UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

RAI STRATEGIC HOLDINGS, INC. and R.J. REYNOLDS VAPOR COMPANY Plaintiffs and Counterclaim Defendants, v. ALTRIA CLIENT SERVICES LLC; PHILIP MORRIS USA INC.; and PHILIP MORRIS PRODUCTS S.A. Defendants and Counterclaim Plaintiffs.	Case No. 1:20-cv-00393-LO-TCB

PHILIP MORRIS' BRIEF ON JURY INSTRUCTIONS AND THE VERDICT FORM PERTAINING TO THE PERMISSIBLE MEASURE OF DAMAGES

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TABLE OF CONTENTS

Page

I. INTRODUCTION 1

II. FACTUAL BACKGROUND 2

A. Reynolds Never Disclosed A Lump Sum Theory 2

B. Reynolds' Revised Proposed Verdict Form Identified A "Lump Sum For Life Of Patent" For The First Time 5

III. LEGAL STANDARD 6

IV. ARGUMENT 6

A. Reynolds' Proposed Jury Instruction and Verdict Form Regarding Any Lump Sum Damages Should Be Struck 7

B. There Is No Evidence Supporting A Lump Sum Royalty 12

V. CONCLUSION 15

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I. INTRODUCTION

The Court instructed the parties to submit any briefs related to the jury instructions and the correct form of damages by 1:00 p.m. on June 11, 2022, and that there would be no response briefs. Philip Morris respectfully submits this brief to the Court on Jury Instruction No. 47 and the Verdict Form regarding the permissible measure of damages in this case.

Based on the revised proposed verdict form that Reynolds filed on June 8th, Philip Morris expects Reynolds to ask the Court to permit it to argue—for the first time in this case—that the jury should award lump sum damages "for the life of [the] patent." Dkt. 1302 at 1, 3. This is the definition of trial by ambush, and represents the latest in a line of improper efforts by Reynolds to avoid the impacts of the rulings by Judge O'Grady and this Court striking its damages expert's third supplemental report on the Fontem-negotiation documents. It should not be permitted. Reynolds never disclosed this theory ***before trial***. In fact, until three days ago, Reynolds had consistently advanced the opposite position: that damages should be based on a ***running*** royalty, not a lump sum. And, the prayer for relief in Philip Morris' claims expressly seeks two equitable remedies (supplemental damages and/or an accounting, and a permanent injunction) that are incompatible with a lifetime royalty and cannot be decided by a jury. Dkt. 199 at 83-84, Dkt. 483. Reynold's effort to seek any lump sum royalty (particularly a life-of-the-patent lump sum) is untimely and should be struck. FED. R. CIV. P. 26, 37. Even if Reynolds had preserved this theory, it is unsupported by any record evidence, incompatible with Plaintiff's prayer for equitable remedies, and therefore improper as a matter of law.

The Court should bar Reynolds from arguing that damages can be based on a paid-up, lump sum royalty, and strike the proposed lump sum question in Reynolds' revised proposed verdict form (Dkt. 1302).

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II. FACTUAL BACKGROUND

A. Reynolds Never Disclosed A Lump Sum Theory

Throughout this case, Reynolds and its damages expert, Dr. Sullivan, unequivocally told both Magistrate Judge Buchanan and Judge O'Grady that the appropriate form of damages for the '265 and '911 Patents is a running royalty. Reynolds and its expert never disclosed that a lump sum royalty was appropriate for the '265 or '911 Patents, and never disclosed any such theory. They said the opposite.

Fact Discovery. On August 11, 2020, Philip Morris served an interrogatory asking Reynolds to "describe in detail ***all*** ***theories and bases*** under which [Reynolds] contend[s] damages should be measured, and explain in detail how such damages are computed." Ex. 1 (PMP's 1st Set of Interr., 8/11/20) at 7-8. On November 9, 2020, Reynolds responded that: it "expects that the royalty would be in the form of a ***running royalty*** based on Reynolds's sales." Ex. 2 (Reynolds' Supp. Resp. to Interr. 4, 11/9/20) at 4. Reynolds conceded that, should Philip Morris prevail, it "may be entitled to an ***ongoing royalty*** after final judgment until the expiration of [the] patents." *Id.* at 5. Reynolds supplemented its response ***five*** times—and never identified a lump sum theory. Ex. 3 (Reynolds' 24th Supp. Resp. to PMP's First Set of Interr. 4, 1/19/22), *passim*.

Separately, Reynolds repeatedly represented to the Court (in discovery motions) that a running royalty was the appropriate form of damages. *E.g.*, Dkt. 555 at 15. For example, Reynolds told Magistrate Judge Buchannan that "both parties" agreed a running royalty was appropriate:

> Again, Defendants concede that Rule 37's inquiry does not apply. Defendants at all times since at least November 2020 knew that the Fontem-RJRV agreement's lump-sum payment would need to be converted to a running royalty, as both parties contended that the Fontem-RJRV agreement was relevant, and both parties contended the proper form of damages was a running royalty. Well before February 24, 2021, Defendants possessed all the documents necessary to

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Dkt. 591 at 23; *see also id.* at 17.

Expert Discovery. Consistent with Reynolds position and representations to the Court in fact discovery, Reynolds' damages expert never opined that a lump sum royalty was appropriate for the '265 or '911 Patents. He said the opposite. In his report, Dr. Sullivan opined that "a running royalty is the economically appropriate royalty structure in this case."

> (213) Several factors indicate that a running royalty is the economically appropriate royalty structure in this case. A running royalty structure allows for payments to be commensurate with the actual value contribution of the technology over time as sales may grow or shrink due to marketplace factors and/or other factors. A running royalty also allows for the sharing between licensor and licensee of risks associated with overpayment or underpayment relative to the value earned in the marketplace on licensed products.[439] Furthermore, Reynolds tracks revenues and unit sales for the accused products, facilitating application of a running royalty.[440]
>
> (214) Accordingly, it is likely that the parties at the hypothetical negotiation would have agreed to a running royalty, either as a percentage of net sales or as a per-unit royalty.

Ex. 4 (Sullivan Rbt. Rpt.) ¶¶ 213-14; *see also, e.g.*, *id.* ¶ 268 ("[A] ***running royalty*** is likely the most appropriate royalty structure in this case."); *id.* at ¶ 315 (same).

Consequently, Dr. Sullivan calculated damages for the '265 and '911 Patents based only on "a percentage ***running royalty***" using the Fontem-Reynolds Agreement. *Id.* ¶¶ 273, 368 ('265 Patent), 280, 369 ('911 Patent). He supplemented his opinions ***seven*** times. He never changed his opinion that "a ***running royalty*** is likely the most appropriate royalty structure." *Id.* ¶ 268.

Instead, at his May 11, 2021 deposition, Dr. Sullivan testified unequivocally that he believes a running royalty is the appropriate form of damages in this case:

> Q. Now, you and Mr. Meyer agree that a running royalty is the economically appropriate royalty structure for each of the five asserted patents; correct?
>
> A. I do recall that is Mr. Meyer's opinion. ***And I agree that a running royalty structure is the most likely outcome***. It is economically reasonable.

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