

Legal Commentary

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Intellectual Property Law

Patent Lawsuits in Good Faith—Enforcement of Right or Extortion

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In July 2018, several media outlets reported that the Shanghai Municipal Public Security Bureau had made a breakthrough in a case involving the alleged extortion of a pre-IPO company. The criminal suspect in the case was alleged to have threatened to influence the company's initial public offering and unlawfully demanded huge sums of money by means of patent litigation¹.

This news immediately aroused widespread social concern and discussion after it was publicized.

Since the law grants patentees the legal right to file patent infringement lawsuits, how can a patentee be prosecuted for initiating a patent infringement lawsuit that is alleged to be “extortion”? This article discusses several relevant issues.

I. Review of the Case

From March to September in 2017, Li utilized Company X, which he controlled, to initiate a patent lawsuit against Company A on the ground that Company A had infringed the patent rights of Company X; during this time, Company A was planning and preparing for its initial public offering. Company A worried that fighting the lawsuit would affect the process of its public offering, and thus signed a “patent license agreement for implementation” with Company X to reach a settlement with Li for RMB 800,000 and obtained a license that authorized all patent rights and the rights to apply for a patent held or controlled by Company X. Afterwards, Li fabricated the fact that the exclusive license of a patent under the name of Company X had earlier been given to Company Y (Company Y's legal representative is Gao who is Li's sister-in-law; and the shareholders are Li's younger brother and sister-in-law, though the actual controller

¹ The Paper News, reporter Li Jiawei, Interns Wang Yucheng, Chen Shuaiqi: “上海破获敲诈拟上市公司案：囤数百“专利”再借诉讼之名勒索”，<https://tech.sina.com.cn/roll/2018-07-22/doc-ihfqtahi3931838.shtml>, latest access time: January 5, 2019.

is Li), and Li's younger brother once again filed a patent infringement lawsuit against Company A in the name of Company Y. During the period, Li designated Gao to provide real-name reporting to the China Securities Regulatory Commission, and Company A reached a settlement with Company Y for RMB 800,000.

Company A reported the incident to the police after its successful initial public offering. Later, Li and others were investigated by the Shanghai police for alleged criminal extortion. In January 2018, Li and his younger brother were detained by the police. On August 24, 2018, the People's Procuratorate of Pudong New Area initiated a public prosecution in court. Li and his younger brother were charged criminal extortion for forcibly demanding public or private property for the purpose of illegal possession and the amount was extremely huge.

The case was tried twice on November 20 and December 12, 2018. The procurator believed that Li threatened patent infringement lawsuits, extorting four companies for more than RMB 2.163 million, and actually obtaining RMB 1.163 million, which constituted criminal extortion², and the procurator also provided as evidence recordings made by the relevant enterprises when they negotiated with Li³.

II. Analysis and Discussion of the Case

The crime of extortion provided under Article 274 of the PRC Criminal Law has been interpreted to refer to demanding public or private property from a victim by means of threat or coercion for the purpose of illegal possession. Therefore, a determination of whether criminal extortion has been committed is based on two elements: (1) whether the conduct was for the purpose of illegally possessing public or private property (that is, whether the perpetrator had the purpose to take possession of property which does not and should not belong to him or herself); and (2) whether threatening or coercive means were used.

1. Whether for the purpose of illegal possession

Did the criminal suspect in this case fulfill the element of "for the purpose of illegal possession"? In the author's opinion, after Li's first settlement with Company A, the conduct of again filing a patent infringement lawsuit against Company A and benefiting therefrom appears to be "legal" but is in fact illegal. In the first settlement, Company A obtained the licensing with authorization of all patent rights and the rights to apply for a patent held or controlled by Company X through the "patent license agreement for implementation" with Company X; that is to say, Li has already obtained the license fees for all patents and patent applications belonging to Company X under his name from Company A, and it was illegal for Li to again obtain property from Company A through other similar conduct. For example, Li fabricated an exclusive patent license agreement exclusively licensing a related patent of Company X to Company Y held by Li's younger brother, backdated the date of the agreement, and colluded with his younger brother as the exclusive licensee to use the patent to initiate a lawsuit against Company A and demand license fees. Li repeatedly charged the same company with patent

² You Bin: "利用专利进行敲诈勒索案开庭审理情况", <https://mp.weixin.qq.com/s/N9fvBDEJl6vklZuoZuor7A>, latest access time: January 9, 2019.

³ You Bin: "利用专利“敲诈勒索”拟上市公司案第二次庭审情况", <https://mp.weixin.qq.com/s/y4gON9Kf452VMKy5wfxyxQ>, latest access time: January 10, 2019.

license fees, and the patent relating to the second license fee had been included in the license agreement signed in the first settlement. Thus, it can be seen that Li's ultimate goal was not to protect the patent rights, but to illegally possess the property of others, that is, "for the purpose of illegal possession".

We note that the Shanghai police have emphasized the following points: first, the time of the lawsuit was at a critical moment for the initial public offering of the other party; second, in previous patent lawsuits, the patentee had never won in a final court trial; third, Li's companies have no corporate business, their main source of revenue relies on litigation and settlement fees, and the patents are low-tech. However, it is debatable to conclude from these three facts that the patent infringement lawsuit and patent licensing conduct involved in the case were for the purpose of illegal possession.

Firstly, a pre-IPO company should not be exempt from patent infringement litigation. If the company has committed patent infringement, it should bear the corresponding legal liability. From the patentee's perspective, under the premise of ensuring that the validity of patent rights, it is completely legitimate for the patentee to freely choose the timing of filing a lawsuit against possible infringement.

Secondly, the parties and facts of this patent lawsuit are different from those of the previous lawsuits. Although the previous patent lawsuits had not been won, it cannot be inferred that the alleged infringement in the patent lawsuits involved in this case would also not be established. Whether a patent infringement is established should be determined by the court after trial and should not be decided by the previous patent lawsuits.

Thirdly, although Li's company is a typical NPE (non-practicing entity) as it does not produce related products per se but specializes in the use of self-owned patents to sue others for license fees or compensation. The Patent Law and related laws, however, do not stipulate that the patentee has the right to file a patent infringement lawsuit against others only if implementing the patent by itself.

From another point of view, in recent years, China has continued to strengthen intellectual property rights protections and increased the amount of compensation, and thus it has become normal for enterprises to use patent litigation as a tool to support various commercial activities. The relevant administrative regulations concerning enterprise initial public offerings contain rules on the suspension or the termination of a company's IPO plans due to patent litigation, which clearly provide space for the relevant parties to choose the appropriate timing for litigation. Therefore, it is also worth considering whether the relevant administrative regulations need to be appropriately revised to reduce public investment risk and effectively protect the legitimate interests of listed companies under the current trend of strong protections and high compensation.

2. Whether threatening or coercive means are used

When determining whether the suspect used threatening or coercive means, the recording of the negotiations submitted by the procurator at the trial stage became critical evidence in support of the judgement. If Li and others did use language involving threats, coercion and intimidation, etc., criminal extortion could be further established following cross-examination. The procurator provided

an excerpt of the recorded information in court, and asserted that the content of the recording indicated Li's purpose was to use the patents to demand money, focusing on the money rather than the appeal in terms of the patent rights, and to sue during the sensitive period when the relevant company was preparing for its initial public offering. Therefore, the procurator believed that Li's language was coercive in nature⁴.

III. Lessons from the Patent Lawsuit Filing

This case has been hotly discussed in both corporate and legal circles immediately after it was publicized by the media. Many viewpoints hold that "patent trolls" should be combated. At the same time, many intellectual property practitioners, experts and scholars have called for the protection of the right of a patentee to legally exercise its patent rights, and believe that civil disputes should be cautiously identified as a crime of extortion.

It is worth noting that the principle of good faith is specifically added in the revision of the Patent Law promulgated by the Standing Committee of the National People's Congress at the beginning of 2019. Patentees are legally required to exercise their rights in good faith, thus establishing the obligation when a patentee exercises its rights from a legal point of view.

We will wait for further trials and court judgments to see whether criminal extortion is established in this case. On the other hand, patent holders should note the following issues if they wish to exercise their patent rights and avoid accusations of "extortion":

First, in the process of implying the behavior of the potential infringer and negotiating the patent license, it should be noted that a lawyer's letter and license fee required in the patent license contract or the compensation required in the complaint should comply with the law. For example, the patentee should ensure that the patents involved in the case are valid, and avoid obviously illegal conduct such as repeatedly demanding license fees.

Moreover, whether reminding the other party to infringe the patent right in written or verbal form and proposing an invitation of license or requesting for the license fee, it should be noted that the wording should point to the protection of the legitimate rights and interests of the patentee without sounding threatening or coercive.

In conclusion, patentees should be very mindful of the boundary between "exercising rights in accordance with law" and "extortion" and act to reasonably safeguard their legitimate rights and interests.

⁴ You Bin: "利用专利“敲诈勒索”拟上市公司案第二次庭审情况", <https://mp.weixin.qq.com/s/y4gON9Kf452VMKy5wfxyxQ>, latest access time: January 10, 2019.

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