

CLIENT ALERT

Unified Patent Court: Non-Practicing and Patent Assertion Entities

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Crowell & Moring's series of alerts provides practical information and professional comment on all the ramifications regarding the introduction of the Unified Patent Court (UPC). For further information, please [see our UPC leaflet PDF](#) or contact the lawyers listed near the bottom of each alert. To view other alerts in this series, [please click here](#).

Undoubtedly some forms of 'patent trolling' currently exist in Europe. Although it is unclear what the exact extent and impact of these practices is, it is clear that they are far less significant than in the United States. This is largely due to the characteristics of the existing European patent litigation system (a hotchpotch of applicable legal regimes, small(er) markets, no pan-European measures, etc.). UPC litigation will in many ways change the current system to resemble more U.S.-style patent litigation. The question therefore arises: will the introduction of the UPC see an increase in U.S.-style patent trolling in Europe? In this issue of our UPC Q&A series we explain why a cautious "no" is probably the answer to this question.

1. What are NPEs, PAEs, and Patent Trolls?

Non-practicing entities (NPEs), patent assertion entities (PAEs), and patent trolls commonly refer to entities seeking to assert patents even though they do not intend to commercially apply the technology covered by the patent. Although it is quite common for some NPEs, such as universities, startups, and research labs, not to commercially apply their patents, this does not mean that by asserting these patents they are exploiting the patent system unfairly. On the other hand, PAEs not only fail to apply the patents that they hold, they also typically are not involved in the active development of inventions. PAEs are focused on enforcement (aggressive litigation). They acquire and subsequently use patents to collect (often high) license fees from alleged infringers who are, for whatever reason (*e.g.*, lack of time or resources) unable or unwilling to defend themselves in court. A "patent troll" is a derogatory term used to describe PAEs.

2. Do the Rules of Procedure prevent PAEs from asserting their patents before the UPC?

The Rules of Procedure do not explicitly prohibit PAEs from enforcing their patents before the UPC. Several fundamental rights (including the right to property) would be infringed if as a matter of principle PAEs were prohibited from submitting their claims to the UPC. Moreover, there is often a thin line between abusive and rightful enforcement of patents that often needs to be considered on a case by case basis. That is why the UPC Agreement and the Rules of Procedure grant the judges of the UPC a fairly broad discretion when it comes to deciding certain aspects of patent disputes. Article 42 of the UPC Agreement for instance obliges the Court ("shall") to consider remedies on a fair and equitable basis. Although such unpredictability is often considered to favor PAEs, it is clear from comments made on the UPC Agreement and the Rules of Procedure that the aim is to allow the UPC judges to act accordingly when they suspect abusive assertion of patents.

3. Will the creation of a pan-European injunction not favor PAEs?

Prior to answering this question it should be clear that the Court will not grant automatic preliminary injunctions. As explained in our [second UPC alert on preliminary injunctions](#), the burden of proof on the applicant for a preliminary injunction is quite significant, in particular if the measure is requested *ex parte*. The same goes for a permanent injunction.

In addition, besides Article 42 of the UPC Agreement discussed above, there are several other provisions in the UPC Agreement and the Rules of Proceedings that distinguish UPC injunctions from those in the U.S. Articles 62(1) and 63 (1) of the UPC Agreement respectively provide that the Court "may" grant both preliminary and permanent injunctions. Article 62(2) of the UPC Agreement expressly states that "*The Court shall have the discretion to weigh up the interests of the parties and in particular to take into account the potential harm for either of the parties resulting from the granting or the refusal of the injunction*". If the defendant can demonstrate that the applicant is clearly a PAE, the UPC will most likely take this into account when deciding whether or not to grant an injunction or other measure.

4. If the UPC is to provide for more efficient patent enforcement in Europe, will the Court not be pro-patentee and therefore pro-PAE?

It is impossible to predict what the position of the different divisions will be with respect to (*prima facie*) validity and/or infringement of the invoked patents. However, there is no reason to assume that the divisions will all be pro-patentee as a matter of principle. It is also important to note that only a panel of professional judges will decide the cases. There will be no jury trials. Moreover, it cannot be excluded that, in particular in the local divisions, the existing national patent court traditions will trickle through.

5. What is the "injunction gap" and is it true that this is a great tool for PAEs?

As explained in our [third UPC alert on counterclaims for revocation](#), it will be possible to bifurcate, *i.e.*, initiate separate proceedings between the same parties for infringement (in a local or regional division) and for invalidity (in the central division) of the same patent. This German-style bifurcation can create an 'injunction gap', when an injunction is granted after quick infringement proceedings and remains in place until there is a ruling on the validity (or invalidity) of the same patent. The prospect of being kept or removed from the European market, for as long as there is no ruling on validity can be a persuasive argument in the hands of PAEs wishing to force a settlement.

However, there is no automatic bifurcation and the conditions to bifurcate are rather strict and leave quite some discretion with the local divisions. It therefore seems that bifurcation will not happen as a matter of course in local and regional divisions of the UPC. As a consequence, we assume that the possibility to bifurcate will not as such be persuasive enough for PAEs to start using the UPC system.

6. Why would the cost allocation system and the awarded damages make UPC litigation less attractive to PAEs?

In the United States, PAEs are typically at low risk of having to pay the legal costs of a prevailing adverse party. Moreover, there are plenty of law firms willing to represent PAEs on a contingency fee-basis, leaving the PAE with little more than some administrative costs to pay in advance. The foregoing explains in part why PAEs are so active in the U.S. With a limited investment and risk, they can generate great profit. This is why under the UPC no contingency fee-deals will be possible. It is also one of the reasons why the prevailing party in UPC proceedings can recover a significant amount of its lawyer fees from the adverse party. Article 69 of the UPC Agreement indeed states that "*as a general rule*" reasonable and proportionate legal costs

and other expenses incurred by the prevailing party shall be borne by the unsuccessful party. A lump sum compensation is being proposed, capped at an amount of 3 million EUR if the value of the action is more than 50 million EUR.

It is expected that the UPC will award higher damages than those currently awarded in many European jurisdictions. The UPC Agreement however clearly states that the main objective of the awarded damages should be to place the injured party in the position it would have been in if no infringement had taken place (Article 68 UPC Agreement). And, if this were not clear enough, Article 68, *ult.* UPC Agreement explicitly states that "*damages shall not be punitive*". Therefore, also from a damages perspective, UPC litigation is less attractive to PAEs than patent litigation in the U.S.

The combination of potentially having to invest significant amounts of money in UPC litigation, and of receiving damages that will only cover actual, and therefore proven, damages, should not fail to affect the behavior of PAEs.

7. Is UPC litigation then PAE-proof?

The answer here is clearly "no." PAEs will always be successful if they can convince a targeted party that it is in their interest to pay a license fee to ensure certainty in the short term, rather than fighting a long and costly battle in court with an uncertain outcome. It does not require a detailed understanding of UPC litigation to conclude that there is still a great deal of uncertainty about virtually every single aspect of UPC litigation. And this uncertainty is likely to remain until the UPC has been up and running for quite a while. With the first case still to be tried before the UPC, it is indeed still unclear how the different divisions will interpret the UPC Agreement and the Rules of Procedure, exactly how long and costly the proceedings will be, how hard it will be to obtain/prevent a preliminary injunction, to which extent and how the judges will use their discretionary power when granting other measures, etc.

In addition to this, it cannot be denied that under the UPC system the potentially affected market is enormous. Losing UPC litigation, and therefore access to potentially about half a billion European consumers, could be a very persuasive argument in favor of settling with a PAE. This will particularly be the case for small and medium-sized technology-driven companies with only a single or at best a limited number of products and/or services in their portfolio. Many of these companies already have issues financing their research and development and/or offering the resultant product or service on the market. If these companies are threatened with having to invest significant means in UPC litigation simply to remain on the market in the EU, it is very probable that several of them will agree to pay a license fee to PAEs, in particular if these fees are reasonable.

8. How can one best prepare for litigation against PAEs before the UPC?

Many factors can play a role when developing a defensive UPC strategy against PAEs. Therefore, a 'magic formula' to anticipate UPC litigation against PAEs does not exist. The best general defense is to be prepared. In most cases that do not settle, PAEs will try to obtain an *ex parte* preliminary injunction to maximize the pressure on the alleged infringer. By sending a protective letter to the Court ([see our second UPC Q&A](#)), the alleged infringer can explain to the Court why the patent is invalid, not infringed or more generally why an injunction is not an appropriate measure. If the PAE has already sent a notice letter to the alleged infringer and/or has a reputation for 'trolling' (in Europe, the U.S. or elsewhere), it is definitely worth informing the Court thereof.

In particular, in scenarios where litigation proves to be unavoidable, it will often be in the interest of the alleged infringer to initiate UPC proceedings and not to wait until the PAE sues. Indeed, the first mover often has significant strategic advantages.

The first mover can decide to file a request for a declaration of non-infringement or opt for classic revocation proceedings. Both will be handled, most often in English, by the central division of the Court. When such proceedings are already pending before the central division, the risk of finding oneself actively involved in infringement proceedings before a local division is reduced significantly. This can be of major importance, in particular if a local division is less experienced and/or would be handling the proceedings in another language than English ([see our fifth UPC Q&A](#)). The first mover also has 'unlimited' time to prepare arguments, experts, etc., whereas the defendant will only have three months to come up with a defense.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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