

Diligence where it's due

The landscape for patent licensing and litigation is changing and, says **Terry Ludlow**, meticulous preparation is key

Recent judicial decisions and changes in legislation highlight some notable trends in patent licensing, enforcement and litigation.

This article looks at some of the trends we believe will become more relevant in the future. Major trends that will gain influence in 2016 and beyond include an increasing emphasis on preparation. For example, cases will be much more fully developed before potential licensees are contacted or litigations are filed.

Cases will also be bigger as multiple patents in multiple venues are required for successful licensing. With multinational licensing and litigation, patent owners will be able to go to wherever they can leverage local legal environment and market forces to extract better licensing results. There will also be a decline in the threat posed by non-practising entities (NPEs) and an ascent of 'innovator versus implementer' as the central struggle in patent licensing.

An increasing emphasis on preparation

Cases will be much more fully developed before potential licensees are contacted or litigations are filed. Plaintiffs must do much more extensive due diligence and prepare much more thoroughly than in the past. Technology patent licensing in 2016 requires patent owners to document thoroughly a wide range of infringing products before starting any kind of negotiation. A portfolio must be documented to show comprehensive evidence of use (EoU) on multiple patents. Convincing EoU is a requirement prompted by the *Alice* decision on patent-eligible subject matter, the *Octane Fitness* decision on fee shifting, and the new complaint requirements initiated on 1 December 2015.

Alice changes the view of patent-eligible subject matter. Post-*Alice* patents often require more complex patent claims that are firmly rooted in hardware or some physical implementation that provides the 'something extra' that is the second prong of the two-part eligibility test and that distinguishes the invention from an abstract idea.

Following the decision in *Octane Fitness* it is clear that claims should not be filed unless all the homework has been done. Infringement needs to be well established before filing or litigants will risk having their case judged as exceptionally frivolous and may be on the hook for their opponent's legal costs.

Under the new pleading requirements, the departure of form 18 means that complaints will need more detail and specificity with regard to the infringement allegations. This is clear from the stipulation that complaints "require facts sufficient to support the allegations".

Bigger cases

Patent values have continued to trend downwards. High quality, valuable patents in litigation are rewarded with smaller and declining damages;

damages and jury awards have been on a downward trend for the past decade. Despite some notable recent jury awards, such as \$234m in *WARF v Apple* in October 2015 and \$626m in *Virnetx v Apple* in February 2016, the overall trend is still down. PwC's annual patent litigation study tracks a dramatic decrease in median jury awards since 2005, with the 2000 to 2004 median award standing at \$7.6m and the 2010 to 2014 number standing at \$2.9m.

Some relief is on the horizon, though, with some optimism that patent values may increase emerging from recent news. For example, the US Supreme Court is scheduled to hear new cases this year on willful infringement (*Stryker v Zimmer* and *Halo v Pulse*) that are expected to bring back a threat of triple damages in more cases where willful infringement can be argued. A case on broadest reasonable interpretation at the Patent Trial and Appeal Board (PTAB) – *Cuozzo Speed Technologies* – may also bring PTAB claim interpretation standards into alignment with district courts'.

Courts have reduced the influence of exemplary patents. Almost no possibility of an injunction outside of the International Trade Commission means little licensing leverage from a single infringement win. Multiple patents are required to survive the increasingly common *inter partes* review (IPR) petition that is now a normal part of technology patent litigation in the US. The concept of efficient infringement has emerged in the literature. It captures effectively the defendants' mindset towards small-scale lawsuits – just fight it out and you have a good probability of killing enough patents in IPR actions or in court to dismiss the suit entirely or in the worst case end up with a reduced payment even when legal fees are included. Small-scale litigations such as the typical NPE suit, an inventor's suit or even an SME with a limited patent portfolio have been made cost-prohibitive.

Multinational licensing and litigation

The US is still the most influential legal environment for technology patent licensing and US law and US patents will continue to be the most influential element in any licensing deal. However, as the US is perceived to be increasingly hostile to patent owners' rights, foreign markets and legal systems are gaining influence and must be considered when looking at the future of technology licensing.

Patent owners will go to wherever they can leverage the local legal environment and market forces to extract better licensing results. There have been a few examples of patent owners filing a blitz of lawsuits citing different patents in different venues. For example, the recent Ericsson patent licence renewal with Apple turned to litigation in January 2015, with an Apple declaratory judgment filed in California inviting Ericsson responses in California, and seven cases in Texas citing

41 different patents. This expanded to two actions in the ITC then went to Europe, with cases filed in the UK, Germany and The Netherlands, before settling in December. This 'shock and awe' strategy is intended to convince a defendant that there is overwhelming evidence of infringement and that a licence is inevitable. Multinational cases by well-funded innovators with large worldwide portfolios are effective at leveraging settlements and will become more prevalent.

In Europe we have experienced the beginnings of a move by multinational companies to use the perceived patent-friendly courts of Germany in particular and, to a lesser extent, the UK. Large multinationals such as Nokia, Philips and Huawei (*Huawei v ZTE*) and also well-funded licensing companies such as Dolby, Marathon and Unwired Planet are already effectively using European courts as an alternate enforcement forum. More will follow as the speed and low cost of a reliable and patent-friendly jurisdiction becomes better appreciated. The upcoming unitary patent and Unified Patent Court will accelerate this trend in future years – potentially becoming a major nexus point in international patent enforcement.

The decline of the NPE threat and the ascent of the innovator versus the implementer as the central struggle

NPE activity will significantly diminish because small lawsuits lose money. The median damages award of \$2.9m may, with careful cost-aware case management, cover the legal costs to take a technology patent litigation to trial.

The 10 top filers of litigations in US last year filed 637 cases. All 10 plaintiffs are small patent portfolio NPEs filing on the same one or occasionally two patents against 50 or more defendants. Settlements on single patents are getting smaller and harder to achieve. The cost of an IPR (\$150,000 - \$600,000) is the new perceived ceiling for early settlements.

Many defendants refuse to settle early on the grounds that they will be perceived as negotiating with trolls and will encourage future litigation. More and more, efficient infringers will file IPRs requiring small patent owners to spend the time, money and effort to defend their patent at the PTAB. The small NPE business model crashes without early settlements or large damages awards. Compound that with the risk of fee shifting and investors will increasingly avoid making new investments in small portfolios.

The vast majority of publicly traded patent assertion entities (PAE, aka NPE) have experienced significant losses in share value in 2015. RPX's Public PAE report cites a 16.2% loss in share value for publicly traded PAEs in the year to 30 September 2015. Large cap PAEs fare better with only a 7.7% drop, but small cap PAEs have suffered a 52.4% drop in the same period. The same report shows that 16 out of 22 tracked NPEs lost money in that time period. Privately held NPEs are likely in even worse shape.

NPE activity will continue at the top end. Well-capitalised companies with large portfolios of valuable patents can afford to launch long term, even multinational, programmes and can still achieve reasonable returns even after legal costs are paid. It is nonetheless bad times for even the top-end NPE.

Innovators versus implementers

A new central battle in the patent world has emerged – that of innovative companies versus implementing companies. Innovative companies invest heavily in R&D and patents, have active patent-licensing programmes and tend to support stronger patent rights. Examples include large operating companies like Qualcomm, Ericsson and Philips and research intensive NPEs such as Rambus and Tessera. It is interesting to note that the interests of large innovative operating

companies and the interests of large PAEs are becoming more closely aligned as part of this debate.

Implementer companies are companies with their primary expertise in developing, building, marketing and selling products that see patents and patent licenses as expenses that should be minimised or eliminated. Companies such as Apple, Google, Cisco, Microsoft, Sony, Canon and Hewlett Packard have supported lobbying efforts for US patent reform bills that would further limit small entities' ability to enforce patent rights.

We have seen the debate between innovators and implementers already in the US, where the opposing views stalled the path of patent reform bills in Congress and open dispute has poisoned the debate around standard-essential patent (SEPs) policies at standard setting organisations such as the Institute of Electrical and Electronics Engineers Standards Association (IEEE-SA).

Worldwide, the debate has used antitrust laws and competition authorities to debate and often limit the rights of IP and patent owners. For example, Qualcomm has faced antitrust suits in multiple jurisdictions including China, Korea and the European Union all aimed at limiting the ability of Qualcomm to assert their patent rights and perhaps to enhance the local competitive companies' ability to obtain a more advantageous and cheaper licence. Courts have spent significant time looking at SEPs and ultimately reducing the value of what was once the gold standard of technology patents. Fair, reasonable and non-discriminatory obligations now encumber SEPs and reduce their value. Some standard-setting bodies, notably the IEEE-SA have added their voice to the debate, prompting a split along innovator/implementer lines, with innovative companies such as Qualcomm and Ericsson threatening to pull out.

Summary

Patent licensing has always been a global business, but the technology industry has always used US patents and courts as the central focus. This focus will continue to erode as owners of large high-quality, high-value patents seek to enforce their patent rights in whatever forums offer a tactical advantage. These licensing efforts will require meticulous preparation commensurate with the business stakes and what is demanded by foreign courts as well as to comply with new US practices. The NPE business model must evolve with the changing environment into something resembling the licensing programmes of their successful innovative operating company counterparts. And the real excitement may well be the bigger battle between the implementing companies and the innovative companies on the world stage of multinational courtroom battles and government antitrust agencies.

It is indeed interesting times in the technology patent licensing world.

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