



UPC_CoA_217/2024
APL_25919/2024
UPC_CoA_219/2024
APL_25923/2024
UPC_CoA_221/2024
APL_25926/2024

ORDER
of the Court of Appeal of the Unified Patent Court
issued on 17 September 2024
concerning security for costs (R.158 RoP)

HEADNOTE

- The Court, when exercising its discretion under Art. 69(4) UPCA and R.158 RoP, must determine, in the light of the facts and arguments brought forward by the parties, whether the financial position of the claimant gives rise to a legitimate and real concern that a possible order for costs may not be recoverable and/or the likelihood that a possible order for costs by the Court may not, or in an unduly burdensome way, be enforceable.
- The burden of substantiation and proof why an order for security for costs is appropriate in a particular case is on the defendant making such a request. Once the reasons and facts in the request have been presented in a credible manner, it is up to the claimant to challenge these reasons and facts in a substantiated manner, especially since that party will normally have knowledge and evidence of its financial situation. It is for the claimant to argue that and why a security order would unduly interfere with its right to an effective remedy.
- The relative financial position of the claimant as compared to that of the defendant is not as such a criterion under R.158 RoP, especially where the (limited) level of funding provided to a special purpose patent enforcement entity is a deliberate business decision.

KEYWORDS

- Security for costs (Art. 69(4) UPCA and R.158 RoP), burden of substantiation and proof

APPELLANT / DEFENDANT IN THE MAIN PROCEEDINGS BEFORE THE COURT OF FIRST INSTANCE

Audi AG, Ingolstadt, Germany

hereinafter also referred to as: 'Audi';

represented by: attorneys at law Dr. Jan Bösing, Saskia Mertsching, Monika Harten, Bardehle Pagenberg, Munich, Germany

RESPONDENT / CLAIMANT IN THE MAIN PROCEEDINGS BEFORE THE COURT OF FIRST INSTANCE

Network System Technologies LLC., Portland, ME, Unites States of America

hereinafter also referred to as 'NST';

represented by: attorney at law Dr. Thomas Gniadek, Simmons&Simmons, Munich, Germany

PANEL AND DECIDING JUDGES

This order has been adopted by the Second Panel:
Rian Kalden, Presiding judge and judge-rapporteur
Ingeborg Simonsson, legally qualified judge
Patricia Rombach, legally qualified judge

IMPUGNED ORDERS OF THE COURT OF FIRST INSTANCE

- Date: 23 April 2024 (signed 25 April 2024)
 - ORD_12232/2024 in related proceedings (requests for security for costs) App_11453/2024 in the main infringement action ACT_597692/2023)
 - ORD_17417/2024 in related proceedings (requests for security for costs) App_11456/2024 in the main infringement action ACT_597693/2023)
 - ORD_12484/2024 in related proceedings (requests for security for costs) App_11444/2024 in the main infringement action ACT_597691/2023)
- Action numbers attributed by the Court of First Instance Munich Local Division:
 - UPC_CFI_514/2023
 - UPC_CFI_515/2023
 - UPC_CFI_513/2023

PATENTS AT ISSUE

EP 1 875 683
EP 1 552 399
EP 1 552 669

LANGUAGE OF THE PROCEEDINGS

English

ORAL HEARING

The oral hearing (in-person) took place on 20 August 2024.

SUMMARY OF FACTS AND PARTIES' REQUESTS

1. On 1 March 2024 Audi filed Applications under Art. 69 (4) UPCA and R.158.1 RoP (App. 11453/2024, App. 11456/2024 and App. 11444/2024), requesting the Munich LD to order NST to provide adequate security for legal costs and other expenses incurred by Audi. The Munich LD denied the Applications. Leave to appeal was granted in the order.
2. In summary the Munich LD considered as follows:
 - a. Factors to be taken into account when issuing an order for security include the financial position of the other party which may give rise to a legitimate and real concern that a possible order for costs may not be recoverable and/or the likelihood that a possible order for costs by the UPC may not, or in an unduly burdensome way, be enforceable. Whether and to what extent such factors are present will have to be determined in the light of the facts and arguments put forward by the parties.
 - b. The protection of the defendant must be balanced against the burden on the claimant caused by an order to provide security.
 - c. It is for the party requesting a security order to provide facts and arguments as to why such an order is appropriate in a particular case. Accordingly, the requesting party must make a "reasoned request",

with the burden of proof generally being on the party relying on those facts (Art. 54 UPCA). On the other hand, once the facts and reasons in support of a security request have been presented in a credible manner, it is up to the responding party to challenge these facts and reasons in a substantiated manner, especially since that party will normally have knowledge and evidence of its financial situation. It is for the respondent to argue that and why a security order would unduly interfere with its right to an effective remedy.

- d. The fact that NST has its registered office in a non-EU country, i.e. in the United States, cannot be relevant, as this would be a form of a priori discrimination.
 - e. The defendants (including Audi) confined themselves to general allegations without providing any precise evidence of an actual risk of insolvency. There is no evidence that NST is or will be insolvent at the time a cost decision will be rendered.
 - f. NST's light organization is consistent with its business, which is primarily focused on managing litigation relating to the infringement of the patents comprised in the portfolio acquired from Philips.
 - g. NST's assets, on the other hand, include precisely those intangibles, which could be seized at the Defendants' initiative if the remaining part of NST's assets were to become insufficient.
 - h. No precise evidence has been provided as to the difficulty of enforcing UPC decisions on US territory. In the United States of America, judgments of foreign courts and associated cost decisions can generally be recognized and enforced. It has not been submitted or is otherwise apparent that this could be different with decisions and orders of this court or is seriously to be expected.
3. Audi has appealed and requests that the Court of Appeal
 - a. set aside the impugned order;
 - b. order NST to provide security for costs in the amount of EUR 200.000 in APL_25926/2024, ACT_597691/2023, in an amount of EUR 200.000 in APL_25923/2024, ACT_597693/2023, and in an amount of EUR 600.000 in APL_25919/2024, ACT_597692/2023 within a time period to be set by the Court;
 - c. order NST to bear the costs of the Applications both before the Munich LD and on appeal and, in the alternative;
 - d. refer the Application back for retrial.
 4. NST requests that the Court of Appeal
 - a. dismiss the appeal;
 - b. orders that Audi bears the costs of the appeal procedure.

POINTS AT ISSUE

Security for legal costs pursuant to R.158 RoP

SUBMISSIONS OF THE PARTIES

5. Audi bases its requests for security pursuant to R.158 RoP on the following - summarised - grounds.
 - a. The financial position of NST gives rise to a legitimate and real concern that a possible cost order might not be recoverable:
 - i. NST is a small company, with only two employees and an annual turnover of below EUR 10 million.
 - ii. The only business of NST is the enforcement of patents. NST does not have any physical assets, such as production facilities or means of production. The address of NST is a

coworking space. Consequently, there are likely no assets that could be used to satisfy a claim for reimbursement of costs. This remained undisputed.

- iii. There is a risk that NST files for insolvency if the claim is dismissed, to avoid cost reimbursement. Insolvency is easy as NST only has two employees and no assets.
 - iv. There are multiple patent infringement actions pending in the US and before the UPC, brought by NST, also against other companies. These proceedings are very expensive and increase the risk that NST cannot fulfill potential cost reimbursement claims of Audi in case the present complaint is dismissed.
 - v. NST's argument that provision of security would significantly limit its ability to enforce its patent rights in parallel is an acknowledgement of risk of insolvency if the infringement claim is dismissed.
 - vi. It is disputed that the patent portfolio price was significant and has relevant value; NST had not provided any proof for it and the Munich LD could not have relied on it failing such substantiation.
 - vii. Most patents are expired or will do so within the next 12 months – before the proceedings will have ended, so they present no value as security for reimbursement of costs. Cost reimbursement will arise when the infringement claim is dismissed, which means there is no infringement or the patents' invalidity is established by the court, and the value of the patents is reduced to zero.
 - viii. Enforcement through IP assets is inefficient and burdensome, as it must be done per country separately and will be impossible if the patents are held invalid.
 - ix. The LD applied an erroneous standard of burden of proof, it imposes an unrealistic burden, denying fair trial to the applicant. Evidence that NST will be insolvent when the claim is denied cannot be delivered, so it is an unfair standard. Only NST has access to further financial information and should be under a duty to produce it.
- b. The enforcement of a judgement on legal costs would not be possible for Audi or only with considerable difficulty, and high legal costs:
- i. NST is a US company with its actual administrative domicile and seat outside EU.
 - ii. In the USA the recognition and declaration of enforceability of foreign civil judgments falls within the competence of the individual States. Under the law of the individual States, a court exequatur is regularly required.
 - iii. The procedure can be lengthy and expensive, as US lawyers and courts are often not very familiar with the recognition and declaration of enforceability of foreign civil judgments. This is also recognized by national courts within the EU.
 - iv. The seat of NST outside the EU was held relevant by other UPC Local Divisions.
- c. The amounts per proceedings as requested is reasonable in view of NST's estimation of the values in dispute.

6. NST in summary argues as follows:

- a. The burden of proof is on the applicant and Audi has not sufficiently substantiated that there is a reason to provide security for costs.
 - i. An SME should not be obliged to provide security to a massive automotive company in view of the interest of protection of IP rights (as stated in the Enforcement Directive) and the public (EU) interest to support SMEs, as it may prevent SMEs to assert IP rights.

- ii. There is no factual basis to make an assessment of NST's assets and liquid funds; it is not for NST to show it has assets and funds.
 - iii. NST indeed maintains expensive litigation in the US and before this Court in parallel and has the financial resources to pay the legal fees and expenses for this. This comprehensive litigation shows NST is well-funded.
 - iv. The need for security would limit NST's ability to enforce its patents, which is needed because they have lapsed or will do so soon.
 - v. NST purchased its patent portfolio from Philips and paid a very significant price, consistent with the market price of such a high-quality patent portfolio, stemming from a European leader in high-tech innovation. The European patent portfolio itself shall be considered as a high valuable asset, which could be seized by Audi; the agreement is added as exhibit, but the purchase prices is redacted (blackened).
 - vi. The Court of Appeal can only review whether the Local Division correctly gathered the facts, observed the legal standard and stayed in the boundaries of its discretion and there are no flaws in that respect.
 - vii. Audi could have asked for production of documents relevant to NST's financial situation pursuant to R.190 RoP.
- b. there is no justification to differentiate between EU and non-EU based claimants
 - i. the UPC legislator deliberately dropped the criterion of domicile of the claimant. NST's seat cannot be taken into consideration.
 - ii. The enforcement of a decision on costs of this Court in the US is not impossible and does not face difficulties. No different concrete facts have been submitted by Audi.
 - c. NST objects to the amount of the security as requested by Audi. 50% of the requested amount would be reasonable.

GROUNDS FOR THE ORDER

- 7. The Court of Appeal agrees with the Munich LD that the Court, when exercising its discretion under Art. 69(4) UPCA and R.158 RoP, must determine, in the light of the facts and arguments brought forward by the parties, whether the financial position of the claimant gives rise to a legitimate and real concern that a possible order for costs may not be recoverable and/or the likelihood that a possible order for costs by the UPC may not, or in an unduly burdensome way, be enforceable.
- 8. The Munich LD also rightly held that the burden of substantiation and proof why an order for security for costs is appropriate in a particular case is on the defendant making such a request, but that – once the reasons and facts in the request have been presented in a credible manner – it is up to the claimant to challenge these reasons and facts and in a substantiated manner, especially since that party will normally have knowledge and evidence of its financial situation. It is for the claimant to argue that and why a security order would unduly interfere with its right to an effective remedy.
- 9. The Court of First Instance has a margin of discretion when deciding on a request for security for costs. On appeal, the review is consequently limited. However, even with this limited scope of review, the order must be set aside, as the Munich LD could not have reasonably come to its decision in view of the standard set out above and the facts of this case.

10. Audi sufficiently substantiated what efforts it made to search for all publicly available financial information on NST. In view thereof, the facts presented by Audi cannot be qualified as 'general allegations', as the Munich LD did. By requiring that Audi provide 'precise evidence' that NST 'is or will be insolvent at the time a cost decision will be rendered' the Munich LD imposed a too high standard of proof. On the basis of the information provided by Audi, which was not disputed, it was credible that NST's financial situation gave rise to a legitimate and real concern that a possible order for costs may not be recoverable. Under those circumstances, it was on NST, as the party having access to all relevant information on its financial situation, to provide further information on the availability of further assets to comply with a possible cost order. It follows that NST's argument that it was not obliged to disclose any details on the assets or funds it may have must be rejected. Since NST had not provided such information, it should have been assumed that NST did not have other relevant assets than those presented by Audi.
11. In the opinion of the Court of Appeal the Munich LD also could not have reasonably taken into account the patent portfolio acquired by NST as a sufficient source of recovery for any cost order. NST had stated that it had 'paid a very significant price, consistent with the market price of such a high-quality patent portfolio' but failed to substantiate this. In the copy of the purchase agreement, which was submitted as an exhibit, the purchase price was blackened. In addition, the purchase price paid will not be indicative of the value of the patents at the time the proceedings will have ended, as most patents are already expired or will do so within the next 12 months, as NST itself submitted.
12. Furthermore, the Munich LD failed to recognize that a cost order against NST would only arise in a situation where the infringement actions initiated by it have failed, either because there was no infringement or the patents were held to be invalid (Audi filed counterclaims and Skoda, a group company, filed revocation actions before the national courts), which would substantially lower the value of the portfolio, in case of invalidity even to zero. In considering that the patents could be seized, the Munich LD also did not take into account that enforcement through seizure of patents must be done per country separately, involving further costs and with a very uncertain return. As such, the existence of the patent portfolio does not prevent that NST's financial situation gives rise to a legitimate and real concern that a possible order for costs may not be recoverable by Audi.
13. The settlement agreements NST entered into in some other cases does not alter any of these considerations. It is insufficient indication of the (future) value of the patent portfolio and failing any details on the content of the agreements, which have not been provided, NST's mere statement that the licence fees NST will receive will be sufficient to cover the legal costs NST may be ordered to reimburse to Audi, which was disputed by Audi, cannot be relied on.
14. The Court of Appeal rejects NST's argument that a duty to provide security for costs would unreasonably deny it access to justice. NST is not blocked from filing any claims as such. NST itself submits that it is a company set up by major external funding companies, specifically for the acquisition of a patent portfolio with a view to claiming damages for past patent infringements and concluding licence agreements for future use of its patents. NST accepts that for this purpose, it should be sufficiently funded to not only pay the purchase price of the patent portfolio and its own costs of litigation, but that this funding should also be sufficient to cover the amount it may have to reimburse in case its claims are rejected and it is ordered to bear the costs of the other party.

15. If NST – as could have been expected from it – had provided sufficiently substantiated information from which it would be clear that NST would indeed have sufficient financial funding to also cover a possible cost order, then there would not be a need to order NST to provide a security for these costs. However, since NST failed to provide sufficient comfort that there is no real concern that a possible order for costs may not be recoverable, an adequate security for cost must be ordered. As NST admits that sufficient financial funding to cover any possible cost orders against it should be part of an appropriate financial funding of its business model, the obligation to provide a security for costs cannot be considered to be an additional burden that hinders NST's access to justice.
16. The Court of Appeal also rejects NST's argument that as an SME, it should not be required to provide security for costs in favour of a massive automotive company such as Audi. The relative financial position of the claimant as compared to that of the defendant is not as such a criterion under R.158 RoP. This is all the more not a factor to be taken into account where the (limited) level of funding provided to a special purpose patent enforcement entity such as NST is a deliberate business decision.
17. From the above it follows that the impugned order must be set aside. The Court of Appeal shall order NST to provide adequate security for costs to Audi. Audi has requested that the security shall be equal to 10% of the value of litigation, so for in an amount of EUR 200.000 in two cases and EUR 600.000 in the third. NST has disputed that these are reasonable amounts. It considers 50% of the requested amounts to be reasonable. The Court of Appeal agrees with this, taking into account that Audi and Volkswagen are both sued in parallel cases and use the same representatives, whose costs can be shared among them.
18. As to the form of the security, the Court of Appeals leaves it open to NST to provide security either by deposit or by a bank guarantee issued by a bank licensed in the European Union. The Court of Appeal considers a time period of three weeks from the date of service of this order reasonable.
19. There is no need to consider and decide on other issues raised, such as the relevance of NST's place of domicile in the US.
20. Audi's request for a cost order will be denied. No decision on the reimbursement of legal costs will be made in this order since this order is not a final order or decision concluding an action.

ORDER

The Court of Appeal

- sets aside the impugned order;
- orders NST to provide security for costs to Audi in an amount of EUR 100.000 in APL_25926/2024, ACT_597691/2023, in an amount of EUR 100.000 in APL_25923/2024, ACT_597693/2023, and in an amount of EUR 300.000 in APL_25919/2024, ACT_597692/2023, either by deposit or by a bank guarantee issued by a bank licensed in the European Union, within three weeks from the date of service of this order;
- rejects the requested cost order.

Issued on 17 September 2024

Rian Kalden, Presiding judge and judge-rapporteur

Ingeborg Simonsson, legally qualified judge

Patricia Rombach, legally qualified judge