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Patent Damages

John L. Skenyon
Christopher Marchese
John Land

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By John L. Skenyon
Christopher S. Marchese
*John Land**

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I. *INTRODUCTION*

Patents, those arcane property rights that nearly all corporate counsel—especially those in the high-tech arena—have encountered at some time in their career. What is so important about patents? Why should we be concerned with them? Even so, why do we need to understand them?

The answer to these and other patent-related questions has become abundantly clear over the past 15 or 20 years: patents can be extremely valuable. With the advent in 1982 of the Court of Appeals for the Federal Circuit ("Federal Circuit"),[1] patent law has become much more solidified. As a consequence, companies and individuals alike have increasingly asserted their patents in court—with great effect. At the same time, the

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* John L. Skenyon is a principal of Fish & Richardson, P.C. in Boston, MA. He received his B.S. in Electrical Engineering from Catholic University in 1969, and his J.D. from Catholic University in 1973. He has practiced patent law since 1973 specializing in intellectual property litigation, and currently specializing in jury trials in IP cases.

Christopher S. Marchese is an associate of Fish & Richardson, P.C. in La Jolla, CA. He received his B.A. in Mathematics from Centre College of Kentucky in 1987, his B.S. in Electrical Engineering from the University of Kentucky in 1987, and his J.D. from George Washington University in 1992. His practice involves intellectual property litigation, patent prosecution, and trademark prosecution.

John F. Land is a principal of Fish & Richardson, P.C. in La Jolla, CA. He received his B.S. *with honors* from California Institute of Technology in 1975, and his J.D. from the University of Southern California in 1978. His practice specializes in patent prosecution in electronics and computer-related technologies. His practice also includes client counseling in copyright, trade secret, trademark and unfair competition matters, as well as technology and intellectual property licensing.

1. *See* Federal Courts Improvement Act of 1982, Public L. No. 97-164 section 402, 96 Stat. 25, 27, *codified at* 28 U.S.C. 1295 (1988).

number of patents applied for and issued has skyrocketed. In today's technological world, patents have become a formidable sword as well as a shield, and we can only expect that their importance and value will continue to grow.

With solidification of the patent laws and the increasing frequency of patent infringement lawsuits, the law of patent damages has likewise become very important. In 1991, for example, Polaroid was awarded over $873 million against Kodak in patent infringement litigation that put Kodak out of the instant photography business.[2] As large as that award was, it was well below the $12 billion Polaroid had sought and the $1.5 to $2 billion industry that analysts had expected.[3] In 1993, after a trial lasting three and a half months, a jury deliberated for three and a half weeks and awarded Litton Industries $1.2 billion against Honeywell for patent infringement—the largest patent infringement award in U.S. history.[4] In another mammoth damages award, 3M was awarded $63 million in damages against Johnson & Johnson for patent infringement.[5]

These are only a small sample of the many financially significant patent infringement cases. Since the Polaroid case in 1991 to the end of 1996, courts have awarded or upheld damages exceeding $1 million in over 30 patent cases.[6] In at least 8 of those cases, the damages originally awarded to the plaintiff—

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2. *Polaroid v. Kodak*, 867 F.2d 1415 (Fed. Cir. 1989), *cert. denied,* 490 U.S. 1047, 109 S.Ct. 1956, 104 L.Ed.2d 425 (1989); *see also Polaroid Corp. v. Eastman Kodak Co.*, 1990 WL 324105, 16 U.S.P.Q.2d 1481 (D. Mass.1990). About half of the award was prejudgment interest. The award, however, was later increased to about $925 million due to post-judgment interest.
3. The Reuter Library Report, October 31, 1990.
4. Litton had sought $1.92 billion in lost profits damages. A new trial on damages was granted in 1996. *Litton Sys., Inc. v. Honeywell, Inc.*, 87 F.3d 1559 (Fed. Cir. 1996). In addition, the Supreme Court ordered a review of the Federal Circuit's holding regarding the doctrine of equivalents in view of the decision in *Warner-Jenkinson Co. v. Hilton Davis Chem. Co.*, 137 L. Ed. 2d 146, 117 S. Ct. 1010 (1997). *See Honeywell, Inc. v. Litton Sys.*, 137 L. Ed. 2d 323, 117 S. Ct. 1240 (1997).
5. *Minnesota Mining & Mfg. Co. v. Johnson & Johnson Orthopaedics, Inc.*, 976 F.2d 1559 (Fed. Cir. 1992). Of the total damage award, $9.5 million was prejudgment interest, and of the remaining $53.5 million, almost $29 million was lost profits based on erosion of 3M's prices on the patented product caused by the infringement, and the rest was for lost profits based on 3M's lost sales of the patented product due to the infringement.
6. This figure is based on a survey conducted by the authors.

usually by a jury—exceeded $100 million.[7] These figures are somewhat misleading, however, in that they fail to account for the scores of settlements reached in patent infringement cases, many of which have far exceeded $1 million. Though settled, it is safe to assume that the parties' respective patent damages analyses—concerning the potential award, the risk of exposure, and the strengths and weaknesses of their respective damages cases—have greatly influenced and shaped the settlements.

Though one may be aware of the ultimate result in these cases, the underlying reasons for the awards are not often fully appreciated. It is true, of course, that each patent damage case depends in very large part on the unique facts involved. Nevertheless, a proper understanding and application of the law of patent damages as it exists today can greatly improve a patent owner's chances of maximizing its recovery and an accused infringer's chances of minimizing its exposure.

This is especially true, in light of the role business decision makers—executives, managers, and corporate counsel—must often play in making decisions about patent litigation strategy and tactics. More often than not, this role is handled without a deep, or even surface understanding of the nuances of patent law, and particularly patent damages. In struggling to understand what is generally considered one of the more arcane areas of law, most decision makers ultimately focus on three issues: (1) the probability of winning or losing a case; (2) the probable magnitude of the gain or loss; and (3) the costs—attorneys' fees, personnel time, *etc.*, of reaching either result. In our experience, a disproportionate amount of time and energy is spent on predicting case outcomes and estimating the costs involved. Damages are often almost an afterthought, relegated importance only at later stages of the litigation. Far too often, damages in patent cases are overestimated by the patent owner's counsel and underestimated by the alleged infringer's counsel. We believe that a more thorough analysis of damages should be undertaken at the earliest stages of litigation—to the extent possible even without the benefit of discovery from the other side.

In this article, we will introduce the basic legal principles of patent damages and many of the economic concepts that are in-

7. This figure is based on a survey conducted by the authors of *Reuters Financial Service* and *The Reuter Business Report* via LEXIS-NEXIS for the period 1991-96.

extricably linked to those legal principles. We will discuss the two basic types of damages that are awarded in patent infringement cases: lost profits and reasonable royalty. In addition, we will provide an overview of these two types of damages. We will also explain the criteria that help determine which type of award is appropriate in different circumstances and provide guidelines for determining how much can be won or lost in a patent infringement lawsuit. Finally, we will describe other facets of patent damages, including enhancement of damages for willful infringement (*i.e.*, punitive damages), awards of attorneys' fees, and limitations on patent damages.

For a much more thorough treatment of patent damages, we refer you to our forthcoming book on the same subject. The book, entitled *Patent Damages: Law and Practice*, will be published in the summer of 1998 by the West Publishing Company.

II. OVERVIEW OF DAMAGES AVAILABLE UNDER THE 1952 PATENT ACT

Since 1952, 35 U.S.C. § 284 has governed the award of damages in patent cases. Section 284 provides:

> Upon finding for the claimant [*i.e.*, patent owner] the court shall award the claimant damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court.
>
> When the damages are not found by a jury, the court shall assess them. In either event the court may increase the damages up to three times the amount found or assessed.
>
> The court may receive expert testimony as an aid to the determination of damages or of what royalty would be reasonable under the circumstances.[8]

In reality, section 284 really provides only one category of patent damages, and that is "damages adequate to compensate for the infringement." Section 284 provides no guidance as to what constitutes such "adequate" damages or how they are to be determined. Instead, the courts—usually with the "help" of at

8. The language of section 284 has not been changed since the current Patent Statute was enacted in 1952.

least one very interested party - have created literally every method of computing damages in this very fertile legal area.

Only two Supreme Court cases have dealt with section 284 since it was enacted.[9] The first was the famous convertible top case, *Aro Mfg. Co. v. Convertible Top Repl. Co.*,[10] which was decided in 1964. The main thrust of *Aro* involved the question of contributory infringement, but the Court also addressed the question of how patent damages should be determined under the 1952 statute by saying that, "[t]he question to be asked in determining damages [under section 284] is 'how much had the Patent Holder and Licensee suffered by the infringement. And that question [is] primarily: had the Infringer not infringed, what would the Patent Holder-Licensee have made?'"[11] Thus, while the Supreme Court did not directly address any damages theory, this quoted language clearly indicates that "damages adequate to compensate for the infringement" equates with putting the patentee in the financial position it would have been in had the infringement not occurred.[12]

Almost 20 years later, the Supreme Court revisited section 284 in *General Motors Corp. v. Devex Corp.*[13] There, the Court held that in the context of a patent damages award, prejudgment interest should be applied (absent some particular justification for withholding it), because such an interest award would be needed "to make the patent owner whole."[14] Once again, the Supreme Court really equated the concept of putting the patentee in the same financial position it would have occupied had the infringement never happened with the section 284 standard of "damages adequate to compensate for the infringement."[15]

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9. An historical review of the earlier Supreme Court cases on patent damages is interesting academically. However, it is the authors' intent to provide some practical help on this subject today, and it is their collective experience that the pre-1952 patent damages cases, dealing with differently-worded patent damages provisions, and indeed, different approaches to patent damages, are not generally useful for that purpose.
10. 377 U.S. 476, 84 S.Ct. 1526, 12 L.Ed.2d 457 (1964).This is second of the *Aro* cases and is often referred to as *Aro II*. The original *Aro* case (*Aro I*) is found at *Aro Mfg. Co. v. Convertible Top Replacement Co.*, 365 U.S. 336, 81 S.Ct. 599, 5 L.Ed.2d 592 (1961).
11. *Aro II*, 377 U.S. at 507.
12. *Cf. id.*
13. 461 U.S. 648, 655-656, 103 S.Ct. 2058, 76 L.Ed.2d 211 (1983).
14. *Id.* at 655.
15. *Id.*

This is the critical starting point for any review of the various patent damages theories or even for a damages analysis in an actual case, regardless of how the damages award is computed or what that damages award is called. As will be discussed in more detail later, it is probably the failure to recognize this basic premise that has resulted in many of the large damages awards for the patentee—awards that otherwise might have been substantially limited.

Unfortunately, neither section 284 itself nor the Supreme Court cases take us very far in any practical damages analysis. Nevertheless, we can summarize some of the types of patent damages that courts have awarded in the recent past.[16] Furthermore, a word of warning is in order: not all of these theories apply to all cases in this heavily fact-driven area, and some very minor changes in the facts can radically change the results. In any event, to provide a guideline, we can summarize the principal damages claims which will then be discussed in greater detail below:

A. *Basic Theories—"Lost Profits" & "Reasonable Royalty"*

In patent infringement suits, a patent owner can seek monetary relief from infringement under two basic theories: "lost profits" and "reasonable royalty."[17] Both theories evolved from its provision for an award of "damages adequate to compensate for the infringement, but in no event less than a reasonable royalty."[18] Lost profits means the amount of money the patent owner lost due to the infringement. Thus, the patent owner must prove that the infringement caused the lost profits.[19] If the patent owner cannot make such proof, it is *entitled* to reasonable royalty damages.[20] A patent owner may recover a mixed or split award, in which lost profits are used as a mea-

16. Given the wide latitude afforded by the statute, the decisions in this area are not uniform. Consequently, we shall focus on the theories and approaches that the Federal Circuit has approved. This should not be interpreted as a rejection of other theories or approaches, however, as this is an area where creative thinking can be and has been highly rewarded.
17. *See* 35 U.S.C.A. § 284.
18. *See* 35 U.S.C.A. § 284.
19. *See, e.g., Bellehumeur v. J.B. Mktg.*, 41 U.S.P.Q.2d 1792 (Fed. Cir. 1996).
20. 35 U.S.C.A. § 284; *see also Rite-Hite Corp v. Kelley* Co, 567 F.3d 1538, 1545-46, 35 U.S.P.Q.2d 1065 (Fed. Cir. 1995) (en banc), *cert. denied*, 516

sure for some infringing sales, while a reasonable royalty is used as a measure for the remaining sales.

The existence of two easily labeled patent damage theories can be misleading. In more than one case, assessing patent damage law in only these terms has led to financial disaster, sometimes of huge proportions. The truth is that both of these terms are misnomers to some degree; therefore, they should be properly understood by anyone attempting to assert or defend any damage claims.

The court has a fair degree of discretion in determining patent damages. The methodology of assessing and computing damages under section 284 is within the sound discretion of the district court.

B. Infringer's Profits

For much of the history of U.S. patent law, the remedy of an accounting of the infringer's profits due to infringement was available. The merger of law and equity courts in the late 1800's, however, eliminated procedural barriers to alternative remedies, and the practical difficulties of apportioning profits to an infringement lead to the abolishment of the accounting remedy with the enactment of the 1946 Patent Act. The only exceptions are design patent cases, under which a design patent owner can still seek damages in the form of the *infringer's profits*.[21] The current 1952 Patent Act continues the provisions of the 1946 Patent Act.

C. Enhancement of Damages

A patent owner may also obtain relief in the form of collateral assessments, which include mandatory pre-judgment interest and discretionary enhancement of damages up to three times the amount found or assessed. The court has a fair degree of discretion in enhancing patent damages, and in exceptional cases may award reasonable attorneys fees to the prevailing party.[22] Post-judgment interest and most costs are awarded in accordance with non-patent law.

U.S. 867, 116 S.Ct. 184, 133 L.Ed.2d 122 (1995), *appeal after remand*, 73 F.3d 376 (Fed. Cir. 1995).

21. *See* 35 U.S.C.A. § 289. A design patent protects the non-functional aspects of an ornamental design that is shown in the patent. *See, e.g., Keystone Retaining Wall Sys., Inc. v. Westrock, Inc.*, 997 F.2d 1444, 1450 (Fed. Cir. 1993).
22. 35 U.S.C.A. § 285.

D. Limitations on Damages

Various limitations on awards of damages exist. The patent statute provides for a "running" period limiting recovery of damages to no more than 6 years before commencement of a cause of action for infringement.[23] The statute further limits recovery of past damages by providing for alternative marking and notice requirements.[24] Furthermore, the Patent Statute includes certain complex provisions relating to the Process Patent Amendments Act of 1988 that basically create a mechanism by which importers, resellers, and users can seek to determine from a patent owner, before being accused of infringement, whether an unpatented product is made in accordance with a patented process.[25] The statute also bars damages (and other remedies) with respect to a medical practitioner's performance of a medical activity that would otherwise constitute direct infringement or inducement of infringement of a patent.[26] Finally, past damages can be barred under the equitable doctrine of laches, and past and future damages can be barred under the equitable doctrine of estoppel.[27]

III. LOST PROFITS

A. Introduction to Lost Profits

The patent statute provides that a patent owner who proves infringement is entitled to damages no less than a reasonable royalty.[28] Therefore, a reasonable royalty represents the floor that the patent owner may receive in compensation for infringement of its patent; the damage award may not fall below this floor.[29] The patent owner may recover its lost profits, however, rather than a reasonable royalty, if the patent owner can prove that the infringement caused the patent owner to lose profits that it otherwise would have made.[30] Courts frequently

23. *Id.* at § 286.
24. *Id.* at § 287(a).
25. *Id.* at § 287(b).
26. *Id.* at § 287(c).
27. We will not address the equitable doctrines of laches and estoppel in this article. For more information on these doctrines, see *A.C. Aaukerman Co. v. R.L. Chaides Constr. Co.*, 960 F.2d 1020 (Fed. Cir. 1992).
28. 35 U.S.C.A. § 284.
29. *See, e.g., Rite-Hite., supra* at 1544.
30. The profits of the infringer cannot be awarded as damages except in the case of design patents. *See, e.g., Bellehumeur, supra* (unpublished opin-

refer to this "causation" element as "but for" causation; that is, the patent owner bears the burden of proving to a reasonable probability that it would have made additional profit *but for* the infringement.[31] The patent owner also bears the burden of proving the *amount* of lost profits.[32]

Because of the causation element, the general rule is that, to be entitled to lost profits, the patent owner must demonstrate that it actually competes with the infringer in the relevant market for the patented product.[33] This general rule forecloses owners of paper patents (*i.e.*, patent owners who do not manufacture or sell) from obtaining lost profits.[34] Such patent owners must settle for a reasonable royalty.

In some circumstances, however, the patent owner may be able to obtain lost profits damages even where virtually no competition exists between the patent owner and the infringer. For example, if the patent owner does not manufacture or sell the patented product, but does sell an *unpatented* product, the patent owner may be able to demonstrate that the infringement caused the patent owner to lose profits on the unpatented product.[35] In addition, patent owners with only a small share of the relevant market may nevertheless be awarded lost profits, at least in proportion to their market share.[36] The only limita-

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ion reported in Table Case Format at 104 F.3d 376 holding that it was an error of law for the district court to have awarded the infringer's profits as damages in a non-design patent case).

31. *See Minnesota Mining & Mfg. Co. v. Johnson & Johnson Orthopaedics, Inc.*, 976 F.2d 1559 1577 (Fed. Cir. 1992); *see also Gyromat Corp. v. Champion Spark Plug Co.*, 735 F.2d 549, 555 (Fed. Cir. 1984); *and King Instr. Corp. v. Otari Corp.*, 767 F.2d 853, 864 (Fed. Cir. 1985), *cert. denied,* 475 U.S. 1016, 106 S.Ct. 1197, 89 L.Ed.2d 312 (1986) (stating that reasonable probability is sufficient to prove the existence of damages and that the trial court must have reasonable flexibility in awarding lost profits).
32. *See, e.g., Smithkline Diagnostics, Inc. v. Helena Labs. Corp.*, 926 F.2d 1161, 1164 (Fed. Cir. 1991).
33. For simplicity, we will refer to patent "products" in this article, unless otherwise noted. Note, however, that the patent statute protects inventions directed to "any new and useful process, machine, manufacture, composition of matter, or any new and useful improvement thereof," subject to the other terms and conditions of the Patent Statute. *See* 35 U.S.C. § 101.
34. *See Rite-Hite*, *supra* at 1548 (stating that, "[n]ormally, if the patentee is not selling a product, by definition there can be no lost profits").
35. *See id.*
36. *Id.*

tions are that the infringement must cause the loss and that the loss must have been reasonably foreseeable.[37]

Lost profits damages frequently bring the patent owner much more than royalty awards. Indeed, a number of highly-publicized lost profits awards have exceeded $100 million.[38] This has spurred patent owners to seek lost profits in nearly every case in which the patent owner manufactures or sells *something* that could reasonably be interpreted as competing with infringer's product. Consequently, lost profits is an extremely important branch of patent damages.

B. Different Theories of Lost Profits

While the phrase "lost profits" conjures up a mental image of a singular damages claim, in reality a "lost profits" case may include several distinct types of damages. That is, a variety of theories exist under the "lost profits" umbrella, including lost sales, price erosion, collateral sales, projected (or future) lost profits, injury to goodwill and business reputation, increased expenses, and impaired growth. One problem is that too often in litigation, the damages analysis is pushed aside to the very end, even in the largest of damages cases. A patent owner, however, should be aware at the outset of what is under the "lost profits" umbrella in order to properly direct its discovery. On the other hand, the accused infringer must be aware of all relevant lost

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37. *See id.* It should be recognized at the outset that lost profits on the patent owner's lost sales of *unpatented* product, where the patent owner does not make or sell the patented product, represents perhaps the outer limits of lost profits. This extension of damages beyond the patented invention to unpatented products is controversial. While this form of lost profits is presently accepted under Federal Circuit law, individual judges of the Federal Circuit have reached opposite conclusions on this issue. *Compare id.,with* . For now, a patent owner *can* seek lost profits on the patent owner's unpatented products, even where the patent owner does not sell the patented product, provided the patent owner proves that the infringement caused the lost profits and that the losses were reasonably foreseeable. *See Rite-Hite, supra at* 1548.

38. *See, e.g,. Polaroid Corp. v. Eastman Kodak Co.*, 16 U.S.P.Q.2d 1481 (D. Mass. 1990) (awarding $873 million in damages for patent infringement, much of which was for Polaroid's lost profits), *amended on reconsideration*, 17 U.S.P.Q.2d 1711 (D. Mass. 1991) (correcting computational errors and increasing award); *see also Litton Sys., Inc. v. Honeywell, Inc.*, 87 F.3d 1559 (Fed. Cir. 1996) (affirming trial court's grant of a new trial on patent damages, where the jury had awarded $1.2 billion in lost profits damages), *vacated and remanded*, 137 L. Ed. 2d 232, 117 S. Ct. 1240 (1997).

profits theories to accurately assess its exposure and formulate a proper response for trial. Thus, taking the term "lost profits" too literally can be, and in some cases has actually been, a serious problem for both parties.[39] The term "actual damages," rather than "lost profits," is a far more accurate description of what can be sought and collected here.

1. Lost Sales and Price Erosion

The classical and most common type of "lost profits" damages are those due to lost sales.[40]. Lost sales constitute sales that the patent owner failed to make due to the infringement, as well as sales the infringer made that the patent owner would have made but for the infringement.[41] Such awards are based on a finding that the patent owner, absent the infringement, would have made all or a portion of the infringer's sales.[42] Basically, the test for determining lost sales examines what the infringer's customers would have done if the infringing product never existed. The test is very subjective.

Price erosion damages are awarded when the patent owner establishes that its sales during the infringing period were made at prices below what they would have been absent infringement.[43] Courts have awarded price erosion damages

39. For example, in *Amstar Corp. v. Envirotech Corp.*, the patentee failed to raise in a timely manner a damages theory based on lost growth. 823 F.2d 1538 (Fed. Cir. 1987). The district court excluded the theory, and, on appeal, the Federal Circuit implicitly agreed with the district court by failing to reach the merits of the lost growth issue. *Id.*
40. 5 Donald S. Chisum, PATENTS § 20.03[1][b][I] (1994). For an early Supreme Court decision on diverted sales and the causation needed to prove such damages, see *Seymour v. McCormick*, 57 U.S. 80, 16 How. 480, 14 L.Ed. 1024 (1854).
41. *See Panduit Corp. v. Stahlin Bros. Fibre Works*, 575 F.2d 1152, 1156 (6th Cir. 1978).
42. *See, e.g., Velo-Blind, Inc. v. Minnesota Mining & Mfg. Co.*, 647 F.2d 965, 974 (9th Cir. 1980), *cert denied,* 454 U.S. 1093, 70 S.Ct. 658, 70 L.Ed.2d 631 (1981).
43. In *Lam, Inc. v. Johns-Manville Corp.*, the court upheld an award of lost profits based on lost sales and price erosion. 718 F.2d 1056, 1069 (Fed. Cir. 1983). The patent owner had provided a pre-infringement growth rate in sales of its patented product and projected this rate through the infringement period. By subtracting its actual sales volume during this period from the projected amount, the patent owner arrived at a total dollar value of lost sales resulting from the infringement. The Federal Circuit Court sustained an award in the full amount lost from the infringer's sales and the patent owner's price reductions. *Id.; see also King Instr. Corp., supra* (upholding an award of lost profits based on the pat-

where the patent owner was forced to lower its prices or offer discounts to meet the infringer's competition.[44] In addition, courts award price erosion damages to compensate the patent owner where it was unable to raise its prices due to the infringement.[45]

Generally, lost sales and price erosion damages are inextricably linked.[46] In other words, they both depend on how the patent owner and infringer interact in the market. The strength of this link is evidenced by the many cases awarding the patent owner both lost sales and price erosion damages as a result of the infringement. Thus, while the lost sales and price erosion are normally evaluated separately, it is important to avoid analyzing them in isolation to prevent inconsistent results.[47]

2. *Collateral Sales*

Collateral sales is a term used to describe unpatented components or items that serve to support or reinforce the patented product as a secondary function. Collateral sales include any sales of unpatented items made concurrently with the sale of the patented product, as well as sales of unpatented items made after the initial sale of the patented product. A distinction is made between "collateral sales" and "derivative sales." Collateral sales are limited to sales of unpatented items made *concurrently* with the patented product, while derivative sales cover unpatented items (*e.g.*, spare parts) sold *after* the patented product for use with it.[48]

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ent owner's preexisting profit margin at the outset of infringement where the patent owner showed that sales and unit profits on the patented product were depressed due to the infringement).

44. *Compare Lam, supra* (lowering prices), *with TWM Mfg. Co. v. Dura Corp.*, 789 F.2d 895 (Fed. Cir. 1985), *cert. denied,* 479 U.S. 852, 107 S.Ct. 183, 93 L.Ed.2d 117 (1986) (offering discounts).
45. *See, e.g., Brooktree Corp. v. Advanced Micro Devices, Inc.*, 977 F.2d 1555 (Fed. Cir. 1992).
46. *Panduit, supra* (holding that "[t]he right to damages caused by price reduction stands on the same ground as that of damages caused by lost sales").
47. *See generally* Sumanth Addanki, ECONOMICS AND PATENT DAMAGES: A PRACTICAL GUIDE 3 (Nat'l Econ. Res. Associates, Inc. Working Paper No. 21, November 1993).
48. *Carborundum Co. v. Molten Metal Equip. Innovations*, 72 F.3d 72, 881 (Fed. Cir. 1995) (at footnote 8). Courts also refer to collateral sales as convoyed sales, auxiliary sales, accessory sales and/or spare parts. For simplicity, we will refer to all such sales as collateral sales.

The "entire market value rule" governs whether collateral sales may be included in a damage award.[49] The entire market value rule limits the inclusion of collateral sales by providing that the collateral, unpatented item must form a functional unit with the patented product; the two must function together in some manner so as to produce a desired end product or result.[50] Otherwise, the patent owner is not entitled to lost profits on the collateral, unpatented item.

3. Future Lost Profits

Projected (or future) lost profits are losses that the patent owner expects to incur in the future due to the infringement. The theory of future damages has become increasingly important, as courts not only have entertained claims of future losses, but have awarded future lost profits damages with increasing frequency.[51] The importance of future lost profits is further demonstrated by its potential for large awards, as the patent owner may be able to project substantial losses far into the future.

Future damages, however, can be the most speculative theory on which to base lost profits.[52] As a result, the courts are circumspect about awarding future lost profits damages and do so only in compelling cases, requiring the patent owner to prove its future losses with a higher degree of certainty than past losses. Thus, the patent owner must consider the unpredictability of the future when presenting its case, and the infringer should use this to its advantage in defending.

Future damages magnify the economic issues that govern lost profits calculations. It is difficult to prove with any degree of certainty that the infringer's past infringement will continue to cause damages after the infringement has ceased. Moreover, the patent owner may be hard-pressed to establish the amount of future damages, especially where the court enters a permanent injunction preventing the infringer from further sales of the infringing product. The patent owner must also consider

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49. *Rite-Hite, supra.*
50. *See id.* at 1550.
51. *See, e.g., Lam, supra; see also Minnesota Mining & Mfg., Inc. v. Johnson & Johnson Orthopaedic, Inc.*, No. 4-86-359, 1991 WL 441901 (D. Minn. April 30, 1991), *adopted in part,* 22 U.S.P.Q.2d 1401 (D. Minn. 1991), *aff'd,* 976 F.2d 1559 (Fed. Cir. 1992).
52. *Cf. Brooktree Corp. v. Advanced Micro Devices*, 977 F.2d 1555, 1581 (Fed. Cir. 1992).

that, the farther into the future it projects damages, the less likely its chances of establishing causation and the amount of lost profits. Consequently, a patent owner seeking future damages must present a compelling economic case establishing the existence and amount of future losses, or the patent owner will likely lose on this theory of lost profits.

4. Damage to Reputation and Goodwill

Another lost profits theory that patent owners have advanced, albeit infrequently, is damage to the reputation and goodwill of the patent owner and/or patented product.[53] Here, the patent owner argues that the infringer's product is inferior to the patent owner's patented product and, as a result, has caused damage to the reputation of the patented product, because the consuming public sees the two products as equivalent, or even as one-and-the-same.[54] In other words, the patent owner claims it has suffered damage because of the inferiority of the infringing product.[55]

Although discussed here as a separate "theory" of lost profits damages, proof of reputational harm generally leads to the conclusion that the patent owner lost sales or suffered reduced prices. Accordingly, in most cases, this theory will actually be an argument on which to base a claim for additional lost sales or price erosion damages.[56] This somewhat novel, unusual theory of lost profits has arisen only in limited circumstances; only a handful of cases have addressed it.[57]

5. Miscellaneous Business Damage

The patent owner can attempt to demonstrate that the infringement caused it to suffer business losses, for example, a reduction in stock prices of the patent owner's business, or an increase in the value of the infringer's business. In the right circumstances, and with adequate proof, the patent owner may

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53. *See, e.g., Lam, supra* at 1068.
54. *See id.*
55. *See id.*
56. *Cf. Minco, Inc. v. Combustion Eng'g*, 95 F.3d 1109, 1120-21 (Fed. Cir. 1996) (refusing to award goodwill damages on the ground that such damages would have constituted a double recovery relative to the reasonable royalty damages awarded by the trial court).
57. *See, e.g., Sun Prods. Corp, Inc. v. B&E Sales Co.*, 700 F.Supp. 366 (E.D.Mich. 1988).

be able to recover such losses.[58] Nevertheless, one should bear in mind that such losses are difficult to prove; many extraneous factors—such as inflation, taxes, or recessionary forces—may be found to have caused the loss or gain, and it is difficult to quantify such losses or gains.[59]

Another theory the patent owner can pursue is that the infringement caused the patent owner's stock prices to fall. This theory, however, is an unlikely winner for the patent owner due to a Federal Circuit ruling that an infringer cannot be held responsible for every conceivable harm that can be traced to an alleged wrongdoing.[60] Accordingly, lost profits based on an alleged reduction in stock prices is a highly suspect theory of lost profits, although it may prove viable in the proper factual circumstances.

C. *The Economics of Lost Profits*

Patent owners should bear in mind that proving lost profits can be complex and difficult, because an in-depth economic analysis is generally required.[61] Establishing the existence and amount of lost profits requires an economic analysis of many factors, as the revenue lost due to infringement is intrinsically economic in nature.[62] The market in which the patent owner and infringer compete must be examined in order to determine how much the patent owner lost due to the infringement.[63] Market analysis, in turn, is aided by the application of economic principles such as supply and demand and market elasticity.[64]

Thus, a patent owner's failure to account for the economics that dictate lost profits will often result in a denial of such an award, as courts have become increasingly aware of the eco-

58. *But cf. Minco, supra* at 1118-21.
59. *Cf. Id.*
60. *Rite-Hite, supra* at 1544-46 (citing a heart attack and loss in value of shares of the common stock of a corporate patent owner caused by infringement as examples of remote consequences that are not compensable).
61. *See generally* Richard T. Rapp & Phillip A Beutel, *Patent Damages: Rules on the Road to Economic Rationality*, 2 PAT. LITIG. 337 (Practicing Law Institute August 19, 1991).
62. *See id.; see also, e.g., Oiness v. Walgreen Co.*, 88 F.3d 1025, 1030 (Fed. Cir. 1996), *cert. denied,* 117 S.Ct. 951, U.S., 136 L.Ed.2d 838 (1997).
63. *See Georgia-Pacific Corp. v. United States Plywood Corp.*, 318 F. Supp. 1116 (S.D.N.Y. 1970), *modified,* 446 F.2d 295 (2nd Cir. 1970), *cert. denied,* 404 U.S. 870, 92 S.Ct. 105, 30 L.Ed.2d 114 (1971).
64. *See Oiness, supra.*

nomics underlying lost profits damages.[65] On the other hand, an infringer who fails to consider economics in formulating and presenting its damages defense will likely be rewarded with a money judgment far greater than it could have imagined.[66] This means that both the patent owner and the infringer must take care to ensure that their respective lost profits cases are well-grounded in sound economic principles.[67]

Many economic factors come into play in lost profits cases. For example, one should consider the following economic principles:

- *cost causality,* which refers to the costs incurred by the patent owner from increasing production;[68]
- *incremental profits*, a principle recognizing that, as production increases, the costs of production do not necessarily increase proportionately, especially fixed costs, which are completely paid at some point in production;[69]
- *market conditions for future damages*:
  —the future harbors many unknowns,
  —the patent owner's claim for future lost profits may not be speculative,
  —the existence of threats and opportunities in the market for the patented product must be considered in defending against a claim for lost profits;[70]
- the *law of demand and elasticity of demand*:
  —assuming the patent owner does not have a monopoly over the patented product, which is almost never the case, demand decreases as price increases;
  —depending on the product and the strength of its patent coverage, demand will vary differently in response to price fluctuations, *i.e.*, demand elasticity.[71]

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65. *Cf. id.*
66. *But cf. id.*
67. *Cf. Minco, supra* at 1118.
68. *See* Rapp & Beutel, *supra; see also Panduit, supra.*
69. *See Paper Converting Mach. Co. v. Magna-Graphics Corp.*, 745 F.2d 11, 22 (Fed. Cir. 1984).
70. *See Lam, supra.*
71. *See, e.g., BIC Leisure Prods. v. Windsurfing Int'l,* 1 F.3d 1214, 1218 (Fed. Cir. 1993) (holding that the patent owner failed to prove lost prof-

Elasticity of demand for a patented product is determined based on at least the following factors:

- the *strength* of the patent covering the patented product;[72]
- the *price to expense ratio*, *i.e.*, the ratio between the price of the patented product and the consumer's total expense budget;[73] and
- the *type* of product and the buying decision.[74]

To ensure that economics are given their due in the lost profits calculus, patent owners and infringers should strongly consider engaging an economics expert to testify on the causation issues. In addition, it is advisable to employ an accountant or financial expert to quantify the amount of lost profits in complex cases.

D. Proving Lost Profits

Assuming the patent owner accounts for the economic principles at work, it is not unduly difficult to prove lost profits. The patent owner need only demonstrate to a reasonable probability that it lost profits.[75] Then, the patent owner must provide a rea-

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its where both the patented and infringing products were sold in a market that included many products at many prices and in which demand was "relatively elastic" and "sensitive to price disparity" and further stating that, "[s]everal manufacturers offered sailboats at prices much closer to [the infringer] than to [the patent owner] . . . On this record, [the patent owner] did not show with reasonable probability that its customers would have purchased from it . . .); *see also Water Technologies Corp. v. Calco, Ltd.*, 850 F.2d 660, 673 (Fed. Cir.198), *cert. denied,* 488 U.S. 968, 109 S.Ct. 498, 102 L.Ed.2d 534 (1988) (holding that the district court erred in awarding lost profits damages when the patent owner's product differed significantly from and cost significantly more than the infringer's product); *accord* Rapp & Beutel, *supra at 349-50; and* Addanki, *supra at 9.*

72. Addanki, *supra.* His paper is useful in calculating price elasticity in a claim for lost profits due to price erosion.
73. *See id.*
74. For example, if the product is a luxury item, such as an exotic sports car, consumers can be expected to pay more for the product because they are motivated by considerations other than price. On the other hand, price is a major consideration in basic consumer products.
75. *See, e.g., Paper Converting, supra* at 21; *see also King Instr. Corp. v. Otari Corp.*, 767 F.2d 853, 863 (Fed. Cir. 1985), *cert. denied,* 475 U.S. 1016, 106 S.Ct. 1197, 89 L.Ed.2d 312 (1986).

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sonable approximation of the amount of lost profits, meaning that the amount need not be proven with unerring precision.[76] Any reasonable doubt concerning the amount of lost profits is resolved against the infringer.[77]

The courts have accepted several "methodologies" or "tests" by which to prove lost profits damages. Courts frequently recite the "but for" test when faced with a patent owner that claims it suffered lost profits.[78] As explained above, under this test, the patent owner must demonstrate that, but for the infringement, it would have made more profits than it did.[79] Courts may consider all kinds of evidence, particularly economic evidence, in determining whether the patent owner has met its burden under the but for test and whether the infringer has adequately rebutted the patent owner's showing.[80] The but for test works well when the patent owner is attempting to prove lost profits on "collateral items," *i.e.*, products that are not patented by are sold with (of after) the patented product and form a functional unit with the patented product.[81]

On its face, the "but for" test seems unlimited in breadth—*any* harm suffered by the patent owner is compensable so long as it would not have occurred but for the infringement. Yet, this test is limited in at least two ways. Even if the patent owner can prove that, absent the infringement, the patent owner would have made greater profits, injuries that are *too remote* will not be compensated.[82] Examples of injuries that are too remote for compensation are a general decline in stock prices of a patent owner corporation and the patent inventor suffering a heart attack.[83] Second, even under the "but for" test, the patent owner's lost profits must have been *reasonably foreseeable*.[84]

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76. *Compare Panduit, supra* at 1156, *with Aro II, supra, and Paper Converting, supra* at 22.
77.
78. The "but for" standard can best be understood by the way that the courts have interpreted the language of section 284. *See* 35 U.S.C.A. § 284; *see also, e.g., Rite-Hite, supra* at 1545; *and Aro II, supra.*
79. *See Rite-Hite, supra.*
80. *Compare Litton, supra, with Micro Motion, Inc. v. Kane Steel Co.*, 894 F.2d 1318, 1322 (Fed. Cir. 1990), *and Sun Prods. Group, Inc. v. B&E Sales Co.*, 700 F. Supp. 366 (E.D. Mich. 1988)
81. *See supra* Section II.B.
82. *See Rite-Hite, supra* at 1546.
83. *Id.*
84. *Id.* at 1548-49.

For example, lost sales on a product in competition with the infringing product are reasonably foreseeable.[85]

Before the advent of the Federal Circuit, the Sixth Circuit Court of Appeals articulated another methodology for proving lost profits.[86] Under the *Panduit* test, which is designed to account for market-based influences in computing lost profits, the patent owner must prove:

(1) demand for the patented product;
(2) an absence of acceptable non-infringing substitutes for the patented product;
(3) that the patent owner had the manufacturing and marketing capacity to exploit the demand; and
(4) the amount of profit the patent owner lost due to the infringement.[87]

In the past, the Federal Circuit has taken a very narrow view of what constitutes an "acceptable" legal substitute.[88] The courts have held on many occasions that the alleged substitute must possess all the technical features and advantages of the patented invention, because a product lacking the advantages of the patented invention can hardly be termed a substitute acceptable to the customer who wants those advantages.[89] This rigid standard, which requires a "technical" substitute, fails to account for the fact that consumers invariably consider a whole host of economic factors in deciding whether a "substitute" is "acceptable." Price, availability, product type, reliability of the

85. *Id.*
86. *See Panduit, supra.*
87. *See id.* Although the *Panduit* test has been widely employed by the Federal Circuit, recent decisions have begun to move away from the *Panduit* methodology. These Federal Circuit decisions generally recite the *Panduit* methodology and factors but frequently apply a different methodology to decide causation and the amount of lost profits. *See, e.g., Rite-Hite, supra; see also Kaufman Co. v. Lantech, Inc.*, 926 F.2d 1136 (Fed. Cir. 1991); *and State Inds., Inc. v. Mor-Flo Inds., Inc.*, 883 F.2d 1573, 1577 (Fed. Cir. 1989), *cert. denied,* 493 U.S. 1022, 110 S.Ct. 725, 107 L.Ed.2d 744 (1990).
88. *See, e.g., Central Soya Co. v. George A. Hormel & Co.*, 723 F.2d 1573, 1579 (Fed. Cir. 1983) (footnote 5).
89. *See, e.g., Kaufman Co. v. Lantech, Inc.,* 926 F.2d 1136, 1141 (Fed. Cir. 1991); *see also TWM Mfg. v. Dura Corp.*, 789 F.2d 895, 901 (Fed. Cir. 1986), *cert. denied,* 479 U.S. 852, 107 S.Ct. 183, 93 L.Ed.2d 117 (1986) (quoting *Panduit* and holding that "[a] product lacking the advantages of that patented can hardly be termed a substitute 'acceptable' to the consumer who wants those advantages").

product, goodwill associated with the product, the significance (or strength) of the patented invention and other economic factors guide this determination.

The Federal Circuit has recently begun to relax this rigid standard requiring "technical" substitutes and has instead recognized that consumers may accept "economic" substitutes for the patented product.[90] These are products that may lack all the technical features and advantages of the patented product, but that consumers would substitute for the patented product if the infringing product were not available.

Since *Panduit*, the Federal Circuit has accepted and extended the degree of economic analysis. The court has observed that fashioning an adequate damages award depends on the unique economic circumstances of each case.[91] It has also noted that the trial court has discretion to make subsidiary determinations in the damages trial, such as choosing a methodology to calculate damages.[92]

A modification of the *Panduit* test—the "two-supplier market" theory—holds that when the patent owner and the infringer are the only suppliers present in the market, it is reasonable to infer that the infringement probably caused the loss of profits.[93] Where a "two-supplier" market is involved, and the patent owner establishes damages under the *Panduit* stan-

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90. *Compare Radio Steel & Mfg. Co. v. MTD Prods., Inc.*, 788 F.2d 1554, 1556 (Fed. Cir. 1986); *with Smithkline Diagnostics, Inc. v. Helena Labs. Corp.*, 926 F.2d 1453, 1458 (Fed. Cir. 1991); *but see, e.g., Kaufman Co. v. Lantech, Inc.*, 926 F.2d 1136, 1142 (Fed. Cir. 1991) (holding that to qualify as an aceptable noninfringing substitute, the product must have neither a disparately higher price nor significantly different characteristics from the patented product).

91. *See, e.g., State Inds., Inc. v. Mor-Flo Inds., Inc.*, 883 F.2d 1573, 1578-80 (Fed. Cir. 1989), *cert. denied,* 493 U.S. 1022, 110 S.Ct. 725, 107 L.Ed.2d 744 (1990); *see also Uniroyal, Inc. v. Rudkin-Wiley* Corp., 939 F.2d 1540, 1545 (Fed. Cir. 1991) (stating that, "[b]ecause [the patent owner] would have possessed only eighty percent of the market, it is more appropriate to assume that [the patent owner] would have made eighty percent of [the infringer's] sales, had [the infringer] not been in the market"); *and Micro Motion, Inc. v. Kane Steel Co.*, 894 F.2d 1318, 1322 (Fed. Cir. 1990) (stating in dicta that, "[o]ther litigants have been held entitled to lost profits damages calculated on aportion of an infringer's sales based on the patentee's market share").

92. *Rite-Hite, supra.*

93. *See Kaufman, supra* at 1141; *see also Lam, supra* at 1065 (stating that causation can be inferred in a two-supplier market).

dard, the inference approaches conclusiveness.[94] Proving a "two-supplier" market is not a prerequisite, however, for proving lost profits; rather, it is merely a tool for the patent owner to lighten its burden of proving causation.[95]

Proof of a "two-supplier" market by the patent owner shifts the burden to the infringer to rebut the inference that the infringement caused the patent owner's losses.[96] To meet its burden, the infringer may submit evidence that acceptable noninfringing substitutes did, in fact, exist. The infringer may also, or alternatively, attempt to rebut the patent owner's case by submitting evidence that the patent owner's losses were due to reasons other than the infringement. For example, the infringer may attempt to demonstrate that the patent owner's own condition, such as its inability to meet demand, or other market conditions, such as a recession, caused the lost profits.

A "two-supplier" market may exist in a discrete market for a generic product or a *mini-market* for a species of a generic product.[97] For example, if the patent owner and infringer are the only manufacturers and sellers of television sets, in which televisions are the generic product, a "two-supplier" market exists.[98] On the other hand, if many competitors exist in the generic product's market, the patent owner can submit evidence to demonstrate that it and the infringer are the only manufacturers of a *species* of the generic product—*e.g.*, high-definition TVS—and that the two of them constitute a "two-supplier mini-market".

To establish a mini-market, the patent owner must prove that the patented feature gives the patented product a special market niche.[99] In this market niche, the patent owner must show that no other competitors exist, *i.e.*, that a two-supplier

94. *Kaufman, supra*; *see also Ristvedt-Johnson, Inc. v. Brandt, Inc.*, 805 F. Supp. 557, 561 (N.D. Ill. 1992) (Rader, J. sitting by designation).
95. *See BIC, supra.*
96. *Cf. id.; see also, e.g., Stndard Havens Prods. v. Gencor Indus.*, 953 F.3d 1360 (Fed. Cir. 1991), *cert. denied,* 506 U.S. 817, 113 S.Ct. 60, 121 L.Ed.2d 28 (1992); *and Yarway Corp. v. Eur-Control U.S.A., Inc.*, 775 F.2d 268, 276 (Fed. Cir. 1985).
97. *See id.*
98. *Cf. id.*
99. *See id.* at 276; *see also Marsh-McBirney, Inc. v. Montedoro-Whitney Corp.*, 882 F.2d 498, 505 (Fed. Cir. 1989) (citing *Yarway* to hold that both the patent owner's and infringer's devices occupied "a separate niche"), *vacated and remanded,* 498 U.S. 1061, 111 S.Ct. 775, 112 L.Ed.2d 838 (1991).

market exists in this mini-market.[100] The strength of the patent and the uniqueness of the patented invention both play a role in the patent owner's ability to demonstrate that a mini-market approach is appropriate. A strong patent gives the product unique and distinguishing characteristics and may thereby create a niche in the market for that product.

Another way for the patent owner to prove a two-supplier market is to demonstrate that the acceptable competitors are so insignificant based on their market share and exploitation of the patented feature that their market presence can be reasonably ignored.[101] Alternatively, the patent owner may prove a two-supplier market by showing that the supposed competitors' products lacked the critical feature of the patented item.[102]

Though an inference of causation is easier for the patent owner to establish in a two-supplier market than in a multi-supplier market, the inference is certainly not out of reach in a multi-supplier market. For example, even if acceptable substitutes do exist in the multi-supplier market, under *Panduit*, the patent owner can still use what is known as the "*market share*" method to obtain lost profits on lost sales for the patent owner's *pro rata* market share.[103] The "market share" method holds that, even if the patent owner and infringer are not the only suppliers in the market for the patented product, the patent owner may nevertheless be entitled to lost profits commensurate with its share of the multi-supplier market.[104]

Consider the following example to better understand the "market share" method. Suppose the patent product holds 20% of the market, with the remaining 80% shared by the infringing product and competing acceptable noninfringing substitutes. The patent owner will argue that, if the infringement had not occurred, it would have made a percentage of the sales of the infringing product that were made by the infringer.[105] Under the "market share" method, the patent owner may be able to prove that it is entitled its lost profits on at least 20% of the infringer's sales.[106] For the remaining infringing products sold

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100. *See Yarway, supra.*
101. *See Lam, supra.*
102. *See, e.g., TWM Mfg., supra.*
103. *See Micro Motion, supra.*
104. *Id.*
105. *See, e.g., State Inds., supra*
106. *See id.; but see Slimfold Mfg., Inc. v. Kinkead Inds., Inc.*, 932 F.2d 1453, 1458 (Fed. Cir. 1991) (stating that, "[i]n *State Industries*, we held that

by the infringer, the patent owner may seek reasonable royalty damages.[107]

Precedent exists for finding causation despite an alternative source of supply, if the source is either an infringer, a competitor that produces a noninfringing product that is an *unacceptable* alternative or a competitor that has insignificant sales.[108]

IV. THE INFRINGER'S PROFITS IN DESIGN PATENT CASES

The remedies available to utility patent owners under sections 284 and 285 are also applicable to design patent cases. Thus, a prevailing design patent owner may be awarded its lost profits or a reasonable royalty, prejudgement interest, costs, and attorney fees in exceptional cases. In addition, damages found under section 284 may be enhanced up to three times the amount found or assessed.

The provisions of 35 U.S.C. § 289 include an additional damage remedy only for infringement of design patents: the infringer's profits. Thus, section 289 provides an alternative remedy when the design patent owner's lost profits or a reasonable royalty may be difficult to prove. Importantly, the remedy is an award of profits, not damages.[109] Accordingly, an award of an infringer's profits under section 289 cannot be enhanced if willful infringement is found.[110] A design patent owner must prove lost profits or reasonable royalty damages under section 284 to be eligible for enhanced damages. However, a design patent owner cannot recover damages under section 284 plus the profits of the infringer under section 289, but must elect one of the remedies.[111]

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the *grant* of lost profits based on market share was not an abuse of discretion. However, that holding does not mean that the contrary is true, *i.e.*, that the *failure* to award lost profits based on market share *would constitute* an abuse of discretion.") (citations omitted).

107. *See State Inds., supra* at 1580-81.
108. *See id.; see also Bio-Rad Lab. v. Nicolet Instr. Corp.*, 739 F.2d 604, 616 (Fed. Cir. 1984), *cert. denied,* 469 U.S. 1038, 105 S.Ct. 516, 83 L.Ed.2d 405 (1984).
109. *See Braun, Inc. v. Dynamics Corp. of America*, 975 F.2d 815, 823 (Fed. Cir. 1992).
110. *See id.*
111. *See id.; see also Bergstrom v. Sears, Roebuck & Co.*, 496 F. Supp. 476, 496 (D. Minn. 1980).

The infringer's "total profit" means the entire profit on the sale of the article to which the patented design is applied, not just the portion of profit attributable to the design or ornamental aspects of the patent.[112] "Total profits," however, do not include profits attributable to other products that may be sold in association with an infringing article embodying the patented design.[113] A design patent owner can recover the profits not only of the manufacturer or producer of an infringing article, but also of other sellers in the chain of distribution.[114]

In determining the infringer's profits, analogous law from the area of copyrights and similar fields may be applied, along with pre-1946 utility patent law.[115] An infringer's profits generally are calculated by initially assuming that profit equals gross revenue, then deducting allowable costs. The burden of estab-

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112. *See id.* at 495.

113. *Compare Trans-World Mfg. Corp. v. Al Nyman & Sons, Inc.*, 750 F.2d 1552, 1566-68 (Fed. Cir. 1984) (holding that the use of a patented design for a display rack for eyeglasses did not permit extension of section 289 to profits on the sale of eyeglasses), *with Tone Bros. v. Sysco Corp.*, 23 U.S.P.Q.2d 1184, 1192 (S.D. Iowa 1992), *rev'd, vacated & remanded,* 28 F.3d 1192 (Fed. Cir. 1994), *cert. denied,* 115 S.Ct. 1356, 514 U.S. 1015, 131 L.Ed.2d 214 (1995). The opinion noted a factual distinction from *Trans-World* as follows:

> "This case involves the container for the goods sold - not separate goods. The court is of the opinion that 35 U.S.C. § 289 permits the recovery of a competitor's profits on goods sold in an infringing container in appropriate circumstances. If plaintiff (Tone) were to show that Sysco's profits were increased by the use of an infringing container or that Tone's profits were decreased because of the infringing container, a proper measure of damages would be established."

114. *See Bergstrom, supra* at 496; *see also L.A. Gear, Inc. v. Thom McAnn Shoe Co.*, 988 F.2d 1117 (Fed. Cir. 1993), *cert. denied,* 114 S.Ct. 291, 510 U.S. 908, 126 L.Ed.2d 240 (1993) (holding that the share of profits paid by the infringer to a non-party (K-Mart) could not be deducted from the infringer's profits; the design patent owner had agreed not to sue the non-party on the assurances of counsel for the infringer and the non-party that the infringer "could provide complete recompense.").

115. *See Schnadig Corp. v. Gaines Mfg. Co.*, 620 F.2d 1166, 1172 (6th Cir. 1980) (stating that, "[a]lthough design patent damage cases are scarce, utility patent and copyright cases provide some guidance in the treatment of fixed expenses in an award of profits."); *see also Bergstrom, supra* at 497 (stating that, "the pre-1946 case law on the subject of recovery of profits by utility patentees should be given substantial weight in the design patent context."). Awards of the infringer's profits were available in utility patent cases until they were abolished by Congress in 1946. *See Aro, supra.*

lishing the nature and amount of these costs, as well as their relationship to the infringing product, is on the infringer.[116] This approach maximizes the recovery to the design patent owner.

V. *REASONABLE ROYALTY*

A. *Introduction to Reasonable Royalty*

The patent statute authorizes only one measure of patent damages—damages adequate to compensate for the infringement.[117] The specifics of this concept, however, can be troublesome, as the patent statute contains no further guidelines, and the case law is not entirely consistent in this area. A fundamental problem that immediately arises is the existence, in reality, of *two* different definitions of the term "reasonable royalty."

The first is an actual licensing rate, to which the patent owner and a licensee would have negotiated and agreed entirely apart from any litigation or damages question. This is the "reasonable royalty" used in section 284.[118] This negotiated reasonable royalty is the *minimum* amount of patent damages the patent owner can recover, equal to what the patent owner would have negotiated as a royalty in the first place.[119]

The second meaning of "reasonable royalty" applies whenever the patent owner is unable to prove actual damages (*i.e.*, its lost profits). The money awarded the patent owner (however it is computed) is usually called a "reasonable royalty." This is also precisely where the danger lies—in taking the name for this catch-all category of patent damages too literally—because in the vast majority of damages cases today, the reasonably royalty *damages* awarded are rarely the "floor" represented by a negotiated royalty.[120] Although couched in terms of a "reason-

116. *Bergstrom, supra.*
117. 35 U.S.C. § 284.
118. "Upon finding for the [patent owner] the Court shall award the [patent owner] damages adequate to compensate for the infringement, but *in no event less than a reasonable royalty* for the use made of the invention by the infringer." *Id.* (emphasis added).
119. *See Bandag, Inc. v. Gerrard Tire Co.*, 704 F.2d 1578, 1583 (Fed. Cir. 1983); *see also Stickle v. Heublein, Inc.*, 716 F. 2d 1550, 1561 (Fed. Cir. 1983); *and Trans-World, supra* at 1568, *and Fromson v. Western Litho Plate & Supply Co.*, 853 F.2d 1568, 1574 (Fed. Cir. 1988); *and Lindemann Maschinenfabrik GmbH v. American Hoist & Derrick Co.*, 895 F.2d 1403, 1406 (Fed. Cir. 1990).
120. *See Information Resources v. Test Marketing Group*, 1993 LEXIS 34021 (Fed. Cir. 1993).

able royalty," damages awarded under section 284 are designed to compensate a patent owner for infringement of patent rights, and are *not* royalty payments at all.[121]

Many overly-optimistic infringers assume that the *maximum* amount of damages they face will be equivalent to the statutory *minimum* royalty they would have negotiated in the first place for use of the patented item.[122] Reasonable royalty damages have historically been much higher and quite often bear very little relationship to any royalty the parties would have ever agreed upon, even in the most fanciful licensing negotiation.[123] In the proper case, reasonable royalty damages can exceed what could be obtained by a lost profit analysis.

Importantly, *no* single accepted method exists for how a court must determine "reasonable royalty" *damages*.[124] In contrast to lost profits damages, the existence of infringement establishes the *fact* of reasonable royalty damages—that is,

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121. *Id.*

122. One example in a long list of such similarly ineffective damages "defenses" is found in *Bott v. Four Star Corp.*, where the infringer argued that damages of about $100,000 were proper based on the standard industry royalty rate of 3% of gross sales. 229 U.S.P.Q.2d 241 (E.D. Mich. 1985). The district court awarded damages of over $1.9 million, which included: (1) lost profits; (2) reasonable royalty at a rate of 5% (which rate the court said would have been "substantially higher" if there had been no lost profit award); (3) increased damages for willful infringement; (4) attorney fees; and (5) prejudgment interest. The award was affirmed on appeal, except for about $60,000 of the lost profits award, which was remanded for findings. *Bott v. Four Star Corp.* 807 F.2d 1567 (Fed. Cir. 1986).

123. In *TWM Mfg. Co. v. Dura Corp.*, the Federal Circuit affirmed a 30% reasonable royalty, stating that it was of little relevance that the patentee may have accepted a lesser rate as a result of actual licensing negotiations with the infringer because to do so would be "to pretend that the infringement never happened." 789 F.2d 895, 900 (Fed. Cir. 1986). In *Deere & Co. v. International Harvester Co.*, the Federal Circuit upheld a 15% reasonable royalty, even though before the infringement began, the patentee had offered a license to the infringer (under the patent in suit) at a rate of 1%. 710 F.2d 1551, 1558 (Fed. Cir. 1983). In *Bio-Rad Lab. v. Nicolet Instrument Corp.*, the Court affirmed a reasonable royalty of about 33% while royalty rates in the industry were normally between 3% and 10%. 739 F.2d 604, 617 (Fed. Cir. 1984). In *Smithkline Diagnostics, Inc. v. Helena Laboratories Corp.*, the Federal Circuit upheld a 25% reasonable royalty award, well exceeding the defendant's proposed 3% royalty. 926 F.2d 1161 (Fed. Cir. 1991),

124. *See TWM, supra* at 899 (stating that,"[s]ection 284 does not mandate how the district court must compute that figure, only that the figure compensate for the infringement.").

establishes causation. For lost profits damages, the patent owner has the burden to prove the *fact* and *amount* of damages. In contrast, for reasonable royalty damages, section 284 obviates the patent owner's burden to prove the *fact* of damage when infringement is admitted or proven.[125]

Although the *fact* of reasonable royalty damages is established by proof or admission of infringement, the patent owner must nevertheless prove the *amount* of reasonable royalty damages by relevant evidence in the record, not by pure conjecture.[126] However, the courts have recognized that a reasonable royalty analysis necessarily involves an element of approximation and uncertainty.[127] The infringer must bear the burden and the entire risk where it is impossible to make a mathematical or estimated apportionment between infringing and noninfringing items.[128] In other words, uncertainty is resolved against the infringer where the infringer's actions have caused the evidentiary imprecision.[129]

The Federal Circuit has held that the trial court's reasonable royalty rate need not be the specific figures advanced by either the patent owner or the infringer.[130] The trial court is free to reject royalty rates offered by the parties and set a different rate where the record supports the trial court's rate.[131] A primary focus of the Federal Circuit on review is not on *how* an award was computed, but rather on whether the dollar *amount* awarded "adequately compensated" the patent owner.[132]

125. *See Lindemann, supra* at 1407.
126. *See Unisplay S.A. v. American Elec. Sign Co.*, 69 F.3d 512, 517 (Fed. Cir. 1995).
127. *See id.*
128. *See Nickson Inds., Inc. v. Rol Mfg. Co.*, 847 F.2d 795, 799 (Fed. Cir. 1988) (holding that the lower court did not commit reversible error where a document prepared by the infringer supported a reasonable approximation of non-infringing sales).
129. *Cf. id.*
130. *SmithKline, supra* at 1168.
131. *See id.* (affirming the trial court's determination of a 25% royalty rate where the patent owner had sought 48% as opposed to 3% proposed by the infringer).
132. *See, e.g., TWM, supra.*

B. Methods for Determining Reasonable Royalties: The Analytical Approach and the Hypothetical License Negotiation

One approved method of arriving at reasonable royalty *damages* is called the "analytical approach," which, in reality, has nothing at all to do with any hypothetical licensing negotiation. Essentially, in one form, this approach involves calculating damages based on the infringer's own internal profit projections for the infringing item at the time the infringement began, and then apportioning the projected profits between the patent owner and the infringer. The projected profits are then applied to the actual infringing sales to determine the total "reasonable royalty" damages. A proper response involves the infringer attacking its own internal documents.[133] The infringer, however, cannot rely on the fact that its actual profits were less than the projected ones.[134]

The second approved method of determining reasonable royalty damages is, of course, the more familiar hypothetical license negotiation, often called the "willing licensor-willing licensee" approach. In the pre-Federal Circuit days, this approach sometimes resulted in damages being set at the statutory minimum—the actual royalty rate the patent owner and the infringer would have mutually agreed upon had they negotiated a patent license at the outset of the infringement.[135] Today, that is far less likely, although certain exceptions exist.

The seminal case of *Georgia-Pacific Corp. v. United States Plywood Corp.*[136] described the hypothetical license negotiation as more of a statement of approach than a tool of analysis. The Federal Circuit has characterized the "willing licensor" fiction

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133. *See, e.g., Hughes Tool Co. v. Dresser Inds., Inc.*, 816 F.2d 1549, 1556-57 (Fed. Cir. 1987), *cert. denied,* 108 S.Ct. 261, 484 U.S. 914, 98 L.Ed.2d 219 (1987); *but see TWM, supra* at 899 (rejecting the infringer's argument that the much lower actual profits it actually realized on the infringing products, rather than its pre-infringement memorandum, was the proper framework for determining reasonable royalty damages).
134. *See id.*
135. *See, e.g., Goodyear Tire & Rubber Co. v. Overman Cushion Tire Co.*, 95 F.2d 978, 984 (6th Cir. 1937), *cert. dism'd,* 59 S.Ct. 459, 306 U.S. 665, 83 L.Ed. 1061 (1939); *see also Rockwood v. General Fire Extinguisher Co.*, 37 F.2d 62, 66 (2nd Cir. 1930), *cert. denied,* 46 S.Ct. 26, 269 U.S. 571, 70 L.Ed. 417 (1935).
136. 318 F. Supp. 1116, 1121 (S.D.N.Y. 1970), *aff'd as mod.*, 446 F.2d 295 (2nd Cir. 1971), *cert. denied*, 92 S.Ct. 105, 404 U.S. 870, 30 L.Ed.2d 114 (1971).

as an absurd characterization of the determination when the parties were previously unable to come to an agreement.

The chief danger in the "willing licensor-willing licensee" approach, particularly for the infringer, is taking the name too literally, and building a damages defense around a very low, actual royalty rate the parties might have negotiated in the real world.[137] Reasonable royalty *damages* can be far different from any pre-infringement, real-world royalty the parties would have actually negotiated.[138] Indeed, the Federal Circuit has routinely affirmed "reasonable royalty" awards that are obviously well in excess of what the parties would have actually agreed to as a result of licensing negotiations prior to infringement.[139] Thus, it appears exceedingly unwise for an infringer to base its damages defense on a strict application of the "willing licensor-willing licensee" fiction, with the mistaken belief that such a presentation will increase the infringer's chances of limiting the damages award.[140]

C. *Factors Relevant to the Hypothetical License Negotiation Method*

The fictional willing licensor-willing licensee negotiation is analyzed as of the date the infringement began.[141] The negotiation requires that the royalty rate be determined on the assumption that the patent was valid and infringed.[142] The courts

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137. The basic framework of this approach includes the significant proviso that, in the context of these fictional negotiations, both parties are assumed to agree that the patent in question is valid and would be respected by the infringer (not used if licensed). *See Trio Process Corp. v. L. Goldstein's Sons, Inc.*, 533 F.2d 126, 129 (3rd Cir. 1976). It is notable (but often overlooked) that such preconditions hardly ever exist in any actual license negotioations.
138. *Cf. Panduit, supra; see also, e.g., Stickle, supra.*
139. *See, e.g., Deere & Co. v. International Harvester Co.*, 710 F.2d 1551, 1554-58 (Fed. Cir. 1983).
140. There are only a few cases where the Federal Circuit has affirmed any reasonable royalty rates which appear to be close to a negotiated rate. *See, e.g., American Orig, Corp. v. Jenkins Food Corp.*, 774 F.2d 459 (Fed. Cir. 1985) (panel failed to note either *Panduit* or *Stickle.*)
141. *See, e.g., TWM, supra* at 899-900; *see also Panduit, supra* at 1158-59 (stating that, "[t]he key element in setting a reasonable royalty after determination of validity and infringement is the necessity for return to the date when the infringement began.").
142. *See, e.g., Trio, supra* at 129; *see also TP Orthodontics, Inc. v. Professional Positioners, Inc.*, 20 U.S.P.Q.2d 1017, 1025 (E.D. Wisc. 1991) (stating that, "[a]ny negotiation is based on the assumption that the pat-

may, however, consider evidence of events subsequent to the onset of infringement, in order to compensate for the difficulties and uncertainties in recreating the hypothetical negotiations.[143]

Almost always, a damages analysis using a hypothetical license negotiation will be based, at least in part, on the royalty factors set forth in the *Georgia-Pacific* case.[144] The district court itemized fifteen factors for use in determining a reasonable royalty under the "willing licensor-willing licensee" method. These factors have been used, or at least acknowledged, by many other courts, including the Federal Circuit as follows:

(1) the royalties received by the patent owner for the licensing of the patent in suit, proving or tending to prove an established royalty;

(2) the rates paid by the licensee for the use of other patents comparable to the patent in suit;

(3) the nature and scope of the license, as exclusive or non-exclusive; or as restricted or non-restricted in terms of territory or with respect to whom the manufactured product may be sold;

(4) the licensor's established policy and marketing program to maintain his patent monopoly by not licensing others to use the invention or by granting licenses under special conditions designed to preserve that monopoly;

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ent was valid and infringed."); *and Syntex (U.S.A.), Inc. v. Paragon Optical, Inc.*, 7 U.S.P.Q.2d 1001, 1027 (D. Ariz. 1987) (stating that, "[i]n setting the stage for the hypothetical negotiations, the patent is presumed valid and infringed."); *and Alpex Computer Corp. v. Nintendo Co.*, 34 U.S.P.Q.2d 1167, 1199 (S.D.N.Y. 1994), *aff'd in part & rev'd in part*, 102 F.3d 1214 (Fed. Cir. 1996).

143. *See, e.g., Sinclair Refining Co. v. Jenkins Petroleum Co.*, 289 U.S. 689, 697-99 (1933); *see also Fromson v. Western Litho Plate & Supply Co.*, 853 F.2d 1568, 1575 (Fed. Cir. 1988) (stating that, "[t]he [hypothetical negotiations] methodology encompasses fantasy and flexibility; fantasy because it requires a court to imagine what warring parties would have agreed to as willing negotiators; flexibility because it speaks of negotiations as of the time infringement began, yet permits and often requires a court to look to events and facts that occurred thereafter and that could not have been known to or predicted by the hypothesized negotiators."); *and Studiengesellschaft Kohle, m.b.H v. Dart Inds., Inc.*, 862 F.2d 1564, 1571-72 (Fed. Cir. 1988) (quoting *Fromson*).

144. 318 F. Supp. at 1120.

(5) the commercial relationship between the licensor and the licensee, such as, whether they are competitors in the same territory in the same line of business; or whether they are inventor and promoter;

(6) the effect of selling the patented specialty in promoting sales of other products of the licensee; the existing value of the invention to the licensor as a generator of sales of his non-patented items; and the extent of such derivative or convoyed sales;

(7) the duration of the patent and the term of the license;

(8) the established profitability of the product made under the patent, its commercial success and current popularity;

(9) the utility and advantages of the patent property over the old modes or devices, if any, that had been used for working out similar results;

(10) the nature of the patented invention, the character of the commercial embodiment of it as owned and produced by the licensor and the benefits to those who have used the invention;

(11) the extent to which the infringer has made use of the invention and any evidence probative of the value of that use;

(12) the portion of the profit or of the selling price that may be customary in the particular business or in comparable businesses to allow for the use of the invention or analogous inventions;

(13) the portion of the realizable profit that should be credited to the invention as distinguished from non-patented elements, the manufacturing process, business risks, or significant features or improvements added by the infringer;

(14) the opinion testimony of qualified experts; and

(15) the amount that a licensor (such as the patent owner) and a licensee (such as the infringer) would have agreed upon (at the time the infringement began) if both had been reasonably and voluntarily trying to reach an agreement; that is, the

> amount which a prudent licensee—who desired, as a business proposition, to obtain a license to manufacture and sell a particular article embodying the patented invention—would have been willing to pay as a royalty and yet be able to make a reasonable profit and which amount would have been acceptable by a prudent patent owner who was willing to grant a license.[145]

These factors do not have equal weight.[146] While the Federal Circuit has specifically affirmed reasonable royalty awards determined on the basis of the *Georgia-Pacific* factors, it has been particularly interested in one factor, while virtually disregarding the two most often heavily relied upon by infringers.[147]

The factor to which the Federal Circuit has paid considerable attention, and which has a very significant impact on the amount of reasonable royalty damages, is the ability of the patented product to help promote the sales of collateral, non-patented items.[148] It is well settled that if the patented item increases the sales of non-patented collateral items, the reasonable royalty rate not only may increase, but may exceed both the expected profits on the infringing item itself and its sale price as well.[149]

Another important *Georgia-Pacific* factor is the existence of an established royalty in the industry for the patent in suit. Where there is an established royalty for the patent in suit, that royalty will usually be adopted as the best measure of reasonable and entire compensation.[150] An asserted established royalty rate, however, must have been paid by such a number of persons as to indicate a general acquiescence in its reasonable-

145. *Georgia-Pacific, supra* at 1119-20.

146. *See id.* at 1120.

147. *See, e.g., Railroad Dynamics, Inc. v. A. Stucki Co.*, 727 F.2d 1506, 1518 (Fed. Cir. 1984), *cert. denied*, 105 S.Ct. 220, 469 U.S. 871, 83 L.Ed.2d 150 (1984); *see also Hanson v. Alpine Valley Ski Area, Inc.*, 718 F.2d 1075, 1077 (Fed. Cir. 1983); *and SmithKline, supra* at 1168.

148. *See, e.g., Deere, supra* at 1558-59; *see also Radio Steel & Mfg. Co. v. MTD Prods, Inc.*, 788 F.2d 1544, 1556-57 (Fed. Cir. 1986).

149. *See Rite-Hite, supra* at 1555.

150. *See Tektronix, Inc. v. United States*, 552 F.2d 343, 347 (Ct. Cl. 1977); *see also Nickson Inds., Inc. v. Rol Mfg. Co.*, 847 F.2d 795, 798 (Fed. Cir. 1988) (affirming the trial court's award of an 8.8% royalty rate, which was the rate paid by the patent owner's licensees under the patent in suit).

ness.[151] Consequently, the touchstone for established royalty is really whether the industry *generally accepts* a particular rate for the patent in suit. One license is not enough, and mere offers to license do not indicate general industry acceptance.[152] Indeed, even if many such licensees for the patent in suit exist, they still may not set a damages royalty rate if widespread infringement made the established rate artificially low.[153] This principle works both ways: a patent owner cannot try to prove a high "established" royalty merely by its high licensing *offers*.[154]

Licenses negotiated to settle actual or threatened litigation may not be relevant to establishing a royalty rate, because the licensee's desire to avoid litigation costs may have more heavily influenced the royalty rate than the actual value of the patented invention.[155] On the other hand, licenses negotiated to settle a case after a court has established validity and infringement of the patent are very probative of reasonable royalty.[156] Such licenses duplicate the analytical process undertaken by the court in setting reasonable royalty damages in the willing licensor-willing licensee fictional negotiation.[157]

The existence of an established royalty generally sets the *minimum* recovery, below which the reasonable royalty rate cannot fall.[158] The patent owner is best served, in proper cir-

151. *Hanson, supra* at 1078 (quoting *Rude v. Westcott,* 9 S.Ct. 463, 130 U.S. 152, 165, 32 L.Ed. 888 (1889)).
152. *Compare id., with Deere & Co. v. International Harvester Co.,*710 F.2d 1555, 1557 (Fed. Cir. 1983), *Trell v. Marlee Electronics Corp.,* 912 F.2d 1443, 1446 (Fed. Cir. 1990), *and Stickle, supra* at 1561.
153. *See Nickson, supra* at 798.
154. *See American Original Corp. v. Jenkins Food Corp.,* 774 F.2d 459, 464 (Fed. Cir. 1985).
155. *See Panduit, supra* at 1164 (footnote 11). A licensing rate may also be considered irrelevant on this issue if the amount received was in any way speculative. *Hanson, supra* at 1078. In addition, the licensing rate may be irrelevant if the value of the patent appeared at the time to be somewhat speculative. *Deere, supra* at 1557.
156. *See, e.g., Snellman v. Ricoh Co.,* 862 F.2d 283, 289 (Fed. Cir. 1988), *cert. denied,* 109 S.Ct. 3199, 491 U.S. 910, 105 L.Ed.2d 707 (1989).
157. *See, e.g., Studiengesellschaft Köhle v. Dart Inds, Inc.,* 862 F.2d 1564 (Fed. Cir. 1988).
158. *See, e.g., Russell Box Co. v. Grant Paper Box Co.,* 203 F.2d 177, 182-83 (1st Cir. 1953) (stating that the lower court was "fully justified in refusing to put [the infringer] in a more favorable position than [the patent owner's] licensees."); *see also B&H Mfg., Inc. v. Foster-Forbes Glass Co.,* 26 U.S.P.Q.2d 1066, 1070 (S.D. Ind. 1993) (stating that prior licenses were "useful to the jury for the purpose of establishing a damages floor"); *and Syntex (U.S.A.) Inc. v. Paragon Optical, Inc.,* 7 U.S.P.Q.2d

cumstances, by establishing an existing royalty rate for the patent in suit but then seeking to prove that this rate is lower than a reasonable rate. The patent owner may accomplish this goal by showing that (1) the licenses were offered against a backdrop of threatened or ongoing infringement litigation[159] or (2) the license rates were depressed by widespread infringement and defiance or disrepute of the patents.[160]

Courts have given weight to licensing practices in the relevant industry in determining a reasonable royalty, such as whether a royalty would have been negotiated based on the use of a patented machine or based on a lump sum.[161] However, while industry licensing practices may help structure reasonable royalty damages, industry licenses for *other* patents are rarely probative in establishing a royalty *rate* for damages for the patent in suit.[162]

Courts have also considered the commercial relationship between the patent owner and infringer in determining a reasonable royalty measure of damages. If the patent owner and infringer are competitors and the patent owner had the capacity to make the infringing sales, the patent owner clearly holds more bargaining power than if the two parties were not competitors.[163] Thus, in cases involving competitors, one should expect the negotiated royalty rate to be higher.[164]

1001k, 1040 (D. Ariz. 1987) (stating that, "[a]lthough pre-existing royalty rates are evidence of a reasonable royalty, the law is explicit that prior royalty rates establish only a minimum floor below which reasonable royalty damages cannot fall.").

159. *See, e.g., Hanson, supra* at 1078-79; *see also Alpex Computer Corp. v. Nintendo Co.,* 1994 WL 139423 at 8 (S.D.N.Y. 1994) (stating that, "[c]ourts have cautioned . . . that licenses offered or granted against a backdrop of ongoing infringement and litigation should be given little weight in determininga reasonable royalty."), *aff'd in part, rev'd in part,* 102 F.3d 1214 (Fed. Cir. 1996).

160. *See, e.g., Fromson, supra* at 1577 (footnote 15); *see also Tights, Inc. v. Kayser-Roth Corp.,* 442 F. Supp. 159, 164-65 (D.N.C. 1977).

161. *See, e.g., Stickle, supra* at 1562-63.

162. *See, e.g., Railroad Dynamics, Inc. v. A. Stucki Co.,* 727 F.2d 1506, 1518 (Fed. Cir. 1984), *cert. denied,* 105 S.Ct. 220, 469 U.S. 871, 83 L.Ed.2d 150 (1984); *see also Bio-Rad Lab. v. Nicolet Instrument Corp.,* 739 F.2d 604, 617 (Fed. Cir. 1984), *cert. denied,* 105 S.Ct. 516, 469 U.S. 1038, 83 L.Ed.2d 405 (1984).

163. *See Panduit, supra* at 1163 (citing *Egry Register Co. v. Standard Register Co.,* 23 F.2d 438, 443 (6th Cir. 1928)).

164. *See id.*

The patent owner's licensing policy may also play a role in the "willing-licensor, willing-licensee" fictional negotiation. For example, the patent owner may have a policy of not licensing the patent in suit and thus would not have been a willing licensor at the time of the infringement. This would mean that the infringer would have had to pay a higher royalty rate to induce the patent owner to license the patent than if the patent owner were a willing licensor.[165]

In determining a reasonable royalty under section 284, the courts have continually considered the patent owner's established profitability for the patented item—unlike that of the infringer—to be an important factor.[166] Hence, a patent owner with a high profit margin for the patented item is better off for damages purposes than the patent owner with a marginally profitable item.[167]

Directly related to profitability is a factor most usually associated with lost profits—the presence or absence of non-infringing substitutes for the patented item. In the past, courts have concluded that the existence of non-infringing substitutes reduces a reasonable royalty.[168] While this conclusion remains true today, it must be qualified somewhat. It now appears that the critical legal definition of just what is an "acceptable" substitute for this purpose is a narrow one, since a product lacking the advantages of the patented invention can hardly be termed a substitute acceptable to the customer who wants those advantages.[169] Consequently, the infringer's view of the "acceptable noninfringing substitute" at the time infringement began—not when the infringement was discovered—is particularly important in determining a reasonable royalty.[170]

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165. *See id.* at 1163-64; *see also Georgia-Pacific, supra* at 1127.
166. Many infringers still appear to take delight in proving that they lost money selling the infringing products. Unfortunately for them, however, the infringer's lack of actual profits has not been considered to be probative on this issue. *See, e.g., Deere, supra* at 1558.
167. *Cf. id.*
168. *See, e.g., Hughes Tool Co. v. G.W. Murphy Inds., Inc.,* 491 F.2d 923, 930-31 (5th Cir. 1973).
169. *See, e.g., Panduit, supra* at 1162.
170. *See, e.g., Deere, supra* at 1558.

VI. *PRE-JUDGMENT INTEREST*

Pre-judgment interest is *routinely* awarded on damages in almost all patent cases.[171] As a practical matter, the only significant factor that will work to reduce or limit pre-judgment interest may be the patent owner's delay in bringing suit or prosecuting the case.[172]

In lost profit cases, pre-judgment interest is limited to past or present lost profits.[173] Pre-judgment interest has no punitive, but only compensatory, purposes. Hence pre-judgment interest cannot be applied to future lost profits, or to the punitive or enhanced portion of a damage award.[174] On the other hand, district courts have inherent equitable authority, in cases of "bad faith or other exceptional circumstances," to award pre-judgment interest on the unliquidated sum of an award of attorneys' fees.[175]

As an element of damages, the patent owner bears the burden of proving the applicable interest rate for pre-judgment interest.[176] A decision to award[177] or not to award[178] pre-judgment interest will only be set aside if the decision constitutes an abuse of discretion.

Pre-judgment interest is computed from the date of injury to the date of judgment.[179] The selection of an applicable interest rate is left to the sound discretion of the trial court and is rarely overturned on appeal.[180] The prime rate is the most com-

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171. *General Motors Corp. v. Devex Corp.*, 461 U.S. 648, 76 L.Ed.2d 211, 103 S.Ct. 2058 (1983).
172. *Id.* at 655-657. The District Court had orginally entered judgment awarding Devex $ 8,813,945.50 in royalties and $ 11,022,854.97 in pre-judgment interest. *Devex Corp. v. General Motors Corp.*, 494 F.Supp. 1369 (D. Del. 1980).
173. *Oiness v. Walgreen Co.*, 88 F.3d 1025, 1033 (Fed. Cir. 1996).
174. *Underwater Devices, Inc. v. Morrison-Knudsen Co.*, 717 F.2d 1380, 1389 (1983); *see also Lam, Inc. v. Johns-Manville Corp.*, 718 F.2d 1056, 1066 (Fed. Cir. 1983); *and Beatrice Foods Co. v. New England Printing & Lithographing Co.*, 923 F.2d 1576 (Fed. Cir. 1991).
175. *Mathis v. Spears*, 857 F.2d 749, 760-761 (Fed. Cir. 1988).
176. *Lam, supra* at 1066.
177. *General Motors Corp. v. Devex Corp.*, 461 U.S. 648, 76 L.Ed.2d 211, 103 S.Ct. 2058 (1983).
178. *Hughes Tool Co. v. Dresser Industies, Inc.*, 816 F.2d 1549 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 914, 98 L.Ed.2d 219, 108 S.Ct. 261 (1987).
179. *Bio-Rad, supra* at 969 (Fed. Cir. 1986).
180. *See, e.g., Gyromat Corp. v. Champion Spark Plug Co.*, 735 F.2d 549, 556-557 (Fed. Cir. 1984); *see also Kaufman Co. v. Lantech, Inc.*, 807 F.2d 970, 978-979 (Fed. Cir. 1986).

mon candidate for an appropriate interest rate, but a higher rate may be used if based on a proper evidentiary showing.[181] The interest rate need not be a constant applied to the entire pre-judgment interest period; a variable interest rate derived from a particular rate measure may be applied.[182] The Federal Circuit has approved both simple interest[183] and compound interest.[184] In several cases, the Court has indicated that compound interest is fairer and assures that the patent owner is fully compensated.[185]

VII. COSTS

Costs in patent suits are nominally covered by section 284. This provision applies *only*, however, to successful patent owners to whom damages have been awarded for patent infringement. In cases where the alleged infringer prevails, the general provision of the Federal Rules of Civil Procedure governs.[186] The primary difference between section 284 and the Federal Rules is that section 284 requires the district court to refer to Federal Circuit precedent for the bounds of the district court's discretion, whereas an award for costs under the Federal Rules is governed by general federal procedural law.[187] As a practical matter, however, this distinction seems to make no substantial difference in how courts award costs.[188]

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181. *See, e.g., Lam, supra* at 1066 ("Once the claimant has affirmatively demonstrated that a higher rate should be used, . . . the district court may fix the interest at that higher rate."); *see also Bio-Rad, supra* at 969 ("the only evidence in the record relating to the appropriate rate of interest suggests the use of either the prime rate or the rate that Bio-Rad paid on its corporate borrowings during the period of infringement. "); *and Uniroyal Inc. v. Rudkin-Wiley Corp.*, 939 F.2d 1540 (Fed. Cir. 1991) ("A trial court . . . may award interest at or above the prime rate.").
182. *Scott Paper Co. v. Moore Business Forms, Inc.*, 594 F. Supp. 1051, 1083 (D. Del. 1984), *supplemental op., mot. denied*, 604 F. Supp. 835 (D. Del. 1984).
183. *Gyromat Corp. v. Champion Spark Plug, Co.*, 735 F.2d 549 (Fed. Cir. 1984).
184. *Railroad Dynamics, Inc. v. A. Stucki Co.*, 727 F.2d 1506 (Fed. Cir. 1984), *cert. denied*, 469 U.S. 871, 83 L.Ed. 2d 150, 105 S.Ct. 220 (1984).
185. *See, e.g., Dynamics Corp. of America v. United States*, 766 F.2d 518, 520 (Fed. Cir. 1985); *see also Fromson, supra* at 1862; *and Rite-Hite, supra* at 1555.
186. FED. R. CIV. P. 54(d).
187. *Delta-X Corp. v. Baker Hughes Production Tools, Inc.*, 984 F.2d 410, 414 (Fed. Cir. 1993).
188. *Compare General Motors, supra* (pre-judgment interest should ordinarily be awarded to a successful claimant under § 284).

As an element of damages, it appears that the patent owner bears the burden of proving the amount of costs under section 284.[189] The burden is on the prevailing alleged infringer for costs awarded under the Federal Rules. Proof generally requires that detailed records be maintained throughout the litigation proceedings.

With the exception of expert witness fees, little significant case law has developed relating to any special issues involving the application of section 284 or the Federal Rules to awards of costs in patent cases.[190] The specific procedure relating to submission of a bill of costs is generally determined by local court rules. In general, the award of costs can include any disbursement incurred by the prevailing party from the time the case was filed through trial. Of course, the district court has discretion to reject any element of costs submitted by the prevailing party.

VIII. POST-JUDGMENT INTEREST

The standard for post-judgment interest in all federal civil cases is defined by federal law,[191] which provides for mandatory interest on any money judgment recovered in a district court.[192] The applicable rate is based on the price of certain U.S. treasury bills. Interest generally is computed daily to the date of payment, and is compounded annually. Interest on an award—including attorneys' fees—runs from the date of the judgment establishing the right to the award, not the date of the judgment establishing the amount of the award.

IX. ENHANCEMENT OF DAMAGES—WILLFUL INFRINGEMENT

A. The Punitive Nature of Enhanced Damages and the District Court's Discretion

The provisions of section 284 provide that a court may increase damages up to three times the amount found or assessed.

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189. *Cf. Lam, supra* at 1066.
190. *See, e.g., Manildra Milling Corp. v Ogilvie Mills*, 76 F3d 1178 (Fed. Cir. 1996) (discussing allowable items of costs pursuant to regional circuit law); *see also* LAURA B. BARTELL, *Taxation of Costs and Awards of Expenses in Federal Court*, 101 F.R.D. 553, 567 (1984).
191. 28 U.S.C.A. § 1961.
192. *Goodwall Constr. Co. v. Beers Constr. Co.*, 991 F.2d 751, 759 (Fed. Cir. 1993); *see also Mathis v. Spears*, 857 F.2d 749, 760 (Fed. Cir. 1988).

Only damages awarded under section 284 may be enhanced. Hence, a court may not enhance an award of attorney fees under section 285 or of the infringer's profits in design patent cases under section 289.[193]

The Federal Circuit has approved enhanced damages where the infringer acted in wanton disregard of the patent owner's patent rights, that is, where the infringement was "willful."[194] While some opinions have referred to awarding enhanced damages for bad faith litigation,[195] recently the Federal Circuit has held that "'bad faith' is more correctly called 'bad faith infringement,' and it is merely a type of willful infringement."[196]

The statute recognizes the tortious nature of patent infringement and the public interest in a stable patent right: Enhanced damages are not compensatory, but rather punitive.[197] Thus, enhanced damages may not be awarded as additional compensatory damages; a court must find that the conduct of the infringer was egregious.[198]

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193. Attorney's fees awarded are not damages, but rather compensation awarded in exceptional cases for a "cost" of litigation. *See Braun, Inc. v. Dynamics Corp. of America*, 975 F.2d 815, 823 (Fed. Cir. 1992) (addressing the impropriety of enhancing an award of the infringer's profits in a design patent case).

194. *SRI Int'l v. Advanced Tech. Lab.*, 127 F.3d 1462 (Fed. Cir. 1997); *see also Read Corp. v. Portec, Inc.*, 970 F.2d 816, 826 (Fed. Cir. 1992); *and Stickle v. Heublein, Inc.*, 716 F.2d 1550, 1565 (Fed. Cir. 1983) ("The court must determine that the infringer acted in disregard of the patent, that is, that the infringer had no reasonable basis for believing it had the right to do the acts.").

195. *State Industries, supra* at 1577; *see also Beatrice Foods Co. v. New England Printing & Lithographing Co.*, 923 F.2d 1576, 1578-79 (Fed. Cir. 1991).

196. *Jurgens v. CBK, Ltd.*, 80 F.3d 1566, 1570-1571 (Fed. Cir. 1996); *see also Read Corp. v. Portec, Inc.*, 970 F.2d 816, 826 (Fed. Cir. 1992):

> As indicated, bad faith behavior as a party to the litigation is a factor to be weighed in assessing the level of a defendant's culpability where an infringement is found willful. While dicta suggest that infringement damages may be enhanced *solely* by reason of misconduct during litigation, . . . such dictum is contrary to our precedent that 'if infringement [is] . . . innocent, increased damages are not awardable for the infringement.'

197. *SRI Int'l v. Advanced Tech. Lab.*, 127 F.3d 1462 (Fed. Cir. 1997).

198. *See, e.g., Beatrice Foods, supra* (award of enhanced damages reversed; "[e]nhanced damages may be awarded only as a penalty for an infringer's increased culpability, namely willful infringement or bad faith. Damages cannot be enhanced to award the patentee additional compen-

The permissive language of the statute makes an award of enhanced damages discretionary rather than mandatory.[199] A finding of willful infringement does not mandate that damages be enhanced, much less mandate treble damages.[200] Instead, an award of enhanced damages for infringement, as well as the extent of the enhancement, from zero to three times the amount of actual damages, is committed to the discretion of the trial court.[201] A significant factor in determining the extent of the enhancement is the infringer's size and financial condition.

Thus, the decision to increase damages has been recognized to be a two-step process:[202]

- the fact-finder must determine whether an infringer is guilty of conduct upon which increased damages may be based—that is, whether the infringement was willful;
- if the fact-finder determines that willful infringement is proven, the court then determines whether, and to what extent, to increase the damages award given the totality of the circumstances. The court determines the amount of an enhanced damage award, which may be based on a jury verdict of willfulness.[203]

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sation to rectify what the district court views as an inadequacy in the actual damages awarded.").

199. *State Industries, supra* at 1576.

200. *Read Corp., supra* at 826; *see also Modine Mfg. Co. v. Allen Group, Inc.*, 917 F.2d 538, 543 (Fed. Cir. 1990), *cert. denied*, 500 U.S. 918, 114 L.Ed. 2d 103, 111 S. Ct. 2017 (1991).

201. *Read Corp., supra*; *see also CPG Products Corp v. Pegasus Luggage, Inc.*, 776 F.2d 1007, 1015 (Fed. Cir. 1985) (reversing finding of no willfulness); *and Kloster Speedsteel AB v. Crucible Inc.*, 793 F.2d 1565, 1579 (Fed. Cir. 1986) (reversing finding of no willfulness).

202. *State Industries, supra* at 1576; *see also Jurgens v. CBK, Ltd.*, 80 F.3d 1566 (Fed. Cir. 1996); *and Code-Alarm, Inc. v. Electromotive Techs. Corp.*, 1997 LEXIS 13031 (Fed. Cir. 1997) (reported in Table Case Format at 114 F.3d 1206).

203. *Shiley, Inc. v. Bentley Laboratories, Inc.*, 794 F.2d 1561, 1567-1568 (Fed. Cir. 1986), *cert. denied*, 479 U.S. 1087, 94 L.Ed. 2d 148, 107 S. Ct. 1291 (1987) (noting that the jury verdict is not "advisory" with respect to findings of fact, but that a jury verdict of willfulness does not mandate an award of attorney fees, which are in the court's discretion.).

A patent owner must prove willful infringement—a question of fact—by clear and convincing evidence.[204] Once a finding of willfulness has been made, the decision to award or deny enhanced damages, and the amount of such damages, is made by the district court.[205] To enable appellate review, a district court is obligated to explain the basis for the award, particularly where the maximum amount is imposed. For a maximum amount, the court's assessment of the level of culpability must be high.[206] On appeal, the court's decision to enhance damages and the extent of the enhancement will be overturned only if the Federal Circuit rules that the decision was an abuse of discretion.[207]

B. Defending a Charge of Willfulness: The Infringer's Good Faith and Advice of Counsel

The paramount determination in deciding to grant enhancement and in determining the amount of enhancement is the egregiousness of the defendant's conduct based on all the facts and circumstances. The court must consider factors that render an infringer's conduct more culpable, as well as factors that are mitigating or ameliorating.[208] The basic test for willfulness is whether a prudent person would have had sound reason to believe that a patent was not infringed or was invalid or unenforceable, and would be so held if litigated.[209]

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204. *Stryker Corp. v. Intermedics Orthopedics*, 96 F.3d 1409, 1413 (Fed. Cir. 1996); *see also Pall Corp. v. Micron Separations.*, 66 F.3d 1211, 1221 (Fed. Cir. 1995); *and Gustafson, Inc. v. Intersystems Industrial Products, Inc.*, 897 F.2d 508, 510-511 (Fed. Cir. 1990); *and Power Lift, Inc. v. Lang Tools, Inc.*, 774 F.2d 478, 482 (Fed. Cir. 1985).
205. *Graco, Inc. v. Binks Mfg. Co.*, 60 F.3d 785, 792 (Fed. Cir. 1995).
206. *Read Corp., supra* at 828.
207. *Graco, supra.*
208. *Compare Ivac Corp. v. Terumo Corp.*, 18 USPQ2d 1637, 1639-1640 (S.D. Cal. 1990) (holding that treble damages are appropriate when it is clear that defendant showed no good faith at the time infringement commenced, made no effort to follow the advice of patent counsel or alter the infringing device, and showed bad faith in litigation.); *with Datascope Corp. v. SMEC, Inc.*, 14 USPQ2d 1071, 1074 (D. N.J. 1990) ("[a] fifty-percent enhancement of damages is appropriate here. Although SMEC's infringement was willful, it was not blatant."); *and Chisum v. Brewco Sales & Mfg., Inc.*, 726 F. Supp. 1499 (W.D. Ky. 1989) ("[t]he lost profits will however be doubled rather than tripled, since we find that Brewer's actions were willful, but not so egregious as to warrant trebling of the damages.").
209. *SRI Int'l v. Advanced Tech. Lab.*, 127 F.3d 1462 (Fed. Cir. 1997).

One who has notice of another's patent rights has an *affirmative duty to exercise due care* to determine whether or not infringement exists.[210] The *minimum* effort required to meet this duty is to seek and obtain competent legal advice from counsel promptly before the initiation or continuation of any possible infringing activity.[211]

Good faith reliance on the competent advice of counsel constitutes a defense to willfulness.[212] A good faith belief exists where the infringer has an "honest doubt" of infringement, validity, or enforceability of the patent.[213] When the "advice of counsel" defense is raised, the court may consider the nature of the advice, the thoroughness and competence of the legal opinion presented, and its objectivity. Aspects in *mitigation*—such as whether the infringer had an independent invention, or attempted to design around and avoid the patent, or any other factors tending to show good faith—will be taken into account and given appropriate weight.[214] Other factors that may be weighed are other acts indicating willfulness, such as deliberate copying or concealment of infringing activity by the infringer,[215] or withholding information from the patent owner's counsel.[216]

To best ensure than an opinion of counsel is legally adequate, the opinion should meet the following criteria:

(1) the opinion should be in writing;[217]

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210. "Notice of another's patent rights" does not mean that the patent owner has made a charge of infringement, or even affirmatively given notice of a patent to the infringer. Little "notice" of the patent in suit is required to trigger the "due care" standard. Notice can include notification by the patent owner; discovery of a relevant patent during routine product clearance searches; mention by a third party of the existence of a patent covering a similar product. "Notice" cannot commence before issuance of a patent; awareness by an infringer of a pending patent application does not trigger a "due care" inquiry.
211. *Underwater Devices, Inc. v. Morrison-Knudsen Co.*, 717 F.2d 1380, 1389-1390 (Fed. Cir. 1983).
212. *Mahurkar v. C.R. Bard, Inc.*, 79 F.3d 1572, 1579 (Fed. Cir. 1996).
213. *Rosemount, Inc. v. Beckman Instruments, Inc.*, 727 F.2d 1540, 1548 (Fed. Cir. 1984).
214. *SRI Int'l, supra.*
215. *Id.*
216. *Amsted Indus. v. National Castings*, 16 USPQ2d 1737, 1742 (N.D. Ill. 1990).
217. *Compare Shiley, Inc. v. Bentley Laboratories, Inc.*, 601 F.Supp. 964, 968 (C.D. Cal. 1985), *aff'd*, 794 F.2d 1561 (Fed. Cir. 1986), *with Radio Steel & Mfg. Co. v. MTD Products, Inc.*, 788 F.2d 1554 (Fed. Cir. 1986) (outside patent counsel rendered an oral opinion of invalidity without

(2) the opinion should be prepared by an outside, independent U.S. patent attorney;[218]

(3) the opinion should discuss pertinent case law;[219]

(4) the opinion should set forth an adequate foundation based on a review of all available facts, including the prosecution history of the patents in issue and discussion of pertinent prior art;[220]

(5) a non-infringement opinion should set forth a detailed description of the accused device or process;[221]

(6) the opinion should set forth an analysis of the claims of the patents in issue, including analysis of specific claims, an interpretation of the claim

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review of the prosecution history; no clear error for the district court *failing* to find willful infringement); *and Minnesota Mining & Mfg. Co., supra* (stating that, "[a]s this court has recognized, oral opinions are not favored . . . Such opinions carry less weight, for example, because they have to be proved perhaps years after the event, based only on testimony which may be affected by faded memories and the forces of contemporaneous litigation.").

218. *Compare Underwater Devices, Inc. v. Morrison-Knudsen Co.*, 717 F.2d 1380, 1389-1390 (Fed. Cir. 1983), *with Acoustical Design, Inc. v. Control Electronics Co.*, 932 F.2d 939, 942 (Fed. Cir. 1991), *cert. denied*, 502 U.S. 863, 116 L.Ed. 2d 146, 112 S.Ct. 185(1991), *and Studiengesellschaft Köhle v. Dart Industries, Inc.*, 862 F.2d 1564 (Fed. Cir. 1988) (no willful infringement even though the infringer relied upon an opinion from its in-house patent counsel), *and McDermott v. Omid International, Inc.*, 723 F.Supp. 1221 (S.D. Ohio 1988), *aff'd*, 883 USPQ2d 1026 (Fed. Cir. 1989).

> It is not believed that the Federal Court meant to suggest that in-house counsel is less competent than outside counsel. Instead, the case reasoning appears to reflect the idea that the party rendering the advice is closely tied to the company and may feel undue pressure to recommend in favor or against any particular patent.

219. *Ortho Pharmaceutical Corp. v. Smith*, 959 F.2d 936, 945 (Fed. Cir. 1992).

220. *Read Corp, supra* at 829; *see also Underwater Devices, Inc. v. Morrison-Knudsen Co.*, 717 F.2d 1380, 1389-1390 (Fed. Cir. 1983); *and Datascope Corp. v. SMEC, Inc.*, 879 F.2d 820, 828 (Fed. Cir. 1989).

221. *Westvaco Corp. v. International Paper Co.*, 991 F.2d 735, 744 (Fed. Cir. 1993).

language and discussion of any means-plus-function claim limitations;[222]

(7) a non-infringement opinion should address the doctrine of equivalents;[223]

(8) an invalidity opinion should discuss objective indicia of non-obviousness;[224]

(9) the issue of possible inequitable conduct should be addressed;[225]

(10) if the opinion addresses invalidity, a prior art search should have been promptly conducted;[226]

(11) the opinion should explain what issues were considered but not fully addressed (*e.g.*, other grounds for invalidity, defects in title, *etc.*);[227] and

(12) the opinion should reach an unequivocal conclusion at least of probable non-infringement, invalidity or unenforceability of each patent in issue.[228]

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222. *Id.*; *see also Critikon, Inc. v. Becton Dickinson Vascular Access, Inc.*, 120 F.3d 1253 (Fed. Cir. 1997).

223. *Compare Datascope, supra, with Westvaco Corp. v. International Paper Co.*, 991 F.2d 735, 744 (Fed. Cir. 1993) (holding that the opinion letter contained enough other indicia of competence that the failure to discuss infringement under the doctrine of equivalents was not fatal).

224. *Sensonics, Inc. v. Aerosonic Corp.*, 81 F.3d 1566, 1571 (Fed. Cir. 1996).

225. *Ortho Pharmaceutical Corp. v. Smith*, 959 F.2d 936, 945 (Fed. Cir. 1992).

226. *Underwater Devices, supra* at 1390; *see also Del Mar Avionics, Inc. v. Quinton Instrument Co.*, 836 F.2d 1320 (Fed. Cir. 1987) (patent search first conducted after suit filed, despite pre-suit notice of the patent).

227. *Compare Westvaco Corp. v. International Paper Co.*, 991 F.2d 735, 744 (Fed. Cir. 1993) (the opinion letter was successfully attacked in the District Court in part for failure to discuss infringement under the doctrine of equuivalents; overturned on appeal).

228. *Read Corp., supra* at 829 (stating in footnote 9 that "[a]n opinion of counsel, of course, need not unequivocally state that the client will not be held liable for infringement. An honest opinion is more likely to speak of probabilities than certainties. A good test that the advice given is genuine and not merely self-seving is whether the asserted defenses are backed up with viable proof during trial which raises substantial questions, as here."); *see also Ortho, supra* at 944 (stating that, "[c]ounsel's opinion must be thorough enough, combined with other factors, to instill a belief in the infringer that a court might reasonably hold the patent is invalid, not infringed, or unenforceable."); *and Graco, Inc. v. Binks Mfg. Co.*, 60 F.3d 785, 793 (Fed. Cir. 1995).

Obtaining an opinion of counsel, however, does not mandate a finding of non-willfulness.[229] Conversely, the absence of an opinion of counsel does not mandate a finding of willfulness.[230] Nevertheless, failure to obtain and follow an opinion of counsel often results in a finding of willful infringement.

If a legal opinion does exist, it must be "competent" before it can be relied upon by an infringer. An opinion should have the appearance of competence, authoritativeness, or internal indicia of credibility.[231] An opinion of counsel need not, however, be legally correct. Indeed, the willfulness defense arises only if the opinion is *incorrect*.[232]

There appears to be very little likelihood of avoiding willful infringement if the infringer did not actually rely on the legal opinion it received.[233] Reasonable reliance is key to the opinion

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229. *See, e.g., Underwater Devices,supra* at 1389-90 (opinion was by in-house counsel who was not a patent attorney, file histories of the patents in issue were not reviewed until after infringement commenced and the opinion was rendered only after suit was filed); *see also Central Soya Co. v. Geo. A. Hormel & Co.*, 723 F.2d 1573, 1576-77 (Fed. Cir. 1983) (attorney's advice was based solely on the file history prior art, and the defendant waited two years to verify whether it was within the parameters of the opinion); *and Read Corp., supra*:

> Those cases where willful infringement is found despite the presence of an opinion of counsel generally involve situations where opinion of counsel was either ignored or found to be incompetent. *See Datascope Corp. v. SMEC, Inc.*, 879 F.2d 820, 828-29 (Fed. Cir. 1989), *cert. denied*, 493 U.S. 1024, 107 L.Ed. 2d 747, 110 S. Ct. 729 (1990); *and Kori Corp. v. Wilco Marsh Buggies & Draglines, Inc.*, 761 F.2d 649, 656-57, 225 USPQ 985, 989 (Fed. Cir. 1985), *cert. denied*, 474 U.S. 902, 88 L.Ed. 2d 229, 106 S. Ct. 230 (1985).

230. *Kloster, supra* (stating that, "[t]hough it is an important consideration, not every failure to seek an opinion of competent counsel will mandate an ultimate finding of willfulness."); *see also King Instrument Corp. v. Otari Corp.*, 767 F.2d 853, 867 (Fed. Cir. 1985); *Machinery Corp. of America v. Gullfiber AB*, 774 F.2d 467, 472 (Fed. Cir. 1985); *Rolls-Royce, Ltd. v. GTE Valeron Corp.*, 800 F.2d 1101, 1109 (Fed. Cir. 1986); *Amstar Corp. v. Envirotech Corp.*, 823 F.2d 1538, 1547 (Fed. Cir. 1987); *Rite-Hite, supra* at 1125; *and Nickson Industries, Inc. v. Rol Mfg. Co.*, 847 F.2d 795, 800 (Fed. Cir. 1988).
231. *Studiengesellschaft, supra* at 1579.
232. *Ortho Pharmaceutical, supra*; *see also Graco, Inc., supra* at 792.
233. *See, e.g., Read Corp., supra* at 829:

> Those cases where willful infringement is found despite the presence of an opinion of counsel generally involve situations where opinion of counsel was either ignored or found to be incompetent. [Citations omitted].

of counsel defense. The infringer must also pay attention to what an opinion covers.

While the patent owner has the overall burden of proving willful infringement, it is the infringer's burden to prove that it has met the duty of due care by obtaining and relying upon an opinion of counsel. Such proof requires the introduction of the opinion itself, with a concomitant *waiver* of the attorney-client privilege associated with the opinion. An infringer who relies on the attorney-client privilege to withhold such an opinion may well be in the position of an infringer with no opinion of counsel at all.

When an infringer refuses to produce an exculpatory opinion of counsel in response to a charge of willful infringement, an inference may be drawn that either no opinion was obtained, or the opinion obtained was unfavorable.[234] Yet, an inference that an opinion was unfavorable does not foreclose consideration of other relevant factors. Possession of a favorable opinion of counsel is not essential to avoid a willfulness determination; it is only one factor to be considered, although an important one. Assertion of the attorney-client privilege does not raise an irrebuttable presumption of willfulness. Such a rule would not accommodate consideration of other facts, nor would it respect the right of a party to assert the attorney-client privilege.[235]

A number of positions have been taken by the district courts when an infringer elects to disclose an opinion of counsel:

- *all* opinions must be disclosed;[236]
- production of any opinion waives the attorney-client privilege for *all* communications relating to the same subject,[237] although some information relating to

234. *Electro Medical Sys. S.A. v. Cooper Life Sciences*, 34 F.3d 1048, 1056-1057 (Fed. Cir. 1994); *see also American Medical Systems, Inc. v. Medical Eng'g Corp.*, 6 F.3d 1523, 1531 (Fed. Cir. 1993); *Fromson, supra* at 1572-73; *and Kloster, supra* at 1579-80.

235. *Electro Medical, supra.*

236. *Board of Trustees v. Coulter Corp.*, 4 U.S.P.Q.2d 1652 (S.D. Fla. 1987).

237. *Macrovision Corp. v. VSA Ltd.*, 12 U.S.P.Q.2d 2011 (D. Or. 1989); *see also McCormick-Morgan Inc. v. Teledyne Industries Inc.*, 21 U.S.P.Q.2d 1412 (N.D. Cal. 1991); *and Micron Separations v. Pall Corp.*, 159 F.R.D. 361, 363 (D. Mass. 1995) (waiver only to extent of issues addressed in the opinion of counsel).

legal strategies *may* be protected under the work product privilege;[238] and

- an attorney who authored an opinion may be called as a witness by an opposing party.[239]

As indicated above, absence of an authoritative opinion does not necessitate a finding of willful infringement. Lack of willfulness may be found where the infringer attempted (unsuccessfully) to design around a patent rather than deliberately copied the ideas or design of the patent owner. A survey of cases indicates that proof of active attempts to design around a patent often result in a denial of enhanced damages. This outcome may be a result of deference to the principle that one of the benefits of the patent system is the incentive it provides for "designing around" patented inventions, thus creating new innovations.[240] Nevertheless, failure to obtain an opinion of counsel, coupled with a finding of deliberate copying, will generally be found adequate grounds for supporting enhanced damages; the copying need not be "slavish" to support a finding of willfulness.[241]

A willfulness finding is generally inappropriate when the infringer mounts a good faith and substantial challenge to the existence of infringement.[242] In determining willfulness, it is relevant whether the infringer acted in good faith during the litigation.[243] The ultimate fact to be proven, however, is not that litigation activities were improper, but rather that the infringement was willful. "Bad faith" properly refers to an infringer's failure to use due care in avoiding infringement of another's patent rights.[244] Thus, although an infringer's inequitable conduct in prosecuting the infringer's own patents or egregious conduct in infringement litigation may be sufficient for other sanctions or fee awards, or may be used as a factor in de-

238. *Coulter Corp., supra*; *see also Thorn EMI N. Am. v. Micron Technology*, 837 F. Supp.616, 622 (D. Del. 1993); *contra*, *Macrovision, supra*.
239. *Amsted Indus. v. National Castings*, 16 U.S.P.Q.2d 1737, 1743 (N.D. Ill. 1990).
240. *Read Corp., supra*; *see also Westvaco Corp. v. International Paper Co.*, 991 F.2d 735, 745 (Fed. Cir. 1993).
241. *See, e.g., Stryker Corp. v. Intermedics Orthopedics*, 96 F.3d 1409, 1414 (Fed. Cir. 1996).
242. *Graco, supra* at 794; *see also Electro Medical, supra* at 1057; *see also Paper Converting Machine Co. v. Magna-Graphics Corp.*, 745 F.2d 11, 20 (Fed. Cir. 1984).
243. *Kalman v. Berlyn Corp*, 914 F.2d 1473, 1484 (Fed. Cir. 1990).
244. *Jurgens v. CBK, Ltd.*, 80 F.3d 1566, 1570-1571 (Fed. Cir. 1996).

termining whether or how much to increase a damages award *after* sufficient culpability is found, these actions generally do *not* provide a sufficient independent basis to justify increased damages under section 284.[245]

X. *ATTORNEY'S FEES*

Section 285 provides that the court in exceptional cases may award reasonable attorney fees to the prevailing party. The law of attorney fee awards under section 285 often parallels the law of enhanced damages under section 284. Nevertheless, the criteria for enhancement of damages and for the award of attorney fees are not necessarily the same, although the contributing factors often overlap.[246]

The permissive language of the statute makes an award of attorney fees discretionary rather than mandatory. A finding that a case is "exceptional" does not mandate that attorney fees be awarded.[247] Accordingly, an award of attorney fees is committed to the discretion of the trial court.[248] In determining whether to award fees, the court should undertake a two-step analysis:[249]

- the first step is to determine whether the case is "exceptional;"[250] and
- the second step is to determine whether awarding attorney fees to the prevailing party is appropriate.[251]

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245. *Jurgens, supra*; *see also Read Corp., supra* at 826.
246. *Sensonics, Inc. v. Aerosonic Corp.*, 81 F.3d 1566, 1574 (Fed. Cir. 1996).
247. *S.C. Johnson & Son, Inc. v. Carter-Wallace, Inc.*, 781 F.2d 198 (Fed. Cir. 1986); *see also National Presto Indus. v. West Bend Co.*, 76 F.3d 1185 (Fed. Cir. 1996).
248. *Serrano v. Telular Corp.*, 111 F.3d 1578 (Fed. Cir. 1997).
249. *J.P. Stevens Co. v. Lex Tex, Ltd.*, 822 F.2d 1047, 1050 (Fed. Cir. 1987) (stating that "[t]he district court must determine whether the case is 'exceptional'; if it is, then it is within the court's discretion to award attorneys' fees to the prevailing party."); *see also Interspiro USA, Inc. v. Figgie Int'l*, 18 F.3d 927, 933-34 (Fed. Cir. 1994); *and Motorola, Inc. v. Interdigital Tech. Corp.*, 121 F.3d 1461 (Fed. Cir. 1997).
250. *Amsted Indus., supra* at 184; *see also L.A. Gear, supra* at 1128.
251. *Amsted, supra*; *see also Modine Mfg. Co. v. Allen Group, Inc.*, 917 F.2d 538, 543 (Fed. Cir. 1990); *Shatterproof Glass Corp. v. Libbey-Owens Ford Co.*, 758 F.2d 613, 629 (Fed. Cir. 1985) (awarding attorneys' fees is within the discretion of the trial court), *cert. dismissed*, 474 U.S. 976, 88 L.Ed. 2d 326, 106 S.Ct. 340 (1985).

As a general rule, attorney fees under section 285 may be justified by any valid basis for awarding enhanced damages under section 284. Conduct which a court may deem "exceptional" and a basis for awarding attorney fees may not qualify as willful infringement supporting an award of enhanced damages. Conversely, conduct that constitutes willful infringement supporting enhanced damages under section 284 may not make a case exceptional under section 285.[252]

Attorney fees are not to be routinely assessed against a losing party in litigation, in order to avoid penalizing a party for merely defending or prosecuting a lawsuit. Attorney fees are awarded to avoid a gross injustice.[253]

The prevailing party must establish the exceptional nature of a case by clear and convincing evidence before the district court decides whether or not to award attorney fees.[254] A court's determination that a case is exceptional is a finding of fact.[255] Once a case is found to be exceptional, the decision to award or deny attorney fees, and the amount of such fees, is reviewed for abuse of discretion.[256] To enable appellate review, a district court is obligated to explain the basis for the award.[257]

A case may be "exceptional" for either of two basic reasons:

- misconduct of a party giving rise to the litigation (*e.g.*, willful infringement by the infringer or inequitable conduct before the Patent Office by the patent owner); or
- misconduct of a party during litigation (*e.g.*, vexatious tactics, pressing of insupportable claims, frivolous suite, or violation of an injunction).[258]

252. *See, e.g., Jurgens, supra* at 1573 (footnote 4); *see also Beckman Instruments, Inc. v. LKB Produkter AB*, 892 F.2d 1547, 1553-1554 (Fed. Cir. 1989); *and Paper Converting Machine Co. v. Magna-Graphics Corp.*, 785 F.2d 1013, 1016 (Fed. Cir. 1986).
253. *Revlon, Inc. v. Carson Products Co.*, 803 F.2d 676 , 679 (Fed. Cir. 1986).
254. *Machinery Corp. of America v. Gullfiber AB*, 774 F.2d 467, 471 (Fed. Cir. 1985); *see also Cambridge Products, Ltd. v. Penn Nutrients*, 962 F.2d 1048, 1050 (Fed. Cir. 1992).
255. *Reactive Metals & Alloys Corp. v. ESM, Inc.*, 769 F.2d 1578, 1582-1583 (Fed. Cir. 1985); *see also Amsted, supra.*
256. *Reactive Metals, supra*; *see also Amsted, supra.*
257. *Hughes v. Novi American, Inc.*, 724 F.2d 122, 124 (Fed. Cir. 1984).
258. *Sensonics, Inc. v. Aerosonic Corp.*, 81 F.3d 1566, 1574 (Fed. Cir. 1996); *see also Beckman Instruments, supra* at 1551; *and Tenax Corp. v. Tensar Corp.*, 27 U.S.P.Q.2d 1216 (D. Md. 1992).

A finding of willful infringement or bad faith by an infringer is sufficient to constitute an exceptional case.[259] If, however, willful infringement is found but the case is ruled not exceptional, the district court ordinarily must explain why the case is *not* exceptional within the meaning of section 285.[260] Similarly, when a case is found to be exceptional without a finding of willful infringement, the court ordinarily must make a specific finding of exceptional circumstances.[261] Failure of an infringer to obtain an opinion of counsel does not *per se* make a case exceptional, and an award of attorney fees based only on such a finding is erroneous.

Attorney fees may only be awarded to the "prevailing" party. In a complex case with many asserted claims and defenses, which party "prevails" may be equally complex. The Federal Circuit has noted that one resolution may be either to deny fees entirely, or to grant fees only to the extent that a party "prevailed." A party can "prevail" without obtaining a judgment after trial.

Determination of the amount of attorney fees is discretionary with the court.[262] However, the amount of the award must bear some relation to the extent of the misconduct.[263] Thus, a court may award partial attorney fees to compensate a party for only the harm caused in opposing specific issues.[264]

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259. *Modine Mfg. Co. v. Allen Group, Inc.*, 917 F.2d 538, 543 (Fed. Cir. 1990), *cert. denied*, 500 U.S. 918, 114 L.Ed. 2d 103, 111 S.Ct. 2017 (1991).

260. *Jurgens, supra* at 1572; *see also Modine, supra*; *and S.C. Johnson & Son, Inc. v. Carter-Wallace, Inc.*, 781 F.2d 198, 201 (Fed. Cir. 1986).

261. *Stevenson v. Sears, Roebuck & Co.*, 713 F.2d 705, 712-13 (Fed. Cir. 1983); *see also Kloster, supra* at 1580-81 (conduct which a court may deem "exceptional" and a basis for awarding attorney fees may not qualify for an award of increased damages as being unrelated to willful infringement); *and Reactive Metals, supra* (stating that, "[i]n order to provide a basis for meaningful review, it is incumbent on the trial court not only to make the ultimate finding that the case is exceptional, but also to articulate the more particular factual findings from which the finding of 'exceptional circumstances' follows.").

262. *Hughes, supra* at 124.

263. *Read Corp., supra* at 831; *see also Beckman Instruments, supra.*

264. *Total Containment v. Environ Prods.*, 1997 U.S. App. LEXIS 793 (Fed. Cir. 1997) (attorney fees awarded to patent owner only for its defense against the infringer's charge of inequitable conduct); *see also Beckman Instruments, supra*; *and Tenax, supra.*

Attorney fees under section 285 generally may only be awarded for work on patent issues.[265] If non-patent issues are so intertwined with patent issues that the evidence would be material to both types of issues, attorney fees under section 285 may be awarded for such "mixed fee" work.[266] The amount of an attorney fee award under section 285 should not be reduced by insurance payments received by the party granted the award, whether or not the insurer has a right to subrogation.

Absent egregious conduct sufficient to invoke the inherent equitable powers of the court, expert witness fees in excess of the amounts provided by statute are *not* allowable as part of attorneys' fees.[267] A judge of any United States court may tax "fees and disbursements for printing and witnesses" as "costs."[268] Expert witness fee awards are limited, however, to an attendance fee of $40 per day for each day's attendance and/or transit time to or from the place of attendance.[269] The current rule is that expert witness fees in excess of the $40 daily amount *cannot* be awarded in patent cases as costs under section 284 or as part of attorneys' fees under section 285. Yet, in a truly egregious case involving a finding of fraud or abuse of the judicial process, where the rules or statutes do not reach "acts which degrade the judicial system," a trial court *can* invoke its inherent sanctioning power to impose expert witness fees in excess of the cap.[270]

If in-house counsel is performing legal work that would otherwise be performed by outside counsel, most courts have allowed an award of attorney fees under section 285 if adequately documented.[271] Time spent by in-house counsel in the role of a

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265. *Hughes, supra*; *see also Water Technologies Corp. v. Calco, Ltd.*, 850 F.2d 660, 674 (Fed. Cir. 1988) (stating that, "[b]ecause the attorney fee award in this case was in part for work connected with the now-defunct unfair competition claim, the amount of the award cannot stand.").
266. *Stickle, supra* at 1564; *see also F.B. Leopold Co. v. Roberts Filter Mfg. Co.*, 119 F.3d 15 (Fed. Cir. 1997) (full text of this unpublished decision at 1997 U.S. App. LEXIS 16233).
267. *Amsted, supra.*
268. 28 U.S.C. § 1920(3).
269. 28 U.S.C. § 1821(b).
270. *Amsted, supra* at 379.
271. *See, e.g., Scripps Clinic & Research Foundation v. Baxter Travenol Laboratories Inc.*, 17 U.S.P.Q.2d 1046, 1047 (D. Del. 1990); *see also PPG Industries, Inc. v. Celanese Polymer Specialties Co.*, 840 F.2d 1565, 1569-1570 (Fed. Cir. 1988); *National Gypsum Co. v. Steel Systems Int'l, Inc.*, 9 U.S.P.Q.2d 2073 (D. Or. 1988); *and Scott Paper Co. v. Moore Business Forms, Inc.*, 604 F. Supp. 835, 837 (D. Del. 1984); *but see Gil-*

client, such as time spent keeping abreast of the progress of the litigation and advising outside counsel of the client's views as to litigation strategy, is not compensable in a fee award.[272] The amount of fees to award for legal work performed by in-house counsel is left to the judgment of the district court. The appropriate rate may be either a cost-plus-overhead standard[273] or a private firm market rate standard.[274]

XI. TIME LIMITATION ON DAMAGES

The Patent Statute does not contain a true statute of limitations barring an infringement action if not commenced within a specified time period after a patent owner knows or should have known of infringing acts.[275] Instead, the Patent Statute provides for a "running" period limiting recovery of damages to no more than six years before commencement of a cause of action for infringement.[276] This form of limitation on damages has certain notable characteristics:

- an action for infringement seeking damages can be brought for up to six years *after* a patent expires (injunctive relief would no longer be available);[277]
- since rights under a patent only arise when a patent issues, a patent owner cannot recover damages for infringing acts occurring before the patent issued, even if an action for infringement is brought within six years after such acts;[278]
- section 286 has no limiting effect on actions for injunctive relief brought by the patent owner;

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breth Int'l Corp. v. Lionel Leisure, Inc., 622 F. Supp. 478 (E.D. Pa. 1985), *aff'd without op.*, 802 F.2d 469 (1986) (unpublished); *and Broadview Chemical Corp. v. Loctite Corp.*, 311 F. Supp. 447 (D. Conn. 1970) (stating that in-house counsel fees are "a regular cost of doing business").

272. *Scripps, supra*; *see also PPG Indus. v. Celanese Polymer Specialties Co.*, 658 F. Supp. 555, 562 (W.D. Ky. 1987) (dicta), *rev'd on other grounds*, 840 F.2d 1565 (Fed. Cir. 1988); *and National Gypsum Co., supra.*
273. *PPG Indus., supra.*
274. *Id.* at 1570.
275. *Standard Oil Co. v. Nippon Shokubai Kagaku Kogyo Co.*, 754 F.2d 345 (Fed. Cir. 1985).
276. 35 U.S.C. § 286.
277. *In re Morgan*, 990 F.2d 1230, 1232 (Fed. Cir. 1993).
278. *State Industries, Inc. v. A.O. Smith Corp.*, 751 F.2d 1226, 1237 (Fed. Cir. 1985) (stating that, "[a] patent has no retroactive effect.").

- section 286 has no limiting effect on declaratory judgment actions for non-infringement or invalidity, or on other claims against a patent owner;
- the six-year period for limiting damages for an action for infringement brought by way of a counterclaim is determined from the filing date of the counterclaim, and not of the underlying complaint. More generally, the six-year period for limiting damages counts backwards from the date a claim is made as to each patent in issue;[279]
- the acts of infringement creating a damage claim must occur within the six-year period;[280]
- to date, no court has held that section 286 can be tolled on equitable grounds.[281] Thus, for example, a patent owner cannot recover damages for concealed infringements beyond the six-year period;[282] and
- section 286 *can* be waived or tolled by express contractual agreement of an accused infringer. Agreements to toll section 286's six-year damage recovery period are properly construed as allowing the potential plaintiff to recover damages for acts of infringement occurring during both (1) the six-year statutory period; and (2) a supplemental damage recovery period specified in the agreement.[283]

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279. *Standard Oil, supra*; *see also Illinois Tool Works, Inc. v. Foster Grant Co.*, 395 F. Supp. 234, 250-251 (N.D. Ill. 1974), *aff'd*, 547 F.2d 1300 (7th Cir. 1976), *cert. denied*, 97 S.Ct. 2631, 431 U.S. 929, 53 L.Ed. 2d 243 (1977):

> Rule 15(c) of the Federal Rules of Civil Procedure states that an amended pleading "relates back to the date of the original pleading whenever the claim or defense asserted in the amended pleading arose out of the same conduct, transaction, or occurrence set forth or attempted to be set forth in the original pleading." This rule does not apply here. An alleged infringement of one patent is not the "same conduct, transaction or occurrence" as the alleged infringement of another patent.

280. *Standard Oil, supra*; *see also A. Stucki Co. v. Buckeye Steel Castings Co.*, 963 F.2d 360 (Fed. Cir. 1992).
281. *Case v. Goodyear Tire & Rubber Co.*, 12 U.S.P.Q.2d 1550 (N.D. Ohio 1989); *see also A. Stucki, supra.*
282. *Pollen v. Ford Instrument Co.*, 108 F.2d 762 (2d Cir. 1940).
283. *Hughes Aircraft Co. v. National Semiconductor Corp.*, 850 F. Supp. 828 (N.D. Cal. 1994).

The accused infringer bears the burden of proving that acts of infringement occurred outside the six-year period, and hence would bear no damages.[284]

XII. PATENT MARKING AND NOTICE TO INFRINGERS

Section 287 provides a second limitation on recovery of past damages: It provides a marking requirement.[285] The marking provision basically holds that a patent owner (and persons making or selling any patented article by authority of the patent owner, such as a licensee) must mark the *patent number* on a patented article (or on packaging or labels in certain cases), or else be precluded from obtaining damages.[286] Marking serves as constructive notice to the public of the patent owner's patent rights.

One exception to the marking requirement arises upon proof that the infringer was actually notified of the infringement and continued to infringe, though damages may be recovered only for infringement occurring after giving actual notice. The requirements for giving actual notice are substantially more stringent than for constructive notice. Examples of effective actual notice include the infringer receiving a letter in which the patent owner charges the infringer with infringement of a specified patent, and filing of an action for infringement.[287] Once actual notice is given, damages accrue only for acts of infringement occurring after the notice date.

For purposes of the marking provision, notice must be of the infringement, not merely notice of the patent's existence or ownership. *Actual notice requires the affirmative communication of a specific charge of infringement of a specific patent by a specific accused product or device.*[288] The "specific charge of infringement" may be a threat of suit, a demand for cessation of

284. *Bianchi v. Barili*, 168 F.2d 793, 803 (9th Cir. 1948).
285. 35 U.S.C. § 287(a).
286. This statement is limited to patent damages. In *Cover v. Hydramatic Packing Co.*, 83 F.3d 1390 (Fed. Cir. 1996), the Federal Circuit held that section 287(a) did not preempt a state commercial law claim for acts arising before actual notice under section 287(a) was given by filing suit.
287. 35 U.S.C. § 287(a). It appears that notice may be given orally, but this is obviously bad practice as being difficult to prove. Proper notice does not require an explanation as to how the claims of a patent read on the accused product or process.
288. *Amsted, supra* at 185; *see also SRI Int'l v. Advanced Tech. Lab.*, 127

infringement, or an offer for a license under the patent in issue. Determining if notice is proper under §287 focuses on the action of the patent owner, not the knowledge or understanding of the accused infringer.

The marking provision does not limit a patent owner's right to recover damages when a patent notice is omitted on unauthorized articles, or when the patent owner's (or a licensee's) notice is removed by an unauthorized entity. Also, the marking provision has no limiting effect on actions for injunctive relief brought by the patent owner.

A relatively complex set of rules has developed as to the circumstances under which a notice is required, and when omission of a required notice affects pre-notice damages. The complexities hinge on whether the patent owner is, directly or indirectly, practicing the claimed invention, and/or whether the claims asserted in suit are apparatus or process claims.

The following table sets forth the current law regarding a duty to mark:

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ing on its interpretation of 1927 First Circuit law, held that notice did *not* require specification of the patent number:

> Once actually notified, the alleged infringer, who is already in communication with the patentee, can at little cost request the number and engage in an assessment of the claim's merits. Indeed, it has been held that once a potential infringer has notice of another's patent rights, he has an affirmative duty to "exercise due care to determine whether or not he is infringing." *See Bott v. Four Star Corp.*, 807 F.2d 1567, 1572 (Fed. Cir. 1986); *see also Milgo Electronic v. United Business Communications, Inc.*, 623 F.2d 645, 666 (10th Cir.), *cert. denied*, 449 U.S. 1066 (1980). Due care would presumably include requesting the number of the patent. In short, the crucial distinction is that, because marking permits the presumption that the defendant had notice, it must comply with more stringent standards. *Actual notice, precisely because it is targeted at the individual defendant and obviates the need to make presumptions about what he knew, is consequently less demanding.* [Emphasis added]

Ceeco Mach. Mfg., Ltd. v. Intercole, Inc., 817 F. Supp. 979 (D. Mass. 1992).

Are authorized patented *articles* made, offered for sale, or sold within, or imported into, the U.S.?	Claims Include:	Marking required?	Damages allowed before actual notice if marking omitted?
No	At least apparatus	No	Yes (no patented article to mark)
No	Only processes	No	Yes (no patented article to mark)
Yes	Processes and apparatus, but apparatus claims are *not* asserted in suit	No	Yes (no patented article subject to marking is in issue)
Yes	At least apparatus, and at least the apparatus claims are asserted in suit	Yes	No (patented article subject to marking *is* in issue)

Although these rules seem to draw "bright line" tests, a patent owner may have some flexibility in evading the marking requirement by careful selection of the claims to assert. The *Hanson* case suggests putting only method claims in issue for a patent having both apparatus and method claims. Further, in one case involving failure by the patent owner to mark a product that contained one patented feature but did not contain a second feature covered by the same patent, where the accused infringer was allegedly using the second feature, a district court held that the marking provision did not bar recovery of past damages.[289]

289. *Toro Co. v. McCulloch Corp.*, 898 F. Supp. 679 (D. Minn. 1995):

> A device is a "patented article" under a patent when it contains all of the elements disclosed in any single claim of the patent. Since a patent may encompass several independent claims, there may be several distinct "patented articles" which arise under that patent, each of which may be the subject of an independent infringement action . . . For the same reason, a patentee may make or sell different "patented articles" which arise under a single patent, some of which embody a "patented article" which has been consistently properly marked, and others which embody a different "patented article" which may not have been properly marked . . . Since section 287(a) refers to a "patented article" which has not been properly marked, the logical reading of the statute indicates that the infringement ac-

Who must mark: The patent owner and any licensees must mark when possible. The patent owner must police compliance by licensees or face the consequences of failure to mark. A "licensee" includes any entity authorized to make, sell, or offer to sell articles covered by a patent regardless of whether the "license" is in the form of a settlement, a covenant not to sue, or a true commercial license.[290] A licensee relationship may be implied rather than express. Thus, a patent owner should contractually require marking and preferably specify the form of the notice.

Contents of the notice: a proper statutory patent notice comprises at least the word "patent" or the abbreviation "pat." together with the number of the patent. The marking on the article must be large enough to be easily read in order for a notice to be effective and comply with the statute.[291]

Multiple patents in the notice: Multiple patent numbers may be listed in a notice, even if some of the patents do not cover the article, as long as at least one patent *does* cover the article.[292]

Location of the notice: The marking provision requires that the notice be fixed on the *patented* article, or "when, from the character of the article, this can not be done, by fixing to it, or to the package wherein one or more of them is contained, a label containing a like notice." While some leeway is given to the patent owner as to whether a label can be used,[293] a number of courts have been exceedingly strict on use of a label in lieu of direct affixation.[294] Merely marking some literature associated

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> tion under which damages are limited is an infringement action based upon that same unmarked "patented article."
>
> . . .
>
> *For the reasons set forth above, the Court finds that § 287(a) does not limit recovery in an action when an unmarked article, which has been made or sold, contains one of the inventions disclosed in the patent but does not contain the invention of the predicate suit.* [emphasis added]

290. *In re Yarn Processing Patent Validity Litigation*, 602 F. Supp. 159, 169 (W.D.N.C. 1984).
291. *Trussell Mfg. Co. v. Wilson-Jones Co.*, 50 F.2d 1027, 1030 (2d Cir. 1931); *see also Rutherford v. Trim-Tex, Inc.*, 803 F. Supp. 158 (N.D. Ill. 1992).
292. *Chicago Pneumatic Tool Co. v. Hughes Tool Co.*, 192 F.2d 620 (10th Cir. 1951).
293. *Sessions, supra.*
294. *Creative Pioneer Products Corp. v. K Mart Corp.*, 5 U.S.P.Q.2d 1841, 1848 (S.D. Tex. 1986).

with a patented article is insufficient to satisfy the marking requirements of the statute.[295] A few older cases have held that "impracticability is not dependent on the question of pecuniary loss or gain to the patent owner", but the modern trend of cases seems to evaluate and balance cost, physical difficulty of affixation, whether an additional manufacturing step would be required, industry custom, and impairment of product aesthetics by affixation of a notice.[296] However, one court noted that a limitation exists to this approach: where the patented article already has other markings or printing on it (*e.g.*, an Underwriter's Laboratory label or a serial number plate) , then marking the package is *not* sufficient compliance with the statute.[297] Thus, the better practice is direct affixation if at all possible. Further, the notice should be in plain sight if possible.

Timing of application of the notice: A statutory notice need only be applied to *patented* articles. Hence, notice need only be applied after a patent issues covering an article. A notice should be applied to all articles as soon as possible, but the courts have recognized that it is impracticable to begin marking literally on the day a patent issues. Consequently, the present rule is that recovery of damages is precluded only for infringements occurring before *substantially consistent and continuous* compliance with the marking requirements of the statute.

XIII. LIMITATION ON MULTIPLE RECOVERIES

The manufacturer who makes and sells, the wholesale distributor and retailer who sell, and the customer who uses an

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295. *Stryker Corp. v. Intermedics Orthopedics*, 891 F. Supp 751, 860 (E.D. N.Y. 1995); *see also Calmar, Inc. v. Emson Research*, 850 F. Supp. 861, 868 (C.D. Cal. 1994):

> [T]he only place in which the '983 patent was included was a piece of promotional material entitled "Fact Sheet." . . . At most, the evidence presented by Calmar indicates that Fact Sheets were routinely left with actual and prospective customers upon delivery of Calmar product samples and that, on occasion, Fact Sheets were included with shipments of Calmar pump sprayer samples to such customers. Both the clear language of section 287(a) and relevant case law indicate that merely marking some literature associated with a patented article is insufficient to satisfy the marking requirements of the statute.

296. *Wayne-Gossard Corp. v. Sondra Mfg. Co.*, 579 F.2d 41 (3d Cir. 1978); *see also Rutherford, supra.*

297. *Rutherford v. Trim-Tex, Inc.*, 803 F. Supp. 158 (N.D. Ill. 1992).

infringing product are all potentially liable for damages to the patent owner as "joint" infringers.[298] The concept of joint infringers is extended to inducers of infringement and to contributory infringers.[299]

The patent law has rejected the common law rule that a release given to one joint tortfeasor necessarily releases all tortfeasors, even if the release expressly reserved rights against other tortfeasors.[300] The modern rule is that a releasing party releases only those other parties that the releasing party intends to release.[301] Accordingly, a release of any infringer that does not dispose of the patent owner's entire infringement claim should expressly reserve rights to pursue other infringers.

Recovery of damages by the patent owner is limited by the principle of full satisfaction: full satisfaction from one tortfeasor prevents further recovery against joint tortfeasors.[302] Full satisfaction generally means complete payment of full compensation.[303] If the patent owner has not recovered full compensation for an infringement from one infringer, the patent owner may proceed against "joint" infringers until full compensation is ob-

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298. *Aro Mfg. Co. v. Convertible Top Replacement Co.*, 377 U.S. 476, 500, 12 L.Ed. 2d 457, 84 S. Ct. 1526 (1964).

299. 35 U.S.C. § 271(b) (inducement); *see also id.* at § 271(c) (contributory infringement).

300. *Aro Mfg. Co., supra* at 503.

301. *Compare Zenith Radio Corp. v. Hazeltine Research*, 401 U.S. 321, 347, 28 L.Ed. 2d 77, 91 S.Ct. 795 (1971), *with Sims v Western Steel Co.*, 551 F.2d 811 (10th Cir. 1977) (court applied parties' agreement choosing state law, under which release of one party generally release all in the absence of an express reservation of rights).

302. *Aro Mfg. Co., supra* at 512-513:

> Hence we think that after a patentee has collected from or on behalf of a direct infringer damages sufficient to put him in the position he would have occupied had there been no infringement, he cannot thereafter collect actual damages from a person liable only for contributing to the same infringement. This principle is but an application of the rule that full satisfaction received from one tortfeasor prevents further recovery against another. It is consistent with the Court's opinion in *Birdsell v. Shaliol* . . .

303. *Laitram Corp. v. Cambridge Wire Cloth Co.*, 229 U.S.P.Q.2d 933, 935 (D. Md. 1986); *see also Amstar, supra* at 1549 (holding that a judgment provision of a corporate guarantee for payment of awarded damages by certified check within 30 days after the mandate of the Federal Circuit was equivalent to full compensation).

tained.[304] A settlement rather than a judgment against one tortfeasor also invokes the full satisfaction rule.

If a suit or threat of suit is resolved by settlement, the accused infringer should seek a provision in the agreement that explicitly provides for a "pass through" license or covenant not to sue that permits end-users of the accused article to continue using the article.

The doctrine of claim preclusion may limit the ability of a patent owner to *serially* seek damages from *related* parties.[305] A plaintiff may sue each distinct unrelated tortfeasor separately, and the liability of each gives rise to a separate cause of action that can support a separate suit for damages. However, a plaintiff who chooses to bring two separate actions against two tortfeasors who are jointly responsible for the same injury runs the risk that the court will find the parties sufficiently related that the second action is barred by claim preclusion.

XIV. PRACTICAL PROBLEMS IN PATENT DAMAGES

Regardless of the damages theories applied, two fundamental problems are associated with any patent damages case, and they affect both the patent owner and the infringer. The first deals with the very real problem of when and how the damages question is decided, particularly by a jury. The second deals with some pervasive damages "myths," on which both the patent owner and the infringer frequently rely to their detriment.

In any non-bifurcated jury case, the infringer faces a very real problem in terms of when the damages decision is made. In most cases, the jury will decide this issue immediately after it has rejected the infringer's position on most, if not all, of the liability issues. A snowball effect is in the works. In order to counter this, the infringer must first recognize its particular vulnerability at this juncture and present a damages defense with this in mind. This involves not only an attack on the patent owner's calculations but also by presenting an alternate damages scenario which is realistic.[306]

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304. *Water Technologies Corp. v. Calco, Ltd*, 850 F.2d 660, 668 (Fed. Cir. 1988).
305. *Mars, Inc. v. Nippon Conlux Kabushiki-Kaisha*, 58 F.3d 616 (Fed. Cir. 1995).
306. After the jury concludes that the infringer copied the invention, willfully infringed 20 patent claims, made $20 million in infringing sales, and presented nothing to show the patent to be invalid, it is usually *not* realistic for the infringer to expect the jury to accept its alternative damages

This problem is compounded by some of the damages myths, which appear in most cases usually from a very incomplete understanding of the law in this area. Not all the myths are relied upon by the infringer, as patent owners, too, have been known to latch on to quite a few with dire consequences. Some of the more significant myths follow.

A. Infringer Myths about Patent Damages

No. 1: *"The patent owner cannot possibly get lost profits—there are too many competitors besides us."*

The notion that lost profits can be awarded only in a "two-supplier" market is a pervasive myth, as there are at least three ways in which lost profits may be awarded in a multi-supplier market: (1) the other suppliers are also infringers;[307] (2) the other suppliers sell products that are unacceptable to the actual purchasers of the infringing products;[308] and (3) the patent owner can demonstrate that in spite of the existence of acceptable non-infringing substitute products sold by third parties, the patent owner would have sold some amount of additional products, usually proportional to its market share in the relevant market, if the infringer had not infringed.[309]

No. 2: *"The patent owner has no hope of recovering lost profits. We had an equally good non-infringing product fully designed which we could have sold instead."*

This is almost a no-win situation for the infringer. First, as the Federal Circuit made clear in *Zygo Corp. v. Wyko Corp.*,[310] an infringer cannot rely on a product as an acceptable noninfringing substitute for the purpose of defeating a lost profits claim unless that product was being marketed during at least some of the period of infringement. A showing that the infringer had stopped selling the substitute once it introduced the infringing device meant that it could not thereafter rely on the substitute in defending against a lost profits claim.

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case based on a "reasonable royalty" of 1% resulting in a minuscule amount of damages. Yet this is often attempted, and the predictable results are some of the biggest damages verdicts.

307. *Bros, Inc. v. W.E. Grace Mfg. Co.*, 320 F.2d 594, 598 (5th Cir. 1963).
308. *TWM, supra* at 901-902.
309. *State Industries, supra* at 1577-78.
310. *Zygo Corp. v. Wyko Corp.*, 79 F.3d 1563 (Fed. Cir. 1996).

But even if the infringer was selling such a non-infringing product during the relevant time period, it may not help. The key customers are those who purchased the infringing products. If they purchased the infringing product instead of the non-infringing alternative also offered by the infringer, the patent owner may really be a long way in proving the infringing product was purchased for the patented feature—which makes the non-infringing version an unacceptable substitute for this key group of customers on which the focus lies.

> ***No. 3:*** *"The patent owner cannot possibly obtain lost profits. It doesn't use its own patent, but practices another technology in its products."*

The holding of the Federal Circuit *en banc* in *Rite-Hite Corp. v. Kelley Co.*,[311] has dispelled the notion that patent owners must practice their own patents to be entitled to lost profits. Patent owners which compete with infringers and lose sales because of the infringement can meet the "but for" test even if their own product is not covered by the patent in suit or any patent for that matter.

> ***No. 4:*** *"Lost profits are out of the question for the patent owner. It didn't even compete for most of the sales we made."*

Again, one must not confuse what the patent owner actually did with what the patent owner would have done, absent infringement. Only the latter is legally relevant. Although on first impression it may seem odd that a patent owner may be entitled to lost profits on jobs for which it never completed, it is analytically sound within the "but for" framework, and the Federal Circuit has approved such an award.[312]

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311. 56 F.3d 1538, 1544-1549 (Fed. Cir. 1995).
312. *See Gyromat Corp. v. Champion Spark Plug Co.*, 735 F.2d 549, 554 (Fed. Cir. 1984) (the fact that the patent owner Gyromat bid against the infringer Champion on only 7 of the 152 infringing sales does not show that the patent owner could not and would not have made all 152 sales if the infringer had not infringed).

No. 5: *"How can the patent owner claim price erosion damages? Our price was higher than the patent owner's."*

Although in the classic price erosion situation, the infringer undercuts the patent owner's price, forcing the patent owner to lower its price that is not the only situation in which a patent owner may suffer price erosion damages. In *Kalman v. Berlyn Corp.*,[313] the reverse situation existed—the patent owner's price was lower than the infringer's. The district court determined that the patent owner was entitled to price erosion damages equal to the difference (15%) between the infringer's price and the patent owner's lower price, and the Federal Circuit affirmed. If the infringing product had not been in the marketplace, the patent owner could have raised his price at least to what the infringer had been charging. Hence, the fact that the infringing product was initially more expensive than the patent owner's was no bar to price erosion damages.

No. 6: *"Reasonable royalty will be small. There's never been a patent in this industry that got more than 1%."*

Reasonable royalty determinations can certainly be more subjective and based on many more factors than lost profits determinations, but one proposition is clear from the case law—royalties on other patents in the industry generally carry little weight in determining a reasonable royalty on the patent in suit. One of the best examples of this is *Bio-Rad Lab. v. Nicolet Instrument Corp.*,[314] in which the Federal Circuit affirmed an approximately 33_% reasonable royalty in the face of evidence that "the industry royalty rate runs from three to ten percent of sales."

No. 7: *"We'll never have to pay a big royalty. We lost money on this product!"*

This too is a lingering myth, which exists in the face of the Federal Circuit's repeated warnings that reasonable royalty is determined at the date of the commencement of infringement, and that it is the infringer's anticipated profit at that time, which is highly probative in determining the reasonable royalty

313. 914 F.2d 1473, 1485 (Fed. Cir. 1990), *clarified*, 22 U.S.P.Q.2d 1303 (Fed. Cir. 1991).
314. 739 F.2d 604, 617 (Fed. Cir. 1984).

it would have constructively agreed to pay on that date (instead of the actual reduced profit the infringer later made).[315]

B. Patent Owner Myths about Patent Damages

No. 1: *"Lost profits are guaranteed. None of the other products in the market has the patented advantages."*

Although the Federal Circuit's precedents have clearly facilitated the obtaining of lost profits awards, there are still many ways in which patent owners can delude themselves, and one is to take too facile a view of the concept of acceptable non-infringing substitute. In *Slimfold Mfg. Co. v. Kinkead Industries, Inc.*,[316] the Court caught one patent owner up short who believed that a substitute cannot be "acceptable" unless it has the advantages of the patented product. That belief is incorrect unless the patent owner can also show that consumers specifically wanted a device with those advantages. In *Slimfold*, the patent owner was unable to make that showing, and the Federal Circuit affirmed on that basis the district court's denial of lost profits.

No. 2: *"The upside for lost profits on lost sales of collateral products is huge. We sold them with the patented products in package deals."*

As is now unmistakably clear from the Court's 1995 *en banc* holding in *Rite-Hite*,[317] "package deals" alone will not justify an award of collateral lost profits. There must also be a "functional relationship" between the patented and unpatented items in the package. The patent owner in Rite-Hite learned this the hard way.

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315. *See, e.g., TWM Mfg. Co. v. Dura Corp.*, 789 F.2d 895, 898-900 (Fed. Cir. 1986) (affirming 30% royalty based on projection of 52.7% expected gross profit); *see also Hanson v. Alpine Valley Ski Area, Inc.*, 718 F.2d 1075, 1081 (Fed. Cir. 1983) (stating that, "[w]hether, as events unfurled thereafter, [Alpine Valley] would have made an actual profit, while paying the royalty determined as of [1972, the year infringement began], is irrelevant.").

316. 932 F.2d 1453, 1458 (Fed. Cir. 1991).

317. 56 F.3d 1538, 1544-1549 (Fed. Cir. 1995).

No. 3: *"Don't worry that our real damages are actually pretty small. The court will automatically increase them because of our high legal costs and infringer's bad conduct."*

There is an innate confusion between "adequate compensation" under section 284 and increased damages under that same section. A trial court may not manipulate the former in order to punish an infringer. The Federal Circuit has made this clear, once in a lost profits context, and more recently in a reasonable royalty case. In *Beatrice Foods Co. v. New England Printing & Lithographing Co.*,[318] the lost profits case, the district court was understandably angered by the defendant's deliberate destruction of sales records, and had set the infringer's gross sales as the measure of the patent owner's lost profits. The district court stated that as a tortfeasor the infringer had no manufacturing costs. The Federal Circuit *en banc* vacated this award, ordering a conventional redetermination of lost profits. In *Mahurkar v. C.R. Bard, Inc.*,[319] the reasonable royalty case, the Federal Circuit vacated the district court's 34.88% reasonable royalty determination, which included a 9% "kicker", apparently to compensate the patent owner for litigation expenses.

In both cases, the Federal Circuit noted that the concerns the district courts had with respect to the defendant's conduct or the plaintiff's legal expenses are properly addressed under the damages enhancement provision of section 284, providing those standards are met. In any event, that type of discretionary increase should be viewed as just that and not something to which the patent owner will be necessarily entitled.

No. 4: *"We'll ask for a 60% royalty, the infringer will offer 1% and the court will split the difference."*

The "split the difference" thinking is pervasive among patent owners (and sometimes infringers) and utterly foolhardy. Perhaps the classic example of this is *Polaroid Corp. v. Eastman Kodak Co.*,[320] where Polaroid argued for a 72.5% reasonable royalty for cameras and a 63.4% reasonable royalty for film, essentially equating its reasonable royalty claims to its claims for lost profits. Kodak countered with a detailed *Georgia-*

318. 899 F.2d 1171, 1175-1176 (Fed. Cir. 1990).
319. 79 F.3d 1572 (Fed. Cir. 1996).
320. 16 U.S.P.Q.2d 1481 (D. Mass. 1990), *amended on recons.*, 17 U.S.P.Q.2d 1711 (D. Mass. 1991).

Pacific analysis and contended a reasonable royalty would be 5%. Far from splitting the difference and awarding Polaroid about 35%, the District Court found Kodak's analysis persuasive and awarded Polaroid 10%, which was far closer to Kodak's number than to Polaroid's. The hundreds of millions of dollars that Polaroid undoubtedly left on the table by overreaching for 60-70% rather than contending for a 25% or 30% reasonable royalty is a stern lesson that reasonable rather than extreme positions are the key to the success of not only the infringer but the patent owner as well.

> ***No. 5:*** *"We'll get a huge royalty. The fact that the infringer had a fully designed acceptable noninfringing product in the wings in irrelevant, because it never sold it."*

This is the converse of the Infringer's Myth No. 2, where the unsold, non-infringing alternative does not help in defending a lost profits claim. Logically, it might seem that the same fact would not count here, but this is not necessarily a logical world, and the "rules" are different with a reasonable royalty. In *Zygo Corp. v. Wyko Corp.*,[321] the Federal Court also held that the existence of a device not on the market but "in the wings" could be relied upon in a reasonable royalty analysis. The Court stated that "Wyko [the infringer] would have been in a stronger position to negotiate for a lower royalty rate knowing it had a competitive noninfringing device 'in the wings'."

> ***No. 6:*** *"We'll get big dollars because the royalty base will include collateral products, not just the patented device."*

This myth is really just an overstatement. Under the "entire market value" rule, as explained in *Rite-Hite Corp. v. Kelley Co.*,[322] collateral products may be included in the royalty base if there is a functional relationship between them and the patented product. But, in *Rite-Hite*, the court found lacking the requisite functional relationship between the collateral product, a dock leveler, and the patented product, a docking restraint, and vacated the district court's decision to include dock levelers in the royalty base.

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321. 79 F.3d 1563 (Fed. Cir. 1996).
322. 56 F.3d at 1549.

XV. CONCLUSION

Patent damages have become an increasingly important part of business. Patents are being litigated at an ever increasing rate, with numerous large damage awards being handed down every year. At the same time, the number of patents applied for and issued is steadily increasing, meaning that the patent enforcement trend is unlikely to subside.

Yet most patent practitioners, corporate counsel, and non-attorney business people have little or no understanding of patent damages. What understanding they do have can be shaded by misperceptions of how to assess potential awards and exposure. By taking a closer look at some of the principles of patent damages, and attempting to gain a solid foundational understanding of some of the nuances, much of the mystery underlying patent damages can be resolved. Consequently, business decision makers will be in a much better position to gauge the effects of patent litigation and to determine whether the costs of obtaining one's own patents are sufficiently offset by the potential pay-off.