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When Is The Hypothetical Negotiation For Patent Damages?

By **James Donohue and Marie Minasi** (June 19, 2020, 6:09 PM EDT)

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A well-established approach to estimating patent damages is a reasonable royalty based on a hypothetical negotiation between the patent owner and the infringer. This construct envisions a hypothetical negotiation at the time of first infringement, with both parties accepting that the patent was valid and infringed, willing to enter a license for the patent, and having full knowledge of the relevant facts and circumstances.

While each of these assumptions can have a meaningful impact on the reasonable royalty outcome, properly identifying the date of the hypothetical negotiation and the specific parties who would have negotiated is often vital to this process.

As demonstrated earlier this year in Glaukos Corp. v. Ivantis Inc., for example, identifying the hypothetical negotiation date requires a careful evaluation early in the litigation process.

In Glaukos v. Ivantis, the defendant presented a hypothetical date that was years prior to the date proposed by the plaintiff, arguing that it would provide a "far more reasonable royalty rate, in part because it resulted from a negotiation that took place before Ivantis's years of investment in the development, testing, and regulatory approval of the" accused product.[1] However, since Ivantis only disclosed the earlier date in a rebuttal report that was issued after certain disclosure deadlines, the U.S. District Court for the Central District of California excluded the earlier hypothetical negotiation date as untimely.[2]

A review of various other cases in which courts have addressed the determination of the hypothetical negotiation date, like in Glaukos, further illustrates the importance and complications associated with identifying the proper hypothetical negotiation date.

When Is the Hypothetical Negotiation Date? When Is It Not?

As described in the 15th Georgia-Pacific factor, the hypothetical negotiation concerns the reasonable royalty that a licensor and a licensee "would have agreed upon (at the time the infringement began)."[3] While determining when infringement began can be straightforward in some circumstances, litigating parties frequently debate this concept and many factors influence the determination of the proper

hypothetical negotiation date.

Infringement generally occurs when an unauthorized party "makes, uses, offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent."[4] For a product made and launched in the United States, the timing of the first infringement could be when the product is made as opposed to when the product is first sold.

For example, in Oracle America Inc. v. Google Inc., the U.S. District Court for the Northern District of California recognized that for a foreign defendant that "expands its sales of an accused product into the United States market, the date the product is first offered for sale in the United States may in fact be the date infringement began. Where an accused product is developed and tested here in the United States, however, 'use' and therefore infringement will almost always begin well before the first sale."[5]

Identifying when infringement begins also considers whether the alleged activity was always considered unauthorized, or if it became unauthorized at a specific point in time. For example, if a product was offered for sale before the patent-in-suit issued, the date of first infringement would generally be when the patent issued as opposed to earlier when the product launched.

The existence of a covenant not to sue could further complicate the determination of first infringement.[6] Assuming the covenant not to sue was enforced for a period, but later expired, the start of unauthorized activity — and the resulting date of first infringement — could be when the covenant not to sue expired. If the infringing party had license rights to the patent for a period, the infringement could begin after the license rights expired.

Courts have also found that the date of first infringement should be based on infringing products that were specifically accused of infringement in the matter at hand.[7] In Papst Licensing GMBH & Co. KG v. Samsung Electronics Co. Ltd., the defendants raised an earlier date of first infringement based on the first sale of products that incorporated the allegedly infringing features.[8] The U.S. District Court for the Eastern District of Texas rejected the earlier date, as it was based on products that had never been specifically accused in that matter.

Similarly, in Applied Medical Resources Corp. v. United States Surgical Corp., the U.S. Court of Appeals for the Federal Circuit rejected an attempt to set the hypothetical negotiation date using the sale of an earlier infringing product (that had been resolved in a previous litigation) as opposed to the sale of a redesigned product that was being accused in the current litigation. The Federal Circuit explained that "[t]here is nothing to suggest that we should tie a hypothetical negotiation to a prior infringement no longer at issue" and that since the "determination of reasonable royalty damages is tied to the infringement being redressed, a separate infringement beginning at a different time requires a separate evaluation of reasonable royalty damages."[9]

Asserting multiple patents can also influence the beginning of infringement. Asserted patents from the same patent family or the same group of standard-essential patents, for example, have resulted in a single hypothetical negotiation covering all patents-in-suit.[10] In In re: Innovatio IP Ventures LLC Patent Litigation, "the parties agree[d] [they] would have negotiated a single license covering all subsequently obtained [ ] standard-essential patents, … including those that were applied for and issued after [the hypothetical negotiation] date." [11]

In Dataquill Ltd. v. High Tech Computer Corp., however, the U.S. District Court for the Southern District of California noted that it was not improper to have different hypothetical negotiation dates with

"different royalty rates [applied] to the different infringements" if asserted claims, such as those added during reexamination proceedings, had different dates of first infringement.[12]

Lastly, courts have made clear that the date of first infringement should not be confused with the notice date or other legal restrictions concerning the recovery of damages.

In Wang Laboratories Inc. v. Toshiba Corp., the defendants argued that the date of first infringement was the date it was given notice that its products were allegedly infringing the plaintiff's intellectual property. While the Federal Circuit acknowledged that the date of notice may limit the period for which damages may be recovered, it rejected the defendants' argument that the date of notice was the date of first infringement. Rather, the court agreed with the plaintiff "that negotiations should have been hypothesized at the start of infringement, i.e. when both a patent had issued and accused products were sold."[13]

Similarly, courts have held that the date of first infringement is not necessarily the date the defendant becomes liable for infringement, nor is it necessarily the date the complaint was filed.[14]

Why Does the Hypothetical Negotiation Date Matter?

The hypothetical negotiation date can be critical because it dictates the specific negotiating parties — i.e. who owned the patent and who was infringing when infringement began — and can frame their bargaining position at that time.[15]

Acquisitions, mergers and other transactions are common and can change the licensor and licensee over time.[16] While the plaintiff and defendant are typically based on the legal form of parties when the complaint is filed, the beginning of infringement could have occurred years earlier when the infringer or the patent owner was a different entity.

In Oracle v. Google, for example, the California federal court excluded the plaintiff's damages expert in part for analyzing a hypothetical negotiation between Oracle and Google, even though Sun Microsystems Inc. owned the patents at the time the alleged infringement began. As stated by the court, "Oracle and Sun were different companies with different interests. Injecting Oracle into the bargaining room was wrong."[17]

Depending on the circumstances, even a small change in the hypothetical negotiation date could meaningfully impact the parties' bargaining positions. In Integra Lifesciences I Ltd. v. Merck KGaA, the plaintiff and defendant disagreed as to the correct date of first infringement by less than one year.[18] This difference in time, although relatively short, was viewed as crucial to the calculation of damages because Merck's bargaining position changed significantly between the two dates. The Federal Circuit noted that "a year can make a great difference in economic risks and rewards."[19]

Further demonstrating the importance of researching the proper hypothetical negotiation date, the Federal Circuit also concluded that the record in that matter did not clearly support the hypothetical negotiation date and requested that the trial court "clarify the proper timing of the reasonable royalty calculus."[20]

The Hypothetical Negotiation Date vs. the Book of Wisdom

When hypothetical negotiation dates are challenged, parties sometimes assert that using a different

hypothetical negotiation date would not meaningfully change damage analysis, or that the "Book of Wisdom" — which, in some circumstances, may allow for the consideration of events that happen after the date of the hypothetical negotiation — can be used to justify the use of a different hypothetical negotiation date.

In American Technical Ceramics Corp. v. Presidio Components Inc., for example, the U.S. District Court for the Eastern District of New York determined that a delay in the hypothetical negotiation was "not, by itself, an apparent error that warrants preclusion" if it was shown to not impact the expert's analysis.[21]

However, in some cases, courts have found that the Book of Wisdom did not cure the use of an incorrect hypothetical negotiation date when the date had a meaningful impact on the relationship between the parties. In Syneron Medical Ltd. v. Invasix Inc., for example, the U.S. District Court for the Central District of California stated that the Book of Wisdom "cannot be used to overturn the fundamental precept that requires an ex ante hypothetical negotiation between the patentee and infringer at a time before the infringement began."[22]

The Book of Wisdom also does not "permit an expert to grant constructive knowledge to the parties of events they did not predict," such as a merger.[23] In Roche Diagnostics Corp. v. Meso Scale Diagnostics LLC, the U.S. District Court for the District of Delaware found that "[n]either the Book of Wisdom" nor the assertion that the damage opinion would be same using the a different hypothetical negotiation date would cure the analysis because "the parties' relationship changed in a highly material, substantial way" between the two different dates.[24]

Similarly, in Cassidian Communications Inc. v. MicroData GIS Inc. the U.S. District Court for the Eastern District of Texas excluded the defendants' damages expert for using an incorrect hypothetical negotiation date, despite the defendants' assertion that using the correct date would not have impacted the damage analysis. While the defendants argued that "the record [was] completely silent with regard to any market changes between the two hypothetical negotiation dates," the court found that it was the defendants' burden to justify the assertion that the difference in dates would not have impacted the damage analysis.[25]

The Right People at the Table at the Right Time

Every case is unique and involves numerous factors that can influence the determination of the proper date of hypothetical negotiation. Courts have recognized that a proper hypothetical negotiation date can be "essential" or a "key element in setting a reasonable royalty"[26] because it can impact both the economic backdrop for the negotiation and the identification of the parties at the table.

While determining the date "just before infringement" is often considered straightforward, or even an afterthought, the analysis can be complicated by many factors.[27] Which products are accused, covenants not to sue, license expirations, corporate transactions, assignments, asserting multiple patents, product development and testing, importing, and various other situations can all influence the date of first infringement.

Carefully evaluating the timing of the accused infringement can identify the correct parties and place them at that the negotiating table on the proper date.

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[1] Glaukos Corp. v. Invantis, Inc., No. 8-18-cv-00620-JVS-JDE (C.D. Cal. Feb. 10, 2020).

[2] Glaukos Corp. v. Invantis, Inc., No. 8-18-cv-00620-JVS-JDE (C.D. Cal. Apr. 8, 2020). Notably, the parties were also disputing whether the earlier European regulatory related clinical trials (the basis of Ivantis's earlier hypothetical negotiation date) constituted infringement. Ivantis - the alleged infringer - asserted that the activity in 2010 was infringing because it was for European regulatory related clinical trials and therefore not safe harbored by 35 U.S.C. § 271(e)(1). Conversely, Glaukos - the patent owner - asserted that the earlier 2010 activity was exempt from infringement under the Safe Harbor of 35 U.S.C. § 271(e)(1). Since the Court excluded the earlier 2010 hypothetical negotiation date due to the disclosure issues, the Court did not rule on whether the earlier European related clinical trials were or were not infringing acts.

[3] Georgia-Pac. Corp. v. U.S. Plywood Corp., 318 F. Supp. 1116 (S.D.N.Y.1970).

[4] 35 U.S.C.S. § 271.

[5] Oracle Am., Inc. v. Google Inc., 798 F. Supp. 2d 1111 (N.D. Cal. 2011).

[6] Vectura Ltd. v. Glaxosmithkline LLC, Civil Action No. 16-638-RGA, 2019 U.S. Dist. LEXIS 49807 (D. Del. Mar. 26, 2019).

[7] Papst Licensing GmbH & Co., KG v. Samsung Elecs. Co., No. 6:18-CV-00388-RWS, 2018 U.S. Dist. LEXIS 231698 (E.D. Tex. Oct. 25, 2018); Fujifilm Corp. v. Motorola Mobility LLC, No. 12-cv-03587-WHO, 2015 U.S. Dist. LEXIS 35235 (N.D. Cal. Mar. 19, 2015).

[8] Papst Licensing GmbH & Co., KG v. Samsung Elecs. Co., No. 6:18-CV-00388-RWS, 2018 U.S. Dist. LEXIS 231698 (E.D. Tex. Oct. 25, 2018).

[9] Applied Med. Res. Corp. v. United States Surgical Corp., 435 F.3d 1356 (Fed. Cir. 2006).

[10] SimpleAir, Inc. v. Google Inc., No. 2:14-CV-11, 2015 U.S. Dist. LEXIS 135915 (E.D. Tex. Oct. 5, 2015); In re Innovatio IP Ventures, LLC, 2013 U.S. Dist. LEXIS 144061 (N.D. Ill. Sep. 27, 2013).

[11] In re Innovatio IP Ventures, LLC, 2013 U.S. Dist. LEXIS 144061 (N.D. Ill. Sep. 27, 2013).

[12] Dataquill Ltd. v. High Tech Comput. Corp., 887 F. Supp. 2d 999 (S.D. Cal. 2011).

[13] Wang Labs., Inc. v. Toshiba Corp., 993 F.2d 858 (Fed. Cir. 1993).

[14] LaserDynamics, Inc. v. Quanta Computer, Inc., 694 F.3d 51 (Fed Cir. 2012); Acceleration Bay LLC v. Activision Blizzard, Inc., 324 F. Supp. 3d 470 (D. Del. 2018).

[15] A patent owner's exclusive licensee can also be a party to the negotiation when they are also a party to the litigation. See Schneider (Eur.) AG v. Scimed Life Sys., 852 F. Supp. 813 (D. Minn. 1994); Pentech Intern., Inc. v. Hayduchok, 931 F. Supp. 1167 (S.D.N.Y. 1996).

[16] See supra note 5.

[17] Ibid.

[18] Integra LifeSciences I, Ltd. v. Merck KGaA, 331 F.3d 860 (Fed. Cir. 2003).

[19] "The correct determination of this date is essential for properly assessing damages. The value of a hypothetical license negotiated in 1994 could be drastically different from one undertaken in 1995 due to the more nascent state of the RGD peptide research in 1994. Indeed, factoring in the rapid development of biotechnological arts, a year can make a great difference in economic risks and rewards. In any event, the record is not clear on the hypothetical negotiation date." Integra LifeSciences I, Ltd. v. Merck KGaA, 331 F.3d 860 (Fed. Cir. 2003).

[20] See supra note 18.

[21] Am. Tech. Ceramics Corp. v. Presidio Components, Inc., No. 14-CV-6544(KAM)(GRB) (E.D.N.Y. May 30, 2019).

[22] Syneron Med. Ltd. v. Invasix, Inc., No. 8:16-cv-00143-DOC-KES, 2018 U.S. Dist. LEXIS 220514 (C.D. Cal. Aug. 27, 2018).

[23] Am. Tech. Ceramics Corp. v. Presidio Components, Inc., No. 14-CV-6544(KAM)(GRB) (E.D.N.Y. May 30, 2019).

[24] Roche Diagnostics Corp. v. Meso Scale Diagnostics, LLC, No. 17-189-LPS-CJB, 2019 U.S. Dist. LEXIS 181500 (D. Del. Oct. 21, 2019).

[25] Cassidian Communs., Inc. v. MicroData GIS, Inc., Civil Action No. 2:12-cv-00162-JRG, 2013 U.S. Dist. LEXIS 200892 (E.D. Tex. Dec. 3, 2013).

[26] LaserDynamics, Inc. v. Quanta Computer, Inc., 694 F.3d 51 (Fed. Cir. 2012); Panduit Corp. v. Stahlin Bros. Fibre Works, 575 F.2d 1152 (6th Cir. 1978).

[27] For example, discovery requests that are limited to the recoverable damages period or to the current patent owner could fail to obtain information relevant to a much earlier hypothetical negotiation date or prior patent owner.