

INTELLECTUAL PROPERTY LITIGATION

AMERICAN BAR ASSOCIATION SECTION OF LITIGATION



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ARTICLES

The Heightened Domestic-Industry Standard for NPEs

By Reza Mirzaie and Irfan A. Lateef – September 12, 2012

Historically, the International Trade Commission (ITC) has been viewed as the federal agency charged with protecting domestic manufacturing entities from unfair international trade activities, such as the importation of articles that infringe a U.S. patent. To this end, Section 337 of the Tariff Act of 1930, the statute that created the ITC, has always required that ITC complainants show they have a “domestic industry” relating to their patent. Initially, this requirement essentially forced ITC complainants to show they made substantial investments relating to the domestic manufacturing of articles covered by the patent. As a result, holders of U.S. patent rights that do not make any products, often referred to as nonpracticing entities (NPEs), were virtually excluded from seeking ITC relief.

In 1988, however, Congress changed the domestic-industry requirement to open the ITC’s doors to some NPEs, provided that the NPEs show a substantial investment in nonmanufacturing “exploitation” of their patents, which includes licensing their patent rights to others. With the rise of NPE patent litigation in the last decade, many NPEs—including those that purchase patent rights for the purpose of enforcing them against manufacturing entities—have sought out the broad exclusionary relief available in the ITC. As a result, courts have had to interpret and apply the amended domestic-industry requirement for NPEs.

Over time, the ITC has set and followed certain trends in deciding which NPE activities are sufficient to show substantial investment in licensing as required under Section 337. Early on, the ITC set forth a seemingly low standard for NPEs to satisfy. Not surprisingly, this resulted in a rise in NPE litigation in the ITC. But more recently, the ITC has clarified and, in fact, raised the standard. As a result, NPEs today must seriously weigh the benefits of seeking ITC relief against the potential risks of failing to prove the domestic-industry requirement.

How the ITC Evolved to Become a Viable Forum for NPEs

Before the creation of the ITC, patentees in the United States could only bring an infringement action in federal district court, but the onset of globalization and the corresponding rise in importation of foreign-made articles created a need for a mechanism to inhibit imported products from infringing U.S. patents. Congress, which has the unique power to both “promote the Progress of Science” and regulate commerce, responded to this need by enacting Section 337 of the Tariff Act of 1930. Over time, that legislation gave the ITC the ability to investigate complaints regarding the alleged importation, sale for importation, and sale after importation into the United States of articles that infringed a valid, enforceable U.S. patent. If the ITC finds that such unlawful activities have taken place, it can give relief to a patentee complainant by issuing an exclusion order to prohibit the importation of the infringing articles.

Unlike district court, however, not all patentees can file an action in the ITC. Rather, to prevail in an action under Section 337, a patentee must show that it has a requisite “domestic industry.” The domestic-industry requirement requires a patentee to satisfy a technical prong and an

economic prong. The technical prong requires patentees to show that their domestic investment relates to the technology claimed in their asserted patents. Before 1988, the economic prong required patentees to show a direct injury to their “efficiently and economically” operated industry in the United States. *See* Smoot-Hawley Tariff Act of 1930, Pub. L. No. 71-361, § 337(a), 46 Stat. 730 (codified as amended at 19 U.S.C. § 1337 (2006)). Patentees likewise were required to show substantial activity that employed the use of American land, labor, and capital. During this time, critics of the statute felt that the requirements under the economic prong made it too difficult for most patentees to bring an action under Section 337 and, consequently, placed too little value on protecting U.S. patent rights in the context of international trade.

In 1988, Congress answered the critics’ call by amending Section 337 to lower the threshold for meeting the domestic-industry requirement. In so doing, Congress paved the way for NPEs to bring infringement actions in the ITC. Under the 1988 amendments, which are still in effect today, Congress eliminated the requirement that asked patentees to show a direct injury to an “efficiently and economically operated” domestic industry. *See* Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418, § 1342, 102 Stat. 1107, 1213. Congress also clarified that patentees could satisfy the economic prong by showing that they have made a “(A) significant investment in domestic plants and equipment; (B) significant employment of labor or capital; or (C) substantial investment in . . . *exploitation, including* engineering, research and development, or *licensing.*” 19 U.S.C. § 1337(a)(3) (emphasis added). As a result, NPEs—which, under the previous statute, could not show an efficiently and economically operated industry that utilized American land, labor, and capital—could now satisfy the economic prong by showing substantial investment in licensing any patents they wished to assert.

The legislative history behind the 1988 amendments suggests that Congress intended to open the ITC’s doors to some, but not all, NPEs. In particular, House and Senate reports expressly state that the amendments were intended to provide relief under Section 337 to “universities and other intellectual property owners who engage in extensive licensing of their rights to manufacturers.” S. Rep. No. 100-71, at 129 (1987). But other parts of the legislative history reveal that Congress did not aim to extend such relief to just any patent holder. For example, Congress explained that the statute was never intended to protect holders of U.S. patent rights who have only limited contact with the United States and, therefore, the amendments should not be used as a loophole to the domestic-industry requirement. Congress also stated that the amendment covers those “actively engaged in steps leading to the exploitation of the intellectual property, including application engineering, design work, or other such activities.” H.R. Rep. No. 100-40 pt. 1, at 157 (1987). Thus, even under the 1988 amendments, Congress intended to limit the protection of Section 337 to those entities that made a substantial investment in domestic innovation or licensing to others for the purposes of domestic manufacturing.

The Seemingly Relaxed Domestic-Industry Requirement for NPEs

Notwithstanding the changes in the domestic-industry requirement, the ITC remained a seldom-used forum for NPEs for many years after the 1988 amendments, but with the rise of NPE litigation in the mid-2000s, several NPEs began testing the waters in the ITC. Around this time,

the ITC handed down a number of decisions that appeared to set a relatively low bar for NPEs to meet the domestic-industry requirement.

In 2009, for example, in *Certain Short-Wavelength Light Emitting Diodes, Laser Diodes, and Products Containing the Same*, Inv. No. 337-TA-640, Order No. 72 (May 8, 2009), the complainant, Professor Gertrude Rothschild, moved for summary determination that she met the economic prong through her licensing and litigation efforts. Rothschild argued that her litigation activities in district court showed “a substantial investment in enforcing her patent and furthering her licensing program.” *Id.* at 55–57. She also argued that her few licensees had made a substantial investment in manufacturing and research and development, which was sufficient to satisfy the economic prong. The administrative law judge (ALJ) agreed, finding that Rothschild’s licensing activity was sufficient to satisfy the economic prong and that she also showed proof of substantial investment through the payment of legal fees for her district-court litigation and related licensing efforts.

Later that year, in *Certain Electronic Devices, Including Handheld Wireless Communications Devices*, Inv. Nos. 337-TA-673 and 667, Order No. 49C (Oct. 15, 2009), another NPE complainant, Saxon Innovations LLC, also moved for summary determination that it satisfied the economic prong. The ALJ in that investigation granted the motion notwithstanding that Saxon had only five employees and a business model arguably focused on purchasing patents and asserting them against potential infringers. To meet its burden in the motion, Saxon relied on the activities of its sole licensee, Motorola, to whom Saxon licensed the asserted patents more than 10 years prior to filing its complaint. The ALJ agreed with Saxon’s argument and found that Motorola’s activities relating to the patented articles were sufficient to satisfy the domestic-industry requirement. Moreover, the ALJ rejected the respondents’ argument that Saxon could not meet the economic prong because it only generated licensing revenue years before the complaint was filed and did not generate a current stream of licensing revenue. The ALJ held that Saxon did not have to show a current revenue stream because Saxon was relying on the investment and activities of its licensee instead of its own licensing activity to meet the economic prong.

In light of the then-apparent trend in setting a low threshold to satisfy the domestic-industry requirement, NPEs, including foreign-based NPEs, began filing ITC complaints in unprecedented numbers. For example, while an average of four NPEs filed ITC complaints annually between 2006 and 2009, 16 NPEs filed such complaints last year. This is not surprising given that ITC litigation provides patentees with several strategic benefits over district-court litigation. These advantages include, most notably, a quicker pace from filing the complaint to trial and injunctive relief that is essentially automatic if the patentee shows an unlawful importation of infringing articles. (In the past, injunctive relief was likewise regularly granted in district court after a finding of infringement, but the 2006 Supreme Court decision in *eBay, Inc. v. MercExchange, LLC*, 547 U.S. 388, 393 (2006), changed this regime by requiring district courts to apply a more stringent test for granting injunctive relief after a finding of infringement.) Now that the ITC appeared to welcome NPE complainants into its courts, why not take advantage of its strategic benefits?

Recent Decisions Make It Tougher to Meet the Domestic-Industry Requirement

Perhaps in reaction to the anticipated rise of NPE litigation in the ITC, recent decisions have scaled back the seemingly relaxed standards set forth in pre-2010 decisions. In *Certain Coaxial Cable Connectors and Components Thereof and Products Containing Same*, Inv. No. 337-TA-650, Comm'n Op. (March 31, 2010), the complainant, PPC, filed a complaint to exclude the importation of all coaxial cables and connectors that infringed its design and utility patents. Because PPC did not practice its design patent, it tried to satisfy the domestic-industry requirement by showing a substantial investment in the exploitation of its patent through its licensing activities. Specifically, PPC argued that its past litigation expenses, incurred in pursuing three separate district court actions against the respondent and the respondent's distributor, were sufficient to show such substantial investment. The ITC rejected PPC's argument, holding that expenditures on patent litigation do not automatically constitute evidence of a substantial investment in the exploitation of a patent. Thus, the ITC held that PPC failed to show a proper nexus between its litigation expenses and a substantial investment in licensing the asserted design patent. PPC appealed to the Federal Circuit, the appellate court tasked with reviewing appeals from final determinations in the ITC.

In a 2011 opinion, a majority panel in the Federal Circuit agreed with the ITC and held that PPC's litigation expenditures were not sufficiently tied to the licensing of the asserted design patent. *John Mezzalingua Assocs., Inc., v. Int'l Trade Comm'n*, 660 F.3d 1322, 1331 (Fed. Cir. 2011). First, the Federal Circuit held that PPC did not engage in sufficient pre-litigation licensing efforts but decided to file infringement suits in lieu of such efforts. Then, the Federal Circuit reached the same conclusion with respect to PPC's post-filing licensing activities during the litigation. On this issue, the court held that the entirety of PPC's district-court litigation expenses could not be relevant to the domestic industry question because some of that litigation did not involve the asserted design patent. With respect to the litigation activities that did involve the asserted design patent, the Federal Circuit held that PPC's expenses did not amount to a "substantial investment" in licensing. The record showed that PPC's litigation resulted in only one executed license, which was only partly related to the design patent. And PPC never formally offered a license to the asserted patent during the litigation. To the contrary, it waited two full years after obtaining a district-court injunction against the respondent before seeking and obtaining that license. These facts indicated that PPC's purpose in litigating "was not to obtain a license but, rather, was to stop [the respondent] from manufacturing infringing connectors." *Id.* at 1329. Therefore, the Federal Circuit held that the ITC was entitled to conclude that the litigation expenses should not be credited as expenses related to licensing under the economic prong.

The Federal Circuit further stated that, outside of the litigation context, "PPC had no formal licensing program and that there was no evidence it had offered to license the patent to any party other than its litigation opponents." *Id.* at 1330. Here, the court did caution that "there is no rule that a single license—such as an exclusive license—cannot satisfy the domestic industry requirement based on a substantial investment in licensing." Nevertheless, based on the evidentiary record, the court held that the ALJ "was entitled to view the absence of other licenses issued or negotiated for the [asserted] design patent as one factor supporting his conclusion that

PPC’s expenditures related to licensing were not substantial.”The Federal Circuit concluded that, “[b]ased on the administrative law judge’s thorough review of the pertinent evidence . . . the Commission’s conclusion as to the licensing issue is supported by substantial evidence.” *Id.* PPC recently petitioned the Supreme Court to review the ITC and Federal Circuit decisions on the domestic-industry issue.

Later in 2011, the ITC rejected another NPE’s domestic-industry argument and further clarified the domestic-industry requirement as it relates to licensing. In *Certain Multimedia Display & Navigation Devices & Systems, Components Thereof, & Products Containing Same*, Inv. No. 337-TA-694, Comm’n Op. (Aug. 8, 2011), the complainant, Pioneer, asserted infringement of two patents related to navigation systems and attempted to show a domestic industry based on its licensing activities. The ITC held that Pioneer did not satisfy the economic prong and set forth detailed factors for consideration of the issue in future cases. First, the ITC held that a complainant seeking to rely on licensing activities must satisfy three requirements: The investment must relate to the exploitation of the asserted patent, the investment must relate to licensing, and the investment must occur in the United States. *Id.* at 7–8.

Under the first requirement, the ITC held that a complainant must show a nexus between the licensing activity and the asserted patent. When the asserted patent is part of a patent portfolio, and the licensing activities relate to the portfolio as a whole, the courts must determine the strength of the nexus between the asserted patent and the licensing activities. On this issue, the ITC provided a non-exhaustive list of factors to consider, such as whether the licensee’s efforts relate to an article covered by the asserted patent; the number of patents in the portfolio; the relative value contributed by the asserted patent to the portfolio; the prominence of the asserted patent in licensing discussions, negotiations, and any resulting licensing agreement; and the scope of technology covered by the portfolio compared to the scope of the asserted patent. *Id.* at 9. The ITC explained that the asserted patent may be shown to be particularly important or valuable within the portfolio where there is evidence that it was discussed during licensing negotiations, it has been successfully litigated before by the complainant, it is related to a technology industry standard, it is a base patent or pioneering patent, it is infringed or practiced in the United States, or the market recognizes the patent’s value in some other way. *Id.* at 10–11.

Under the second requirement, the ITC held that the activities relied on must have a sufficient nexus to licensing as opposed to other activities, per the Federal Circuit’s analysis in *Coaxial Cable*. Thus, for example, to rely on litigation expenditures, a complainant’s efforts to license a potential infringer should be ongoing, and settlement discussions should be conducted throughout the litigation process.

As for the third requirement, the ITC held that showing a sufficient nexus to the United States is a case-specific inquiry into the extent to which a complainant conducts its licensing operations in the United States. In particular, ALJs should consider the extent to which the complainant employs domestic personnel or utilizes domestic resources. This makes sense, given that an original purpose of the statute was to protect entities with domestic operations that may be harmed by the importation of infringing articles.

Further, the ITC held that “[o]nly after determining the extent to which the complainant’s investments fall within [the three] statutory parameters can we evaluate whether complainant’s qualifying investments are ‘substantial,’ as required by the statute.” *Id.* at 8. On this issue, the ITC provided several factors in determining substantiality. These include whether the complainant has exploited the asserted patents through activities such as research, development, or engineering; provides any compliance, training, or technical support for its licensees; is continuing its licensing activities; and has licensing activities that are consistent with those that are referenced favorably in the legislative history of the 1988 amendments to Section 337. *Id.*

Turning to the case at hand, the ITC held that Pioneer’s investment was not substantial because its in-house licensing activity did not have a sufficient nexus to the asserted patents. In particular, the ITC held that Pioneer’s licensing efforts were directed to its entire navigation portfolio, rather than the asserted patents, and that there was little evidence that Pioneer’s licensing efforts related to an exploitation of the asserted patents. (The ITC’s opinion in *Navigation Devices* was recently applied to deny relief to another NPE in *Certain Integrated Circuits, Chipsets, and Products Containing Same Including Televisions*, Inv. No. 337-TA-786, Order No. 19 (Fed. 15, 2012).) Further, the ITC gave little weight to Pioneer’s expenditures on outside counsel, in part because such expenditures were related to litigation. More notably, the ITC also gave reduced weight to Pioneer’s overall licensing activities because they were revenue-driven and not the “industry-creating, production-driven licensing activity that Congress meant to encourage.” Thus, the ITC signaled its disfavor toward the purely revenue-driven licensing programs employed by many NPEs today, without outright rejecting the notion that such programs may be sufficient to satisfy the domestic-industry requirement in other cases with different facts.

The Outlook for the Future

Recent decisions appear to have raised the bar for NPEs to prove domestic industry through their licensing activities. Far from having a low threshold to show domestic industry, the decisions in *Coaxial Cable* and *Navigation Devices* set forth seemingly rigid requirements that many NPEs—particularly those involved in purchasing patents and asserting them for purely revenue-driven reasons—may find difficult to satisfy.

Moreover, there is reason to believe that the ITC will likely maintain the increased level of domestic-industry scrutiny for the foreseeable future. First, as previously stated, legislative history relating to the 1988 amendments suggests that Congress intended to limit the coverage of Section 337 to NPEs that actively innovate or license their rights to others for domestic production or employment. In this regard, the increased domestic-industry scrutiny set forth in recent decisions appears to be in line with the congressional intent relating to the very amendments that allowed NPEs to litigate in the ITC. Second, the increased scrutiny will likely diminish the recent explosion of ITC complaints being filed by NPEs, particularly those with little or no connection to employment or production in the United States.

NPEs now need to think long and hard about whether they are willing to spend the resources to file an ITC complaint because there is an increased possibility that the ITC will deny the relief they seek for failure to meet the domestic-industry requirement.

Keywords: litigation, intellectual property, nonpracticing entities, domestic-industry requirement, International Trade Commission

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Making Sense of *Prometheus*

By Marc Goldman and Bradford Lyerla – September 12, 2012

Coming only two years after its decision in *Bilski v. Kappos*, 130 S. Ct. 3218 (2010), the Supreme Court's unanimous decision in *Mayo Collaborative Services v. Prometheus Laboratories, Inc.*, 132 S. Ct. 1289 (2012), constitutes the Supreme Court's latest attempt to resolve a longstanding tension in patent law concerning what subject matter is eligible for patent protection under Section 101 of the Patent Act. In the *Prometheus* decision, the Supreme Court explained the arguments for both a broad view and a narrow view of Section 101 and then set forth an approach that purported to chart an intermediate course, albeit one that narrowed the scope of patentability as compared with the view articulated by the Federal Circuit.

The Court identified two principal factors for determining whether an invention is patentable or whether it constitutes a nonpatentable “law of nature, natural phenomenon or abstract idea”: whether, after setting aside any law of nature, natural phenomenon, or abstract idea encompassed in the claim, a patent contains an inventive concept and whether the patent claims fewer than all applications of the law of nature, natural phenomenon, or abstract idea. With respect to how these factors should be applied and what they mean, however, the opinion is often either vague or contradictory, providing practitioners grist to argue for or against patentability in almost any case. The vague and contradictory nature of the opinion may result from difficulties inherent in resolving the tensions in this area of the law given the tasks the Court set forth—to disallow the patentability of laws of nature, natural phenomena, and abstract ideas even when they are embodied in concrete products and processes but to avoid eviscerating all of patent law. Despite multiple decisions interpreting Section 101, the Court has yet to clearly explain how it is possible to achieve both goals in a principled fashion.

Background

Under Section 101 of the Patent Act, anyone who “invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent therefor, subject to the conditions and requirements of this title.” 35 U.S.C. § 101. While this language is very broad, the Supreme Court has long held that “laws of nature, natural phenomena, and abstract ideas” are not patentable. *Prometheus* at 1293 (citing *Diamond v. Diehr*, 450 U.S. 175, 185 (1981)). Newton, for example, could not have patented the law of gravity. *Diamond v. Chakrabarty*, 447 U.S. 303, 309 (1980). This conclusion could be said to stem from the language of Section 101—the law of gravity is not a process, machine, manufacture, or composition of matter. In *Prometheus*, however, the Court emphasized, as it had in prior cases, that, under longstanding precedent, it is not simply laws of nature, natural phenomena, and abstract ideas that are unpatentable under Section 101. Processes and products based on laws of nature, natural phenomena, and abstract ideas can themselves be unpatentable based on an “implicit exception” to Section 101. *Prometheus*, 132 S. Ct. at 1293; *see also Bilski*, 130 S. Ct. at 3225.

The Court thus rejected the approach to Section 101 advocated by the United States and many practitioners in which “virtually any step beyond a statement of a law of nature itself should transform an unpatentable law of nature into a potentially patentable application,” with overbroad or obvious claims invalidated based on other provisions in the Patent Act. The Court explained that the government’s preferred approach would be inconsistent with prior cases because it “would make the ‘law of nature’ exception to § 101 a dead letter” by confining it to claims to a law of nature itself, not to any applications of such a law. *Prometheus*, 132 S. Ct. at 1303. If, for example, an inventor discovered a law of nature and appended conventional steps to it to claim a concrete process that encompassed all applications of a law of nature, the claim would be patentable under the approach the Court attributed to the United States. In the Court’s view, there are important precedential and policy reasons why this should not be. The Supreme Court’s prior cases, *Prometheus* explained, “warn us against upholding patents that claim processes that too broadly preempt the use of a natural law.” *Id.* at 1294. That is because the monopolization of basic tools of scientific work, such as natural laws, would impede innovation rather than promote it. *Id.* at 1293, 1304. Sections of the Patent Act other than Section 101 cannot protect this important goal. A claim appending routine steps to a newly discovered law of nature would not be invalidated as obvious under Section 103, for example, because the law of nature itself would not previously have been described in the art. *Id.* at 1303–04.

The Court simultaneously emphasized, however, that its prior decisions recognize “that too broad an interpretation of this exclusionary principle [the law of nature exception] could eviscerate patent law. For all inventions at some level embody, use, reflect, rest upon, or apply laws of nature, natural phenomena, or abstract ideas.” *Id.* at 1293.

In explaining the balanced approach the Court attributed to its prior decisions, the Court pointed to two cases that have long been thought to reflect opposed views of patentability. In the first, *Parker v. Flook*, 437 U.S. 584 (1978), the Court found unpatentable a process that used a novel mathematical algorithm to adjust “alarm limits” in the catalytic conversion of hydrocarbons based on temperature readings. Even though the claims used the algorithm as part of a process that produced useful results, the Court found that the steps in the claim aside from the formula were so well known that there was no inventive concept aside from the formula. *Id.* at 586, 589–90, 594.

In the second case, *Diamond v. Diehr*, 450 U.S. 175 (1981), the Court found patentable a process for curing rubber in which a computer plugged certain inputs into a new mathematical equation and, based on the results, determined the proper time to signal a device to open a press. The Court held that the invention was based on an abstract idea (an algorithm) and that the fact that the steps beyond the algorithm might not be novel was irrelevant. Inventions must be considered as a whole, and the invention of *Diehr* was novel when considered in that way. *Id.* at 188–89. The Court explained that “[t]he ‘novelty’ of any element or steps in a process, or even of the process itself, is of no relevance in determining whether the subject matter of a claim falls within the § 101 categories of possibly patentable subject matter.” *Id.* Moreover, if Section 101 required an assessment of whether elements other than the algorithm were novel, this “would, if carried to its extreme, make all inventions unpatentable because all inventions can be reduced to

underlying principles of nature that, once known, make their implementation obvious.” *Id.* at 189.

For years, *Diehr* was seen by many as largely repudiating the result in *Flook*. After *Diehr*, a series of Federal Circuit cases found processes patentable so long as they produced useful, tangible, and concrete results, *see, e.g., State St. Bank & Trust Co. v. Signature Fin. Group*, 149 F.3d 1368, 1373 (1998). The Federal Circuit concluded in *Bilski* that this test was too broad, and replaced it with a test that continued to permit patentees to claim broad applications of abstract ideas or natural laws so long as the ideas/laws were implemented on a machine or involved the transformation of matter. *In re Bilski*, 545 F.3d 943, 954 (Fed. Cir. 2008) (*en banc*).

In reviewing the Federal Circuit’s decision in *Bilski*, the Supreme Court began breathing life back into *Flook*, a process it continued in *Prometheus*. In *Bilski*, the Supreme Court concluded that the Federal Circuit’s machine or transformation test was too narrow—a process could be patentable even if it did not occur on a machine or transform matter. However, the Court held that the particular process at issue in *Bilski* was not patentable because it consisted principally of the abstract idea of hedging risk reduced to a mathematical formula and that the inclusion of “token postsolution components” in some of the patent’s claims did not render it patentable. *Bilski*, 130 S. Ct. at 3231. In holding that post-solution activity is insufficient, the Supreme Court relied on *Flook*, but this holding was also cited in *Diehr*.

In *Prometheus*, the Court relied even more centrally on *Flook* while simultaneously relying on *Diehr*. It charted a course that purported to be consistent with both decisions and thus to serve the goal of preventing the patentability of claims that too broadly preempt a law of nature without eviscerating all of patent law. In doing so, however, the Court failed to articulate a clear way forward, providing grist for practitioners to argue both for and against patentability in almost any case.

The Holding of *Prometheus*

The patent at issue in *Prometheus* claimed a process that involved the administration of thiopurine drugs to a patient, the measurement of the level of a metabolite produced in the patient, and the consideration of that level in deciding proper dosage for the patient based on research findings involving correlations between metabolite levels and likely harm or ineffectiveness of the drugs. (The patent did not actually direct consideration of the metabolite levels in treatment; it instead said that certain levels indicated a need to increase or decrease dosage. The Supreme Court, however, treated the patent as one specifying consideration of the metabolite levels in treatment.) The Federal Circuit found that administration of the drugs transformed the human body, the determination of metabolite levels transformed the blood, and these transformations, considered as a clue to patentability, were sufficient to establish that the claims do not preempt laws of nature. *See* 581 F.3d 1336, 1345–47 (2009); 628 F.3d 1347, 1355 (2010).

The Supreme Court reversed. The claimed process involving the transformation of matter did not establish patentability, the Court said, because, among other things, the machine-or-transformation test does not trump the law-of-nature exclusion. *Prometheus*, 132 S. Ct. at 1296.

According to the Court, the law-of-nature exception came into play because the correlation between metabolite levels and drug toxicity constitutes a law of nature. *Id.* at 1297–98, 1302.

The other steps in the claimed process did not save the patent. They:

Add[ed] nothing specific to the laws of nature other than what is well-understood, routine, conventional activity, previously engaged in by those in the field. And since these [we]re steps that must be taken in order to apply the laws in question, the effect [wa]s simply to tell doctors to apply the law somehow when treating their patients.

Prometheus, 132 S. Ct. at 1302.

Thus, the Court set forth two critical factors in assessing patentability. The first was whether the steps added to the law of nature constitute “routine, conventional activity” (*Id.* at 1298) or instead are “inventive” (*Id.* at 1299) (the inventiveness prong). The second was whether the steps added to the law of nature are ones that must be taken to apply the laws in question (the limitations prong). *See also id.* at 1294 (characterizing prior cases as warning against upholding claims “that too broadly preempt the use of a natural law” and requiring that claimed processes contain an “inventive concept.”) (quoting *Flook*, 437 U.S. at 594). *Prometheus*’s claims thus violated the principle “that simply appending conventional steps, specified at a high level of generality, to laws of nature, natural phenomena and abstract ideas cannot make those laws, phenomena and ideas patentable.” *Prometheus*, 132 S. Ct. at 1300.

Because of the Court’s emphasis on the inventiveness of steps beyond the law of nature, *Prometheus* can be read as a return to *Flook*. That, however, would leave almost every patent claim vulnerable to challenge based on the issue identified in *Diehr*. If courts evaluate whether a claim is inventive *aside* from any laws of nature or abstract ideas embodied in the claims, it may be that very little is patentable. Such an approach provides practitioners seeking to argue against patentability a basis to do so in almost every case. But the Court simultaneously said that it did not intend such a result. Practitioners arguing in favor of patentability can rely on this intention to argue against any interpretation that would lead to this result. They can do so by arguing that, even if the only claim steps considered are those aside from a law of nature and even if such steps will rarely be novel, these steps can nonetheless be inventive, and a claim can be patentable if it meets the limitations prong even if it does not meet the inventiveness prong.

The Inventiveness Prong

Reading the Inventiveness Prong to Render Almost Any Claim Unpatentable

Practitioners seeking to challenge a claim as unpatentable can argue that *Prometheus* constitutes a return to the principles of *Flook* while simultaneously arguing that, when these principles are applied, virtually nothing is patentable. In addition to the language the Court used in specifically invalidating *Prometheus*’s patent, there are numerous passages throughout the opinion that suggest that, in assessing the inventiveness of a claim for purposes of Section 101, a court should set aside any law of nature or abstract idea encompassed in the claim and look only at the additional steps to determine whether they are novel. For example, the Court favorably cited

Flook itself as based on the principle that claiming steps beyond use of a mathematical algorithm does not render a claim patentable if these steps are “‘well known,’ to the point where, putting the formula to the side, there was no ‘inventive concept’ in the claimed application of the formula.” *Prometheus*, 132 S. Ct. at 1299 (quoting *Flook* at 589, 590). Similarly, the Court approvingly cites an old English case (*Neilson v. Harford*, Web. Pat. Cases 295, 371 (1844)) that treated a principle discovered by the inventor “as if the principle [were] well known” and then assessed patentability based on whether the additional steps constituted an inventive way of applying that principle—seemingly in direct conflict with the teaching of *Diehr* that novelty should be assessed based on the invention as a whole. *Prometheus*, 132 S. Ct. at 1300 (citing *O’Reilly v. Morse*, 56 U.S. 62, 114–15 (1854)). Indeed, *Neilson* was cited in *Flook* for the proposition that patentability must be evaluated based on an assumption that the law of nature or abstract idea is well known with the separate steps then evaluated to determine whether they are inventive. *Flook*, 437 U.S. at 592.

In addition, *Prometheus* explained the result in *Diehr* without reliance on what has long been thought to be *Diehr*’s core holding: that the novelty of patent claims must be assessed as a whole. *Prometheus* said that the claims in *Diehr* were patentable because the steps that were combined with the algorithm in the claims “apparently added to the formula something that in terms of patent law’s objectives had significance—they transformed the process into an inventive application of the formula.” *Prometheus*, 132 S. Ct. at 1299. In other words, *Prometheus* explained *Diehr* with a focus on the effect of the steps that were combined with the algorithm in the claim, not with reference to the claim as a whole (although it did cite *Diehr*’s holding regarding whole claims).

Prometheus also asserted that, for purposes of Section 101, it would be inadequate to assess the inventiveness of a patent claim by analyzing a patent claim as a whole. In rejecting the United States’ proposed approach in which “virtually any step . . . [w]ould transform an unpatentable law of nature into a potentially patentable application” with overbroad or obvious claims invalidated based on other provisions in the Patent Act, the Court emphasized that these other sections would not suffice. *Id.* at 1303–04. As discussed at the outset, the Court concluded that the non-obviousness requirement would not suffice to weed out claims that append conventional steps to a newly discovered law of nature. *Prometheus*, 132 S. Ct. at 1304. Analyzed as a whole, a claim that merely appends conventional steps to a law of nature would not be obvious if the claimed law of nature itself was newly discovered. *Id.* (“Intuitively, one would suppose that a newly discovered law of nature is novel.”). And such claims *should* be weeded out as nonpatentable, in the Court’s view. Otherwise, careful drafting could permit inventors to claim all applications of a law of nature merely by appending conventional steps to their claims. *Id.* at 1300–02.

In one respect, *Prometheus* broadens the arsenal of arguments against the patentability of a claim even beyond that stemming from *Flook* itself. *Prometheus* treated as a natural law the correlation between metabolite levels and toxicity claimed in *Prometheus*’s patent, even though the metabolites exist only as a result of administration by doctors of a drug created by humans. *Prometheus*, 132 S. Ct. at 1297–98, 1300. If a correlation that results from human activity

constitutes a natural law, as *Prometheus* concludes, there is an argument that everything is “natural” and hence unpatentable, including even products created by humans. Indeed, new products are created only as the result of natural laws regarding combinations of ingredients and the effects of those combinations, and the products thus could be said to be obvious once those natural laws are understood. Thus, *Prometheus* provides grist for arguments against patentability in virtually any case, including those involving product claims.

A Narrow Reading of the Inventiveness Prong

The Court, however, plainly did not intend its decision to result in the conclusion that nothing is patentable. It disavowed interpretations of Section 101 that would have that result (*id.* at 1294), and it contrasted *Prometheus*’s claims in which the additional steps “add nothing of significance to the natural laws themselves” with “a typical patent on a new drug or a new way of using an existing drug” that “confine[s] the[] reach [of the laws] to particular applications of the laws.” *Id.* at 1302.

Moreover, despite repeated references to an approach that analyzes inventiveness by separating a law of nature from steps appended to it, the Court’s decision in one place lauded the very “whole claim” approach from *Diehr* that it elsewhere seemed to reject. In discussing the non-obviousness requirement of Section 103, the Court stated that the non-obviousness requirement should not be applied in a manner that focuses solely on the claimed steps other than a law of nature or an abstract idea. The Court said that such an approach would be inconsistent with the holding of *Diehr* that “patent claims ‘must be considered as a whole’” under Sections 102 and 103. *Id.* at 1304 (quoting *Diehr*, 450 U.S. at 188).

As a formal matter, it is possible to reconcile the Court’s statements lauding use of the whole-claim approach for purposes of Sections 102 and 103 with the Court’s apparent rejection of this approach for purposes of Section 101. That would not, however, reconcile *Prometheus* with *Diehr* even as a formal matter because *Diehr* explicitly adopted the whole-claim approach for purposes of Section 101 and disavowed any use of novelty to assess patentability under Section 101. More importantly, the reason the Court provided as to why patent claims should be analyzed as a whole for purpose of Sections 102 and 103 seems equally applicable to Section 101. That reason is that “studiously ignoring all laws of nature when evaluating a patent application under sections 102 and 103 would ‘make all inventions unpatentable because all inventions can be reduced to underlying principles of nature which, once known, make their implementation obvious.’” *Id.* (quoting *Diehr*, 450 U.S. at 189 n.12).

Given the Court’s view that all claims would be obvious if claims were not considered as a whole, it is possible to argue that *Prometheus* cannot possibly have rejected *Diehr*’s whole-claim approach even for purposes of Section 101. But, as discussed above, the Court does seem to have rejected that approach.

Unless the Court is blind to this seeming contradiction in its reasoning, the Court must believe that something other than a whole-claim approach can be used for Section 101 without rendering all claims unpatentable, even though this would not be possible under Sections 102 and 103. In other words, the Court must believe that ignoring laws of nature/abstract ideas when assessing

the patentability of a claim will not have the same result as it would when assessing obviousness or anticipation. Because that appears to be the Court’s view, practitioners seeking to establish the patentability of a claim have a basis to argue that the inventiveness and limitations prongs in *Prometheus* must in some respect be less rigorous than would an obviousness or anticipation inquiry under Sections 102 or 103.

The Inventiveness Prong Can Be Read as Less Rigorous than Non-Obviousness

One possibility for practitioners seeking to establish the patentability of claims is to argue that inventiveness means something different than non-obviousness under Section 103. Although the Court has said that the steps to implement a law of nature will be obvious once a law of nature is understood, it may be that such steps can nonetheless be inventive as the Court understands the term. *Cf. id.* at 1304 (explaining that the Section 101 patent eligibility inquiry and the Section 102 novelty inquiry “might sometimes overlap . . . [b]ut that need not always be so”); *but cf. id.* at 1298 (quoting *Flook* for the proposition that “[p]urely conventional or obvious’ [pre-solution activity] is normally not sufficient to transform an unpatentable law of nature into a patent-eligible application of such a law”) (emphasis added).

As noted above, *Prometheus* explained the finding of patentability in *Diehr* as based on the proposition that the claims “apparently added to the formula something that in terms of patent law’s objectives had significance—they transformed the process into an inventive application of the formula.” *Id.* at 1299. Similarly, in approvingly citing the reasoning of the *Neilson* case, the Court said that the English court found the process patentable because the process implemented the abstract idea through “several unconventional steps.” *Id.* at 1300. Thus, the Court apparently believes that it is possible for steps implementing a law of nature/abstract idea to be inventive or unconventional even though the Court said that all such steps will be obvious once the abstract principle they are implementing is understood. Logically, the Court can only believe both things if the concept of inventiveness in Section 101 means something different than non-obviousness.

The Court did not say what that difference is. *Prometheus* contrasted inventive steps with “well-understood, routine, conventional activity.” *See, e.g., id.* at 1294. It did not otherwise explain the meaning of inventiveness. What that meaning could be is left for practitioners to argue about and lower courts to articulate. Whether there even is a sensible theory of inventiveness distinct from non-obviousness remains uncertain.

Of course, it may be that the Court was wrong in asserting that steps appended to a law of nature will always be obvious once a law of nature is understood. Because this assertion was an observation rather than a holding of the Court, practitioners seeking to defend the patentability of a claim are free to argue that appended steps are not obvious and therefore inventive. The fact that the Court believes both that all appended steps are obvious and that some of these steps are inventive merely provides an additional argument—that the standard of inventiveness must be less rigorous than the standard of non-obviousness.

The Limitations Prong

A second possibility for practitioners seeking to establish the patentability of a claim after

Prometheus is to argue that the claim satisfies the limitations prong and that this is sufficient to establish patentability regardless of whether the claim satisfies the inventiveness prong.

As discussed above, the Court found *Prometheus*'s claims unpatentable both because the steps appended to the law of nature were not inventive and because they did not limit the claims to any particular application of the law of nature. The claims did not direct doctors to employ any particular treatment based on the metabolite levels found in a patient's blood but instead simply directed doctors to consider the results of the correlation in making treatment decisions. As a result, the claims encompassed all applications of the law of nature by "t[ying] up the doctor's subsequent treatment decision whether that treatment does, or does not, change in light of the inference he has drawn using the correlations." *Id.* at 1302; *see also id.* at 1300.

The Court was deliberately unclear as to whether *Prometheus*'s claims would have been patentable if they satisfied the novelty prong but not the limitations prong or the limitations prong but not the novelty prong. After noting that *Prometheus*'s claims tied up all applications of a law of nature, the Court stated that "[w]e need not, and do not, now decide whether were the steps at issue here less conventional, these features of the claims would prove sufficient to invalidate them." *Id.* at 1302. The Court also did not need to, and did not, decide the converse: whether were the steps at issue more limiting, the conventional features of the claims would have been sufficient to invalidate them. It said, for example, "that simply appending conventional steps, specified at a high level of generality, to laws of nature, natural phenomena and abstract ideas cannot make those laws, phenomena and ideas patentable." *Id.* at 1292. But it did not say whether appending conventional steps that were not highly general could make the laws, phenomena, and ideas patentable.

The Court's discussion of prior cases does not answer the question of whether the limitations prong is independent of the inventiveness prong. Throughout its opinion, when it explained why past decisions found claims either patentable or unpatentable, the Court referenced the limitations prong as well as the inventiveness prong, making it impossible to infer whether either alone would have sufficed. In discussing *Flook*, for example, *Prometheus* noted that the finding of unpatentability in that case was based on both the routine nature of the claimed steps and on the fact that the steps "did not limit the claim to a particular application," *Id.* at 1292 (quoting *Flook* at 589, 590). Similarly, in approvingly citing the *Neilson* case referenced above in which an English court found a claim to be patentable, the Court noted not only the supposed inventiveness of the added steps, but also that the steps "confined the claims to a particular, useful application of the principle." *Id.* at 1300.

Because the Court did not decide whether a claim that meets the limitations prong but not the inventiveness prong is patentable, practitioners defending patentability of a claim can argue that meeting the limitations prong suffices. Indeed, they can argue that the limitations prong alone must be sufficient to establish patentability. If a claim also had to satisfy the inventiveness prong, it might be that few, if any, claims would be patentable given the Court's conclusion that steps appended to a law of nature are likely to be obvious, and that is not the result the Court intended. Practitioners can also argue that the Court's overarching purpose in *Prometheus* was to ensure

that patentees do not claim all applications of a law of nature or an abstract idea—a purpose that is satisfied so long as the limitations prong is met even if the inventiveness prong is not met. So long as the limitations prong is met, the claim at issue satisfies the Court’s stricture that a claim must “provide practical assurance that the process is more than a drafting effort designed to monopolize the law of nature itself.” *Id.* at 1297.

After arguing that a claim is patentable so long as it satisfies the limitations prong, practitioners seeking to defend the patentability of a claim can argue that almost any limitation can satisfy the limitations prong. They will have to acknowledge that not every limitation will be sufficient, because the Court stated that the question is whether the limiting steps “add *enough*” to a natural law to be patentable. *Id.*; *see also id.* at 3 (patent must claim “significantly” more than natural law); *id.* at 1294 (finding a claim unpatentable because it would “disproportionately” tie up natural law). Indeed, the Court held that the fact that Prometheus’s claim applied only to doctors did not save the claim because, under *Bilski*, limiting the use of an abstract idea or law of nature to a particular technological environment is insufficient to satisfy the limitations prong. *Id.* at 1297 (citing *Bilski*, 130 S. Ct. at 3230). Nonetheless, practitioners can argue that most limitations add enough to a natural law to satisfy the limitations prong.

They can point to an important contrast the Court drew between Prometheus’s claims in which the additional steps “add nothing of significance to the natural laws themselves” and the claims in “a typical patent on a new drug or a new way of using an existing drug” that “confine[s] the[] reach [of the laws] to particular applications of the laws.” *Id.* at 1302. In drawing this contrast, the Court did not explain how a patent for a new use of a drug (or a new drug) would confine the natural law discovered (that treatment with the drug reduces a particular disease) to a greater extent than did Prometheus’s patent. The lack of explanation leaves room for practitioners to argue that any standard type of claim remains patentable and that the limitations prong is relatively easy to satisfy. Such practitioners can reasonably argue that the result in *Prometheus* is based on its relatively unique facts, in which the claim required doctors simply to consider the results of a correlation and that it does not suggest that any other types of claims are unpatentable.

But those arguing against the patentability of a particular claim also have a strong basis in *Prometheus* to counter these arguments related to the limitations prong. To begin with, they can dispute the contention that a claim is patentable if it satisfies the limitations prong alone without satisfying the inventiveness prong. They can say that the reason *Prometheus* rejected an approach that would rely only on Sections 102 and 103 to assess novelty is that the Court views inventiveness as an integral part of the analysis under Section 101. *Id.* at 1303–04. Moreover, the Court relied heavily on *Flook*, and *Flook* expressly rejected the notion that “post-solution activity, no matter how conventional or obvious in itself, can transform an unpatentable principle into a patentable process” simply because it limits the claim, though this holding may apply only to post-solution activity. *Flook*, 437 U.S. at 589. Finally, while *Prometheus* repeatedly referenced both the inventiveness prong and the limitations prong, it sometimes suggested that a claim must include inventive steps to satisfy the limitations prong. For example, in discussing *Diehr*, the

Court said that it was because the claim included unconventional steps that the patent did not preempt all uses of the equation. *Prometheus*, 132 S. Ct. at 1299.

Moreover, practitioners arguing against patentability can say that if the limitations prong alone sufficed to establish patentability and the limitations prong could be satisfied through virtually any steps that limit a claim to fewer than all applications of a law of nature, then careful draftsmen could readily ensure the patentability of virtually any claim. That would not be consistent with the Court's intent, because the Court inveighed against interpreting Section 101 in a manner that makes patent eligibility depend on the draftsman's art. *Id.* at 1294. *See also Flook*, 437 U.S. at 588.

An Additional Source of Uncertainty

The Court's approach to patentability assumes that even though everything is at bottom based on a law of nature or an abstract idea, it is possible to differentiate those claim steps that implement a law of nature or an abstract idea from those that embody the law of nature or abstract idea. It is the implementing steps that must be inventive and/or limiting. As discussed, there is substantial uncertainty in evaluating the inventiveness and limitations prongs. There is an additional source of uncertainty as well. Practitioners opposing patentability can always argue that any supposedly inventive/limiting step is not an implementing step at all, but rather that the step itself embodies a law of nature or an abstract idea. Consider the claim step in *Diehr* involving the closing of a mold. While that step might help implement the mathematical algorithm in the claim, it could also be said to embody a different law of nature—the law of nature that pressure can turn liquids into solids. The use of a mold could be considered a routine implementation of that law of nature.

Conclusion

Prometheus focuses the analysis of patentability on whether a claim contains inventive steps separate from a law of nature and the extent to which those steps limit application of the law of nature. The relationship and meaning of these novelty and limitations prongs, however, remain uncertain. There are aspects of the Court's opinion that provide a basis for practitioners to argue that very few claims are patentable, along with aspects that provide a basis to argue that virtually all claims are.

The uncertainty may be inevitable given the Court's view of the goal of Section 101. The Court believes that there is a need based on precedent and policy to find unpatentable more than just natural laws and abstract ideas themselves, and it does not want to accept the use of a test such as the machine or transformation test that would automatically establish patentability if claims meet certain definitive parameters. However, the Court simultaneously wants to avoid interpreting Section 101—a provision designed to say what *is* patentable—as rendering unpatentable broad categories of claims. Given the Court's understanding that all patents can be reduced to natural laws and abstract ideas that make their implementation obvious, it is unclear whether it is possible to articulate a principled basis for holding that some claims constitute unpatentable natural laws or abstract ideas while others constitute patentable applications of these natural laws or abstract ideas.

The Supreme Court has recently granted, vacated, and remanded in two cases in light of *Prometheus—WildTangent, Inc. v. Ultramercial LLC*, No. 11-962 (May 21, 2012) and *Ass’n for Molecular Pathology v. U.S. Pat. & Trademark Office*, No. 11-725 (March 26, 2012) (*Myriad*). While these actions say nothing about the Court’s views on the merits of these cases, they leave the Federal Circuit in the difficult position of quickly applying *Prometheus* in important contexts. Given the tensions within *Prometheus*, the Federal Circuit will have a difficult task in articulating a principled basis to distinguish what is patentable under *Prometheus* from what is not and may ultimately be forced to rely on a “you know it when you see it” sort of approach. But one place the Federal Circuit and other courts can start is by evaluating whether there is a sensible interpretation of the inventiveness prong in *Prometheus* that would permit claim steps to be found inventive even if they would be obvious once the underlying law of nature is understood. A second place to start is evaluating whether the limitations prong can provide a path to patentability distinct from the inventiveness prong.

Keywords: litigation, intellectual property, Supreme Court, patentability, *Prometheus*

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Deconstructing Inventorship: A Method to the Madness

By Paul R. Coble and Carrie C. Ruzicka – September 12, 2012

Patent prosecutors, litigants, and fact finders in court frequently find it difficult to identify who has invented a novel chemical composition. The difficulty arises because inventorship in such cases requires “both knowledge of a specific chemical structure of the compound and an operative method of making it.” *Fina Oil & Chem. Co. v. Ewen*, 123 F.3d 1466, 1473 (Fed. Cir. 1997).

On January 12, 2012, in *Falana v. Kent State*, 669 F.3d 1349 (Fed. Cir. 2012), the U.S. Court of Appeals for the Federal Circuit sought to clarify where to draw the line expanding the pool of inventors of novel chemical compounds in at least one regard. The concept of inventorship now includes an individual who created a novel process used to make the claimed compound, even if that individual never actually made the claimed compound. While *Falana* is a reasonable extrapolation of well-settled inventorship law for chemical compounds, the decision will require increased scrutiny of inventorship during both prosecution and enforcement of claims in the chemical arts.

In *Falana v. Kent State*, Dr. Olusegun Falana sued Kent State University, Kent Displays Inc. (KDI), and the inventors named in U.S. Patent No. 6,830,789 (the '789 patent), requesting that he be added under 35 U.S.C. § 256 as an inventor to the '789 patent. KDI and Kent State own the '789 patent, and KDI is a spin-off technology company from Kent State that designs and manufactures liquid crystal displays (LCDs) used in electronic devices. The three named inventors were Joseph Doane, Asad Khan, and Alexander Seed. After Falana filed suit, he dismissed KDI, Doane, and Khan when they each filed statements with the district court, stating they had no disagreement with the addition of Falana as an inventor to the '789 patent. Kent State and Seed (collectively Kent State) remained as defendants.

The Northern District of Ohio held that Falana should have been named as an inventor on the '789 patent and ordered the U.S. Patent and Trademark Office to issue a certificate of correction adding him as a named inventor. *See Falana v. Kent State Univ.*, No. 08-cv-720, 2010 U.S. Dist. LEXIS 132486 (N.D. Ohio Dec. 15, 2010). On appeal, the Federal Circuit addressed whether a putative inventor who envisioned the structure of a novel genus of compounds, and created a method of making those compounds, is a joint inventor of a claim covering those compounds. Affirming the district court's ruling, the Federal Circuit held that an individual who invents a novel method of making a new class of chemical compounds contributes to the conception of the compounds within that class.

The invention at issue in *Falana* rose from a KDI research program to develop new chiral additives—chemical compounds used to improve the performance characteristics of LCDs, such as color, contrast, and brightness. One of the main goals of the project was to develop a proprietary chiral additive for KDI that was temperature-independent over a wide range of temperatures for use in portable LCDs. The other named inventors of the '789 patent hired Falana to conceive and synthesize new chiral additives that satisfied the goals of the project.

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While working on the KDI project, Falana synthesized numerous compounds as part of a team effort with the named inventors. Falana also developed a synthesis protocol to make a new class of chemical compounds called “naphthyl-substituted TADDOLS” (NATs). Falana used his new process—known simply as the Synthesis Protocol—to synthesize a chiral additive called Compound 7.

While Compound 7 showed great promise and significant progress toward finding a new, temperature-independent chiral additive, its range of temperature independence was not broad enough to satisfy the goals of the KDI research project.

Shortly after Falana left KDI, Seed, another researcher on the project, used Falana’s Synthesis Protocol to synthesize another NAT known as Compound 9. Testing revealed that Compound 9 had a substantial range of temperature independence, satisfying the objectives of the project. Compound 9 and Compound 7 have the same chemical formula, and both fall within the same genus of NATs. The only difference between the compounds is that Compound 9 is an RR enantiomer, and Compound 7 is an SS enantiomer. In other words, the only structural difference between the two compounds is that they each have two atomic centers that are mirror images of each other, which results in the molecules twisting in different directions.

KDI and Kent State filed a patent application for NATs, naming all the researchers on the KDI project except Falana. By the time Falana discovered he was omitted, the application had been filed as the ’789 patent. When he could not obtain the consent of KDI, Kent State, and all the named inventors to add his name as an inventor on the ’789 patent, Falana brought suit in the Northern District of Ohio, demanding to be added as an inventor pursuant to 35 U.S.C. § 256.

Kent State opposed the addition on multiple grounds. Kent State argued that Falana’s development of the Synthesis Protocol was insufficient to make him a co-inventor of the ’789 patent because the patent is directed toward the chemical compositions, and not the method by which they are created. Even though the specification of the ’789 patent disclosed Falana’s Synthesis Protocol as the operative method of making the claimed class of chiral compounds, the Synthesis Protocol is not claimed by the ’789 patent.

To minimize the significance of the Synthesis Protocol, Kent State argued that the key steps of the protocol were known in the art, and therefore, Falana did not provide an inventive contribution. Kent State further contended that the claims do not cover the specific NAT that Falana synthesized—namely, Compound 7. In what became a somewhat self-destructive maneuver, Kent State argued that the claimed NATs should be limited to RR enantiomers that exhibit temperature independence over the full range of temperatures required by the KDI project, and also argued that the claims should be limited to Compound 9 in an effort to exclude Compound 7, the NAT that Falana first synthesized—and of which he was indisputably an inventor.

The district court agreed with Kent State that the claims should be limited to RR enantiomers, but the court refused to read the additional limitation of temperature independence from the specification into the claims. Despite Kent State’s partial victory in excluding Compound 7 from

the literal scope of the claims, the district court held that Falana was an inventor because he contributed to the conception of the claimed invention by developing the novel Synthesis Protocol, which was the operative method of synthesizing the claimed compounds. The district court ultimately found the case to be exceptional under 35 U.S.C. § 285 on the basis that Kent State “took an untenable position in defending this case” and continued to defend the case despite testimony that “lacked credibility.” 2010 U.S. Dist. LEXIS 132486, at *56. Accordingly, Kent State was ordered to pay the attorney fees Falana incurred as a result of its actions. *Id.* at 58.

Kent State appealed to the Federal Circuit on the ground that the district court erred in concluding that Falana was a joint inventor of the '789 patent. The Federal Circuit framed the inventorship issue with the well-settled law that conception of a chemical compound necessarily requires knowledge of both the chemical structure of the compound and an operative method for making that compound. *Falana*, 669 F.3d at 1358. A method of making a new compound is therefore critical to the conception of that compound, and those who contribute to that method contribute to the conception of the compound itself.

Nevertheless, the Federal Circuit noted that individuals cannot be considered joint inventors where their only contributions are within the knowledge of one of ordinary skill in the art. The contributions must be novel, but where the method requires more than the exercise of ordinary skill, the discovery of such a method is as much a contribution to the compound as the discovery of structure of the chemical compound.

The Federal Circuit cautioned, however, that the inventor of a method of making a new genus of compounds is not automatically an inventor of all members of that genus that are discovered later. Once the process becomes publicly known, it is assimilated into the body of knowledge possessed by one of ordinary skill in the art and ceases to be a novel contribution worthy of inventorship. The Federal Circuit reiterated that one who discovers a novel process is not a joint inventor of later-discovered compounds using that process without sufficient collaboration. While joint inventorship may be found even if the co-inventors did not physically work together or at the same time, joint inventorship occurs only “when the inventors have some open line of communication during or in temporal proximity to their inventive efforts.” *Falana*, 669 F.3d at 1358 (quoting *Eli Lilly & Co. v. Aradigm Corp.*, 376 F.3d 1352, 1359 (Fed. Cir. 2004)).

In affirming the district court’s ruling that Falana was a co-inventor, the Federal Circuit found that Falana’s Synthesis Protocol was novel. The court also found that the Synthesis Protocol made possible the creation of a previously unknown class of the NATs chemical compounds. The method Falana used to synthesize Compound 7 was the same method Seed used to synthesize Compound 9 and is the only method disclosed in the '789 patent for making the claimed compounds. It was not dispositive for the Federal Circuit that Falana had left KDI before the claimed compounds were first synthesized. “Falana’s lack of contribution to the discovery of Compound 9 itself does not negate his contribution of the method used by the other inventors to make the genus of compounds covered by the claims at issue.” *Falana*, 669 F.3d at 1359.

Falana's Synthesis Protocol was necessary to enable one to make the claimed compounds, and just as important, the protocol was novel in and of itself.

The Federal Circuit also agreed with the district court's refusal to read into the claims a limitation regarding temperature independence, though it is apparent that the district court's claim construction was not outcome-determinative. Given the reasoning of the Federal Circuit, Kent State still would not have been able to defeat Falana's inventorship claim even if the courts had adopted Kent State's request to further limit the scope of the claims. Conception of a patented compound requires knowledge of chemical structure and the operative method of making it, but it does not require knowledge of the effective properties of that compound. Kent State successfully excluded Compound 7—the only NAT Falana synthesized—from the claims of the '789 patent, yet both the district court and the Federal Circuit found Falana's contribution sufficient to establish inventorship. Further limitation of the scope of the claims of the '789 patent would have been to Kent State's detriment.

Since *Falana*, the issue of joint inventorship for chemical compounds has arisen in at least two published opinions. First, in *Brigham Young Univ. v. Pfizer, Inc.*, Case no. 2:06-cv-890 TS, 2012 U.S. Dist. LEXIS 39636 (D. Utah Mar. 22, 2012), the U.S. District Court of Utah denied Pfizer's motion for summary judgment, which allowed Brigham Young University to proceed with action to include a BYU professor as a joint inventor on several of Pfizer's COX-2 inhibitor patents. The professor developed a novel method for testing existing compounds for COX-2 selectivity and shared the method with Pfizer, which used that method to develop a series of patents related to COX-2 inhibition—all of which claimed a COX-2 inhibitor. The district court found the professor's method of testing for COX-2 selectivity to be a material contribution to the claims, and therefore denied Pfizer's motion for summary judgment. Interpreting *Falana*, the court stated: "[A]n inventor of a method may be entitled to joint inventorship on a patent that discloses only compounds if (1) the plaintiff conceived of a method; (2) that is outside the exercise of ordinary skill; and (3) is in fact used to create the compound in the patent." *BYU*, 2012 U.S. Dist. LEXIS 39636, at *7.

The district court also rejected Pfizer's argument that the method of synthesizing the claimed compound in *Falana* was materially distinct from the BYU professor's method of testing compounds. The Utah district court reasoned that the BYU professor's "contribution would have the same effect in the end: providing the capability to develop COX-2 selective NSAIDs." *BYU*, 2012 U.S. Dist. LEXIS 39636, at *8 n.23. The Utah district court's reasoning, however, arguably extended from the underlying principle of *Falana* that conception of a chemical compound requires a method of *making* the compound. The District of Utah found that the professor may be an inventor because he developed an operative method of *testing* the compound.

Unlike *Falana*, the BYU professor's method was not necessary to synthesize the claimed compounds—it was only needed to test the efficacy of compounds synthesized by other processes. While methods of testing the efficacy of new compounds can be just as important as the methods by which those compounds are created from a practical perspective, courts and

attorneys should be mindful of this distinction in analyzing inventorship in both patent prosecution and litigation.

In *Schering Corp. v. Mylan Pharms, Inc.*, Civ. Action No. 9-6383 (JLL), 2012 U.S. Dist. LEXIS 59160 (D.N.J. April 27, 2012), the U.S. District Court of New Jersey focused on the novelty of the method at issue. The *Schering* court held that a scientist who was the first to create new compounds was not an inventor of similar compounds because the method he used to synthesize them was known in the art. The chemical structure of the claimed compounds was first conceived by others. While the scientist in *Schering* was the first to synthesize these compounds, he did so by using methods known in the art.

The district court also found that the claims did not cover the actual compounds the scientist synthesized—the claims were directed to *similar* compounds, and thus the scientist's contributions were too far removed from the claims at issue. While the court's *Schering* decision rested on multiple grounds, the focus on the novelty of the putative inventor's contribution serves as useful guidance in future inventorship disputes. A non-novel contribution to the elements of conception does not give rise to inventorship.

In the wake of *Falana*, practitioners should consider the contributions of all individuals to the creation of novel chemical compounds, and not only the individuals who synthesize the compounds actually claimed. Prosecutors should ensure that they fully investigate the methods and processes used to synthesize new compounds and determine whether those processes are known in the art. If the processes are not known, prosecuting attorneys must consider whether it would be appropriate to list the inventors of those processes on new patent applications.

When questions arise regarding a pending application or an issued patent, portfolio managers should audit their portfolios to determine whether corrective action should be taken. Inventorship may be corrected pursuant to 35 U.S.C. § 116 before the patent issues, or pursuant to 35 U.S.C. § 256 after issuance, with the consent of all presently listed inventors and all current assignees. If one of these parties objects to correction, inventorship can be corrected either through reissue or through an action in a federal district court, depending on which party objects. Section 256 can also be invoked by the patentee if the problem with inventorship comes to light for the first time in a declaratory judgment or infringement action. In litigation, both the patentees and infringement defendants should investigate whether the inventorship of an asserted patent is accurate. If it is not, the first side to unearth the issue may ultimately gain the upper hand.

Falana also highlights the practical importance of obtaining proper assignments in the wake of *Stanford v. Roche*, 131 S. Ct. 2188, 563 U.S. (2011). If *Falana* had signed an effective assignment contract, there likely would have been little reason for Kent State not to agree to list him as an inventor. It appears, however, that one concern Kent State had in adding *Falana* was his ability to practice and license the technology, because no assignment contract existed. An effective assignment from *Falana* to Kent State might have obviated protracted litigation in which Kent State sought to narrow its claims and ultimately incurred sanctions.

When defending against challenges to inventorship, parties must remain aware of how arguments regarding inventorship will affect a patentee's ability to enforce the patent at issue. Kent State's arguments with respect to the Synthesis Protocol being known in the art could provide fodder for future invalidity challenges to the '789 patent. Additionally, its claim construction positions in *Falana* might significantly narrow the scope of the '789 patent's claims. To the extent that Kent State effectively dedicated Compound 7 to the public by opposing Falana's claim to inventorship, the school would most likely be estopped from arguing any claim construction that includes Compound 7 within the scope of the '789 patent.

Another potential consequence of *Falana* is that an individual might qualify as an inventor by preparing an intermediary compound that can be converted to a novel compound through technology known in the art. In such circumstances, the putative inventor's contribution of creating a novel synthesis of an intermediary may be equivalent to creating an operative method of making the claimed compound. Under the reasoning in *Falana*, the person synthesizing the intermediary might be an inventor of the claimed compound even if that person did not actually make the claimed compound.

Although the Federal Circuit decision in *Falana v. Kent State* begins to clarify the murky waters of who is the inventor of a chemical compound, the decision also highlights the depth of analysis that is necessary for patent applicants, patent practitioners, and the courts in assessing inventorship. The focus of any such assessment must extend beyond the conception of the compound itself to include the process by which that compound is manufactured.

Keywords: litigation, intellectual property, inventorship

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Scope of Waiver: Post-*Seagate* Trends

By Reginald J. Hill and Nangah N. Tabah – September 12, 2012

Courts have struggled immensely with the scope of waiver of attorney-client privilege and work product immunity in the context of an accused infringer's reliance on the advice-of-counsel defense to accusations of willful patent infringement. The well-established standard for determining the scope of the waiver of attorney-client privilege is that the waiver applies to "all other communications relating to the same subject matter." *Fort James Corp. v. Solo Cup Co.*, 412 F.3d 1340, 1349 (Fed. Cir. 2005); *see also In re Seagate Tech., LLC*, 497 F.3d 1360, 1372 (Fed. Cir. 2007) (en banc), *cert. denied*, 552 U.S. 1230 (2008); *Hercules, Inc. v. Exxon Corp.*, 434 F. Supp. 136, 156 (D. Del. 1977). The scope of waiver of work product immunity, however, is more nuanced.

The Federal Circuit has recognized three categories of work product relevant to the advice-of-counsel defense: "(1) documents that embody a communication between the attorney and client concerning the subject matter of the case, such as a traditional opinion letter; (2) documents analyzing the law, facts, trial strategy, and so forth that reflect the attorney's mental impressions but were not given to the client; and (3) documents that discuss a communication between attorney and client concerning the subject matter of the case but are not themselves communications to or from the client." *In re EchoStar Commc'ns Corp.*, 448 F.3d 1294, 1302 (Fed. Cir. 2006). The *EchoStar* court noted that because counsel's opinion is relevant only to decipher the alleged *infringer's* state of mind, and not for its legal correctness, documents that counsel prepared but did not communicate to the client—the second category of work product—do not inform the court of an infringer's willfulness and are not discoverable. *Id.* at 1300.

The third category of work product is discoverable only to the extent that it discusses a communication to the client concerning whether a patent is valid, enforceable, and infringed, even though the document itself—such as an internal memorandum or email—was not communicated to the client. What is waived, for both attorney-client privilege and work product, are "letters, memorandum, conversation, or the like between the attorney and his or her client, [and] includes, when appropriate, any documents referencing a communication between the attorney and client." *Id.* at 1304.

While *Seagate* is clear that, as a general rule, the subject of waiver of attorney-client privilege and the waiver of work product immunity triggered by the advice-of-counsel defense will not extend to trial counsel, in light of *Seagate's* "chicanery" exception, district courts have taken varying approaches with respect to the scope of the waiver as it extends to trial counsel under circumstances the courts deem unique or exceptional. *See Seagate*, 497 F.3d at 1372–73. To further complicate the scope of waiver landscape, district courts have been left to apply *EchoStar's* holding that the waiver rules should be the same between in-house counsel and outside counsel. *See EchoStar*, 448 F.3d at 1299 ("[W]hen [defendant] chose to rely on the advice of in-house counsel, it waived the attorney-client privilege with regard to any attorney-client communications relating to the same subject matter . . .").

This article addresses how district courts have carved out the scope of waiver of attorney-client privilege and work product immunity in patent infringement cases post-*Seagate*. The article looks specifically at waiver with respect to opinion counsel versus trial counsel, and outside counsel versus in-house counsel. The article discusses circumstances deemed “unique” by the district courts to warrant waiver for trial counsel and recommends steps to minimize waiver.

***Seagate* Opinion**

Seagate squarely addressed the question of scope of waiver in willfulness cases with respect to opinion counsel and trial counsel, but left much uncertainty concerning when waiver applies to trial counsel—the so-called “chicanery” exception. *Seagate* had relied on the advice-of-counsel defense to defend against a charge of willful infringement. The district court held that the waiver of privilege extended to communications with opinion counsel as well as trial counsel. *See Seagate*, 497 F.3d 1366–67. On appeal, the Federal Circuit disagreed, siding with *Seagate* that opinion counsel and trial counsel perform significantly different functions, and “fairness counsels against disclosing trial counsel’s communications on an entire subject matter in response to an accused infringer’s reliance on opinion counsel’s opinion to refute a willfulness allegation.” *Id.* at 1373.

The court distinguished opinion counsel’s role as one “to provide an objective assessment for making informed business decisions,” whereas “trial counsel focuses on litigation strategy and evaluates the most successful manner of presenting a case to a judicial decision maker.” Trial counsel is also engaged in an adversarial process, and thus the court held as a general proposition that “asserting the advice of counsel defense and disclosing opinions of opinion counsel do not constitute waiver of the attorney-client privilege for communications with trial counsel.” *Id.* at 1374. Similarly, the court held that “relying on opinion counsel’s work product does not waive work product immunity with respect to trial counsel.” *Id.* at 1376. Finally, because willful infringement is based mainly on prelitigation conduct, communication with trial counsel has little, if any, relevance warranting its disclosure.

The court carved out an exception, however, in which trial courts could use their discretion to extend waiver to trial counsel under unique circumstances, such as if a party or counsel engages in “chicanery.” *Id.* at 1375–76. Chicanery is defined as “a deception by artful subterfuge or sophistry.” *Merriam-Webster.com*. 2012. <http://www.merriam-webster.com/dictionary/chicanery> (June 5, 2012). Post-*Seagate*, district courts have deemed certain circumstances to be extraordinary enough for waiver with respect to trial counsel, although no case law was found expressly identifying attorney conduct as chicanery sufficient to warrant waiver.

Scope of Waiver Post-*Seagate*

Waiver Regarding Opinion Counsel

Consistent with *Seagate* and *EchoStar*, district courts have found that disclosure of attorney opinion to rebut claims of willful patent infringement waives privilege for all communications with opinion counsel on the same subject matter. *See, e.g., Reedhycalog UK, Ltd. v. Baker Hughes Oilfield Operations Inc.*, 251 F.R.D. 238, 241 (E.D. Tex. 2008); *Alloc, Inc. v. Pergo*,

L.L.C., 2010 WL 3808977, at *6–7 (E.D. Wis. Sept. 23, 2010). It follows that where a defendant does not raise the advice-of-counsel defense, there is generally no waiver.

Waiver Regarding Trial Counsel

Since *Seagate*, with a few exceptions, district courts have generally held that relying on opinion counsel’s work product does not waive work product immunity with respect to trial counsel. For example, a court in the Southern District of New York noted that “[i]t is clear that the scope of discovery is relegated to prelitigation and gaining trial counsel’s opinions is not relevant.”

Convolve, Inc. v. Compaq Computer Corp., 2007 WL 4205868, at *3 (S.D.N.Y. Nov. 26, 2007). The *Convolve* court observed that the accuser needs to focus on whose opinion the defendant is relying upon, and then needs to separate the communication made and created before litigation from all other privileged communications that were shared with the alleged infringer. *Id.* at *4.

We are not aware of a district court decision that has expressly explored the “chicanery” exception, but district courts have found waiver with respect to trial counsel under three exceptional or unique circumstances.

Exceptional circumstances have been found **when opinion and trial counsel belong to the same firm or are the same person, thus warranting waiver**. The U.S. District Court for the Northern District of New York ordered the deposition of trial counsel who was also opinion counsel. *NewRiver, Inc. v. Newkirk Products, Inc.*, 2008 WL 5115244, at *3 (N.D.N.Y. Dec. 4, 2008). The court noted that since one of the opinion counselors was also acting as one of the trial attorneys, “the lines may be blurred between prelitigation opinion related disclosures and post-complaint communications with trial counsel.” The court also noted that “Newkirk should not be allowed to evade an inquiry into the opinions simply because it chose one of the opinion counselors as its trial counsel.” Most important, the court held that post-complaint communication with trial counsel may remain confidential. Recognizing that in the course of obtaining prelitigation opinion disclosures, “there is a risk of encountering nondisclosed work product and trial-generated work product and communications between client and trial counsel,” the court proffered that proper guidance would minimize this risk.

Another case finding exceptional circumstances is *Tyco Healthcare Group LP v. E-Z-EM, Inc.*, 2010 WL 2079920, at *2 (E.D. Tex. May 24, 2010), in which opinion and trial counsel belonged to the same law firm and opinion counsel was an active member of the trial team. The court ordered disclosure of all communication on the same subject matter included in the opinion letter, stating that the case presented the “unique circumstances” envisioned by *Seagate*. *Id.* at *4. The communication waived was between opinion counsel and the client, E-Z-EM; opinion counsel and the rest of the trial team; and the trial team and the client. The court also found that E-Z-EM waived immunity for all work product that referenced such communications, and for all work product on the same subject that was communicated to the client. *Id.* at *3. The court was concerned that the defendant had “casted doubt on the credibility of the opinion letter by asking the drafter of the opinion to become an active member of the trial team,” and E-Z-EM had blurred the distinction between the functions of opinion and trial counsel by allowing opinion counsel to join the trial team.

In contrast, however, waiver does not extend to new trial counsel that replaced the original trial counsel, which was also opinion counsel. *See Alloc, Inc. v. Pergo, L.L.C.*, 2010 WL 3808977, at *6–7 (E.D. Wis. Sept. 23, 2010). In *Alloc*, for example, the accused infringer’s (Pergo) opinion counsel had originally acted as its trial counsel when the suit was filed. *Id.* at *1. Pergo produced several opinions of counsel received from its opinion counsel around the time the lawsuit was commenced. Opinion counsel, however, was replaced with different trial counsel shortly thereafter, and trial counsel later wrote five additional opinion letters on validity, enforceability, and infringement. The court ruled that since trial counsel appeared to be operating independently from opinion counsel, the waiver of privilege from producing opinion counsel’s opinions did not extend to trial counsel’s opinion that came approximately five years later. *Id.* at *6–7.

The court ultimately noted that “while Pergo’s decision may have been prescient, no evidence [was] presented suggesting that Pergo switched trial counsel primarily to circumvent the waiver of privilege.” *Id.* at *7. Further, it is prudent litigation strategy—not chicanery—to retain trial counsel separate from opinion counsel.

When trial and opinion counsel are not independent. Though trial counsel is ordinarily shielded from waiver, communication between opinion counsel and trial counsel on the same subject matter of the opinion—prior to the litigation being filed—can be subject to discovery. The court may also order deposition of persons who offered technical information to opinion counsel. *See Se-Kure Controls, Inc. v. Diam USA, Inc.*, 2008 WL 169029, at *2 (N.D. Ill. Jan. 17, 2008). In *Se-Kure Controls*, the accused infringer’s trial counsel provided documents and materials for opinion counsel to review before his deposition, and the court granted the patentee’s motion to compel the accused infringer to produce emails and other documentary communications such as opinion letters and memoranda from the trial counsel given to the opinion counsel *before* the litigation commenced that is relevant to the patent at issue. *Id.* at *3.

Similarly, in *SPX Corp. v. Bartec USA, LLC*, 247 F.R.D. 516 (E.D. Mich. 2008), the court granted the patentee’s motion to compel the accused infringer to produce documents regarding communication it had with opinion counsel, and communication it had with trial counsel before the suit was commenced based on the waiver of privilege from relying on an opinion of counsel. What is important here, however, is that notwithstanding the patentee’s overbroad document requests, the accused infringer’s failure to provide an adequate privilege log compelled the court to require compliance with patentee’s document requests. *Id.* at 518. The accused infringer failed to show that any of the communications with trial counsel were after the suit was commenced.

While the court recognized the categories of communications and work product that are not subject to the waiver—(1) uncommunicated work product that does not memorialize a conversation between lawyer and client; (2) communications with trial counsel that post-date the filing of the lawsuit; and (3) confidential communications that do not relate to the invalidity, unenforceability, or non-infringement—it was “impossible to determine from the privilege log . . . whether any of the documents not produced [fell] within the protected categories.” *Id.* at 527.

Disclosure of opinion of counsel to a third party (government agency and accused infringer’s customers). Opinions of counsel may be discoverable when an accused infringer

discloses the conclusion of the opinions to third parties. *American Family Life Assur. Co. of Columbus v. Intervoice, Inc.*, 2010 WL 3000238, at *1, *3–4 (M.D. Ga. July 28, 2010). *American Family* was an indemnification action in which the court ruled that the defendant waived privilege associated with opinions of the counsel it had obtained analyzing the infringement and validity of asserted patents, by disclosing to the SEC and to one of its customers that it obtained opinions that concluded there was no infringement and the claims were invalid. The court found that by revealing the conclusions of the opinion, the defendant had waived attorney-client privilege, and once outside counsel had communicated the opinion letter to the defendant—its client—any work-product immunity associated with the opinion letter became waivable should the client disclose the letter, as was done.

Waiver Regarding In-House Counsel

With respect to opinions and communication with in-house counsel, two sets of considerations are important—identifying whose opinion the defendant seeks to rely on, and separating pre- and post-litigation communication and work product. See *Convolve, Inc.*, 2007 WL 4205868, at *5.

Pre-litigation. Waiver extends to pre-litigation communication with in-house counsel to the extent that defendants rely on issued opinions in an advice-of-counsel defense. Asserting the advice-of-counsel defense based on opinions issued by in-house counsel “waives work product protection and the attorney-client privilege for all communications on the same subject, as well as any documents memorializing attorney-client communications.” This waiver does not, however, “extend to work product that was not communicated to the alleged infringer.” *Convolve*, 2007 WL 4205868, at *5 (citing *Seagate* and noting that this holding was consistent with *EchoStar*).

Post-litigation. While post-litigation communication is a closer question, the Southern District of New York observed that in-house counsel more closely resembled opinion counsel than trial counsel “because they offer what the defendants treat as objective assessments for making business decisions.” *Convolve*, 2007 WL 4205868, at *5. Nonetheless, the court found no basis for taking discovery of in-house counsel communication after the commencement of litigation. Because post-litigation opinions, even of outside opinion counsel, are of “marginal value”—the willfulness analysis focuses on pre-litigation conduct—a court will likely find no basis for taking discovery of in-house counsel communication after the litigation was commenced. See *id.* Cf. *V. Mane Fils, S.A. v. International Flavors and Fragrances Inc.*, 2009 WL 1968925, at *5–6 (D. N.J. July 1, 2009) .

Simply designating in-house counsel to be trial counsel, however, may not get around the waiver. In *Duhn Oil Tool, Inc. v. Cooper Cameron Corp.*, 2009 WL 3381052, at *15 (E.D. Cal. Oct. 15, 2009), the accused infringer relied on an opinion of counsel by in-house counsel to defend against a willful infringement allegation. The court granted the patentee’s motion to compel the accused infringer to produce documents of communication with its in-house counsel that fell within the scope of the waiver, and rejected the accused infringer’s argument that in-house counsel was also acting as trial counsel and therefore could rely on the trial counsel shield of *Seagate*. The court was not persuaded by Cameron’s assertion that in-house counsel was also

trial counsel due to the circumstances, which included the fact that in-house counsel had previously been identified on numerous occasions as serving in a traditional in-house counsel role, and the *pro hac vice* application for in-house counsel was filed years into the litigation and just *one* day prior to the filing of the joint statement being considered by the court.

Conclusion and Steps to Minimize Waiver

While district courts generally hold that waiver does not extend to trial counsel, courts may waive privilege when there is a concern that the defendant is attempting to use the privilege as a sword and shield. The following circumstances and communications have been deemed to fall within the scope of waiver: when opinion and trial counsel are the same person or belong to the same firm; pre-litigation communication between opinion and trial counsel on the subject matter of the opinion; and suspicious timing of identifying in-house counsel as trial counsel. As district courts continue to further define the scope of waiver with respect to trial and in-house counsel, it will be interesting to see what other circumstances are identified as unique or exceptional to warrant waiver.

Against this backdrop, litigants should take steps to minimize the risk of waiver, such as ensuring that separate issues are addressed in separate opinions; maintaining a clear line between the end of opinion work and start of pre-litigation and litigation work; minimizing communications that comment on the opinion, as these also may be subject to discovery; recognizing the paper trail being created and discarding unnecessary drafts; limiting or avoiding post-filing opinions of counsel; and generally, limiting access to the opinion.

Keywords: litigation, intellectual property, waiver, attorney-client privilege, work product immunity, prelitigation, opinion counsel, trial counsel

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Is MDL Still Possible When Joinder Is Improper?

By Audra Dial – September 12, 2012

The America Invents Act (AIA), signed into law on September 16, 2011, made substantial changes to various aspects of patent law “to correct flaws in the system that have become unbearable, and to accommodate changes in the economy and the litigation practices in the patent realm.” *America Invents Act: Hearing on H.R. 1249 Before the H. Comm. on the Judiciary*, 112th Cong. 38–9 (June 29, 2011). Interestingly, the AIA limits the joinder of multiple defendants to a single patent infringement action in such a way that parties to one patent lawsuit must be engaged in concerted behavior, not just infringement of the same patent, to be properly joined in a single case.

Thereafter, patent plaintiffs began suing defendants in individual lawsuits, often on the same day and even in the same court. These serial cases raising infringement of the same patent against a range of defendants had the chance to proceed independently at different paces, depending on the court assigned to the case. As a result, it became apparent that the new joinder rules may not have provided the efficiency and fairness that the AIA was touted to provide, and many began to question whether the AIA was intended to prevent any sort of pretrial consolidation, including that offered through multidistrict litigation MDL, particularly if joinder of the potentially consolidated defendants would have been improper.

The arguments against pretrial consolidation stem from the AIA’s legislative history, which demonstrates that Congress passed the AIA to “end[] the abusive practice of treating as codefendants parties who make completely different products and have no relation to each other.” 157 Cong. Rec. H4420-06. Yet, the plain language of the AIA suggests that the statute did not expressly preclude pretrial consolidation as allowed under the MDL process. Thus, in at least one instance, defendants challenged the efficacy of a MDL proceeding after those defendants had been found to have been improperly joined in one case. *See In re Bear Creek Technologies, Inc.*, (’722) *Patent Litigation*, 2012 WL 1523340, U.S. Judicial Panel on Multi-District Litigation (No. MDL 2344). In approving consolidation, at least one panel has concluded that the AIA is not the death knell for MDL proceedings in patent litigation, even in cases where the defendants would not be properly joined in one action.

The AIA

Section 19(d) of the AIA, 35 U.S.C. § 299, states in part (emphasis added):

With respect to any civil action arising under any Act of Congress relating to patents, other than [those actions for infringements involving drugs or biological products], parties that are accused infringers *may be joined in one action as defendants or counterclaim defendants, or have their actions consolidated for trial*, or counterclaim defendants only if—(1) any right to relief is asserted against the parties jointly, severally, or in the alternative with respect to or arising out of the same transaction, occurrence, or series of transactions or occurrences relating to the making, using, importing into the United States, offering for sale, or selling

of the same accused product or process; and (2) questions of fact common to all defendants or counterclaim defendants will arise in the action.

For purposes of this subsection, accused infringers *may not be joined in one action* as defendants or counterclaim defendants, *or have their actions consolidated for trial, based solely on allegations that they each have infringed the patent* or patents in suit.

This language strengthens the commonality requirement for consolidating and joining defendants in patent infringement actions. Before the AIA, Rule 42 of the Federal Rules of Civil Procedure governed consolidation and required only that actions share a common question of fact or law for consolidation at trial. Now, consolidation for trial is coextensive with the standard for permissive joinder found in Rule 20 of the Federal Rules of Civil Procedure. The joinder of defendants in patent-litigation matters now not only requires commonality of fact, but it also requires that actions against multiple defendants arise out of the same transaction or occurrence.

The AIA made it clear that the mere infringement of the same patent, without any allegation that the defendants were acting in concert or otherwise engaged in the same transaction, was insufficient to join unrelated defendants to one action. Moreover, the AIA eliminated the opportunity for a plaintiff to consolidate separate actions against multiple defendants accused of infringing the same patent for trial. Without common facts underpinning the allegations of infringement, there is no longer a basis for joinder or trial consolidation.

But does this heightened standard apply to all forms of consolidation? The AIA's language specifically mentions consolidation for trial. If the joinder of defendants would be improper under the AIA, is it appropriate to nevertheless consolidate multiple cases involving infringement of the same patent through MDL proceedings? And, in so doing, is that an end-run around the AIA's stronger joinder requirements?

Congress authorized the Judicial Panel on Multi-District Litigation (JPML) to “[transfer] to any district for coordinated or consolidated *pretrial* proceedings[]” civil actions “involving one or more common questions of fact.” 28 U.S.C. § 1407 (emphasis added). Often this procedure is employed when dozens or even hundreds of cases are pending across various jurisdictions, such as is the case in large products-liability matters. Before the AIA, patent-litigation matters began to employ the MDL procedure, particularly when multiple accused infringers were alleged to have infringed by virtue of following an industry standard. *See In re Rembrandt Technologies LP, Patent Litigation*, 493 F. Supp. 2d 1367, 1369 (JPML 2007) (granting MDL treatment for patent-litigation cases alleging that compliance with an industry standard infringed the patents in suit). However, with the AIA's stronger requirements regarding joinder and trial consolidation, the efficacy of MDL proceedings became questionable.

Statutory Construction of the AIA

The plain language of the AIA states that “accused infringers may . . . have their actions consolidated for trial . . . only if [the two-part standard is met].” 35 U.S.C § 299(a). On its face, consolidation for pretrial purposes is not subject to this exclusive requirement, or else the words

“for trial” would be superfluous. Other rules and statutes, in contrast, specifically address pretrial consolidation. For example, Rule 42 authorizes a district court to “join for hearing or trial any or all matters at issue in the actions [before the court]” if multiple cases involve common questions of law or fact. Fed. R. Civ. P. 42(a). Section 1407, which authorizes MDL consolidation, authorizes the JPML to “transfer[] to any district for coordinated or consolidated pretrial proceedings” civil actions “involving one or more common questions of fact.” 28 U.S.C. § 1407(a). When read together with the AIA, the absence of the phrase “pretrial consolidation” is noteworthy.

The JPML is charged with protecting the individuality of each action by remanding each case that is consolidated to the transferor court for trial. 28 U.S.C. § 1407 (“Each action so transferred shall be remanded by the panel at or before the conclusion of such pretrial proceedings to the district from which it was transferred . . .”); *Lexecon, Inc. v. Milberg Weiss Bershad Hynes & Lerach*, 523 U.S. 26, 28, 34, 40–1 (1998) (holding that a transferee court hearing consolidated pretrial proceedings had no authority to assign the transferred case to itself for trial). Thus, the issues of fairness relating to improper consolidation (including potential juror confusion and lack of time to present one’s unique defenses at trial) are eliminated by MDL, which is designed solely to enable efficient pretrial proceedings.

Because the AIA mentions consolidation for trial only, it does not expressly overlap with any statute dealing with pretrial consolidation. Even if there was some overlap between the AIA and pretrial consolidation by virtue of the strengthened joinder requirement, in such instances, a court will presume harmony, not contradiction. *Bruesewitz v. Wyeth, LLC*, 131 S. Ct. 1068, 1076 (2011) (stating that the Court will not read-in intent through “implication”); *Scheidler v. Nat’l Org. for Women, Inc.*, 547 U.S. 9, 19 (2006) (“[The Court] will not presume that [a statutory] revision worked a change in the underlying substantive law unless an intent to make such a change is clearly expressed.”) (internal quotation marks and punctuation changes omitted). Given this philosophy of statutory construction, it does not appear that the AIA precludes pretrial consolidation through MDL, absent express discussion of this concern in the legislative history of the AIA.

Legislative History of the AIA

The legislative record of the AIA focuses on how the statute affects joinder of parties and consolidation for trial. Pretrial consolidation was not addressed specifically during the debates on the AIA. Senator John Kyl stated that Section 299 “bars joinder of accused infringers as codefendants, or consolidation of their cases for trial, if the only common fact and transaction among the defendants is that they are alleged to have infringed the same patent.” 157 Cong. Rec. S5429 (Sept. 8, 2011). Senator Kyl was initially “skeptical” of the necessity for the added language about consolidation at trial but, without it, he noted that “under current law, even if parties cannot be joined as defendants under Rule 20, their cases can still be consolidated for trial under Rule 42.” *Id.* (citing *Ohio v. Louis Trauth Dairy, Inc.*, 163 F.R.D. 500, 503 (S.D. Ohio 1995) (“Even when actions are improperly joined, it is sometimes proper to consolidate them for trial.”)).

Few other statements regarding consolidation were made during the floor debate other than brief summaries of the purpose and effect of the AIA. In each reference, the AIA was described as merely limiting joinder and consolidation into one action for trial. Nothing in the record contains a discussion about pretrial proceedings. *America Invents Act: Hearing on H.R. 1249 Before the H. Comm. on the Judiciary*, 112th Cong. 54 (June 29, 2011) (“[The AIA creates] a new § 299 that addresses joinder under Rule 20 and consolidation of trials under Rule 42.”); 157 Cong. Rec. H4426 (June 22, 2011) (statement of Rep. Bob Goodlatte) (“[The AIA] restricts joinder of defendants to cases arising out of the same facts and transactions . . .”).

It is clear that Congress added the “consolidation for trial” language specifically to prevent plaintiffs from using Rule 42 to circumvent the stricter joinder rules because at least three courts had previously allowed Rule 42 consolidation despite having found the defendant to be misjoined. *See Ohio v. Louis Trauth Dairy, Inc.*, 163 F.R.D. 500, 503 (S.D. Ohio 1995); *Kevin v. Newburger, Loeb & Co.*, 37 F.R.D. 473 (S.D.N.Y. 1965); *Stanford v. TVA*, 18 F.R.D. 152 (M.D. Tenn. 1955). No courts have used Rule 42 to support pretrial consolidation when parties were previously severed under Rule 21. Thus, it is possible that Congress did not expressly include “pretrial consolidation” in Section 299 because doing so would have been unnecessary, given the lack of evidence that Rule 42 was being used in this manner.

Pretrial Consolidation Results in Similar Difficulties as Consolidation for Trial

Pretrial consolidation through MDL can harm an accused infringer, particularly if that defendant is consolidated with many other defendants for pretrial proceedings, in the same ways that consolidation for trial would. For example, rather than having the full amount of time allotted in the federal rules for taking the deposition of key witnesses (including the inventor), a party in an MDL proceeding may obtain just a fraction of the seven hours allotted per deposition because it must share that time with the other defendants whose cases have been consolidated. Likewise, during claim construction, it may be difficult for parties to present their individual arguments and the particularities of their unique technology in one *Markman* hearing. Although consolidation in patent-infringement actions can help a plaintiff economize its discovery efforts, pretrial consolidation harms the multiple defendants who wish to develop a defense tailored to their specific facts.

In essence, there is no practical difference between pretrial joinder and pretrial consolidation. Construing the AIA to prohibit pretrial joinder but allowing pretrial consolidation could negate the purpose behind the stricter joinder requirements in the AIA and the impetus for the AIA’s enactment (to end “abusive practices” that had occurred with lawsuits involving dozens, and even hundreds, of defendants whose only connection was that they were alleged to have infringed the same patent). Allowing pretrial consolidation would therefore create a substantial loophole in the law and allow a plaintiff to obtain the efficiencies of litigating one case rather than dozens of individual cases, even when the parties to be consolidated have no true connection to each other. Courts are disinclined to “interpret federal statutes to negate their own stated purpose.” *John v. United States*, 247 F.3d 1032 (9th Cir. 2001) (quoting *New York State Dep’t of Soc. Servs. v. Dublino*, 413 U.S. 405, 419–20 (1973)). Because Congress showed an intention to tip the balance toward defendants by making consolidation more difficult for trial,

how can the AIA allow pretrial consolidation, particularly when joinder and trial consolidation would be improper?

The JPML Panel's Decision

The JPML panel heard these arguments in March 2012 when deciding Bear Creek's motion to consolidate 14 defendants. *In re: Bear Creek Technologies, Inc., ('722) Patent Litigation*, 2012 WL 1523340, U.S. JPML (No. MDL 2344). In that case, Bear Creek had initially sued all 14 defendants in one action in the U.S. District Court for the Eastern District of Virginia. In a pre-AIA decision, the defendants were found to be improperly joined, and the case against all but the first named defendant was dismissed. *Bear Creek Techs., Inc. v. RCN Commc'ns*, No. 2:11-CV-103 (E.D. Va. Aug. 12, 2011). The next day, Bear Creek initiated individual actions against the dismissed defendants in Virginia and Delaware.

Months later, after the case against one defendant had proceeded through claim construction, Bear Creek sought to consolidate the cases for pretrial purposes through the MDL process. Many defendants opposed the consolidation, raising arguments that Bear Creek was attempting to avoid the misjoinder ruling by MDL consolidation and that Congress's intent in passing the AIA was to avoid this sort of gamesmanship, particularly by nonpracticing entities such as Bear Creek.

During oral argument, the JPML raised concerns about the burden on the court system, particularly with regard to claim construction if the AIA was interpreted to preclude pretrial consolidation. Even though the JPML acknowledged that the case presented different technology and would raise different issues among the various defendants, it concluded that "the America Invents Act, 35 U.S.C. § 299 . . . does not affect our authority to transfer this litigation for coordinated or consolidated pretrial proceedings pursuant to 28 U.S.C. § 1407." Thus, at least for now, the MDL process remains an avenue for the pretrial consolidation of multiple defendants involved in patent litigation, even if those defendants could not be properly joined in one case.

Conclusion

The AIA's changes to joinder and consolidation at trial still present challenges for parties seeking to obtain the fairness the AIA was intended to afford. The use of MDL consolidation for pretrial purposes can, at times, circumvent the policy considerations of the AIA, forcing defendants into one lawsuit for discovery and claim construction regardless of whether those defendants are acting in concert in their alleged infringement. However, the plain language of the AIA does not support a finding that MDL consolidation is improper in any circumstances.

The JPML's ruling in *Bear Creek* suggests that the panel is not concerned that it will be overwrought with requests to consolidate patent cases in which there is no efficiency to be gained from MDL consolidation. Despite the JPML's decision allowing consolidation of the *Bear Creek* patent-infringement cases, arguments against MDL consolidation still remain and are certainly bolstered by the policy considerations underpinning the AIA. As a result, defendants facing a request for MDL consolidation should consider whether there are such individualized facts in their cases that would make consolidation inappropriate. If so, the AIA's policy considerations could be used to bolster an argument against MDL treatment. Simply relying on

the AIA as a bar to pretrial consolidation will be unsuccessful now that the JPML has spoken in the *Bear Creek* matter.

Keywords: litigation, intellectual property, multidistrict litigation, joinder, Judicial Panel on Multi-District Litigation, America Invents Act

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The Pendulum Swings: *Bosch* and Permanent Injunctions

By Christopher B. Lay – September 12, 2012

The Federal Circuit's recent decision in *Robert Bosch LLC v. Pylon Manufacturing Corp.* 659 F.3d 1142, 1149 (Fed. Cir. 2011) has been widely recognized for its explicit "jettison[ing]" of the presumption of irreparable harm previously applied in patent infringement cases where the prevailing patentee sought a permanent injunction. This ruling ended a debate that erupted after the U.S. Supreme Court in *eBay Inc. v. MercExchange, LLC* 547 U.S. 388 (2006) struck down the Federal Circuit's "general rule" in patent cases that a permanent injunction should necessarily follow a finding of infringement. Although the express elimination of the presumption of irreparable harm ended any lingering doubts, many district courts had already concluded that the presumption was likely dead.

Behind the fanfare of the Federal Circuit's confirmation that *eBay* eliminated the presumption of irreparable harm lies the body of the Federal Circuit's opinion, which, in both its tenor and conclusions, signals to defendants that avoiding permanent injunctions in the future may be more difficult than in the past since district courts began applying the tenets of *eBay*. Specifically, the court warned that, "[a]lthough *eBay* abolishes our general rule that an injunction normally will issue when a patent is found to have been valid and infringed, it does not swing the pendulum in the opposite direction." 659 F.3d at 1149. Just how far the pendulum may swing back toward the Federal Circuit's "general rule" is the subject of this analysis.

Traditional Rules of Equity

The Supreme Court has consistently reviewed injunctive relief through the prism of equitable principles. Following those principles, the Court has held that irreparable harm and the inadequacy of legal remedies form the basis for injunctive relief. *Weinberger v. Romero-Barcelo*, 456 U.S. 305, 312 (1982). Because an injunction is an equitable remedy, it is not automatic. *Amoco Production Co. v. Village of Gambell*, 480 U.S. 531, 542 (1987). Rather, the traditions of equity emphasize the power of the district court to exercise its sound discretion. 456 U.S. at 320. Analyzing the facts of the case before it, the district court must balance opposing allegations of harm and consider the effect on each party of granting or denying such relief. 480 U.S. at 542. The hallmark of equity is that "[f]lexibility rather than rigidity has distinguished it." 456 U.S. at 312 (quoting *Hecht Co. v. Bowles*, 321 U.S. 321, 329 (1944)). But before exercising its discretionary power to issue an injunction, a court should strongly consider the impact on the public of that "extraordinary remedy."

According to the Supreme Court, district courts retain full discretion in deciding whether to grant an injunction unless Congress has expressly restricted that discretion. 480 U.S. at 542. Without any such expression from Congress, statutes that permit injunctive relief as a remedy do not require it. 456 U.S. at 316. In both *Weinberger v. Romero-Barcelo* and *Amoco Production Co. v. Village of Gambell*, the Supreme Court determined that the statutes at issue did not limit the discretionary power of the district court, and concluded in each case that Congress had not

expressed or implied any intention that injunctions should automatically be issued following a violation of the statute.

Against that backdrop, the Federal Circuit forged a different philosophy in patent cases concerning injunctive relief. Because patent rights are property rights, the court considered the patent owner's right to exclude an essential element of those rights. Therefore, after a finding of infringement, a denial of an injunction ran afoul of the laws of property. *Richardson v. Suzuki Motor Co.*, 868 F.2d 1226, 1246–47 (Fed. Cir. 1989). The Federal Circuit thus embraced a “general rule” that when infringement is found, an injunction should be issued absent exceptional circumstances. *Id.* at 1247.

In 2005, the Federal Circuit reaffirmed its general rule when it reversed the district court in *MercExchange, LLC v. eBay, Inc.*, a case in which the Eastern District of Virginia denied a permanent injunction. 401 F.3d 1323, 1339 (Fed. Cir. 2005). Although the court acknowledged that in “rare instances,” district courts appropriately denied permanent injunctions, it emphasized that the circumstances justifying a denial must relate to an extraordinary public interest. *Id.* at 1338–39. In *MercExchange*, however, the Federal Circuit found nothing “sufficiently exceptional” that justified the “unusual step” of denying injunctive relief. *Id.* at 1339.

The Supreme Court in *eBay* Rejects the General Rule

Following the Federal Circuit's decision in *MercExchange*, the Supreme Court granted certiorari “to determine the appropriateness of this general rule.” To assess the rule, the Court first discussed permanent injunctions in the context of traditional equitable principles. It enumerated the four-factor test that a party moving for a permanent injunction must satisfy. The “plaintiff must demonstrate: (1) that it has suffered an irreparable injury; (2) that remedies available at law—such as monetary damages—are inadequate to compensate for that injury; (3) that, considering the balance of hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction.” *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 391 (2006).

Under this framework, the Court unanimously rejected the Federal Circuit's general rule. In the opinion, Justice Thomas explained why the treatment of injunctive relief in patent cases must be no different from that applied in all other cases, which followed naturally from precedent that a “decision to grant or deny permanent injunctive relief is an act of equitable discretion by the district court, reviewable on appeal for abuse of discretion.”

Tracking its analysis in earlier, non-patent cases, the Court reviewed the Patent Act and found no language signifying an intention by Congress to limit the district courts' discretionary powers. The Court noted, however, that the Patent Act includes provisions equating patents to personal property, which include the right to exclude. *Id.* at 392 (citing 35 U.S.C. §§ 261, 154(a)(1)). The Court also focused on Section 283 of the Patent Act, which states that courts “may grant injunctions in accordance with the principles of equity.” *Id.* at 392 n.2 (quoting 35 U.S.C. § 283).

Because of the discretion afforded to district courts by Section 283, the Court expressly rejected the use of “categorical rules” that would dictate a district court's determination of whether to

grant or deny an injunction. The Court determined that the *eBay* district court “erred in its categorical denial of injunctive relief,” and that the Federal Circuit, applying its general rule, “erred in its categorical grant of such relief.” *Id.* at 394. In conclusion, the unanimous Court stated that “[w]e hold only that the decision whether to grant or deny injunctive relief rests within the equitable discretion of the district courts, and that such discretion must be exercised consistent with traditional principles of equity, in patent disputes no less than in other cases governed by such standards.”

Two concurring opinions in *eBay*, cited often by courts granting permanent injunctions, sought to restrain district courts’ discretion within the confines of past precedent. One of the concurring opinions, that of Chief Justice Roberts, noted that from the early 1800s “courts have granted injunctive relief upon a finding of infringement in the vast majority of patent cases,” and urged that “there is a difference between exercising equitable discretion pursuant to the established four-factor test and writing on an entirely clean slate.” *Id.* at 395.

District Courts Following *eBay* Largely Avoid Categorical Rules

When determining whether to grant or deny permanent injunctions, district courts have largely attempted to follow the principles set forth in *eBay* and have faithfully applied the traditional four-part test. Although courts have been careful not to use categorical rules to support the grant or denial of injunctions, they nonetheless have gravitated toward certain fact patterns that inform their analyses. One set of recurring themes can be seen in cases in which injunctions have been granted, and another set can be seen in cases in which injunctions have been denied.

In post-*eBay* cases where permanent injunctions have been granted, several recurring fact patterns have emerged that are often used by courts as support for their determination that the four-factor test has been satisfied. Irreparable harm, for example, has often been found where the patentee directly competes with the infringer. This is especially true where the patentee can demonstrate that its market share, sales, goodwill, reputation as an innovator, or research efforts have been negatively impacted by sales of the infringing product. *ePlus, Inc. v. Lawson Software, Inc.*, 2011 WL 2119410, at *7, 11 (E.D. Va. May 23, 2011); *Smith & Nephew, Inc. v. Arthrex, Inc.*, 2010 WL 2522428, at *2 (E.D. Tex. June 18, 2010). In addition, irreparable harm is often found where a patentee’s invention lies at the core of its business, as in *Trading Techs. Int’l, Inc. v. eSpeed, Inc.*, 2008 WL 4531371, at *3 (N.D. Ill. May 22, 2008), for example.

Inadequate remedies at law, including damages, are intertwined with a finding of irreparable harm. Thus, the same facts that support irreparable harm also tend to support the inadequacy of money damages, as found in *Metso Minerals, Inc. v. Powerscreen Int’l Distribution Ltd.*, 788 F. Supp. 2d 71, 76 (E.D.N.Y. 2011). Inadequacy of damages and irreparable harm are often found where the patentee’s harm is unquantifiable, as in *ActiveVideo Networks, Inc. v. Verizon Commc’ns, Inc.*, 2011 WL 5878365, at *7 (E.D. Va. Nov. 23, 2011).

Under the balance of harms factor, courts granting permanent injunctions sometimes compare the harms that are likely to befall the patentee in the absence of an injunction, with the likely harm to the infringer in the presence of an injunction. *Power Integrations, Inc. v. Fairchild Semiconductor Int’l, Inc.*, 2008 WL 5210843, at *1 (D. Del. Dec. 12, 2008). The court states

often, however, that any harm the infringer might incur as a result of an injunction will be the direct consequence of its infringement.

The public interest is generally examined for serious or life-threatening public health or safety concerns. Courts under this high bar generally find that these issues are not implicated, or that they can be mitigated under a provision of the injunction. Counterbalanced against any public health interest is often the public's "interest in a strong patent system." *Smith & Nephew*, 2010 WL 2522428, at *5. In other words, the public interest is generally served by enjoining infringers.

The statutory right to exclude is frequently cited by courts in support of granting a permanent injunction. The court typically invokes this right while still acknowledging that under *eBay* the statutory right to exclude alone is insufficient to justify an injunction. *ePlus*, 2011 WL 2119410, at *6.

Where permanent injunctions have been denied, courts have often considered the following circumstances under the irreparable harm or inadequacy of legal remedies factors to provide support: (1) lack of direct competition in the same market between the patentee and the infringer, or competition between more than two competitors in which the patentee cannot show a relationship between the infringer's sales and harm suffered by the patentee; (2) licensing by the patentee to other competitors, or systematic licensing of the patents at issue; (3) small relative size or importance of the inventive technology compared with the accused product as a whole; and (4) adequacy of money damages. *Accentra Inc. v. Staples, Inc.*, 2011 WL 7563039, at *28 (C.D. Cal. Dec. 19, 2011) (competition); *Advanced Cardiovascular Sys., Inc. v. Medtronic Vascular, Inc.*, 579 F. Supp. 2d 554, 558-59 (D. Del. 2008) (multiple competitors); *Johnson & Johnson Vision Care, Inc. v. Ciba Vision Corp.*, 712 F. Supp. 2d 1285, 1287-89 (M.D. Fla. 2010) (licensing); *LaserDynamics, Inc. v. Quanta Computer, Inc.*, 2010 WL 2574059, at *2 (E.D. Tex. June 22, 2010) (small proportion); *Conceptus, Inc. v. Hologic, Inc.*, 2012 WL 44064, at *2-3 (N.D. Cal. Jan. 9, 2012) (adequacy of money damages).

Courts' assessment of the balance of harms factor has typically weighed the size of and potential harm to the patentee relative to the size of and potential harm to the infringer. *LG Elecs. U.S.A., Inc. v. Whirlpool Corp.*, 798 F. Supp. 2d 541, 564 (D. Del. 2011). The balance of harms factor and the public interest factor generally play roles secondary to the first two factors. Occasionally, however, the public interest factor plays a key part in supporting the denial of a permanent injunction, even where dire health consequences are not implicated. *Johnson & Johnson Vision Care*, 712 F. Supp. 2d at 1292-93. Of course, where the removal of a medical device from the market poses life-threatening risks, courts invariably find that public interest weighs heavily against granting an injunction. *Bard Peripheral Vascular, Inc. v. W.L. Gore & Assocs., Inc.*, 2009 WL 920300, at *8 (D. Ariz. Mar. 31, 2009).

In addition, courts denying injunctions routinely focus on the burden of proof—which *eBay* places squarely on the patentee—and on the patentee's inability to provide sufficient evidence to satisfy that burden. As aptly stated by the district court in *MercExchange, L.L.C. v. eBay, Inc.* on remand, "putting *the onus on the plaintiff* to prove irreparable harm is much more than an idle

exercise as numerous case-specific facts may weigh against the issuance of an injunction, notwithstanding the nature of the patent holder's right." 500 F. Supp. 2d 556, 569 (E.D. Va. 2007) (emphasis in original). Thus, even where facts tend to favor an injunction, courts will often cite as fatal to a motion for injunctive relief a patentee's failure to provide sufficient evidence of irreparable harm or inadequacy of money damages. *Advanced Cardiovascular*, 579 F. Supp. 2d at 560; *Edwards Lifesciences AG v. CoreValve, Inc.*, 2011 WL 446203, at *15 (D. Del. Feb. 7, 2011); *Presidio Components Inc. v. Am. Technical Ceramics Corp.*, 723 F. Supp. 2d 1284, 1336–37 (S.D. Cal. 2010); *Humanscale Corp.* District courts recognize that, although *eBay* did not identify the "quantum" of evidence necessary to support a permanent injunction, the patentee in every instance must establish the irreparability of its harm. *eBay Inc. v. MercExchange, LLC*, 500 F. Supp. 2d at 577–78.

The Pendulum Swings Back

In 2010, the district court in *Robert Bosch, LLC v. Pylon Manufacturing Corp.* denied Bosch's motion for a permanent injunction. The court concluded that Bosch failed to satisfy its burden of demonstrating that such relief was justified. *Robert Bosch LLC v. Pylon Manufacturing Corp.*, 748 F. Supp. 2d 383, 407 (D. Del. 2010). It acknowledged the Supreme Court's rejection of "categorical rules, classifications, and assumptions in permanent injunction analyses," but then identified several trends common to cases in which injunctions had been granted. These included the circumstances discussed above, such as where the plaintiff practices its invention, the parties are direct competitors, and the invention comprises the core of the plaintiff's business. *Id.* at 407–08.

The district court held that "Bosch has failed to show that it would suffer irreparable harm absent a permanent injunction." *Id.* at 408. The court also noted Bosch's failure to sufficiently define the relevant market, as well as the parties' failure to disclose their market shares. Together, the evidentiary failures, presence of multiple competitors, and the non-core nature of the patented technology provided the court's justification for its denial.

The Federal Circuit reversed and remanded, directing the court to enter an injunction. *Robert Bosch LLC v. Pylon Manufacturing Corp.*, 659 F.3d at 1145. After confirming that the presumption of irreparable harm was eliminated by the Supreme Court in *eBay*, the court seemed to adopt the sentiments contained in *eBay*'s concurring opinions. Specifically, the court stated that the "abolition of categorical rules and the district court's inherent discretion to fashion equitable relief" do not "mandate that district courts must act on a clean slate." *Id.* at 1149. Rather, standards developed by the Federal Circuit over the last 25 years should "inform the four-factor inquiry and, in particular, the question of irreparable harm." *Id.* at 1150. According to the Federal Circuit, by "ignoring these standards, and supplanting them with its own," the district court "committed legal error by the weight given to the factors cited, and made a clear error in judgment in its analysis of the irreparable harm factor."

To support its denial, the Federal Circuit labeled as legal error the district court's reliance on the presence of multiple competitors in the market and the small size of Bosch's wiper blade technology relative to its entire business. In explaining this ruling, the court arguably

mischaracterized the district court’s analysis. The Federal Circuit stated that the lower court erred in “concluding that the absence of a two-player market *effectively prohibits* a finding of irreparable harm,” and also in concluding that “if a fact supports the granting of an injunction, its absence *likely compels* denial of one.” *Id.* at 1151–52. The district court neither expressed nor implied either of these conclusions.

The Federal Circuit in *Bosch* further criticized the reasoning it attributed to the district court by stating that, “[w]hile the existence of a two-player market may well serve as a substantial ground for *granting* an injunction . . . the converse is not automatically true . . .” *Id.* at 1151 (emphasis in original). However, the district court never came close to resorting to such categorical reasoning.

Most important, by finding legal error in the weight the district court gave to certain evidence—or lack thereof—the Federal Circuit appeared to meddle with the district court’s exercise of discretion. Further, in finding that the district court “erred in attributing weight,” implying *any* weight whatsoever to the “non-core nature of Bosch’s wiper blade business,” the court came very close to establishing a new categorical rule of its own. *Id.* at 1152.

The opinion further stated that the lower court “committed a clear error in judgment when it concluded that Bosch failed to demonstrate irreparable harm.” The court cited, among other things, “undisputed evidence of direct competition”; “unrebutted evidence of loss of market share and access to potential customers”; and “unrebutted” evidence of irreversible price erosion demonstrating that Bosch’s harm was irreparable. *Id.* at 1152–54. The court found it important that in the mass-merchandise segment of the industry, Bosch secured Wal-Mart as a customer, lost their business to Pylon. Although noting that it was Bosch’s failure to timely deliver its product that caused the loss of Wal-Mart’s business, the court credited testimony of a Bosch executive as evidence that Bosch’s inability to re-acquire the Wal-Mart account—or other mass-merchandise business—as showing that Bosch suffered irreparable harm at the hand of Pylon. *Id.* at 1153–54.

In addition, the court highlighted evidence that Pylon might not be able to satisfy a judgment for past or future damages, and pointed to the company’s failure to provide evidence to the contrary as supporting a finding of irreparable harm. *Id.* at 1154–55. In this and other contexts, the court emphasized the lack of rebuttal evidence provided by the infringer. In another example, the court faulted Pylon for providing no evidence to rebut Bosch’s “prima facie showing” of lost market share. *Id.* at 1154. By requiring Pylon to put forth evidence that the harm to Bosch was not irreparable, the court appeared to place the onus on the defendant to disprove irreparable harm.

The court concluded that together with its determination that the remaining factors also supported an injunction, there was “no basis on which the district court rationally could have concluded that Bosch failed to demonstrate irreparable harm, or that a remedy other than an injunction is sufficient to address its harm.” *Id.* at 1155. As a result, the court reversed and remanded the case with instructions that an injunction be entered.

Circuit Judge Bryson, dissenting in part, disagreed that the record compelled the court to enjoin Pylon. Judge Bryson explained that “injunctive relief is a fact-intensive inquiry that requires a

careful balancing of competing equitable concerns, none of which is dispositive.” *Id.* at 1157. Therefore, he argued, weighing the competing facts is a function purely of the district court—echoing the mandate of *eBay*. *Id.* at 1157–58.

Further, Judge Bryson questioned the sufficiency of the evidence cited by the majority, finding that the evidence supplied by Bosch regarding the loss of market share, price erosion, loss of customers, and loss of access to new customers was not compelling. Noting that the majority appeared to shift the burden to the defendant, the dissent asserted that the evidence “was not so clear-cut that those issues can be resolved based on a shifting of the burden of proof.” Judge Bryson urged his colleagues not to usurp the district court’s discretion by directing it to enter an injunction without further analysis. *Id.* at 1158.

Looking Forward

The Federal Circuit in *Bosch* has seemingly aligned itself with the concurring opinions in *eBay*. Because courts in patent cases historically have granted injunctions in all but extreme circumstances, courts’ discretionary ability to deny permanent injunctions must be molded within the framework of pre-*eBay* Federal Circuit precedent. This view, however, seems to ignore the main thrust of the unanimous opinion in *eBay*, which is that the decision to grant or deny an injunction is to be decided by the district court exercising its sound discretion under traditional equitable principles.

Nonetheless, *Bosch* makes it more likely that an injunction will be issued almost as a matter of course where the parties compete and seems to lower the bar for the “quantum” of evidence needed to support an injunction. So although district courts will continue to avoid overt categorical rules, with the imprimatur of the Federal Circuit, they may be emboldened to wield the vestiges of categorical rules to justify a post-*eBay* grant of an injunction that otherwise should not be issued.

Keywords: litigation, intellectual property, permanent injunction, irreparable harm, patent infringement, patent rights, injunctive relief

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Section 101: A Defense to Assert Early (and Often)

By Charles A. Bieneman – September 12, 2012

For all of the recent turmoil and uncertainty surrounding patent-eligible subject matter, accused patent infringers know that today, invalidity under 35 U.S.C. § 101 is a viable defense against a wide variety of claims, and Section 101 invalidity is a defense that courts cannot ignore. Although some judges are decidedly unenthusiastic about confronting questions of patent-eligibility, in recent decisions, the U.S. Supreme Court has called Section 101 analysis a “threshold test” (*Bilski v. Kappos*, 561 U.S. ___, 130 S. Ct. 3218, 3225 (2010)), and stressed that other provisions that give rise to invalidity defenses—for example, 35 U.S.C. §§ 102, 103, and 112—are not “equipped” to perform the “screening function” provided by Section 101. *Mayo Collaborative Services v. Prometheus Laboratories, Inc.*, ___ U.S. ___, 132 S. Ct. 1289, 1304 (2012).

Nonetheless, some lower courts—notably exemplified by the majority opinion in *MySpace, Inc. v. Graphon Corp.*, 672 F.3d 1250 (Fed. Cir. 2012)—have openly stated their policy of deferring patent-eligibility questions until all other validity issues are decided. Attorneys, however, may find this reluctance frustrating. To paraphrase the late Justice Potter Stewart, most experienced practitioners will tell you that upon reading certain patent claims, they know potential Section 101 invalidity when they see it. So what is an accused infringer to do?

What Factors Govern Raising a Section 101 Defense?

In the wake of courts’ varying degrees of receptiveness toward evaluating patent-eligibility, accused infringers must consider when and under what procedural mechanisms to raise the defense of Section 101 invalidity. First, a defendant will want to assert the defense in a way and at a stage in the case when the court is most likely to be favorably disposed to it. But before the likelihood of success can be a factor, one must also consider the odds that the trial court will address rather than defer the issue. Thus, there are several factors that an accused infringer must weigh in deciding whether and how to mount a Section 101 defense.

Can patent-eligibility under Section 101 be decided before the court has performed claim construction—and if so, can Section 101 be addressed in a motion to dismiss or for judgment on the pleadings under Rule 12 of the Federal Rules of Civil Procedure? Or, are arguments for invalidity under Section 101 more properly brought as motions for summary judgment under Rule 56 of the Federal Rules of Civil Procedure?

The answers to these questions—as with all questions of litigation tactics—depend on more than what arguments are justified by both the applicable procedural and substantive law. One must also consider how receptive a court will be to a party’s arguments, regardless of how well-justified those arguments are under the applicable law. And as the divergent opinions in *MySpace* demonstrate, some judges may be reluctant to entertain arguments under Section 101.

MySpace and the Debate on When Patent-Eligibility Should Be Addressed

The opinion of the majority panel in *MySpace*, which came after *Bilski* but before *Prometheus*,

provides a candid look at the antipathy that many judges have when approaching the task of evaluating patent-eligibility under Section 101 (the *dicta* of the Supreme Court notwithstanding). All three panelists in *MySpace* agreed that the claims directed to creating users' entries in a computer database were invalid. The panel majority, however—Judge Plager and Judge Newman—rejected the notion that the claims needed to be evaluated under Section 101 before other bases of invalidity could be considered.

The *MySpace* majority acknowledged support for the position that Section 101 presented an antecedent threshold analysis, and then explicitly rejected this approach. “The problem with addressing § 101 initially,” Judge Plager’s majority opinion explained, is that the exercise involves the difficult task of determining whether an invention embodies an “abstract idea”—whether, “in the broad sweep of modern innovative technologies, does this invention fall outside the breath of human endeavor that possibly can be patented under § 101?” *MySpace*, 672 F.3d at 1258. Difficulties in understanding what constitutes “abstract ideas,” Judge Plager continued, have resulted in “indeterminacy of the law governing patents . . . becoming an even greater problem now” than in the past. *Id.* at 1259. Better to rely, wherever possible, on Sections 102, 103, and 112, whose “criteria are well developed and generally well understood.” *Id.* at 1260.

Judge Mayer’s dissent, in contrast, cited copious authority for the proposition that Section 101 presents a threshold question that must be decided before other invalidity analyses are undertaken. *Id.* at 1264. He was of the view that Sections 102, 103, and 112 had done a poor job of weeding out questionable patents, and disagreed with the notion that Section 101 should be used as a “coarse eligibility filter.” *Id.* at 1268. He also would have considered the Section 101 question even though it had not been addressed by the trial court, and invalidated Graphon’s patent claims because they were “significantly broader in scope and [had] the potential to wield far greater preemptive power than those at issue in *Bilski*.” *Id.* at 1264.

Although Judge Mayer’s position concerning the procedural role of Section 101 seems to be supported by the Supreme Court, any consideration of when and how to assert a Section 101 invalidity defense must be cognizant of judicial attitudes reflected by the *MySpace* majority. With these attitudes in mind, what principles should guide a defendant's Section 101 strategy?

Is Claim Construction Necessary for Section 101 Analysis?

Relatively few courts appear to have addressed the issue of claim construction as a necessary prerequisite to determining patent-eligibility under Section 101. Most courts considering the issue, however, found that claim construction is *not* necessary for determining patent-eligibility. *Bancorp Servs., L.L.C. v. Sun Life Assur. Co. of Can.*, 771 F. Supp. 2d 1054, 1059 (E.D. Mo. 2011), seems to be representative in deciding to take up the defendant’s “§ 101 arguments before proceeding with claims construction.” The *Bancorp* court, which granted a motion of summary judgment of invalidity under Section 101, explained that claim construction is not necessary for Section 101 analysis where changing the construction of claim terms relevant to the determination of patentable subject matter would not change the analysis. In *Bancorp*, for example, the court found no “meaningful distinction in the analysis of ‘process’ claims versus ‘system’ claims.”

Similarly, in *Nazomi Communications, Inc. v. Samsung Telecommunications, Inc.*, No. C-10-05545, 2012 U.S. Dist. LEXIS 39468, *10 (N.D. Cal. March 21, 2012), the plaintiff argued that the defendant’s motion for invalidity under Section 101 was premature, but the court went on to consider the motion anyway—and to find that the plaintiff’s claims were patentable under Section 101. Further, in *Digitech Information Systems, Inc. v. BMW Financial Services NA, LLC*, No. 6:10-cv-1373, 2012 U.S. Dist. LEXIS 44480, *5–7 (M.D. Fla. March 30, 2012), the court found that claim construction was unnecessary to a Section 101 analysis where “computer” was the only term the plaintiff pointed to as requiring construction for patent-eligibility analysis in order to proceed.

A number of courts have considered patentability under Section 101 at the pleadings stage before any could have taken place, much less claim construction. In *Graff/Ross Holdings LLP v. Fed. Home Loan Mortg.*, No. 07-796, 2010 U.S. Dist. LEXIS 141399, *6–7 (D. D.C. Aug. 27, 2010), the court converted a motion to dismiss to a motion for summary judgment, but found itself able to address, and grant, the motion without claim construction having taken place. In *Glory Licensing LLC v. Toys “R” Us, Inc.*, No. 09-4252, 2011 U.S. Dist. LEXIS 51888, *2–3, 18 (D. N.J. May 16, 2011), the court found that the patent claims at issue were “addressed to abstract ideas” without performing claim construction. (The *Glory Licensing* court acknowledged claim constructions performed by another court addressing related patents, but these were not a factor.) Even a court denying a motion for judgment of invalidity on the pleadings under Rule 12(c) of the Federal Rules of Civil Procedure did so without mentioning the question of claim construction. *IconFind, Inc. v. Google, Inc.*, No. 2:11-cv-0319, 2012 U.S. Dist. LEXIS 5460 (E.D. Ca. Jan. 18, 2012).

This is not to say that courts never consider claim constructions when evaluating patent-eligibility, but even in cases where claim construction comes into play, it may not be crucial. In *Dealertrack, Inc. v. Huber*, 674 F.3d 1315, 1332 (Fed. Cir. 2012), for example, the trial court’s claim constructions weighed in its determination that the claims at issue failed the machine-or-transformation test. The Federal Circuit likewise considered these constructions and ultimately decided that the claim terms were simply too abstract to be patentable. *Id.* at 1333–34. One must wonder, however, whether the Federal Circuit’s result in *Dealertrack* would have been different had claim construction not taken place.

Some trial courts, leery of tackling patent-eligibility, may be prone to defer the issue until after claim construction or until other bases of invalidity can be considered. In general, however, accused infringers have a strong basis for arguing that a district court can and should address patent-eligibility regardless of the status of claim construction.

How to Put the Issue of Patent Eligibility Before the Court

Let us assume that in any colorable case, an accused infringer will move for a judgment of invalidity under Section 101 before trial. If claim construction is not a prerequisite, such a motion can likely be brought in a variety of guises any time after a complaint is filed until the court’s deadline for filing dispositive motions prior to trial. So, when *should* a motion for a judgment of invalidity under Section 101 be brought? Should a defendant move for dismissal in

response to the plaintiff's complaint? Is there any advantage to moving for a judgment on the pleadings as discovery gets underway, or should the defendant bring a summary judgment motion at the time of claim construction—or sometime thereafter?

The answers to these questions will vary according to the tactical considerations in play in each particular case, but unlike other invalidity motions, a motion for a judgment of invalidity under Section 101 generally does not require recourse to discovery materials or any documents other than the patent owner's pleading of patent infringement and the asserted patent(s). The asserted patents should be attached to the complaint and should be considered part of the pleadings. Unlike other invalidity arguments, Section 101 analysis usually does not require claim construction, so since the issue of patent-eligibility can generally be decided on the pleadings alone, there are good arguments for bringing a motion for a judgment under Section 101 early in a case—perhaps even as part of an accused infringer's first filed response to claims of infringement.

Rule 12 of the Federal Rules of Civil Procedure provides two main vehicles for early consideration of patent-eligibility. Rule 12(b)(6) provides for motions to dismiss based on a “failure to state a claim upon which relief can be granted,” while Rule 12(c) provides that “[a]fter the pleadings are closed—but early enough not to delay trial—a party may move for judgment on the pleadings.” Rule 12(d) allows the motion to be treated as one for summary judgment under Rule 56 if “matters outside the pleadings are presented to and not excluded by the court.”

Because a motion for summary judgment of invalidity under Section 101 will likely rely on neither discovery nor other outside materials, and makes arguments based solely on the complaint for patent infringement—including the asserted patent(s) is incorporated into the complaint or other pleading—Rule 12(d) generally should not be an issue. *See, e.g., Glory Licensing*, 2011 U.S. Dist. LEXIS 51888, at *2–3 (granting Rule 12(b)(6) motion without considering outside material or invoking Rule 12(d)); *IconFind*, 2012 U.S. Dist. LEXIS 5460 (denying Rule 12(c) motion but nowhere mentioning Rule 12(d)).

Because Rule 12(c) requires pleadings to be closed—that is, for an answer to have been filed to all claims and counterclaims, and because a judge is not necessarily required to take up a Rule 12(c) motion for a case to move forward—a Rule 12(b)(6) motion may be preferred for forcing consideration of Section 101 as early as possible. But even under Rule 12(b)(6), a court could take the position that claim construction was a necessary prerequisite to the determination of patent-eligibility. Furthermore, for various reasons, an accused infringer may not be ready to file a substantive motion on Section 101 within 21 days of being served, and Rule 12(c) motions still stand a good chance of getting a court to provide early consideration of patent eligibility.

The downside is that an unsuccessful Section 101 argument at the pleadings stage may make it more difficult, or practically impossible, to raise the issue later. An accused infringer probably does not want to be in the position of arguing that a particular claim construction is necessary to support a finding of invalidity, which could be the case if a court denies a Rule 12 motion on the

basis that a non-construed claim term may render a claim patent-eligible. An argument lost once is often harder to win if made a second time.

Regardless of when and how an accused infringer moves for judgment of invalidity under Section 101, cases since *Bilski* make clear that good grounds exist for arguing that a court should address the issue before claim construction and before other potential invalidity bases are explored.

Conclusion

A motion for a judgment of invalidity under 35 U.S.C. § 101 may be brought at various stages of litigation. Statements by the U.S. Supreme Court, and decisions of lower courts, show that Section 101 presents a threshold issue that is ripe for decision generally very early—perhaps as soon as a complaint is filed. The best option for asserting a Section 101 defense may be a motion to dismiss under Rule 12(b)(6) because a motion to dismiss can be filed in lieu of an answer. A motion for judgment on the pleadings under Rule 12(c) may be an attractive option because patent-eligibility generally can be decided simply by referring to the patents-in-suit, without recourse to matters outside the pleadings. Whether Rule 12(c) or under the summary judgment provisions of Rule 56, a motion for a judgment of Section 101 invalidity often need not await claim construction. A defendant faced with asserted patents whose claims appear at all suspect under Section 101 should formulate—and possibly execute—a strategy for asserting a Section 101 defense as early in a lawsuit as possible.

Keywords: litigation, intellectual property, patent-eligibility, Section 101

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Use-Based Damage Theory Garners an Unreasonable Royalty

By Konrad Sherinian – September 12, 2012

A reasonable royalty for the use of an invention by an infringer sets the floor for damages that a patent holder can recover, but the recent case of *Michael S. Powell v. The Home Depot USA, Inc.*, 663 F.3d 1221 (Fed. Cir. 2011), conclusively demonstrates that a reasonable royalty is not always less than what would be recovered by way of lost profits. *Powell* also demonstrates the power of use-based theories in assessing a reasonable royalty, and how in certain circumstances, it can lead to significantly higher dollar awards than sales-based theories or lost profits.

In *Powell*, the patentee had a long-standing business relationship with Home Depot. He was the company's point of contact for the installation and maintenance of radial saws in each of its stores. Home Depot used the radial saws—as did many of their competitors—to cut lumber to customer-specified dimensions. Cut lumber was, in many ways, integral to Home Depot's strategy to be a "one-stop shop" for contractors.

But the company had a very serious problem. The radial saws at its stores resulted in numerous injuries to employees—with lacerations and finger amputations being most common. In addition to harm caused to employees, the number of lawsuits filed and the subsequent compensation employees were paid had grown significantly.

Lowes's, one of Home Depot's competitors, decided that despite the utility that cut lumber offered its customers, the radial saws were simply too dangerous and stopped offering cut lumber. Home Depot CEO Robert Nardelli became aware of the issue and told his management team to find a solution or the radial saws would be removed. The team that Home Depot assigned to examine the issue, however, concluded that while injury claims were costing the company more than \$1 million a year, the extra sales generated by cut lumber outweighed the cost of the injuries to employees. Home Depot, therefore, set out to find a way to make the radial saws safe.

Independent contractor Michael Powell realized that his business of installing and maintaining radial saws depended on Home Depot continuing to provide cut lumber. He created a saw guard that would protect employees from injury while using the saws and demonstrated his invention to Home Depot in July 2004. The company ordered eight prototypes, which were installed in Home Depot stores the following month, and Powell applied for a patent for his saw guard. Unbeknownst to Powell, however, Home Depot was not satisfied in paying approximately \$2,000 per saw guard.

In an effort to obtain a better price, Home Depot showed Powell's saw guards to Georgia-based manufacturer Industriaplex and asked the company if it could produce saw guards for less than \$2,000 per unit. Industriaplex agreed, and eventually sold Home Depot nearly 2,000 saw guards at a price of \$1,295 each.

Powell continued discussions with Home Depot but could not come to an agreement to produce saw guards at the price the company was willing to pay—\$1,200 per saw guard, including installation.

Powell's patent was issued in May 2006, and he sued Home Depot a year later. He was awarded \$15 million in damages (later increased by \$3 million in enhanced damages and \$2.8 million due to willful infringement by Home Depot), or approximately \$7,736 per infringing radial saw, following a jury trial. This award was approximately \$11,122,000 more than the total revenue Powell would have received—using the \$2,000/unit he charged Home Depot in 2004—if Home Depot had initially purchased the radial saws from him. The award was also approximately \$12,488,995 more than Home Depot paid Industriaplex to build and install the infringing saw guards.

On appeal, the Federal Circuit ruled—apparently for the first time in history—that lost profits are not a cap on the value of a reasonable royalty in a patent case. While the previous cases of *Golight v. Wal-Mart Stores*, 355 F.3d 1327 (Fed. Cir. 2004), and *State Industries v. Mor-Flo Industries*, 883 F.2d 1573 (Fed. Cir. 1989), established that a reasonable royalty could exceed an infringer's net profit margin, Home Depot argued that the upper bounds of Powell's damages was the amount that he had agreed to take in exchange for providing the radial saw guards during their 2004 negotiations. This amount was a number that Home Depot conservatively estimated at \$2,180 per radial saw guard, but the Federal Circuit rejected this argument for two reasons.

First, while the court acknowledged that Powell would have supplied Home Depot with radial saw guards for \$2,180 per radial saw guard in 2004, the correct point of reference was when the infringement began with the issuance of Powell's patent in May 2006. Home Depot by then had nearly two years to observe the effectiveness of Powell's radial saw guards—as manufactured and installed by Industriaplex—in preventing the types of laceration and amputation injuries that its employees had been suffering. This additional objective evidence of effectiveness could have persuaded Home Depot to pay a higher price than when Powell first demonstrated the saw guards two years prior.

Second, while the court acknowledged that both an infringer's net profit margin and a patentee's profit expectation could be used as factors in determining a reasonable royalty, neither set a ceiling on what a reasonable royalty can be. In particular, the court stated that “damages to the patent holder cannot simply be calculated in all cases by determining the difference between his pecuniary condition after the infringement, and what his condition would have been if the infringement had not occurred” (quoting *Yale Lock Manufacturing v. Sargent*, 117 U.S. 536, 552 (1886)).

In addressing the question of whether substantial evidence supported the jury's verdict, the court found that Powell presented extensive evidence of the benefit that Home Depot received from the radial saw guards. This evidence included the directive of CEO Robert Nardelli that the rate of employee injuries was not acceptable and the radial saws must be fixed or removed; the cost of employee injuries resulting from radial saws was in excess of \$1 million per year; one of Home Depot's chief competitors—Lowe's—made the decision to remove radial saws from its

stores and no longer offered cut lumber; continuing to offer cut lumber gave Home Depot a significant competitive advantage over Lowe's and others due not only to the sale of cut lumber, but also from add-on purchases of nails, hinges, and other goods that are often purchased with cut lumber; and not one injury occurred in stores where infringing saw guards were installed. Based on this evidence, Powell's damages expert submitted a range for the reasonable royalty bounded on the lower end by the \$2,180 that Powell had agreed to supply Home Depot for in 2004, to an upper range of \$8,500—or less than 8.5 percent of the savings that Home Depot enjoyed from the use of the saw guard.

Home Depot attempted to counter this use-based evidence by arguing that a reasonable royalty would be three to five percent of the \$1,295 it paid Industriaplex (in other words, \$38–\$65 per saw). As an upper range, Home Depot argued that Powell was willing to deliver the saw guards for \$2,180 in 2004, and therefore a reasonable licensee would never pay more than that. The Federal Circuit largely rejected these arguments as “nothing more than what it might have preferred to pay,” citing its en banc decision in *Rite-Hite v. Kelley*, 56 F.3d 1538, 1554–55 (Fed. Cir. 1995).

It should be noted that *Powell* presents a relatively rare set of facts that make what nominally appears as a poor damages case into a superior damages case. In particular, Powell likely would not have recovered his cost of litigation if he had pursued a standard percent-of-sales theory in determining a reasonable royalty. In addition, he would have had to overcome additional evidentiary hurdles, such as those imposed by *Uniloc USA v. Microsoft*, 632 F.3d 1292 (Fed. Cir. 2011), regarding the application of the entire-market-value rule.

By marshaling use-based evidence, however, Powell was able to impose a much higher royalty on Home Depot. His attorneys recognized that his saw guards had a measurable benefit to the company far beyond the amount that he set for Home Depot prior to the issuance of his patent. Accordingly, plaintiffs in patent cases should at least consider a use-based damage theory for trial.

Defendants, however, can counter a use-based damage theory by presenting a noninfringing alternative to the infringing product. By presenting a noninfringing alternative, a defendant can cap damages to a quantity approximated by the cost of the noninfringing alternative, accounting for any improvement in performance of the infringing product. *See Riles v. Shell Exploration and Production*, 298 F.3d 1302, 1312 (Fed. Cir. 2002) (the market does not award a royalty divorced of all relation to a potential noninfringing alternative method); *Grain Processing v. American Maiz*, 185 F.3d 1341, 1347 (Fed. Cir. 1999) (the difference in production cost between an infringing and a noninfringing product capped the reasonable royalty award).

If Home Depot produced a noninfringing alternative saw guard that worked as well as Powell's and cost \$2,800 per saw guard, damages would have been capped at \$2,800 per unit, which is far closer to the value that a sales-based theory would have produced. Therefore, while *Powell* and use-based damage theories provide another tactic for patent plaintiffs to generate higher damages, it is likely to be a little-used tool, given that use-based damage theories have relatively narrow applicability, and they are susceptible to being diffused by the presentation of a

noninfringing alternative. This noninfringing alternative effectively caps the reasonable royalty to the difference in cost of the noninfringing and infringing products accounting for any improvement in performance of the infringing product.

Keywords: litigation, intellectual property, use-based damage theory, sales-based damage theory

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NEWS AND DEVELOPMENTS

Christensen Brothers Win Appeal Against USA Network

“The Force” of law was with Hayden Christensen—famous for his role as Anakin Skywalker in the *Star Wars* prequels—and his brother, Tove Christensen, last month, when the U.S. Court of Appeals for the Second Circuit overturned an order of the U.S. District Court for the Southern District of New York that had granted defendant Universal Television Network’s [motion to dismiss](#) the Christensen brothers’ lawsuit against the network. The suit, *Forest Park Pictures v. Universal Television Network, Inc.* (the television production arm of NBCUniversal, a subsidiary of Comcast Corp., which controls USA Network), was originally brought in 2010 and alleges a breach of contract between Forest Park Pictures, the brothers’ production company, and Universal Television Network over USA Network’s show, *Royal Pains*.

The suit alleges that in 2005, Forest Park developed an idea for a show called *Housecall*, “in which a doctor, after being expelled from the medical community for treating patients who couldn’t pay, moves to Malibu and attends to the rich and famous.” Forest Park created a series treatment for the concept that included storylines and character bios, and the Christensen brothers met with Alex Sepiol, a programming executive at USA Network, to pitch the idea. The brothers allege that, although Sepiol was receptive to the idea, nothing ever materialized after the meeting. Subsequently, in 2009, USA began airing *Royal Pains*, a show that the brothers claim is a rip-off of their concept for *Housecall* that focuses on the life of a “concierge doctor” providing medical services to the wealthy residents of the Hamptons.

Judge Colleen McMahon had originally dismissed the suit on the grounds that the claims brought against USA Network were preempted by the [Federal Copyright Act](#). She ruled that, because the allegations entailed the theft of uncopyrightable ideas, the suit had no merit. The Second Circuit, however, disagreed, based largely on the fact that the plaintiffs chose to allege [breach of implied contract](#) rather than copyright infringement. The Second Circuit ruled that a claim under state law for breach of implied contract, including a promise to pay, is quantitatively different from a suit to vindicate a right included in the Copyright Act and is therefore not subject to federal preemption.

Judge John M. Walker Jr., writing for the Second Circuit, [explains](#) [PDF] that, even though uncopyrightable material may fall within the subject matter of the Copyright Act, the equivalency requirement for preemption is not met in this case because “extra elements” exist that create qualitative differences between a contract claim and a copyright-violation claim. Among other things, the Copyright Act, unlike contract law, “does not provide an express right for the copyright owner to receive payment for the use of a work.” The court, accepting the plaintiffs’ version of the facts as true for the purpose of the motion, concluded that an implied contract, including a promise to pay, was formed on the Christensen brothers pitching their show concept to Sepiol and that USA Network’s failure to compensate Forest Park Productions for *Royal Pains* gave rise to a cause of action not subject to preemption. The court also ruled on two other issues, holding that, based on the choice of law rules for a federal court in New York sitting

in diversity jurisdiction, California law should be applied in this case and that, in addition to the court's finding of no preemption, the plaintiffs' complaint is adequate under the Supreme Court standards in [Twombly and Iqbal](#).

The Second Circuit's ruling comes on the heels of another important decision for the entertainment industry, [Montz v. Pilgrim Films & Television, Inc.](#) In that suit, NBCUniversal suffered a big loss when the U.S. Court of Appeals for the Ninth Circuit ruled that a state-based contract allegation surrounding the Syfy Channel's *Ghost Hunters* was not preempted by federal copyright law and could be brought even though a copyright claim had been dismissed; the Supreme Court subsequently denied a petition for certiorari. Together, these two rulings present significant new challenges for studios in defending themselves against [idea-theft lawsuits](#), especially because the two decisions come from circuits that cover the two main entertainment hubs of the United States—New York and Los Angeles. Studio execs and legal teams will likely pay close attention to see how the Christensen suit ultimately plays out on remand to the Southern District of New York.

The Christensen brothers and Forest Park Productions are represented by David Marek of Liddle & Robinson, LLP. Universal Television Network, Inc., is represented by Susan Weiner, deputy general counsel for NBCUniversal Media LLC, as well as Robert Penchina and Amanda M. Leith of Levine, Sullivan, Koch & Schulz, LLP.

Keywords: litigation, intellectual property, Royal Pains, Christensen, breach of contract, copyright, preemption, idea-theft

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