

**IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS**

In re Innovatio IP Ventures, LLC, Patent
Litigation

This Document Relates To:

All Cases

Case No. 1:11-cv-09308

Judge James F. Holderman
Magistrate Judge Sidney Schenkier

**DEFENDANTS BENCH MEMORANDUM IN RESPONSE TO THE COURT'S
SEPTEMBER 6, 2103 ORDER IDENTIFYING A KEY ISSUE IN DISPUTE AND
REQUESTING INPUT FROM PARTIES**

In its September 6, 2013, Order Identifying A Key Issue In Dispute And Requesting Input From Parties, the Court asked whether the parties believed that the smallest salable patent-practicing unit (“SSU”) standard is “inappropriate to apply to claims covering systems and methods,” and, if so, to “be prepared to articulate an alternative standard that the court can apply in these circumstances.” (Dkt. 901 at 2.) Defendants/Declaratory Judgment Plaintiffs respectfully submit that it *is* appropriate to apply the SSU standard to the system and method claims asserted by Innovatio in this case, and that this is required by the controlling case law.

1. The SSU Standard Is Applicable To System And Method Claims

The right to compensation for patent infringement has limits, and those limits are set by the value of the patented invention. Thus, the law requires that “[a]t all times, the damages inquiry *must* concentrate on compensation for the economic harm caused by infringement of *the claimed invention.*” *ResQNet.com, Inc. v. Lansa, Inc.*, 594 F.3d 860, 869 (Fed. Cir. 2010) (emphasis added). This raises particular concerns when the accused product or method contains or uses many features or steps beyond that claimed in the patent because there is a “considerable risk that the patentee will be improperly compensated for non-infringing components of that product.” *LaserDynamics, Inc. v. Quanta Computer, Inc.*, 694 F.3d 51, 67 (Fed. Cir. 2012). Yet, for over 100 years the Supreme Court has required that where “a patent is for an improvement, and not for an entirely new machine or contrivance . . . the patentee . . . must in every case give evidence tending to separate or apportion the defendant’s profits and the patentee’s damages between the patented feature and the unpatented features, and such evidence must be reliable and tangible, and not conjectural or speculative.” *Garretson v. Clark*, 111 U.S. 120, 121 (1884).

The Federal Circuit’s recent SSU jurisprudence seeks to address these concerns by requiring that the royalty base used for patent damages be the “smallest salable infringing unit *with close relation to the claimed invention.*” *LaserDynamics (quoting Cornell Univ. v. Hewlett-*

Packard Co., 609 F.Supp.2d 279, 288 (N.D.N.Y. 2009) (Rader, J)) (emphasis added); *see also Dynetix Design Sols., Inc. v. Synopsis, Inc.*, 2013 WL 4538210, at *3 (N.D. Cal. Aug. 22, 2013) (Grewal, MJ) (noting that the *LaserDynamics* “language affirms that the smallest salable unit must be closely tied to the patent to suffice.”). Using the SSU as a starting point for a damages analysis is designed to ensure that patent damages be based on value that the *patented invention* actually contributes to the overall accused product or process.

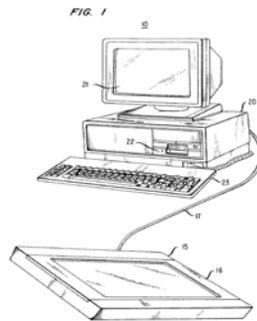
Determination of the SSU with the closest relation to the invention, however, is not a rote exercise that simply looks at the words in a claim. Rather, the focus is on determining the SSU that most closely relates to the *inventive* feature(s) in order to prevent patentees from enlarging their damages base by simply incorporating known elements into a claim. The fact that patent claims may be expressed in different formats, and of different scope, should not allow the patent owner to point to the revenue associated with an overall accused product or process as the proper revenue base. As the Federal Trade Commission explained in its March 2011 Report:

Another artificial construct for identifying the base that courts should reject is always to equate it with the device recited in the infringed claim. In many cases, there will be an easy correspondence between the inventive feature, the device recited in the infringed claim, and the appropriate base. In other cases, the correspondence will not be so clear. For example, a software invention for rendering video images can be recited in a claim covering video software, or in a claim covering a standard personal computer running the video software. . . . ***The real focus ought to be on the economic realities and not the vagaries of claim drafting, particularly because the way claims are drafted [is] . . . so manipulable.***

(Ex. A, The Evolving IP Marketplace: Aligning Patent Notice and Remedies with Competition, Federal Trade Commission, March 2011, at 211 (emphasis added, internal quotations omitted).)

Use of the SSU as a basis for an apportionment analysis also can be done in the context of method or systems claims. This is exactly what occurred in the Federal Circuit’s seminal decision in *Lucent Techs. Inc. v. Gateway, Inc.*, 580 F. 3d 1301 (Fed. Cir. 2009). There, among

the claims that were asserted against the infringing “date picker” function was a *method* of using a *computer with a display* which, by its literal terms, covered a broad multi-functional end-user product such as a desktop computer.¹ The patent at issue in that case was titled “Touch Screen Form Entry System” and method claims 19 and 21 (the two the jury found were infringed) literally required the step of “displaying on [a] display,” which the patent clearly shows was a piece of computer hardware like a “touch sensitive screen” such as shown annotated in Figure 1 at elements 15 and 16:



(Ex. B, U.S. Patent No. 4,763,356 at Fig. 1, Col. 2: 19-20 and 34-36.) Notwithstanding the literal recitation of these elements, both the district court and the Federal Circuit identified Microsoft’s Outlook software program—namely, software operating on the computer with a

¹ The jury determined that Claim 19 and 21 of U.S. Patent No. 4,763,356 patent were infringed by the “date picker” functionality within Microsoft’s Outlook software program, which was itself typically sold as part of Microsoft Office software. Independent claim 19 of the asserted patent in *Lucent* claimed as follows:

19. A method for use in a computer having a display comprising the steps of

displaying on said display a plurality of information fields,

identifying for each field a kind of information to be inserted therein,

indicating a particular one of said information fields into which information is to be inserted and for concurrently displaying a predefined tool associated with said one of said fields, said predefined tool being operable to supply information of the kind identified for said one field, said tool being selected from a group of predefined tools including a tool adapted to supply an individual entry from a menu of alternatives and at least a tool adapted to allow said user to compose said information, and

inserting in said one field information that is derived as a result of said user operating said displayed tool.

display—as the SSU for the allegedly infringing “date picker” function. Thus, while the Federal Circuit ultimately overturned the jury’s verdict for failure to satisfy the Entire Market Value Rule, its analysis of Outlook as the SSU confirms that where system and method claims are involved the SSU standard still must be applied and the royalty base should be, at most, the component which most closely relates to the inventive feature(s) of the claim, which in this case is indisputably the Wi-Fi chips which are sold in the market and that include the 802.11-essential functionality. Of course, determining the appropriate SSU does not necessarily end the analysis since the purpose of the analysis is to determine, as closely as possible, the value of the patented invention. *See, e.g., AVM Techs., LLC v. Intel Corp.*, 2013 WL 126233, *3 (D. Del. Jan. 4, 2013) (noting that “[t]he use of a saleable unit that is greater than the patented feature is going to introduce *Uniloc* error when the patented feature is a ‘date picker’ whether the saleable unit is a computer loaded with ‘Outlook’ or simply ‘Outlook.’”)

There are other reasons why use of the SSU can be appropriate even where the SSU does not practice or contain every element of the claim. For example, requiring that the SSU practice every element of a claim would be inconsistent with prevailing patent exhaustion law. “The longstanding doctrine of patent exhaustion provides that the initial authorized sale of a patented item terminates all patent rights to that item.” *Quanta Comp., Inc. v. LG Elecs., Inc.*, 553 U.S. 617, 625 (2008). A component may qualify as a “patented item” that results in exhaustion even if it does not practice every element of the claims, so long as it “embodies essential features of [the] patented invention.”² *Id.* at 630-35. There is no justification for adding requirements to the definition of the SSU for the purpose of determining the appropriate royalty base in patent

² US patent law also recognizes that infringement may exist by the supply of components that do not literally satisfy each claim element pursuant to, for example, contributory infringement under 35 U.S.C. § 271(c).

damages, when the Supreme Court has rejected such limitations in defining a “patented item” for purposes of exhaustion law.

An application of the SSU that rigidly required every claim element be literally present in the SSU, instead of identifying the SSU with close relation to the invention (as initially framed by Chief Judge Rader), would also lead to the anomalous result that a broader claim with less recited structure would have more limited damages than a narrower claim that recited more structure. For example, a broad claim directed to inventive functionality that resided solely on a chip would be valued using the chip as a base whereas a *narrower* dependent claim that added a claim limitation requiring use of that functionality in a supercomputer would use the far more expensive supercomputer as the base. Similarly, a clever drafter could claim the inventive Wi-Fi-related functionality residing on the chip in the context of a method of using additional non-inventive equipment in order to enlarge the relevant base.³ Yet, as this Court has recognized in this case, it is inappropriate to permit a patentee to enlarge their damages due to the inclusion of non-inventive elements into a claim because “[w]hen that additional element is merely basic technology that adds nothing novel to the claim, *that added value is likely to be zero.*” (Dkt. 851 at 36 (emphasis added)). The Court should accordingly apply the SSU methodology to all of the claims here and find that the starting point for the analysis of damages here is the component that most closely relates to the inventive feature(s) of the claims, namely the Wi-Fi chip incorporating the accused infringing 802.11-essential functionality.

³ Notably, a claim to an abstract idea does not become patent eligible under 35 U.S.C. § 101 merely because use of a “computer” is recited in the claims. *See, e.g., Bancorp Servs., L.L.C. v. Sun Life Assurance Co. of Canada*, 687 F.3d 1266, 1276 (Fed. Cir. 2012) (“As we have explained, ‘[s]imply adding a ‘computer aided’ limitation to a claim covering an abstract concept, without more, is insufficient to render the claim patent eligible.’”) (*quoting Dealertrack, Inc. v. Huber*, 674 F.3d 1315, 1333 (Fed. Cir. 2012).) Likewise, a patentee should not be able to enlarge the scope of the SSU simply by including non-inventive technology in a claim.

2. Regardless Of The Royalty Base Used, Technical Apportionment Establishes The Wi-Fi Chip As The Relevant Component With The Inventive Features

In addition, regardless of whether the Wi-Fi chip or some other unit is identified as the SSU, an apportionment analysis must still be applied in order to determine the appropriate base for valuing of the patented technology. For example, in *LaserDynamics*, the Federal Circuit rejected the use of laptops as the royalty base because that would render too difficult the task of apportioning the royalty base. *LaserDynamics*, 694 F.3d at 70 (noting that if laptops were the royalty base, “when it comes time to then apportion a royalty rate that accounts for the ODD contribution only, the exceedingly difficult and error-prone task of discerning the ODD’s value relative to all other components in the laptop remains”); *see also AVM Techs.*, 2013 WL 126233 at *3 (holding that microprocessors, despite being the smallest salable unit, must still be apportioned to arrive at the value of the accused dynamic logic circuits); *Dynetix*, 2013 WL 4538210 at *3 (“Thus, *LaserDynamics* supports the premise that an apportionment is required even where there the accused product is the smallest salable unit or where whatever the smallest salable unit is it is still a multi-component product encompassing non-patent related features.”) This is because, as the Federal Circuit has recognized, “the patentee . . . must in every case give evidence tending to separate or apportion the defendant’s profits and the patentee’s damages between the patented feature and the unpatented features, and such evidence must be reliable and tangible, and not conjectural or speculative.” *Uniloc USA, Inc. v. Microsoft Corp.*, 632 F.3d 1292, 1318 (Fed. Cir. 2012) (quoting *Garretson v. Clark*, 111 U.S. 120, 121 (1884).)

Significantly, where the SSU includes non-novel elements or components unrelated to the inventive feature(s) of the patented technology, the apportionment analysis—which remains necessary—becomes more prone to error. Indeed, as one court recently observed:

The use of a saleable unit that is greater than the patented feature is going to introduce *Uniloc* error when the patented feature is a “date picker” whether the

saleable unit is a computer loaded with “Outlook” or simply “Outlook.” The *Uniloc* error will be greater with the computer loaded with “Outlook” than with “Outlook” alone, but the difference in error is one of degree, not of kind. Further, as *Laser Dynamics* holds, the difficulty in determining a royalty base in a situation such as this one with dynamic logic circuits is not a reason to accept an unreliable method.

AVM Techs., 2013 WL 126233 at *3. Here, there is no dispute that the allegedly inventive feature(s) of the asserted claims are all embodied in the Wi-Fi chip. Thus, regardless of the SSU utilized, determination of a RAND royalty will necessarily involve consideration of the contribution of the patented technology to the functionality of the Wi-Fi chip. Accordingly, by limiting the SSU to the component which most closely relates to the allegedly inventive feature(s) of the claim (*i.e.*, the Wi-Fi chip), rather than a multi-component end user product, the Court will more readily allow for apportionment and a correct determination of the incremental value of the patented technology required by the RAND analysis.

3. Utilization Of An *Ex Ante* Alternatives Analysis Will Result In A Correct Determination Of A RAND Royalty

Finally, in the event the Court determines that either the SSU standard or apportionment are inappropriate, Defendants respectfully submit that the Court should apply the *ex ante* alternatives test. As Defendants explained in their RAND Trial Brief, and will demonstrate at trial, this test looks to determine the incremental value of the patented technology, exclusive of any lock-in value resulting from standardization, by (1) determining whether viable non-infringing alternatives existed at the time of standardization; and (2) assessing the relative costs and benefits of those alternatives compared to the patented technology at issue. (Dkt. 893 at 16-17.) This test, which has been endorsed by the courts⁴ and the FTC,⁵ thus seeks to identify

⁴ See, e.g., *Microsoft Corp. v. Motorola, Inc.*, 2013 WL 2111217, at *13 (W.D. Wash. Apr. 25, 2013) (Robart, J) (“*ex ante* examination of the incremental contribution of the patented technology to the standard can be helpful in determining a RAND rate in the context of a dispute over a RAND royalty rate”)

the incremental value of the patented technology independent of the royalty base. Importantly, as set forth in Defendants' Trial Brief, and as will be demonstrated at trial, the validity of the *ex ante* alternatives is confirmed by application of proportionality and the modified Georgia-Pacific test which both reach similar results. (*Id.* at 21-23.) The methodology, moreover, is well-known and familiar to the courts in assessing patent damages and, importantly, allows for identification of any value of the patented technology independent of its inclusion in the standard. See, e.g., *Apple, Inc. v. Motorola, Inc.*, 2012 WL 2376664, at *11 (N.D. Ill. June 22, 2012) (Posner, J) (“[t]he purpose of the FRAND requirements . . . is to confine the patentee’s royalty demand to the value conferred by the patent itself as distinct from the additional value—the hold-up value—conferred by the patent’s being designated as standard-essential.”) The *ex ante* alternatives test thus represents a viable alternative that the Court should adopt in the event it considers application of the SSU and apportionment to be insufficient in the context of method and system claims.⁶

⁵ Ex. A, The Evolving IP Marketplace: Aligning Patent Notice and Remedies with Competition, Federal Trade Commission, March 2011, at 22-23 (“[c]ourts should cap the royalty at the incremental value of the patented technology over alternatives available at the time the standard was chosen”)

⁶ See, e.g., Ex. C, Brief of Amici Curiae Altera Corporation et al. Regarding Standards on Damages in Support of Neither Party, December 4, 2012 (proposing use of the *ex ante* alternatives test as a starting point for any reasonable royalty analysis, and also discussing the appropriate use of apportionment and other damages modalities).

Dated: **September 9, 2013**

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CERTIFICATE OF SERVICE

I hereby certify that on September 9, 2013 a true and correct copy of the foregoing **DEFENDANTS BENCH MEMORANDUM IN RESPONSE TO THE COURT'S SEPTEMBER 6, 2103 ORDER IDENTIFYING A KEY ISSUE IN DISPUTE AND REQUESTING INPUT FROM PARTIES** was electronically filed with the Court via the CM/ECF system which sent notification of such filing to all Counsel of Record.

Dated: **September 9, 2013**

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