Donna Kline is a reporter for *Pittsburgh Business Reports* and a former reporter for *Bloomberg* New York.

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||| Big trouble ahead for Facebook IPO?

The undisclosed patent infringement case

Updated 2/17/2012 11:53 PM—As you may know, Facebook filed for an initial public offering on February 1, 2012. What you may *not* know, is that there was a very ominous omission in the S-1:

> Facebook has been found guilty of patent infringement against Leader Technologies.

> An additional trial is set to begin March 5, 2012.

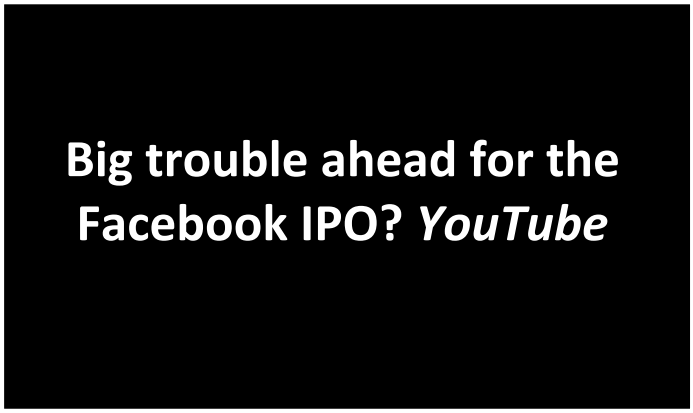

Fig. 1 – Big trouble ahead for the Facebook IPO? Donna Kline reports for *Pittsburgh Business Report* and is a former reporter for *Bloomberg*.

Yes, there are many cases pending against FB that are *alluded* to in the S-1 filing e.g.: *"We are currently, and expect to be in the future, party to patent lawsuits and other intellectual property rights claims that are expensive and time consuming, and, if resolved adversely, could have a significant impact on our business, financial condition or results of operations."* p. 19 But NOTHING that states there is **a jury verdict against them for literal infringement on 11 of 11 claims of U.S. Patent # 7,139,761.** (See *Leader Technologies, Inc. v. Facebook Technologies, Inc., 08-CV-862-LPS (D.Del. 2008)*

What is Patent # 7,139,761?

Oh, just the source code for the entire Facebook platform. **(WHAT? YOU CANNOT BE SERIOUS!!!)** Leader Technologies claims it was stolen from them during the infamous Zuckerberg hacking event at Harvard University on October 28, 2003. (See

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http://en.wikipedia.org/wiki/History_of_Facebook under FaceMash) (Also see http://www.youtube.com/watch?v=odOzMz-fOOw for the dramatization of the event. The first dormitory to pop up in this video scene is Kirkland House, which *happens* to be the dorm next to Winthrop House where Leader Technologies CEO, Michael McKibben's, son lived.)

McKibben explains that he had sent the technical white paper describing key components of their invention to his son via Email on October 22, 2003. This email was in his son's Winthrop inbox during the hacking event mentioned above. **A patent for this technology had been filed on December 11, 2002.** The white papers had **'Copyright 2003, Leader Technologies Incorporated, PATENTS PENDING, All Rights Reserved.'** clearly printed in the footer of each page. (See Leader White Paper, Oct. 22, 2003, Doc. No. 477; See also Archive.org.)

In October of 2003, Leader Technologies was conducting confidential clinical trial beta tests with Boston Scientific, including Cleveland Clinic and clients of *Accel Partners*. Accel is heavily peopled with Harvard graduates. Accel's official story is that managing partner James Breyer first met Zuckerberg in early 2005 – almost a year after Zuckerberg moved to California. However, given Breyer's close Harvard connections this official story is dubious in view of the stupendous *The Harvard Crimson* coverage given to Zuckerberg as a 19 year old student (See below), and his business partner Peter Theil's $500,000 investment in Zuckerberg a year earlier in June 2004. (http://ecorner.stanford.edu/authorMaterialInfo.html?mid=1567).

(www.accel.com)

Accel Partners' website currently states they "partner with entrepreneurs around the world who have unique, breakthrough ideas and the courage to be *first*." Translation, they provide capital, *publicity* and direction for their clients. Interestingly enough, from October 1, 2003 to June 1, 2004, "Zuckerberg" and "thefacebook" have more citations in *The Harvard Crimson* than President George Bush or Google. And many more than "Winklevoss" or "Harvard Connection" who were in the beginnings of an investigation against Zuckerberg at that time. (See http://www.thecrimson.com/search/.) Facebook launched in February and incorporated in June 2004.

Accel's total holding in Facebook, including individual partners through various investing entities, is difficult to determine from the S-1 filing, but appears to exceed 15% ownership in Facebook. See *Crunchbase*.

Just the beginning

On June 24, 2004, Leader Technologies' patent application published. Zuckerberg has testified that Facebook's "groups" functionality was programmed in the summer of 2004 by an *intern* named Steven Dawson-Haggerty. (See http://www.scribd.com/doc/61612724/The-Facebook-vs-ConnectU-Mark-Zuckerberg-Deposition-April-25-2006 p. 91) There are '*complexities*' revealed in the deposition cited above. Namely, on pages 40 and 41, Zuckerberg states that he began writing the code for Facebook sometime in January of 2004, while taking a full class load

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at Harvard. Facebook launched on February 4, 2004. Zuckerberg says that he wrote the code for Facebook in "somewhere between a week and two weeks…" (**WHAT**???) And, that an *intern* was somehow able to write the code for the "groups" component over summer vacation. (**ARE YOU KIDDING ME?) (**See **http://facebook-technology-origins.blogspot.com/2011/08/mark-zuckerberg-used-leader-white-paper.html.)** Zuckerberg also testified in the ConnectU trial that there were other sources of information that he lifted, but cannot remember what they are. (p. 36)

Anyone with a programming background knows that it takes *much* longer to program and test code of this nature. Leader Technologies invested *145,000 man-hours and 10 million dollars* into creating their invention by late 2002. They have argued that the similarities between their product and the engine running Facebook are eerily too similar. (**And they won**.)

Legal Battle Timeline

* Leader Technologies is awarded patent # 7,139,761 Nov. 21, 2006. * Leader files patent infringement suit against Facebook on Nov. 19, 2008 (*Leader Technologies Inc., v. Facebook Technologies Inc., 08-CV-862-LPS (D.Del. 2008)* * Trial begins on July 19, 2010 * Jury returns a *split verdict* on July 28, 2010. Leader prevails on "literal infringement" of all 11 of 11 claims of patent infringement and no published prior art. Facebook prevails on "on sale bar." (See http://www.leader.com/docs/Leaderpressrelease-07-29-10-LeaderFacebookSplitVerdict.pdf.)

How it all went down

In a patent litigation, the plaintiff (Leader) has one primary goal: to prove that they were, in fact, the original inventor, and that the defendant (Facebook), infringed their patent. The defendant, on the other hand, can attempt to prove that either: 1) the patent was not infringed 2) the patent is unenforceable or 3) the patent was never valid. Many law firms will tell you that it is the party with "the most money and resources that is ultimately the victor." (See http://www.ip-holdings.com/patent-infringement-litigation-patent-lawsuit.)

Quick Tutorial

During the 'discovery period' of a lawsuit, the plaintiff and defendant learn as much as they can about the other party's claims and defenses. Discovery can occur through; 1) Interrogatories – written questions to the opposing party; 2) Requests for documents and/or 3) Depositions. The discovery period is designed to eliminate "surprises" and clarify what the lawsuit is about.

Plan A – False Marking

During the discovery period of *Leader v. Facebook,* Facebook attorneys were pursuing a claim that accused Leader of 'false marking', which essentially claims that Leader didn't invent *anything* – they merely affixed a patent symbol to material and code that was already in existence. (See US Patent Office Examiner's Manual – False Marking and "No evidence? No problem. Fabricate it.".) Facebook attorneys requested access to LeadertoLeader source code. (See item 8 at Leader's lawyers dismantle Facebook's "schizophrenic" response brief.) They stated that it was

impossible for them to do an element-by-element analysis without access to the code. Leader obliged and made the code available pursuant to the court's order. **(After all that, this code was never brought up again as evidence against Leader.)**.

Plan B – On Sale Bar or "The Old Switcheroo"

On July 17, 2010, after the discovery period had closed and three months before trial began, Facebook attorneys asserted the "on sale bar" claim against Leader. This accusation is exactly the opposite of the original claim. "On sale bar" means that the inventor cannot offer his patent for sale more than 12 months before the patent application is filed. In other words, the invention *did* exist and was sold too early. (See US Patent Office Examiner's Manual – On Sale.) Here is an excerpt from Leaders appellate brief currently on file and set to begin arguments March 5, 2012:

> "From March through November 2009, Facebook served multiple interrogatory responses regarding its invalidity contentions; not once did it mention the on-sale or public-use bars. Instead, Facebook filed a false-marking counterclaim in December 2009 alleging that Leader had falsely marked Leader2Leader as embodying the patented invention because, in Facebook's view, "Leader2Leader *does not practice* the invention disclosed by the claims of the '761 patent." JA4355 (emphasis added). Consistent with that position, Facebook's expert report on invalidity, submitted in April 2010 after the close of fact discovery, did not assert invalidity under the public-use and on-sale bars. Just three months before trial and after the close of discovery, however, Facebook made an about-face. In its third supplement to an interrogatory response, Facebook asserted that Leader2Leader did embody the patented invention after all, that it had done so since some unspecified time before December 11, 2002, and that public demonstrations and offers for sale of Leader2Leader before that date rendered the patent invalid. The district court denied Leader's motion *in limine* to exclude that eleventh-hour defense. *See* JA225 (DI 683); *see also* JA13142." (See http://www.scribd.com/doc/61125483/Leader-v-Facebook-APPEAL-Leader-Opening-Brief-July-25-2011 p. 9.)

The above is "legalese" for Facebook alleging one defense, seeking evidence for that defense, then ultimately choosing the *opposite* tactic during trial. Courts are not supposed to permit new claims so close to trial when a party is prejudiced, but this court did—after discovery had closed.

Trial Begins

Now that Facebook's "clear and convincing" burden is to "prove" that Leader offered its product for sale more than a year before filing the patent, you would expect them to show Leader's source code and expert testimony to back their case. They did not. (See http://www.scribd.com/doc/61256189/Leader-v-Facebook-FULL-DOCKET-Case-08-cv-862-JJF-LPS-D-Del-2008.)

Leader had conducted *beta tests* in October of 2003. These tests are designed to see if the software meets the requirements that guided its design and development; works as expected; and/or can be implemented with the same characteristics. Participants included The Limited, Wright Patterson Air Force Base and Boston Scientific (including Accel clients.) Leader's non-disclosure agreements signed by the participants contained a special

provision called a “no-reliance” or “no legal effect” clause that specifically *prevents* preliminary discussions from being construed as offers. (i.e. product for sale.) Since Facebook’s “on sale bar” claim was added after the close of discovery, Leader had no opportunity to prepare customary defenses for these claims. This normally includes gathering hard evidence like expert testimony, engineering records, depositions of the alleged customers, and most importantly, source code. All Facebook had were some emails making reference to various Leader brand names, no source code, no nothing except altered evidence and snippets of video. **CLEAR AND CONVINCING EVIDENCE? ARE YOU KIDDING ME???**

Interrogatory No. 9

This section related to questioning whether or not Leader’s software products in 2009 practiced the invention (source code) for false marking. Facebook chose to re-purpose this question and allege that it also applied to Leader’s product in 2002. They chose this path AFTER they failed to prove “false marking” of the patent The U.S. Constitution, in Article 1, Section 8 explicitly protects authors and inventors:

> “To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive right to their respective Writings and Discoveries.”

http://facebook-technology-origins.blogspot.com/2012/01/facebooks-tricks-with-key-evidence.html

The Verdict

Jury returns a *split verdict* on July 28, 2010. **Leader prevails on “literal infringement” of all 11 of 11 claims of patent infringement and no published prior art.** Facebook prevails on “on sale bar.” (See http://www.leader.com/docs/Leaderpressrelease-07-29-10-LeaderFacebookSplitVerdict.pdf.) Leader files an appeal on July 25, 2011 at the Federal Circuit Court of Appeals in Washington D.C.

Back to the S-1 Filing

Where in the Facebook S-1 filing is this ongoing lawsuit with Leader Technologies mentioned? Nowhere. Facebook *did* dedicate a paragraph to the “Paul D. Ceglia” lawsuit (in discovery) on page 93 of the S-1 filing. If you search the name Paul Ceglia, you will find that he is has convicted of possessing 400 grams of ‘magic mushrooms’, *and* has been charged with grand larceny and fraud in the state of New York. (Sounds like an upstanding guy.) But again, no mention of Leader Technologies, although **this is the first and only case against Facebook to 1) have a jury trial and 2) make it to the Federal District of Appeals.**

What’s at stake?

If Leader prevails in appeal, damages against Facebook could be 5-25% of Facebook’s gross revenues from 2006 through 2021. (YOU DO THE MATH.) And, if it is proven that Facebook has knowingly, deliberately, intentionally, willfully or wantonly infringed the patent, punitive damages can be tripled. (http://www.invention-protection.com/ip/publications/docs/Damage_Relief_for_Patent_Infringement.html.)

Materiality?

In the S-1, Facebook alludes to ongoing lawsuits that may be "expensive and time consuming" but makes no mention of the *Leader v. Facebook* trial set to begin on March 5, 2012. The Federal District Court of Appeals is the second highest court in the United States. The S-1 rule is that the applicant is required to disclose all *material* litigation. Material in this case must *surely* include the first and only litigation against Facebook to be pending in a Federal Appeals Court. In other words, the company cannot hide from investors the risks associated with a pending lawsuit that may have significant negative impact on shareholder value if Facebook loses. And certainly a pending injunction that could shut them down.

* * *

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Posted by Donna Kline on Sunday, February 12, 2012, at 4:36 pm.
Filed under Investigation.
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Comments

1. **KC-CA** | February 13, 2012 at 10:16 am | Permalink
Hi Donna,

Some of my business friends in California have been following Leader vs. Facebook and were utterly dumbfounded when they read Facebook's gyrations to avoid disclosing infringement of 11 of 11 Leader patent claims. They said they would be filing complaints with the SEC.

Something doesn't smell right.

McKibben's son at Harvard at the same time as Zuckerberg – - in the next dorm! Zuckerberg claiming to have built something in one or two weeks that took Leader 145,000 man hours and 10,000,000 dollars. The "groups" feature appearing in Facebook months after the US Patent Office published it in Leader's patent application. Accel Partners and their Harvard alums laying down a false story of first encounters with Zuckerberg. Accel Partners and other insiders already cashing out much of their stock to DST, Goldman Sachs and Russian oligarchs. Do they think all us investors are dumb as rocks? They must.

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