

NEW PATENT LICENSING STRATEGIES REQUIRED



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"FOR DEFENDANTS, IT WILL BE FAR EASIER TO INVALIDATE PATENTS."

Introduction

Trillions of dollars are at stake as a result of the combined effect of two recent patent decisions handed down by the US Supreme Court—namely, the March 2006 case of *eBay Inc. v. MercExchange, L.L.C.* (*eBay*) and the April 2007 case of *KSR Int'l Co. v. Teleflex Inc.* (*KSR*). The effects of these rulings are impacting the enforcement strategies of individual patent owners as well as owners of large patent portfolios.

Strategy factors

The validity of patents that may be infringed, and the right of patent owners to obtain an injunction against infringers, are important factors that will influence a decision whether or not to pursue patent infringement litigation. With median US legal fees through trial (not including out-of-pocket costs) reaching \$5 million or more, this decision is not one to be taken lightly.

The pendulum has swung

There is a growing consensus that the combined effect of *eBay* and *KSR* has caused the pendulum to swing in favour of those seeking licences under patents.

eBay

In *eBay*, the Supreme Court, in effect, removed the near automatic injunctive relief previously routinely awarded to patent owners against infringers. Accused infringers and would-be infringers are expected to be emboldened. Patent owners must now ever more seriously consider offering licences under their patents, since they will not have the same 'injunction weapon' leverage that would threaten an infringer's day-to-day business operations. Accused infringers will no longer be staring down the barrel of a gun, and will have greater bargaining power in seeking out-of-court settlements. That said, the Court did not remove injunctions entirely from the patent owner's arsenal, and the survival of a business may still be at stake.

KSR

In *KSR*, the Supreme Court dealt another blow to patent owners, by imposing more restrictive guidelines on whether any given invention meets the burden of being 'non-obvious'—a fundamental century-old criterion for obtaining a US patent. It will be more difficult to obtain a valid patent and to enforce an existing one. For defendants, it will be far easier to invalidate patents.

Economic licence considerations

In deciding whether or not to grant a licence, commercial patent owners have historically compared the amount of royalty to be realised under a licence to the profits they will likely lose to sales made by an infringing competitor. While the gross profit margin on sales will normally dwarf a licence royalty, many patent owners have chosen the route of enjoying the licence revenue stream from the competitor, rather than pursue litigation. Licensors attempt to negotiate agreements that provide for periodic licensee royalty reports, which include valuable competitive sales information. Licensees often attempt to avoid reporting provisions by negotiating flat licence fees or by reporting to an independent third party, for audit purposes.

Impact upon investors and start-ups

It is too early to draw any firm conclusions regarding the effect that *eBay* and *KSR* will ultimately have upon start-ups. Clearly, the risks for early stage investors have increased, now that the traditional weapons used to enforce IP associated with new technologies have been impacted. Investors often shun this type of uncertainty, and will gravitate toward leading-edge technology based upon key IP. Venture capital funds are attracted to big investments with short exit strategies. Due diligence investigations, which have always been important, will become even more critical. If entrepreneurs are to be encouraged to develop new technologies and industries, our legal system will need to support them with adequate, well-defined IP protection. Furthermore, our scientists and engineering students need assurances that their innovations will be introduced into a system capable of providing protection for worthy inventions.

Patent trolls have been hurt

eBay and *KSR* have, together, dealt a severe blow to patent 'trolls'—companies that exist primarily to make money from patent litigation and that use the system to force lucrative settlement. They no longer possess the injunction weapon that has been so effective for them. And their patents of questionable validity will be more vulnerable to legal attack by the 'deep pocket' companies they usually target. Many such patent trolls utilise the services of attorneys who are retained on a contingency fee basis and who may now be less willing to pursue cases through trial and appeal.

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