Consultation on UPC Fees

Submission by UK Intellectual Property Lawyers' Association

This submission is presented by the UK Intellectual Property Lawyers' Association ("IPLA"). IPLA acts as a representative body for law firms in the UK with intellectual property practices who wish to lobby for improvements to IP law. Over 65 firms are members of IPLA, and the vast majority of patent and other litigation and transactional work relating to intellectual property rights in the UK is conducted by these member firms. Because of the international nature of IP, member firms are also familiar with how things operate in many other countries across Europe and in the United States of America. Members act for a wide range of clients, from major multi-national groups of companies to SMEs and technology start-up companies, as well as universities and private inventors and investors. As a group, IPLA probably has unparalleled experience of how existing IP litigation systems work in practice.

IPLA is one of the few organisations which has lodged submissions in all three consultations on the draft UPC Rules of Procedure (the 8th, 14th and 15th drafts), as well as making a number of observations at the Trier public meeting.

There are three important considerations when designing the fee structure for the new Unified Patents Court. The first is the objective is set by Article 36 of the UPC Agreement, which requires that, following the transitional period, the Court's financial revenues (in effect, court fees) should balance its expenditure.

The two other considerations are not set out in the Agreement, but are nevertheless of great practical importance. The UPC is a new court and, at least during the transitional period, will in effect be in competition with national courts. In a number of quarters, there is some scepticism about the new court. The fees should not be set at so high a level as to act as a further disincentive or barrier to entry. Once the Court has established itself, the fees can then be (gradually) increased to a full economic level.

Third, the Court has no mechanism for enforcing payment of its fees. There accordingly needs to be an incentive on a party to pay the fees; the most logical being that the ensuing steps in the procedure will not take place unless the fee is paid. This does not cover the position, however, where a party – usually the claimant – has lost interest in the litigation. For example, if at the end of the written procedure, the claimant concludes that it does not wish to continue, it can simply do nothing. The Court will no doubt subsequently set the value-based fee, but such a claimant has no interest in paying it (even if the amount is substantially discounted), and there is at present no way of compelling payment.

In the remainder of this submission, we will address first "Alternative 1", then "Alternative 2", and then the provisions common to both alternatives.

1. <u>Alternative 1</u>

Alternative 1 provides for reimbursement of the court fees if an action is withdrawn or settled, in varying percentages depending whether the withdrawal or settlement takes place during the written, interim or oral procedures. This is an attractive proposal, in that it provides an additional incentive for parties to settle, or for a claimant to recognise the weakness of its case and to withdraw at an early stage, when the reimbursement is largest. IPLA accordingly supports Alternative 1.

There are however some practical issues with Alternative 1 which we believe need to be addressed.

As the Rules currently stand, the value-based fee is not assessed (Rule 22) or payable (Rule 371(4)) until the interim procedure. The requirement for a very detailed written procedure means that that a likely time for settlement will be the end of that procedure, when the parties have details of each other's cases. If the parties settle, or if the claimant decides that it no longer wishes to pursue its claim, before the value-based fee becomes payable pursuant to Rule 371(4), they can apply to the Court under Rules 365 (settlement) or 265 (withdrawal), and the Court will then no doubt proceed to determine the value of the litigation so that the (discounted) value-based fee can then be paid.

The problem is that parties who have no further interest in the litigation have no incentive to pay the (discounted) value-based fee. This is particularly likely with non-practising entities, who can readily transfer the patent into the name of a shelf company which would be wound up as soon as the litigation was over.

There are two possible ways round this problem.

The first option, which is our strong preference, is that no value-based fee should be payable at all until it has been assessed. In effect, this means that there would be a 100% discount off the value-based fee if a settlement took place during the written procedure or at the very beginning of the interim procedure. However, this is not unreasonable: the fixed fee of €11,000 will have been paid, and this should cover the costs incurred by the Court during the written procedure, which involve limited formalities checks and very little engagement by the judge rapporteur.

There will of course be cases where the litigation makes significant use of the court's resources during the written procedure, for example, where there is an application for provisional measures etc. To deal with this, Rule 371 might specify that the value-based fee will be assessed at the Case Management Conference or (if earlier) at the first inter partes application: the fee would be payable within 14 days of assessment.

The second, less preferred, option would be that the value-based fee should be payable by the Claimant at the outset on the basis of its estimate of the value of the litigation. A balancing payment or rebate would then be payable once the value of the litigation has been determined by the Court. The timing of the payment needs to be sensible: the value-based fee can be very substantial, and even for a large corporation, releasing the funds for payment may take some time. However, this should not hold up the start of proceedings, which in many cases may be urgent. We would suggest that the time for payment should be one month after the statement of claim is lodged, with the fall back provision that the defence is not required to be lodged until two months after payment of the value-based fee by the Claimant.

If the value-based fee is assessed at a later stage, a suitable incentive for payment might be that the recoverable damages be limited to the value in respect of which the fee has been paid; alternatively all steps in the case should be suspended for so long as the value-based fee remains unpaid.

2. **<u>Alternative 2</u>**

We object to Alternative 2 for four reasons, namely, that it is not permitted under Article 36(3) of the UPC Agreement; that it is in practice unfair; that it can lead to inefficiency; and it is open to abuse.

<u>Article 36(3)</u>

Alternative 2 provides for the value-based fees to be exempted for SMEs, micro-entities, non-profit organisations, universities and public research organisations. It appears to be based on Article 36(3) of the UPC Agreement. However, Article 36(3) provides that: "*the Court fees shall be fixed at such a level as to ensure a right balance between the principle of fair access to justice, in particular for small and medium-sized enterprises, micro-entities, natural persons, non-profit* *organisations, universities and public research organisations and an adequate contribution of the parties for the costs incurred by the Court, recognising the economic benefits to the parties involved, and the objective of a self-financing court with balanced finances.*"

In other words, the amount of the court fees should not impede fair access to justice for the identified entities; Art 36(3) does not say that there should be a special or different fee regime for all of such entities. Rather, the final sentence of Article 36(3) states: "Targeted support measures *for small and medium-sized enterprises and micro-entities* may be considered" (our italics). In other words, if there is to be an exemption from the standard rules on value-based fees, it should apply only to SMEs and micro-entities. In our view, there is some justification for waiving the value-based fee for SMEs and micro-entities who might find it difficult to afford the fees (while falling above the "threatens the economic existence" provision in draft Rule 370(7)), but we see less justification – not least because Article 36(3) does not envisage it - for special exemptions for non-profit organisations, universities and public research organisations which are not SMEs; if they are big enough, they should be able to pay.

Fairness

There is inevitably a boundary between an enterprise which is an SME and one which is not, and it is manifestly unfair that an organisation which lies just below the threshold should pay no value-based fees at all, while one which has, say, one additional employee or a slightly higher turnover, should pay what might be a very substantial value-based fee, which could, indeed, be much greater than the marginal difference in turnover.

There is a more important but more subtle way in which an exemption from value-based fees for SMEs is unfair. As defined, an SME is an enterprise or group of linked enterprises having less than a defined turnover or balance sheet total, and number of employees. However, there are many larger companies or groups of companies in which individual business units fall within the financial and employee thresholds, but do not qualify as SMEs because of their association with the larger group. Nevertheless, they are required to operate within the financial constraints of their own business, and there is no reason why they should face a substantial barrier to entry to patent enforcement litigation, in the form of value-based fees, which is not faced by business units of the same size which are not part of a larger organisation.

Inefficiency

Although the basic definition in Article 2 of Title 1 of the Annex to Commission Recommendation number 2003/361 is relatively straightforward, the definition of an SME contains a number of uncertainties or potential areas of dispute. For example, there is no definition of "public investment corporation" in Article 3(2)(a). Where there is a significant advantage in qualifying as an SME, and where a defendant might see significant tactical advantage in establishing that a claimant is not an SME (and so has to pay the full value-based fee), there is potential for significant disputes as to whether a Claimant is indeed an SME, given rise to undesirable satellite litigation.

Abuse

There is a very significant financial advantage, if alternative 2 is adopted, in a patentee being an SME, and patentees will do what they can to secure that advantage. Since patents are freely assignable, there is no legal reason why a substantial enterprise should not transfer a patent into a company which qualifies as an SME (it could be owned by nominee shareholders, for example) which then acts as claimant and secures the advantage of no value-based fees. For many enterprises, such manipulation of the system is likely to be impracticable, since it will adversely impact the claim for damages, and may have adverse tax consequences. However, in businesses where the patent ownership is not linked to trading activities, as in the case of non-practising entities, manipulation of patent ownership so as to avoid payment of value-based fees will be relatively straightforward. Such abuse could give non practising entities a significant tactical advantage.

The real reason why it might be appropriate to exempt an SME from value-based fees is that, if it had to pay those fees, it simply could not afford to litigate. However, although the fees are substantial, they are no more, and in most cases much less, than the legal fees which the company will incur in the litigation. We ask, rhetorically, why, if a company can afford the legal fees, it should not also be required to pay the value-based fees? In some cases, an SME might be supported by a third party funder, and again, if the funder will pay the legal fees, why should it not also pay the court fees?

The solution to this problem lies in proposed Rule 370(7). The threshold test could advantageously be a little more generous to the SME – for example, that the Court fees are more than a certain percentage of its gross profits for the previous year. In any event a party should be required to explain why it can afford to pay its lawyers but cannot afford to pay the Court. There may well be circumstances where the answer would justify an exemption, for example, if the lawyers are acting essentially "pro bono" or on a "no win no fee" basis, or if a small patentee faced very large volume of infringements from major companies – where the value-based fee might be disproportionately large.

Although a litigant may be unable to afford the value-based fee at the outset of litigation, if the value of the litigation is substantial, and the party is successful, then it can expect to receive a substantial payment by way of damages. In such circumstances, the justification for an exemption at the outset no longer applies and we suggest that the value-based fee should be payable when damages are paid, or when a case is settled for a large payment of compensation.

3. **General Comments**

It is important that value-based fees are not duplicated. For example, a claim for a declaration of non-infringement might be met by a related claim for infringement. A value-based fee should not be payable in respect of the claim for infringement if a value-based fee has already been triggered by the claim. Similarly, if a value-based fee has been paid for an action for revocation (as we propose below), no value-based fee should be payable on a responsive action for infringement of the same patent.

Declarations of non-infringement ("DNIs") raise particular issues in any event. In some cases, a DNI is sought because a patentee has made allegations of infringement, and the accused infringer needs to be able to bring the case to court to achieve judicial certainty where the patentee is reluctant to start proceedings. In such circumstances, the accused infringer may legitimately take the view that the value of the litigation is negligible, since it is seeking to establish that it has no liability to the patentee. In other cases, a prudent company might be aware that a proposed product could be accused of infringement, and brings proceedings to secure judicial certainty before it invests in manufacturing the concerned product. In such circumstances, it is impossible to come up with any sensible valuation of the litigation (even on the basis of the volume of products made which the claimant says are not infringements) since the expected turnover in the concerned product is too far into the future to make any but the most speculative of estimates.

Even if it is possible to value a DNI case sensibly, a further problem arises. If the patentee starts proceedings for infringement following the DNI action, then the DNI claim is stayed under Rule 71. In such circumstances, the DNI claimant has received no "value" from the Court and it seems inappropriate that it should have to pay a value-based fee, or at least that such fee should be refunded.

Further observations with regard to declarations and non-infringement and revocation claims

It is inappropriate as a matter of principle that a party should be required to pay a value-based fee for something which is in effect a defence. We understand that this is the basis on which no value-based fee is payable in respect of a counterclaim for revocation.

This leads however to the question: does the same argument justify there being no value-based fee for a freestanding revocation claim in the Central Division?

We submit that, if a person initiates proceedings, that person should pay a value-based fee (based on the value of the proceedings to the Claimant, not the value to the patentee), even if the purpose of the proceedings is defensive (e.g. that if the Claimant is successful, it will "clear the way" for a proposed new product). However, it is not appropriate that a value-based fee be payable where a party files a (counter)claim in response to an earlier claim. This principle applies not only to a revocation, but also to a declaration of non-infringement.

Furthermore, if the patentee responds to a claim for a declaration of non-infringement with a claim for infringement, the Court should not receive any more value-based fees than if the declaratory action had not been started and the plaintiff simply sued for infringement.

The need to avoid duplication of value-based fees is one reason for deferring the assessment (and payment) to the interim procedure, when the situation will be clearer.

Guidelines

It is difficult to comment in much further detail without the proposed Guidelines referred to in draft Rule 370(5). We understand that draft Guidelines have been prepared. We strongly urge the Preparatory Committee to put the proposed Guidelines out for consultation. As the basis of assessment will be crucial to decisions fixing the value-based fees, users should be given an opportunity to comment on this basis before it is put in place.

It has been suggested that the UPC will simply value cases in the same way as is currently done by the German courts. This is unsatisfactory for a number of reasons.

First, we have been unable to find any clear description of how the German courts assess the value of the case.

Secondly, the majority of judges in the UPC will not be German and will have no experience of how the German system operates.

Thirdly, the UPC is a new court, and its procedures should be justified on their own merits and not simply because they reflect what has previously been done in one or other national system. The fact that German courts have valued cases in a particular way is not sufficient reason for that valuation method to be adopted by the UPC.

One major difference between the UPC and the German system is that, in the UPC, a claim can be made in respect of more than one patent. We understand that this does not happen in Germany. Guidance will be needed as the how to approach the valuation exercise in a case where more than one patent is asserted. It is not appropriate that a separate value-based fee should be assessed in respect of each patent, since there can be significant savings in court time in dealing with more than one patent: there is usually significant overlap in the factual and technical background.

We note the proposal in draft Rule 370.2(6) that a value-based fee should be payable on final appeals. IPLA considers that this is inappropriate. Certainly, the Rules Committee did not consider that there should be a value-based fee on appeals (see Rule 288, which is in the set of the Rules approved by the Preparatory Committee). As a matter of principle, an appeal is essentially a continuation of the procedure to resolve the dispute between the parties. Further, if the appeal succeeds, the losing party would have to pay two value-based fees because the court at first instance was mistaken, which is not fair.

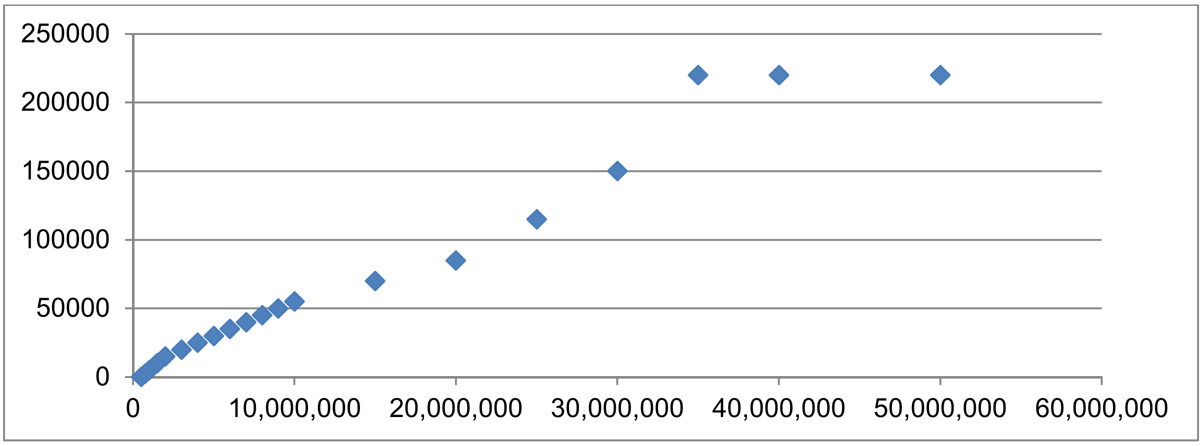
In addition, since (save in exceptional circumstances) no new facts or evidence can be admitted on an appeal, significantly less case management will be required and payment of a very substantial value-based fee is not justified.

Furthermore, is it safe to assume that the value of an appeal is the same as the value of the first instance case? This may seem sensible (and administratively simple) but this should be clarified. Otherwise, there may be another round of discussion about the value upon which to base a fee (for example, to the extent that the value is based on the turnover in the accused product, more information will be available at the time of an appeal than when the first instance action is begun). And what happens if the appeal relates to only part of the subject matter of the first instance case?

Similar considerations arise in relation to the procedure for the determination of damages. First, it is not fair that an unsuccessful defendant should pay two value-based fees for what is essentially the same claim. Second, the procedure is not a separate claim; it is simply the continuation of a claim for infringement, which has been bifurcated so that the court's time is not wasted on damages issues unless a decision on liability shows that the assessment is necessary.

4. <u>Amounts of value-based fees</u>

The value-based fees set out in the Table of Fees rise steeply between €20m and €30m, there is then a huge jump between €30m and over €30m, and then no further increases – see graph below. We are concerned that, if there is a significant difference in the amount of the value-based fee payable above and below a particular threshold, there is an incentive on litigants to argue which side of the threshold the true value lies – many defendants will try to force the claimant to pay a higher fee because this will confer a tactical advantage.



We accordingly propose that the value-based fees should be set in a way which minimises this problem. What we propose is, quite simply, that the value-based fee should be 0.7% (or perhaps 0.6%) of the value of the litigation, up to a total value-based fee of €220,000.

5. <u>Fixed Fees</u>

In the fixed fees for actions, why is the fee for an application to determine damages disproportionately low, whereas the fee for an appeal is disproportionately high, compared to the fixed fees for an infringement action (as well as counterclaim for infringement, application for declaration of non-infringement and action for compensation for license of right, all of which are €11,000)? We suggest these should all be the same.

The fee for an application for provisional measures also seems disproportionately high, particularly in comparison to applications for an order to freeze assets, for inspection and preserving evidence, all of which can raise similar issues and use similar amounts of court resources. These fees seem somehow to be related to the remedies sought, rather than the use of court resources. We suggest the fees for all such interim applications for relief/court orders should be the same. We appreciate that provisional measures may have a greater value to the claimant than some of the other remedies. This can be dealt with, as suggested above, by the court assessing the value of the litigation at the time of the first application to the court, even if during the written procedure.

If an application for leave to appeal is made, which is allowed, the additional fee for an interlocutory appeal should not be payable: if the first instance Court refused leave and the Appeal Court rules that leave should have been granted, why should the appellant pay double the fee? Further, as provided, the fee for an interlocutory appeal under Rule 220.1(c), which is an appeal in relation to orders under inter alia Articles 59 and 60, is nearly nine times that for the first instance applications themselves. This seems disproportionate. We would suggest that the initial fee and the appeal fee should be the same, and not set so as to serve as a disincentive to appeal.

We have considered whether there should be a separate value-based fee on an application for provisional measures (interim injunction), which can be a particularly powerful remedy. We take the view that this would not be appropriate since the value of provisional measures is likely in very general terms to correspond to the damages payable for infringements committed where the provisional measures not granted.[1] Nevertheless, we are aware that in many cases, the grant of an interim injunction will lead to a case being settled, and it would be undesirable that, having occupied significant court time, and providing the claimant with significant benefit, the claimant were then to secure a substantial discount on the value-based fee if the case is settled. This is another consideration in support of our suggestion that the value-based fee be assessed early where there is an application for provisional measures.

6. <u>Ceilings on Recoverable costs</u>

We generally support the principle that there should be ceilings on recoverable costs (meaning a limit on the size of a costs order that may be made against a losing party) according to the value of an action, without taking into account the simplicity or complexity of the legal and factual issues, since irrespective of the simplicity or complexity, the costs incurred by the lawyers ought to relate to the value of the action. A party may choose to "push the boat out" in a low value action, but if it wins, it should not expect its opponent to pay for that luxury. There are nevertheless some issues which the current proposal does not address.

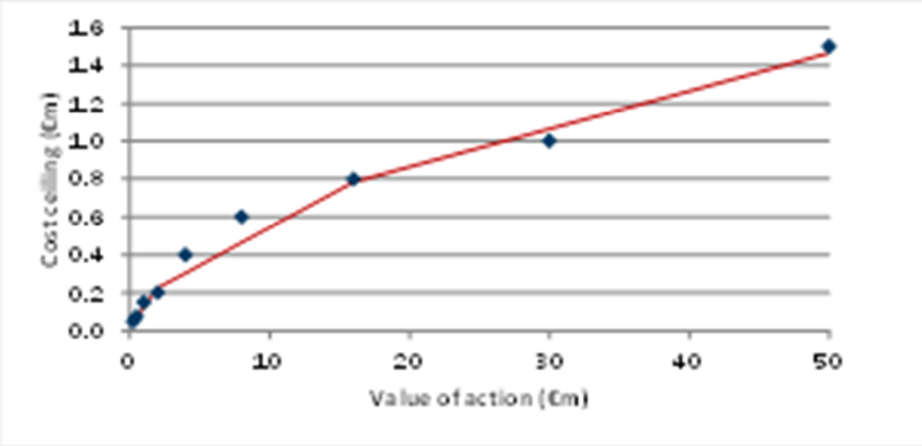
First, we assume that, where cases are settled, the parties will make their own agreement as to the costs of the action (including court fees). However, when an action is withdrawn unilaterally before the value of the action has been assessed, how does the court determine which ceiling applies – especially if the parties in their written submissions have not agreed on the valuation (which is quite likely)?

Second, how does the court assess the appropriate ceiling for a revocation action or counterclaim for revocation, where there is no value-based fee at all (hence there will have been no value assessment before the end of the interim procedure, and order to that effect)?

Third, what happens if there is more than one patent in suit in an action?

[1] It is accepted, at least in the UK, that some infringements can cause significantly more damage than can be quantified by a conventional damages calculation based on sales by the infringer – that indeed is one of the major reasons why interim injunctions are granted by the English courts. However, we understand that it is not intended that the valuation of litigation should involve that degree of sophistication – and, indeed, if it did, it is likely to lead to significant argue and satellite litigation.

As with the value-based fees, there is a problem that the ceilings “jump” around the various value thresholds. Something where the ceiling is a reducing percentage of the total value may be preferable, as shown in the following graph:



This graph shows:

- Ceiling is 20% of the first €0.25m
- Plus 10% of the next €1.75m
- Plus 4% of the next €14m
- Plus 2% of all additional amounts (possibly with a cap when the ceiling reaches €2m)

The proposal does not address the position where an action involves more than one patent. We suggest that the ceiling should be raised by 50% if there is a second patent in suit, and 25% (of the original ceiling) for each additional patent above two.

We assume that the ceilings will apply to the total representatives’ costs for an action and counterclaim for revocation of the patent in suit. Should a reduction in the ceilings be made if there is no counterclaim for revocation? We suggest not, as where there is no counterclaim for revocation, the matter can be left to the judge to assess whether the costs in an “infringement only” case are reasonable and proportionate.

7. <u>Opt out fee</u>

We are concerned about the wisdom of attempting to raise revenue through opt out fees. It is expected that parties may see it as attractive to attack the concept, for example because they have a large number of patents they wish to opt out so that the total fee is large or because a patent is attacked and they had failed (for whatever reason) to register an opt out. They might seek to do so on the following lines:-

1. Article 70(1) UPCA only empowers fees to be collected in respect of proceedings before the court, but at the time of an opt out there are no such proceedings so the collection of opt out fees is ultra vires. Further, rules can only be made in respect of proceedings before the UPC - see Article 41 UPCA. This supports the view that any rule that purports to affect anything which is not part of proceedings is ultra vires. Thus whilst it is appropriate for the status of any opt out to be checked at the start of litigation, see R 16, this does not extend the proper ambit of the rules or any fees regime to the pre-litigation phase.

2. It may also be pointed out that under EPC article 2(2), European Patents are to be "subject to the same conditions as a national patent ... unless this Convention provides otherwise."

Both the opt out fee and the requirement to give notice under art 83(3) subject European Patents to different conditions from national patents and so contravene the EPC. Whilst article 149a envisages some States entering into an agreement (such as the UPCA), an applicant for a European Patent might have supposed that if such an agreement called for national patents and European Patents to be treated differently, those states would have sought first to procure an amendment to the EPC. It may also be argued that before 13 December 2007, when EPC 2000 came into effect, there was not even a suggestion that any later agreement (such as the UPCA) would seek to distinguish between European Patents and national patents. The transitional provisions for EPC 2000 make clear that EPC 2000 only applies to applications made after 13 December 2007.

3. The Preparatory Committee for the UPC may therefore be unwise to count on being able to recover opt out fees – in our view it would be better to play safe and not try to recover them but rather collect court fees only from those who are unambiguously parties to proceedings before the court, in line with Article 70(1). This may mean that some other court fees should be slightly increased.

4. Further if, notwithstanding this risk, the Preparatory Committee is determined to attempt to charge opt out fees, we do not understand how €80 can be the cost of notifying each opt out. All that appears to be required is the patent number, brief details of the patent (though why this information is required by the rules is unclear) and the identity of the proprietor(s) or applicant(s), appropriate contact details for the person filing the opt out and, where applicable, of their representative and payment of the fee - see UPCA article 83(3) and rule 5(3). If an SPC is to be opted out corresponding details are required for the SPC. Those details will be supplied electronically in fields on the relevant electronic form and can be automatically transferred to a database of opt outs as soon as payment has been logged by the UPC's computer system and any necessary information (rule 5 (12)) passed to the EPO (which could also be generated automatically). The procedure will be entirely automatic and will involve no work by UPC staff at all. The time when any deficiency in such a registration will come to light is when proceedings are commenced and the opt out is scrutinised under rule 16. Once proceedings are commenced fees become payable and these can be set at the level necessary to cover the cost of scrutiny.

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