

## NUTS &amp; BOLTS

# Patent Infringement Damage Awards: A Business Opportunity

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On February 14, 2006, the U.S. Patent and Trademark Office awarded its seven millionth patent, U.S. Patent No. 7,000,000 B1, to inventor John P. O'Brien and assignee, the E.I. du Pont de Nemours and Company, of Wilmington, Delaware. This milestone marks the importance of patented technology to businesses here and abroad. With the issuance of more patents and a steady increase in patent litigation since the inception of the Federal Circuit in 1982 comes a greater need for businesses to recognize the potential for profit or loss in the form of patent infringement damage awards.

Patent infringement is a tort.<sup>1</sup> Like other tortious behavior, the wrongdoer's conduct entitles the injured party (patent holder) to compensation for the wrong committed.<sup>2</sup> The patent laws set a minimum threshold of a reasonable royalty for infringement but otherwise do not specify the compensatory damages recoverable.<sup>3</sup> Typically, compensatory damages in patent cases take the form of lost profits, an established royalty, a reasonable royalty,<sup>4</sup> or a combination of lost profits and a royalty.<sup>5</sup> In addition, a patent holder may recover pre- and postjudgment interest,<sup>6</sup> costs, other than attorney fees;<sup>7</sup> enhanced damages, including, possibly, treble damages;<sup>8</sup> and, in exceptional cases, attorney fees and expenses.<sup>9</sup> Although not addressed herein, provisional patent damages are also available in cases for infringement that occur after a patent is published but before the patent is awarded.<sup>10</sup>

## Lost Profits and the *Panduit* Factors

The Polaroid Corporation recovered the largest patent infringement damage award—\$924,526,554—in a case filed against the Eastman Kodak Company<sup>11</sup> in a dispute about instant cameras. Patent holders, like Polaroid, may recover lost profits due to infringement by demonstrating “a reasonable probability that, ‘but for’ the infringement, [the patent holder] would have made the sales that were made by the infringer.”<sup>12</sup> A common way for a patent holder to establish lost profits requires proof of four factors known as the *Panduit* factors:

- demand for the patented product
- absence of acceptable noninfringing substitutes

- manufacturing and marketing capability to exploit the demand
- the amount of the profit it would have made<sup>13</sup>

The first three *Panduit* factors address causation. Proof of the first factor, market demand, generally requires evidence of sales of the patented product by the patent holder or infringer.<sup>14</sup> The second *Panduit* factor, no substitutes, is discussed often in terms of what is not an acceptable substitute but appears to require proof that other products on the market do not satisfy the same customer need or preference for the patented product. In this regard, the Federal Circuit has held that a product is not an

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acceptable substitute merely because it competes in the market with the patented product.<sup>15</sup> It has similarly held that products not for purchase in the market<sup>16</sup> or those that are not fully developed and disparately priced<sup>17</sup> do not qualify as acceptable substitutes. Products also do not qualify simply because they do the job where they lack a preferred feature of the patented product.<sup>18</sup> A greater degree of similarity is usually required. Thus, for example, a licensed supplier may be an acceptable source of noninfringing alternatives.<sup>19</sup> The third *Panduit* causation factor, capacity, typically requires evidence of current or prospective manufacturing and distribution ability to meet the demand for the patented product.<sup>20</sup>

The last *Panduit* factor requires a patent holder to prove the profits it likely would have made if not for the infringer.<sup>21</sup> Here, a patent holder can seek damages for, among other things, actual lost sales, projected lost sales, price erosion, accelerated market reentry by the infringer on termination of the patent, future lost profits, increased costs, an entire product where the patented product is only one part, lost sales of products sold simultaneously with the patented product, lost sales of related products,

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and lost sales of products the patent holder sold that competed with the patented product.<sup>22</sup> Basically, and in accordance with the open-ended nature of compensatory damages, a patent holder may claim and recover for any loss needed to compensate for the infringement.

### Royalties and the *Georgia-Pacific* Factors

As an alternative to lost profits, a patent holder may instead recover compensatory damages in the form of a royalty. This royalty may be one established in the industry or the minimum threshold of a reasonable royalty mandated by the patent laws. To demonstrate an established royalty, a patent holder must show that the royalties occurred before the infringement, were paid often enough in the industry to indicate acceptance and reasonableness, are fairly uniform, were not paid under threat of litigation, and are to licenses comparable in scope.<sup>23</sup> Even where an established royalty exists, however, it does not preclude a patent holder from seeking a higher royalty under a reasonable royalty theory; it does appear, though, to preclude recovery of a greater sum under a lost profits theory.<sup>24</sup>

A reasonable royalty is the amount that a willing licensor (patent holder) would accept and the amount a willing licensee (infringer) would pay after a hypothetical negotiation on the date of first infringement.<sup>25</sup> The most common method of establishing a reasonable royalty involves a weighing of 15 factors known as the *Georgia-Pacific* factors:

- royalties tending to show an established royalty
- royalties paid for comparable patents
- the territorial scope and exclusive nature of the license
- the patent holder's licensing policy
- the relationship between the patent holder and infringer in the market
- the effect of the patent on sales of the patent holder's other products
- the remaining life of the patent term and the length of the license
- the profitability and commercial success of the patented product
- the patented product's utility and advantage over similar older products
- the nature and benefit of the patented invention and its embodiment
- the extent of the infringer's use of the patented invention
- the portion of profit or selling price customary for use of similar inventions

- the portion of realizable profit attributable to the patented invention
- the opinion of an expert
- the royalty the parties may have agreed to voluntarily<sup>26</sup>

In contrast to an established royalty, determining a reasonable royalty relies more heavily on the discretion of the fact finder. The *Georgia-Pacific* factors are flexible in that each factor may have different weight depending on the facts of the case. For example, the patent holder and the infringer may be direct competitors in a limited-supplier market. Under such facts, the relationship between the parties may indicate that a higher royalty would have been negotiated between the two parties.

### Interest and Costs

In addition to lost profits and royalties, prejudgment interest should be awarded in patent cases, "absent some justification for withholding such an award."<sup>27</sup> Discretion lies with the district court to set an appropriate rate.<sup>28</sup> Moreover, like other litigants in federal court, patent holders are entitled to postjudgment interest<sup>29</sup> and costs, other than attorney fees.<sup>30</sup> Postjudgment interest is "calculated from date of entry of judgment at a rate equal to the 1-year constant maturity Treasury yield" published for the calendar week immediately preceding entry of judgment.<sup>31</sup> Recoverable costs in federal court include such items as fees for clerks, marshals, and court reporters; certain printing, copying, and witness fees; docketing fees; and fees for court-appointed experts and interpreters.<sup>32</sup>

### Enhanced Damages and Attorney Fees and Expenses

A district court may also award enhanced damages in patent cases "up to three times the amount found or assessed."<sup>33</sup> An award of enhanced damages is discretionary after a finding of willful infringement, which itself must be established by clear and convincing evidence.<sup>34</sup> To avoid a finding of willfulness, an infringer must act in good faith and under a reasonable belief that it was not infringing.<sup>35</sup> A fact finder should consider the totality of circumstances when assessing willfulness.<sup>36</sup> Relevant to the inquiry is whether the infringer copied the patent holder's invention.<sup>37</sup> The fact finder need not find "slavish copying" in order to conclude that the infringer copied the patentee's invention.<sup>38</sup>

In exceptional cases, patent holders may also recover attorney fees and expenses.<sup>39</sup> Attorney fees may "include those sums that the prevailing party incurs in the preparation for and performance of legal services related to suit."<sup>40</sup> To award attorney

## Resources on the Web

- <http://www.patentvaluepredictor.com/RelServices.asp>—This website provides resources for pricing and valuing patents and patent portfolios.
- <http://www.ipnewsflash.com/>—This website provides hourly updates regarding developments and business news related to patent law.
- <http://patentlaw.typepad.com/patent/>—This website provides information about recent cases and developments relating to patent law.

fees, the district court must first find the case to be “exceptional” by clear and convincing evidence.<sup>41</sup> Second, it must in its discretion deem the award appropriate.<sup>42</sup> Exceptional cases often involve “inequitable conduct before the [patent office]; litigation misconduct; vexatious, unjustified, and otherwise bad faith litigation; a frivolous suit or willful infringement.”<sup>43</sup> The district court’s discretion should be guided by “the degree of culpability of the infringer, the closeness of the question, litigation behavior, and any other factors whereby fee shifting may serve as an instrument of justice.”<sup>44</sup>

### Limits on Damages—Failure to Mark and Laches

Damages in patent cases may be reduced where an infringer has no actual knowledge of the patent and the patent holder fails to mark its product with the patent number.<sup>45</sup> Similarly, an unreasonable delay in bringing an infringement action following actual or constructive notice of infringement may prevent a patent holder from recovering presuit damages.<sup>46</sup> A six-year delay is often considered unreasonable.<sup>47</sup>

### Conclusion

Before creation of the Federal Circuit, patent holders often had a difficult time recovering a damage award sufficient to cover the expense of litigation.<sup>48</sup> That is not the case anymore.<sup>49</sup> Today, patent infringement damage awards pose a real potential for profit and a real threat of loss for businesses. The value of patented technology may change quite radically during a patent’s life cycle. A patent with little value at issuance may increase dramatically in value as industries emerge in the same field of technology. Businesses should be cognizant of this reality and have a professional regularly evaluate their patents and those of their competitors.♦

### Endnotes

1. *Heath v. A.B. Dick Co.*, 253 F.2d 30, 34 (7th Cir. 1958) (“Infringement of a patent is a tort or wrong; it is a trespass on the property rights of the patentee, or at least it is analogous to a trespass.”) (citation omitted); *see also* *Hoechst Celanese Corp. v. BP Chem. Ltd.*, 78 F.3d 1575, 1583 (Fed. Cir. 1996) (“Willful infringement is thus a measure of reasonable commercial behavior in the context of the tort of patent infringement.”); *but see* *N. Am. Phillips Corp. v. Am. Vending Sales, Inc.*, 35 F.3d 1576, 1579 (Fed. Cir. 1994) (questioning whether infringement should be characterized as a tort).
2. *See* 35 U.S.C. § 284, ¶ 1 (“Upon finding for the claimant the court shall award the claimant damages adequate to compensate for infringement but in no event less than a reasonable royalty for the use made of the invention by the infringer . . .”).
3. *See id.*
4. *See* 7 DONALD S. CHISUM, CHISUM ON PATENTS § 20.03 (2002).
5. “The Patent Act permits damages awards to encompass both lost profits and a reasonable royalty on that portion of an infringer’s sales not included in the lost profits calculation.” *Minco, Inc. v. Combustion Eng’g, Inc.*, 95 F.3d 1109, 1119 (Fed. Cir. 1996).
6. *Gen. Motors Corp. v. Devex Corp.*, 461 U.S. 648, 652–57 (1983) (prejudgment interest should be awarded in patent cases absent justification for denial); 28 U.S.C. § 1961 (mandating interest “from the date of entry of the judgment” on monetary awards in federal courts).
7. FED. R. CIV. P. 54(d)(1).
8. 35 U.S.C. § 284.
9. 35 U.S.C. § 284; 35 U.S.C. § 285 (attorney fees); *Gen. Soya Co., Inc. v. Geo. A. Hormel & Co.*, 723 F.2d 1573, 1577–78 (Fed. Cir. 1983) (expenses).
10. *See* 35 U.S.C. § 154(d). For a more extensive discussion of provi-

sional damages—and some of the uncertainty surrounding them—see Bradley Rademaker’s article in this issue.

11. *See* *Polaroid Corp. v. Offerman*, 496 S.E.2d 399, 400 (N.C. Ct. App. 1998) (citing *Polaroid Corp. v. Eastman Kodak Co.*, 17 U.S.P.Q.2d 1711 (D. Mass. 1991)).
12. *Rite-Hite Corp. v. Kelly Co., Inc.*, 56 F.3d 1538, 1545 (Fed. Cir. 1995), *cert. denied*, 516 U.S. 867 (1995) (en banc) (citation omitted).
13. *Id.* (citing *Panduit Corp. v. Stahlin Bros. Fibre Works*, 575 F.2d 1152, 1156 (6th Cir. 1978)).
14. *See* *State Industries, Inc. v. Mor-Flo Indus., Inc.*, 883 F.2d 1573, 1578–79 (Fed. Cir. 1989), *cert. denied*, 493 U.S. 1022 (1990). In a two-supplier market, a court may presume that the patent holder would have made the infringer’s sales, assuming the patent holder “has the manufacturing and marketing capabilities . . .” *Id.* at 1578.
15. *TWM Mfg. Co., Inc. v. Dura Corp.*, 789 F.2d 895, 901 (Fed. Cir. 1986).
16. *Zygo Corp. v. Wyko Corp.*, 79 F.3d 1563, 1571 (Fed. Cir. 1996); *but see* *Grain Processing Corp. v. Am. Maize-Prods. Co.*, 185 F.3d 1341, 1347–49 (Fed. Cir. 1999) (product not on the market may still be available and an acceptable noninfringing alternative).
17. *Kaufman Co., Inc. v. Lantech, Inc.*, 926 F.2d 1136, 1142 (Fed. Cir. 1991).
18. *Id.* (citation omitted).
19. *Pall Corp. v. Micron Separations, Inc.*, 66 F.3d 1211, 1222–23 (Fed. Cir. 1995).
20. *E.g.*, *Joy Techs. Inc. v. Flakt Inc.*, 954 F. Supp. 796, 805 (D. Del. 1996) (“The Federal Circuit has construed manufacturing capability to mean that the patent owner either had existing or potential capacity to meet the demand.”).
21. The law does not require a patent holder to prove damages with absolute certainty. *See, e.g.*, *Del Mar Avionics, Inc. v. Quinton Instrument Co.*, 836 F.2d 1320, 1327 (Fed. Cir. 1987) (“When the amount of the damages is not ascertainable with precision, reasonable doubt is appropriately resolved against the infringer.”).
22. BARRY L. GROSSMAN, *Patent Infringement Damages*, in PATENT LITIGATION STRATEGIES HANDBOOK 527, 530–34 (Barry L. Grossman & Gary M. Hoffman eds., 2000).
23. *Id.* at 534.
24. *See* CHISUM, *supra* note 4, at § 20.03[2].
25. *See id.* at § 20.03[3].
26. *Ga.-Pac. Corp. v. U.S. Plywood-Champion Papers, Inc.*, 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970), *modified and aff’d*, 446 F.2d 295 (2d Cir. 1971), *cert. denied*, 404 U.S. 870 (1971).
27. *Gen. Motors*, 461 U.S. at 657.
28. ROBERT L. HARMON, PATENTS AND THE FEDERAL CIRCUIT 909–10 (7th ed. 2005).
29. 28 U.S.C. § 1961.
30. FED. R. CIV. P. 54(d)(1).
31. 28 U.S.C. § 1961.
32. 28 U.S.C. § 1920.
33. 35 U.S.C. § 284.
34. *SRI Int’l, Inc. v. Advanced Tech. Labs., Inc.*, 127 F.3d 1462, 1465 (Fed. Cir. 1997).
35. *Id.*
36. *Id.* at 1464–65.
37. *Stryker Corp. v. Intermedics Orthopedics, Inc.*, 96 F.3d 1409, 1414 (Fed. Cir. 1996) (citation omitted).
38. *Id.*
39. *Central Soya*, 723 F.2d at 1577–78.
40. *Id.* (citation omitted).
41. *Ruiz v. A.B. Chance Co.*, 234 F.3d 654, 669 (Fed. Cir. 2000) (citation omitted).
42. *Cybor Corp. v. FAS Techs.*, 138 F.3d 1448, 1460 (Fed. Cir. 1998) (en banc).
43. *Forest Labs, Inc. v. Abbott Labs*, 339 F.3d 1324, 1329 (Fed. Cir. 2003) (citation and internal quotes omitted) (alteration in original).
44. *Superior Fireplace Indus., Inc. v. Majestic Prods. Co.*, 270 F.3d 1358, 1378 (Fed. Cir. 2001) (citation and internal quotes omitted).
45. GROSSMAN, *supra* note 22, at 543.
46. *See id.*
47. *Id.*
48. HARMON, *supra* note 28, at 871.
49. *Id.* at 872.