17 product. You have to prove but for the infringement you  
18 would have sold something.

19 MS. MICHEL: Yes.

20 MR. LASERSOHN: An example would be if you're a  
21 medical products company, for example, you might have a  
22 product, but the defendant would say it doesn't matter,  
23 the doctor won't buy from you anyway because you're a  
24 pip-squeak, so there are things other than having a  
25 product that you actually have to prove.

1 MS. MICHEL: Sure. My surprise was that in  
2 these early stages, that the company had a product at  
3 all and that lost profits did come in, but it sounds  
4 like you're talking about slightly later stage companies  
5 there.

6 Kevin?

7 MR. RHODES: I would just add briefly on the  
8 question of recovery of lost profits in a multi-player  
9 marketplace. As Phil said, it is possible to get lost  
10 profits with the market based analysis, with the more  
11 full analysis breaking down the competitive situation in  
12 the marketplace.

13 If there are three or four competitors it can be  
14 done. What we found though is sometimes markets get so  
15 fragmented that you couple together the chances of  
16 actually getting lost profits -- the amount of proof and  
17 expert discovery that's going to entail, the detailed  
18 disclosures that will require us to make on our own  
19 product lines and their profitability -- at some point you  
20 reach diminishing or no returns, and it's not worth  
21 going for in that situation.

22 MS. MICHEL: So the issue of whether to pursue  
23 lost profits is also a litigation strategy issue?

24 MR. RHODES: Indeed, and we've had cases where  
25 we had a product. There was direct competition, and for



1 some of those reasons I just mentioned, we decided not  
2 to go for lost profits but rather for an injunction and  
3 reasonable royalty damages.

4 MS. MICHEL: Phil?

5 MR. JOHNSON: The strategy of going for  
6 damages at all is frequently a litigation decision, or  
7 how much time to spend more often on damages, especially  
8 for defendants. If you think you have a good case on  
9 the merits, many trial attorneys think that you don't  
10 want to spend time standing up and putting on an  
11 elaborate damages case, for fear that the jury will get  
12 the idea that you think you ought to be paying something,  
13 because in order to put on a damages case, you have to  
14 assume that you're going to lose and then talk about how  
15 much you're going to pay.

16 So many times, especially for defendants, and I  
17 think Jack mentioned that this morning -- he said he  
18 didn't put on damages cases. Really, what you're seeing  
19 is you're seeing situations where that was a strategic  
20 decision to emphasize liability, and some of the cases  
21 that produce aberrant results are explainable when you  
22 go back and look at it because they didn't put on  
23 damages experts. They really didn't put on a damages  
24 case or they didn't put on a credible damages case, very  
25 abbreviated because they made a strategic decision that

1 they were going to win on liability and then were  
2 surprised that they didn't.

3 MS. MICHEL: For those of you who are sometimes  
4 defendants, what are your reactions to the thought --  
5 Judge Robinson's comments about bifurcating? Phil? Do  
6 you think that's a good idea, a bad idea? And also  
7 what's your experience and how often that happens?

8 MR. JOHNSON: I think it happens more and more,  
9 and I think the experience is generally good. I really  
10 don't think that the plaintiffs gain all that much by  
11 making a lot out of damages in a complex case.

12 I don't care what your invention is. It's very  
13 complicated for the jury, and what they really don't  
14 want to give up, the plaintiffs don't want to give up  
15 any willfulness attributes or willfulness evidence if  
16 they can avoid it, but now after *Seagate*, that's  
17 frequently dismissed and not allowed during the  
18 liability portion of the trial anyway.

19 So I think the biggest downside is it prolongs  
20 the proceedings. If someone is a small company and/or  
21 someone is hoping to collect money and doesn't want to  
22 give a below market rate loan to their competitor, it  
26.000 oney and doesn't wantu PofjETday

1           There will be at least one more appeal, and it  
2 will take you that much more time for you to get your  
3 paycheck if you're the plaintiff, but other than that,  
4 if you're talking strictly on the merits it's probably a  
5 purer way to address the issue.

6           MS. MICHEL: All right. Reasonable royalties,  
7 how should they be calculated? They are out there. Is  
8 the hypothetical negotiation just the best of all  
9 terrible alternatives or is it actually just a good  
10 idea? Marian?

11           MS. UNDERWEISER: Well, I think that the  
12 hypothetical negotiation model is -- as I think some of  
13 the panelists discussed this morning, I think it is a  
14 useful tool in certain contexts, but I think that  
15 fundamentally the problem with the model is that it's  
16 used as this baseline, this hypothetical negotiation,  
17 and it's inherently a construct. It's inherently  
18 speculative.

19           So part of the advantage of looking for a focus,  
20 which was also discussed a lot this morning. If  
21 something -- again as a starting point but looking for a  
22 focus to the invention, what is really the economic  
23 value of the invention, and to focus on that first -  
24 instead of trying to reconstruct this kind of  
25 hypothetical environment -- is that you're really more

1 focused on the substance of what was contributed just to  
2 start with.

3 So I think the inquiry gets lost in the context,  
4 and it doesn't mean that the contextual issues are not  
5 important or that they won't affect the royalty  
6 calculation, but if you can look at the invention to  
7 start with, you can use that to help you with these  
8 other tools, all right.

9 So if you had, for example, a question about non-  
10 infringing alternatives, something that was discussed  
11 this morning, well, won't it help guide the fact-finder  
12 to understand in the first instance what that invention  
13 is? What am I focused on here? What am I supposed to  
14 be focused on? If I know what the invention is, then I  
15 ought to be able to value this compared to what that  
16 closest non-infringing alternative is.

17 And I could give a mechanical example. I mean,  
18 if you have -- if you have a device that I would call a  
19 separable device, right, so let's say you have an  
20 invention where -- you have an invention for use in any  
21 kind of vending device, right, so it could be soda  
22 machines or it could be washing machines or it could be  
23 anything where somebody puts money in and something  
24 happens.

25 If your invention is separable to that

1     component, you have created a new device that takes  
2     bills instead of just coins, then you can compare that  
3     to other purely coin operated devices that could be used  
4     in lots more machines.

5             If you have instead an invention that actually

1 royalty rates in these industries. Now, first of all,  
2 it's very hard to figure out that the industries are  
3 because let's just say there's a big difference between  
4 Bose's headphones or Bose's loud speakers and Intel  
5 microprocessors, but nonetheless, I think they get  
6 lumped into the same place.

7 In addition to which, when you read the articles  
8 carefully, they say, Well, a lot of these things -- it's a  
9 little hard to say what the real number is because  
10 there's floors and there's ceilings. Now, a 5 percent  
11 royalty where you have a ceiling of a million dollars a  
12 year is a big difference from a 5 percent royalty where  
13 there is no ceiling.

14 So as a result, a lot of this is used as a  
15 way -- as a vehicle in my view to get stuff in that  
16 really has very little bearing in the industry. We keep  
17 hearing about the royalty base and the running -- and  
18 what percentage to apply to the damages. That's not the  
19 way we negotiate licenses at Intel.

20 Our view is it's an inappropriate way to deal  
21 with it in our business, so as a result, it's a very  
22 different -- it's a very different model. Yet everybody  
23 uses this as a vehicle to try to say it would have been  
24 a running royalty rate.

1           MR. SIMON: The alternative presumably being a  
2 lump sum. What was the value of this at the time we  
3 made the decision and balancing the risks of using that  
4 approach to the other approaches that were available to  
5 us. It's rare that in our industry there's only way to  
6 do something.

7           MS. MICHEL: How successful is that as a  
8 litigation tactic to say in the hypothetical world, we  
9 would have only ever paid lump sums, so let's talk about  
10 that?

11          MR. SIMON: We have yet to figure that out.

12          MS. MICHEL: That means it hasn't worked yet.

13          MR. SIMON: It hasn't worked and it hasn't not  
14 worked.

15          MS. MICHEL: Okay. Got it. Keith?

16          MR. AGISIM: Thanks. I think the hypothetical  
17 negotiation can work. Obviously I don't think it's a  
18 one size fits all solution. It's really very context  
19 specific.

20                 There's one aspect of it I wanted to comment on  
21 is the hypothetical negotiation is supposed to occur the  
22 day before infringement begins. So there's an artificial  
23 construct, and I think -- and again the day before  
24 infringement begins, most company's marketing department  
25 have sort of grandiose visions of the world. Otherwise

1 it wouldn't launch these products.

2 I think once place where it falls down is I  
3 don't think there's enough clear rules around again, what  
4 really happened, right? It's not just artificial day  
5 before infringement, but real world, what happened?  
6 There should be more analysis, more reliance on actual  
7 economics of what occurred during infringement.

8 As we heard this morning there's enough  
9 assumptions, enough hypothetical and theoreticals built  
10 into these damages models from the experts as it is, that  
11 to the extent real data does exist, I think that's  
12 something important to factor into these analysis.

13 MS. MICHEL: Gary?

14 MR. LOEB: I just want to go back to a few of  
15 the comments that I've heard on sort of the reasonable  
16 royalty analysis and the hypothetical negotiation. It  
17 is inherently speculative, but I haven't heard an  
18 alternative that is any better, and I think that this  
19 concept of what is an invention, what is the invention  
20 really or the inherent contribution or what are the  
21 essential features of the invention or product, creates  
22 sort of a mini patent office review procedure in the  
23 middle of a trial or court proceeding that is largely  
24 going to be how well does the invention translate or  
25 inspire a layperson or a judge to think: Oh, that was a



1 really cool idea.

2           And it's not going to be any less, or any fairer  
3 to sort of go down that approach. It essentially  
4 creates a mini grading system of it is a grade A patent,  
5 this is a grade B patent, this is a grade C patent. And  
6 if we wanted to do that, by sort of saying well this  
7 invention has two essential features or this invention  
8 has three essential features, all of which are embodied  
9 in the product, I think that's a dangerous path to start  
10 going down.

11           I think the reasonable royalty in the  
12 *Georgia-Pacific* analysis allows you to take in the  
13 entire range of factors and doesn't try and distill the  
14 invention in a way that might -- that I think doesn't  
15 necessarily give it the force that it deserves.

16           And I guess I want to make one point about the  
17 aberrant awards where you have an invention that's a  
18 very small piece of a larger product and the fear that  
19 that's going to really create a huge reward because  
20 defendants aren't allowed to spend much time talking  
21 about their product, and I think that's a very real  
22 concern.

23           I think that sometimes the defendants end up  
24 talking a lot about their product in the context of  
25 secondary considerations of non-obviousness and sort of

1 the commercial success of their product with respect to  
2 their own patents or to be able to sort of talk about  
3 those types of things, if they are a practicing entity  
4 of their own patents, and sometimes they're then able to  
5 present a lot of evidence on their own infringing  
6 product, but it's the rare case that that happens.

7           So then you can end up with these situations  
8 where you have aberrant awards, but it's just the  
9 ability to make sure that that issue is properly vetted  
10 to make sure the reasonable royalty analysis works. And  
11 I guess I want to sort of raise a question with respect  
12 to sort of a company like Intel that has enough money  
13 that you could always do a net present value analysis  
14 where if the reasonable royalty is low enough, it's  
15 going to be exactly identical to you from a cash basis  
16 as a lump sum.

17           Maybe it's a really low reasonable royalty.  
18 Maybe it's one that you're embarrassed to say before a  
19 jury, which is .000015 percent or something like that,  
20 and maybe that's the problem with why you're saying it's  
21 a non-starter, but you always have both royalty base and  
22 royalty rate.

23           So it doesn't seem to make sense that -- all a  
24 lump sum is doing is sort of saying the royalty rate  
25 here is so low that is it worth the transactional effort

1 of keeping track? But it always seems like there's some  
2 rate that could approximate whatever that lump sum is  
3 going to be.

4 MS. MICHEL: Do you want to respond, Dave?

5 MR. SIMON: Okay. So by the way, as part of my  
6 response, I disagree with the statement that you make  
7 that there aren't grade A, B or C patents in terms of  
8 economic value. I think absolutely there are clearly  
9 patents that are more valuable and patents that are less  
10 valuable.

11 In terms of what -- the reason why I say it  
12 doesn't make sense to take a running royalty is we look  
13 at it as -- there are a couple of different -- in many  
14 instances we have lots of options of how we're going to  
15 do something, okay. There are benefits for using a  
16 technique and there are disadvantages of using a  
17 technique in almost every single case.

18 They're going to get relative performance for  
19 certain things and not for other things, and we're  
20 hoping that we're going to project four years out when  
21 we do these designs decisions, that we're going to guess  
22 for the right place for the market, and we haven't  
23 always guessed right.

24 That's the way we're looking at it, and if  
25 somebody comes up and says, I want -- let's take the

1 example of the Microsoft versus AT&T. That 1.52 billion  
2 dollar judgment, and let's not forget that .02 there  
3 because that's 20 million bucks, was a .5 percent  
4 royalty rate for a decoder, one of several decoders  
5 actually. There's two decoders, one of which didn't work.

6 And if Microsoft had been presented a choice of  
7 you can use this decoder and pay a .5 percent running  
8 royalty on PC sales, which is what that was, or not use  
9 it, it's really simple. We won't use it. We don't need  
10 it. There were other ways to do that decoding.

11 From our standpoint we look at these things, and  
12 if you tell us it's going to cost us .5 percent running  
13 royalty or .1 percent running royalty, almost invariably  
14 there's a cheaper choice. That's why running royalties  
15 don't make sense typically in our business because  
16 there's almost always another choice of what we can do.

17 There may be -- they may not be quite as good.  
18 They may have certain other -- they may have certain  
19 disadvantages. They may have certain advantages, but  
20 the idea that we would say, we are going to take a  
21 revenue stream on a product that literally has, like the  
22 Supreme Court has said, thousands of patents in it to  
23 any one patent just doesn't make sense to the business.

24 MR. ADKINSON: Bryan?

25 MR. LOEB: I think another thing that we have

1 sort of stipulated to in this discussion and sort of  
2 overlooked when we talked just about damages is the fact  
3 that if we're at damages, we have concluded that  
4 infringement has occurred, and we ought not simply  
5 overlook that fact.

6 Infringement is not supposed to occur. We're  
7 supposed to have a system that actually disincentivizes  
8 infringement from occurring, and when it does, then have  
9 certain circumstances that we have spent a lot of time  
10 talking about here to address that situation, but I  
11 think we have a public policy arena, and I think we're  
12 all in agreement with this, that we're 00000 0.3% have

1 you've done is really put water and beans into this cup,  
2 I think it's worth about a nickel.

3 And they said, No, it's worth 3.95, and I say  
4 it's a nickel, and then I say, I'll tell you what, how  
5 about if we find somebody else to try and come up with  
6 an objective standard for what this thing is worth?

7 Somewhere I guess in between perhaps is the  
8 answer, but at the end of the day, Starbucks should have  
9 the right to say, You don't get that cup of coffee.  
10 It's up to you whether you want to walk into my store,  
11 drink the cup of coffee or not, and I think it's the  
12 same argument about infringement.

13 We ought to start with a public policy regime  
14 that says don't infringe, and if you do, then we'll find  
15 out a way to reconcile the differences between the  
16 parties.

17 MR. ADKINSON: Jack?

18 MR. LASERSOHN: Yeah. I think that in the final  
19 analysis, the search in all of these conversations for  
20 damages is ultimately to find the economic value. I  
21 think that is really what is going on.

22 My impression of the function of the  
23 hypothetical negotiation is to put a process in place  
24 for the jury to actually find that economic value.  
25 That's what the -- that's what the hypothetical

1 negotiation is all about.

2           It says: Okay, we want to find the economic  
3 value and the jury says, Well, how, and you say, imagine  
4 that you were negotiating at the time, what would you  
5 have agreed on? That is the economic value, and the  
6 answer then is, well, what should I consider, and then  
7 they pull out *Georgia-Pacific* and their 15 different  
8 thing you should consider.

9           Well, as a famous physicist once said, you said  
10 simplify things as much as possible but no more, and  
11 unfortunately, this is complicated. Every single  
12 company in our portfolio has a different situation.  
13 Every single competitor is different. Every environment  
14 is different.

15           We heard this morning that in the Wal-Mart case  
16 where they cut the price by 75 percent, and so the  
17 actual royalties were greater than the selling price.  
18 There are models, business models now where people give  
19 away software for nothing in order to collect a service  
20 fee.

21           So every single -- Intel doesn't want to pay a  
22 running royalty, okay. That would have been part of  
23 that hypothetical negotiation. We will under no  
24 circumstances pay a running royalty. Well, if everyone  
25 else pays a running royalty, that may or may not have

1       been persuasive as an argument.

2               I just don't see how if the ultimate search is  
3       to find the economic value that you can simplify that to  
4       some formalistic approach. It is complicated, and the  
5       hypothetical negotiation, at least to me, when I again  
6       as a non-lawyer think about it from a common sense  
7       approach, how would I do that, I would say: Well,  
8       imagine you were negotiating. And that's in fact as I  
9       understand it what the law is.

10              MR. ADKINSON: Taraneh?

11              MS. MAGHAME: I think Jack said about 80 percent  
12       of what I was going to say, is that the whole  
13       hypothetical negotiation needs some parameters. After  
14       all, it is what one side is willing to pay and one side  
15       is willing to take.

16              So David's point about what he is willing to pay  
17       comes into play in the hypothetical negotiation  
18       situation, and all these other factors, the  
19       *Georgia-Pacific* factors also come into play because the  
20       ultimate goal is to determine economic value, and





1 possibility of compulsory licensing, what kind of rates  
2 do you set for a compulsory licensing type scenario.

3 Courts have not decided that yet. We've seen I  
4 think one or two instances where they've tried to do it,  
5 but it's even more difficult to set a reasonable royalty  
6 going forward now because of things that we discussed  
7 this morning in terms of changes in the economics, but  
8 at least in that respect, you know what's happened in  
9 the past.

10 If you can -- if you need the flexibility to do  
11 a market based evaluation, and the *Georgia-Pacific*  
12 factors with possibly further guidance from the Court,  
13 allow you that flexibility.

14 MR. ADKINSON: Marian?

15 MS. UNDERWEISER: Thank you. I'll respond to  
16 some extent to what was said before about looking at an  
17 objective standard like the one that IBM is proposing to  
18 use, the standard in *Quanta*, the economic value of the  
19 essential features of an invention.

20 The first thing that I want to say is we  
21 can't -- I don't think we can give up on some level of  
22 objectivity, some level of public notice, essentially  
23 because otherwise we don't promote the ability licensors  
24 and licensees to be able to efficiently agree in a  
25 licensing negotiation. B12..00w0 0,bstantl,- I think I

1 should explain a little bit better why the analysis in  
2 *Quanta* was relevant and what the Court was doing there  
3 because the Court was making a real-world economic  
4 decision.

5 The court was looking at a situation where a  
6 product was sold and asking the question of whether that  
7 product sale exhausted the patentee's rights. What does  
8 that mean? That means once the patent is exhausted, the  
9 patentee can't assert the patent anymore against that  
10 product, so against downstream buyers or users of the  
11 product, it can't be asserted anymore.

12 So the Court's making a decision about the scope  
13 of the patent right with respect to the product that's  
14 being sold and it has a complicated problem. It's a  
15 product that had certain characteristics that -- a  
16 microchip is sold. Does it exhaust a system covering a  
17 system that includes -- it's a component system but it  
18 includes standard and common items.

19 So the question the Court was answering was  
20 whether or not this sold product embodies the essential  
21 features of the invention, and it's a value question.  
22 Was the patentee fully compensated for that patent when  
23 that product was sold? That's the question, so if the  
24 patentee was fully compensated, that's a good way to see  
25 where the economic value of the invention is.

1           The other thing I should point out here is that  
2           the Court recognized in response to an argument by the  
3           patentee that this is a standard that is substantive.  
4           It's based on the type of invention. It's not just a  
5           one-dimensional analysis. When faced with an invention  
6           the patentee raised the issue of the Aro case, where  
7           the Court was evaluating an invention that was a  
8           combination invention you could call it, where all of  
9           the elements of the invention may have been in the prior  
10          art, and the inventiveness was in the combination.

11           And the Court said: Well, that's not going to be  
12          subject to the same analysis. There the invention is in  
13          the combination, I can't break that up, so the Court's  
14          recognizing that there are these different situations  
15          that can be encompassed by this, that the Court can make  
16          a substantive analysis of the invention, that the  
17          Court's going to have to do that if it's faced with this  
18          issue, and that the Court expects the marketplace to be  
19          able to cope with this and to be able to read the  
20          characteristics of a product and understand how it  
21          relates to what this invention is.

22           MS. MICHEL: Is your *Quanta* argument that even  
23          where the claim is to the whole computer, if the  
24          inventive feature of the patent, the reason the patent

1 have to worry about compensating -- coming up with  
2 damages based on the chip?

3 MS. UNDERWEISER: Yeah, sure. That's part of  
4 it. That's part of the concept here -- how do I focus  
5 on what's going on, and part of it is absolutely to mak T2-wof

1 invention, presuming willingness on each side, and it  
2 does mirror a lot of the considerations that take place  
3 in actual licensing negotiations, so I think it does  
4 provide the flexibility and the grounding and economic  
5 reality that one needs to do a proper damages analysis.

6 Further to that, the idea that the economic  
7 value is more objective I don't think is realistic, and  
8 we're still talking here about an inherently adversarial  
9 process by the time we get to litigation. We're not  
10 going to get the plaintiff and defendant sitting down  
11 agreeing on what the economic value is.

12 They're each going to hire experts. They're  
13 both going to come up with different evaluations of what  
14 the economic value is, and then it's going to be up to  
15 the jury or judge to decide, so which type of framework  
16 do we want that adversarial process to proceed under?  
17 One that has a host of factors that replicate real world  
18 licensing negotiations, including perhaps, if the  
19 defendant or the plaintiff, whichever side you're on,  
20 does not believe in running royalties, or do we have one  
21 that's been boiled down to a single factor?

22 I should point out that economic value is  
23 embodied in a number of the *Georgia-Pacific* factors. I  
24 think number 9 off the top of my head is the patented  
25 invention as compared to earlier or prior products and

1 what the added benefit is, so it's flexible enough to  
2 deal with that, but it doesn't constrain the analysis.

3

4 Now, I said at the outset that I was balanced,  
5 and I did find a point of agreement with my neighboring  
6 table here. I do think there is room for improvement on  
7 these industry comparables that David was talking about  
8 or the rules of thumb that we talked about this morning.

9 I think to the extent we're divorcing the  
10 damages analysis from the facts of a particular case and  
11 trying to rely on these rules of thumb or comparables or  
12 the like, I do think the courts could help judges and  
13 juries or the courts could help juries in that analysis.

14 I do, however, think that the tools are there.  
15 I think Rule 702 of the Federal Rules of Evidence, I  
16 think *Daubert* give the courts the tools to do that. I  
17 know there's been some legislative proposals on  
18 gatekeeper. I think legislation could help on the  
19 gatekeeping function, although the point was made this  
20 morning, with which I agree, legislation is a blunt  
21 instrument. Look at Section 284 of the damages laws  
22 right now, it's very general.

23 Intentionally we have decades of case law and  
24 decades of fact patterns that we need to tailor,  
25 decisions, common-law development of tort, and I think

1 that's the preferable way to do it. I don't think  
2 legislation can encompass all the different fact  
3 patterns you get with different industries, different  
4 business models of monetizing IP.

5 MR. ADKINSON: Well, let me press you and Jack  
6 on one item here. This morning, there was pretty broad  
7 agreement on the panel that the *Georgia-Pacific* factors  
8 were well as considerations, even for negotiations, but  
9 that throwing them before a jury was the problem, that  
10 it just enabled the jury -- could support any decision  
11 the jury would get to.

12 So that in the right hands they could be useful  
13 tools, but are they good litigation tools for a jury  
14 trial?

15 MR. RHODES: With all due respect to Judge  
16 Robinson, I do think there's a role for the Court as a  
17 gatekeeper in that process. I think that by way of  
18 careful analysis of motions in limine, really working  
19 through the factors perhaps at the charge conference,  
20 the *Georgia-Pacific* factors that go to the jury should  
21 mirror what the evidence was that was presented at  
22 trial.

23 So I do recognize there could be a problem if 15  
24 factors are presented to the jury. It's not clear which  
25 are really supported by the evidence, which aren't, and



1 I think that judges can help juries in that regard.

2 MR. ADKINSON: Jack, I'm going to give you -

3 MR. LASERSOHN: I completely agree with that.

4 NVCA has supported the gatekeeper -- expanding and  
5 redefining some of the gatekeeper functions as well, but  
6 the question is: What's the alternative? And it isn't  
7 at all obvious to me that an even more obscure  
8 alternative would actually help the jury more.

9 I mean, I have to be careful how I say this, but  
10 the problem in, for example a case, as I see it, of  
11 *Lucent* for example, is that juries are mathematically  
12 challenged. In granting a half a percent royalty, they  
13 in fact thought they were granting an incredibly tiny  
14 little royalty.

15 In other words, they got the principle right,  
16 which is that this is a tiny little component. There  
17 were lots of alternatives, et cetera. To them a half a  
18 percent was a little, teeny-tiny royalty, when in fact  
19 it should have been ten to the minus 18th, and that's  
20 not -- that's just beyond --that's a fundamental problem  
21 I think with the jury system.

22 But what the alternative is, which is to say  
23 economic value of the essential feature? I mean, I  
24 think the results would be even worse. You need to have  
25 more control over the juries, which *Georgia-Pacific*

1 attempts to do, say, Look, here are a check list of  
2 things you really should consider as opposed to one very  
3 broad and I think completely obscure formalistic  
4 approach.

5 MR. ADKINSON: This morning we had the question  
6 that a decimal point could mean the difference between a  
7 \$10 million award and \$100 million award.

8 MR. LASERSOHN: Good luck explaining that.

9 MR. ADKINSON: Taraneh?

10 MS. MAGHAME: Yes. Well, I just raised that.  
11 There were other people in front of me.

12 MR. SIMON: So just responding back. I mean,  
13 there are a couple things that people tend to forget  
14 about *Georgia-Pacific*. Judge Ron White from the  
15 Northern District of California was on a panel with me a  
16 few years back. I forget whether it was at the ABA or  
17 AIPLA and he just said, Look, this is one case,  
18 *Georgia-Pacific*, and it's dealing with a very specific  
19 product. Yet this is something that for whatever reason  
20 has come to be used, and I frankly don't find it very  
21 helpful.

22 I'm paraphrasing. I'm apologizing, but that was  
23 in essence what the judge said, in addition to which  
24 everybody loves to talk about how *Georgia-Pacific* has  
25 all these factors. Everybody forgets that the Second

1 Circuit actually reversed and vacated the District Court  
2 decision because it was a judge decision. In reaching  
3 that decision the district court forgot to allow the  
4 fact that the plaintiff -- or the defendant, the accused  
5 infringer, would in fact in any reasonable negotiation  
6 have ended up with a profit.

7 And the District Court had allocated all the  
8 profit to the plaintiff, and the Second Circuit said,  
9 That's wrong. The Federal Circuit by the way glances  
10 over that point too. They have repeatedly said that's  
11 not the guidepost for us.

12 So as a result we've moved away from what  
13 originally had some economic underpinning to something  
14 that now is in my view slanted the table very much in a  
15 compensation -- in the we must compensate factor.

16 And I think we need to really look at this is  
17 supposed to -- this is a business tort. It's about  
18 value. It's about economics. We heard I think all the  
19 economists say these don't really help us very much. We  
20 can use them to reach almost any result. That's a  
21 fundamental problem that I think we need to rethink what  
22 we're doing.

23 MR. ADKINSON: Phil, how about you?

24 MR. JOHNSON: We negotiate hundreds of licenses  
25 a year, and when we sit down to negotiate, we use

1 methodologies that are very much like the  
2 *Georgia-Pacific* factors. We don't call them  
3 *Georgia-Pacific* factors. Our business people are  
4 looking to what it would cost to pay. We both pay.

5           We pay hundreds of millions of dollars in  
6 licenses, license fees to others, and we collect quite a  
7 bit as well, but when we sit down, we are looking at  
8 those factors that are mentioned in *Georgia-Pacific*.

9           To us, the hypothetical negotiation is a good  
10 proxy for what business people do when they sit down and

1 his cases and explain why a lump sum royalty for a given  
2 feature is the appropriate approach and why he had  
3 alternatives at the time in the benchmark time period  
4 and in the hypothetical negotiation when presented with  
5 the feature which is the subject of the dispute. He  
6 should be able to say: Had we had a negotiation at that  
7 time, rather than pay you more than X as a lump sum, I  
8 would have done something else.

9 I think that's entirely appropriate, but if the  
10 other side wants to come in and say: No, you wouldn't  
11 because here's what your chairman said at an analyst  
12 meeting about how they would beg, borrow or steal in  
13 order to get this feature into your chip, they ought to  
14 be allowed to do that.

15 MR. ADKINSON: If it's a question of putting in  
16 what they view as comparable patents and the royalty rates  
17 associated with them, should there be any restrictions  
18 on that?

19 MR. JOHNSON: To me every invention is unique  
20 and every situation is unique so I have a lot of  
21 sympathy for people who are objecting to industry  
22 standard rates or rules of thumb or the like without an  
23 awful lot of foundation, and I do think that here's  
24 where the judges can be of assistance because they can  
25 hear the motions to exclude during the trial and make

1 either -- exclude it from evidence or give cautionary  
2 instructions or work on the jury instructions because  
3 they may have little or no weight in many situations,  
4 but in some situations where there's a regular and  
5 established royalty perhaps they do have weight, so it's  
6 a touchy area, but I have -- I have sympathy for that.

7 MS. MICHEL: Marian?

8 MS. UNDERWEISER: Thank you. One thing I want  
9 to clarify is that when I talk about using a standard  
10 like the economic value of the essential features, it's  
11 not meant to be the only factor that a court would  
12 consider, right, but it informs the analysis of damages.  
13 It doesn't dictate its complete valuation.

14 That said, I think we could all agree that what  
15 the inventor -- what the patentee should really be  
16 compensated for is the value that's added by the patent.  
17 That's really substantively the fair and the correct  
18 answer, and in looking at a substantive test, using that  
19 to focus the initial context of the inquiry, rather than  
20 saying that the most important thing about my damages  
21 inquiry is the hypothetical negotiation, by trying to  
22 refocus the court on what was invented, you're looking  
23 at a substantive question that should not be obscure to  
24 the court.

25 What could be less obscure or relevant than

- 1 asking what was the value or what did the inventor
- 2 really do? What is the substance of what was

1 for a couple reasons, one of which is it helps the jury.  
2 It helps the fact finder, but the other reason is that  
3 it provides a certain level of public notice.

4 If the judge actually rules on the record  
5 regarding what works or doesn't work in terms of  
6 admissibility of evidence, then again this is another  
7 piece of guidance for patentees and licensees, so you  
8 can say, okay, I understand. I understand what works  
9 and what doesn't work in this context so I think that  
10 would be a very helpful thing to encourage.

11 MR. ADKINSON: Gary?

12 MR. LOEB: I have three quick points hopefully.  
13 One, I agree with Dave on one thing that there's lots  
14 of instances where Genentech doesn't want to take  
15 running royalties either. One of the key ones of those  
16 is research tools where our actual product doesn't  
17 practice the patent, and that's the thing I mentioned in  
18 my opening comments about reach-through royalties and  
19 reach-through claims.

20 The ability to get -- reach the royalties is  
21 something that's now just sort of bubbling up the system  
22 with respect to biotech and pharma. Reach-through  
23 claims are an issue of what is patentable, and I think  
24 that that's -- I think that a little bit of what I hear  
25 from Marian and Dave is the tail wagging the dog with





1 that technology. They have to come up to speed on  
2 biotech in the course of a case, but patents are  
3 presumed to be valid, and they're looking at very  
4 specific issues of enablement and written description  
5 and obviousness in light of what was done previously,  
6 but they're not in a position to say: Oh, this was  
7 really a big leap over what was there before.

8 That's the reason why most patent examiners in  
9 the biotech field have Ph.D.s in the area, and they're  
10 flawed. The patent office is flawed, but to ask a judge  
11 or a jury to go down that path in addition to all the  
12 other things they have to do in evaluating a patent I  
13 think is really inviting mischief.

14 MR. ADKINSON: What do you suggest trying to  
15 figure out the value of the decoder? Is that similar to  
16 what you're talking about in trying to figure out the  
17 value of the specific invention?

18 MR. LOEB: It was the decoder -- I'm not  
19 familiar with the patent in the *Lucent* case, but it was  
20 a patent involving a decoder.

21 MR. SIMON: It was a patent involving a decoder  
22 of audio information.

23 MR. LOEB: Right, so you would look at a royalty  
24 base of what does the decoder sell for, and then maybe  
25 you get .5 percent of the value of the decoder. I mean,

1 and maybe the jury should never see the bigger sales,  
2 and unfortunately that's maybe a *Daubert* issue, which we  
3 don't necessarily want to deal with, or maybe it's just  
4 an evidence 702 issue or whatever it is, but I don't  
5 think that putting the judges in the position of trying  
6 to reevaluate how much of a leap this invention is is a  
7 good use of judicial resources.

8 MS. MICHEL: How do you identify the economic  
9 value of the invention without thinking about how  
10 significant the invention was? Gary, do you understand  
11 my question? If part of the goal here is to decide what  
12 the economic value of the invention is and to  
13 compensate, doesn't it matter whether this is a minor  
14 advance with several alternatives or a major advance  
15 with no alternatives? No, why? Phil? No, I went to  
16 Gary? No.

17 MR. JOHNSON: Because some of the greatest  
18 technological advances are commercially valueless and  
19 some of the most valuable from an economic standpoint  
20 advances may not rise to the -- obviously to be  
21 patentable, they have to meet the patentability  
22 standards, but they may not be valuable in comparison to  
23 the technical advance that they represent because think  
24 about I don't know, gene splicing, when it happened it  
25 was scientifically fabulous and commercially valueless

1 for a long, long time.

2 Other things are very small advances that put  
3 some technology or a product over the top to make them  
4 fabulously valuable.

5 MS. MICHEL: That would be an economically  
6 valuable patent then?

7 MR. JOHNSON: Yeah.

8 MS. MICHEL: The gene slicing, an example would  
9 be helpful here to understand how you could have a very  
10 economically valuable patent that did not make a  
11 significant contribution as compared to the prior art.

12 The gene slicing example, why is that -- why is  
13 that not commercially valuable? Is it because there's  
14 not infringement? Is it because there's not a product  
15 to protect the infringement?

16 MR. JOHNSON: Well, at the time it was invented,  
17 it wasn't commercially valuable. It took years before  
18 other things happened, further development, and then it  
19 did at that time become commercially valuable, but it  
20 was not at the time it was invented as opposed to --  
21 think of my favorite, which is -- I don't know if it's  
22 patented or not, but in hotels, I spend a lot of times  
23 in hotels, is the curved shower curtain rod, and it's  
24 great, and it's in every shower apparently in every  
25 hotel in America.

1           MR. LASERSOHN: He must go to different hotels  
2 than I do.

3           MR. JOHNSON: Technically perhaps not the  
4 biggest leap, but commercially, I'm assuming very  
5 commercially successful. Now, every invention to be  
6 patentable has to still at some level meet the inventive  
7 standards.

8           MS. MICHEL: Let's go back to the shower curtain  
9 idea there. Are you suggesting because it's  
10 commercially successful there should be very high  
11 damages then, even though it's not technically much of  
12 an advance?

13           MR. JOHNSON: Well, whether they're high damages  
14 or not would depend on all the *Georgia-Pacific* factors,  
15 among them whether the infringer was selling a lot of  
16 them and when they decided to do it, and once every  
17 hotel room in the country already has one --

18           MS. MICHEL: It's not cost.

19           MR. JOHNSON: Well --

20           MS. MICHEL: Or not capturing different costs.

21           MR. JOHNSON: People may not pay much for one  
22 now that every hotel already has one. There are all  
23 kinds of factors, and so it would depend on the  
24 circumstances of the case.

25           You can't just say: Well, because it's popular,

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1 and the other thing, inventions change in value a huge  
2 amount during their lifetime. Like in the gene  
3 splicing, a classic area is in AIDS drugs. You get a  
4 new protease inhibitor that works for highly experienced  
5 patients who are running out of treatments.

6 It's very valuable, but then after awhile, after  
7 it's used and AIDS develops a resistance to it, it  
8 becomes less and less valuable, and then the next new  
9 thing comes along, and that's what's valuable.

10 So you have to value the invention, and we  
11 generally value the invention at the time the  
12 infringement begins, and eclipsing technology is one way  
13 that most patents and most inventions lose value because  
14 of the next generation of technology comes in, and then  
15 nobody wants the last one.

16 MR. ADKINSON: Keith, you've been very patient.  
17 Thanks.

18 MR. AGISIM: Sitting next to Phil you have to  
19 be.

20 MR. JOHNSON: This is about our 25th panel  
21 together.

22 MR. AGISIM: Listening to everything that people  
23 are talking about I think it does -- *Georgia-Pacific* may  
24 play a role in figuring this out, but ultimately I think  
25 it comes back to you need to create an objective

1 standard. People have talked about wanting enhanced  
2 gatekeeping. Well, if you want enhanced gatekeeping,  
3 gatekeeping against what?

4 It has to be some sort of objective standard,  
5 and I think we all agreed earlier in this conversation  
6 that damage is compensatory and so what are you  
7 compensating for? You're compensating for the economic  
8 value of the invention, and depending on when the  
9 infringement is, that value can change.

10 It's like people's houses now. People's  
11 houses -- their values change a lot. The beauty of the  
12 house hasn't changed but the value of that house has.  
13 The economic value of that house has changed over time,  
14 and so it's the same thing here. You need to provide an  
15 objective standard, which I think would be the economic  
16 value.

17 Then the question is: Of what? I think we're  
18 talking about *Quanta* and sort of the essential features,  
19 of avoiding the problem you would raise, and you raised  
20 this morning of the computer comprising, and so I think  
21 if you have the objective standard, you're able to  
22 implement a lot of the gatekeeping that people have  
23 talked about, and I think when -- from a gatekeeping  
24 perspective, there's so much they can do pretrial, and  
25 that's important.

1           But I think there's also sort of a post-trial  
2 component. We saw this morning on some of the  
3 statistics where the awards from judges were  
4 substantially lower than the awards from juries. We  
5 assume that the judges are the ones generally getting it  
6 right that tells us that there's some discrepancy when  
7 they're hearing the same evidence. There would be a  
8 discrepancy in what they come out with.

9           I think the problem is now there are no  
10 mechanisms, there's no standards upon which -- the  
11 standards are too high so judges can't correct those  
12 issues when they do come up, and so I think some of the  
13 gatekeeping functions need to address that.

14           A potential solution of that area is to create  
15 more of a -- sort of more of a record to help the  
16 district court judge post-trial and on appeal, sort of  
17 we're all back in school, show your work. It would be  
18 great if you had the jury sort of show their work around  
19 damages, how do they arrive at it, how do they figure it  
20 out?

21           MR. ADKINSON: Thanks, Keith. Taraneh?

22           MS. MAGHAME: First of all, I think it's -- I  
23 don't know how many people here know this. I think it's  
24 worth pointing out that this huge judgment that we keep  
25 talking about, the 1.5 billion dollar, was actually the



1 one that was actually set aside, so I hate harping on  
2 something the judge itself found was not supported by  
3 the evidence and immediately set the judgment aside.

4 So with that said, there was also a suggestion  
5 that possibly because that was -- the judgment was in  
6 error and it was based on a royalty base that was too  
7 high because it was the whole price of the computer,  
8 maybe we should consider perhaps the selling price of  
9 the decoder.

10 That reminded me of something that was said this  
11 morning about the invoice price, and I think that's a  
12 totally wrong direction to be headed in as well. There  
13 is no correlation between an invoice price or a selling  
14 price of an item and what that economic value would be.  
15 The value of something that is sold at the time of sale  
16 could be very different from the value that the  
17 seller -- that the buyer gets from it by combining it  
18 with a product.

19 MS. MICHEL: Just I want to clarify that. They  
20 were talking about what the base side would be, not what  
21 the whole economic value would be, and why can't you get  
22 the economic value you want out of the base by adjusting  
23 your royalty rate?

24 Is it fair to just point to -- to say that  
25 that's not the economic value there in the decoder if



1           You could -- and we've talked about that I know  
2           at length in the patent reform debate and made a lot of  
3           proposals as to how judges can determine what evidence  
4           has been presented and what factors may be supported by  
5           that evidence and sent those factors to the jury.  
6           That's a possibility.

7           But I don't see that any of this can be labeled  
8           objective per se, because you still have to have the  
9           flexibility, and the flexibility is part of the  
10          subjectivity of this determination to start with.

11          MR. ADKINSON: Gary?

12          MR. LOEB: I think actually will agree with Dave  
13          on the point of the decoder, and maybe he wouldn't go as  
14          far as I would go, but on the issue of not looking at  
15          the entire value of the product all the time, I think  
16          that there is some middle line with respect to the  
17          royalty base, and I'll go back to the curved shower  
18          curtain example because maybe that's one that we can all  
19          understand.

20          Do you get a royalty on the cost of renting out  
21          the hotel room for having the curved shower because you  
22          claim -- because some clever patent attorney claims a  
23          hotel room that includes a curved shower rod in their  
24          hotel? And in that type of problem, should the judge  
25          have the ability, even if the claim ultimately says the

1 hotel room that includes this curved shower rod --  
2 should the judge have the ability to say, well, really  
3 the invention here relates to the curved shower rod and  
4 your royalty base that should go to the jury is the cost  
5 of the rod, not the cost of the hotel room.

6 And I think that the judges should potentially  
7 have flexibility on that standard. I don't know that  
8 there's a lot of situations where that applies, but  
9 there's certainly some situations where that applies and  
10 you can sort of see that, but it's much more effective  
11 to come at it and much more understandable to come at it  
12 from that way instead of trying to grade the economic  
13 value of particular inventions and to say that some are  
14 class A or class B from an economic value perspective.

15 MR. ADKINSON: Bryan?

16 MR. LORD: Two points. One, the question was  
17 asked earlier how do you know if there's value. The  
18 very simple answer is: Was there infringement? If the  
19 technology has been used, it's I think a rational  
20 assumption to conclude that there has been value  
21 derived.

22 Most rational organizations do not add elements  
23 to their technology offerings because they add no value.  
24 Most add them because there is some value, so I think we  
25 can sort of stipulate to the fact that, as my comments

1 were earlier -- if in fact we found infringement we  
2 should be able to conclude that some value

3 that is derived by that, no matter how -- we can argue

4 about significance, and is significance, and is significance



1           I'll point out a situation in the apportionment  
2 debate. If you recall, some folks talked about, imagine  
3 if there was a situation if someone had, I don't know,  
4 like a delay switch on a windshield wiper. Would we  
5 really consider that to be something where you should  
6 actually get royalties on the end value of the car? We  
7 talked about apportionment being a good example on how  
8 to solve the delay feature on the windshield wiper.

9           And lo and behold, whatever it was 18, 24  
10 months, a movie comes out about the delay wiper on  
11 windshield wipers, genius, right? And it talked about  
12 this inventor who came up with the delayed feature on  
13 the windshield wiper and how all the car companies were  
14 ignoring the inventor and clamoring for a way to put  
15 this windshield wiper into their car to drive the sales

1 on a windshield wiper, but there was certainly a day  
2 where that inventor should have been entitled to have a  
3 negotiation with Ford or with Chrysler or GM and say,  
4 here's my invention, would you like to have the  
5 competitive advantage of adding it to your product. And  
6 I think that's what we can't lose sight of.

7 MR. LASERSOHN: So I would like really to agree  
8 strongly with what Bryan just said and expand on it a  
9 little bit because in fact that is how innovation  
10 occurs. It occurs in this very incremental way, tiny  
11 little improvements where the goal isn't sort of to get  
12 paid some abstract value for how many hours it took to  
13 make the invention, but rather to get the economic  
14 value.

15 It's interesting that every single case that  
16 we've just talked about here can be looked at both ways,  
17 so let's go back to the shower curtain example, and the  
18 point was: Well, what's the value of that? I could buy  
19 it from somebody for X price here if somebody offers it  
20 cheaper. Well, it is possible that people actually  
21 changed which hotel they would stay at on the basis of  
22 did it have the shower curtain or not.

23 Now, I have no idea if that's true, but that  
24 is -- that is one of the ways to think about economic  
25 value, which is actually the way that most innovators



1 think about it. They are not looking to get paid a  
2 tenth of a billionth percent of a royalty on  
3 compensating them for their time. They're looking to  
4 capture the economic value that the invention has on an  
5 entire marketplace.

6 Now, Phil is probably too modest to use this as  
7 an example because it's a Johnson & Johnson example, but  
8 in the case of coronary stents, the addition of a  
9 molecule to the drug coating the stent -- the addition  
10 of a molecule, a change to a molecule to the drug  
11 coating on a stent could affect and did affect the  
12 likelihood of that stent becoming thrombotic or non-  
13 thrombotic, and that complication was only 1 percent, so  
14 you're talking about affecting something in the market  
15 that maybe only had maybe a 1 percent change, but  
16 basically it was a commoditized market.

17 All the other stents were roughly the same. The  
18 introduction of an invention like that could shift -- where  
19 the drug coating or drug itself cost virtually nothing  
20 in terms of -- could shift a billion dollars, a billion  
21 dollars of profit to the company who licensed it, so it  
22 only becomes a question of: Who is entitled to that  
23 profit?

24 A company that choose to do it and infringed and  
25 made the extra billion or the inventor? That's really

1 what it comes down to, and in that case I would argue  
2 the inventor's entitled to that, not the infringer. If  
3 it shifted the entire market, the inventor is entitled  
4 to that because his invention caused that to happen.

5 Now, it gets vastly more complicated because you  
6 would say: Well, you have to have a stent business, and  
7 you have to have licenses for stents and all sorts of  
8 other things to do it, which gets into this hypothetical  
9 negotiation, which is: Well, you're right, I couldn't get  
10 the whole billion dollars, but look at how much this one  
11 little tiny change meant in terms of economic value,  
12 let's negotiate.

13 I don't think you can simplify it beyond that.  
14 Every example that you could come up with, including the  
15 MP3 player in Microsoft Windows, had the potential to  
16 become that kind of effect. Would p stee4wuuyand potential to

1 MS. UNDERWEISER: Thank you, yes. I think we  
2 have to distinguish here that it is not a one-to-one  
3 linear relationship between how inventive is the  
4 invention versus how much economic value it has. I  
5 think it's clearly true that an invention will have  
6 value that depends on its context, how it's used, how  
7 it's implemented.

8 So, for example, you can have a significant  
9 technological invention that is way before its time and  
10 is not used until after the patent expires. It ends up  
11 garnering for the patentee nothing, so the point is you  
12 do need to distinguish between those two. They're not  
13 going to necessarily correlate with each other, but that  
14 doesn't mean that you can't discard the question of:  
15 Well, what was the invention?

16 And once you figure out what it was, you can ask  
17 these other questions: Well, is it the basis for market  
18 demand, for a larger product? That's when those  
19 questions became relevant, but in order to ground the  
20 question, you have to start with trying to determine  
21 what really is the invention here.

22 MR. ADKINSON: Phil?

23 MR. JOHNSON: Well, what the invention is is  
24 what the patenting process is all about. We spend an  
25 awful lot of time in the patent office arguing over the

1 appropriate claim to be the definition of the invention,  
2 and the invention could be an improved hotel room, and  
3 it could be that -- and I doubt people are booking  
4 because of the shower, but it could be that the data  
5 would show that people have a more pleasant experience  
6 in the hotel, and that hotels find that if they install  
7 these shower curtains, that they have a lower vacancy  
8 rate.

9 I would guess -- I don't know what they're sold  
10 for. Maybe it's quite a lot, but I know that whatever  
11 they're sold for, the inventor is sharing the value of  
12 the shower curtain with the hotel chain. If they  
13 weren't, the hotel chain wouldn't be installing them in  
14 all these rooms. That's as with all -- as with all  
15 inventions, the inventor who prices his invention to try  
16 to garner 100 percent of the value, if it's a billion  
17 dollars, and keep it all for himself has an invention  
18 that is never adopted. You must share it down the road.

19 I think that a far better way than to try to  
20 dissect a claimed invention into its sub-parts is to  
21 compare it with its closest non-infringing alternate,  
22 which Gail suggested this morning, and I would agree.  
23 In our hotel room case it would be the hotel room with a  
24 straight shower curtain or who knows, some other type of  
25 shower curtain if that was closer, that was non-



1 pretend that the Court opined on the value of inventions  
2 is simply not what the case says.

3 MR. ADKINSON: David?

4 MR. SIMON: So a couple points. First of all, I  
5 want to be clear that I agree with both Jack and Phil  
6 that sometimes it would -- could be viewed as Oh, gee,  
7 you change three or four molecules or you changed three  
8 or four little things, can make a significant difference  
9 in the value of what is patented.

10 However, I do think trying to use the artificial  
11 constructs, since the United States does not require a  
12 Jepson format claim of trying to put everything that's  
13 in the prior art up in the preamble and only permitting  
14 in the body of the claim what is new and non-obvious, you  
15 really do have a problem.

16 There are articles written saying write claims  
17 to cover systems because you can claim a bigger royalty  
18 base. That makes no economic sense to me, that the  
19 patent attorney's decision on how I write the claim is  
20 what's going to determine what the royalty base is. I  
21 just think that's wrong.

22 And I would also respectfully disagree with Bill



1 to determine what's appropriate for damages and the  
2 economic value of an invention. It's that by focusing  
3 on the substance of what was invented, focusing on the  
4 essential features, I think that informs using many of  
5 these other tools, so that's how you can tell the  
6 difference. That's how you can figure what the closest  
7 non-infringing alternative really is.

8 MR. ADKINSON: Kevin?

9 MR. RHODES: I disagree with the notion that the  
10 invention is something different than what's claimed. I  
11 think the claims define the invention. That is a  
12 question of claiming. If there is a perceived problem  
13 in how claims are drafted, that's a different question  
1T1.ds.1.ds.1.h13 in how claims are drafted, that's a different ques



1 calculation.

2 As to *Quanta*, I mean, the essential features of  
3 the invention sound a lot like prior art subtraction to  
4 me cloaked in a Supreme Court case, so now it has the  
5 premise of having more validity, but I echo what Phil  
6 was saying. *Quanta* had nothing to do with actually  
7 ascribing value to an invention. It did have to do with  
8 double-dipping.

9 Whatever that value is, where in the value chain  
10 does the patentee exhaust that value? It didn't talk  
11 about what the invention is worth, much less dissecting  
12 the invention and what are particular elements of that  
13 invention worth. And I think the idea that we would get  
14 better, more objective damages law by going through the  
15 entire liability phase of the trial, then we come to  
16 damages, and we essentially re-create validity to  
17 determine what is the essential feature or the novel  
18 aspect of the invention.

19 And then of course since that analysis leads to  
20 zero values for combination claims, so the Post-it note  
21 for example is worth nothing . The Post-it note  
22 adhesive was old, it had been separately patented.  
23 Paper of course was not new. You get no value.

24 But the Court was careful to distinguish *Aro*  
25 and say, this doesn't apply in the sense of combination

1 claims. Now, we have another layer of complexity. Is  
2 it a combination claims? Well, most claims are. Maybe  
3 this is. Maybe this isn't, so the idea that we're going  
4 to get to a better end state comparing the law to date  
5 to where it will be with this more objective standard I  
6 think is a fallacy.

7 I don't think it's going to add any objectivity.  
8 I don't think it's going to simplify, and I don't think  
9 it's going to have any effect other than to lower  
10 damages awards, which may be the intended effect.

11 MR. ADKINSON: Thank you very much, and I guess  
12 I now -- the phrase layers of complexity resonates. We  
13 really appreciate all of your thoughts.

14 I would like to have you go around and give one  
15 last set of thoughts, anything you're thinking about,  
16 the extent to which there's a problem, and if so, what  
17 you think might be done it or whatever other thoughts  
18 you might have.

19 MS. MICHEL: Last chance for comments. We're  
20 wrapping up.

21 MR. AGISIM: We did talk earlier, in our  
22 industry, there's a clear problem. I think it's well  
23 articulated, well documented.

24 In terms of the solution, I think you need an  
25 objective standard. I think it should be based on the

1 economic value. If damages are not based on the  
2 economic value, then there is something wrong. What are  
3 they being based on? So I'm not sure where the -- why  
4 there's so much fight over that, but I think regardless  
5 of what the standard is, you really need to have  
6 gatekeeping in a significant way that can deal with it  
7 both pretrial and post-trial.

8 MR. JOHNSON: One of the problems with non-  
9 practicing entities from my conversations with my  
10 counterpart in the tech industry is that they are being  
11 held up, if you will, by the cost of the transaction  
12 involved in litigation, that is the 3 to \$5 million, and  
13 they are being coerced to settle without regard to the  
14 merits of the claim.

15 Whatever we do, we should do something to  
16 discourage people from bringing frivolous actions and  
17 taking advantage of the fact that uniquely, as many have  
18 pointed out, in this area frivolous cases can impose  
19 such a burden on the defendant that they can extract  
20 large amounts of money from them.

21 I don't know if loser pays is the right way or  
22 what else is involved, but something needs to be done to  
23 stop people from abusing the system at that level.

24 MR. LASERSOHN: I'll make two quick points. The  
25 first is that I don't think anybody disagrees that

1 economic value is the core idea that we are searching  
2 for, but that is very different than economic value of  
3 an essential feature or economic value of the invention  
4 over the -- contribution over the prior art. That is

1 example, are worried about.

2 If there are cases where there is -- the  
3 contribution of the invention is truly insignificant,  
4 has really insignificant economic value, doesn't shift  
5 the marketplace, it doesn't save a lot of money, it's  
6 just a different font for the letter F in Microsoft  
7 Word, that could be cut out as a special case. That's  
8 the way to deal with what is perceived to be some sort  
9 of black swan type outcomes here, which we would in fact  
10 be happy to support.

11 MR. LOEB: I think one of the interesting issues  
12 raised in some of the positions of Dave and Marian is in  
13 some ways we're incentivizing innovation for really  
14 expensive products if we're allowing these, and we're  
15 not incentivizing innovation for things like forks where  
16 you can't claim something that's really expensive in  
17 connection with your innovation.

18 So I think that's sort of a fundamental policy  
19 decision that: Is there some sort of bad situation that  
20 arises from that. And that's where I sort of sympathize  
21 with these patent claims that try to claim more than  
22 what they should with respect to the invention, but I do  
23 think that coming at it from a damages standpoint is  
24 very wrong-headed.

25 I think that we haven't actually seen a whole

1 lot of really bad damages cases, and most of those that  
2 we have seen have either not been upheld or can often be  
3 explained through specific litigation tactical  
4 decisions, so I think there's actually surprisingly  
5 few.

6 I think actually one of the reasons for that is  
7 that thankfully patent cases are in federal court, and I  
8 think the quality of justice you get in Federal Circuit  
9 is maybe a little bit higher than what you get in state  
10 court, so we don't see the type of runaway case that  
11 you see in products liability or other situations like  
12 that.

13 So I do think that the way to come at this is  
14 really more from a patent reform system. Are there  
15 things to the patent system? Do we need to open up post  
16 grant opposition proceedings so that patents that seem  
17 really obvious can be challenged early on, so they can't  
18 be held up against companies that might practice them, or

1 influential these days economist, and he talked about  
2 the fact that innovation policy is the single most  
3 important policy matter that our country faces these  
4 days.

5           What he did was he contrasted between two  
6 different circumstances. One where there's a decreasing  
7 returns to scale type of regime, it's sort of zero sum,  
8 winners, losers, and frankly it echoes a lot of this  
9 debate here: Who should win, who should lose, what  
10 should be the spoils?

11           That's fine, we can have that discussion, but  
12 Romer really talks about this increasing return to scale  
13 regime. It's part of his emerging economics view, and  
14 he distinguishes the old regime with the new, and the  
15 difference is ideas, and he talks about how important  
16 ideas are in the paradigm of the old, which is  
17 decreasing returns to scale, and ideas which are  
18 increasing returns to scale.

19           Those ideas he talks about fundamentally need to  
20 be protected for all the reasons that Jack, and I hope I,  
21 have talked about. You need to encourage people to take  
22 risks. You need to encourage entrepreneurs to take  
23 risks with their time and venture capitalists take risks  
24 with their money, and the difference between whether we  
25 protect ideas or decrease the protection for ideas is





1 establish IP laws such that they will promote  
2 competition, and they will help us with our economy?

3 And I think that's what we're all talking about  
4 here is how we can do this so as to not create a bad  
5 situation for us, not to damage ourselves?

6 Now, a lot of issues came up over the last few  
7 years that people said needed to be dealt with, and if  
8 you look at the history of what the courts have done  
9 over these years, they've dealt with just about every  
10 one of those issues. We had issues about injunctions.  
11 *eBay* took care of that.

12 We had validity issues with patents. Are there  
13 bad patents out there? Then we got *KSR* with the non-  
14 obviousness standard being strengthened. Exhaustion,  
15 *Quanta* recently came down dealing with that. We've got  
16 willfulness and *Seagate*. Venue issue, *MedImmune* to  
17 some extent has taken care of that, so the Courts have  
18 really been able to deal with these issues.

19 At this point to step in and say, we need to  
20 legislative reform damages standard I think is  
21 unnecessary, particularly since as we've discussed  
22 several times here, the data is not there to support the  
23 statement that there is a problem.

24 Yes, there are outliers. Courts have dealt with  
25 some of them. There's outliers in every area of the

1 law, but we could seriously damage ourselves by coming  
2 in at this point and saying we need legislation to fix a  
3 problem that really doesn't exist and why don't we let  
4 the system fix itself the way it has with some of these  
5 other cases, and let's focus on the patent quality.

6 I mean, that's what this all boils down to.  
7 When we're talking about NPEs, we're not talking about  
8 companies -- at least I don't think we're talking about  
9 companies like Tessera who spent hundreds of millions of  
10 dollars developing technology that is valuable to the  
11 industry.

12 We're talking about bad patents. That's what I  
13 always understood it to mean, whether you call it troll,  
14 NPE, whatever you call. It we're talking patents that  
15 should have never been issued, so let's focus on issuing  
16 the quality patents. Let's focus on making the PTO  
17 function in a way that allows us to do that.

18 MR. RHODES: I think the other panelists have  
19 made my points very well, so thanks again, Bill and  
20 Suzanne.

21 MR. SIMON: I promised in an effort to get  
22 everybody out of here that I would pair myself with  
23 Kevin, so I will pass on.

24 MS. MICHEL: Good enough.

25 MS. UNDERWEISER: Well, I'll be brief. I think



1           As I mentioned this morning, we will continue to  
2 accept comments through May 15. I believe the web site  
3 was down last week for submitting comments. If anyone  
4 tried it, it's back up, and also feel free to contact  
5 us. We would love to hear from you. Thank you.

6           (Applause.)

7           (Whereupon, at 5:10 p.m. the workshop was  
8 adjourned.)

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