

## Patent Assertion Entities, Reasonable Royalties, and a Restitution Perspective

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The changing nature of patent litigation over the last fifty years has forced patent stakeholders to think differently about remedies for patent infringement.<sup>1</sup> A major catalyst for changes in how courts award specific remedies such as injunctions and attorney fees has been the successful assertion of patents by entities that do not practice the patent (aka Non-Practicing Entities (NPEs), Patent Assertion Entities (PAEs), or, colloquially, patent trolls).<sup>2</sup> Since lost profits are not available to those who do not make, use, or sell the invention, these claimants must recover no less than a reasonable royalty. However, commentators disagree as to how this reasonable royalty should be determined and what theories of recovery should apply.<sup>3</sup> In their forthcoming paper, Professors John M. Golden & Karen E. Sandrik argue that the law of restitution is useful in thinking about how a court can determine a reasonable royalty in the

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1. See, e.g., W. Keith Robinson, *Awarding Attorney Fees and Deterring "Patent Trolls"*, 20 LEWIS & CLARK L. REV. 281 *passim* (2016) (discussing the impact of recent Supreme Court decisions concerning the remedy of awarding attorney fees to the prevailing party).

2. See, e.g., Daniel Harris Brean, *Ending Unreasonable Royalties: Why Nominal Damages are Adequate to Compensate Patent Assertion Entities for Infringement*, 39 VT. L. REV. 867, 888 (2015) (arguing that the current interpretation of the law permits patent assertion entities to receive windfall damage awards improperly). Whether patent assertion entities are good or bad for the patent system is beyond the scope of this essay. However, there is little doubt that this modern trend in patent litigation affects the debate about reasonable royalty determinations.

3. See Caprice L. Roberts, *The Case for Restitution and Unjust Remedies in Patent Law*, 14 LEWIS & CLARK L. REV. 653, 653 (2010) (arguing that restitution and unjust enrichment remedies should be available for patent infringement); cf. Amanda Frye, *"Inextricably Intertwined": A Restitution Perspective in Patent Remedies*, 26 HARV. J.L. & TECH. 669, 670 n.3 (2013) (arguing for restitution damages for patent infringement).

absence of other types of proof.<sup>4</sup> This essay briefly describes the debate about reasonable royalties and explains how Golden & Sandrik inject the conversation with new life by using restitution theory as a lens for thinking differently about how a court might determine reasonable royalties in a way that aligns with the underlying purpose of the patent system.

To understand why patent stakeholders care about reasonable royalty determinations, one must consider the current climate of patent litigation. Over the last fifteen years, PAEs have been prominent participants in patent litigation.<sup>5</sup> While there are numerous characterizations of PAEs, the most despised of these entities, patent trolls, use the threat and cost of patent litigation to generate revenue.<sup>6</sup> Some blame the U.S. civil procedure system for the proliferation of patent troll litigation.<sup>7</sup> In response, the Supreme Court recently opined on cases concerning the remedies of injunctive relief and attorney fees in ways that impact lawsuits involving all PAEs.<sup>8</sup> However, how a court should determine a reasonable royalty in a suit involving a PAE is still an open question.

Section 284 of the Patent Act indicates that reasonable royalties are a floor for recovery.<sup>9</sup> There are various methods a court may use to calculate a reasonable royalty.<sup>10</sup> The debate over which

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4. John M. Golden & Karen E. Sandrik, *A Restitution Perspective on Reasonable Royalties*, 36 REV. LITIG. (forthcoming 2017).

5. PAEs are also referred to as patent trolls. “Patent troll” was first used in 2001 to describe an entity that, instead of commercializing its patented technology, chose to license the technology to others. Brenda Sandburg, *Trolling for Dollars*, THE RECORDER (July 30, 2001), <http://www.therecorder.com/id=900005370205/Trolling-for-Dollars?slreturn=20150911181220>.

6. See Eric Rogers & Young Jeon, *Inhibiting Patent Trolling: A New Approach for Applying Rule 11*, 12 NW. J. TECH & INTELL. PROP. 291, 301 (2014) (acknowledging that a definition of “patent troll” is hard to obtain); see also Kristen Osenga, *Formerly Manufacturing Entities: Piercing the “Patent Troll” Rhetoric*, 47 CONN. L. REV. 435, 443 (2014) (discussing the etymology of the term “patent troll”).

7. See Rogers & Jeon, *supra* note 6, at 298 (“A patent-trolling strategy’s success largely derives from the high legal costs associated with defending against a patent infringement claim, even if simply to get the claim dismissed at the summary judgment stage.”).

8. See John F. O’Rourke et al., *Silver, Garlic, and Attorney’s Fees*, 56-OCT ORANGE COUNTY LAW. 28 at 30 (Oct. 2014) (discussing the Supreme Court’s shift in favor of awarding attorney fees when litigation is “exceptional” or “unreasonable”).

9. 35 U.S.C. § 284 (2011).

10. *St. Indus., Inc. v. Mor-Flo Indus., Inc.*, 883 F.2d 1573, 1576–77 (Fed. Cir. 1989) (indicating that selecting the method for computing damages can be chosen at the discretion of the court).

method is best takes on added complexity when the entity asserting a patent is a PAE. For example, should a reasonable royalty be calculated using a compensatory perspective or should restitution theory be employed? Compensatory damages are sufficient to indemnify the patent owner for the loss suffered.<sup>11</sup> In contrast, restitution damages are “awarded to a plaintiff when the defendant has been unjustly enriched at the plaintiff’s expense.”<sup>12</sup>

Unlike compensatory damages, there is disagreement as to whether restitution theory has any use in the calculation of a reasonable royalty. For example, Brean asserts that PAEs improperly rely on restitutorial facts and, as a result, are overcompensated for infringement.<sup>13</sup> Brean argues that damages should be compensatory in nature and based on the harm suffered by the patent owner.<sup>14</sup> This idea appeals to those who dislike patent trolls, because in most cases patent trolls have suffered no harm and therefore will only recover nominal damages.<sup>15</sup>

Other commentators have rejected the pure compensatory approach for restitution theory.<sup>16</sup> In response to Brean’s concern that a restitution theory of recovery will lead to over compensation for PAEs, Amanda Frye suggests courts make recovery available only in certain circumstances.<sup>17</sup> For example, Frye limits recovery under a restitution theory if litigation is abusive and in cases where the patent has been asserted against innocent infringers.<sup>18</sup>

The forthcoming paper “A Restitution Perspective on Reasonable Royalties” may help in solving the debate over how to determine a reasonable royalty. The authors, Golden & Sandrik, endorse restitution theory and suggest ways (referred to in their paper as “cross-pollination possibilities”) that restitution principles can alleviate concerns about how patent damages are calculated for PAEs. The paper begins with a thorough examination of restitution and unjust enrichment. Golden & Sandrik then explain how restitution and patent law share some similarities in that they both (1) seek to encourage parties to enter into licensing agreements and (2)

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11. *Compensatory Damages*, BLACK’S LAW DICTIONARY (10th ed. 2014).

12. *Restitution Damages*, BLACK’S LAW DICTIONARY (10th ed. 2014).

13. Brean, *supra* note 2, at 868.

14. *Id.* at 870.

15. *Id.* at 882.

16. See Roberts, *supra* note 3, at 672 (supporting “an important unjust enrichment remedy: disgorgement”); see also Frye, *supra* note 3, at 670 (noting that the adoption of a pure compensatory approach “is not necessarily sound”).

17. See Frye, *supra* note 3, at 691–93 (“A restitution approach should take these uses into account and not allow enhanced damages when they are present.”).

18. *Id.*

seek to deter egregious behavior. Additionally, “A Restitution Perspective on Reasonable Royalties” argues that restitution theory can be used to arrive at a reasonable royalty that aligns with the underlying purpose of the patent system. The remainder of this essay discusses Golden & Sandrik’s efforts in greater detail and the contribution they make to the patent damages debate.

“A Restitution Perspective on Reasonable Royalties” argues that the law of restitution can provide useful guidance for how we should think about the assessment of reasonable royalty damages.<sup>19</sup> As noted above, this exercise is important given the current patent litigation landscape and that reasonable royalties may be the only realistic remedy available to patentees. According to Golden & Sandrik, the advantage that the lens of restitution provides is that it is a flexible approach that seems suited to discourage bad-faith infringement and reward innovators.<sup>20</sup>

Given this goal, the paper sets forth some interesting historical context. Historically, damages for patent infringement were measured by a pre-established royalty rate, lost profits, nominal damages, or disgorgement of the infringer’s profits.<sup>21</sup> However, the Supreme Court found that in the 1940s Congress eliminated the disgorgement remedy when it eliminated the recovery of profits and allowed a remedy only for the recovery of damages in patent infringement suits.<sup>22</sup> Despite the elimination of this remedy, courts still struggle with several issues that made the disgorgement remedy challenging to implement.<sup>23</sup> These issues include dealing with uncertainty, complexity, and expert testimony.<sup>24</sup>

Determining a reasonable royalty requires the court to consider a number of factors. In *Georgia-Pacific v. Plywood Corporation*, the court set out fifteen factors that could be considered, since referred to as the *Georgia-Pacific* factors.<sup>25</sup> Despite these enumerated factors, the consistency and fairness of outcomes can be impacted by a court’s ability to use a number of

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19. Golden & Sandrik, *supra* note 4, at 1.

20. *Id.* at 2.

21. 7 Donald S. Chisum, CHISUM ON PATENTS § 20.02[2] (2016).

22. *Aro Mfg. Co. v. Convertible Top Replacement Co.*, 377 U.S. 476, 505 (1964).

23. *See generally* Golden & Sandrik, *supra* note 4.

24. *Id.* at 11.

25. *Georgia-Pac. Corp. v. U.S. Plywood Corp.*, 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970), *modified sub nom.* *Georgia-Pac. Corp. v. U.S. Plywood-Champion Papers, Inc.*, 446 F.2d 295 (2d Cir. 1971).

methods, at its discretion.<sup>26</sup> In addition to these methods, a court can also vary its damage calculations based on the infringing activity.<sup>27</sup>

Golden & Sandrik suggest two specific areas where restitution might be helpful in thinking about reasonable royalty calculations: alternative measures for monetary relief and fault and responsibility.<sup>28</sup> Under measures for monetary relief, the paper asserts that the cost of the process of invention and the social value of the invention could be used to arrive at a reasonable royalty.<sup>29</sup>

Golden & Sandrik argue that in addition to the existing *Georgia-Pacific* factors, cost measures should also be considered.<sup>30</sup> A cost-based measure would reward a patentee for the relevant cost of the invention.<sup>31</sup> One implication of using cost-based measures might be that it restricts remedies available to certain patentees. For example, would this framework prevent PAEs from obtaining large damage awards? The cost-based measures framework also seems likely to favor companies with large R&D budgets, which may be why Golden & Sandrik highlight the social and technical value of the asserted patent as an important factor.<sup>32</sup>

Specifically, the authors claim that these considerations are in harmony with the underlying purpose of the patent system and mirror the way in which restitution uses liability concerns to resolve difficult cases.<sup>33</sup> But an open question remains as to how a court would determine social value or technical significance of a patent during its term.

A final advantage of embracing restitution theory is that courts can consider the blameworthiness of a defendant in fashioning a measure of recovery.<sup>34</sup> Golden & Sandrik identify two liability concerns of interest: fault and responsibility.<sup>35</sup> They argue that these concerns can be used beyond determinations for attorney fees in exceptional cases and can also be applied to the reasonable royalty calculus.<sup>36</sup>

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26. *State Indus., Inc. v. Mor-Flo Indus., Inc.* 883 F.2d 1573, 1576 (Fed. Cir. 1989).

27. *See Bio-Rad Labs., Inc. v. Nicolet Instrument Corp.*, 739 F.2d 604, 616 (Fed. Cir. 1984) (“To obtain lost profits, a patent owner must prove that he would have made the sales but for the infringing activity.”).

28. Golden & Sandrik, *supra* note 4, at 25–26.

29. Golden & Sandrik, *supra* note 4, at 31–32.

30. *Id.* at 31.

31. *Id.* at 34.

32. *Id.* at 32.

33. *Id.* at 35–36.

34. *Id.* at 17.

35. *Id.* at 28.

36. *Id.* at 36.

The paper also suggests five categories of blameworthiness: (1) independent inventor, (2) infringer without notice, (3) infringer with no mitigating characteristics, (4) infringers without notice of some risk, and (5) conscious infringers.<sup>37</sup> There is evidence that courts have applied a version of this fault or responsibility framework. For example, in *Stickle*, the Federal Circuit supported the idea that in setting the reasonable royalty, a court could consider the fact that the party using the invention is an infringer, not a willing licensee.<sup>38</sup> Further, *Sun Studs* seems to suggest that courts can consider who the infringer is and the commercial consequences of their infringement.<sup>39</sup>

In sum, “A Restitution Perspective on Reasonable Royalties” is an insightful work that acknowledges that patent law does not exist in a vacuum. Golden & Sandrik contribute to the patent damages debate by explaining how a considered examination of restitution theory can help alleviate some of the concerns regarding patent damages and patent assertion entities. Moreover, the paper attempts to demonstrate how restitution theory aligns with encouraging invention and innovation.

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37. *Id.* at 37.

38. *Stickle v. Heublein, Inc.*, 716 F.2d 1550, 1563 (Fed. Cir. 1983).

39. *See Sun Studs, Inc. v. ATA Equip. Leasing Inc.*, 872 F.2d 978, 994 (Fed. Cir. 1989), *overruled on other grounds by A.C. Aukerman Co. v. R.L. Chaides Const. Co.*, 960 F.2d 1020 (Fed. Cir. 1992) (“We have recognized that compensation for infringement can take cognizance of the actual commercial consequences of the infringement, and that the hypothetical negotiators need not act as if there had been no infringement, no litigation, and no erosion of market position or patent value.”).