

Underdeveloped Comparability Analysis Means Exclusion of Reasonable Royalty Opinion

***Meridian Mfg. v. C&B Mfg.*, 2018 U.S.
Dist. LEXIS 172243 (October 5, 2018)**

This patent infringement case in which both parties raised *Daubert* challenges to the opposing expert's damages opinions provides a recap of key legal principles informing reasonable royalty and lost profits calculations. Among the contested issues was how an expert may use noninfringing alternatives when developing a hypothetical negotiation and what an expert, relying on prior licenses, must do to establish comparability to the patented technology. The court here, as well as in other cases, makes it clear that an expert's "superficial recitation of the *Georgia-Pacific* facts, followed by conclusory remarks" does not make the testimony admissible.

Background. The plaintiff was the owner of a patent for an agricultural trailer that helps farmers transport large boxes of seeds to planters in the fields. The trailer features guide plates that facilitate centering the box on a wheeled bed. The guide plates are a special feature. The defendant, a manufacturer of consumer and industrial products, sold a seed tender that the plaintiff claimed violated its patent. After the plaintiff sent a cease and desist letter, the defendant continued selling its trailers. However, following a hearing in late 2015, the court found the defendant's seed tender infringed a specific claim of the plaintiff's patent and the defendant began to redesign its seed tender. The parties continued to disagree over whether the redesign solved the infringement.

Both sides filed pretrial motions, including motions to exclude damages expert testimony under Rule 702 of the federal rules of evidence and *Daubert*.

Defense expert admissible. The defendant's expert was an experienced CPA and certified financial forensic analyst who provided a reasonable royalty analysis and a lost profits analysis.

The expert stated that the defendant had advised her that the contested seed tender had a number of features and that the guide plates were a key feature. The expert therefore identified the latter as the "patentable feature," and, since this feature was only a portion of the tender, she found that apportionment between the guide plates and the tender's other features was necessary. The expert also determined that she lacked the information she would need for an apportionment analysis. Based on information from the defendant, the expert understood the redesigned seed trailer received a good response from dealers and customers because it was sturdier and less expensive to produce. Considering the difficulty of apportioning, the expert therefore proposed that a reasonable royalty in this case should be based on the production cost differences between the infringing design and the redesign. Put differently, "a reasonable royalty would not be more than the cost to [the defendant] to develop and implement an alternative, non-infringing design," the expert said. She proposed a lump-sum royalty of \$15,000 to \$30,000.

The plaintiff argued the expert's testimony was inadmissible. The expert lacked the qualifications to comment on technical matters, specifically to testify about a "patentable feature," the plaintiff said. The court quickly dismissed this objection, noting the expert would be able to explain how a particular feature informed her damages analysis.

The plaintiff also claimed the expert used an unreliable methodology in that she tried to limit reasonable royalty damages to the cost of developing a redesigned seed trailer and in that she considered the defendant's redesigned trailer to be an acceptable noninfringing alternative.

The court first explained the various ways for calculating a reasonable royalty. An expert might rely on an established royalty, the infringer's profit projections for infringing sales, or develop a hypothetical negotiation between the patentee and infringer. The Federal Circuit has found that there is no law that requires reasonable royalty rates be based on the cost of implementing an available noninfringing alternative. At the same time, the Federal Circuit also has held that, practically, the difference between the infringing product or technology and the noninfringing alternative placed a limit on the reasonable royalty rate because in a hypothetical negotiation the infringer would not have paid more than that difference.

The court in the instant case said that the defendant's expert did not put an "automatic cap" on damages based on the cost of redesigning the seed trailer. Rather, the expert concluded that, under the specific facts and circumstances, a reasonable royalty would not be higher than the cost of the redesign. This conclusion was admissible, the court found.

The plaintiff's objection to the defense expert's use of the redesigned seed tender as an acceptable noninfringing alternative for purposes of her lost-profits analysis focused on whether the redesigned product was "available" at the time of the infringement.

The court explained that, under the law, lost profits are not available to the patent holder if acceptable noninfringing alternatives were available at infringement. "Available," the court noted, does not necessarily mean the alternative product had to be on the market. Rather, it could be considered "available" if the infringer could have produced an alternative "and would have known it would be acceptable to consumers at the time of the infringement." Whether an alternative product was "acceptable" is a question for the jury to decide, the court noted.

Here, the defendant's expert understood from statements by the defendant that dealers and customers were reacting positively to the redesigned trailer and that it would have been possible to develop and build the redesign earlier. "If the necessary equipment, know-how and experience were available at the time of infringement, a substitution may be considered an acceptable, available alternative even if it was not on the market," the court said. It found that the defense expert's characterization of the redesigned product was admissible.

The court concluded that all the objections the plaintiff raised regarding the defense expert testimony were appropriate subjects for cross-examination. But they did not require exclusion of the testimony.

Plaintiff's expert partly admissible. The plaintiff's expert performed a reasonable royalty calculation that produced a range of reasonable royalty rates, from 3% to 10% of sales. The analysis was based on the *Georgia-Pacific* factors and particularly on the second factor that considers rates the licensee paid for use of other patents comparable to the patent in suit.

The expert explained that he "examined market rates for similar royalties paid in the industry," using the RoyaltySource database to search for rates "in the machinery, agricultural, forestry and fishing industries." He acknowledged there were limitations regarding the data but did not explain

what the limitations were or how they affected the rates he chose for his analysis. Ultimately, the expert chose six licenses and developed a chart in which he briefly described the licensed technology, but he did not explain how these technologies related to the patented technology. He said he chose the six licenses based on his judgment.

In addition, the plaintiff's expert mentioned other *Georgia-Pacific* factors, describing what these factors focused on. But he did not specifically tie the factors to the facts of the case. "Based upon the factors previously noted, I have identified four potential reasonable royalty rate data points," the expert concluded.

The court found this expert opinion was inadmissible because the expert failed to provide sufficient support for his conclusions. Under case law, prior licenses that do not mention the patent in suit or that "show[] no other discernible link to the claimed technology" are not comparable, the court noted. Further, while those other licenses may cover more patents than the contested patent(s) and include additional terms or cover foreign property rights, the expert drawing on the licenses must account for any distinguishing facts. The court must consider to what extent the expert testimony might "skew unfairly the jury's ability to apportion the damages to account only for the value attributable to the infringing features." See *Ericsson, Inc. v. D-Link Sys., Inc.*, 773 F.3d 1201 (Fed. Cir. 2014).

The court noted that here the expert did not show how the six licenses he claimed were comparables were in fact similar to the patented technology or how they differed and how the differences affected a hypothetical license negotiation in this case. Citing prior case law, the court said, "[A]lleging a loose or vague comparability between different technologies or licenses does not suffice." See *LaserDynamics, Inc. v. Quanta Comput., Inc.*, 694 F.3d 51 (Fed. Cir. 2012).

Regarding the expert's treatment of the other *Georgia-Pacific* factors, the court said the expert

failed to "complete the crucial step of explaining how those factors would influence the parties in a hypothetical negotiation to reach agreement as to his proposed reasonable royalty rates."

For these reasons alone, the court found the plaintiff's expert opinion on reasonable royalty was inadmissible.

All was not lost for the plaintiff, however, because the expert also performed a lost profits analysis based on a market share analysis that was sufficiently reliable to be admissible.

Relying on the industry analysis by the Line of Sight Group (LOSG), internal plaintiff and defense statements, and other studies and documentation, the expert assumed the plaintiff would have made about 24% to 44% of the defendant's sales but for the defendant's infringement. This translated into about \$2.4 million in lost profits, the expert concluded. The combination of reasonable royalty and lost profits damages amounted to total damages in a range of \$3.7 million to \$5.7 million, the plaintiff's expert asserted.

The defendant argued that the expert's lost profits opinion was unreliable because there were available and acceptable noninfringing alternatives. Moreover, the market share analysis was unreliable primarily because the expert "blindly relied" on a third-party analysis and plaintiff information. He failed to perform an independent analysis, the defendant claimed. Also, the profit margins he assumed were unreliable because they included profit margins for other products and certain margin changes.

The plaintiff countered that the market share analysis was permissible under the law and the third-party analysis was the best available evidence. This was the kind of analysis experts in the relevant field typically rely on, the plaintiff said.

The court explained that one of the elements a patent holder claiming lost profits must satisfy is

that there are no acceptable, noninfringing alternatives to the patented technology. If there are such alternatives, a patent holder may show this element by proving, with reasonable probability, that the patent holder would have made sales the infringer made but for the infringement.

The court noted that experts routinely rely on the opinions of other experts the retaining party hired. Here, the expert explained what sources he used and said he had discussions with the plaintiff's management; he also relied on "public information about the industry." The court said the expert appeared to have done his own financial analysis of the plaintiff and the defendant. The expert's opinions on market share and lost profits were not so "fundamentally unsupported" that they had to

be excluded. Moreover, the court found that the expert's decision to apply a historical average profit to the hypothetical sales absent infringement, instead of the actual profit margin for sales alleged to be affected by the infringement, did not make his opinion so unreliable as to be inadmissible. All of these objections can be explored on cross-examination, the court decided.

In conclusion, the court excluded the plaintiff expert's reasonable royalty determination but admitted his lost profits analysis. The court admitted the defense expert's reasonable royalty and lost profits analyses.

Editor's note: All cases referenced can also be found on BVLaw.

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