

Settlement Evidence and Patent Damages

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Critical in most patent-infringement litigation is what damages—or, often, what “reasonable royalty”—an infringer must pay to the holder of a valid and enforceable and infringed patent. (According to 35 U.S.C. § 284, in a patent-infringement action, “[u]pon finding for the claimant the court shall award the claimant damages adequate to compensate for the infringement but in no event less than a reasonable royalty for the use made of the invention by the infringer”) In calculating a reasonable royalty, fact finders generally follow the “willing licensor-willing licensee” approach, which asks them to construct a hypothetical arm’s-length pre-infringement licensing negotiation. In constructing the hypothetical pre-infringement licensing negotiation, fact finders typically rely on the 15 factors described in *Georgia-Pacific Corp. v. United States Plywood Corp.*, 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970), *modified and aff’d*, 446 F.2d 295 (2d Cir. 1971). The first factor is what royalties the patentee has received for licensing the patent-in-suit; the second factor is what royalties licensees have paid to license similar (comparable) patents; the 15th factor is what royalty the parties would have agreed to at the time the infringement began if they had reasonably and voluntarily tried to reach agreement. *Id.*

In recent years, disputes have proliferated over whether settlement license agreements and settlement license negotiations are discoverable and admissible to prove reasonable royalties. These disputes have arisen in various procedural contexts, including motions to compel discovery, *Daubert* motions and motions *in limine* to exclude expert testimony, and arguments over limiting jury instructions. Although the federal courts have not spoken unanimously, the trend is to allow *discovery* of both settlement license agreements and settlement license negotiations. There is less agreement regarding whether and in what circumstances agreements and negotiations are *admissible* at trial.

The U.S. Court of Appeals for the Federal Circuit, which has appellate jurisdiction over all patent-infringement cases, 28 U.S.C. § 1295, has recently ruled on two related issues. In *In re MSTG*, 675 F.3d 1337, 1348 (Fed. Cir. 2012), the court held that there is no “settlement discovery privilege” protecting settlement license negotiations. The Federal Circuit has not clearly resolved other issues; however, its recent opinions have supplied ammunition to proponents of broader access and broader use of settlement license agreements and negotiations. For example, in *ResQNet.com, Inc. v. Lansa, Inc.*, 594 F.3d 860, 872 (Fed. Cir. 2010), while not holding that either settlement license agreements or settlement license negotiations are generally

discoverable or admissible, the court ruled that, at least in certain situations, a settlement license agreement may be used to support an expert's reasonable royalty calculation. (In *In re MSTG*, the court explicitly declined to decide what limits, if any, exist on the discovery of settlement license negotiations, or whether they are admissible. 675 F.3d at 1346–47, 1347 n.4.) In the wake of *ResQNet*, district courts have reached different, and sometimes contradictory, conclusions about when and whether agreements or negotiations are discoverable or admissible. Most recently, in *LaserDynamics, Inc. v. Quanta Comp., Inc.*, 694 F.3d 51, 77–78 (Fed. Cir. 2012), the Federal Circuit appears to have limited the circumstances in which settlement license agreements may be admitted into evidence and it made clear that *ResQNet* should not be read as generally authorizing the admissibility of settlement license agreements.

Whether settlement license agreements or negotiations are discoverable or admissible depends on the interpretation and application of various federal rules, including Federal Rule of Civil Procedure 26(b)(1) (scope of discovery) and Federal Rules of Evidence 402 (relevancy), 403 (unfair prejudice and jury confusion *inter alia*), 408 (compromise negotiations), and 702 (expert testimony). In addressing the discoverability and admissibility of settlement license agreements in patent-infringement actions, courts have considered such factors as the comparability of the patent and technology-in-suit to licensed patents and technology; the status of settlement license agreements (consummated, failed, or ongoing negotiations); the nature of the parties (competitors or non-practicing entities (NPEs), which are also sometimes referred to derogatorily as trolls); the fact finder (judge or jury); and whether a nonparty's confidential information is covered by a protective order.

Because district courts have weighed these factors differently, there are few general rules. Nonetheless, if the patent and technology-in-suit are comparable to licensed patents and technology, *settlement license agreements are most likely discoverable*, and *settlement license negotiations are likely discoverable*. See, e.g., *ResQNet*, 594 F.3d at 872 (first *Georgia-Pacific* factor “must consider licenses that are commensurate with what the defendant has appropriated. If not, a prevailing plaintiff would be free to inflate the reasonable royalty analysis with conveniently selected licenses without an economic or other link to the technology in question.”); *Lucent Techs., Inc. v. Gateway, Inc.*, 580 F.3d 1301, 1326 (Fed. Cir. 2009) (second *Georgia-Pacific* factor “examines whether the licenses relied on by the patentee in proving damages are sufficiently comparable to the hypothetical license at issue in suit”). The admissibility of agreements usually hinges on whether they cover patents and technology that are truly comparable to the patent or technology-in-suit, or can be distinguished in one or more ways. The admissibility of negotiations is more controversial, and there are strong legal and policy arguments that negotiations should not be admissible to prove patent-infringement damages.

For attorneys representing accused infringers, the current state of the law means that they should press for discovery of both settlement license agreements and settlement license negotiations. When a patent-holder has settled or negotiated for a relatively low license fee or royalty rate (common with NPEs, which usually settle for amounts or rates lower than those that result from

arm's-length negotiations between operating companies), accused infringers should attempt to introduce the amounts or rates at trial to suppress damages. For attorneys representing patent-holders contemplating settlement, they should always keep in mind the possible effects of any settlement negotiations or agreements on pending or future litigation. Attorneys representing patent-holders may view the current state of the law differently than do attorneys representing accused infringers, but there are good policy reasons to allow broad discovery, and to permit damages experts to at least consider all consummated settlement license agreements.

In all events, attorneys on both sides of settlement license negotiations or agreements should be alert for opportunities to convince courts and juries why the negotiations or agreements are or are not comparable to negotiations or agreements that are not influenced by pending or threatened litigation—and must always be aware that negotiations or agreements today might become evidence in patent-infringement trials tomorrow.

Opening the Door to Settlement License Agreements

When weighing the *Georgia-Pacific* factors, fact finders may consider, among many other factors, any royalties that a patentee has received and a licensee has paid for comparable patents. Before 2010, however, courts generally prohibited parties from introducing evidence concerning settlement license agreements at trial. In doing so, courts routinely relied on and/or quoted from the Supreme Court's nineteenth-century decision in *Rude v. Westcott*, in which the Court observed:

It is clear that a payment of any sum in settlement of a claim for an alleged infringement cannot be taken as a standard to measure the value of the improvements patented, in determining the damages sustained by the owners of the patent in other cases of infringement. Many considerations other than the value of the improvements patented may induce the payment in such cases. The avoidance of the risk and expense of litigation will always be a potential motive for a settlement.

Rude v. Westcott, 130 U.S. 152, 164 (1889). Despite later widespread reliance on the *Rude* Court's observation, in fact, the Court did not hold that settlement licenses arising out of litigation could never be considered in calculating a reasonable royalty. Indeed, the *Rude* Court rejected the concept of a reasonable royalty. *Id.* at 167. *See, e.g., Volumetrics Med. Imaging, LLC v. Toshiba Am. Med. Sys.*, No. 1:05CV955, 2011 WL 2470460, at *9 (M.D.N.C. June 20, 2011). The Supreme Court did not approve a "reasonable royalty" as a basis for patent-infringement damages until 1915. *See Dowagiac Mfg. Co. v. Minnesota Moline Plow Co.*, 235 U.S. 641, 648 (1915). Congress codified the *Dowagiac* decision in 1922, for the first time authorizing recovery of "reasonable royalties." *See, e.g., Christopher B. Seaman, Reconsidering the Georgia-Pacific Standard for Reasonable Royalty Patent Damages*, 2010 B.Y.U. L. Rev. 1661, 1671 (2010). The *Rude* Court only ruled that two or three prior licenses did not establish a "market price" for a patented technology and, therefore, the patent-holder had not adequately proved damages. *Id.* at 163-65. For a "market price" to be established as a measure of damages, the Court explained, "it must be paid or secured before the infringement complained of; it must be paid by such a number

of persons as to indicate a general acquiescence in its reasonableness by those who have occasion to use the invention; and it must be uniform at the places where the licenses are issued.” *Id.* at 165.

Prior to 2010, there was judicial consensus that settlement license agreements were not admissible. That said, district courts split over whether such agreements were discoverable, even in light of Fed. R. Evid. 408. As one magistrate judge noted in granting a motion to compel discovery of settlement license agreements relevant to a patent-related tortious interference claim, courts were “all over the map on how to apply Rule 408” in patent-litigation contexts. *Constar Intern., Inc. v. Ball Plastic Container Corp.*, No. 05-C-669-C, 2006 WL 6021150, at *1 (W.D. Wis. Mar. 27, 2006). Then, the Federal Circuit decided *ResQNet*.

In *ResQNet*, the court vacated a damages award, concluding that the award “relied on speculative and unreliable evidence divorced from proof of economic harm linked to the claimed invention,” and found that the patent-holder’s damages expert based his opinion on licenses that were not comparable to the license that would have resulted from a pre-infringement hypothetical negotiation and, therefore, those licenses would not be relevant to establish a reasonable royalty to calculate patent-infringement damages. 594 F.3d at 865, 868. The expert based his opinion on seven licenses of the patent-holder, five of which the Federal Circuit found had no relation to the claimed invention. 594 F.3d at 870-71. Two arose from prior patent-infringement litigation; only one of those two “straight” licenses was a “running license,” while the other was a “lump-sum payment” license. *Id.* The Federal Circuit suggested, but did not find, that, on remand, the district court could consider the “running license” in calculating a reasonable royalty. *Id.* at 872-73.

Conceding that the “hypothetical reasonable royalty calculation occurs before litigation and [] litigation itself can skew the results of the hypothetical negotiation,” the *ResQNet* majority (Judges Lourie and Rader—Judge Newman concurred in part and dissented in part, explicitly disagreeing with the majority’s damages holding) determined that the “most reliable license in this record arose out of litigation.” *Id.* at 872. The court remanded the case to give the district court the “opportunity to reconsider the reasonable royalty calculation,” and implied that the district court could consider that one settlement license agreement. *Id.* at 872-73. On remand, the district court focused on two licenses that it found to be relevant (and which the parties apparently agreed were relevant); one was the result of a settlement agreement, the other was not. *ResQNet.com, Inc. v. Lansa, Inc.*, 828 F. Supp. 2d 688, 694 (S.D.N.Y. 2011). After a second appeal, the parties settled before oral argument at the Federal Circuit. *See ResQNet.com, Inc. v. Lansa, Inc.*, 2012 WL 4171262 (Fed. Cir. Sept. 20, 2012).

After *ResQNet*, district courts struggled to understand the significance of the Federal Circuit panel’s *dicta* regarding whether and when settlement-related evidence may be considered in determining patent-infringement damages. For example, patent-savvy judges in the Eastern District of Texas opined both that *ResQNet* “may have changed the legal landscape regarding the admissibility of litigation-related licenses,” *Datatreasury Corp. v. Wells Fargo & Co. et al.*, No. 2:06-CV-72-DF, 2010 WL 903259 at *1 (E.D. Tex. March 4, 2010) (Judge Folsom), and that the

“Federal Circuit’s observation was not the adoption of a bright-line rule regarding the reliability of litigation licenses nor even a ruling on their admissibility. It was merely a reflection on the evidence before it,” *ReedHycalog UK, Ltd. v. Diamond Innovations Inc.*, 727 F. Supp. 2d 543, 546 (E.D. Tex. 2010) (Judge Davis).

MSTG: No Settlement Discovery Privilege

One feature of the district court split following *ResQNet* is whether *negotiations* preceding settlement license agreements are *discoverable*. Under Federal Rule of Civil Procedure 26(b)(1), parties may obtain discovery of “any nonprivileged matter that is relevant to any party’s claim or defense,” regardless of whether the discovery is admissible, provided only that the “discovery appears reasonably calculated to lead to the discovery of admissible evidence.” Even after *ResQNet*, some district courts, following the Sixth Circuit decision in *Goodyear Tire & Rubber Co. v. Chiles Power Supply, Inc.*, 332 F.3d 976, 979-83 (6th Cir. 2003), continued to recognize “a settlement privilege that applies to negotiations underlying licensing agreements arising out of litigation.” See, e.g., *Software Tree, LLC v. Red Hat, Inc.*, No. 6:09-CV-097, 2010 WL 2788202, at *4 (E.D. Tex. June 24, 2010) (Magistrate Judge Love) (concluding that *ResQNet* did not constitute “clear precedent compelling a new tack”). Resolving the district court split, in *MSTG*, 675 F.3d at 1348, the Federal Circuit explicitly held that, “in light of reason and experience . . . settlement negotiations related to reasonable royalties and damage calculations are not protected by a settlement negotiation privilege.”

MSTG arose from a motion to compel production of information regarding settlement license negotiations. During discovery, MSTG produced seven settlement license *agreements*, but objected when AT&T sought discovery of the underlying *negotiations*. *Id.* at 1339. A magistrate judge initially denied AT&T’s motion to compel. After MSTG served an expert damages report in which the expert opined (based on the deposition testimony of an MSTG executive) that the settlement license agreements reflected litigation-induced compromises and were therefore not relevant to any pre-infringement hypothetical negotiation between MSTG and AT&T, the magistrate judge granted AT&T’s renewed motion to compel, finding that the negotiation documents might show that MSTG’s expert had based his opinion on erroneous grounds. The district court agreed and also found that, because MSTG’s damages expert had relied on the executive’s deposition testimony regarding “business reasons” for entering into the settlement license agreements, it would be unfair for MSTG to “then shield those reasons from further examination.” *Id.*

Following this reasoning, the court in *Implicit Networks, Inc. v. Juniper Networks, Inc.*, No. C 10-04234 SI, slip. op. at 2–3 (N.D. Cal. June 5, 2012), initially denied Juniper’s motion to compel the production of all documents regarding licenses, including all draft licenses and communications with actual or potential licensees. However, after Implicit argued that the royalty rates in prior licenses were “‘discounted’ in light of business decisions,” the court allowed Juniper’s renewed motion to compel the emails and letters regarding Implicit’s licensing negotiations. *Id.*, slip op. at 1–2 (N.D. Cal. July 23, 2012).

The Federal Circuit began by ruling that the issue is governed by Federal Circuit law. *Id.* at 1341. The court confirmed that it applies its own law both “to issues of the scope of the attorney-client privilege and work product doctrine,” and to “determining whether a privilege or other discovery limitations protect disclosure of information related to reasonable royalties.” *MSTG*, 675 F.3d at 1341 (internal citations omitted). The Federal Circuit then rejected MSTG’s invitation to invoke Federal Rule of Evidence 501 (common law governs privilege claim) to fashion a settlement discovery privilege. *Id.* at 1342. The court pointed out that, “to the extent [that it needed] to protect the sanctity of settlement discussions and promote the compromise and settlement of dispute,” a district court has broad discretion to issue protective orders and “to regulate or prevent discovery even though the materials sought” otherwise falls within the proper scope of discovery. *Id.* at 1346-47 (quoting Fed. R. Civ. P. 26 advisory committee’s note (1970 Amendment subdivision (b))).

Importantly, the court also stated that it was reserving “for another day the issue of what limits can appropriately be placed on discovery of settlement negotiations,” *id.*, and (citing *ResQNet*) that it had not decided whether such negotiations would be admissible at trial, *id.* at 1347 n.4. Finally, the *MSTG* court ruled that the district court had not abused its discretion in ordering MSTG to produce all documents reflecting communications between MSTG and prospective licensees or potential infringers, because MSTG’s expert went “beyond the four corners” of the settlement license agreements by relying on the MSTG executive’s deposition testimony regarding MSTG’s “business reasons” for entering into the agreements. *Id.* at 1348. “As a matter of fairness,” the court explained, “MSTG cannot at one and the same time have its expert rely on information about the settlement negotiations and deny discovery as to those same negotiations.” *Id.*

LaserDynamics: Limitations on the Admissibility of Settlement License Agreements

While *ResQNet* may have opened the door to the admissibility of settlement license agreements, in August 2012, a different panel of Federal Circuit judges (Judge Reyna, joined by Judges Dyk and Clevenger) ruled that *ResQNet* does not stand for the general proposition that settlement license agreements are admissible. In *LaserDynamics*, the owner of a patent directed to a method of optical disk discrimination (*i.e.*, enabling a disk drive to recognize whether the user has inserted a CD or DVD) sued Quanta Computer, Inc., and (after a second damages trial) obtained a jury verdict of \$8.5 million. *LaserDynamics*, 694 F.3d at 64–65. During the second damages trial, 29 licenses were admitted into evidence, of which 28 provided for lump sum license payments of \$1 million or less. *Id.* at *58. The sole exception was a \$6 million lump sum settlement license agreement payment that LaserDynamics received from BenQ Corporation to settle rancorous two-year long patent-infringement litigation. *Id.* As the Federal Circuit noted, the agreement was executed less than two weeks before the scheduled start of trial. *Id.* Moreover, as the Federal Circuit explained,

by the time of the settlement, BenQ had been repeatedly sanctioned . . . for discovery misconduct and misrepresentation. The district court had allotted BenQ one-third less time than [plaintiff] for *voir dire*, opening statement, and closing argument, had awarded attorneys’ fees to [plaintiff] for

bringing the sanctions motion, had stricken one of BenQ's pleaded defenses, and had sanctioned BenQ \$500,000 as an additional punitive and deterrent measure.

Id. Before the second damages trial, Quanta unsuccessfully moved *in limine* to exclude the BenQ settlement license agreement. *Id.* at 64. After the verdict, Quanta appealed, raising numerous arguments, including that the BenQ settlement license agreement should not have been admitted into evidence and relied upon by LaserDynamics's damages expert. *Id.* at 65–66.

The Federal Circuit held that the district court abused its discretion in denying Quanta's motion *in limine* and in admitting the BenQ settlement license agreement. *Id.* at 66, 77. The court stated that “[t]he propriety of using prior settlement agreements to prove the amount of a reasonable royalty is questionable.” *Id.* at 77 (citing and quoting *Rude*, 130 U.S. at 164). This panel of the Federal Circuit acknowledged that *ResQNet* permitted “reliance” on settlement license agreements to “establish reasonable royalty damages . . . under certain limited circumstances.” *Id.* However, the panel pointed out that, unlike the subject settlement license agreement in *ResQNet*, the “BenQ settlement agreement appears to be the least reliable license by a wide margin.” *Id.* at 77–78. The court emphasized that the agreement was made shortly before “a trial in which BenQ would have been at a severe legal and procedural disadvantage,” *id.* at 78, and that its \$6 million license fee, which was six times higher than the next highest royalty paid for the patent-in-suit, “ostensibly reflects not the value of the claimed invention but the strong desire to avoid further litigation under the circumstances.” *Id.*

The court also noted that, given the rapidly changing technology and financial environment, the 2006 BenQ settlement license agreement was “in many ways not relevant” to a hypothetical negotiation which would have taken place in 2003, on the date of Quanta's initial infringement of LaserDynamics's patent. *Id.* Finding that the other 28 licenses were “far more reliable indicators of what willing parties would agree to in a hypothetical negotiation,” *id.*, the court opined that “[t]his record stands in stark contrast to that in *ResQNet*, where a lone settlement agreement stood apart from all other licenses in the record as being uniquely relevant and reliable.” *Id.*

The *LaserDynamics* court concluded that the “probative value of the BenQ settlement agreement is dubious . . . and its probative value is greatly outweighed by the risk of unfair prejudice, confusion of the issues, and misleading the jury,” and ordered the agreement excluded, based on Fed. R. Evid. 403, from the trial on remand. *Id.*

While the eventual impact of *LaserDynamics* remains to be seen, the *ResQNet* decision may be limited to its peculiar facts. *ResQNet* does not broadly sanction admitting settlement license agreements into evidence at trial, although it permits trial courts to consider settlement license agreements, according to the *LaserDynamics* panel, “under certain limited circumstances.” Courts may also limit *LaserDynamics* to its unique facts, and exclude settlement license agreements from evidence only when there are indicia that the agreements were strongly influenced by litigation.

Discovery of Settlement License Agreements after *ResQNet* and *MSTG*

Post *ResQNet* and *MSTG*, district courts generally agree that information about *settlement license agreements* involving comparable patents and technology is *discoverable*. As Magistrate Judge Cott of the Southern District of New York stated, “although it did not address either the discoverability or the admissibility of the litigation licenses . . . *ResQNet* nevertheless appeared to endorse an approach in which the district court—and thus the patentee who bears the burden of establishing damages—considers all information concerning royalty rates for the patent-in-suit to establish a factual basis for a reasonable royalty.” *Small v. Nobel Biocare USA, LLC*, 808 F. Supp. 2d 584, 590 (S.D.N.Y. 2011). Numerous district courts now permit discovery of settlement license agreements. *See, e.g., Volumetrics Med. Imaging, LLC*, No. 1:05CV55, 2011 WL 2470460, at *13–15 (M.D.N.C. June 20, 2011) (collecting cases). This result is consistent with the Federal Circuit’s decision in *Uniloc USA, Inc. v. Microsoft Corp.*, 632 F.3d 1292, 1317-18 (Fed. Cir. 2011), in which the court emphasized that reasonable royalty evidence “must be tied to the relevant facts and circumstances of the particular case at issue and the hypothetical negotiations that would have taken place in light of those facts and circumstances at the relevant time.” *Cf. Bascom Global Internet Servs., Inc. v. AOL, LLC*, No. CV 08–1765 (LDW) (ARL), 2011 U.S. Dist. LEXIS 100609, at *6 (E.D.N.Y. Sept. 8, 2011) (citing *Rude* and distinguishing *ResQNet*).

Discovery of Settlement License Negotiations after *ResQNet* and *MSTG*

Although the status of *settlement license negotiations* is not as clear, information about settlement license negotiations is *probably discoverable*, especially where the negotiations lead to an agreement that involves the same patent or similar technology. *See, e.g., High Point SARM v. Sprint Nextel Corp.*, No. 09–2269–CM–DJW, 2011 WL 3241432, at *5 (D. Kan. July 9, 2011) (compelling production of correspondence relating to license negotiations with non-parties based on broad discovery permitted by Rule 26 and “[b]ecause the requested discovery relates to the courses of action followed by similarly situated alleged infringers of the patents-in-suit”). On the other hand, at least two judges in the Eastern District of Texas have suggested that such discovery, while not forbidden, will be unusual and determined on a case-by-case basis. *See Clear with Computers, LLC v. Bergdorf Goodman, Inc.*, 753 F. Supp. 2d 662, 664 (E.D. Tex. 2010) (Judge Davis) (“The Court expects that its finding here allowing discovery will be the exception, not the rule, and in most cases discovery of the negotiations will not be warranted.”); *Charles E. Hill & Assocs., Inc. v. ABT Elecs., Inc.*, 845 F. Supp. 2d 427, 428–30 (E.D. Tex. 2012) (Judge Gilstrap) (“[A]pplying the case-by-case analysis adopted in *Clear with Computers*, this Court finds that here, the *Goodyear* rule must yield to the exception attributed to *ResQNet*.”).

An important factor may be the stage of negotiations. For example, former Judge Ward, also of the Eastern District of Texas, refused to allow discovery of “ongoing or unconsummated settlement and licensing negotiations with the patents-in-suit.” *See Mondis Tech., Ltd. v. LG Elecs., Inc.*, Nos. 2:07–CV–565–TJW–CE and 2:08–CV–TJW, 2011 WL 1714304, at *5 (E.D. Tex. May 4, 2011). (Objections based on Fed. R. Evid. 408 are misplaced because that Rule

governs admissibility, not discovery, and Fed. R. Civ. P. 26 authorizes discovery of relevant, non-admissible evidence. *See, e.g., Small*, 808 F. Supp. 2d at 586.)

In general, district courts will permit discovery of settlement license negotiations if the negotiations are relevant to the calculation of a reasonable royalty. Therefore, a party seeking such discovery should explain how the negotiations are relevant to that calculation. *See, e.g., MSTG, Inc. v. AT & T Mobility LLC*, No. 08 C 7411, 2011 WL 841437, at *3–4 (N.D. Ill. Mar. 8, 2011). Different district courts, however, may impose heightened standards on parties seeking discovery of such negotiations. For example, in *Implicit Networks*, the court initially denied without prejudice Juniper’s motion to compel the production of documents regarding Implicit’s licenses and negotiations “in light of the special concerns surrounding the disclosure of settlement negotiation information” and because “Implicit has *not* put its negotiations of the licenses in dispute”. *Implicit Networks*, slip. op. at 2-3 (N.D. Cal. June 5, 2012) (emphasis in original); *see also ABT Sys., LLC v. Emerson Elec. Co.*, No. 4:11CV00374 AGF, 2012 WL 6594996, at *3 (E.D. Mo. Dec. 18, 2012) (denying motion to compel discovery of correspondence related to settlement and licensing negotiations because Emerson “has not posited any particularized relevance to the information it seeks,” but authorizing Emerson to seek further discovery of the negotiations “[s]hould it become apparent that ABT’s experts make use of statements made during the settlement negotiation to form their opinions”); *Avocent Redmond Corp. v. Rose Elecs.*, No. C06–1711RSL, 2012 WL 4903272, at *3 (W.D. Wash. May 29, 2012) (sustaining objections to proposed Rule 30(b)(6) deposition topics seeking information regarding settlement license negotiations); *but see Barnes and Noble, Inc. v. LSI Corp.*, 2012 WL 6697660, No. C–11–02709EMC (LB) at *2 (N.D. Cal. Dec. 23, 2012) (ruling that *MSTG* does not require moving party to make a “heightened” showing to discover draft licenses and licensing communications).

Admissibility of Settlement License Agreements after *ResQNet* and *LaserDynamics*

Following *ResQNet* and *LaserDynamics*, settlement license agreements may be admissible to prove reasonable royalty damages if there is a close “fit” between the patents-in-suit and the technology that is the subject of the agreements, and if the party proffering the agreements convinces the trial court that the agreements reliably reflect royalty terms that the parties would have agreed upon pre-infringement.

District courts have adopted three different approaches when considering whether settlement license agreements are admissible. Some courts have established a bright-line rule that comparable agreements are admissible. *See, e.g., Datatresury*, 2010 WL 903259, at *2 (agreements admissible for “essentially all purposes” and “concerns about the reliability of litigation-related licenses are better directed to weight, not admissibility”). Others perform a case-by-case analysis to determine whether the agreement is comparable or would confuse the jury. *See, e.g., ReedHycalog*, 727 F. Supp. 2d at 547 (admissibility of litigation licenses “must be assessed on a case-by-case basis”); *Douglas Dynamics, LLC v. Buyers Products Co.*, No. 09-cv-261-wmc, 2010 WL 4118098, at *1 (W.D. Wis. Oct. 8, 2010) (Judge Conley) (“Because determining a reasonable royalty is a fact-specific inquiry dependent on the consideration of

many factors . . . even licenses arising from resolution of unrelated patent litigation can ordinarily be considered.”); *ePlus, Inc. v. Lawson Software, Inc.*, 764 F. Supp. 2d 807, 813 (E.D. Va. 2011) (Judge Payne) (agreements excluded because they “differ considerably from the factual predicates present here”). Finally, at least two district courts have opined that a settlement license agreement is ordinarily not admissible to prove patent-infringement damages, but might be admissible if it were a basis for a damages expert’s *Georgia-Pacific* analysis. *See, e.g., Abbott Labs. v. Sandoz, Inc.*, 743 F. Supp. 2d 762, 766–67 (N.D. Ill. 2010) (Judge Coar) (denying Abbott’s motion *in limine* to exclude evidence of settlement license agreements because, while agreements would otherwise be inadmissible under Rule 408, Abbott’s damages expert relied on them); *Century Wrecker Corp. v. E.R. Buske Mfg. Co.*, 898 F. Supp. 1334, 1341 (N.D. Iowa 1995) (Judge Bennett) (because plaintiff’s expert relied on settlement agreements in reasonable royalty calculation, defendant could introduce agreements to rebut expert’s testimony). *Cf. PharmaStem Therapeutics, Inc. v. Viacell, Inc., et al.*, No. C.A. 02–148 GMS, 2003 WL 22387038, at *3–4 (D. Del. Oct. 7, 2003) (Judge Sleet) (excluding agreements based on policy of Rule 408, despite damages expert’s initial reliance on them).

To attempt to exclude a settlement license agreement at trial, a party can argue that it “arises under the threat of litigation . . . [and therefore] has little relevance to the hypothetical reasonable royalty situation.” *See Cornell Univ. v. Hewlett–Packard Co.*, No. 5:01–cv–1974–RRR–DEP, slip op. at 7 (N.D.N.Y. May 14, 2008) (Fed. Cir. J. Rader, sitting by designation). Obviously, that argument would be strengthened by facts showing that the subject settlement license agreement was the product of a party’s particularized concerns about litigation exposure. *See, e.g., LaserDynamics*, 694 F.3d at 77 (citing *Rude*, 130 U.S. at 164). (Like the facts in *ResQNet*, the facts in *LaserDynamics* were extreme. *See* discussion *supra* at 9–11. The proponent of the admissibility of a settlement license agreement could argue that *LaserDynamics* only stands for the general proposition that courts should consider the best evidence of a hypothetical negotiation, and that the best evidence might be a settlement license agreement.)

Courts will also consider whether admitting a settlement license agreement into evidence might confuse the jury, or would misrepresent the value of the patented invention. For example, in *Fenner Investments, Ltd. v. Hewlett-Packard Co.*, No. 6:08–CV–273, 2010 WL 1727916, at *1–3 (E.D. Tex. Apr. 28, 2010), Magistrate Judge Love, citing *Rude*, excluded settlement license agreements under Fed. R. Evid. 403 because, in his view, the potential for jury confusion outweighed whatever probative value the licenses might have had. He distinguished *ResQNet*, observing that the *ResQNet* majority did not consider admissibility, pointing out that the damages holding was limited to the first *Georgia-Pacific* factor regarding licenses of the patent-in-suit, and noting that the trial in *ResQNet* was a bench trial, and so there was no risk of jury confusion. *Id.* at *3.

Attorneys arguing against the admissibility of a settlement license agreement may also point to the difficulties of determining whether it is comparable to the patent or technology-in-suit. As Judge Coar cautioned, admitting evidence of settlement license agreements with third parties would “invite a ‘mini-trial’ on similarities and differences in the facts regarding the ‘same’

claims against other defendants.” *Abbott Labs*, 743 F. Supp. 2d at 767 (quoting *Pioneer Hi-Bred Intern., Inc. v. Ottawa Plant Food, Inc.*, 219 F.R.D. 135, 145 (N.D. Iowa 2003)).

Admissibility of Settlement License Negotiations after *ResQNet* and *MSTG*

It is *not clear* whether or when *settlement license negotiations* are *admissible* to prove a reasonable royalty. As indicated by cases such as *Abbot Labs.*, 743 F. Supp. 2d at 767, negotiations are, at least, arguably admissible if they were relied on by a party’s damages expert, and may be admissible in other situations as well. Some commentators argue that settlement-related information should never be admissible as evidence of patent damages. See Tejas N. Narechania & Jackson Taylor Kirklin, *An Unsettling Development: The Use of Settlement-Related Evidence for Damages Determinations in Patent Litigation*, 2012 U. Ill. J.L. Tech & Pol’y 1, 36 (2012) (“[A] close look at Federal Rule of Evidence 408 suggests that settlement-related evidence ought to be categorically excluded when offered to prove damages in a patent infringement case.”).

Historically, the Federal Circuit, citing Fed. R. Evid. 408, has ruled that settlement negotiations are not admissible to prove reasonable royalty damages. See, e.g., *MSTG*, 675 F.3d at 1347 n.4 (collecting cases); *Vanderlande Indus. Nederland BV v. Int’l Trade Comm’n*, 366 F.3d 1311, 1322 (Fed. Cir. 2004) (mediation statement from prior litigation inadmissible under Rule 408); *Medtronic Inc. v. Intermedics, Inc.*, 799 F.2d 734, 741 (Fed. Cir. 1986) (no abuse of discretion excluding settlement offer evidence). Unlike the district court in *Abbot Labs.*, 743 F. Supp. 2d at 767, moreover, some district courts refuse to admit evidence of settlement negotiations *regardless* of whether a party’s damages expert relied on that evidence. See, e.g., *Carpenter Tech. Corp. v. Allegheny Techs., Inc.*, No. 08-2907, slip op. at 2 (E.D. Pa. Nov. 13, 2012) (“Where, as here, the negotiations occurred between the parties to the litigation, concerned the subject of the litigation, and are being offered for the purpose of establishing a reasonable royalty (i.e., the ‘amount of a disputed claim’), Rule 408(a) bars their admission Nor do I find persuasive Carpenter’s contention that the pre-suit negotiations must be admitted because ATI’s expert . . . considered these negotiations as part of his reasonable royalty analysis.”) (internal citation omitted). It is also noteworthy that some district courts do not even apply Rule 408 to settlement negotiations from prior cases or cases involving third parties. See, e.g., *Donnelly Corp. v. Gentex Corp.*, 918 F. Supp. 1126, 1133 (W.D. Mich. 1996) (“[I]t is obvious that the Rule [408] itself does not preclude evidence of these compromises in this case because the offers to compromise the claims do not concern the claim being litigated in this case.”).

While a district court might exclude evidence of settlement license negotiations based on Rule 402 (relevancy), 403 (unfair prejudice and jury confusion *inter alia*), and/or 408 (compromise negotiations), the Federal Circuit’s decision not to consider the admissibility of settlement negotiations in *MSTG* leaves open the possibility that such negotiations are admissible, at least under some circumstances.

Practice Points

The message signaled by all the cases cited in this article is that parties negotiating settlement

licenses in patent-infringement cases should be aware of the potential effects of settlement license agreements and negotiations on pending or future patent-infringement litigation, because those agreements and negotiations may be discoverable and admissible. Attorneys representing settling parties should:

- First and foremost, make their clients aware that settlement license agreements will most likely be discoverable and may be admitted into evidence. Even settlement license negotiations may be discoverable and admissible. When advising patent-holders, point out how settlement terms may influence the monetization of a patent. Agreeing to a reduced royalty because of extraneous considerations, such as an aversion to litigation or the desire for an ongoing business relationship, may come back to haunt the patent-holder during infringement litigation with another party over the same patent.
- If it is desirable that a settlement license agreement and/or settlement license negotiations not be factored into a future reasonable royalty calculation, attempt to incorporate self-serving provisions into the negotiations and agreement to explain why the agreed upon royalty does not reflect the true value of the patent. Explanations might include the exchange of additional valuable consideration such as a cross-license of the accused infringer's patents, or the limited role that the patented invention plays in the accused infringer's products, or the inability of the accused infringer to pay a higher royalty.
- If a court allows prior settlement license agreements and/or negotiations to be used at trial, consider asking for a limiting jury instruction. *See, e.g., Lucent Techs., Inc. v. Microsoft Corp.*, 837 F.Supp.2d 1107, 1125 (S.D. Cal. 2011) (denying motion for judgment as a matter of law where court admitted licenses but instructed jury that licenses must be comparable for jury to consider them as examples of Lucent's licensing policy).
- If it is important that a settlement license agreement or settlement license negotiations remain confidential, add a strong confidentiality provision into the agreement that encompasses all negotiations. While the *MSTG* court reserved "for another day" the issue of discoverability of settlement negotiations, the court strongly hinted that district courts could use their discretionary powers under Rule 26 to limit discovery of confidential settlement negotiations in the absence of a heightened showing of a need for such communications. *MSTG*, 675 F.3d at 1347-48.
- Consider seeking (by agreement if possible) a protective order prohibiting the discoverability of license settlement agreements and negotiations.

- If there is a possibility of protecting settlement license negotiations from discovery, restrict your damages expert to the “four corners” of settlement license agreements when assessing whether they involve patents and technology that are comparable to the patents and technology-in-suit. Otherwise, as in *MSTG*, 675 F.3d at 1348, a court might order that, as a matter of fairness, all documents related to settlement license negotiations must be produced, and they might be admitted into evidence.

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