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Your Future Is Our Purpose

Corporate Survival Guide for NPE Litigation

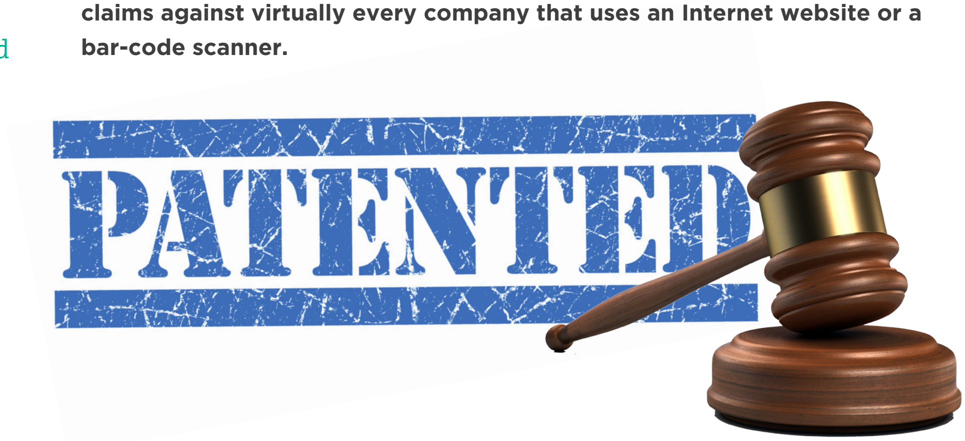
by Edward H. Rice

A FREEBORN & PETERS LLP LITIGATION WHITE PAPER

ABOUT THIS WHITE PAPER:

This paper provides a short primer for managing the risks and costs arising from patent infringement claims asserted by certain "non-practicing entities" (aka "patent trolls"). These infringement claims have grown exponentially in recent years and have affected businesses, large and small, across virtually all industries.

In the "old days," only technology companies had to worry about patent litigation. Patent lawsuits used to be battles between competitors—often manufacturers—fighting over rights to their latest innovations and the revenue generated by those innovations. Ah, the good old days. Today, every business that *uses* technology could fall victim to a patent infringement claim. And in our high-tech society, that means virtually every business is vulnerable. In recent years, certain types of non-practicing entity (aka "patent trolls") have asserted infringement claims against virtually every company that uses an Internet website or a bar-code scanner.



So what do you do if an NPE asserts an infringement claim against your company? There is no simple answer. It depends on the strength of the claim, the reasonableness of the NPE, your risk tolerance, and your ability to shift—or at least spread—your potential risks and costs. This paper will address some of the issues you may want to consider and will provide some "best practice" suggestions.

1. Evaluate the Claim

Find out what products or activities are allegedly infringing and what the NPE is demanding. Once you do, you can determine the following:

(a) Should someone else assume or share your liability? If you are a retailer, your supplier may owe you an indemnity obligation. If the answer is unclear, the supplier nonetheless may be willing to negotiate some cost-sharing deal rather than fight its customer on an indemnity dispute.

(b) How much is the NPE demanding? Some NPEs assert dozens or even hundreds of infringement claims with relatively modest demands. Many of these NPEs price their demand so that it is cheaper to pay than to fight. In some cases, it may be cheaper to take a license than to analyze the patent issues. The most economical solution may be simply to pay the demand. For some companies, however, this approach saves money only in the short-run. You need to consider whether you are inviting future claims by "rolling over" without a fight.

(c) Is your potential exposure significant? The answer will change your cost/benefit equation. If the stakes are high, you may want to invest more money and resources into your defense. The harder you look, the more likely you are to identify a defense theory that boosts your negotiating leverage or positions you for a litigation victory. If the demand is a mere nuisance, and you don't want to fight on principle, your defense costs will quickly surpass your exposure. In that case, you need an efficient and creative strategy. Ideally, the sum of your attorney fees and your settlement cost is less than the NPE's initial demand. Your advantage in these nuisance cases is that you have little to lose and the NPE has little to gain. In other words, the NPE may have at least as much incentive to settle as you do. Recognizing this fact may help you leverage a better deal.

(d) Do you have a simple (low-cost) defense? Fighting a patent infringement case on its merits can be very expensive and in some cases, it also may be unnecessary. Look for alternative, non-technical defenses that can kill the claim or provide negotiating leverage. These defenses include patent exhaustion, license (an upstream user's license may cover your use of the technology), lack of standing (i.e., if the NPE has not acquired sufficient rights under the patent to sue), etc. Damage limitation "defenses" also provide leverage by reducing the claim value. For example, a patent marking problem or a laches issue may dramatically reduce the potential damage base and deflate the NPE's expectation for a big payday. Check the patent's litigation history for a quick and inexpensive way to identify potential defenses. In some cases, another defendant may have done your work for you (*e.g.*, won a ruling that applies to you as well). Likewise, if you identify a weakness in the patent that others have missed, you may set yourself up as the defendant that the NPE would rather not fight.

(e) Can you attack the patent outside of district court litigation? If you have a strong invalidity position, consider challenging the patent in the U.S. Patent and Trademark Office (PTO). In addition to reexamination, new procedures including inter-parties review (IPR) and post-grant review (PGR) may provide good alternatives for attacking the NPE's patent. The PTO procedures have their own risks and benefits, but they may enable you to put a district court lawsuit on hold, which will allow you to save—or at least, postpone—litigation defense costs.

(f) Can you avoid the technology? If you can live without the allegedly infringing product or services, you can limit your potential damages and gain negotiating leverage. NPEs typically negotiate lump sum, fully-paid up licenses that extend until the patent expires. If you can live without the accused technology, you have nothing to fear from an injunction (though it is difficult for an NPE to get an injunction anyway) and you can argue down from the NPE's "standard rate" because you are interested only in a limited "license" covering past use. If your past use is minimal and you are willing to drop the accused product or service, the NPE may stop chasing you altogether.

2. Determine Settlement Timing

Timing is important. "Conventional wisdom" says you don't want to be the first to settle, or the last. The first to settle may be offered a "sweetheart" deal, but in fact may end up paying more. If the NPE has asserted its claim against a large group, a lot of lawyers will be searching for weaknesses in the claim. If someone finds an Achilles heel, the NPE may reduce its demand, or it may find itself losing a summary judgment motion. Those who settle "too soon" miss that benefit. On the other hand, many savvy NPEs will jack up the demand each time someone takes a shot at the patent and misses. Those who wait for someone else to kill the patent may pay a cost for the privilege of sitting on the sidelines. And the last "infringer" standing may find itself litigating alone against the NPE. In short, you face risk any way you turn. You must know how much risk you are willing to take. If you feel strongly that the claim is weak, and you can stomach the risk of a rising demand, hold your ground. If certainty is more important to you, or your exposure risk is too high for you, settle sooner.

3. Cost Control Strategies

(a) Can you share costs with other accused infringers? Many NPEs sue multiple parties in the same court. Often, law firms will offer to represent a group of defendants to spread common costs across the group. This deal can work well if: (a) you trust the firm, (b) there are no likely conflicts (e.g., if the accused products or methods work in essentially the same way for all defendants in the group), and (c) you don't mind relinquishing some degree of control over your defense. Alternatively, you can hire your own counsel and cut deals with other defendants to share defense costs for specific tasks, such as expert reports, document review, dispositive motions, etc. If you belong to a large defense group, you can potentially save a lot of money this way. On the other hand, large defense groups provide inefficiencies of their own. Weekly conference calls lasting several hours with 25 lawyers on the line are expensive and often unproductive (typically, some active participants add value but often those with the least to add speak the most).

(b) Can you get an alternative fee deal from your outside counsel? Alternative fees may help you control costs. And there are many options. But first, you need to know, at least roughly, the value of the claim. To do that, you evaluate your potential exposure against your likelihood of success and the NPE's demand. The claim value gives you a sense for where you need to cap your defense spending. With that cap in mind, you can negotiate a variety of alternative fee deals with outside counsel, for example:

- Flat fee

  Either for the entire defense or on a project-by-project basis (e.g., $X for initial pleadings, $Y for fact discovery, etc.)

- Payments spread over time to avoid huge spikes
- Reverse contingency (X payment for achieving deal of Y or better)

- Hourly rate discount with success bonus kicker
- Soft caps

  Hourly rates that are discounted as fees hit pre-set cap limits. (E.g., X% discount for fees that exceed the cap by 10% and Y% discount for fees that exceed the cap by 20%, etc.)

(c) Can you get patent litigation insurance? Your company's general liability policy almost certainly does not cover patent infringement. But some insurance companies offer coverage for patent infringement liability, defense costs, or both. Because patent litigation can generate enormous risk, these policies typically have fairly high premiums, high deductibles, and low caps. The low caps make these policies unattractive for high-stakes claims. And for nuisance claims, these policies may not provide great value because of the relatively high deductible. But for some companies, these policies hit a sweet spot and may provide a good hedge against a significant portion of their typical NPE litigation risk exposure.

(d) Can you benefit from an alternative cost-spreading opportunity? In response to the rise of NPE litigation, organizations (like RPX) buy "high-threat" patents "defensively" for their members. They identify high-threat patents and buy them to take them out of circulation and prevent them from falling into the hands of some company that will assert them against the organization's members. These organizations do not function equally well in all industries. They tend to perform best in industries where big players are likely to sign up for membership and where high risk patents are easier to identify. But if you operate in one of these industries, you should at least consider the benefits that these organizations may offer.

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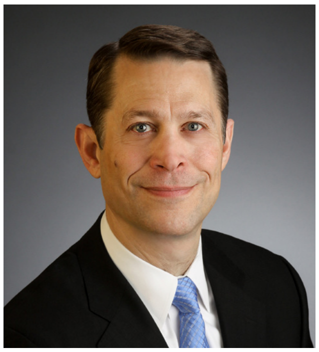
ABOUT THE AUTHOR



Edward H. Rice

Partner, Litigation Practice Group

Chicago Office
(312) 360-6874

erice@freeborn.com

Ed Rice is a trial and appellate lawyer who, since 1988, has focused primarily on patent cases and other technology disputes. He received his earliest patent trial experiences at the U.S. Department of Justice in Washington, D.C., where he defended the government in patent infringement cases filed in the U.S. Court of Federal Claims.

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CHICAGO
311 South Wacker Drive
Suite 3000
Chicago, IL 60606
(312) 360-6000
(312) 360-6520 fax

SPRINGFIELD
217 East Monroe Street
Suite 202
Springfield, IL 62701
(217) 535-1060
(217) 535-1069 fax