

Compulsory Licensing of Nonpracticing Patentees After *eBay v. MercExchange*

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ABSTRACT

The Supreme Court's 2006 decision in *eBay Inc. v. MercExchange, LLC* ended the Federal Circuit's practice of automatically granting permanent injunctions for patent infringement, auguring an era of compulsory licensing for certain patentees, particularly those who do not commercialize their patents. Denials of permanent injunctions and compulsory licensing were rare before *eBay* as most courts refused to assign a value to patents for ongoing infringement. An exception was the Second Circuit, which denied injunctions and issued compulsory licenses that awarded rates equal to the "reasonable royalty" that a patentee would have negotiated had there been no litigation—often less than the rate a patentee armed with an injunction might have negotiated. A review of subsequent Federal Circuit and district court decisions addressing post-verdict remedies where injunctions have not been issued reveals that federal courts are following the Second Circuit practice, reducing the value of patent infringement verdicts for nonpracticing patentees.

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I. INTRODUCTION

Requests for injunctive relief in patent infringement cases have not been the same since 2006’s Supreme Court decision *eBay Inc. v. MercExchange, L.L.C.*¹ As is now well known, *eBay* dramatically changed the way federal courts decide whether to grant injunctive relief after a patent infringement verdict, overturning decades of Federal Circuit precedent that granted a nearly automatic right to post-verdict injunctive relief. *eBay* held that courts can award injunctions only after evaluating traditional equitable principles, in particular using the standard four-factor balancing test. District courts no longer grant injunctive relief as a matter of course but only after considering evidence on all four factors.²

eBay also triggered a deeper change—the level of compensation a patentee should expect for patents adjudicated to be valid and infringed, particularly for “nonpracticing patentees” who do not commercialize their patents. After *eBay*, such patentees began facing the specter of compulsory licensing, as district courts began denying their injunction requests and ordering ongoing-royalty arrangements, a practice the Federal Circuit has affirmed is within district courts’ authority should they deny requests for permanent injunctions.³

While injunctions are officially invoked to fulfill the equitable right to not have one’s property appropriated without consent, injunction requests are often motivated by

¹ 547 U.S. 388 (2006).

² *Id.* at 391.

³ *Paice LLC v. Toyota Motor Corp.*, 504 F.3d 1293, 1314–15 (Fed. Cir. 2007); *Innogenetics, N.V. v. Abbott Labs.*, 512 F.3d 1363, 1379–81 (Fed. Cir. 2008).

the leverage that they provide in subsequent licensing negotiations.⁴ Patentees and other property rights holders who obtain injunctions acquire the ability to impose severe sanctions that allow them to charge a steep price for continued appropriation. This was exemplified by the pre-*eBay* 2006 settlement agreement between RIM, maker of the ubiquitous Blackberry email device, and NTP, the nonpracticing holder of patents that RIM was adjudicated to infringe. After exhausting its appeals and facing the threat of an injunction, RIM settled with NTP for \$612 million, almost thirty times the amount of damages awarded by the jury.⁵

Such compensation for nonpracticing patentees has been widely criticized and provided much of the motivation for recent congressional reform proposals.⁶ This conflict arises from two competing views on the compensation owed a patentee for the use of its patent. On one hand lies the belief that the market, through bilateral bargaining, can set the royalty rate more accurately than the judiciary. In this view, a successful patentee in an infringement action should be granted an injunction, after which the infringer and the patentee would negotiate the market (and therefore correct) rate.⁷ On the other hand are those who argue that awarding injunctive relief to patentees, particularly nonpracticing patentees and those holding patents of questionable validity or value, causes a “hold-up” problem in which such patentees can obtain royalties greater than the true value of their patents. In this view, overcompensating patentees distorts the incentives to innovate, design, and sell new technologies to the detriment of the economy and public interest.⁸

⁴ See Barton H. Thompson Jr., *Injunction Negotiations: An Economic, Moral, and Legal Analysis*, 27 STAN. L. REV. 1563, 1571 (1975).

⁵ Tom Krazit & Anne Broache, *BlackBerry Saved*, CNET NEWS, Mar. 3, 2006, available at http://www.news.com/BlackBerry-saved/2100-1047_3-6045880.html.

⁶ Recently introduced versions of the Patent Reform Act of 2009 included a controversial provision limiting the damages that could be awarded for infringement, including limits on the use of the “entire market value rule” and the reasonable royalty for a valid and infringed patent. See http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:s515is.txt.pdf; http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h1260ih.txt.pdf; Stephen Condon, *Controversial Provisions Remain in Patent Reform Bill*, CNET NEWS, Mar. 3, 2009, http://news.cnet.com/8301-13578_3-10187240-38.html?tag=mncol;txt. As of the time of writing, the Patent Reform Bill was approved by the Senate Judiciary Committee with a weaker version of damages reform, codifying the current method of damages calculations but increasing the gatekeeper function of the judiciary in determining the kinds of damages awards that will be allowed. See http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:s515rs.txt.pdf; Diane Bartz, *U.S. Senate Panel Approves Patent Reform*, REUTERS, Apr. 2, 2009, <http://www.reuters.com/article/companyNews/idUKN0150753120090402>.

⁷ See, e.g., WILLIAM N. LANDES & RICHARD A. POSNER, *THE ECONOMIC STRUCTURE OF INTELLECTUAL PROPERTY LAW* 7–8 (2003) (asserting that when intellectual property is “propertized” and made subject to a regime of legally enforceable property rights, remedies should be provided in order to coerce a would-be infringer into negotiating with the owner rather than just taking the owner’s property subject to the Court’s determination of the price, which is a less efficient method of resource allocation. Landes and Posner note that this argument depends on the assumption that intellectual property should be treated as property, which may not be appropriate).

⁸ See Carl Shapiro, *Injunctions, Hold-up, and Patent Royalties*, available at <http://faculty.haas.berkeley.edu/SHAPIRO/royalties.pdf> (and on file with the author); Mark A. Lemley & Carl Shapiro, *Patent Hold-up and Royalty Stacking*, 85 TEX. L. REV. 1991, 1995–2010 (2007) (arguing that

eBay and recent Federal Circuit cases have echoed this academic debate. In *Paice LLC v. Toyota Motor Corp.*,⁹ the Federal Circuit recognized that there may be inefficiencies in having a court decide upon a royalty rate that will govern the parties' prospective relationship, usually embodied in a complex licensing agreement consisting of many provisions of which the royalty rate is just one (and not always the most controversial). Such judicial monitoring takes courts outside of their more traditional purview—issuing and enforcing judgments and monitoring injunctions through contempt hearings. The *Paice* court commented that it would be preferable for the parties to “negotiate a license amongst themselves regarding future use of a patentee invention.”¹⁰ Judge Rader wrote separately to argue that courts should be *required* to remand the royalty issue to the parties or obtain their permission before setting an ongoing royalty rate.¹¹ He decried the majority's euphemistic styling of the remedy as an “ongoing royalty,” stating that “calling a compulsory license an ‘ongoing royalty’ does not make it any less a compulsory license.”¹² He further argued that “[a]s licenses are driven largely by business objectives, the parties to a license are better situated than the courts to arrive at fair and efficient terms.”¹³ A different Federal Circuit panel in *Innogenetics, N.V. v. Abbott Laboratories*¹⁴ reversed the federal district court's grant of a permanent injunction because it found that the jury's award of a reasonable royalty accounted for much of the revenue from future sales.¹⁵ The Federal Circuit remanded to the district court to “delineate the terms of a compulsory license,” claiming the added benefit of allowing the court to maintain jurisdiction and ensure compliance.¹⁶

While both Judge Rader's and the majority opinions in *Paice* reflect a preference for bilateral bargaining to resolve ownership and use of property rights, the *Innogenetics* panel embraced the court's role in setting a compulsory license (including for a commercial patentee). Those who believe that nonpracticing patentees are overcompensated when awarded injunctions also favor a greater judicial role in replacing injunctions with compulsory licensing arrangements. Surrounding *eBay* was criticism of the leverage wielded by “patent trolls” who obtained injunctions. “Patent troll” is the pejorative term for a company that does not manufacture or sell products, but only purchases patents in order to license them (such as NTP).¹⁷ As will be later shown, federal district courts have applied *eBay* to dramatically change the economics of patent litigation for nonpracticing patentees, including the so-called trolls.

injunctive relief results in overcompensation of nonpracticing patentees in subsequently negotiated license agreements). Cf. John M. Golden, “*Patent Trolls*” and *Patent Remedies*, 85 TEX. L. REV. 2111 (2007) (arguing that Lemley and Shapiro assert an unsupportable view of the appropriate compensation due a nonpracticing patentee, who may be undercompensated in some circumstances).

⁹ 505 F.3d 1293 (Fed. Cir. 2007).

¹⁰ *Id.* at 1315.

¹¹ *Id.* at 1316–17 (Rader, J., concurring).

¹² *Id.* at 1316.

¹³ *Id.* at 1317.

¹⁴ 512 F.3d 1363 (Fed Cir. 2008).

¹⁵ *Id.* at 1380–81.

¹⁶ *Id.* at 1381 n.9.

¹⁷ The term “patent troll” is a reference to the trolls in fairy tales who charge tolls at bridges and other crossings—the idea being that the patent troll is charging a toll for use of technology.

Prior to *eBay*, several Federal Circuit decisions accepted that injunctions might provide nonpracticing patentees with additional leverage, and disfavored compulsory licenses as judicial attempts to guess at a market rate.¹⁸ But such solicitude was not universal, for a different strain of federal courts contended that nonpracticing patentees were not entitled to the leverage of injunctions, which actually would overcompensate them.¹⁹ These courts argued that nonpracticing patentees do not need injunctions if they can be fully compensated by their normal licensing royalties—rates negotiated without litigation and without the leverage of injunctions. In this articulation, increased compensation for the patentee was subordinate to the manufacturing infringer’s right to sell products without paying monopoly rents. The underlying assumption was that the “appropriate” compensation was determined by the market without the factor of an impending injunction. As explained below, the Second Circuit championed this approach, and it is fast becoming the dominant judicial position with respect to nonpracticing patentees.

The per curiam opinion in *eBay* did not expressly address the dispute over nonpracticing patentees’ compensation. Justice Kennedy was not so reticent in his concurrence. Justice Kennedy specifically stated that injunctions give nonpracticing patentees inappropriate leverage in subsequent licensing negotiations, leading to overcompensation.²⁰ He placed the Supreme Court’s imprimatur on the Second Circuit view—that injunctions overcompensate nonpracticing patentees. He further reflected the view that rather than helping the market set the appropriate royalty rates, injunctions distorted that calculus and gave patentees higher monopoly rates than those justified by the true value of their patents. As shown below, a review of post-*eBay* federal district court decisions shows that though it is not the opinion of the Court, Kennedy’s concurrence has proven to be highly persuasive. District courts have almost without exception divided patentees into two camps—those who sell or manufacture products and compete against the infringers, and those who have not commercialized their inventions and seek to earn revenues from licensing. The former have generally been granted injunctions, whereas nonpracticing patentees have generally been denied.²¹ Almost every other factor has become subordinate to this division.

This article examines how courts have reacted to *eBay*, and to Kennedy’s concurrence, when ordering compulsory licenses for nonpracticing patentees. After *eBay*, courts had several options in dealing with post-verdict infringement upon denying injunctive relief. Though a patentee might not be entitled to an injunction under

¹⁸ See, e.g., *Fromson v. W. Litho Plate and Supply Co.*, 853 F.2d 1568, 1576, 1577 n.15 (Fed. Cir. 1988); *Stickle v. Heublein, Inc.*, 716 F.2d 1550, 1563 (Fed. Cir. 1983).

¹⁹ See, e.g., *Nerney v. New York, N.H. & H.R. Co.*, 83 F.2d 409 (2d Cir. 1936); *Am. Safety Device Co. v. Kurland Chem. Co.* 68 F.2d 734 (2d Cir. 1934).

²⁰ See *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 396–97 (2006).

²¹ See Andrew Beckerman-Rodau, *The Aftermath of eBay v. MercExchange*, 120 S. Ct. 1837 (2006): *A Review of Subsequent Judicial Decisions*, 895 J. PAT. & TRADEMARK OFF. SOC’Y 631, 633, 653–57 (2007) (noting that permanent injunctions are generally granted where patentee and infringer are direct marketplace competitors and are typically denied if the patent owner is a nonpracticing entity; other factors such as willful infringement, venue, the existence of a complex invention incorporating a patented feature, the willingness of the patent owner to license the invention and the likelihood of future infringement were not predictive).

traditional equitable principles (because, for example, an injunction might not be in the public interest), courts might have accounted for the leverage injunctions provide patentees when determining royalties for future infringement. Some pre-*eBay* Federal Circuit precedents may have sanctioned such an approach, under the rationale that patentees' patent rights deserve increased compensation. The Second Circuit view, and Justice Kennedy, would object to such an approach as contrary to the principle of avoiding overcompensation of nonpracticing patentees. The *eBay* per curiam opinion, the law of the land, did not state which approach to take.

As it turned out, federal courts have groped their way to a compulsory license doctrine that largely adopts the Second Circuit approach. These courts have decided, though not always expressly, that a nonpracticing patentee is entitled only to the royalty it would have earned had the parties executed a license, the reasonable royalty unimpacted by any leverage the patentee would have gained from an adjudication of its rights. These courts have both explicitly and implicitly rejected the idea that nonpracticing patentees might deserve the potentially higher royalty rates they might have obtained with injunctions, and have instead followed the logic of Justice Kennedy's *eBay* concurrence. Nonpracticing patentees should thus expect less compensation for their patents.

Part II examines the *eBay* decision and Justice Kennedy's concurrence, which lays out the rationale for denying nonpracticing patentees' requests for injunctive relief. Part III examines the legal and economic principles of the pre-*eBay* practice of compensating nonpracticing patentees with injunctive relief and other remedies, while Part IV examines the Second Circuit approach of denying injunctions and the leverage they provide to nonpracticing patentees. Finally, Part V reviews how district courts have interpreted and applied *eBay* to effectively adopt the minority approach sanctioned by Justice Kennedy, which dictates lower compensation for nonpracticing patentees.

II. *EBAY* AND INJUNCTIVE RELIEF

The story of *eBay* is well known. Plaintiff MercExchange won a verdict that *eBay* infringed its business method patents.²² The district court denied MercExchange's request for an injunction, applying the traditional four-factor equitable test for determining whether injunctive relief is appropriate: (1) whether the plaintiff will suffer irreparable harm if an injunction is not issued; (2) whether there is an adequate legal remedy, such as monetary compensation, in lieu of equitable injunctive relief; (3) whether the balance of hardships militates in favor of an injunction; and (4) whether the public interest would be served by an injunction. The district court concluded that the "plaintiff's willingness to license its patent" and "its lack of commercial activity in practicing the patent" were sufficient to establish that it would not suffer irreparable harm if *eBay* were not enjoined.²³

The Federal Circuit reversed the district court's ruling, applying its "general rule that courts will issue permanent injunctions against patent infringement absent

²² *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388 (2006).

²³ *Id.* at 393.

exceptional circumstances.” The Supreme Court reversed, finding that the Federal Circuit’s general rule improperly ignored the traditional four-factor test. The Court rejected the idea that there could be a general rule, unique to patents, presuming the right to an injunction.²⁴

The Court also criticized the district court for appearing to categorically refuse to grant injunctions to noncommercializing patentees who are willing to license their patents:

[T]raditional equitable principals do not permit such broad classifications. For example, some patent-holders, such as university researchers or self-made inventors, might reasonably prefer to license their patents, rather than undertake efforts to secure the financing to bring their works to market themselves. Such patent-holders may be able to satisfy this traditional four-factor test, and we see no basis for categorically denying them the opportunity do so.²⁵

The Supreme Court also affirmed *Continental Paper Bag Co. v. Eastern Paper Bag Co.*,²⁶ which held that courts can grant injunctive relief even for patent holders who may “unreasonably” decline to use their patents.²⁷ Thus, while holding that courts must review the four-factor test, Justice Thomas’ opinion for the unanimous Court was officially agnostic on the question of whether nonpracticing patentees were entitled to injunctive relief.

The per curiam opinion was accompanied by two concurrences somewhat in tension. Chief Justice Roberts cautioned that courts should not ignore the history of previous grants of injunctions, suggesting that the practice of routinely granting injunctions should continue. Roberts believed that the Court’s opinion properly affirmed district courts’ equitable discretion, but such discretion does not mean they write on an “entirely clean slate” but against the backdrop of the previous practice of granting injunctive relief. “When it comes to discerning and applying those standards, in this area, as others, ‘a page of history is worth a volume of logic.’”²⁸

Justice Kennedy’s concurrence struck a far different tone, focusing in particular on why nonpracticing patentees should be refused injunctions. Kennedy responded to Roberts’ affirmation of federal courts’ frequent granting of injunctions by noting that past cases were only as relevant as their factual circumstances allowed, and that the old rule of automatically issuing injunctions may need to give way to the realities of modern patent litigation.²⁹ Kennedy believed that while previously patent litigation involved manufacturing companies properly exploiting their patent monopolies in the market,

²⁴ *Id.* at 393–94.

²⁵ *Id.* at 393.

²⁶ 210 U.S. 405 (1908).

²⁷ *eBay*, 574 U.S. at 393.

²⁸ *Id.* at 395 (Roberts, C.J., concurring) (quoting *N.Y. Trust Co. v. Eisner*, 256 U.S. 345, 349 (1901)).

²⁹ *Id.* at 396.

many recent patent cases involved nonpracticing patentees seeking to extort high monopoly rents from the more legitimate, traditional economic enterprises:

In cases now arising, courts should bear in mind that in many instances the nature of the patent being enforced and the economic function of the patent holder present considerations quite unlike earlier cases. An industry has developed in which firms use patents not as a basis for producing and selling goods, but, instead, primarily for obtaining licensing fees. For these firms an injunction, and the potentially serious sanctions arising from its violation, can be employed as a bartering tool to charge exorbitant fees to a company that seeks to buy license to practice the patent. When the patented invention is but a small component of the product the companies seek to produce and the threat of an injunction is employed simply for undue leverage in negotiations, legal damages may well be sufficient to compensate for the infringement and an injunction may not serve the public interest.³⁰

Justice Kennedy essentially signaled that injunctions should be denied for patentees who make money by licensing patents rather than by making products. He attacked the assumption of injunctive relief in patent cases directly, particularly for nonpracticing patentees seeking the leverage injunctions gave them in licensing negotiations. Kennedy's short concurrence belies a deeper conflict in patent law—the appropriate compensation of a nonpracticing patentee. Until *eBay*, nonpracticing patentees were routinely deemed entitled to the leverage injunctions provided. Only a minority of courts approached compensation of nonpracticing patentees differently, a minority that *eBay*, and Justice Kennedy in particular, have revived.

III. COMPENSATION OF NONPRACTICING PATENTEES PRIOR TO *EBAY*

In 1908, the Supreme Court rejected the notion that injunctions should be denied to patentees who “unreasonably” refuse to practice their patents.³¹ The Court found that whether non-use promoted the progress of the useful arts as called for by the U.S. Constitution was irrelevant because at issue was simply the “rights and remedies” granted to patent holders.³² Patent rights were not created to give patentees the right to use the patented technologies, a right they already had. A patent provides the right to *exclude* others, unconditionally.³³ Given that absolute property right, it followed that a nonpracticing patentee had a right to exclude to the same extent as a practicing one.

The Federal Circuit eventually articulated a general rule that injunctions should be almost automatic, and applied it equally to nonpracticing patentees.³⁴ The right to

³⁰ *Id.* at 396–97.

³¹ *Cont'l Paper Bag Co. v. E. Paper Bag Co.*, 210 U.S. 405 (1908).

³² *Id.* at 423.

³³ *Id.* at 424.

³⁴ *Richardson v. Suzuki Motors Co.*, 868 F.2d 1226, 1246–47 (Fed. Cir. 1994). *Richardson* approved of an injunction for an individual inventor who was not manufacturing the patented invention, stating that

exclude preserved the full value of the invention, including, potentially, leverage to charge higher licensing rates. In *Smith International, Inc. v. Hughes Tool Company*,³⁵ the Federal Circuit, reviewing a district court's denial of a preliminary injunction,³⁶ declared that denying patentees injunctions would diminish the right to exclude and "seriously undermine" the constitutional purpose of patent rights to promote the progress of the useful arts.³⁷ Without the right to obtain an injunction, the patentees' right to exclude would be reduced to a fraction of its value, reducing the incentives for scientific and technological research.³⁸ Thus, injunctions may be appropriate for certain nonpracticing patentees to allow them the "full value" of their patents and justify their investments in research and development.

Commentators have argued that ensuring that patentees obtain compensation through bargaining was more economically efficient than government setting of compensation.³⁹ The prevalence of the view that private bargaining of property rights leads to more efficient outcomes than "judicial guesstimates" of appropriate royalty rates led to judicial and academic disapproval of compulsory licensing of patents.⁴⁰

Patentees were denied this leverage only when guilty of some wrongdoing rendering them undeserving of the right to negotiate higher royalty rates using the leverage of injunctions. In *Odetics v. Storage Technology Corp.*,⁴¹ the Federal Circuit affirmed the denial of an injunction in favor of a patentee guilty of laches (and thereby denied pre-complaint damages).⁴² "Using the leverage of an injunction, patentees could—in theory—extract at minimum a reasonable royalty from current users of the pre-complaint infringing products"—damages denied by virtue of the patentee's laches.⁴³ The Federal Circuit reasoned that infringers might be willing to pay far more than a

"the right to exclude recognized in a patent is but the essence of the concept of property." *Id.* (quoting *Connell v. Sears, Roebuck & Co.*, 722 F.2d 1542, 1548 (Fed. Cir. 1983)).

³⁵ 718 F.2d 1573 (Fed. Cir. 1983).

³⁶ *Id.* at 1577.

³⁷ *Id.* at 1578.

³⁸ *Id.*

³⁹ Economists have argued that legally established and enforceable property rights allow parties to determine market value through bargaining, leading to a more efficient outcome than a value established by government fiat. The former more accurately reflects the preferences of the parties involved. *See, e.g.*, R.H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON 1 (1960). Such "property rules" have been favored over "liability rules," under which violations of a property right are allowed, provided that the violating party later pays a judicially set compensation. *See* Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089, 1106–07 (1972).

⁴⁰ *See, e.g.*, *In re Mahurkar Double Lumen Hemodialysis Catheter Patent Litig.*, 831 F. Supp. 1354, 1396–97 (N.D. Ill. 1993) (granting an injunction because "[t]he injunction creates a property right and leads to negotiations between the parties. A private outcome of these negotiations—whether they end in a license at a particular royalty or in the exclusion of an infringer from the market—is much preferable to a judicial guesstimate about what a royalty should be."). *See also* Robert P. Merges, *Contracting Into Liability Rules: Intellectual Property Rights and Collective Rights Organizations*, 84 CAL. L. REV. 1293, 1305–06 (1996) (arguing that compulsory licensing induces a bargaining process in which the judicially-set rate functions as an inappropriate ceiling on the value ultimately allocated).

⁴¹ 185 F.3d 1259 (Fed. Cir. 1999).

⁴² *Id.* at 1273.

⁴³ *Id.*

“reasonable royalty” given their significant investment in their products, and that this windfall should not be given to a patentee without fully clean hands.⁴⁴

The inclination to automatically grant injunctions was in part motivated by an aversion to compulsory licensing, which was perceived to favor infringers over patentees. In *Dawson Chemical Co. v. Rohm & Haas Co.*,⁴⁵ which involved allegations of patent misuse under 35 U.S.C. § 271(d), the Supreme Court rejected the defendant’s argument that the patentee had unreasonably refused to license the infringer. The Court noted that

petitioners’ argument runs contrary to the long-settled view that the essence of a patent grant is the right to exclude others from profiting by the patented invention. If petitioners’ argument were accepted, it would force patentees either to grant licenses or to forfeit their statutory protection against contributory infringement. Compulsory licensing is a rarity in our patent system, and we decline to manufacture such a requirement out of § 271(d).⁴⁶

Forcing patentees to issue licenses was thus disfavored. Compulsory licensing would result in a judicially established rate that would function as a ceiling on the value awarded via subsequent bargaining.⁴⁷ In contrast, injunctions provide a property right that a patentee can easily enforce against an infringer. Under some circumstances (as exemplified by the NTP–RIM settlement described above), an enjoined infringer will pay more for a license than one subject to a judicially set rate.⁴⁸

Where a patentee cannot recover lost profits based upon lost sales or price erosion, the traditional remedy is the “reasonable royalty” determined by hypothesizing a negotiation between a willing licensor and a willing licensee.⁴⁹ Several pre-*eBay* Federal Circuit opinions argued that a reasonable royalty may undercompensate patentees, and may even be a form of unfair compulsory licensing, given that most prelitigation negotiations occur in circumstances where the validity and infringement of the patents at issue are not established, in contrast to the post-verdict setting where validity, enforceability, and infringement are unquestioned. In *Panduit Corp. v. Stahl Bros. Fibre Works, Inc.*,⁵⁰ the Sixth Circuit reviewed a district court’s award of a reasonable royalty for past damages and stated that

[t]he setting of a reasonable royalty after infringement cannot be treated, as it was here, as the equivalent of ordinary royalty negotiations among truly “willing” patent owners and licensees. That view would constitute a pretense that the infringement never happened. It would also

⁴⁴ *Id.* at 1273–74.

⁴⁵ 448 U.S. 176 (1980).

⁴⁶ *Id.* at 215 (citation omitted).

⁴⁷ Merges, *supra* note 38, at 1305–06.

⁴⁸ See Mark Schankerman & Suzanne Scotchmer, *Damages and Injunctions in Protecting Intellectual Property*, 32 RAND J. ECON. 199, 201–02, 206–08 (2001).

⁴⁹ *Rite-Hite Corp. v. Kelley Co.*, 56 F.3d 1538, 1554 (Fed. Cir. 1995).

⁵⁰ 575 F.2d 1152 (6th Cir. 1978).

make an election to infringe a handy means for competitors to impose a “compulsory license” policy upon every patent owner.⁵¹

This placed the infringer in a “heads I win, tails you lose” position. The infringer might never be sued, or if sued, it could defeat the allegations and pay nothing. Even if the patentee won, unless it could meet the enormous hurdles of proving lost profits, the infringer would simply be forced to pay the licensing fee initially demanded. The *Panduit* rationale was adopted in several Federal Circuit decisions holding that adequately compensating patentees pursuant to 35 U.S.C. § 284 may require more than an award of a royalty that would be negotiated in a prelitigation setting more favorable to the infringer/licensee.⁵²

Such Federal Circuit cases applied this reasoning equally to nonpracticing patentees. In *Fromson v. Western Litho Plate and Supply Co.*,⁵³ the Federal Circuit declared that it would be unjust to strictly apply the willing licensor–willing licensee approach for an individual inventor with weaker bargaining power than an infringing corporation: “Though the methodology must on occasion be used for want of a better, it must be carefully applied to achieve a truly reasonable royalty, for the methodology risks creation of the perception that blatant, blind appropriation of inventions patented by individual non-manufacturing inventors is the profitable, can’t-lose course.”⁵⁴ Properly valuing a patentee’s right to exclude was necessary to ensure adequate returns on investment in research and development for both corporations and ill-funded, nonmanufacturing individual inventors. *Fromson*’s rationale of awarding higher damages to a nonpracticing patentee, to ensure adequate return on research and development, echoes *Smith*’s justification of the automatic injunction rule, in which the right to exclude was preserved as a factor increasing the value of patent rights.⁵⁵

The Federal Circuit did not sanction arbitrary increases in damages, rejecting the notion of a “*Panduit* kicker” which automatically augmented a reasonable royalty rate.⁵⁶ The patent statutes provide for enhanced damages, including attorneys’ fees and treble damages, available after appropriate findings of willfulness and sufficient to avoid the “heads I win, tails you lose” scenario feared by *Panduit* and its Federal Circuit progeny.⁵⁷ Nonetheless, such pre-*eBay* Federal Circuit cases expressed solicitude for increasing the value of nonpracticing patentees’ patent rights, through automatic awards of injunctive relief.

Other federal courts, particularly in the Second Circuit, rejected these propositions. Under their approach, injunctions were not appropriate for nonpracticing patentees, as the leverage they provided caused them to be *overcompensated*.

⁵¹ *Id.* at 1158.

⁵² *See, e.g.*, *Fromson v. W. Litho Plate and Supply Co.*, 853 F.2d 1568, 1576, 1577 n.15 (Fed. Cir. 1988); *Stickle v. Heublein, Inc.*, 716 F.2d 1550, 1563 (Fed. Cir. 1983).

⁵³ 853 F.2d 1568 (Fed. Cir. 1988).

⁵⁴ *Id.* at 1574–75.

⁵⁵ *Id.* at 1575.

⁵⁶ *Mahurkar v. C.R. Bard, Inc.*, 79 F.3d 1572, 1581 (Fed. Cir. 1996).

⁵⁷ *Id.*

IV. THE SECOND CIRCUIT APPROACH: REDUCED COMPENSATION FOR NONPRACTICING PATENTEES

Commentators have criticized awards of injunctive relief to nonpracticing patentees, arguing that strengthening a nonpracticing patentee's right to exclude is anticompetitive and suppresses technology,⁵⁸ and that compulsory licensing regimes do not reduce innovation or incentives to invest in research and development.⁵⁹ Nonpracticing patentees have been accused of "extortion"⁶⁰ when they seek higher royalties wielding an injunction, under the assumption that compensation beyond that which is negotiated without litigation is a windfall.⁶¹

A strain of federal jurisprudence contrasts with the pre-*eBay* Federal Circuit cases described above by treating nonpracticing patentees' requests for injunctive relief with less favor, concluding that they should be compensated only by royalties based on the (potentially lower) rates negotiated by patentees prior to any litigation. At the turn of the century, a federal court in Pennsylvania in *Electric Smelting & Aluminum Co. v. Carborundum Co.* issued a compulsory license under these principles for a patentee not accused of wrongdoing.⁶² The plaintiff obtained a verdict that defendant Carborundum Co. infringed plaintiff's patents for the manufacture of silicide of carbon, the chemical name of the material carborundum, used at the time as an abrasive in several industries.⁶³ The plaintiff licensed its patent rights and did not manufacture carborundum. The court refused to issue an injunction, reasoning that the defendant would be bankrupted if it were enjoined, with little benefit to the plaintiff. The court noted that the plaintiff had licensed the patent to others, which would provide a basis for determining the damages that the defendant would owe for continued infringement.⁶⁴ Thus, long before the modern reasonable royalty doctrine, a federal court found that a patentee who simply sought to license infringers could be compensated for *future* infringement by the rate set by the patentee's other licenses—in effect, a reasonable royalty unmodified by the

⁵⁸ See Richard Dunford, *The Suppression of Technology as a Strategy for Controlling Resource Dependence*, 32 ADMIN. SCI. Q. 512 (1987); Karl M. Saunders, *Patent Nonuse and the Role of Public Interest as a Deterrent to Technology Suppression*, 15 HARV. J.L. & TECH. 389 (2002).

⁵⁹ Colleen Chien, *Cheap Drugs at What Price to Innovation: Does the Compulsory Licensing of Pharmaceuticals Hurt Innovation?*, 18 BERKELEY TECH. L.J. 853 (2003).

⁶⁰ See Robert E. Thomas, *Vanquishing Copyright Pirates and Patent Trolls: The Divergent Evolution of Copyright and Patent Laws*, 43 AM. BUS. L.J. 689 (2006).

⁶¹ *Fromson v. W. Litho Plate and Supply Co.*, 853 F.2d 1568, 1574–77 (Fed. Cir. 1988).

⁶² 189 F. 710 (C.C.W.D. Pa. 1900).

⁶³ *Id.* at 712.

⁶⁴ *Id.* at 713. Curiously, the plaintiff's only justification was that the defendant's refusal to be licensed encouraged others to contest the patent and made them unwilling to pay royalties, a reason which the court found insufficient given that the patent was held valid and infringed and thus suffered no loss of marketability. Otherwise, the plaintiff stated, "[i]n point of fact, an injunction is of great value and indeed of supreme importance to the complainant. Business reasons forbid the spreading upon record all the facts which make an injunction of prime importance to the complainant; some of them were disclosed in the oral argument, but many other weighty reasons exist which could be stated if circumstances permitted." *Id.* Thus, whether the plaintiff advanced an argument that an injunction would give it greater bargaining power over the infringer and allow it to negotiate a higher rate, and what the court might have thought of this argument, cannot be determined.

bargaining power an injunction would provide. Other federal courts followed with awards of compulsory licenses to nonpracticing patentees, in lieu of injunctions.⁶⁵

The Second Circuit most fully articulated a theory under which nonpracticing patentees should be denied injunctions *and* the potential additional compensation injunctions provide, rejecting their claimed need for an injunction to preserve the value of their patents. In *Nerney v. New York, N.H. & H.R. Co.*,⁶⁶ the Second Circuit vacated an injunction preventing the defendant from using railroad cars that infringed the plaintiff's hand brake patent.⁶⁷ The Second Circuit found that an injunction would greatly burden the defendant while furnishing little benefit to the patentee, as "it is recognized that [if] the only real advantage to a plaintiff in granting the injunction would be to strengthen its position in negotiating a settlement, an injunction should not issue."⁶⁸ Similarly, in *American Safety Device Co. v. Kurland Chemical Co.*,⁶⁹ the Second Circuit affirmed the denial of an injunction where monetary damages were sufficient.⁷⁰

Nerney's implication that injunctions are unjustified when they merely serve as bargaining leverage for nonpracticing patentees was the express rationale for the Second Circuit's more recent denial of injunctive relief in *Foster v. American Machine & Foundry Co.*⁷¹ In *Foster*, the plaintiff obtained a verdict of infringement of its welding system patent and obtained damages for a reasonable royalty. The Second Circuit affirmed the district court's decision to deny an injunction in lieu of a compulsory license at the royalty fixed by the court, finding that injunctive relief "is not intended as a club to be wielded by a patentee to enhance his negotiating stance."⁷² Because the appellant did not manufacture a product, the district court concluded that the infringer would suffer hardship without any benefit to the patentee.⁷³

The Second Circuit's doctrine of denying nonmanufacturing patentees' compensation via the bargaining leverage provided by an injunction was not adopted by the Federal Circuit. As explained above, until *eBay*, nonmanufacturing patentees were entitled to the same fruits of an injunction. But Justice Kennedy's concurrence breathed new life into the Second Circuit's approach, for he adopted the Second Circuit's conclusion: that nonpracticing patentees whose only business is to profit from licensing or suing upon their intellectual property should not be able to use an injunction to force legitimate manufacturing companies to overcompensate them, ultimately harming the

⁶⁵ See, e.g., *Allied Research Prods., Inc. v. Heat Bath Corp.*, 300 F. Supp. 656, 657 (D.C. Ill. 1969) (ordering the plaintiffs to grant the defendant a license "on the same royalty basis as plaintiffs were granting licenses to other manufacturers who were competing with the plaintiffs and defendants," even though it found the plaintiff's patents infringed and noted that the defendant's infringement was indefensible); *Nerney v. New York, N.H. & H.R. Co.*, 83 F.2d 409 (2d Cir. 1936); *Foster v. Am. Machine & Foundry Co.*, 492 F.2d 1317 (2d Cir. 1974).

⁶⁶ 83 F.2d 409 (2d Cir. 1936).

⁶⁷ *Id.* at 409–10.

⁶⁸ *Id.* at 411.

⁶⁹ 68 F.2d 734 (2d Cir. 1934).

⁷⁰ *Id.* at 734–35.

⁷¹ 492 F.2d 1317 (2d Cir. 1974).

⁷² *Id.* at 1324 (citing, inter alia, *Nerney*, 83 F.2d at 410–11).

⁷³ *Id.*

economy and the public. After *eBay*, district courts were faced with the question of how to apply the equitable principles of *eBay* to the question of how nonpracticing patentees should be able to value their patents.

V. COMPULSORY LICENSES FOR NONPRACTICING PATENTEES AFTER *EBAY*: THE ONGOING ROYALTY

The federal courts' application of *eBay* has not been encouraging for nonpracticing patentees, as district courts have largely denied their injunction requests. The Federal Circuit has affirmed the discretion of district courts to issue compulsory licensing orders, but has not provided principles by which the licenses are to be valued. The district courts' decisions, however, have largely denied patentees the compensation that could be attributed to the bargaining leverage provided by injunctions.

A. The Federal Circuit Affirms That District Courts Can Order "Ongoing Royalties" or "Compulsory Licenses"

Although the Federal Circuit has commented on district courts' power to award patentees ongoing royalties or compulsory licenses in lieu of injunctions in several cases since *eBay*, it has not provided principles by which courts should set the value of the license. The Federal Circuit has left such valuation within district courts' discretion, though requiring courts to hold hearings evaluating evidence on the appropriate royalty to be issued rather than perfunctorily adopting a rate (such as a jury determination of a reasonable royalty).

In *Paice LLC v. Toyota Motor Corp.*, the Federal Circuit approved of the Eastern District of Texas' authority to award an ongoing royalty, but vacated the district court's adoption of the jury's royalty rate in calculating past damages.⁷⁴

After the jury found that Toyota's hybrid vehicles infringed the plaintiff's patents, the district court denied the plaintiff's request for an injunction because it did not commercialize the patents but only sought to obtain licensing royalties.⁷⁵ Judge Folsom had explicitly noted that the bargaining advantage provided by injunctions did not merit the award of an injunction to the plaintiff, a nonpracticing patentee:

The court notes that monetary relief could result in lower licensing rates than the Plaintiff would desire. The court also recognizes that, if an injunction were to issue, the Plaintiff would have a more impressive bargaining tool. This consideration, however, doe [sic] not replace the four-factor test that must be satisfied for equitable relief.⁷⁶

⁷⁴ 504 F.3d 1293, 1315 (Fed. Cir. 2007).

⁷⁵ *Paice LLC v. Toyota Motor Corp.*, 2006 U.S. Dist. LEXIS 61600, at *11–15 (E.D. Tex. Aug. 16, 2006).

⁷⁶ *Id.* at *15 n.3.

The district court then held that the jury's royalty rate was appropriate for a post-judgment license.⁷⁷ While it did not say whether the availability of that "impressive bargaining tool" should be calculated in the compulsory license rate, by relying on the jury's reasonable royalty it effectively failed to factor the requested injunction into the royalty calculation.

On appeal, the Federal Circuit reviewed Paice's challenge to the royalty award (but not to the denial of an injunction itself).⁷⁸ The Federal Circuit called the award an "ongoing royalty," (rejecting the term "compulsory license,") and held that if necessary for an effective remedy, such rates are within the statutory power of 35 U.S.C. § 283, which authorizes injunctive relief.⁷⁹ The Federal Circuit vacated the award because it could not evaluate whether the district abused its discretion without understanding how it had determined the award. It remanded for a further hearing where the parties could present evidence. The Federal Circuit did not criticize Judge Folsom's rejection of the argument that an injunction was required because of the bargaining leverage it provided, and did not opine on whether such leverage should be incorporated into the award.

In *Innogenetics*, the Federal Circuit overturned the district court's granting of a permanent injunction and remanded to the district court for delineation of the terms of a compulsory license.⁸⁰ The Federal Circuit did not specify the terms to be ordered by the district court, but suggested that future sales of the infringing products could be conditioned on payment of the running royalty used by the jury to calculate past damages (and thus, without the leverage of an injunction).⁸¹

The Federal Circuit provided a counterpoint to *Paice* and *Innogenetics* in *Amado v. Microsoft Corp.*,⁸² which involved a determination of the appropriate license rate for infringement occurring after an injunction has been issued and then stayed pending appeal. After the jury rendered a patent infringement verdict in favor of Amado, the district court issued a permanent injunction against Microsoft that it stayed pending appeal, while ordering Microsoft to deposit \$2.00 per unit sold in an escrow account.⁸³ The district court ultimately dissolved the injunction under *eBay*, which was decided during the appeal.⁸⁴ One of the issues was the value of the royalties owed to Amado for Microsoft's sales while the injunction was in effect but stayed. The district court had ordered a rate of \$0.12 per unit, which was treble the jury's reasonable royalty of \$0.04 per unit.⁸⁵

After rejecting Amado's argument that the district court was bound by the \$2.00 royalty set for the escrow, the Federal Circuit rejected Microsoft's arguments that the

⁷⁷ *Id.* at *19.

⁷⁸ *Paice LLC v. Toyota Motor Corp.*, 504 F.3d 1293 (Fed. Cir. 2007).

⁷⁹ *Id.* at 1313 n.13, 1315.

⁸⁰ 512 F.3d 1363, 1380–81 (Fed. Cir. 2008).

⁸¹ *Id.* at 1381.

⁸² 517 F.3d 1353 (Fed. Cir. 2008).

⁸³ *Id.* at 1356.

⁸⁴ *Id.*

⁸⁵ *Id.* at 1356–57.

district court was required to use the jury's reasonable royalty of \$0.04 per unit, noting that a royalty based on a prelitigation hypothetical negotiation was much different from a post-verdict rate.⁸⁶ However, the Federal Circuit also rejected the district court's stated reason of trebling the jury's rate based on a finding of willful infringement, finding that willfulness could not be an issue "when the infringement is permitted by a court-ordered stay."⁸⁷ The Federal Circuit also distinguished Microsoft's position from that of Toyota's in *Paice*, where the court was to set a royalty after denying injunctive relief.⁸⁸ The Federal Circuit thus created another class of infringers for whom rates must be determined—those who are subject to an injunction that is stayed. This likely minimal class is in a different posture from those denied injunctions, and they may receive a rate higher than the reasonable royalty.

B. Federal District Courts Reject Incorporation of the Bargaining Leverage of Injunction into the Reasonable Royalty Calculus

It is unlikely that district courts will incorporate the bargaining power of injunction into the ongoing royalty calculus. The nature of the courts' application of equitable principles in deciding whether to issue injunctions reveals an inherent tendency against such valuation. The practice of awarding injunctions to practicing patentees, while denying them to nonpracticing patentees, ultimately rests on the conclusion that practicing patentees have more valuable rights than nonpracticing patentees. Officially, patentees who compete with infringers and can show a potential for lost sales, lost market share, or harm to their brand will be able to establish the irreparable harm and inadequacy of legal remedies necessary to justify an injunction; nonpracticing patentees will more often be forced to issue licenses to adjudicated infringers because of their inability to show such future harm. But beneath this official veneer lies certain normative statements embedded in district courts' decisions. One court stated that a company "has a right, granted by Congress, not to assist its rival with the use of proprietary technology."⁸⁹ Another court noted that "intellectual property enjoys its highest value when it is asserted against a direct competitor in the [patentee's] market."⁹⁰ In an echo of *Panduit*, one court stated that a competitor who, after a "long, expensive, and arduous trial," finally forces an infringer to pay what it would have paid in a hypothetical negotiation should not be allowed to continue to use the patentees' invention as its own by paying the same fee as would be charged in a license.⁹¹ A commercializing patentee would also be denied the ability to control the use of its technology through other licensing terms.⁹² Thus, manufacturing patentees are entitled to legally exercise their right to exclude, or, if they

⁸⁶ *Id.* at 1361–62 (citing cf. *Paice LLC v. Toyota Motor Corp.*, 504 F.3d 1293, 1317 (Fed. Cir. 2007)).

⁸⁷ *Id.* at 1362.

⁸⁸ *Id.*

⁸⁹ *Novozymes A/S v. Genencor Int'l, Inc.*, 2007 U.S. Dist. LEXIS 10577, at *55 (D. Del. Feb. 16, 2007).

⁹⁰ *Visto Corp. v. Seven Networks, Inc.*, 2006 U.S. Dist. LEXIS 91453, at *12 (E.D. Tex. Dec. 19, 2006).

⁹¹ *Innogenetics, N.V. v. Abbott Labs.*, 2007 U.S. Dist. LEXIS 193, at *73 (E.D. Wis. Jan. 3, 2007).

⁹² *TransOcean Offshore Deepwater Drilling, Inc. v. GlobalSantaFe Corp.*, 2006 U.S. Dist. LEXIS 93408, at *19 (S.D. Tex. Dec. 27, 2006).

desire, to earn compensation above what they would have obtained in hypothetical prelitigation negotiation.⁹³

Nonpracticing patentees do not deserve these considerations in the modern, post-*eBay* articulation. As shown below, patentees that have been denied injunctions have obtained compensation limited to the “reasonable royalty” awarded for past damages, unmodified by the leverage an injunction would have provided in actual negotiations. Without expressly doing so, district courts have implicitly applied *eBay* to adopt the Second Circuit’s doctrine of limiting nonpracticing patentees to compulsory licenses at royalty rates negotiated without litigation.

Particularly exemplary is the Eastern District of Virginia’s handling of MercExchange’s injunction request. The Supreme Court had remanded the case to the district court to decide the issue under the four-factor equitable test and in conformance with the Supreme Court’s opinion.⁹⁴ The district court allowed additional discovery and then heard the renewed motion. Additional facts were presented, including discussions between MercExchange and uBid, a potential competitor of eBay. uBid obtained a nonexclusive license to MercExchange’s patent portfolio, and briefly negotiated an exclusive license in exchange for a 25 percent interest in the company.⁹⁵

In denying injunctive relief for MercExchange, the district court’s decision embodies many of the criticisms of the asserted overcompensation of nonpracticing patentees. Animating its analysis was its finding that MercExchange sought not to commercialize the patents but rather to maximize licensing revenue. Unlike self-made inventors or university researchers who license their inventions for development because they lack capacity, the court noted that MercExchange’s strategy was to license to companies who are already market participants and who will enter into license agreements to avoid the costs of litigation:

Such consistent course of litigating or threatening litigation to obtain money damages by a company of the employees, the inventor of the patents, a former patent attorney, indicates that MercExchange has utilized its patents as a sword to extract money rather than as a shield to protect its right to exclude or its market share, reputation, goodwill, or name recognition, as MercExchange appears to possess none of these.⁹⁶

The uBid discussions were consistent with this characterization. MercExchange agreed only to a nonexclusive license for royalties, and the discussions for an exclusive

⁹³ Competitors must ensure that they provide sufficient evidence of future lost sales, market share, or brand name or reputation loss, and not simply rely upon their status as competitors to ensure the successful grant of an injunction. *See Praxair, Inc. v. Atmi, Inc.*, 2007 U.S. Dist. LEXIS 21589, at *8–11 (D. Del. Mar. 27, 2007).

⁹⁴ *MercExchange, L.L.C. v. eBay Inc.*, 500 F. Supp. 2d 556 (E.D. Va. 2007).

⁹⁵ *Id.* at 561–62.

⁹⁶ *Id.* at 572.

license appeared to be motivated by a desire to position MercExchange for an injunction hearing.⁹⁷

The court disapproved of MercExchange's use of its patent rights, distinguishing the nonpracticing patentee who seeks to extract as much rent as possible from its monopoly position from more favored practicing patentees or patentees who use license fees to develop more technologies. In analyzing whether MercExchange had an adequate remedy at law if denied an injunction, the court noted that MercExchange's "established course of conduct is to negotiate fees and royalties for alleged infringement" such that court-ordered monetary damages would be adequate compensation.⁹⁸

While finding that the balance of hardships favored neither party, the court noted that MercExchange's business plan of obtaining fees from threatened litigation suggests it would not suffer hardship from denial of injunctive relief.⁹⁹ As far as the public interest was concerned, eBay was a multi-billion dollar corporation with a substantial impact on the economy, while MercExchange was "a company with two employees that work out of their homes and appear to specialize in litigation and obtaining royalties for licenses based on the threat of litigation."¹⁰⁰

Accordingly, the court decided that MercExchange's "track record for pursuing monetary recovery through litigation" and its pursuit of an injunction "as a bargaining chip to increase the bottom line" militated against an award of injunctive relief.¹⁰¹ There could not be a clearer exposition and adoption of the Second Circuit's doctrine of denying nonpracticing patentees' monopoly rents from their patents.

Other courts have reached similar conclusions. In *z4 Technologies, Inc. v. Microsoft Corp.*,¹⁰² the Eastern District of Texas issued the first post-*eBay* denial of a plaintiff's request for a permanent injunction, capping any future compensation the patentee could obtain at the jury's reasonable royalty. *z4* had obtained a jury verdict of \$115 million in damages against Microsoft, whose Windows and Office software was found to infringe *z4*'s product activation software patents.¹⁰³ The court held that *z4* would not suffer irreparable harm if an injunction was denied since it would not lose profits, brand name recognition, or market share as a result of Microsoft's continued sales of infringing products.¹⁰⁴ The court specifically noted Justice Kennedy's admonition that trial courts consider the economic position of the patent holder (i.e., whether the patent holder was a competitor who commercialized the invention or merely sought to earn licensing revenues) and the relative importance of the patented technology.¹⁰⁵ The court

⁹⁷ *Id.* at 576–77.

⁹⁸ *Id.* at 583 n.24.

⁹⁹ *Id.* at 584.

¹⁰⁰ *Id.* at 587.

¹⁰¹ *Id.* at 588.

¹⁰² 434 F. Supp. 2d 437 (E.D. Tex. 2006).

¹⁰³ *Id.* at 438–39.

¹⁰⁴ *Id.* at 440.

¹⁰⁵ *Id.* at 441 (citing *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 396 (2006) (Kennedy, J., concurring)).

found that z4 could be compensated by the reasonable royalty rate found by the jury.¹⁰⁶ The court then severed z4's causes of action for post-verdict infringement and ordered Microsoft to file quarterly reports in the new action.¹⁰⁷ Thus, the court decided that the jury's reasonable royalty was adequate to compensate the patentee for future infringement, unmodified by the bargaining power an injunction would have provided.

In *Finisar Corp. v. DirecTV Group, Inc.*,¹⁰⁸ the Eastern District of Texas granted a compulsory license with a thorough analysis of the factors determining the royalty rate. The *Finisar* court denied a request for a permanent injunction after the plaintiff had obtained a verdict of infringement,¹⁰⁹ and ordered an ongoing royalty of \$1.60 for each set-top box activated by or for DirecTV.¹¹⁰ The court noted that there was no established royalty rate, and it therefore relied on royalty rates for comparable patents. The nonexclusivity of the license and the fact that Finisar was not trying to exploit a patent monopoly itself but was trying to license the patents "would tend to lower the rate." In addition, the parties were not competitors, and Finisar would benefit from a higher volume of DirecTV sales and thus would want to charge a lower rate.¹¹¹ The infringed patent was important, but not necessarily more important than the 200 patents involved in the infringing product.¹¹² The court then concluded that the rate would be determined through the prism of a hypothetical negotiation between a willing licensor and willing licensee, based largely on the rates paid for other, comparable patents.¹¹³ The \$1.60 rate was justifiably higher than the jury's rate because the passage of seven years would inflate its value.¹¹⁴

The court rejected Finisar's argument that an injunction was needed to allow the market to set the license rate. Finisar had argued that the "market rate" was the rate set by the parties, with Finisar holding the enormous leverage of an injunction and DirecTV facing shutdown of its entire business.¹¹⁵ Finisar's counsel even referred to the RIM-NTP settlement as indicating that the "market rate" might be much larger than reasonable royalty of a jury verdict, remarking that "when the jury awarded \$23 million, the parties eventually sold for \$612.5 million. Who would have thought that the right to exclude in that case was worth over \$600 million?"¹¹⁶ The court rejected this argument and denied

¹⁰⁶ *Id.* at 440–41.

¹⁰⁷ *Id.* at 444.

¹⁰⁸ 2006 U.S. Dist. LEXIS 76380 (E.D. Tex. July 7, 2006).

¹⁰⁹ *Id.* at *4–5.

¹¹⁰ The district court's royalty calculus, spelled out in the transcript of the hearing but not its published order, consisted of a review of the fifteen factors employed in *Georgia Pacific Corp. v. U.S. Plywood Corp.*, 318 F. Supp. 1116 (S.D.N.Y. 1970), *aff'd*, 446 F.2d 295 (2d Cir. 1971) after the receipt of additional evidence. See Transcript of Hearing at 127–36, *Finisar*, 2006 U.S. Dist. LEXIS 76380 (No. 1:05-CZ-264). Judge Clark said that "the court recognizes that the *Georgia Pacific* factors are frequently used in terms of instructing the jury on a reasonable royalty in a hypothetical situation in the past, but it doesn't see any reason at all why these same factors can't be used in—to help the Court analyzing what would be an appropriate royalty amount." *Id.* at 127.

¹¹¹ *Id.* at 129–30.

¹¹² *Id.* at 133.

¹¹³ *Id.* at 135 (utilizing factors 15 and 2, respectively, from *Georgia Pacific*, 318 F. Supp. at 1120).

¹¹⁴ *Id.* at 135–36.

¹¹⁵ *Id.* at 8–9, 14–15.

¹¹⁶ *Id.* at 15.

injunctive relief.¹¹⁷ It also apparently rejected the notion that the market rate should account for Finisar's hypothetical leverage, given that the license rate awarded was not significantly higher than the rate for past damages, unlike NTP's settlement recovery from RIM.¹¹⁸

Other district courts, such as the *Paice* court discussed above,¹¹⁹ have followed suit in awarding compulsory licenses based on royalty determinations without calculating the leverage provided. The Eastern District of Michigan also did so in *Voda v. Cordis Corp.*¹²⁰ Defendant Cordis Corporation was found to have infringed an individual inventor's angioplasty guide catheter patents. The court found that there was no irreparable harm and that monetary damages were adequate, and ordered a compulsory license using the rate assessed by the jury.¹²¹ Thus, the court perfunctorily concluded that the jury's rate was appropriate and that no post-verdict action by Voda was needed.

In *Sundance, Inc. v. Demonte Fabricating Ltd.*, the Eastern District of Michigan denied a patentee's injunction request in part because it could not demonstrate any potential lost sales.¹²² Plaintiff Sundance unsuccessfully argued that it needed an injunction to prevent its legitimate licensees from suffering competitive disadvantage due to defendant's infringing sales. The court found that a monetary award was adequate because Sundance licensed patents to others, and offered to license the patent in question to the defendant prior to filing the lawsuit. The court noted that this conduct "indicates an interest only in obtaining money damages against accused infringers."¹²³ The *Sundance* court thus followed Kennedy's intimation that patentees who did not commercially use their patents do not deserve an injunction—and strongly implied that any reasonable royalty should be limited to the rate set by the jury or an established rate based on actual or other rates.¹²⁴

A rare decision granting an injunction to a nonpracticing patentee further reveals that courts will try to incorporate the bargaining leverage provided by injunctions in setting a compulsory license. In *Commonwealth Scientific and Industrial Research Organization v. Buffalo Technology, Inc.*,¹²⁵ the patentee was a scientific research organization of the Australian Federal Government that had patented technology deemed fundamental to certain iterations of the IEEE 802.11 wireless standard. The defendant, Buffalo Technology, infringed the patents through the production and sale of wireless

¹¹⁷ *Id.* at 11–14, 135–36.

¹¹⁸ *Id.* at 135–36 (setting the rate at \$1.60, slightly above the jury's rate).

¹¹⁹ *See supra* p. 39–40.

¹²⁰ 2006 U.S. Dist. LEXIS 63623 (W.D. Okla. Sept. 5, 2006).

¹²¹ *Id.* at *20.

¹²² 2007 U.S. Dist. LEXIS 158, at *7–8 (E.D. Mich. Jan. 4, 2007).

¹²³ *Id.* at *9.

¹²⁴ The Eastern District of Michigan granted Sundance's renewed motion for an injunction after Sundance was awarded a large money judgment for damages and finding that defendant Demonte's solvency and ability to pay that judgment was called into question. *See Sundance v. Demonte Fabricating Ltd.*, 2007 U.S. Dist. Lexis 77728 (E.D. Mich. Oct. 19, 2007). The court's decision was not a repudiation of its finding that an injunction was not needed to satisfy Sundance's right to future compensation, but a response to Sundance's need to vindicate its past damages.

¹²⁵ 492 F. Supp. 2d 600 (E.D. Tex. 2007).

products utilizing the standard.¹²⁶ The court held that the patentee would suffer irreparable harm to its licensing program and reputation as a research organization that could not be redressed by monetary compensation.¹²⁷ In noting the inadequacy of monetary damages in the form of royalties paid under a compulsory license, the court stated that “[t]he royalty payment would be extrapolated from a determination of Buffalo’s past sales, which may not adequately reflect the worth of the patent today to Buffalo.”¹²⁸ The court thus assumed that the royalty would be based on past damages and sales alone, and not based on the present positions of the parties. While this can no longer be the case after *Paice*’s requirement of a full evidentiary hearing where more current data could be presented, it is notable that the court took into account the fact that the royalty could be too low in deciding to award an injunction. While granting an injunction to a nonpracticing patentee, the court acknowledged that a compulsory license rate would not reflect the leverage provided by an injunction in actual negotiations between the parties.

VI. CONCLUSION

In the regime of compulsory licensing for nonpracticing patentees following injunction denials under *eBay*, federal courts are likely to award moderately compensatory licenses that approximate royalties reached under *George Pacific Corp. v. U.S. Plywood Corp.*¹²⁹ and are potentially lower than that which might have been negotiated had the court issued an injunction. These cases seem to follow Justice Kennedy’s assertion that nonpracticing patentees are overcompensated when they obtain injunctions, regardless of the importance of their patent or proof of irreparable harm. By reducing their compensation, these courts and Justice Kennedy have given effect to some of the industry and academic concerns that the patent rights of nonpracticing patentees may be anticompetitive and injurious to the economy if given the protection they have traditionally been accorded.

This result did not necessarily follow from pre-*eBay* Federal Circuit case law, which had asserted that unless a patentee had unclean hands (i.e., was guilty of antitrust violations), the patentee’s right to enforce an injunction may legitimately give it leverage in negotiating a licensing royalty.¹³⁰ Several courts held that infringers should not be given incentives to infringe through the award of reasonable royalties based on hypothetical prelitigation negotiations, even where nonpracticing patentees are involved. The Federal Circuit rejected the notion of a “*Panduit* kicker”—an arbitrary increase in the reasonable royalty rate—largely because patentees could obtain treble damages or attorney fees after appropriate findings of willful infringement, options not necessarily available in a compulsory license regime. Instead, district courts have followed Justice Kennedy and the Second Circuit’s approach, rejecting the notion that an injunction can legitimately give nonpracticing patentees leverage in negotiations with infringers. Such

¹²⁶ *Id.* at 602.

¹²⁷ *Id.* at 604.

¹²⁸ *Id.* at 606.

¹²⁹ 318 F. Supp. 1116 (S.D.N.Y. 1970). *See supra* notes 110, 113 and accompanying text.

¹³⁰ *See supra* p. 34.

patentees cannot rely upon judicial solicitude of their adjudicated patent rights in seeking compensation for future infringement.