

Why most patents are invalid – Extent, reasons, and potential remedies of patent invalidity

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EARLY DRAFT, COMMENTS WELCOME.

Joachim Henkel^{a, b}, Hans Zischka^a

^aTUM School of Management, Technische Universität München
Arcisstr. 21, 80333 Munich, Germany. henkel@wi.tum.de, zischka@wi.tum.de. +49 89 289 25741
^bCenter for Economic Policy Research (CEPR), London, United Kingdom

Abstract: The legal stability of granted patents is uncertain, a fact that entails inefficiencies for the patentee as for third parties. It is an important question for intellectual property policy and management how severe this problem is. Only few patents are litigated, and those that are are not a random selection. We thus ask: if a randomly picked patent underwent revocation proceedings with a thorough search for prior art, what would be the odds of it being invalidated? We address this question for the case of Germany, where revocation proceedings are separate from infringement suits. This bifurcation facilitates a focused analysis of the former. Our study is based on court decisions, expert interviews, and a survey among patent lawyers. We find that patents entering revocation proceedings are about as legally robust as the average patent. However, less than half of all revocation proceedings conclude with a decision, and those that do involve more robust patents. Thus, the share of court decisions that declare the focal patent partially or fully invalid—75% in Germany—is a conservative estimate of the share of all patents that would be partially or fully invalidated if challenged in court. Furthermore, the plaintiff’s budget was seen as having a positive effect on the likelihood of finding invalidating prior art, and so the assumption of a thorough search for prior art increases this share further. We show that our arguments carry over to other legislations. While we concur with earlier studies that a more detailed examination would not solve the problem, we do not consider “rational ignorance at the patent office” a satisfactory explanation. Even patents that are never litigated create inefficiencies. To address the problem that many patents are latently invalid we suggest a significant increase of the required inventive step.

Keywords: Patent, Patent Validity, Patent Invalidation, Inventive Step

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1. Introduction

The possibility to enforce patents is essential for the patent system to work. However, enforcement may fail because the focal patent is invalidated. In fact, much infringement litigation is decided by invalidation of the patent in suit, an observation that Lemley and Shapiro (2005) aptly capture with the notion of “probabilistic patents.” This uncertainty about a patent’s legal robustness entails inefficiencies for the patentee, who cannot fully rely on its patents; for third parties, who are facing more exclusion rights than legally should have been granted; and for policy makers concerned about incentives to innovate. Patents that are “latently invalid”—i.e., are valid but would be invalidated if challenged in court—unduly restrict innovative activities of third parties; expose them to the risk of infringement litigation; impose a cost burden for invent-around or licensing; and obfuscate the patent system, making patent search and monitoring more difficult.

It is thus an important question for intellectual property (IP) policy and management how severe this problem actually is. Only a very small fraction of all patents are litigated, and this fraction is not a random selection. It may be that those patents are litigated that lack legal robustness, in which case the problem of probabilistic patents would be less severe for the universe of all patents. But it may also be that patents in suit are more robust than the average patent: invalidity decisions are mostly triggered by infringement proceedings, and given the choice a patentee is more likely to enter these with robust patents.

We thus ask a simple yet important question. If a randomly picked patent underwent revocation proceedings, what would be the odds of it being invalidated? Are these odds higher or lower than the share of patents that, after being challenged in court, actually are invalidated? In other words, do the selection effects at work lead to patents whose validity is tested in court being more robust or less robust than the average patent?

We address the above questions for the case of Germany. The German patent system is characterized by a bifurcation between infringement and revocation proceedings (e.g., Cremers et al., 2013), which facilitates a focused analysis of the latter. We base our study on a descriptive analysis of all decisions in invalidity suits by the Federal Patent Court (*Bundespatentgericht* or *BPatG*) and the court of second (and last) instance (the Federal Court of Justice,

Bundesgerichtshof or *BGH*) from 2000 until 2012, 19 hours of expert interviews, and a survey among 320 patent lawyers.

On a descriptive level, we find that 55% of invalidity suits before the Federal Patent Court between 2000 and 2012 are settled, while 45% conclude with a decision. Of these, 69% are appealed. Overall, the decision in the respective final instance is “fully invalid” in 35% and “partially invalid” in 40% of all cases. That is, only in 25% of the cases with decisions the patent is held fully valid. Regarding selection effects, both interviewees and survey participants consider patents that enter invalidity suits to be of average robustness. However, the patents in those 55% of suits that settle are seen as significantly less robust—the logic being that, anticipating invalidation, the patentee would offer the plaintiff a license on favorable terms in exchange for withdrawal of the suit. Furthermore, the plaintiff’s budget was seen as having a positive effect on the likelihood of invalidation.¹ Given the patent office’s requirement of absolute novelty, the standard for testing validity of a patent should be a very thorough search for prior art, which can best be performed with a large budget. Thus, assuming that in the hypothetical suit involving a randomly picked patent a large budget was spent by the plaintiff, the likelihood of invalidation would be further increased compared to the sample of actual decisions. It is thus safe to conclude that a randomly picked patent would be invalidated, partially or fully, with a probability above that found for actual invalidation decisions. For Germany, thus, more than 75% of all active patents are latently invalid, either fully or partially.

We argue that the same logic holds for other legislations. In fact, in countries such as the U.S. where validity is tested within the infringement proceedings rather than separately as in Germany, the incremental robustness of patents whose validity is challenged over the average patent should even be higher. We suggest that a significant increase of the required inventive step would help to address the problem of the high rate of latently invalid patents, and discuss the benefits and challenges of such a measure.

The paper is organized as follows. In the next section, we review the literature on the determinants of patent infringement and patent validity. Section 3 presents method and data, and Section 4, results. The final sections provide a discussion of our findings and conclusions.

¹ Preliminary results of an econometric analysis of actual decisions between 2010 and 2012, not reported in this study, confirm this finding, using the plaintiff’s revenues as a proxy for the budget spent on the suit.

2. Literature Review

A common defense against an infringement action is to challenge validity of the underlying patent (Lanjouw and Schankerman, 2001), such that patents facing a revocation action are usually preselected at the infringement stage. Thus, it is necessary to examine patent infringement and its determinants before addressing the factors influencing revocation.

2.1. Patent infringement

One of the inefficiencies caused by latently invalid patents is that they may expose other parties unduly to the risk of being sued for infringement. This is the more a cause of concern the more widespread infringement in general is. So, how frequent is patent infringement? Infringement *litigation*, in any case, is rare—according to Lemley (2001), only about 1.5% of all U.S. patents are ever asserted in court.² For Germany, Stauder (1989) estimates a share of 1% of all patents. However, actual litigation is only the tip of the iceberg as patentees may not find out about the infringement, not react to it, or settle with the infringer (Weatherall and Webster, 2014). Also, since patents do not fulfill their notice function properly as argued by Bessen and Meurer (2008), it is plausible that much patent infringement is inadvertent and also goes unnoticed by the patentee. For Australia, Weatherall and Webster (2010) find that 28% of the patents in the sample were perceived by the respective inventor as having been infringed.³ Considering that most inventors do not actively search for infringement, the actual number will likely be higher.

Various surveys, recently reviewed by Weatherall and Webster (2014), study the incidence of infringement on the level of firms. Kingston (2001) and Rodwell et al. (2007) find that two-thirds to three-quarters of the European SMEs in their sample faced some kind of IP infringement. By surveying UK SMEs and micro-firms, Greenhalgh et al. (2010) discovered that roughly 35% of the respondents had already faced a patent dispute. While firm-level results are not directly informative about the incidence of infringement on the patent level, they do support the notion that patent infringement is far more widespread than patent litigation. This, in turn, implies that the risk of being sued for infringement of latently invalid patents is a serious cause of concern.

² This number varies strongly by industry and reaches six percent for the biotechnology sector (Lerner, 1995).

³ While the authors mostly use “copying” instead of “infringement,” they make clear that they do not differentiate between the terms. They use “copying” to mean “conduct the inventor perceives as involving use of their idea/invention” (Weatherall and Webster, 2010: 24) without implying intent on the part of the presumed copier.

To understand the selection effects that lead to patents being involved in revocation actions, we now review the factors that affect the likelihood of a patent being involved in infringement litigation (which in turn triggers most revocation actions). The most obvious of these factors is the patent's commercial value. The more valuable the underlying invention, the more likely it is that third parties will pursue similar research and come up with products or processes that infringe on the focal patent, or will even consciously infringe on the patent. This economic reasoning is confirmed by empirical observations showing that patents with a higher number of forward citations—an established indicator of patent value—are more likely to enter infringement actions (Allison et al., 2004; Cremers, 2004; Lanjouw and Schankerman, 2001, 2004; Somaya, 2003).⁴ The same is true for patents that are part of a larger patent family (Cremers, 2004; Harhoff et al., 2003), which also indicates patent value (as perceived by the applicant). Furthermore, a patent's being involved in litigation, which causes considerable cost⁵, constitutes in itself a signal of value (Lemley and Shapiro, 2005).

Several studies find a positive relation between the number of backward citations of a patent and the likelihood of it being involved in infringement litigation (Allison et al., 2004; Cremers, 2004; Harhoff et al., 2003; MacGahee, 2011). In contrast, Lanjouw and Schankerman (2004) find a negative relationship, arguing that backward citations are an indicator for a well-developed field of technology where uncertainty less likely results in legal disputes. Further, a positive relationship has been identified with the number of claims (Allison et al., 2004; Lanjouw and Schankerman, 2001; MacGahee, 2011), the application-to-grant lag (Allison et al., 2004; Somaya, 2003), and patent age (Allison et al., 2004). Finally, Harhoff et al. (2003) and Cremers

⁴ See Cooter and Rubinfeld (1989) as well as Lanjouw and Schankerman (2001) for an overview of the key determinants of litigation in general and with respect to patent litigation, respectively.

⁵ According to the American Intellectual Property Law Association (2013) each party in a litigation proceeding faces median costs of \$700,000 for patents worth < \$1 million. Those costs can increase to up to \$5.5 million for patents valued at more than \$25 million (American Intellectual Property Law Association, 2013). For the case of Germany the costs for first instance proceedings are typically in between €75,000 to €1,380,000, for values in dispute from €500,000-€30,000,000. Costs for the second instance proceeding are roughly 15% higher (Bardehle Pagenberg Partnerschaft, 2013b). Total costs (including nullity action) can be as high as €2 million for €10 million in dispute (IP Campenhausen, 2004; Mejer and van Pottelsberghe de Potterie, 2012). Moreover, an estimation by Bessen and Meurer (2012) for U.S. public firms on proceeding related costs for alleged infringers exceeds \$16 billion a year.

(2004) find a positive correlation between a patent's having survived opposition or re-examination and the incidence of later infringement proceeding.

Of interest in our study is if patents entering infringement actions are more robust than the average patent. The correlations reported above are mostly inconclusive in this regard, though. Value should increase both with the patent's inventive step and with its breadth; legal robustness, however, should increase with the former but decrease with the latter. Any predictions regarding a correlation between robustness and backward citations, number of claims, grant lag, or age appear even more speculative. The same is true for characteristics of the patent holder, which various authors have studied as potential correlates of infringement litigation.⁶

What is relevant in our context is the positive correlation between a patent being involved in infringement proceedings and its having survived opposition or re-examination (Cremers, 2004; Harhoff et al., 2003). Such patents have shown a certain legal robustness, by virtue of which they increase the average robustness of all patents involved in infringement proceedings. A second argument pointing in the same direction is based on the patentee's decision situation. Legal action is not an automatic reaction to detecting infringement. A patentee will be more likely to file suit if it perceives the allegedly infringed patent as robust; and in case a product is seen to infringe on several patents, the patentee will *ceteris paribus* select those it perceives as most

⁶ Foreign-owned patents seem to be less likely involved in a patent infringement action than domestic-owned patents, likely due to the higher costs foreign parties would face as well as cultural and language differences (Allison et al., 2004; Lanjouw and Schankerman, 2001; MacGahee, 2011; Moore, 2003; Weatherall and Jensen, 2005). Analyzing US proceedings between 1978 and 1999, Lanjouw and Schankerman (2004) find that patents assigned to individuals and domestic firms with small patent portfolios are more likely part of infringement proceedings than firms holding larger patent portfolios. This finding has been confirmed by other scholars analyzing similar settings (e.g. Allison et al., 2004; Ball and Kesan, 2009; Bessen and Meurer, 2005; Somaya, 2003). The outcomes are similar for Germany (Cremers, 2004) and Australia (Weatherall and Webster, 2010). Greenhalgh et al. (2010), however, come up with a contrary finding. According to their study on UK cases between 2003 and 2009, large foreign firms were prominent among the litigants. Weatherall and Webster (2014) summarize possible explanations for the finding that small firms are more likely involved in patent litigation: they only have a small number of patents available for possible cross-licensing and therefore a reduced bargaining power; they have more at stake and hence more to lose; they have wrong expectations and are more confident of winning a dispute; and they may face issues of asymmetric information as larger firms are typically more experienced about patents and how to litigate them. With respect to the business model of parties involved, several scholars find a steadily increasing share of non-practicing entities (NPEs) in infringement proceedings (Ball and Kesan, 2009; Chien, 2009; Freedman, 2010). This is in line with the fact mentioned earlier that more valuable patents are more likely to enter those proceedings and NPEs tend to own more valuable patents (Fischer and Henkel, 2012; Risch, 2012).

robust for its legal action. Summarizing, we have indications that patents involved in infringement proceedings are more robust than the average patent.

2.2. Patent validity

2.2.1. Patents entering invalidity proceedings

About 1% of all granted patents find their validity challenged in court, both in Germany (e.g. Keukenschrijver, 2011) and in the U.S. (e.g. Lanjouw and Schankerman, 2001). For Germany, Stauder and Luginbuehl (2009) identify a steady upward trend. Nearly all of these validity challenges are triggered by infringement proceedings (Keukenschrijver, 2011, pp. 73–74; Stauder, 1989, p. 39; Stauder and Luginbuehl, 2009, p. 296). In turn, one third to half of all patents that are involved in infringement proceedings are subsequently subject to validity challenges instituted as a defense by the alleged infringer.⁷ In countries where validity is challenged within infringement proceedings, this share is considerably higher. Stauder (1989) reports 81% for France and 93% for the UK. For the U.S., the share is estimated to be above 90%.

Which characteristics of a patent correlate with the likelihood of it entering invalidation proceedings? We are not aware of any research on the selection of patents into revocation proceedings. Obviously, since most invalidity proceedings are triggered by infringement proceedings, the selection effects at work for the latter also come to bear for the former. In particular, we had identified a selection of more robust patents. In a bifurcated system as in Germany this selection effect is counteracted by the fact that, subsequently, the alleged infringer will be more likely to challenge the patent's validity the less robust it is perceived to be. Compared to all patents in infringement proceedings, those in invalidity proceedings should thus be less robust on average. To judge the net effect of both selections, relative to the population of all patents, on the basis of earlier research and economic arguments alone appears unfounded. We will address this issue empirically in our Results section.

⁷ For the period of 1972 to 1974 Stauder (1989) reports a share of 44% to 57%. Averaging over the years of 2000 to 2008 (filing year of the respective infringement action), Cremers et al. (2014: 24) find that “slightly less than a third of infringement cases (counted at the patent level) are associated with a revocation action.”

Note that the counteracting selection effect described above is largely absent in legal systems such as the U.S. where validity is challenged in most infringement proceedings. In such countries, patents whose validity is tested in infringement proceedings should thus be more robust than the average patent.

2.2.2. *Outcomes of invalidity proceedings*

When invalidity proceedings in Germany are concluded with a decision, significantly more than half of all patents are either partially or fully invalidated. For 1963 till 1971, Liedel (1979) finds a rate of partial or full invalidation of 71% in the first as in the second instance. Keukenschrijver (2011) reports for the first instance a rate of 66% for 1961 till 1980 and 52,1% for 1980 till 1990. In the same range, Fischer (2011) finds a rate of 65% in the first instance for the period of 1985 to 1999, and Stauder and Luginbuehl (2009) even report a rate of 76% for 2000 till 2008. This number is in line with our own analysis, reported below, for 2000 till 2010.

The high rates of invalidation reported above are not specific to Germany. Early studies on U.S. patent litigation unveil an invalidation rate of 60% to 70% for the period 1948 to 1954 (Federico, 1956) and roughly 65% from 1953 to 1978 (Koenig, 1980). Allison and Lemley (1998) report an overall invalidation rate of 46% for the period of 1989 to 1996. More recently, Mann and Underweiser (2012) find for the years 2003 through 2009 that the Federal Circuit held 60% of the patents in the cases it adjudicated not valid. In other countries, invalidation rates are in similar ranges. For Australia, Weatherall and Jensen (2005) report a rate of full or partial invalidation of 53% (first and second instance) for the period of 1997 to 2003. Oyama (2012) finds an invalidation rate of 73% at the Japanese district courts, and a UK study examining the years 2000 to 2008 indicates an overall rate of about 50% partially or fully invalid in the first instance (Helmers and McDonagh, 2013). France seems to be special case, with according to Véron (2010) only 27% of the cases before the court of first instance in Paris between 2000 und 2009 resulting in a revocation decision.

Given that globally more than half of all invalidation proceedings concluding with a decision lead to partial or full invalidation of the patent, the question arises which factors correlate with, or even drive, the likelihood of invalidation. We address in turn factors relating to the granting process, the patent, and the parties in suit.

Granting process. Henry and Turner (2006) trace how the establishment of the Court of Appeals for the Federal Circuit (CAFC) affected invalidity decisions. Analyzing the years 1953

through 2002, they show that the CAFC significantly decreased the rate of revocation and overruled the first instance invalidity decision three times more often. As a result the lower courts halved their revocation rulings and patentees appealed more likely in case of a first instance invalidity. Cockburn et al. (2002) analyzed the CAFC rulings during the period 1997 to 2000 with respect to examiners' characteristics, but found no correlation between the examiners' experience, his or her workload, or the age of the patent and the outcome of the invalidation proceedings. Further, Marco (2006) estimated the probability of wrongful validity and invalidity rulings by district and appellate courts. Allison and Lemley (1998) find that juries are more patentee friendly and patents in jury trials are therefore more likely upheld. Atkinson et al. (2009) show that patents in patentee-defendant cases—where the patent challenger initiates litigation—are less likely ruled valid. According to MacGahee (2011) this effect significantly increases for cases involving continuations. Finally, Cockburn et al. (2002) and MacGahee (2011) find a positive relationship between the time a patent spent in examination and the probability of invalidation, while Fischer (2011) identifies a negative correlation.

Patent characteristics. Various patent characteristics have been analyzed regarding their correlation with the likelihood that a patent would be ruled invalid. Results have been partly contradictory. For the number of backward citations, MacGahee (2011) finds a negative relationship analyzing U.S. cases between 1929 and 2006, while Fischer (2011) finds no correlation for German invalidity suits between 1985 and 1999. Fischer (2011) also finds no correlation with the number of forward citations. Both authors show a negative relationship with the number of claims (Fischer, 2011; MacGahee, 2011). Fischer (2011) further specifies that a larger number of claims positively correlates with partial but not with complete survival—a plausible finding since a larger number of claims makes it more likely that at least one is upheld in invalidation proceedings. Equally plausible, Fischer (2011) further finds a positive correlation between a patent's having survived opposition and its surviving invalidity proceedings without any amendments. Finally, both Atkinson et al. (2009) and MacGahee (2011) find that older patents are less likely to be ruled invalid, while Cockburn et al. (2002) find no such correlation.

Characteristics of the parties in suit. There is little research on how plaintiff and defendant characteristics correlate with invalidation probability. Using patent portfolio size as a proxy for company size, Fischer (2011) was able to show that defendant size has an inverted U-shaped relationship with the probability that a patent survives. There is further evidence that corporate as

well as foreign patentees are more likely to win, implying a higher probability that their patents are upheld (MacGahee, 2011).

2.2.3. *Oppositions*

During the first nine month after grant of a patent by the European Patent Office (EPO), respectively three month at the German Patent and Trademark Office, the patent's validity can be challenged by any third party through an opposition (post-grant review) before the respective patent office. Just as revocation actions before the Federal Patent Court, oppositions may be triggered by an infringement suit⁸, but in the majority of cases are filed as a preventative action against "potentially dangerous patents of competitors" (Bardehle Pagenberg Partnerschaft, 2013). Doing so is an attractive option not least because the fees for an opposition are rather low. Cost estimates for each instance and party reach from €15,000 to € 25.000 (Harhoff and Reitzig, 2004) to € 50,000, depending on the complexity of the case (Bardehle Pagenberg Partnerschaft, 2013).

We focus in our study on invalidation proceedings rather than including oppositions as well, for the following reason. The fact that they are initiated by third parties (while nearly all revocation actions are triggered by infringement suits) implies that patents perceived as weak should be opposed more often. Since a relatively large share of all granted patents are opposed (roughly 5%)⁹, this suggests that the opposition procedure weeds out quite a few weak patents. In fact, approximately one-third each are fully revoked, maintained with amendments, and fully maintained.¹⁰ Accordingly, those still in force after the end of their respective opposition period should be more robust. By focusing on invalidation proceedings rather than also including

⁸ During the opposition period, invalidation of the focal patent can only be effected through an opposition; a suit before the Federal Patent Court is possible only after that period. Accordingly, a defendant in an infringement suit filed during the opposition period needs to resort to an opposition (or to wait until the end of the opposition period) if it wants to take legal steps to invalidate the patent.

⁹ See, e.g., Bardehle Pagenberg Partnerschaft (2013), Calderini and Scellato (2004), Caviggioli et al. (2013), Harhoff et al. (2007), Scellato et al. (2011). Oppositions are significantly more frequent than invalidation proceedings (Harhoff and Reitzig, 2004; Harhoff et al., 2003). Out of 24,116 granted patents with the priority year 1979, 2,036 were opposed and only 73 of them were subject to a revocation proceeding (Harhoff et al., 2003).

¹⁰ See Caviggioli et al. (2013), Harhoff et al. (2007), Scellato et al. (2011). The outcomes of German national cases are quite similar to the EPO cases (cf. Caviggioli et al., 2013; Scellato et al., 2011).

oppositions we thus obtain a more conservative estimate of the share of all patents that would be invalidated if challenged.¹¹

Nonetheless, due to the obvious parallels between invalidation actions and oppositions it is appropriate in the context of our study to review existing research on the latter. Specifically, we report findings on the correlates of the incidence and outcome of oppositions, related to the patent and to the parties involved.

Regarding the focal patent, studies have demonstrated that more valuable patents are more likely to be challenged in opposition proceedings. Empirical research identified amongst others that patents' forward and backward citations, the number of claims and the size of the patent family are positively correlated with the probability of facing an opposition (Caviggioli et al., 2013; Graham et al., 2002; Hall et al., 2009; Harhoff and Reitzig, 2004; Jerak and Wagner, 2006; Schneider, 2011). Evidence on correlates of opposition outcomes is mixed. Caviggioli et al. (2013) report a positive correlation with patent value indicators such as backward citations and number of claims on the survival likelihood. Family size, however, shows a positive correlation with a revocation probability. Furthermore, Graham et al. (2002) identified a higher amendment probability for highly cited patents and patents with many claims.

With respect to characteristics of the parties involved, Harhoff and Hall (2002) were able to show that oppositions in the haircare industry repeatedly occur between larger firms. Contrary to this finding, Calderini and Scellato (2004) provide evidence from the telecommunication industry that larger firms more likely oppose patents of smaller companies, whereas the probability of oppositions between two larger players is significantly lower. In his study on cases in the plant biotechnology sector, Schneider (2011) discovered that patents of companies with larger patent portfolios more likely face an opposition. However, there seems to be no statistical difference between large firms and small firms (measured by the number of employees) with respect to an opposition probability (Schneider, 2011).

By and large, thus, the identified correlates of invalidation probability are consistent between oppositions and invalidity actions. The key difference, as explained, resides in the way either is initiated, which should select more robust patents into invalidity actions than into oppositions.

¹¹ One could also consider oppositions as part of the granting process. In this sense, our study focuses on those patents whose granting process is fully completed.

3. Method and Data

3.1. Institutional background

Before illustrating the methods and data used, we provide a brief description of German revocation proceedings. Once the opposition period has expired, the validity of a German patent or the German part of a European patent can be challenged through revocation proceedings. Such proceedings can be initiated by any legal entity, both for its own and for a third party's purpose (Keukenschrijver, 2011). Nevertheless, a revocation suit is usually filed as a counterclaim to an ongoing infringement dispute (Keukenschrijver, 2011). Due to the German bifurcated patent litigation system, questions regarding infringement and invalidation are not subject to the same proceeding. Whereas district courts (*Landgerichte*) are responsible for the first instance of infringement proceedings, the first instance jurisdiction over revocation disputes lies with the Federal Patent Court. The district courts examine alleged infringement assuming validity of the patent in suit.¹² However, according to §148 ZPO the court can stay an infringement proceeding¹³ if it expects a (partial) revocation of the patent in a co-pending revocation proceeding (Keukenschrijver, 2011).¹⁴

Once a revocation proceeding has been filed with the Federal Patent Court, the judges (who are technically trained) have to decide on whether the patent at stake is valid, partially invalid, or invalid. The reasons for a patent revocation are based on §22 PatG in conjunction with §21 PatG and can be classified as follows: non-patentability, insufficiency of disclosure (lack of enablement), extension of the subject matter beyond the content of the application as originally filed, extension of the scope of protection, and “theft” of the invention by the patentee (Bardehle Pagenberg Partnerschaft, 2014; Keukenschrijver, 2011). Liedel (1979) identified non-patentability based on a lack of inventive step as the predominant reason for an invalidation ruling. An action is dismissed—and the patent therefore maintained as granted—if the claim is inadmissible or the examination shows that the claimed invention is patentable.

¹² A potential invalidity of the patent-in-suit is an inadmissible defense. A revocation proceeding has to be filed with the Federal Patent Court.

¹³ Even ex officio.

¹⁴ Practically this is done quite seldom and only if the probability of a (partial) revocation is high.

Whereas “invalid” and “valid” are unambiguous decisions, a partial invalidity ruling is not. However, it can usually be interpreted as either “invalid” or “valid” in the context of the infringement case that triggered it, depending on the fate of the claims relevant in that case. The parties in the revocation case may also restrict their challenge, or defense respectively, to a subset of all claims. The plaintiff may request a partial invalidation of the patent, contesting only certain claims. The court then only examines those claims the plaintiff filed invalidation for. A “partial invalid” ruling in line with the plaintiff’s filing effectively amounts to a full invalidation from the plaintiff’s point of view (Liedel, 1979). In turn, the defendant has the option to restrict its defense to a limited number of claims. Only these claims will be subject to the court action, while the non-defended claims become by operation of law invalid (Keukenschrijver, 2011). In this case the patent can only be ruled partial invalid—if some or all of the defended claims are upheld—or invalid if the defended claims are ruled invalid. An indication of whether a “partial invalid” decision means a success for the plaintiff or the defendant is the filing of an appeal by one or the other party.

In total approximately two-third of the first instance decisions on the merits are appealed before the Federal Court of Justice (Stauder and Luginbuehl, 2009) where five legally trained judges of the X. Senate decide on the validity of the patent within one oral hearing (Keukenschrijver, 2011). The Federal Court of Justice ruling is final and cannot be appealed. If the first-instance plaintiff withdraws its claim in a Federal Court of Justice proceeding, the patent remains valid notwithstanding the first instance ruling. A withdrawal of the appellate proceeding will result in a legally binding first instance decision.

The central question addressed in this study concerns the selection effects that lead from the population of all active patents to those that enter revocation proceedings which end with a decision (see Figure 1). In this population there is an unknown number of infringed patents (1). Some of these infringed patents and some of the non-infringed patents get involved into infringement proceedings (2). A certain share of these patents (plus very few others) are subject to a revocation proceeding (3). Cases that are not settled reach a first instance decision at the Federal Patent Court (4). A particular percentage of the aforementioned Federal Patent Court rulings are appealed before the Federal Court of Justice and result in a final ruling unless they are settled (5). On each stage there are several legal, patent related and party specific determinants influencing the probability that a patent proceeds to the next level.

Figure 1 here

3.2. Analysis of court decisions

We built a dataset of all decisions connected to patent validity by the Federal Patent Court between 2000 and 2012 as well as the corresponding appellate decisions by the Federal Court of Justice from 2000 until 2014.

We sourced the first instance decisions including a wide range of case specific information from the Federal Patent Court's decision database, which provides online access to all its decisions since 2000.¹⁵ We complemented the first instance data with the related second instance decisions using the online judgment database of the Federal Court of Justice providing access to all its decisions (by the X. Senate) since 2000.¹⁶

We verified our findings by comparing them with a list of all patent validity cases (including their outcomes) filed at the Federal Court of Justice within the last two centuries, which was provided by the Federal Court of Justice's X. Senate. This information allowed us to identify the appellate cases without a final decision on the merits, yet with out of court settlements or withdrawals.

3.3. Interviews

To gain further insights into the nature of patent revocation proceedings as well as the factors influencing these proceedings at the various stages of the process, we conducted 12 semi-structured interviews with 15 different interviewees.¹⁷ We selected our interview partners based on the following criteria. First, the interviewees need to be experienced in our field of study, i.e., familiar with infringement and revocation proceedings and senior with respect to professional experience. Second, the interview partners should provide a comprehensive view of the topic. The interviewees were therefore selected from different professions as well as different

¹⁵ See: http://www.bundespatentgericht.de/cms/index.php?option=com_wrapper&view=wrapper&Itemid=77&lang=en.

¹⁶ See: <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/list.py?Gericht=bgh&Art=en&Datum=Aktuell&Sort=12288>.

¹⁷ Three phone and nine face-to-face interviews.

technological backgrounds. Among the interview partners are judges from the Federal Patent Court and Federal Court of Justice, representatives of the patent office, and lawyers and patent attorneys with or without former industry experience.¹⁸

As a framework we used an interview guideline based on the invalidation process and the various selection stages (see 3.1.). We started with general questions related to infringement and revocation proceedings. With respect to our research questions we guided the interviewees through the whole process and asked for determinants influencing every single stage. We further asked the participants to assess the importance of these factors. The questions had an open form and often initiated lively discussions. In total we conducted 19 hours of interviews, corresponding to an average duration of 1h 35min. The interviews were fully recorded, transcribed, encoded and evaluated using QRS's nVivo software.

3.4. Survey

Based on the interview results and research questions, we developed a five page paper-based questionnaire to gain further insights into the proceeding's selection process. The survey is divided into four parts. The first block contains personal questions on the participants' professional career. The second and third part include questions regarding factors influencing infringement as well as first and second instance revocation proceedings. The survey concludes with questions related to the participants' employers. We mainly used closed-ended questions with default response options on a five-point Likert scale as well as some open estimation questions.¹⁹ For reasons of quality and clarity improvement, we did several pre-tests with patent attorneys and research assistants.

Potential participants were identified using a ranking of patent law firms in the field of patent infringement as well as a list of further renowned patent law firms, both provided by the JUVE publishing house.²⁰ By thoroughly searching and analyzing the ranked law firms' websites, we were able to identify patent attorneys and lawyers engaged in infringement and in particular in revocation related proceedings. This approach resulted in a list of 1165 potential participants

¹⁸ Please refer to appendix X for an anonymized list of our interview partners.

¹⁹ For some of the questions we allowed for a "no answer possible" response.

²⁰ See <http://www.juve.de/handbuch/de/2013/ranking/24450#ranking-24450>;
<http://www.juve.de/handbuch/de/2013/weiterekanzleien/24450#weiterekanzleien-24450>

(among them are 74% patent attorneys and 26% lawyers) working for 100 different national and international law firms with offices in Germany. Following an announcement in the newsletter of the chamber of patent attorneys in Germany, we sent out the paper-based questionnaire including cover letter, survey and a postpaid envelope. Besides, we set up an online version of the survey to provide a choice of medium to the participants. After two follow-ups (four and seven weeks after the initial distribution), we achieved an overall response rate of 28%. The survey demographics show that 64% of the respondents are patent attorneys, 36% lawyers. The median participant was involved into 6-10 revocation proceedings and shows 11-15 years of revocation suit experience.²¹ Nearly 40% of the respondents work in law firms with more than 150 employees.

4. Results

4.1. Descriptive analysis of court decisions

We base our study on a descriptive analysis of all final decisions by the German Patent Court (BPatG) and the court of second instance (BGH) during the course of patent revocation proceedings in Germany from 2000 until 2012. In total we analyzed 1144 different first instance decisions and 328 corresponding BGH rulings on 1111 different German Patents.²² Figure 2 illustrates the process of a German revocation action including first and second instance proceedings including statistics.

Figure 2 here

Due to data restrictions we only consider those proceedings that reached a judgment on the merits.²³ During the analyzed period, on average roughly 46% of the first instance revocation

²¹ To preserve anonymity, these variables were asked as categories.

²² Number includes German parts of European patents.

²³ This is in line with Liedel (1979).

proceedings reached such a final ruling.²⁴ 54% of the proceedings were concluded by a withdrawal of the revocation action or settlements between the parties. According to the Federal Patent Court decisions in our dataset, 24% of the cases were dismissed and the patent therefore upheld. The court partially revoked the patent in 39% of the cases and decided on a full revocation in 37%. That is, only in 25% of the cases the patent is held fully valid. Analyzing the partial revocations reveals that 45% of them conform to the plaintiff's claim. Effectively, thus, we can consider these rulings as full revocations in the context of the corresponding infringement suit, increasing the share of fully revoked patents from 37% to 55%.²⁵ Also a certain share of those "partial invalid" decisions where the plaintiff had claimed a full invalidation may be tantamount to an effective full invalidation, though we cannot determine this share precisely.

69% of the first instance decisions on the merits are appealed at the Federal Court of Justice. 41% of these appellate proceedings reach a final decision (the split being 22% fully valid, 43% partially revoked and 35% fully revoked).²⁶

The outcomes of the cases reaching their final judgment at the first or second instance can be divided up into 25% "valid", 41% "partially revoked", 34% "fully revoked". The aforementioned revocation rates at the first, second and first or second instance are roughly the same for patents granted at the European Patent Office as well as for patents granted at the German Patent Office. Table 1 summarizes the decisions at each stage as well as the final decisions of the first or second instance.

Table 1 here

According to Table 2, the majority of patents in revocation proceedings protect technologies of the mechanical engineering sector (34%). This finding is in line with Cremers et al. (2013).

²⁴ We calculated this number, analyzing the yearly statistics of the Federal Patent Court on revocation proceedings, reported in the respected March issues of the Blatt für Patent-, Muster- und Zeichenwesen (Blatt für PMZ).

²⁵ See Section 3.1..

²⁶ 59% of the cases did not reach a final decision due to the following reasons: 27% withdrawal of the appeal; 19% withdrawal of the claim; 2% settlements at court; 7% pending; 4% other.

According to their study, the majority of litigants in patent disputes are associated with the machinery industry. A closer look at the outcomes for each industry reveals that the (partial) revocation rate is equal to or higher than 70% across all industries. The highest number of (partial) revocation judgments is pronounced in the Chemical industry (84%).

Table 2 here

4.2. Legal stability of patents in revocation suits

In order to draw conclusions for the population of all patents from the observed invalidity decisions we need to identify the selection effects at work (see Figure 1). As discussed earlier, economic reasoning suggests that patents involved in infringement cases should be more robust than the average, while the subsequent selection stage—in most cases the filing of an invalidity suit by the alleged infringer—should favor less robust patents. This reasoning is confirmed by our interviews, from which we report specific quotes for illustration:

I wouldn't have proceeded on the basis of a non-robust patent [...]. (Patent attorney)

As expected, our interviews reveal that the positive selection at the first stage is counteracted by the next step leading to revocation proceedings:

“Well, I assume after all that there would have been some sort of tangential result, affecting the granted patent [...] And this in turn indicates to me that the suits which are filed are not without any prospect of success.” (Patent attorney)

These findings are in line with our survey results. As Table 3 shows, survey participants perceive patents involved in infringement proceedings as more robust than the average (mean: 0.20; test median=0: p=0.000). The net effect of both selection stages is seen to be zero (mean: 0.04; test median=0: p=0.243). That is, both interviewees and survey participants consider patents that enter invalidity suits to be of average robustness.

4.3. Influence of firm size and budget

We now address the influence of two key characteristics—size and budget—of plaintiff and defendant on the outcome of revocation proceedings. Liedel (1979) reports estimates that the share of invalidations could be increased to up to 95% if the plaintiff sued without time and budget restrictions. While this is clearly a bold estimate, it is plausible that invalidation becomes more likely the more time and budget is spent on searching for prior art.

According to our interviews, firm size by itself does not have an influence, but—unsurprisingly—does correlate with budget spent on the case:

“The little guy has an even chance if he deploys equal means. And what is unfortunately observable time and again is that they do not do this. Either they are poorly represented or they’re not willing to invest the money in decent research.”
(Patent attorney)

“Not necessarily. Well, size doesn’t really confer any premium in itself.” (Judge)

Budget spent is seen to matter, though:

“If you search long enough and with sufficiently large amounts of money that you put into the thing, you’ll eventually find something.” (Patent attorney)

“Well, as regards the success of revocation suits, I do think that the investment in good lawyers pays off to some extent” (Patent attorney)

Survey results are mostly in line with interview findings (Table 3). Plaintiff size is seen to increase the probability of an invalidation ruling slightly (mean: 0.19; test median=0: p=0.000), whereas defendant size is considered to have no effect (mean: -0.01; test median=0: p=0.653). Regarding budget, survey participants clearly believe that a larger budget will strongly increase the probability of finding new prior art suitable to achieve an invalidation ruling (mean: 1.40; test median=0: p=0.000).

4.4. Revocation suits that settle

As already shown in Section 4.1., a large share of revocation suits settle (55% of the first instance proceedings). Economic reasoning suggests that these settlements would have ended in (partial of full) invalidations had they been brought to a decision. By settling when invalidation is imminent, and the patent holder providing a free license to the plaintiff, the parties in suit save on costs while maintaining the patent as a barrier against outsiders.²⁷ In contrast, when a “valid” ruling is to be expected the patentee improves its position vis-à-vis third parties by receiving the confirmation of validity of its patent.

Interview results are consistent with this argument:

“In my opinion, this means that behind these very high figures there are, in essence, potentially successful revocation suits.” (Patent attorney)

“They would probably also all have been revoked, or many would have been revoked.” (Judge)

“These certainly are the weak patents. If one’s pretty sure of one’s position, then one sees it through.” (Patent attorney)

Survey participants confirm the interview results that settled proceedings would more likely have led to a partial revocation (mean: 0.59; test median=0: p=0.000) as well as a full revocation decision (mean: 0.20; test median=0: p=0.001) than proceedings that ended with a decision.

4.5. Newly found prior art vs. differing evaluation standards

Invalidation decisions on German patents are taken by the Federal Patent Court or the Federal Court of Justice, while the grant decision is taken by the EPO or the German Patent and Trademark Office. In our context, the respective court’s decision is relevant since it *defines*, by

²⁷ Lemley and Shapiro (2005: 76) note in this context: “Indeed, virtually every patent licensing and cross-licensing agreement can be seen as the settlement of a patent dispute. However, the frequency or form of such private settlements may not serve the public interest, because litigating patent disputes to completion tends to generate positive externalities, by clarifying the limits of patent protection if the patent is upheld or encouraging wider use of the innovation if the patent is invalidated.”

law, validity of the focal patent. Nonetheless, in order to suggest policy measures that could address the issue of latently invalid patents it is important to understand if the large number of invalidations by the German courts is due to newly found prior art or to differing evaluation standards. According to our interviews, the former clearly matters:

“Well, in those cases I spontaneously recall now, new prior art was virtually always submitted.” (Patent attorney)

“I do believe, however, that in most cases new prior art will be found or submitted.” (Patent attorney)

Yet, also differing evaluation standards play a role:

“And here, the thing is that, in my view – this is just my personal estimation now – 50 percent of the decisions taken by the Federal Patent Court would have reached the opposite conclusion at the European Patent Office.” (Patent attorney)

“That happens, too. That is, that prior art was not considered as relevant in the examination procedure by the EPO as it was before the Federal Patent Court in a revocation suit - that happens a lot.” (Patent attorney)

The survey (Table 3) clarifies that newly found prior art is seen as the predominant invalidation reason at the Federal Patent Court (mean: 4.46, between “important” (4) and “very important” (5)), while differing evaluation standards (Federal Patent Court vs. DPMA/EPO) are considered as being between “somewhat important” (3) and “important” (4), with a mean of 3.51.

4.6. Resulting selection bias

Overall, patents in first-instance invalidation proceedings that conclude with a decision should be more robust than the average patent: the net selection effect of patents in infringement suits, followed by the selection of a share of these patents (and very few others) into invalidation suits is seen to be neutral, while the selection into decisions by the Federal Patent Court (as opposed to settlements) favors more robust patents.

Since the subsequent selection into the second instance (see Figure 2) is fairly symmetric among the first-instance outcomes, and the second-instance decisions show largely the same distribution as those in the first instance, there is no indication of a selection bias in the step from first to second decision. However, the logic that settlements are more likely to occur if an invalidation appears imminent applies equally at the second instance. Again, thus, patents in invalidation cases concluding with a decision should be more robust than the average patent.

5. Discussion

Are these findings worrisome? Lemley (2001) argues that patent offices are “rationally ignorant” of the objective validity of patents because examining each patent in detail would be far too costly: “Because so few patents are ever asserted against a competitor, it is much cheaper for society to make detailed validity determinations in those few cases than to invest additional resources examining patents that will never be heard from again.” While we follow the argument that a more detailed examination of each patent application would not solve the problem, and an examination as thorough as in a court case would be unfeasible for patent offices, we do not consider “rational ignorance” a satisfactory explanation. Even patents that are never litigated create inefficiencies—they deter third parties from using the patented invention, create a risk for others of being litigated, cause cost for their application, examination, grant, monitoring, and obscure the patent system by their sheer quantity.

So how could the problem that the majority of German patents—and large shares of all patents also in other countries—are latently invalid be addressed? Increasing fees for examination and grant may go some way in reducing the number of legally weak patent applications, though only to the extent that patent value as perceived by the applicant correlates with robustness. However, this measure would likely affect financially constrained applicants more than legally weak patents.

We suggest that a significant increase of the required inventive step would help to address the problem. The intuition is as follows. Prior art existing at the time of application but unidentified by the examiner should be distributed along the “inventive-step over the known prior art” dimension with a density that decreases with the inventive step, the reasoning being that prior art with a larger inventive step is harder to invent and easier to find. Increasing the required inventive step of the focal invention over the known prior art by some measure δ —which we

acknowledge is hard to quantify—should thus be most effective for small values of delta and exhibit decreasing marginal effectiveness with increasing delta. In other words, “jumping” a good share of the non-obviousness destroying unknown prior art should be possible with a significant, but not too large increase of the required inventive step. This suggestion will be developed further in future versions of this study.

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Figures and Tables

Figure 1: Invalidation process and selection stages

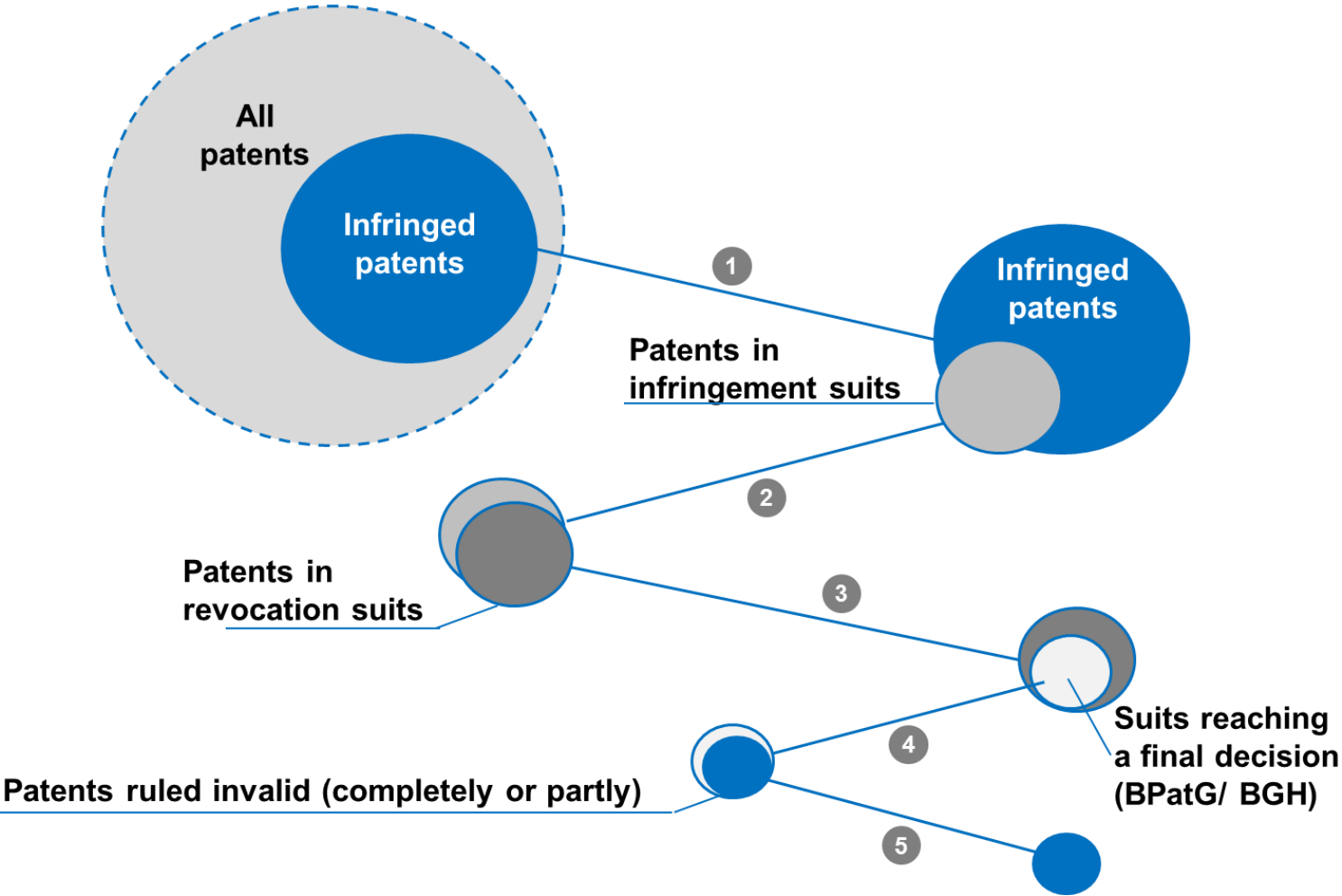
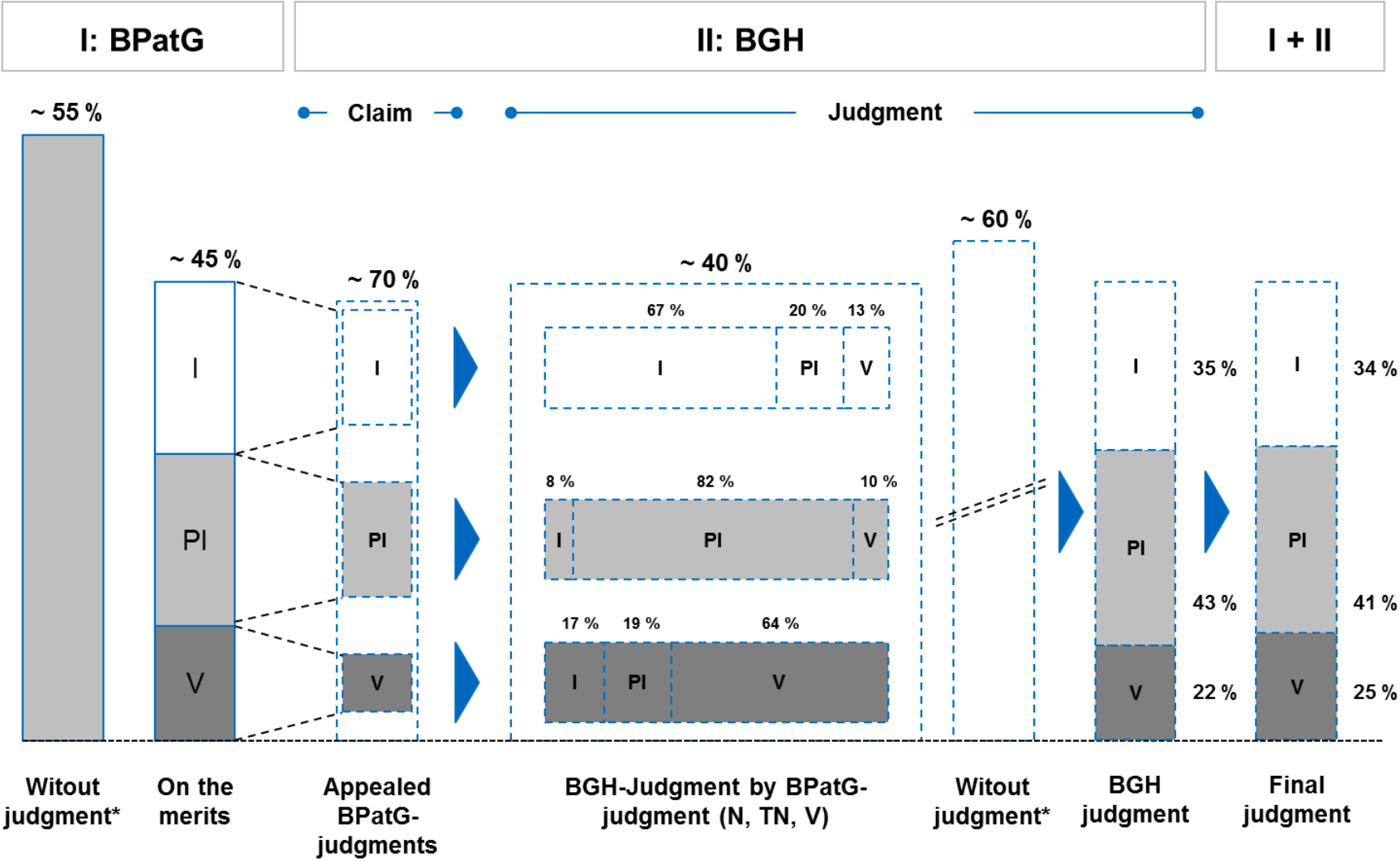


Figure 2: Process and statistics of German revocation actions



*Including withdrawals of the claim, settlements and pendings

I=Invalid; PI=Partially Invalid; V=Valid

Table 1: Revocation rates across the instances

	I. Instance			II. Instance			I. Instance or II. Instance		
	DE	EP	Total	DE	EP	Total	DE	EP	Total
Decision									
<i>Valid</i>	35%	25%	24%	18%	23%	22%	24%	26%	25%
<i>Partially Revoked</i>	38%	36%	37%	47%	42%	43%	42%	40%	41%
<i>Fully Revoked</i>	37%	39%	39%	34%	35%	35%	34%	34%	34%

Table 2: Revocation rates across industries

	Industries					
	Electrical engineering	Instruments	Chemistry	Mechanical engineering	Other fields	Total
Decision						
<i>Valid</i>	24%	18%	16%	30%	30%	24%
<i>Partially Revoked</i>	32%	43%	40%	36%	34%	37%
<i>Fully Revoked</i>	44%	39%	44%	34%	36%	39%
Total	18%	13%	19%	34%	16%	100%

Table 3: Survey results

<i>Legal robustness: Patents in infringement/ revocation proceedings, compared to average patent:</i>									
	significantly less valid (-2)	somewhat less valid (-1)	roughly same validity (0)	somewhat more valid (+1)	significantly more valid (+2)	N	Median	Mean	Wilcoxon signed-rank test
<i>Infringement proceedings</i>	3%	5%	66%	22%	4%	295	0	0.2	0.000
<i>Revocation proceedings</i>	2%	11%	70%	14%	3%	293	0	0.044	0.243
<i>Firm size/budget: Influence of parties' size on likelihood of invalidation: The likelihood of invalidation...</i>									
	significantly decreases (-2)	considerably decreases (-1)	does not increase (0)	somewhat increases (+1)	significantly increases (+2)	N	Median	Mean	Wilcoxon signed-rank test
Size Plaintiff	0%	4%	76%	16%	4%	229	0	0.19	0.000
Size Defendant	0%	9%	82%	8%	1%	228	0	-0.01	0.653
<i>Firm size/budget: Influence of plaintiff's budget on likelihood of finding relevant prior art:</i>									
<i>Plaintiff's budget</i>	0%	0%	6%	47%	47%	294	1	1.40	0.000
<i>For cases that settle: what would have been the outcome in case of a decision compared to proceedings ending with a decision?</i>									
	significantly less likely (-2)	somewhat less likely (-1)	roughly same probab. (0)	somewhat more likely (+1)	significantly more likely (+2)	N	Median	Mean	Wilcoxon signed-rank test
<i>Probability of partial invalidation</i>	0%	9%	39%	35%	17%	202	1	0.59	0.000
<i>Probability of complete invalidation</i>	5%	14%	41%	34%	5%	202	0	0.20	0.001
<i>Newly found prior art vs. differing evaluation standards: Reasons for invalidation by Federal Patent Court after grant by patent office:</i>									
	not at all important (1)	low importance (2)	somewhat important (3)	important (4)	very important (5)	N	Median	Mean	One-sample t test
<i>Newly found prior art</i>	0%	1%	2%	47%	50%	289	4	4.46	0.000
<i>Differing Evaluation Standards</i>	1%	4%	44%	46%	5%	274	4	3.51	0.000