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Summary report of replies to the public consultation on the follow-up study on patent litigation insurance, carried out by CJA Consultants, Ltd

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1. INTRODUCTION TO THE FOLLOW-UP STUDY: BACKGROUND AND MAIN CONCLUSIONS

1.1. Background of the follow-up study

Patent litigation insurance (PLI) has long been considered important as a means of **ensuring access to patents for SMEs** which do not have extensive legal resources and are put off from developing, patenting or litigating patents on new technologies due to the expense, complexities and delays in the patent systems in Europe. However, attempts by the private sector to provide such insurance have rarely been successful up to now.

This issue was raised in the 1997 Commission 'Green paper on the Community patent and the patent system in Europe'¹ and the subsequent 1999 follow-up Communication² in which the Commission committed itself to "examine the most appropriate way to give the legal costs insurance system the impetus it deserves".

As part of this examination, the DG Internal Market and Services of the European Commission commissioned in January 2002 to CJA Consultant, Ltd a study³ aiming to analyse the need for, the feasibility and the implications of introducing an insurance scheme against cost for litigation in patent cases at European level.

This first study laid out a number of broad alternatives proposed by the parties concerned and which could form the basis of possible viable insurance schemes in future. Therefore, in the light of the need for definitive conclusions after that first study, a follow-up study was commissioned in 2004 to CJA Consultants, Ltd with the aim to evaluate on a highly detailed basis (i.e., a detailed business plans), the feasibility of a small number of alternative insurance schemes. This study was finalised in 2006⁴.

1.2. Main conclusions of the follow-up study

The follow-up study proposes to reach a widespread patent litigation insurance scheme through a temporarily **mandatory system**. Such scheme would provide a critical mass of premiums and would avoid the high cost of an initial technical risk assessment.

A risk assessment would only be carried out for the reduced percentage of patents that finally get involved in litigation.

¹ Detailed information about the Green paper can be found in:

http://ec.europa.eu/internal_market/indprop/patent/index_en.htm#docs

The Green paper can be found in: http://ec.europa.eu/internal_market/indprop/docs/patent/docs/pat_en.pdf

² http://ec.europa.eu/internal_market/indprop/docs/patent/docs/8682_en.pdf

³ This study is available in the European Commission - DG Internal Market and Services website:

http://ec.europa.eu/internal_market/indprop/patent/index_en.htm#studies

⁴ This study is available in the European Commission - DG Internal Market and Services website:

http://ec.europa.eu/internal_market/indprop/patent/index_en.htm#studies

Both pursuit and defence cover would be always foreseen for insured patentees. However, a insured patentee would only be entitled to litigate with insurance cover if a technical risk assessment gives at least a 51% chance of success. Moreover, the cost of the technical risk assessment for an insured plaintiff would only be covered if he gets an assessment of its chances of 51%

The proposed mandatory insurance would apply to all patents granted by the European Patent Office.

However, some companies would be exempted from such a mandatory scheme. These companies would have either global business ("global oriented" companies) and therefore global litigation, or they would be known highly risk-adverse patentees (an insurance pool is proposed for these ones). Companies already having bespoke insurance would also be exempted.

National patent offices would control the existence of the required insurance policy or the exemption certificate at the moment the patentee pays the renewal fees for its patent.

Premiums for several scheme options are calculated. The table below provides an example of premiums for one of the studied scheme options covering European patents for pursuit and defence, with exclusion of damages, certain excesses/co-insurance and a limit of €250.000 indemnity. The table shows the impact of the premiums on the total cost of obtaining and maintaining a patent in several jurisdictions for a period of ten years after filing without any public funding:

(Part of) Table 14: Examples for European Patents validated in:	All costs	premium	Premium as % of all costs	Premium as % grant, validation & renewal costs
Germany, UK and France :	60,209 €	12,240 €	20 %	28 %
UK, France and Spain	49,874 €	5,700 €	11%	15 %
Germany and Netherlands	52,227 €	9,000 €	17%	24 %
Germany, France, Spain and Belgium	58,242 €	10,080 €	17%	23 %

The table below provides putative premiums as a percentage of costs for the projected Community Patent⁵ for a period of 10 years from application (without public funding):

Table 15: Calculations for a Community Patent						
Costs to Grant (Average of Direct and PCT Route)	Probable Order of Opposition Costs	Probable Order of Renewal Costs	License Handling	Litigation Costs (200 cases per year, first instance and 50 appeals)	Total	Premiums
						Percentage of costs
10,000 €	1,950 €	2,500 €	8,568 €	360 €	23,378 €	1,500 €
						6.4 %
20,000 €	1,950 €	2,500 €	8,568 €	360 €	33,378 €	1,500 €
						4.4 %
30,000 €	1,950 €	2,500 €	8,568 €	360 €	43,378 €	1,500 €
						3.4 %

⁵ Assuming that 200.000 Community Patents are granted per year with a litigation ratio of 1:1000 and €250.000 indemnity

2. ANALYSIS OF THE RESULTS OF THE PUBLIC CONSULTATION ON THE FOLLOW-UP STUDY

Subsequent to the submission of the final report of the follow-up study by the consultants, DG Internal Market and Services launched a public consultation at the beginning of October 2006 through its website⁶. Interested parties were invited to provide the European Commission with comments on this study until 31 December 2006.

DG Internal Market and Services received 28 replies. Out of those, 3 came from insurers, 2 from national patent offices, 14 replies from national, European and American industry and SMEs associations active in several different sectors (including biotechnology, pharmaceuticals and IT), 1 contribution from a company, 4 from associations of national patent attorneys, and 4 from individuals.

2.1. General remark

The overall **stakeholders' reaction** to the study's conclusions **is negative**.

All the responses to the consultation oppose the introduction of the insurance schemes proposed by the study. The most criticised issue is the proposal of introducing a mandatory insurance scheme. Only two responses could support the idea of a **mandatory system** but not as the one proposed.

The following paragraphs sum up the stakeholders' responses, grouped together under some main topics.

2.2. Mandatory PLI system and some related issues

Stakeholders consider that a mandatory system would entail serious problems and many responses underline that its effects would be **detrimental for European innovation** and competitiveness, especially for SMEs. Only one response from the CGPME (an association representing French SMEs) states that a mandatory system could be acceptable if premiums were affordable.

Some stakeholders underline that "insurance cover pushes the balance towards litigating rather than settling an infringement dispute" which is not desirable, i.e., mandatory schemes could trigger **more litigation in Europe**, creating greater legal uncertainty.

Furthermore, since the proposed schemes foresee defence cover and are available for patentees from non-European countries, some stakeholders fear that foreign "patent trolls" could be encouraged to enter the European market and take legal action against alleged infringers of unexploited, often trivial patents. However, some responses coming from SMEs' representatives consider defence cover as a way to prevent threats of unjustified litigation by big companies.

⁶ http://ec.europa.eu/internal_market/indprop/patent/index_en.htm#studies

The federation of German enterprises, DIHK, suggests that a compulsory insurance for patent litigation is a "too intensive intervention in their company's strategy" since most of its associated companies try to reach cross licensing agreements with infringers rather than going to court.

The proposed **level of premiums** is considered **too high** by stakeholders. Some of them consider that table 14 above shows that the already high patenting and maintaining cost could be increased by up to almost 30%

The proposed schemes are broadly seen as a sort of extra tax or cost mainly for SMEs. Furthermore, it is indicated that the proposed pool for uninsurable patentees (paragraph 16.16 of the study) could substantially increase premiums.

It is also feared that manufacturer SMEs would have to face additional costs for patent clearance searches before launching a new product (paragraph 14.28.1) which does not apply to globally oriented companies.

Some responses also indicate that since the schemes apply only to European patents, it could discourage SMEs from using European patents, undermining the European Patent Convention.

Some concerns are expressed regarding the increase of the administrative burden on **national patent offices** since the study proposes them to check annually whether an insurance policy or a certificate of exemption has been issued before renewing the patent.

One response indicates that the position of the insured vis-à-vis the insurers is unbalanced since "individual insurers could refuse to insure specific patents or specific patentees for any reason" which could mean that the proposed schemes would be mandatory for patentees, but not for insurers.

Also some **legal concerns** are expressed. In a comparative basis, it is pointed out that "no country in the world has felt a need for substantive law on patent litigation insurance, not even the USA, notoriously the most patent-aware and litigious society in the world". Another response suggests that the "form proposed could not be introduced without the agreement of the entire membership of the European Patent Convention⁷".

The French Intellectual Property Office (INPI) and the Danish Patent and Trade Mark Office are in favour of an optional scheme and point out alternative ways to spread the risk so as to avoid a mandatory scheme. INPI suggests involvement of patent attorneys in the promotion of a PLI, broader insurance covering patents, designs and trade marks, cover for national titles and cover for at least all the new titles of the patentee's portfolio. The Danish office proposes international cooperation and "awareness-raising" about the existence of the scheme.

⁷ Article 137(1) provides that a patent application transmitted to a National Patent Office by the European Patent Office with its certificate of grant approval: "shall not be subjected to formal requirements of national law which are different from or additional to those provided for in this Convention". Making the provision of a certificate of insurance a condition of validation, as proposed in the study, it is seen by some stakeholders as a new requirement contrary to Article 137(1).

2.3. Exemptions from the mandatory system

Some responses see the exemption of "global oriented companies" as a **discrimination**, mainly against SMEs.

It is criticized that "any patent that is deemed uninsurable will be legally tainted, even if insurance is secured subsequently via a **pool** (section 15.16). This tainting effect is a risk to which exempt companies would not be exposed, tilting the playing field against SMEs".

It is also underlined that for some global oriented companies it would be difficult⁸ to prove the grounds for exemption and it would also involve an **administrative overhead**. One response draws attention to the fact that global oriented companies would also still have to pay a contribution to the fund for uninsurable risks (section 18.2.5). Another related concern is who would be responsible for actually deciding who qualifies for exemption.

An additional question would be whether a global oriented company that might wish to obtain the proposed PLI is eligible for it.

INPI considers that expiry of a patent for failing to obtain insurance or exemption certificate is a disproportionate penalty.

2.4. Delayed technical risk assessment and right to litigate

The joint response of the insurers associations CEA and RIAD states that most European insurers oppose the proposed **delay of the technical risk assessment** as contrary to fundamental rules of the insurance business and actuarial principles. Moreover, due to the enormous liability risk, patent experts will hesitate to give an opinion on the chances of success, especially in difficult cases.

The feature that an insured plaintiff would only be covered for the **cost** of the **technical risk assessment** if he gets an assessment of its **chances of success of 51%** or better (paragraph 5.1.10) is seen as a source of legal uncertainty by many stakeholders since for them "the insured party has no guarantee that the insurance company will pay out before he embarks on the costly and critical stage of seeking a technical risk assessment. In that sense the scheme seems to be a complete lottery" and "the patentee would not know who is liable to pay until after the technical risk assessment had been completed"

Furthermore, although the study underlines that the **right to litigate** would always be preserved, the insured patentee would only be entitled to litigate **with insurance cover** if its technical risk assessment gives at least a **51% chance of success** (paragraph 14.19.2). Some stakeholders see this condition as a source of conflict of interest between insurer and insured, and wonder whether patentees' premiums would be subsequently increased.

⁸ It is suggested by one stakeholder that a clear exemption criteria for "global oriented companies" would be "that the patent owner has sought patent protection for the same invention in a certain number of countries outside Europe [...], for example, by filing a PCT application".

The "51% threshold" is also considered too high by some stakeholders who comment that "the proposed system would only apply to a very limited number of cases that are likely to be settled anyway, without conducting an extensive court battle".

A stakeholder states that "According to the study, the patentee would have a degree of control over the conduct and outcome of any litigation covered by the insurance (paragraph 14.19). However, once the costs of the litigation exceed a predetermined level (paragraph 15.26.2) then the insurer would take over direct **control of the litigation**. As admitted by the study, in practice this would mean that virtually all insured litigations would be directly overseen by the insurer. This would be undesirable to the patentee who may wish to drive to a different conclusion to that of the insurer. Litigation management is vital to any potential litigant."

The **review of the prospects** during conduct of litigation (paragraph 14.27) by the insurer is described by some stakeholders as "the insurance walking away in the middle of the battle".

2.5. Statistics and methodology followed by the consultants

Some concerns are raised regarding the "validity of the [used] figures on both litigation costs and damages". The CEA and RIAD joint response suggests that the "data and figures on which the mandatory scheme together with the calculation of premiums are supposed to be funded do not meet actuarial standards and principles and are neither accurate nor reliable".

One response considers that most of the consulted stakeholders are British, another response points out that banks and private equity funds should have been consulted as well.

The INPI proposes a European initiative aiming at collecting reliable and harmonised statistics for all EU-Member States, with segmentation between SMEs and big industry.

Some replies suggest that a unitary European/Community jurisdiction, and especially a Community patent, would make it easier to obtain reliable statistics and hence to set up a patent litigation insurance.

2.6. Other comments

Some stakeholders disagree with what they call the "basic assumption underlying the study", namely that users generally desire insurance covering patent litigation. The INPI suggests that the lengthy court proceedings and the effectiveness of the judgments (the level of sanction toward the infringer) discourage SMEs from getting patents more than the cost of litigation.

A response argues that the current declining availability of patent litigation insurance reflects the low demand of this product and that insurers seem not to want to provide them. The European Association of Craft, Small and Medium-sized Enterprises (UEAPME) believes that very few insurers offer this kind of insurance schemes as the volume of request is weak and, in general, the product seems to be inappropriate to the needs and means of SMEs.

Some concerns are raised in relation to the feasibility of the proposed **cover for defendant**, which is only available for patentees. The study proposes a scheme which only protects

products and processes covered by the defendant's patents (paragraph 14.15). For some stakeholders: "products and processes commercialised by a company do not always match the scope of patent protection, and sometimes the defendant company may not have any relevant patent protection. Therefore, the study appears to be inappropriately linking patentability with patent infringement".

Moreover, a response suggests that if the insurance policy of a particular patent means that it provides for insurance cover to the patentee's entire line of products, the designed schemes could induce filings for patents simply to give insurance protection to the whole line of unpatented products of the patentee.

The **exclusion of cover for opposition proceedings** before the European Patent Office is found controversial. A stakeholder comments that, since an opposition is a known prospect of litigation and insurance would not be provided for patents under opposition proceedings, "potential infringers may deliberately oppose patents knowing that this will exclude those patents from insurance cover".

The suggested higher cost for high risk/cost patents (mainly IT and pharmaceutical fields in paragraphs 22.1.5 and 22.2) is rejected by stakeholders in these fields. It is suggested that such a diversification of costs could be contrary to Article 27 of TRIPS which requires that patent rights shall be enjoyable without **discrimination as to the field of technology**.

Some concerns are raised regarding the geographical scope of the proposed schemes. For some companies the real problem is the infringement of patents in **Asia**, not in Europe.

The Danish Patent and Trademark Office and INPI consider that **national patents** should be part of any European/Community patent litigation insurance system.

Some stakeholders highlight the need of survey on **alternative resolution** system for patent disputes like ADR, arbitration, incontestability, etc.