

2012-1548, -1549

**United States Court of Appeals
for the Federal Circuit**

APPLE INC. and
NEXT SOFTWARE, INC. (formerly known as NeXT Computer, Inc.),
Plaintiffs-Appellants,

v.

MOTOROLA, INC. (now known as Motorola Solutions, Inc.)
and MOTOROLA MOBILITY, INC.,
Defendants-Cross Appellants.

*Appeals from the United States District Court for the Northern District of
Illinois in case no. 11-CV-8540, Judge Richard A. Posner.*

(CORRECTED)

**BRIEF OF AMICI CURIAE ALTERA CORPORATION, CISCO SYSTEMS,
INC., CME GROUP, INC., GARMIN INTERNATIONAL, INC., HEWLETT-
PACKARD COMPANY, LOGITECH INC., NEST LABS, INC., NETGEAR,
INC., NEWEGG, INC., RACKSPACE HOSTING, INC., SAFEWAY INC.,
SAS INSTITUTE INC., SYMANTEC CORPORATION, WAL-MART
STORES, INC., AND XILINX, INC. REGARDING STANDARDS ON
DAMAGES IN SUPPORT OF NEITHER PARTY**

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December 4, 2012

CERTIFICATE OF INTEREST

Pursuant to Circuit Rules 21(a)(2) and 47.4(a)(1), counsel for the amicus curiae certify the following:

1. The full name of every party represented by me is:

Logitech Inc.

2. The name of the real party in interest (if the party named in the caption is not the real party in interest) represented by me is:

n/a

3. All parent corporations and any publicly held companies that own 10 percent or more of the stock of the party represented by me are:

Logitech Inc. is a wholly-owned subsidiary of Logitech International S.A. No public company owns more than 10% of the stock of Logitech International S.A.

4. The names of all law firms and the partners or associates that appeared for the party now represented by me in the trial court or agency or are expected to appear in this court are:

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Dated: December 4, 2012

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Pursuant to Circuit Rules 21(a)(2) and 47.4(a)(1), counsel for the amicus curiae certify the following:

1. The full name of every party represented by me is:

Nest Labs, Inc.

2. The name of the real party in interest (if the party named in the caption is not the real party in interest) represented by me is:

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3. All parent corporations and any publicly held companies that own 10 percent or more of the stock of the party represented by me are:

None, except as follows:

A venture investment arm of Google, Inc. owns more than 10% of Nest Labs, Inc.

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CERTIFICATE OF INTEREST

Pursuant to Circuit Rules 21(a)(2) and 47.4(a)(1), counsel for the amicus curiae certify the following:

1. The full name of every party represented by me is:

Altera Corporation; CME Group, Inc.; Cisco Systems, Inc.; Garmin International, Inc.; Hewlett Packard Company; Netgear, Inc.; Newegg Inc.; Rackspace Hosting, Inc.; SAS Institute Inc.; Safeway Inc.; Symantec Corporation; Xilinx, Inc.; and Wal-Mart Stores, Inc.

2. The name of the real party in interest (if the party named in the caption is not the real party in interest) represented by me is:

n/a

3. All parent corporations and any publicly held companies that own 10 percent or more of the stock of the party represented by me are:

None, except as follows:

Garmin International, Inc. is a wholly-owned subsidiary of Garmin Ltd.
FMR, LLC owns more than 10% of Netgear, Inc.'s stock.

4. The names of all law firms and the partners or associates that appeared for the party now represented by me in the trial court or agency or are expected to appear in this court are:

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Dated: December 4, 2012

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INTERESTS OF *AMICI CURIAE*

Amici curiae span a broad range of industries—from grocers and retailers to leading high-technology, software, and financial services companies. Each of *amici* has faced or is facing patent infringement actions in which the patent owner seeks damages far in excess of the value of the patented invention. *Amici* file this brief with the consent of all parties to this appeal.

For purposes of Rule 29 of the Federal Rules of Appellate Procedure, no party's counsel played any role in authoring this brief, no party or party's counsel contributed money that was intended to fund preparation or submission of the brief, and no person other than the *amici curiae*, their members, or their counsel, contributed money that was intended to fund preparation or submission of this brief.¹

INTRODUCTION

A consistent and economically rational framework for calculating patent damages—one that rewards innovation based on its contributed value, but not based on attributes unrelated to that contributed value—is a necessary component of a modern and effective patent system. Yet current damages methodologies frequently lead to unreliable, uncertain, and speculative outcomes. This

¹ One *amici*, Nest Labs, Inc., is owned, in part, by a venture investment arm of Google, Inc. Google, Inc. is the parent company of one of the Defendants-Appellants, Motorola Mobility, Inc. Neither Google, Inc. nor Motorola Mobility, Inc. took any part in drafting this brief.

unpredictability, and the excessive damages that often result from use of these methodologies, allocate resources away from innovation and implementation of new technologies and create obstacles to the negotiation of licenses and settlement of litigations.² This problem has become acute because the products and processes used, developed, or sold by *amici* and other leading companies have evolved, often encompassing thousands of inventions in a single product or process.³

This Court has grappled with these issues in recent years and has begun to demand that patentees utilize rigorous, economically-sound methodologies in determining appropriate damages in patent cases. *See, e.g., Lucent Techs., Inc. v. Gateway, Inc.*, 580 F.3d 1301 (Fed. Cir. 2009); *ResQNet.com v. Lansa, Inc.*, 594 F.3d 860 (Fed. Cir. 2010); *Uniloc USA, Inc. v. Microsoft Corp.*, 632 F.3d 1292 (Fed. Cir. 2011); *LaserDynamics, Inc. v. Quanta Computer, Inc.*, 694 F.3d 51 (Fed. Cir. 2012). This case presents an opportunity for this Court further to clarify that reasonable royalty patent damages should measure the value of the patented invention at the time of design; to set aside the traditional *Georgia-Pacific* factors

² *See generally, e.g.,* J. Bessen and M. Meurer, *The Direct Costs from NPE Disputes*, Boston Univ. School of Law Working Paper No. 12-34 (June 28, 2012), available at http://www.bu.edu/law/faculty/scholarship/workingpapers/documents/BessenJ_MeurerM062512rev062812.pdf.

³ The terminology “product or process” as used in this brief is intended broadly to cover products, components, apparatus, methods, processes, systems and anything else amenable to patenting. *Amici* believe that the principles articulated herein apply regardless of the type of patent claim asserted and regardless of what is accused of infringement.

and the entire market value rule as unreliable methodologies for calculating damages in cases involving complex products or processes; and expressly to replace them with the more rigorous methodologies the Court has begun to articulate for determining damages in patent cases. Furthermore, this Court should encourage district courts to play an early and proactive role—just as the district court did here—to ensure the appropriate development and presentation of parties’ damages theories.

ARGUMENT

I. Generalized Methodologies Currently Used To Calculate Reasonable Royalty Damages Lead To Inconsistent And Unreliable Results Because They Are Not Sufficiently Tied To The Patented Invention.

As this Court has recognized, the calculation of a reasonable royalty is “often a difficult judicial chore,” but at all times “the damages inquiry must concentrate on compensation for the economic harm caused by infringement of the claimed invention.” *ResQNet.com*, 594 F.3d at 869. *Amici* respectfully submit that two of the approaches traditionally utilized by litigants to calculate a reasonable royalty—use of the *Georgia-Pacific* factors and the entire market value rule—have become increasingly divorced from an economically sound framework tied to the value of the patented invention and have limited utility in the context of today’s complex products and processes. *Amici* submit that this Court should formally set aside those traditional approaches in favor of a more rigorous economic analysis

that focuses upon the value of the patented invention, rather than the revenue associated with the accused product or process.

A. The Fifteen *Georgia-Pacific* Factors Fail To Provide Meaningful Guidance And Are Not A Reliable Methodology For Calculating Reasonable Royalty Damages.

This Court regularly has emphasized that a damages inquiry must be carefully tied to the value of the patented invention. More than forty years have passed since the Southern District of New York’s identification of fifteen non-exclusive factors that may be relevant in determining a reasonable royalty. *Georgia-Pacific Corp. v. U.S. Plywood Corp.*, 318 F. Supp. 1116 (S.D.N.Y. 1970). But the list of fifteen factors provides little, if any, guidance to juries (or courts) on how they are to be applied. As the District Court below noted:

This [the *Georgia-Pacific* factors] is a formidable list. The “some” in the second sentence is particularly rich—how many additional factors may be lurking somewhere? And could a judge or a jury really balance 15 or more factors and come up with anything resembling an objective assessment?

Apple, Inc. v. Motorola, Inc., No. 1:11-cv-08540, 2012 WL 2376664, at *9 (N.D. Ill. June 22, 2012); *see also ResQNet.com*, 594 F.3d at 869 (describing the list of *Georgia-Pacific* factors as “unprioritized and often overlapping” and that application of the factors “seem[s] often to involve more the talents of a conjurer than those of a judge”). That concern is particularly acute in the context of modern information technology and consumer electronics products, which can encompass

hundreds or even thousands of inventions. Juries tasked with considering a complete (or even partial) list of the *Georgia-Pacific* factors are given little guidance on their application, permitting patentees to introduce evidence and arguments untethered to any economically sound analysis of the value of the patented invention—in effect, “provid[ing] a grab bag for use by parties seeking to establish whatever reasonable royalty serves their purposes.”⁴

Amici respectfully submit that it is time for this Court definitively to state that use of the *Georgia-Pacific* factors is not an appropriate damages methodology and generally does not result in an economically sound assessment of the value of the patented invention. Rather, this Court should clarify that the fifteen *Georgia-Pacific* factors represent a non-exhaustive list of potential evidence that may be—but is not necessarily—relevant to a damages analysis in any given case. Indeed, a proper reasonable royalty analysis need not take into consideration *any* of the fifteen *Georgia-Pacific* factors. *Whitserve, LLC v. Computer Packages, Inc.*, 694 F.3d 10, 31 (Fed. Cir. 2012).

Moreover, this Court should emphasize that district courts must not treat evidence as admissible simply because it corresponds to one of the *Georgia-*

⁴ FEDERAL TRADE COMMISSION, *The Evolving IP Marketplace: Aligning Patent Notice And Remedies With Competition* at 184 (March 2011) (hereinafter “FTC REPORT”), available at <http://www.ftc.gov/os/2011/03/110307patentreport.pdf>.

Pacific categories.⁵ District courts instead must ensure that the evidence is sufficiently tied to the value of the patented invention **and** the specific facts of the case, and that it is also a reliable source of information that can aid the factfinder in the determination of a reasonable royalty. *See, e.g., Whitserve*, 694 F.3d at 31 (explaining that superficial recitation of the *Georgia-Pacific* factors, followed by conclusory remarks, cannot support the jury's verdict).

B. Use Of The “Entire Market Value Rule” Should Presumptively Be Abolished.

Reasonable royalty awards often turn on the identification of an appropriate revenue base. But the determination of a proper revenue base is particularly difficult—and accordingly becomes ripe for abuse—when the inventive aspect of a patented technology is only one feature of an accused product or process that may include tens or even thousands of features. Although this Court recently has clarified that the entire revenue associated with an accused product rarely should be used,⁶ *amici* respectfully submit that the entire market value rule has become an unwarranted and unnecessary complication in patent damages analysis, and it should presumptively be abolished.

⁵ As the Federal Trade Commission has explained, blanket admission of all evidence that may correspond to any of the *Georgia-Pacific* factors leads to jury confusion, unreliable results, and substantial difficulty in appellate review. FTC REPORT at 184.

⁶ *See, e.g., LaserDynamics*, 694 F.3d at 66-68; *see also Rite-Hite Corp. v. Kelley Co., Inc.*, 56 F.3d 1538, 1549, 1551 (Fed Cir. 1995); *Lucent Techs.*, 580 F.3d at 1336-38.

First, as this Court repeatedly has recognized, the overall revenue associated with a complex product or process has no demonstrated correlation to the value of the patented invention when that invention covers only a small part of that product or process. *See, e.g., LaserDynamics*, 694 F.3d at 68. In reality, customer demand for complex products and processes—such as smartphones, computers, and the software and methods that run on them or are run by them—is driven by myriad considerations.

In this context, allowing patentees to argue that any single feature drives demand can only lead to jury confusion and impermissibly skewed damages awards. *See Uniloc*, 632 F.3d at 1320 (explaining that evidence presented as part of an entire market value theory “cannot help but skew the damages horizon for the jury, regardless of the contribution of the patented component, to th[e] revenue [generated by the overall product]”); *LaserDynamics*, 694 F.3d at 67, 68 (holding that “calculating a royalty on the entire product carries a **considerable risk** that the patentee will be improperly compensated for non-infringing components of that product” and “only serve[s] to make a patentee’s proffered damages amount appear modest by comparison, and to artificially inflate the jury’s damages calculation beyond that which is ‘adequate to compensate for the infringement’”) (citing 35 U.S.C. § 284) (emphasis added). Reference to the overall revenue associated with

a complex product or process therefore should be eliminated, as it is typically more prejudicial than probative of the value of the patented invention.⁷

Moreover, a separate rule for the use of the entire market value is wholly unnecessary if appropriate damages methodologies (as discussed further below) are properly utilized. For instance, the use of an overall product's or process's profit to determine a reasonable royalty may be appropriate if, after apportionment, all or most of the profit of the accused product or process is attributable to the patented invention—which may be the case for a single-component product or process, such as a pharmaceutical. But in this circumstance, there is no need to ask the separate question of whether the patented feature drove demand for the accused product or process. On the other hand, if applying the appropriate damages methodology results in something less than the entire profit being attributable to the patented invention, inquiry into the purported “basis for demand” will have been wasteful, confusing, and potentially prejudicial to the accused infringer. Indeed, the ongoing difficulties in applying the entire market value rule have led to jury confusion and inconsistent results in the district courts and justify its elimination. *See, e.g., Mirror Worlds, LLC v. Apple, Inc.*, 784 F. Supp.2d 703, 724-27 (E.D. Tex. 2011)

⁷ *See also* FTC REPORT at 211 (“Courts should eliminate the entire market value rule and the question of whether the patented feature was the ‘basis for customer demand’ from the determination of the appropriate base in a reasonable royalty damages calculation. It is irrelevant and it risks injecting significant confusion that threatens to produce inaccurate awards.”).

(district court vacating jury's more than six hundred million dollar damages award in part because of the patentee's improper use of the entire market value rule), *aff'd on other grounds*, 692 F.3d 1351 (Fed. Cir. 2012); *see also, e.g., Lucent Techs.*, 580 F.3d at 1337 (appellate court vacating damages award due to "lack of evidence demonstrating the patented method of the [asserted patent] as the basis—or even a substantial basis—of the consumer demand for [the accused product]").

II. This Court Should Affirm That Reasonable Royalty Damages Must Focus On The Value Of The Patented Invention At The Time Of The Design To A Reasonable Licensor And Licensee.

The crucial issue in calculating a reasonable royalty begins with determining the value of the patented invention. *Garretson v. Clark*, 111 U.S. 120, 121 (1884) ("The patentee . . . must in every case give evidence tending to separate or apportion the defendant's profits and the patentee's damages between the patented feature and the unpatented features."). As technology has evolved—and products and processes have become increasingly complex—many litigants and courts have lost sight of this basic principle that a reasonable royalty analysis must be based on the value of the patented invention, not the revenue associated with the accused product or process. Patentees bear the burden of establishing the value of the patented invention.⁸ *See, e.g., ResQNet.com*, 594 F.3d at 872; *IP Innovations*

⁸ Moreover, a patentee cannot avoid the fundamental task of determining the value of the patented invention by using a small enough royalty rate. *See Uniloc*, 632 F.3d at 1320.

L.L.C. v. Red Hat, Inc., 705 F. Supp. 2d 687, 690 (E.D. Tex. 2010) (Rader, J., sitting by designation) (rejecting plaintiff’s contention that it had “no way to value the accused feature separately” and reiterating that the burden is on the patentee).

Amici respectfully submit that this Court should affirm certain guidelines for conducting a sound and reasonable royalty analysis. First, the value of the patented invention must be established by the patentee using a rigorous methodology that meets acceptable accounting standards and is based on reliable, admissible evidence. *See ResQNet.com*, 594 F.3d at 868 (vacating damages award because it “relied on speculative and unreliable evidence divorced from proof of economic harm linked to the claimed invention.”).

Second, that value should be measured, and the hypothetical negotiation must be focused, on the *time of design*—not necessarily the time of first infringement by the accused infringer. The hypothetical negotiation paradigm is intended to prevent patent damages from reflecting the value of any sunk investment, or the “lock in” difficulty of changing designs after adoption.⁹ In some circumstances, this will lead to a hypothetical negotiation right before first infringement by the accused infringer. In other circumstances, the date of design

⁹ *See* FTC REPORT at 190 (“A reasonable royalty damages award that is based on high switching costs, rather than the *ex ante* value of the patented technology compared to alternatives, overcompensates the patentee. It improperly reflects the economic value of investments by the infringer rather just than the economic value of the invention.”); *see also, e.g.*, Thomas F. Cotter, *Patent Holdup, Patent Remedies, and Antitrust Responses*, 34 J. CORP. L. 1151 (2008-2009).

might be the date just before a feature or function was adopted into a standard, or the date just before a supplier to the accused infringer adopted a feature or function into its product or process, which later was incorporated into the accused product or process.

Third, a reasonable royalty analysis must address the fair distribution of the value of the patented invention to a licensor and licensee if the licensor and licensee were both willing and reasonable in their negotiations. In other words, a reasonable royalty analysis must address how much of the value of the patented invention would be allocated to the licensor, and how much would be retained by the licensee, if the licensor and licensee were both willing and reasonable in their negotiations. *See, e.g., Lucent Techs.*, 580 F.3d at 1337.¹⁰

III. To Provide Further Guidance To District Courts, This Court Should Establish Three Methodologies For Determining The Value Of The Patented Invention.

Amici submit that there are three primary methodologies to value a patented invention that this Court should adopt in lieu of the traditional *Georgia-Pacific* and entire market value approaches: (1) determination of the incremental value of the

¹⁰ *Amici* submit that an appropriate jury instruction on reasonable royalty damages might simply state that reasonable royalties are intended to compensate for the value of the patented invention at the time of design to a willing and reasonable licensor and a willing and reasonable licensee. Such simplification could reduce jury confusion and lead to more reliable damages awards, particularly in comparison to instructions that merely list the fifteen *Georgia-Pacific* factors without guidance or elaboration.

patented invention over the next best alternative; (2) determination of the patented invention's value through apportionment; and (3) consideration of an established royalty for the patented invention to determine its economic value.¹¹ Regardless of which of these methodologies is applicable in a particular matter, the reasonable royalty still must be based on reliable and admissible evidence and on accepted accounting standards to ensure that a reasonable royalty award is tied to the specific facts of the case and accurately reflects what the parties would have agreed to if they had willingly entered into negotiations at the time of design.

A. Where It Can Be Determined, Reasonable Royalty Damages Should Be Capped At The Incremental Value Of The Patented Invention Over The Next Best Alternative.

Courts have long considered the availability of non-infringing alternatives relevant to the determination of damages in patent cases.¹² Economic theory supports such a consideration; indeed, it would be irrational for an accused infringer to pay more for a license to a patent than he would pay to implement a technically equivalent—but non-infringing—alternative to the patented

¹¹ *Amici* do not mean to suggest that all three of these methodologies will apply in every case. Instead, *amici* submit that at least one of these methodologies can be applied in almost every circumstance. Of course, which of the methodologies to apply in a particular matter will depend on the type and substance of the admissible evidence.

¹² See, e.g., *Panduit Corp. v. Stahl Bros. Fibre Works, Inc.*, 575 F.2d 1152, 1159 (6th Cir. 1978); *Hughes Tool Co. v. G.W. Murphy Indus., Inc.*, 491 F.2d 923, 931 (5th Cir. 1973); *Smithkline Diagnostics, Inc. v. Helena Labs. Corp.*, 12 U.S.P.Q.2d 1375, 1379 (E.D. Tex. 1989), *aff'd*, 926 F.2d 1161 (Fed. Cir. 1991).

technology. As such, *amici* respectfully submit that reasonable royalty damages should be capped at the “incremental value” of the patented invention over the best non-infringing alternative.

This Court has endorsed a similar approach in the context of a lost profits damages analysis. For instance, in *Grain Processing*, this Court recognized that “a fair and accurate reconstruction of the ‘but for’ market also must take into account, where relevant, alternative actions the infringer foreseeably would have undertaken had he not infringed.” *Grain Processing Corp. v. Am. Maize-Prods. Co.*, 185 F.3d 1341, 1350-51 (Fed. Cir. 1999).¹³ The same economic considerations warrant application of *Grain Processing* to the reasonable royalty context. *See, e.g., id.* at 1347 (holding that the difference in production costs between infringing and non-infringing products “effectively capped the reasonable royalty award”); *Riles v. Shell Exploration & Prod. Co.*, 298 F.3d 1302, 1312 (Fed. Cir. 2002) (“The economic relationship between the patented method and non-infringing alternative methods, of necessity, would limit the hypothetical negotiation.”).¹⁴ Numerous

¹³ *See also id.* at 1351 (“Without the infringing product, a rational would-be infringer is likely to offer an acceptable noninfringing alternative, if available, to compete with the patent owner rather than leave the market altogether. The competitor in the ‘but for’ marketplace is hardly likely to surrender its complete market share when faced with a patent, if it can compete in some other lawful manner.”).

¹⁴ *See also, e.g., Zygo Corp. v. Wyko Corp.*, 79 F.3d 1563, 1571-72 (Fed. Cir. 1996) (vacating and remanding the district court’s damages determination where both lost profits and reasonable royalty failed to take into account non-infringing

commentators also have urged that the practical realities favor the application of the “incremental value” cap to the reasonable royalty context. *See, e.g.*, FTC REPORT at 189 (“Courts should recognize that when it can be determined, the incremental value of the patented invention over the next-best alternative establishes the maximum amount that a willing licensee would pay in a hypothetical negotiation. Courts should not award reasonable royalty damages higher than this amount.”).¹⁵

This Court should apply the reasoning of *Grain Processing* to the reasonable royalty context and limit any reasonable royalty award to the aggregate cost associated with implementing a technically and commercially feasible non-infringing alternative in place of the accused instrumentality.¹⁶ Such a rule would

alternatives that would have given the alleged infringer a “stronger position to negotiate for a lower royalty rate); *Apple, Inc. v. Motorola, Inc.*, No. 1:11-cv-08540, 2012 WL 1959560, at *7 (N.D. Ill. May 22, 2012) (explaining that the lowest cost of avoiding patent infringement, either by “invent-around software development or in loss of consumer goodwill (resulting in a loss of sales revenue),” would be the “ceiling on [a potential infringer’s] willingness to pay for a patent license.”).

¹⁵ *See also, e.g.*, Joan L. Eads, Commentary, *Does Grain Processing Apply in a Reasonable Royalty Damage Analysis?*, 10:26 ANDREWS INTELL. PROP. LITIG. REP. 13 (April 13, 2004); Liane M. Peterson, *Grain Processing and Crystal Semiconductor: Use of Economic Methods in Damage Calculations Will Accurately Compensate For Patent Infringement*, 13 FED. CIRCUIT B.J. 41 (2003); John W. Schlicher, *Measuring Patent Damages by the Market Value of Inventions – The Grain Processing, Rite-Hite, and Aro Rules*, 82 J. PAT. & TRADEMARK OFF. SOC’Y 503 (2000).

¹⁶ *Amici* recognize that this Court previously has rejected the notion that reasonable royalty damages should be capped at the cost of implementing a non-infringing

be consistent with economic realities and, accordingly, the prospective nature of the hypothetical negotiation: to the prospective licensee, the marginal value of the patented invention is the difference between the values of the inventive improvement and available alternatives.

B. Proper Apportionment May Be Used As A Basis To Approximate The Value Of The Patented Invention.

Many factors contribute to the revenue and market success associated with a product or process. Those factors include, among other things, features covered by other patents, non-patented features and components, reliability, brand reputation, marketing, sales efforts, and manufacturing quality and capability. This Court should reiterate that, if the revenue associated with the accused product or process is to be used to approximate the value of the patented invention, the starting point for any reasonable royalty analysis must involve “apportionment”—a determination as to what value the *patented invention* actually contributes to the overall accused product or process.¹⁷ In other words, if revenue associated with

alternative in place of the accused instrumentality. *Mars, Inc. v. Coin Acceptors, Inc.*, 527 F.3d 1359, 1373 (Fed. Cir. 2008) (citing *Monsanto Co. v. Ralph*, 382 F.3d 1374, 1383 (Fed. Cir. 2004)). But neither *Mars* nor *Monsanto* considered reasonable royalty awards in the context of non-competing entities. *Amici* respectfully submit that, at the very least, where competitive considerations are absent, the incremental value of the patented invention over the next-best alternative establishes the maximum amount a willing licensee would pay in a hypothetical negotiation.

¹⁷ See, e.g., *ResQNet.com*, 594 F.3d at 869 (“[T]he trial court must carefully tie proof of damages to the claimed invention’s footprint in the market place.”).

the accused product or process is used as the basis to determine the value of the patented invention, all other factors that contribute to that revenue must be apportioned out of that revenue so that what remains approximates the value of the patented invention.

For example, in some circumstances, an appropriate starting point for an apportionment analysis may be the incremental difference in value between a product or process containing or utilizing the patented invention and a similar product or process that does not include or utilize the patented invention. In other circumstances, an appropriate starting point may be the “smallest saleable unit” containing or utilizing the patented invention.¹⁸ The smallest saleable unit might be something sold by the accused infringer or it might be the value of a component containing the allegedly inventive functionality that is sold to the accused infringer for incorporation into the accused product or process.

¹⁸ See, e.g., *Cornell Univ. v. Hewlett-Packard Co.*, 609 F. Supp. 2d 279, 287-88 (N.D.N.Y. 2009) (Rader, J., sitting by designation) (explaining that “counsel would have wisely abandoned a royalty base claim encompassing a product with significant non-infringing components” and that “[t]he logical and readily available alternative was the smallest salable infringing unit with close relation to the claimed invention”); *LaserDynamics*, 694 F.3d at 67 (“Where small elements of multi-component products are accused of infringement, calculating a royalty on the entire product carries a considerable risk that the patentee will be improperly compensated for non-infringing components of that product. Thus, it is generally required that royalties be based not on the entire product, but instead on the smallest salable patent-practicing unit.”) (internal quotations omitted).

Regardless of the starting point used, the objective of the analysis should be to apportion the royalty base as closely as possible to reflect the portion of the value attributable to the patented invention—and to exclude all other aspects of the accused product or process that contribute to its revenue.¹⁹ This generally will require apportionment beyond whatever starting point is used. For example, if the smallest saleable unit is used as the starting point—but that unit also contains non-patented components, features, or other value beyond that attributable to the patented invention—then the value attributable to those additional factors must be further apportioned out of the royalty base. Proper apportionment should ensure that a patentee receives fair value for the patented invention while preventing a reasonable royalty calculation from including, among other things, non-patented features or processes, or implementation and manufacturing costs that factor into a

¹⁹ As discussed further below in Section IV, this Court should insist that district courts carefully review damages theories—and ensure that proper apportionment measures have been utilized—*before trial*, to minimize the very real risk of “skew[ing] the damages horizon for the jury.” *Uniloc*, 632 F.3d at 1320. Evidence of the total revenue associated with the accused product or process should not be presented to the jury; rather only the properly apportioned amount that approximates the value of the patented invention should be presented. *LaserDynamics*, 694 F.3d at 68 (“Admission of . . . overall revenues, which have no demonstrated correlation to the value of the patented feature alone, only serve to make a patentee’s proffered damages amount appear modest by comparison, and to artificially inflate the jury’s damages calculation beyond that which is adequate to compensate for the infringement.” (internal quotations omitted)).

product's sales price and revenue but are wholly unrelated to the patented invention.²⁰

Finally, in assessing revenue base apportionment, this Court should emphasize that the focus must remain on the *inventive* aspect of the claims—not necessarily the device recited in the asserted claims. The fact that patent claims may be expressed in different formats, and of different scope, should not allow the patent owner to avoid apportionment and point to the revenue associated with an overall accused product or process as the proper revenue base. As the Federal Trade Commission explained in its March 2011 Report:

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

²⁰ Associated revenue in a reasonable royalty calculation should factor out any material costs, labor costs, overhead, or costs of inventory, e.g., it should factor out the cost-of-goods sold or services provided. These types of costs relate to creating a usable product or process for the marketplace, not to the value of the patented invention. *See, e.g., ResQNet.com*, 594 F.3d at 869 (“Any evidence unrelated to the claimed invention does not support compensation for infringement but punishes beyond the reach of the statute.”); *Whitserve*, 694 F.3d at 33 (“35 U.S.C. § 284 requires that patentees be compensated for the infringement, not that their entry into the industry be fully financed.”).

*the vagaries of claim drafting, particularly because the way claims are drafted [is] . . . so manipulable.*²¹

C. In Certain Circumstances, Evidence Of An Established Royalty May Be Considered In The Determination Of The Value of the Patented Invention.

Evidence of an established royalty may be relevant to the reasonable royalty analysis if it can be shown that the established royalty reflects the economic value of the patented technology.²² But—as this Court has noted—that is not always the case. For instance, licenses may reflect the value of litigation avoidance, not the value of the claimed invention.²³ Similarly, licenses entered into after an accusation of infringement may reflect the patent’s hold-up value—including the threat of an injunction—and thus be of little use in determining a reasonable

²¹ FTC REPORT at 211 (emphasis added, internal quotations omitted).

²² In the same vein, if the patent has been purchased rather than internally developed, the price paid for the patent generally is relevant evidence of the maximum value of the patented invention. It would be economically irrational for a licensee to pay more to license a patent than it would have cost to purchase the patent outright.

²³ See, e.g., *LaserDynamics*, 694 F.3d at 77 (noting that “[t]he propriety of using prior settlement agreements to prove the amount of a reasonable royalty is questionable” and that the “notion that license fees that are tainted by the coercive environment of patent litigation are unsuitable to prove a reasonable royalty is a logical extension of *Georgia-Pacific*, the premise of which assumes a voluntary agreement will be reached between a willing licensor and a willing licensee”); *ResQNet.com*, 594 F.3d at 872 (“[L]icense fees negotiated in the face of a threat of high litigation costs may be strongly influenced by a desire to avoid full litigation.”) (citing *Hanson v. Alpine Valley Ski Area, Inc.*, 718 F.2d 1075, 1078-79 (Fed. Cir. 1983)).

royalty.²⁴ Further, a license's terms may be artificially inflated for purposes of use in litigation, such as by applying a nominally high rate on an extremely narrowly-defined set of products or by having a high rate but capping the amount paid, and therefore bear little relation to the value of the patented invention (or even the amount actually paid by the licensor). Accordingly, this Court should clarify that, in limited circumstances, evidence of an established royalty for the patented invention (outside the context of litigation) may inform an assessment of the *economic value of a patented invention* and, accordingly, the determination of a reasonable royalty. Conversely, evidence concerning royalties or royalty rates with no link to the patented invention, which are of questionable merit in determining the value of the patented invention, or which have indicia of unreliability for other reasons including, in almost every circumstance, those that are in settlement of litigation, must be excluded. *See ResQNet.com*, 594 F.3d at 872.

²⁴ This is particularly true of licenses agreed to before the Supreme Court's 2006 *eBay* decision. *See eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388 (2006). Pre-2006 licenses—particularly those granted by non-practicing entities—may be inflated by the fear of an injunction that the Supreme Court has since determined should be unavailable. Indeed, even post-*eBay*, this “injunction premium” may be present in existing licenses.

IV. This Court Should Reaffirm District Courts' Gatekeeping Function To Ensure That Only Scientifically Reliable Damages Evidence And Methodologies Are Presented To The Jury.

As a recent handbook for federal district court judges explained, “[n]o issue in a patent trial cries out for strict application of [a district court’s] gatekeeping tools . . . more than damages.”²⁵ Regardless of this Court’s ultimate determination in this case, *amici* urge this Court once again to remind the district courts that they must exercise their gatekeeping role—as the district court did here—to prevent unreliable damages methodologies and evidence from reaching the jury.

To be most valuable, such gatekeeping should be done at an early stage. In most circumstances, expert reports concerning damages issues are not disclosed until the end of discovery—often near (or even after) summary judgment deadlines. Furthermore, disputes regarding damages issues are raised in at least three different contexts: summary judgment motions, *Daubert* challenges, and motions *in limine*. Such variability causes significant inefficiencies, as a party might have to file—and the court consider—three separate motions at different times challenging different but often intertwined aspects of an expert’s testimony and conclusions. While *amici* believe that the procedures for damages challenges should be determined by each district court, *amici* submit that this Court should

²⁵ Federal Judicial Center, *Compensatory Damages Issues in Patent Infringement Cases: A Pocket Guide for Federal District Court Judges* at 28 (2011), available at [http://www.fjc.gov/public/pdf.nsf/lookup/damagespatent.pdf/\\$file/damagespatent.pdf](http://www.fjc.gov/public/pdf.nsf/lookup/damagespatent.pdf/$file/damagespatent.pdf).

strongly encourage district courts to consider reliability and admissibility of damages related methodologies, theories, evidence, and expert opinions at the same time and early, just as the district court did here. Appropriate gatekeeping reduces jury confusion and excessive results by ensuring that unreliable conclusions, evidence, and methodologies are not presented to the jury. It also streamlines the damages case presented at trial.

Amici also urge this Court to clarify that evidence is not reliable or admissible merely because it happens to correspond to one of the *Georgia-Pacific* factors. Nor can mere recitation of the factors or other “superficial testimony” be permitted. *Whitserve*, 694 F.3d at 32. Further, although *amici* endorse the three methodologies described above *in the appropriate circumstances*, it is the responsibility of the district court actively to ensure that the methodology used in a particular case is based on sound economic and factual predicates and is carefully tied to the value of the patented invention and the facts of the specific case. *LaserDynamics*, 694 F.3d at 67; *see also Apple*, 2012 WL 1959560, at *7-*11 (recognizing that lowest cost of avoiding patent infringement would be the “ceiling on [a potential infringer’s] willingness to pay for a patent license”, but ultimately rejecting expert testimony of both parties concerning that theory as unreliable under the circumstances of this case). In addition, district courts must ensure that all admitted evidence be reliable and not be more prejudicial than probative. *See*,

e.g., id. at 68 (“Admission of . . . overall revenues, which have no demonstrated correlation to the value of the patented feature alone, only serve to make a patentee’s proffered damages amount appear modest by comparison, and to artificially inflate the jury’s damages calculation beyond that which is adequate to compensate for the infringement.” (internal quotations omitted)).

CONCLUSION

Amici respectfully urge this Court to provide further clarification and guidance, as set forth in this brief, concerning the proper methodologies and procedures for calculating reasonable royalty damages. Additional clarity will benefit district courts and a wide variety of business and consumer interests, appropriately and fairly reward innovation, and foster implementation of new technologies.

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Respectfully submitted,

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**United States Court of Appeals
for the Federal Circuit**

APPLE INC. v MOTOROLA, INC., 2012-1548, -1549

CERTIFICATE OF SERVICE

I, John C. Kruesi, Jr., being duly sworn according to law and being over the age of 18, upon my oath depose and say that:

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The brief was original filed and served via the CM/ECF system on December 4, 2102 (in the same manner listed below).

I hereby certify that on December 5, 2012, I electronically filed the foregoing (corrected) **BRIEF OF AMICI CURIAE ALTERA CORPORATION, et al.** with the Clerk of Court using the CM/ECF System, which will serve notice of such filing to any of the following counsel registered as CM/ECF users:

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December 5, 2012

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CERTIFICATE OF COMPLIANCE

In accordance with Fed. R. App. Proc. 32(a)(7)(C), the undersigned certifies that this brief complies with the type-volume limitations of Fed. R. App. Proc. 32(a)(7)(B).

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Dated: December 4, 2012

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