

Fed. Circ. Standard On Patent Damages Needs Clarity

By **Jason Shull** (October 22, 2019, 4:40 PM EDT)

A long-standing issue in calculating damages in patent lawsuits is the accused infringer's sale of a multicomponent product in which the asserted patent only covers one feature of the product. For over a century, the U.S. Supreme Court has held that plaintiffs must take care in seeking only those damages attributable to the infringing features.

Stretching back 135 years, in *Garretson v. Clark*, the plaintiff sought damages based on the defendant's sales of entire mops based on a patent for a mop head clamp.[1] The court determined that this was in error: "The patentee ... must in every case give evidence tending to separate or apportion the defendant's profits and the patentee's damages between the patented feature and the unpatented features." [2]

The court explained that "[w]hen a patent is for an improvement, and not for an entirely new machine or contrivance, the patentee must show in what particulars his improvement has added to the usefulness of the machine or contrivance" and "[h]e must separate its results distinctly from those of the other parts, so that the benefits derived from it may be distinctly seen and appreciated." [3] According to the court, "such evidence must be reliable and tangible, and not conjectural or speculative." [4] This concept — that a plaintiff should only be rewarded for the incremental value of its invention and not a product's unpatented features — is known as apportionment.[5]

The issue of apportionment, however, is simple to frame yet hard to resolve. As discussed below, within the last decade, an increasing number of decisions from U.S. Court of Appeals for the Federal Circuit have been divided on what constitutes "evidence tending to separate or apportion ... between the patented features and the unpatented features." [6]

Different fact patterns produce sincere opposing arguments as to the proper methodology for apportioning damages to ensure the plaintiff is receiving all that it is owed, but no more. With the variance in Federal Circuit decisions, perhaps the time is right for the Supreme Court to clarify this key damages requirement and provide a consistent framework for apportionment.

On one hand, some Federal Circuit decisions hold that the plaintiff cannot merely contend for a percentage of the entire value of a multicomponent product that contains the patented invention. Those decisions require the plaintiff to select a reasonable starting point for the damages analysis and then to subtract the value of all unpatented features. Those decisions closely examine the evidence of apportionment and reject the damages award if the evidence or analysis is deficient.[7]

For example, in *LaserDynamics Inc. v. Quanta Computer Inc.*, the Federal Circuit affirmed the district court's rejection of a \$52 million damages award where damages were based on the entire cost of a laptop computer but the asserted patent claims covered only technology that allowed a disc drive to identify the type of disc inserted — e.g., a CD versus a DVD.[8]

The plaintiff and its expert contended that "a 2% running royalty was applied to [defendant's] total revenues from sales of laptop computers in the United States — \$2.53 billion — was an appropriate and reasonable royalty." [9] The court rejected the plaintiff's argument that "apportionment" was satisfied merely by selecting a low royalty rate on the sale price of the entire laptop.[10] The court emphasized that "the requirement to prove that the patented feature drives demand for the entire product may not be avoided by the use of a very small royalty rate." [11]

The court explained:

Admission of such overall revenues ... only serve to make a patentee's proffered damages amount appear modest by comparison, and to artificially inflate the jury's damages calculation beyond that which is 'adequate to compensate for the infringement ... the fact remains that the royalty was expressly calculated as a percentage of the entire market value of a laptop computer rather than a patent-practicing ODD alone.[12]

Likewise, in *VirnetX Inc. v. Cisco Systems Inc.*, the Federal Circuit vacated a \$368 million damages award where the plaintiff sought damages based on the entire cost of a phone, but the asserted patent claims covered only the features of VPN and FaceTime software.[13] The plaintiff's damages analysis started with "the entire cost of the iOS devices, ranging in value from \$199 for the iPod Touch to \$649 for the iPhone 4S." [14] The plaintiff then subtracted "only charges for



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additional memory sold separately” and “did not even attempt to subtract any other unpatented elements from the base, which therefore included various features indisputably not claimed ... e.g., touchscreen, camera, processor.”[15]

The court explained that proper apportionment should have either subtracted the numerous unpatented elements or started with the \$29 cost of the software upgrade alleged to contain infringing features.[16] Quoting LaserDynamics, the court emphasized: “Whether ‘viewed as valuable, important, or even essential,’ the patented feature must be separated.”[17]

On the other hand, some Federal Circuit decisions have taken a more relaxed approach resulting in plaintiffs calculating royalties from revenues for the entire, multicomponent product, even where the incremental benefit claimed by the patent was directed to only a specific feature of the product.[18] In those cases, apportioning the value to the patented feature was accomplished by using the Georgia-Pacific factors[19] and, in particular, permitting plaintiffs to import royalty rates from “comparable” license or settlement agreements involving different patents, products and parties.[20]

Those decisions, however, have offered little clarity on the standards by which a royalty rate may actually be considered “apportioned” by using the Georgia-Pacific factors.[21]

For example, in *Exmark Manufacturing Co. v. Briggs & Stratton Power Products*, the asserted patent claims a multiblade lawn mower having improved “flow control baffles” that more efficiently direct grass clippings toward a side discharge opening and thereby improve the quality of the mowing operation.[22] Although the asserted claims broadly covered a multiblade mower, the asserted patent makes clear that the improvement related only to the flow control baffle.

The Federal Circuit affirmed the district court’s decision allowing the plaintiff to use sales of entire lawn mowers as the royalty base, as opposed to just the royalty based for the innovative “baffle component.”[23] “[A]pportionment can be addressed in a variety of ways,” the court held, “including by careful selection of the royalty base to reflect the value added by the patented feature [or] ... by adjustment of the royalty rate so as to discount the value of a product’s non-patented features; or by a combination thereof.”[24]

The court explained that “the standard Georgia-Pacific reasonable royalty analysis takes account of the importance of the inventive contribution in determining the royalty rate that would have emerged from the hypothetical negotiation.”[25] The court noted that using the entire accused lawn mower as the royalty base “accurately reflects the real-world bargaining that occurs” and was consistent with a prior license relied on by the plaintiff’s expert.[26] In addition, deriving the royalty base from sales of complete mowers was “particularly appropriate in this case,” the court found, because the patent claimed an entire “multiblade lawn mower,” and not only “a single component thereof.”[27] “

In *Sprint Communications Co. LP v. Time Warner Cable Inc.*, the Federal Circuit affirmed a \$140 million damages award, where the district court allowed the patent owner to import a reasonable royalty from a jury verdict from a different case, involving a different defendant, and some of the same patents. The jury verdict from the different case awarded a royalty based on other defendant’s entire revenues for its VoIP product.

The court determined that the jury verdict from the first case, based on the total revenues for the entire VoIP product, was sufficiently reliable as a basis for a royalty because “[b]y operation of the hypothetical negotiation method of calculating damages, the award compensated Sprint for the incremental value of Sprint’s technology, not for the value of unpatented features of Vonage’s VoIP system.”[28]

The Federal Circuit rejected the defendant’s argument that a proper apportionment had not been conducted, citing to two third-party license agreements for the patented technology, both of which applied the same royalty rate as the jury verdict in the first case.[29] The court also relied on the fact that patent owner’s expert “addressed apportionment at some length during his testimony” and that “the jury was specifically instructed on apportionment.”[30]

In *Elbit Systems Land & C4I Ltd. v. Hughes Network Systems LLC*, the Federal Circuit affirmed a \$21.1 million award based on a third-party settlement agreement, where the patent owner’s expert testified that apportionment was “implicitly considered within the royalty rate” in the prior agreement.[31] The patent owner’s expert testified that rather than “parse out a value for each of the claims,” he “came up with a market, comparable royalty rate, and then [he] adjusted it as necessary” for the hypothetical negotiation.[32] The Federal Circuit found that the damages evidence did not violate principles of apportionment because the patent owner’s expert testified that apportionment was “essentially embedded in the comparable value” from the prior agreement.[33]

As the above cases illustrate, there is no unanimity as to how the apportionment rule should be applied in every case, and different methods for apportionment yield vastly divergent outcomes. Without a consistent framework for apportionment, damages awards tend to be unpredictable and run the risk of overcompensating plaintiffs by allowing damages for a small component based on the price of a much larger product.

A consistent framework is important because rules governing damages can impact competition and innovation in markets for technology. For example, court-awarded damages “play a central role ... by establishing the legal shadow in which negotiations occur.”[34] They “have a ‘ripple effect’ on the ... cases in which royalties are negotiated to avert or settle negotiation.”[35]


If damage awards are unpredictable and parties have divergent expectations regarding the value of a license, then licensing through bilateral negotiation is likely to fail — leading to the patent owner filing suit or the other party agreeing to a license and accepting a value significantly different than its expectation in order to minimize litigation risk. “Long term, a patent system which leads to such licenses will either provide inventors with diminished incentives to innovate or will

provide patent holders with misplaced incentives for patent assertion in lieu of other means of monetization.”[36]

Unpredictable and inflated damages awards could also discourage innovation by increasing the costs of product development and the risks of investment for manufacturers. Indeed, such damages awards could discourage product manufacturers from starting in the first place.[37]

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[1] [Garretson v. Clark](#) , 111 U.S. 120, 121 (1884).





[2] *Id.*

[3] *Id.*

[4] *Id.*

[5] There is one, narrow exception to the apportionment rule. The exception, according to the Court in *Garretson*, is where the plaintiff can “show ... that the profits and damages are to be calculated on the whole machine, for the reason that the entire value of the whole machine, as a marketable article, is properly and legally attributable to the patented feature.” *Garretson*, 111 U.S. at121. This exception, known as the entire market value rule, potentially relieves a patentee from apportioning its damages when the patentee can show that “the patent-related feature is the ‘basis for customer demand.’” [Rite-Hite Corp. v. Kelley Co.](#) , 56 F.3d 1538, 1549 (Fed. Cir. 1995).

[6] *Garretson*, 111 U.S. at121.

[7] See, e.g., [Power Integrations, Inc. v. Fairchild Semiconductor Int’l, Inc.](#) , 904 F.3d 965, 977 (Fed. Cir. 2018); [VirnetX, Inc. v. Cisco Systems, Inc.](#) , 767 F.3d 1308, 1327 (Fed. Cir. 2014); [LaserDynamics, Inc. v. Quanta Computer, Inc.](#) , 694 F.3d 51, 66-70 (Fed. Cir. 2012); [Lucent Techs., Inc. v. Gateway, Inc.](#) , 580 F.3d 1301, 1336 (Fed. Cir. 2009).

[8] *LaserDynamics*, 694 F.3d at66-70.

[9] *Id.* at 68.

[10] *Id.* at67, 69.

[11] *Id.* at67.

[12] *Id.* at68.




[13] *VirnetX*, 767 F.3d at1328.


[14] *Id.*

[15] *Id.*


[16] *Id.* at1329.

[17] *Id.*

[18] See, e.g., [Sprint Communications Co., L.P. v. Time Warner Cable, Inc.](#) , 760 Fed.App’x. 977, 982-83 (Fed. Cir. 2019); [Exmark Mfg. Co. v. Briggs & Stratton Power Prods.](#) , 879 F.3d 1332, 1348-49 (Fed. Cir. 2018); [Mentor Graphics Corp. v. EVE-USA, Inc.](#) , 851 F.3d 1275 (Fed. Cir. 2017).

[19] The Georgia-Pacific factors are fifteen, non-exclusive factors originally set forth in [Georgia-Pacific Corp. v. U.S. Plywood Corp.](#) , 318 F. Supp. 1116 (S.D.N.Y. 1970).

[20] A common method for calculating patent damages relies on evidence provided by comparable license agreements. Comparable license agreements, however, often times provide for a royalty on an entire product, where only an aspect or feature of that product is patented. In such cases, application of the apportionment requirement has required creative economic analysis on behalf of the patent owner’s expert to determine an appropriate royalty base.

[21] Notably, the Federal Circuit in [Ericsson, Inc. v. D-Link Sys., Inc.](#) , suggested that the Georgia-Pacific factors should not be relied upon to ensure apportionment. See 773 F.3d at 1228 n.5 (“While factors 9 and 13 of the Georgia-Pacific factors allude to apportionment concepts, we believe a separate instruction culled from *Garretson* would be preferable in future cases.”). Other legal scholars and professionals agree. See, e.g., Bensen & White, *Using Apportionment to Rein in the Georgia-Pacific Factors*, 9 Colum. Sci. & Tech. L. Rev. 1, 46 (2008) (“treating

apportionment merely as a factor in the reasonable royalty analysis, where it may be given more or less weight or ignored altogether, is insufficient to meet long-standing apportionment requirements”); see also Hon. Gajarsa, Lee, & Douglas, *Breaking the Georgia-Pacific Habit: A Practice Proposal to Bring Simplicity and Structure to Reasonable Royalty Damages Determinations*, 26 *Tex. Intell. Prop. L. J.* 60 (2018) (“multiple Georgia-Pacific factors (Factors 6, 8, 10, and 11) are inconsistent with the apportionment principles (Factor 13) that have now become critical components of damages determinations”); Amy L. Landers, *Patent Claim Apportionment, Patentee Injury, and Sequential Invention*, 19 *Geo. Mason L. Rev.* 471, 473 (2012) (“Today, the prevailing method courts use to calculate a reasonable royalty, the Georgia-Pacific Corp. v. U.S. Plywood Corp. test, includes consideration of the patentee’s contribution as one factor of fifteen. These considerations are folded together in a manner that loses this crucial causative link in a malleable, and virtually unreviewable, verdict amount.”) (footnotes omitted); Patent Reform in the 111th Congress: Legislation and Recent Court Decisions Before the S. Comm. On the Judiciary, 111th Cong. 14 (2009) (statement of Mark A. Lemley, Professor of Law, Stanford Law School), available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_senate_hearing&docid=f:54059.pdf (testifying that the Georgia-Pacific factors are open to manipulation and that they do not reflect the contribution of the patented technology to the technology at issue).

[22] *Exmark*, 879 F.3d at 1338.

[23] *Id.* at 1348.

[24] *Id.* (internal quotes omitted).

[25] *Id.* at 1349.

[26] *Id.*

[27] *Id.*

[28] *Sprint Communications Co.*, 760 Fed.Appx. at 982-83.

[29] *Id.* at 983.

[30] *Id.* at 984.

[31] *Elbit Systems Land & C4I Ltd. v. Hughes Network Systems, LLC* , 927 F.3d 1292, 1299-1301 (Fed. Cir. 2019).

[32] *Id.*

[33] *Id.* at 1301.

[34] See Fed. Trade Comm’n, *The Evolving IP Marketplace: Aligning Patent Notice and Remedies With Competition* 138 (2011).

[35] *Id.* at 144.

[36] Dubiansky, *A Competition Perspective on Apportionment* 4 (2016)

[37] See Michel, *Bargaining for RAND Royalties in the Shadow of Patent Remedies Law*, 77 *Antitrust L.J.* 889, 895 (2011) (“[I]nflated damage awards can discourage innovation by raising the costs of product development and increasing the risks of investment for other innovators and manufacturers.”).