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### ***Patents / Validity (Litigation)***

#### **Supreme Court Affirms Clear and Convincing Standard of Patent Invalidation Proof**

by Jeremiah Armstrong and Paul Devinsky

Delivering what is likely the final blow to its battle against a \$240 million infringement judgment, the Supreme Court of the United States unanimously rejected Microsoft's plea to modify the clear and convincing evidence standard of proof required to invalidate a patent. *Microsoft v. i4i*, Case No. 09-1504 (Supr. Ct., June 9, 2011) (Justice Sotomayor) (Justices Breyer and Thomas, concurring).

The appeal stems from a 2009 jury verdict that certain versions of Microsoft Word were found to infringe plaintiff i4i's patent related to editing and formatting XML documents. Microsoft challenged the validity of the patent, based on the §102(b) on-sale bar, citing i4i's sales of a software product called S4 more than a year before applying for the asserted patent. The S4 product was never presented to the U. S. Patent and Trademark Office (USPTO) examiner.

The U.S. Court of Appeals for the Federal Circuit [squarely rejected](#) Microsoft's argument that the jury should have been instructed to apply a preponderance of the evidence standard of proof to the issue of patent invalidity. The Federal Circuit [also rejected](#) Microsoft's request to reduce the willful damages award, partially due to Microsoft's failure to file a pre-verdict judgment as a matter of law (JMOL).

## History

Microsoft petitioned the Supreme Court for *certiorari* to consider whether an accused infringer that challenges patent validity based on prior art not considered by the USPTO during prosecution must overcome the 35 U.S.C. §282 presumption of validity by "clear and concurring evidence" or whether some lower standard of proof will suffice (see [IP Update, Vol. 13, No. 12](#)).

The "clear and concurring" standard of proof has been used by Federal Circuit since its pronouncement in the seminal 1984 case, *American Hoist & Derrick v. Sowa & Sons*. Prior to the 1982 establishment of the Federal Circuit,

most of the regional courts of appeal applied the less differential “preponderance” standard to the issue. However, the Federal Circuit, in setting its rule, took note of the “the deference that is due to a qualified government agency presumed to have properly done its job.”

Microsoft, in its *certiorari* petition, was supported for review of the Federal Circuit standard of proof by 11 *amici* representing major corporations, law professors and trade associations. Most of the *amici* faulted the deference given to the USPTO examiners who have limited time and resources for the examination of any particular application, who examine applications on a strictly *ex parte* basis and who only infrequently consider non-patent prior art publication or prior products. The *amici* also note that juries already tend to give undue deference to the decision of the USPTO in issuing a patent, especially in cases where the technology is complex.

Microsoft and the *amici* characterized the Federal Circuit rule as inflexible and another “bright line” test, a characterization that has resulted in the reversal of several Federal Circuit rulings in recent history, including the *KSR* obviousness case; a case in which the Supreme Court, *in dicta*, noted that the rationale for showing deference to the USPTO was “much diminished” where the prior art in issue was not before the examiner.

## Supreme Court Decision

In its analysis, the Supreme Court considered whether §282 established the standard of proof for invalidity as requiring clear and convincing evidence given the statutory language that a “patent shall be presumed valid” and “[t]he burden of establishing invalidity ... rest[s] on the party asserting such invalidity.” While §282 does not explicitly state an invalidity standard, the Supreme Court explained that the language used when the statute was enacted in 1952 was synonymous with the clear and convincing evidence standard that was part of the recognized common law, as described by Justice Cardozo in *Radio Corp. of America v. Radio Engineering Laboratories, Inc.* Accordingly, the Supreme Court deferred to the opinion of Judge Rich, a primary author of the 1952 Patent Act, in *American Hoist & Derrick*, where he wrote that under §282 the “burden is constant and never changes and is to convince the court of invalidity by clear evidence.”

The Supreme Court said this strict invalidity standard *always* applies, even when evidence before the fact-finder was not previously available to the USPTO during the examination process: “[H]ad Congress intended to drop the heightened standard of proof where the evidence before the jury varied from that before the PTO—and thus to take the unusual and impractical step of enacting a variable standard of proof that must itself be adjudicated in each case—we assume it would have said so expressly.”

However the Supreme Court did suggest the use of tailored jury instructions: “When warranted, the jury may be instructed to consider that it has heard evidence that the PTO had no opportunity to evaluate before granting the

patent” and “may be instructed to evaluate whether the evidence before it is materially new, and if so, to consider that fact when determining whether an invalidity defense has been proved by clear and convincing evidence.”

Notably, the Supreme Court recognized that new evidence not considered by the USPTO during examination—like the S4 software product in issue here—may “carry more weight” at trial (*i.e.*, “the challenger’s burden to persuade the jury of its invalidity defense by clear and convincing evidence may be easier to sustain”) and, citing its earlier *KSR* decision, conceded that where prior art was not before the USPTO, “the rationale underlying the presumption—that the PTO, in its expertise, has approved the claim—seems much diminished.” As the Supreme Court explained, “if the PTO did not have all of the material facts before it, its considerable judgment may lose considerable force. And, concomitantly, the challenger’s burden to persuade the jury of its invalidity defense by clear and convincing evidence may be easier to sustain.”

### ***Patents / Active Inducement***

#### **Actual Knowledge an Element of § 271(B) Inducement, but Willful Blindness Will Suffice**

by Paul Devinsky and Brock Wilson

The Supreme Court of the United States essentially affirmed the Federal Circuit in ruling (8-1) that induced infringement under 35 U.S.C. §271(b) requires knowledge that the induced acts constitute patent infringement, but that one cannot escape liability through “willful blindness” that a copied product is patented. However, the Supreme Court did reject the Federal Circuit’s “deliberate indifference” standard as a substitute for knowledge. *Global-Tech Appliances Inc. v. SEB S.A.*, Case No. 10-6 (Supr. Ct. May 31, 2011) (Justice Alito) (Justice Kennedy, dissenting).

In upholding the Federal Circuit but rejecting the “deliberate indifference” standard, the Supreme Court held that the evidence presented at trial was sufficient to find liability for induced infringement under a theory of “willful blindness,” even though there was no evidence that the defendant had actual knowledge of the asserted patent prior to the filing of the lawsuit. In so holding, the Supreme Court noted that the inducement statute, §271(b), and the contributory infringement statute, §271(c), both stem from the same contributory infringement precedent and that, based on that precedent, both require knowledge that the acts complained of constitute patent infringement, which includes knowledge of the patent. As explained by the Supreme Court, “[t]he two provisions have a common origin in the pre-1952 understanding of contributory infringement, and the language of the two provisions creates the same difficult interpretive choice. It could thus be strange to hold that knowledge of the relevant patent is needed under §271(c) but not under §271(b).”

## Willful Blindness

The Supreme Court then turned to whether the knowledge requirement could be satisfied by something less than actual knowledge and, if so, what the level of that knowledge should be. Looking at criminal case law, the Supreme Court focused on cases in which other courts have held statutes requiring proof that a defendant acted willfully or knowingly to be satisfied—even though the defendant lacked actual knowledge—because the defendant “deliberately shield[ed] themselves from clear evidence of critical facts that are strongly suggested by the circumstances.”

Adopting a similar standard, the Supreme Court concluded that “[g]iven the long history of willful blindness and its wide acceptance in the Federal Judiciary, we can see no reason why the doctrine should not apply in civil lawsuits for induced patent infringement under 35 U.S.C. §271(b).”

Having established willful blindness as the threshold for the knowledge requirement to satisfy induced infringement liability, the Supreme Court set forth two “basic components for willful blindness: (1) the defendant must subjectively believe that there is a high probability that a fact exists and (2) the defendant must take deliberate actions to avoid learning of that fact.”

The Supreme Court then distinguished this willful blindness from the even lower threshold of “deliberate indifference,” *i.e.*, the test applied by the Federal Circuit, concluding that deliberate indifference “permits a finding of knowledge when there is merely a ‘known risk’ that the induced acts are infringing,” and it does “not require active efforts by an inducer to avoid knowing about the infringing nature of the activities.” In comparison to the willful blindness test which stems from criminal law, the deliberate indifference test is more akin to simple negligence.

Applying the willful blindness standard to the facts of the case, the Supreme Court found that the evidence in the present case, taken cumulatively (including evidence that defendant reverse-engineered a foreign, unmarked product of its competitor, copied it and sold it as its own; that defendant commissioned a “right-to-use” study, but did not inform the commissioned lawyer that the product was copied; that defendant’s president was well-versed in U.S. patent law and was a named inventor on 29 patents; and testimony that supported an inference that the defendant did not inform the commissioned attorney the product was copied in order to manufacture a claim of plausible deniability) could support a jury finding “that [defendant] subjectively believed there was a high probability that [plaintiff’s product] was patented, that [defendant] took deliberate steps to avoid knowing that fact, and that it therefore willfully blinded itself to the infringing nature of [its customer’s] sales.”

## Dissent

In dissent, Justice Kennedy wrote that even willful blindness is not enough to satisfy the knowledge requirement of §271(b). “Willful blindness is not knowledge and judges should not broaden a legislative prescription by analogy.”

Justice Kennedy warned that this case could have serious repercussions in terms of criminal cases that involve a knowledge requirement.

## ***Patents / Bayh-Dole***

### **Even Under Bayh-Dole, Employee Inventor Has First Dibs**

by Paul Devinsky

In its second [affirmance of a Federal Circuit decision](#) in the span of two weeks, the Supreme Court of the United States, in a blow to the university technology transfer world, held (7-2) that federal contractors do not have an automatic right to claim title to inventions. The statutory rights of the inventor, even in the case of federally funded research, trumps the Bayh-Dole vesting provision. *Board of Trustees of the Leland Stanford Junior University v. Roche Molecular Systems*, Case No. 09-1159, 563 U.S. \_\_\_\_ (June 6, 2011) (Chief Justice Roberts) (Justice Sotomayor, concurring) (Justice Breyer and Justice Ginsburg, dissenting).

The Bayh-Dole Act dates back to 1980 and is acknowledged to be largely responsible for the vast increase in university licensing of the fruits of federally funded research. In the present case, the issue is raised as to whether the patent rights ownership provision of Bayh-Dole immediately vests ownership in a federally funded invention in the contractor, in this case Stanford University. (See Cert Alert, [IP Update, Vol. 13, No. 11](#)) The Supreme Court has now answered that it does not. While Bayh-Dole clarifies the priority of allocation of rights as between the government and the contractor—all ownership rights stem initially from the inventor.

## **Background**

Stanford sued Roche for infringement of three patents that claim methods for using the polymerase chain reaction (PCR) to measure the amount of HIV in blood samples and using those measurements to infer the effectiveness of antiretroviral drugs.

The standing question arose because Mark Holodniy, one of the named inventors of the patents, signed multiple contracts defining his obligations to assign his invention rights. First, upon joining Stanford, Holodniy signed a Copyright and Patent Agreement (CPA) in which he agreed “to assign or confirm in writing to Stanford and/or Sponsors that right, title and interest in” any inventions he conceived of or first reduced to practice. At the behest of Stanford, however, Holodniy also visited Cetus Corp., a company collaborating with Stanford, to acquire background knowledge about PCR technology. In doing so, Holodniy signed a Visitor’s Confidentiality Agreement (VCA) with Cetus, which stated, “I will assign and *do hereby assign* to CETUS, my right, title, and interest in each of the ideas, inventions and improvements” (emphasis added).

In 1991 Roche purchased Cetus's PCR business, including its agreements with Stanford and its researchers, and began making HIV detection kits. In 1992 Stanford filed the patent application to which the three patents-in-suit claim priority. After extensive negotiations between the two entities, Stanford filed suit against Roche in 2005. In its defense, Roche alleged, *inter alia*, that it possessed ownership rights in the patents-at-issue and that Stanford therefore lacked standing. In response, Stanford argued that it was a *bona fide* purchaser and that the Bayh-Dole Act superseded any transfer of rights from Holodniy to Cetus.

### The Federal Circuit Decision

The Federal Circuit found that Stanford did not possess standing to sue for infringement of the patents-in-suit because the CPA between Stanford and Holodniy was merely a promise to assign, while the VCA was a present transfer of Holodniy's future inventions to Cetus (see *IP Update, Vol. 12, No. 10*). Thus, according to the Federal Circuit, "Cetus immediately gained equitable title to Holodniy's inventions" and any subsequent assignment to Stanford was negated. The Federal Circuit also dismissed Stanford's claim that it was a *bona fide* purchaser. Because "[a]n organization can be charged with notice of its employees' assignments," the Court found that "Stanford had at least constructive or inquiry notice of the VCA." Therefore, Stanford did not qualify as a *bona fide* purchaser. Finally, the Federal Circuit rejected Stanford's argument that "the Bayh-Dole Act negated Holodniy's assignment to Cetus because it empowered Stanford to take complete title to the inventions." Rather, the Federal Circuit concluded that while Bayh-Dole empowers the government to take title to certain inventions under specified circumstances, it neither "automatically void[s] *ab initio* the inventors' rights in government-funded inventions" nor "voids prior contractual transfers of rights." Similarly, "claiming title under Bayh-Dole does not override prior assignments." Stanford sought and was granted *certiorari* by the Supreme Court.

### The Supreme Court

The Supreme Court explained that since its genesis, U.S. patent laws have "operated on the premise that rights in an invention belong to the inventor" and that Bayh-Dole does not "displace" that norm and "automatically" vest title to federally funded inventions in federal contractors.

Specifically, the Supreme Court rebuffed the argument posed by Stanford (and supported by the United States as *amicus curiae*) that Bayh-Dole reorders the normal priority of rights in an invention conceived or first reduced to practice in the course of federally funded research by vesting title in such inventions to the federal contractor, *i.e.*, the inventor's employer. As concluded by the Supreme Court, "nowhere in the Act are inventors deprived of their interest in federally funded inventions. Instead the Act only provides that contractors *may elect* to retain title to any subsection invention" (emphasis added).

According to the provision of Bayh-Dole, granting a right to “elect” confirms that the act does not vest title. Rather, as explained by Chief Justice Roberts (writing for the majority), at the time of conception, rights to an invention lie with the inventor:

Although much in intellectual property law has changed in the 220 years since the first Patent Act, the basic idea that inventors have the right to patent their inventions has not. Our precedents confirm the general rule that rights in an invention belong to the inventor. It is equally well established that an inventor can assign his rights in an invention to a third party. Thus, although others may acquire an interest in an invention, any such interest—as a general rule—must trace back to the inventor.

In accordance with these principles, we have recognized that unless there is an agreement to the contrary, an employer does not have rights in an invention ‘which is the original conception of the employee alone.’ Such an invention ‘remains the property of him who conceived it.’ In most circumstances, an inventor must expressly grant his rights in an invention to his employer if the employer is to obtain those rights.

## **Dissent and Concurrence**

Justice Breyer, joined by Justice Ginsburg, dissented. Quoting the order granting cert, Justice Breyer noted “the question presented is whether rights in inventions arising from federally funded research can be terminated unilaterally by an individual inventor through a separate agreement purporting to assign the inventor’s rights to a third party.”

In the view of the dissent, “the answer to this question is likely no. But because that answer turns on matters that have not been fully briefed (and are not resolved by the opinion of the Court) [Justice Breyer] would return this case to the Federal Circuit for further argument.”

The dissent explained that Congress enacted Bayh-Dole “against a background norm that often, but not always, denies individual inventors patent rights growing out of research for which the public has already paid. This legal norm reflects the fact that patents themselves have both benefits and costs.” Citing back to the letters of founding fathers Jefferson and Madison to the effect that patent monopoly was a “compensation” for the “community benefit” that a patent bestowed, Justice Breyer explained “the importance of assuring this community ‘benefit’ is reflected in legal rules that may deny or limit the award of patent rights where the public has already paid to produce an invention, lest the public bear the potential costs of patent protection where there is no offsetting need for such protection to elicit that invention. Why should the public have to pay twice for the same invention?”

Justice Sotomayor agreed with the majority but only because Stanford didn't raise the issues raised in the dissent. She noted her understanding that "the majority opinion [would] permit consideration of these arguments in a future case."

### ***Patents / Inequitable Conduct***

#### **Federal Circuit Ratchets Up Materiality Requirement for Inequitable Conduct**

by Mary Boyle, Ph.D. and Paul Devinsky

In a decision likely to please practitioners involved in patent prosecution as well as patent owners, a divided U.S. Court of Appeals for the Federal Circuit issued its *en banc* ruling addressing the legal standard for inequitable conduct. Citing the rampant overuse and unintended consequences of the doctrine, the court imposed a new, heightened standard for materiality. *Therasense, Inc. v. Becton Dickinson & Co.*, Case No. 08-1511 (Fed. Cir., May 25, 2011) (*en banc*) (opinion for the court by Rader, C.J., joined by Judges Newman, Lourie, Linn, Moore and Reyna) (O'Malley, J., concurring-in-part and dissenting-in-part) (Dyson, J., dissenting, joined by Judges Gajarsa, Dyk and Prost).

A deeply divided (6-1-4) Federal Circuit revised the materiality prong of the inequitable conduct defense, which permits a patent infringer to argue that an entire patent (as well as related patents and patent applications) should be declared unenforceable in light of the patentee's wrongful conduct during patent prosecution. Six judges joined in the entirety of the court's opinion. A seventh judge joined part of the court's opinion discussing intent and wrote a separate opinion concurring-in-part and dissenting-in-part as to the materiality standard. The remaining four judges dissented in a lengthy opinion.

In the trial court, the district judge found inequitable conduct based on failure to disclose to the U.S. Patent and Trademark Office (USPTO) that contradictory statements had been made in a different proceeding. The patent-in-suit is for test strips with an electrode and reactant system used to measure blood sugar in diabetic patients. Measurements of blood sugar can be made either from whole blood samples or from other types of samples. The issue involved whether a person of ordinary skill in the art would understand that an electrode system for use with whole blood must have a membrane to protect the electrode. According to an earlier patent, strips to test whole blood samples "optionally, but preferably" had a membrane. In European patent proceedings, the patent owner argued that the language "optionally, but preferably" meant a membrane was not required, *i.e.*, it was optional. In the USPTO, the patent owner submitted a sworn declaration and supporting argument stating that the language "optionally, but preferably" in the prior art patent would be read by a person of ordinary skill to mean that a membrane was required, *i.e.*, it was not optional. The declaration submitted to the USPTO was in direct response to concerns expressed by the examiner. The patent owner never disclosed the statements that were made in the European

proceeding to the USPTO. The trial court found specific intent to deceive the USPTO and that the contradictory statements were material, and ruled that the patent-in-suit was unenforceable.

## New “But for” Standard for Materiality

The Federal Circuit reiterated that the law of inequitable conduct relating to nondisclosure continues to require two separate showings: specific intent to deceive and materiality. The burden of proof that the accused infringer must meet is still clear and convincing evidence.

As articulated by the majority, the intent requirement remains unchanged. Specifically, the proper standard for intentional nondisclosure is “knowing and deliberate,” although the majority concedes that some cases had incorrectly suggested that a negligence-type, “should have known” intent standard was sufficient. In the words of the Court, the intent requirement requires “clear and convincing evidence that the applicant knew of the reference, knew that it was material, and made a deliberate decision to withhold it.” When circumstantial evidence of intent is used, intent to deceive must be the most reasonable inference.

It is the materiality standard that has never been radically changed. Prior to *Therasense*, the Federal Circuit had developed a materiality standard that was based on the USPTO’s Rule 56, which sets forth disclosure standards for lawyers and others involved in patent prosecution. The *Therasense* opinion jettisons that approach. The Court rejected the current version of Rule 56, which provides that information is “material” if it is noncumulative and “refutes, or is inconsistent with, a position the applicant takes in opposing an argument of unpatentability relied on by the [USPTO], or asserting an argument of patentability” as setting “such a low bar for materiality” that it encourages the existing and problematic practice of dumping prior art of marginal relevance on the USPTO during patent prosecution.

After *Therasense*, the legal standard for materiality is not tied to the Rule 56. Instead, if an applicant has failed to disclose prior art to the USPTO, the trial court will be required to determine whether the undisclosed art meets a “but for” materiality test, which means that the USPTO would not have allowed a patent claim if it had been aware of the undisclosed prior art. To make that determination, the trial court is instructed to apply a preponderance of the evidence standard and give claims their broadest reasonable construction, *i.e.*, apply the evidentiary standards that the USPTO would have used to decide whether the prior art rendered the claim unpatentable. This is an appropriate standard, the Court explained, because it looks to whether the patentee actually reaped an unfair benefit by its wrongful failure to disclose.

## Exceptions for Egregious Conduct

The Court's opinion sets up an exception to the new "but for" standard in cases of "affirmative egregious conduct." The Court recognized that the "but for" test would not, by itself, be adequate to capture all cases of egregious and abusive conduct. This exception, the Court stated, incorporates elements of early "unclean hands" cases from the Supreme Court of the United States, which dealt with egregious misconduct. Using this exception, the majority believes it will achieve the necessary balance between encouraging honesty and curtailing the excessive use of the inequitable conduct defense, often referred to as a "plague." While the Court used the specific example of a false affidavit to illustrate the exception, the Court indicated the exception was not so limited, but rather is intended to ensure the materiality standard had sufficient flexibility to capture and punish abusive conduct.

## The Majority's Rationale

The Federal Circuit's *Therasense* opinion plainly states that this change in the law was made out of necessity to address "the problems created by the expansion and overuse of the inequitable conduct doctrine." Over time, the intent and materiality standards for proving inequitable conduct were lowered to encourage full disclosure to the USPTO. "This new focus on encouraging disclosure has had numerous unforeseen and unintended consequences." The inequitable conduct defense came to be raised in virtually every case, cabined only by the limits of attorney imagination to find "the slenderest grounds" to support a charge of inequitable conduct. The availability and overuse of this defense led to expanded discovery and increased litigation costs, discouraged settlement and diverted attention and resources from the merits of infringement and invalidity issues. "Perhaps most importantly, the remedy for inequitable conduct is the 'atomic bomb' of patent law," rendering whole patents, and in some cases, entire families of patents, unenforceable. "Left unfettered, the inequitable conduct doctrine has plagued not only the courts but also the entire patent system."

## The Dissent

There is deep disagreement within the Court over the rule announced by the majority. The main group of four dissenters disagreed with the replacement of the Rule 56 standard. Those judges thought that long-standing precedent should not be overturned, and they would have made more limited changes to the legal standards, including a tightening of the intent element. They argued that, in other areas of law, a "but for" standard of materiality has been largely rejected, and that it had been repeatedly rejected by the Federal Circuit itself in cases involving inequitable conduct. Moreover, in their view, it is critical that the courts should continue to look to Rule 56, which encompasses the USPTO's considered view of what standard of conduct is needed and should govern the examination of patents. The dissenting group also expressed a belief that the higher standard for materiality will undermine the existing incentives to refrain from dishonesty before the USPTO. Indeed, they asserted, the "but for"

test comes close to abolishing the doctrine of inequitable conduct altogether, since a finding of inequitable conduct will generally be made only after claims have been found invalid.

The other dissenter, Judge O'Malley, agreed that the old Rule 56 standard was inadequate, calling it, "too vague and too broad." On the other hand, Judge O'Malley objected that the new test was too narrow and too rigid. She supported a test that included the "but for" standard, but also deemed conduct to be material if it constitutes a false or misleading representation of fact, or was "so offensive that the court is left with a firm conviction that the integrity of the PTO process as to the application at issue was wholly undermined." Judge O'Malley also suggested that the remedy for inequitable conduct should not be limited to ruling that a whole patent is unenforceable. Rather, in Judge O'Malley's view the courts, in the exercise of their equitable powers, should have discretion to fashion an appropriate remedy.

### ***Patents / Discovery***

#### **Rambus Encore: Duty to Preserve Documents for Litigation Clarified**

by Paul Devinsky

Reconciling the opposite conclusions recited by two district courts on essentially identical facts, the U.S. Court of Appeals for the Federal Circuit has clarified when a litigant is under a duty to preserve documents at risk of committing spoliation. *Micron Technology v. Rambus, Inc.*, Case No. 09-1263 (Fed. Cir., May 13, 2011) (Linn, J.) (Gajarsa, J., concurring-in-part, dissenting-in-part); *Hynix Semiconductor, Inc. v. Rambus, Inc.*, Case No. 09-1299; -1347 (Fed. Cir., May 13, 2011) (Linn, J.) (Gajarsa, J., concurring-in-part, dissenting-in-part, joined by Newman, J.). In these cases, the Federal Circuit concluded that Rambus improperly destroyed millions of pages of documents in advance of litigation, handing the technology licensing giant a major setback in its patent enforcement program.

Rambus licenses patents that relate to enhanced performance memory chips. Most of Rambus cash flow is from patent licensing revenue. Rambus initiated its first enforcement action in 2000, slightly before Micron and Hynix initiated declaratory judgment actions against it, seeking declarations of invalidity, non-infringement and unenforceability. In advance of its enforcement actions against Micron or Hynix, Rambus, in 1999, conducted what has been termed "shred days" or a "shred party," during which millions of pages of documents were destroyed. In the *Micron* case, the district court (Delaware) concluded that Rambus had engaged in spoliation of documents that related to its patent licensing program and ordered dismissal of the action against Micron as a sanction. The district court did so after concluding that litigation was reasonably foreseeable (to Rambus) by the end of 1998.

In the *Hynix* case, the district court (ND Ca) concluded that litigation was not foreseeable (to Rambus) at the time of the shredding and so found that there was no spoliation. In the opinion of *Hynix* court, litigation must be “immediate” or “certain” to be foreseeable.

In the present appeal the Federal Circuit was called upon to resolve the issue of when litigation was foreseeable and so a duty to preserve documents arose. Rambus urged the Court to adopt a standard whereby a party would be obligated to preserve documents only when litigation became “probable.”

In the *Micron* case, the Federal Circuit affirmed the district court ruling that spoliation had occurred but reversed the district court on the sanction of dismissal and remanded the case for reconsideration of that sanction. The Federal Circuit left it to the district court to determine, based on the totality of the circumstances, the date the duty to preserve arose, but the Federal Circuit did conclude that the duty to preserve did arise prior to the August 1999 shred day and that spoliation had occurred. In terms of the circumstances to be considered (under the totality of circumstances test), the Federal Circuit cited facts such as Rambus’ knowledge of the potentially infringing activity (of Micron), as well as the steps it had taken in furtherance of litigation such as selecting forums, prioritizing targets and creating claim charts. The Court noted that for Rambus, litigation was “an essential element of its business model.”

As part of the remand, the Federal Circuit instructed the Delaware district court to make a determination on the issue of bad faith and to re-assess its finding of prejudice, *i.e.*, in terms of whether, independent of the propriety of Rambus’ document destruction, the shredding had an impact on the ability of potential defendants to defend themselves. In reversing the dismissal sanction, the Federal Circuit instructed the district court to reassess the sanction based on the degree of bad faith and prejudice it found and whether there was another, lesser sanction that would be sufficient.

In the *Hynix* appeal, the Federal Circuit reversed the district court, concluding that the standard of foreseeability used in that case (“imminent or probable, without significant contingencies”) was too narrow and that even if there are contingencies, so long as their resolution is “reasonably foreseeable,” the litigation is also reasonably foreseeable.

The district court was instructed, on remand, to determine (under the same totality of the circumstances test) when Rambus’ duty to preserve arose and whether *Hynix* was entitled to relief.

#### **Attorney-Client Privilege and Crime-Fraud Exception**

The Federal Circuit agreed with both district courts that even though the evidence used to advance the spoliation argument was subject to an attorney-client privilege, that privilege was “pierced” by the crime-fraud exception since the communications in issue were in furtherance of a violation of a destruction of evidence statute (notwithstanding Rambus’ argument that the California statute in question only applied where there was “immediacy of temporal closeness” between the time the destruction occurred and the time set for document production). The Court rebuffed

Rambus' argument, noting that it would make "no sense" given Rambus' control of the timing of events, to permit a party to intentionally destroy evidence and then just wait some "arbitrary period of time" before filing suit to avoid the consequences of the crime-fraud exception.

***Patents / Non-obviousness and Analogous Art***

**Analogous Art Must Address the Entire Problem Solved by the Patent**

by Hasan Rashid and Blake Wong

The U.S. Court of Appeals for the Federal Circuit has interpreted the analogous art doctrine narrowly in an obviousness analysis, concluding that all the art relied on by the U.S. Patent and Trademark Office (USPTO) was non-analogous art with respect to the claimed invention. *In re Klein*, Case No. 10-1411 (Fed. Cir., June 6, 2011) (Schall, J.).

The invention in issue is a device for mixing sugar and water in configurable ratios to create nectar for different birds and butterflies. The device includes a pitcher for holding liquids and a movable divider separating the pitcher into a sugar and a water section. The movable divider varies the sizes of the two sections, adjusting the ratio of sugar and water based on whether the user is feeding the nectar to hummingbirds, orioles or butterflies. Once the bird is chosen and the movable divider is set, the user then fills the sections with sugar and water and lifts the divider to mix the ingredients into nectar.

Using five prior art references, the USPTO upheld an obviousness rejection. Three of the references were directed to movable dividers for separating solid objects, as in a drawer or cabinet. The other two references were directed to immovable partitions for separating liquids to be mixed.

The inventor argued that the five references were not analogous art and that the references could not be applied to render the claimed invention obvious. The Board of Patent Appeals and Interferences disagreed, finding that the five references were reasonably pertinent to the problem of "making a nectar feeder with a moveable divider to prepare different ratios of sugar and water for different animals." Klein appealed.

The Federal Circuit reversed, concluding that the five references were not analogous with regard to the claimed invention because they did not address the entire problem addressed by the invention. Although the first three references described movable dividers, the dividers separated solid objects and not liquids. Similarly, although the last two references described dividers that separated liquids, the dividers were immovable. Thus, the Court concluded that the cited references were not related to solving the entire problem of "making a nectar feeder with a moveable divider to prepare different ratios of sugar and water for different animals."

**Practice Note:** The Federal Circuit decision did not cite to the Supreme Court's 2007 *KSR* decision, which focused on the question of obviousness and which speaks to the issue of analogous art. Nevertheless, *In re Klein* will likely be often cited to the USPTO in support of the argument that analogous art must be directed towards the entire problem addressed by the patent, not just pieces of the problem.

### ***Patents / Claim Construction***

#### **For Infringement Purposes, Preamble Can Define a Limiting Environment Rather than a Claim Limitation**

by Ryan N. Phelan

The U. S. Court of Appeals for the Federal Circuit has explained that terms of a patent claim preamble can define a limiting "environment." Such terms of the limiting environment may be performed or met by third parties, setting the stage for infringement by parties accused of practicing the limitations of the claim body. *Advanced Software Design Corp. v. Fiserv, Inc.*, Case Nos. 09-1585, 10-1011 (Fed. Cir., June 2, 2011) (Bryson, J.).

Advanced Software Design and Fiserv offer competing products that generally work by encrypting selected information on a check, e.g., the name of the payee or the amount to be paid, and printing the encrypted information on the check. The information is later used to validate whether the check is legitimate rather than fraudulent or forged. A key feature of Fiserv's products was that its products performed only the validation feature and not the related encrypting or printing features.

Advanced Software Design sued Fiserv for patent infringement of its patents directed to guarding against check fraud and forgery. Following discovery and claim construction, one asserted patent remained. Fiserv filed a summary judgment motion for non-infringement based, in part, on its position that it did not practice all of the steps of the asserted claims requiring each of "encrypting," "printing" and "validating" of checks. The district court granted Fiserv's motion, in part, based on its finding that Fiserv did not direct or control "encrypting" or "printing" steps and, therefore, could Fiserv could not directly infringe the patent.

However, the "validating" step was the only step of the three steps at issue discussed in the body of the asserted claims. The "encrypting" and "printing" steps were found in the preamble. Nonetheless, the district court construed the "encrypting and "printing" steps as limiting, adopting Fiserv's position that each of these steps must be performed by the accused infringer. Advanced Software Design appealed.

The Federal Circuit reversed, concluding that while the preamble's encrypting and printing steps were limiting, the limitation only defines the "environment in which the accused infringer must practice the [invention]." The Court found its earlier decision in *Uniloc USA* instructive: "[l]ike the claim in *Uniloc*, the claims at issue in this case contain

preambles that define the environment in which an accused infringer must act or describe capabilities that an accused device must have.”

There remained an issue of material fact as to whether Fiserv, or its products, practiced the “validating” step found in the body of the asserted claim. On this issue, the Court stated that “[f]or infringement purposes, *the preamble steps need not be performed by the system or the party that uses the system.*” Focusing on an exemplary claimed, the Court noted that the claim covers a “process for validating a negotiable financial instrument’ comprising reading information from the check and decrypting or re-encrypting to validate the check. Fiserv therefore could ‘use’ the [claimed] method ... by validating checks *even though it does not encrypt and print them.* It would infringe the [claimed] method ..., however, only by validating checks that have been encrypted and printed in accordance with steps described in the preamble.”

### ***Patent / Declaratory Judgment Standing***

#### **Vendor’s Economic Injury Is Insufficient to Establish DJ Jurisdiction, but Implicit Claim of Contributory Infringement Is Enough**

by Christina A. Ondrick

The U.S. Court of Appeals for the Federal Circuit has now ruled that a supplier vendor has standing to commence a declaratory judgment action if a patent holder accuses the supplier’s customers of direct infringement and if the supplier’s product functions as a material component in the allegedly infringing system or the supplier’s product is used in the performance of the allegedly infringing method. *Arris Group v. British Telecommunications PLC*, Case No. 10-1292 (Fed. Cir., May 19, 2011) (Dyk, J.).

Arris makes and sells cable telephony and data products for use in networks with Voice over Internet Protocol (VoIP) telephone services. British Telecommunications (BT) sent Arris’ customer, Cable One, a letter accusing Cable One’s network of infringing various system and method claims of the patents-in-suit. Licensing discussions ensued. BT sent Cable One a 118-page presentation comparing the patent claims to Cable One’s network, which included repeated identification of Arris’ products as meeting certain system claim elements and steps of the method claims. BT’s presentation identified Cable One (not Arris) as a direct infringer. Thereafter, at Cable One’s request, Arris became involved in the licensing discussions. BT offered Cable One a license but declined to license Arris. Arris filed a declaratory judgment action against BT; the district court dismissed the action, finding that Arris lacked standing because there was no case or controversy between Arris and BT. Arris appealed.

The Federal Circuit rejected Arris’ argument that case or controversy exists because Arris has suffered an economic injury as a result of BT’s infringement threats. The Court held that a mere adverse *economic* interest was insufficient

to create declaratory judgment jurisdiction and that the Supreme Court's *MedImmune* decision did not alter the prior law in this regard. What is required to establish jurisdiction is an adverse *legal* interest of sufficient immediacy and reality. However, the Federal Circuit found an adverse legal interest because BT implicitly asserted that Arris contributorily infringed the BT patents when it accused Cable One of direct infringement. Arris' products were "central" to the BT's direct infringement allegations against Cable One and, for many of the asserted claims, BT identified Arris' products as meeting virtually all of the claim elements. The Court further found that, at a minimum, BT identified Arris' products as satisfying at least one central element of every asserted claim. BT allegations that Arris' products complied with industry standards also suggested that Arris' products were especially made or adapted for uses that infringe and are not staple articles of commerce. Other relevant factors to the Court's conclusion included Arris' involvement in the prior licensing negotiations, as well as BT's refusal to grant Arris a covenant not to sue.

**Practice Note:** The "central" nature of Arris' products in the infringement allegations entitled the Court to finding that standing existed. However, the nature and quantity of contacts between the Arris and BT also strongly supported the Court's conclusion. Patent holders seeking to avoid declaratory judgment battles with indirect infringers should take care to minimize the nature of the allegations made about indirect infringers and should not rely on non-binding disclaimers that suppliers are not being accused of infringement.

### ***Patents / Patent Exhaustion***

#### **Patent Exhaustion Still Applies when Licensees Fail to Pay Royalties**

by Hasan Rashid and Blake Wong

The U.S. Court of Appeals for the Federal Circuit has concluded that patent rights are exhausted even when the licensor has not received royalties under a patent license. *Tessera, Inc. v. Int'l Trade Comm'n*, Case No. 10-1176 (Fed. Cir., May 23, 2011) (Linn, J.).

Tessera licensed the patent in suit and required royalties from its licensees. However, some of Tessera's licensees sold products under the license without paying royalties on the sales. Tessera initiated an ITC action against Elpida, a downstream customer of these non-paying licensees.

Elpida asserted a patent exhaustion defense in the ITC. Elpida argued that Tessera may not recover damages because Tessera exhausted the patent rights when Tessera licensed the patent to the licensees. In response, Tessera argued that because some licensees failed to pay royalties, Tessera's patent rights had not been exhausted—although patent exhaustion prevents "double recovery," Tessera had not even received a "single recovery." After the ITC agreed with Elpida, Tessera appealed.

The Federal Circuit affirmed, focusing on a single question: did Tessera authorize the sales? In *Quanta*, the Supreme Court explained that the “patent exhaustion [doctrine] provides that the initial authorized sale of a patented item terminates all patent rights to that item.” Thus, if the sales were authorized, then Tessera’s rights were exhausted; if the sales were unauthorized, then Tessera’s rights were not exhausted. The Court read the licenses to have authorized the licensees’ sales. Specifically, Tessera had authorized its licensees to sell first, then pay royalties later. As the Court explained, nothing in the licenses converted the initially authorized sales into unauthorized sales upon nonpayment of royalties.

To hold otherwise would create an “absurd result” contrary to the purpose of the patent exhaustion doctrine. Namely, the doctrine “prohibit[s] postsale restrictions on the use of a patented article.” The Court noted that Tessera should have pursued an action against its licensees, not those licensees’ customers. For example, Tessera should have sued its licensees to recover for breach of contract for failing to pay royalties.

### ***Patents / Obviousness***

#### **Endo Finds Pain Relief from Board’s “Erroneous Reasoning”**

by Heather Morehouse Ettinger, Ph.D.

Reviewing a decision of the Board of Patent Appeals and Interferences (BPAI) finding of three patent applications directed to the pain relief formulation known as Opana® to be obvious, the U.S. Court of Appeals for the Federal Circuit affirmed the BPAI’s decision in two of the applications, but vacated and remanded the BPAI decision in the third application. *In re Kao*, Case Nos. 10-1307 and -1308, and *In re Ahdieh*, Case No. 10-1309 (Fed. Cir. May 13, 2011) (Linn J.).

The three patent applications at issue concern controlled-release formulations of oxymorphone and are being pursued by Endo Pharmaceuticals in connection with its prescription pain tablets Opana® ER. The Court found that with respect two of three applications at issue, the BPAI’s obviousness findings were supported by substantial evidence and that Endo’s evidence of secondary consideration, namely the commercial success of Opana® ER, and showing of unexpected results were insufficient to rebut the *prima facie* showing of obviousness. However, with respect to the application for the formulation of Opana®, the Court found that the BPAI did not base the factual conclusions it used to find the claims obvious on substantial evidence, and therefore vacated and remanded that application.

The Court also found that the BPAI had erred by failing to give due weight to evidence of secondary considerations of non-obviousness of the claimed formulation. The Court reminded the BPAI that evidence of a secondary consideration, such as commercial success, does not need to be across the entire claimed range in order to be

reasonably commensurate with the scope of the claims. However, the Court also noted that Endo, on remand, will need to show that the proffered secondary consideration, *i.e.* commercial success, results from something that is both claimed and *novel* in the claim. With respect to unexpected results, the Court advised the BPAI to consider on remand whether there is a nexus between the unexpected results and aspects of the claimed invention not already in the prior art.

**Practice Note:** The Federal Circuit considered the patentability of only one of two claims of the remanded application that it could have considered. The Federal Circuit reasoned that Endo had waived its right to have the two claims considered separately, both at the BPAI and at the Court, because Endo had failed to make separate, substantive arguments on the patentability each. To prevent such a waiver, applicants are advised (when possible) to provide clear statements separately asserting the patentability of the appealed claims.

#### ***Patents / Obviousness***

### ***In re Brimonidine Patent Litigation: Obviousness Determinations Revisited***

by Shilpa V. Patel, Ph.D.

The U.S. Court of Appeals for the Federal Circuit reversed-in-part and affirmed-in-part a district court finding of non-obviousness in a Hatch-Waxman litigation involving an improved brimonidine formulation for reducing intraocular pressure associated with glaucoma. *Allergan Inc. v. Exela PharmSci Inc. and Apotex Inc.*, Case Nos. 10-1102, -1103 (Fed. Cir., May 19, 2011) (Bryson, J.) (Dyk, J., concurring-in-part, dissenting-in-part).

In 2001, Allergan introduced Alphagan<sup>®</sup> P brimonidine solution intended to address an allergic response in some patients to Allergan's Alphagan<sup>®</sup> brimonidine solution. Alphagan<sup>®</sup> P solution contains a lower concentration of brimonidine, higher pH and a solubility-enhancing component. Despite concern of possible oxidation of brimonidine, the Alphagan<sup>®</sup> P solution also contained stabilized chlorine dioxide (SCD) instead of benzalkonium chloride, a known eye irritant. After Exela and Apotex each submitted an Abbreviated New Drug Application (ANDA) for to the U.S. Food and Drug Administration (FDA) for marketing approval of a generic version of Alphagan<sup>®</sup> P brimonidine solution, Allergan alleged infringement of its patent directed to a buffered, aqueous ophthalmic solution and four related patents each directed to brimonidine-containing products. Following a bench trial, the district court found all of the asserted patents to be non-obvious. Apotex then stipulated to infringement and the district court entered an injunction. The defendants appealed.

On appeal, Apotex challenged the district court findings of non-obviousness. Apotex's invalidity argument relied on to prior art patents, Stockel and Ratcliff. Apotex argued that Stockel explicitly discloses the modifications that Allergan argues impart patentability (*i.e.*, use of SCD as a preservative in an ophthalmic solution and that the

desirability of an isotonic solution). Allergan argued that Stockel teaches away from the use of SCD as the only preservative because it would irritate the eye and recommends a combination of preservative agents. The Federal Circuit concluded that Stockel's teaching regarding the quantity of SCD does not undercut the strength of the teaching that physiologic pH and osmolality by use of buffer and tonicity components would have been simple and well-known modifications.

Apotex also argued that Ratcliff discloses an SCD solution and that the modifications that led to the claimed invention would have been obvious to a person of ordinary skill in the art. Allergan argued that Ratcliff requires activation of the disclosed SCD. The Federal Circuit disagreed with Allergan, noting that the claims in issue are directed to an SCD solution irrespective of its activation. The Court also stated that it would have been obvious to a person of ordinary skill in the art to create an ophthalmic solution that was adjusted to ocular pH and tonicity and that relied upon SCD as to sole preservative.

As to the four other related patents, Apotex argued that every asserted claim reads on a combination Refresh Tears<sup>®</sup> product and Alphagan<sup>®</sup> brimonidine solution, both owned by Allergan, and that such a combination would have been obvious to a person of ordinary skill in the art and faulted the district court for considering each asserted reference in isolation. The Federal Circuit, giving deference to the district court's weighing of testimony, concluded that the district court did not err in its factual determinations because the combination of Allergan's products would not have been an "anticipated success" and that a person of ordinary skill in the art would not have been expected to disregard the solvability and oxidation roadblocks caused by the prior art.

The Federal Circuit also reversed the district court's holding that Exela's product would infringe an Allergan patent. The Court distinguished the facts here from its holding as to when it is appropriate for a court to consider material outside the four corners of the ANDA to determine if an ANDA describes an infringing product. Here, neither Allergan nor Exela dispute that if Exela complies with its ANDA, Exela will never manufacture or sell a product at a pH falling within the asserted claims. Thus, the Court stated that it cannot assume that Exela will not act in full in compliance with its representations to the FDA.

Judge Dyk, in dissent, cited *KSR* and concluded that for the four related patents the "obvious to try" standard was met because a person of ordinary skill in the art would have been motivated to try a combination of Allergan's products to arrive at the claimed formulation. Judge Dyk engaged in a deep factual review of the record and concluded that the district court made erroneous fact findings that led it to determine that solubility and oxidation concerns would have deterred a person of ordinary skill from trying the combination of Allergan's products.

**Patents / Injunction Bond**

**Wrongful Injunction Raises Presumption of Recovery of Bond**

by Whitney D. Brown and Christopher L. May

In a case of first impression, the U.S. Court of Appeals for the Second Circuit ruled that wrongfully enjoined parties are entitled to a presumption in favor of recovery against an injunction bond for provable damages. However, the Court concluded that while InterDigital contention that it deserves damages associated with a stay of patent infringement action against Nokia has merit, the case record was insufficient for appellate review. *Nokia Corp. v. InterDigital Inc. et al.*, Case No. 10-1358 (2d Cir., May 23, 2011) (Parker, J.).

The parties' dispute first arose at the International Trade Commission, where InterDigital alleged that Nokia had infringed its patents. In 2007, the ITC granted Nokia's motion to consolidate the investigation with a separate investigation filed by InterDigital against Samsung over the same patents. In December 2007, Nokia moved to stay the consolidated investigation, arguing that a pre-existing agreement between Nokia and InterDigital required arbitration. The ITC denied the motion, and Nokia then sued in federal district court. The district court granted Nokia's motion for a preliminary injunction in March 2008 and ordered InterDigital to stay or terminate the ITC proceedings against Nokia and submit to arbitration. The court required Nokia to post a \$500,000 bond as a condition of obtaining the injunction.

The 2d Circuit subsequently vacated the injunction (see [IP Update, Vol. 11, No. 8](#)), and the district court dismissed Nokia's suit. Thereafter, InterDigital filed a motion in the district court to recover attorneys' fees and expenses incurred in moving to stay the ITC proceedings and preparing to arbitrate with Nokia. It asked to be awarded attorneys' fees and costs incurred as a result of litigating separate proceedings against Nokia and Samsung. The district court rejected InterDigital's request, finding that InterDigital had failed to show that the damages sought were "proximately caused" by the injunction. InterDigital appealed.

The 2d Circuit held that a wrongfully enjoined party is entitled to a presumption in favor of recovery, finding that the existence of such a presumption was implied by the text of Fed. R. Civ. Pro. 65(c), and that the First, Seventh, Ninth, Eleventh and D.C. Circuits followed similar rules. However, the court ruled that the improperly enjoined party must still show that any damages claimed were proximately caused by the injunction. Based on the lack of explanation by the district court for the denial of recovery, the 2d Circuit vacated the lower court's order and remanded the issue for reconsideration and clarification. However, the 2d Circuit noted that certain legal expenses, such as filing a motion to stay the ITC case with respect to Nokia that were ordered by the district court in its injunction order, should be recoverable absent a compelling reason otherwise.

**Patents / Damages**

**No *En Banc* Rehearing for the 25 Percent Rule**

by Leigh J. Martinson

By a vote of 10-1, the U. S. Court of Appeals for the Federal Circuit denied Uniloc's requests for a panel rehearing and for a rehearing *en banc*, respectively. *Uniloc USA, Inc. and Uniloc Singapore Private Limited v. Microsoft Corporation*, Case Nos. 10-1035, -1055 (Fed. Cir., May 16, 2011) (*per curiam*) (O'Malley, J., dissenting).

In January of 2011, the Court determined that evidence relying on the 25 percent rule of thumb is inadmissible under *Daubert* and the Federal Rules of Evidence because it fails to tie a reasonable royalty base to the facts of the case at issue (see [IP Update, Vol. 14, No. 1](#)). Thus, the Court held that as a matter of Federal Circuit law that the 25 percent rule of thumb is a fundamentally flawed tool for determining a baseline royalty rate in a hypothetical negotiation and should not be used.

Uniloc filed a combined petition for panel rehearing and rehearing *en banc*. The Court also granted leave to file *amici curiae* briefs to 10 damages experts, all of whom appeared *pro se*.

Now by a vote of 10-1, the Court denied both requests by Uniloc. Judge O'Malley dissented from the denial of the petition for rehearing *en banc*, but filed no separate opinion.

**Cert Alert**

**Prometheus Rises Again**

by Paul Devinsky

After having *certiorari* vacated and being remanded back to the Federal Circuit in the wake of decision of the Supreme Court of the United States in *Bilski v. Kappos*, (see "[Bilski v. Kappos—Back Where We Started?](#)" and to [IP Update Vol. 12, No. 7](#)) the Supreme Court has again granted *certiorari* in *Mayo Collaborative Services v. Prometheus Labs., Inc.*, Supreme Court Case No. 10-1150 (June 20, 2011) to consider the patent eligibility of a claim directed to a medical diagnostic test.

On remand, the Federal Circuit (consistent with its initial decision in this case (see [IP Update, Vol. 12, No. 9](#)) concluded the subject matter claimed was "transformative" and therefore passed muster under 35 U.S.C. § 101. (See [IP Update, Vol. 14, No. 1](#)).

The question on which cert was granted is as follows:

*Whether 35 U.S.C. § 101 is satisfied by a patent claim that covers observed correlations between blood test results and patient health, so that the claim effectively preempts all uses of the naturally occurring correlations, simply because well-known methods used to administer prescription drugs and test blood may involve “transformations” of body chemistry.*

A similar issue was considered by the Supreme Court several years ago when it granted cert in *Laboratory Corp of America v. Metabolite Laboratories*, but after full briefing and oral argument, cert was dismissed as having been improvidently granted and no decision was rendered. (See [“U.S. Supreme Court Dismisses LabCorp’s Petition at the Eleventh Hour”](#).)

### ***Trademarks / Injunctive Relief***

#### **eBay Standard Applies to Preliminary Injunctions in Trademark Cases**

by Matthew McCloskey

Considering whether requests for preliminary injunctions against alleged trademark infringement are subject to the traditional equitable principles set forth by the Supreme Court of the United States in *eBay v. MercExchange*, the U.S. Court of Appeals for the First Circuit vacated the district court’s grant of preliminary injunction to a trademark owner. *Voice of the Arab World, Inc. v. MDTV Medical News Now, Inc.*, Case No. 10-1396 (1st Cir., May 27, 2011) (Torruella, J.).

Voice of the Arab World filed an action against MDTV Medical News Now in the District Court of Massachusetts, seeking a declaratory judgment that the plaintiff’s use and registration of the mark “MDTV” did not infringe on the defendant’s trademark rights. After filing counter claims, including one alleging trademark infringement, the defendant moved to preliminarily enjoin the plaintiff from using the MDTV mark. After the district court granted the preliminary injunction, the plaintiff appealed to the 1st Circuit.

The plaintiff challenged the district court’s preliminary injunction order on three grounds. First, the plaintiff argued that the district court erred in finding that the defendant demonstrated a likelihood of success on the merits of its trademark infringement claim. Second, the plaintiff alleged that the lower court erred as a matter of law by presuming that the defendant would likely suffer irreparable harm in the absence of preliminary injunctive relief and in not requiring the defendant to actually demonstrate such likelihood of irreparable harm. Third, the plaintiff argued that even if a preliminary injunction was appropriate, the district court abused its discretion by issuing an overly broad injunction.

The plaintiff's argument concerning irreparable harm was two-fold. First, the plaintiff argued that presuming irreparable harm in trademark infringement cases where preliminary injunctive relief is sought is inconsistent with the Supreme Court's 2006 decision in *eBay Inc. v. MercExchange, L.L.C.* In the alternative, the plaintiff contended that even if irreparable harm is properly presumed in certain trademark infringement cases, such a presumption could not apply in this case due to the defendant's excessive delay in seeking injunctive relief.

Citing *eBay*, which dealt with a request for permanent injunction in a patent infringement case, the court held that a request to preliminarily enjoin alleged trademark infringement is subject to the traditional equitable principles delineated in *eBay*. Specifically, the court reiterated the *eBay* holding 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." In recognizing that *eBay* properly applies to non-patent cases, the court noted that "it is significant that the Court in *eBay* supported its formulation of the traditional four-factor permanent injunction standard by citing cases that were unrelated to patent law." The court also recognized that "nothing in the Lanham Act indicates that Congress intended to depart from traditional equitable principles," noting, "like the Patent Act, the Lanham Act provides a court the 'power to grant injunctions, according to principles of equity and upon such terms as the court may deem reasonable, to prevent[.]' among other things, trademark infringement and domain name cybersquatting" citing 15 U.S.C. § 1116(a) (emphasis supplied). The court stated that the fact that *eBay* dealt with a permanent injunction did not change the conclusion that its principles are equally applicable in the context of preliminary injunctions.

### ***Copyright Infringement / Jurisdiction***

#### **Second Circuit Revives Copyright Infringement Suit Against Non-Resident for Uploading Copyrighted Material Online**

by Rita Weeks

Employing the standard set out by the New York Court of Appeals in internet copyright infringement cases, the U. S. Court of Appeals for the Second Circuit has revived a copyright infringement suit brought by a New York resident against a non-resident based upon defendant's alleged uploading of copyrighted materials onto the internet.

*Penguin Group (USA) Inc. v. American Buddha*, Case No. 09-1739 (2d Cir., May 12, 2011) (*per curiam*).

Plaintiff Penguin Group, a New York book publisher, sued defendant American Buddha, an Oregon corporation located in Arizona, for copyright infringement, in New York. Penguin Group alleged that American Buddha published complete copies of four of the plaintiff's books on American Buddha's websites. The defendant moved to dismiss the complaint for lack of personal jurisdiction, arguing that it lacked sufficient ties to New York and that the plaintiff had alleged no infringing activity within New York. The district court granted American Buddha's motion to dismiss.

Due to a split of authority on the jurisdictional issue, the 2d Circuit certified a question the following New York's highest court, its court of appeals: "In copyright infringement cases, is the situs of injury for purposes of determining long-arm jurisdiction under N.Y. C.P.L.R. § 302(a)(3)(ii) the location of the infringing action or the residence or location of the principal place of business of the copyright holder?" The New York Court of Appeals ultimately determined that in copyright infringement cases involving the uploading of a copyrighted printed literary work onto the internet, the injury caused by the infringement is suffered where the copyright owner is located—and not where the infringing material may have been uploaded from (see [IP Update, Vol. 14, No. 4](#)).

Based upon that New York Court of Appeals ruling, the 2d Circuit has now determined that the situs of the plaintiff's alleged injury was New York, where the plaintiff resides. Accordingly, the 2d Circuit vacated the district court's judgment for defendant and remanded the case for the district court to consider whether Penguin Group has established the four remaining jurisdictional requirements and the extent to which the exercise of jurisdiction over the defendant would be consistent with the requirements of due process.

### ***Copyright / Prejudgment Interest***

#### **Prejudgment Interest in Copyright Infringement Suit Tracks to Date of First Infringement**

by Whitney D. Brown

The U.S. Court of Appeals for the Third Circuit affirmed a nearly \$20 million verdict in favor of a plaintiff-appellee, finding that an additional award of prejudgment interest should be applied from the date when a fraud that resulted in a copyright infringement began, not when the plaintiff discovered the infringement. *William A. Graham Co. v. Haughey et al.*, Case No. 10-2762 (3d Cir., May 16, 2011) (Smith, J.).

In 1991, Thomas P. Haughey left his position with The Graham Company, an insurance brokerage, to join USI MidAtlantic Inc., one of Graham's competitors. When Haughey left Graham, he took two binders containing hundreds of pages of text describing various types of insurance coverages, exclusions, conditions and similar matter. The materials had been prepared by Graham employees and were protected by Graham's copyrights. From July 1992 until 2005, Haughey and employees at his new employer used the materials to prepare insurance coverage proposals for presentations to clients.

Graham did not discover the unauthorized use of its binder materials until November 2004. In February 2005, plaintiff Graham filed a copyright infringement suit against Haughey and USI MidAtlantic. The defendants argued that the Copyright Act's three-year statute of limitations barred the plaintiff's claims, but the district court rejected their argument. The district court determined that the "discovery rule," which tolls the limitations period until the plaintiff learns of the cause of action or with reasonable diligence could have done so, applied to the Copyright Act. At trial,

the plaintiff did not seek statutory damages, but instead sought actual damages in the form of the defendants' profits attributable to the infringement. The plaintiff argued that defendant USI MidAtlantic had earned \$32 million in profits that was directly attributable to the infringement, with defendant Haughey personally earning \$3 million from the infringement due to commissions. The burden then shifted back to the defendants to prove that their revenues were attributable to factors other than the copyrighted work. The jury found for the plaintiff, awarding more than \$16.5 million against defendant USI MidAtlantic and nearly \$2.3 million from defendant Haughey, representing about 70 percent of USI's profits and 75 percent of Haughey's profits. Subsequently the court set aside the jury's verdict, determining that Plaintiff had in fact been placed on notice of Defendants' conduct as early as fall of 1991. A second trial, limited to damages, resulted in a second jury verdict awarding \$1.4 million in damages against defendant USI and \$268,000 against defendant Haughey.

The parties appealed to the 3d Circuit (*Graham I*). The plaintiff argued that the district court's holding regarding notice was mistaken, while the defendants argued that the plaintiff had failed to prove a causal nexus between the defendants' alleged infringement and profits. The 3d Circuit ruled in *Graham I* that the plaintiff had effectively shown causation and that the district court had erred in finding that the plaintiff could have reasonably discovered the infringement before February 2002. The 3d Circuit remanded the case to the district court for a determination of whether the defendants were correct in their argument that 70 percent and 75 percent apportionments of the defendants' profits was "excessive." On remand, the district court rejected the "excessiveness" argument and reinstated the original jury verdict.

In their second appeal to the 3d Circuit (*Graham II*), the defendants argued that the nearly \$20 million jury verdict "shocks" the judicial conscience and was improper. The defendants further argued that the award of prejudgment interest dating from when the fraud allegedly began was improper, maintaining that such interest should only be applied from 2004, the date when the plaintiff allegedly discovered the infringement. The defendants also argued that the district court's tolling of the limitations period because of the "discovery rule" and USI MidAtlantic's alleged concealment of the infringement should also toll the interest period.

The 3d Circuit disagreed, upholding the jury verdict and finding that use of the discovery rule to change the date of accrual and delay the onset of prejudgment interest would "warp its fundamentally plaintiff-friendly purpose" and would "give defendants additional incentive to conceal their tortious or otherwise illegal acts," given that "a fraudster would owe no interest on his purloined cash until discovery of the theft, and would thus be allowed to benefit from an interest-free loan." The 3d Circuit also rejected USI's arguments that its profits could be attributed to the expertise and hard work of its brokers, more than its use of the plaintiff's copyrighted materials, noting that while it had some sympathy for USI MidAtlantic, "such sympathy is not, however, sufficient to justify overturning the jury's verdict."

**Practice Note:** If a plaintiff overcomes the tolling of the statute of limitations based on the “discovery rule,” that rule has no effect on the date upon which prejudgment interest begins to accrue. Prejudgment interest will accrue beginning on the date the infringement occurred, *not* the date when the plaintiff discovered the infringement.

## *Unfair Competition / California § 17200*

### **Standing Under California § 17200 Only Requires Injury From Business Practice**

by William Diaz and Daniel Powers

Drawing upon recent California Supreme Court rulings, the U.S. Court of Appeals for the Federal Circuit reversed a California federal district court’s dismissal of claims under the state’s unfair competition law, finding the court had wrongly dismissed the claims for lack of standing. *Allergan, Inc. et. al. v. Athena Cosmetics, Inc. et. al.*, Case No. 10-1394 (Fed. Cir., May 24, 2011) (Gajarsa, J.).

Allergan, a manufacturer of an FDA-approved treatment for inadequate eyelash growth, Latisse®, brought suit alleging the defendants had infringed or induced infringement of multiple patents. Allergan also claimed defendants violated California’s unfair competition law, U.C.L. §§17200 *et seq.* With respect to the latter claim, Allergan contended that defendants’ manufacture, sale or marketing of hair/eyelash growth products that had not been approved by the FDA or state health regulators constituted unfair competition under the California statute.

The defendants countered that Allergan lacked standing because the statute only protects persons who have suffered a loss that is eligible for restitution. Restitution is a remedy that seeks to restore the status quo; it requires the plaintiff to have had an ownership interest in the money or property it seeks to recover. The district court found Allergan had no such interest in lost profits or market share because defendants’ profits derived from third-party consumers. Allergan appealed; its patent claims were stayed pending appeal of the unfair competition claim.

The Federal Circuit rejected the district court’s narrow view of the California unfair competition statute. While acknowledging that California voters had approved Proposition 64 to restrict standing requirements and address abuses that had resulted in frivolous lawsuits, the Court noted that the California Supreme Court’s decisions in two cases that were decided while the Allergan appeal was pending (*Kwikset Corp. v. Superior Court of Orange County* and *Clayworth v. Pfizer, Inc.*), demonstrated that Proposition 64 did not limit standing solely to injuries compensable by restitution. Instead, a plaintiff need only allege an injury in fact that was the result of the unfair business practice. Applying this reasoning, the Court held that Allergan had adequately pleaded a claim under U.C.L. §17200.

Importantly, the Court also rejected the defendants' claims that standing under U.C.L. §17200 required a plaintiff to have direct business dealings with a defendant. The Court denied that Proposition 64 added any such "business dealings" requirement to U.C.L. §17200 claims.

**Practice Note:** The *Allergan* decision demonstrates that while standing to file suit under §17200 is more limited than it was in the past, §17200 remains a potent tool that litigants can use to challenge a competitor's practices.

### ***Trade Secrets / Disclosure***

#### **Combining Disclosed Technology Can Be a Protectable Trade Secret**

by Adam A. Auchter

The U.S. Court of Appeals for the Fifth Circuit has held that, under Texas law, unique combinations of previously disclosed elements can constitute a trade secret. *Tewari De-Ox Sys., Inc. v. Mountain States/Rosen, L.L.C.*, Case No. 10-50137 (5th Cir., Apr. 5, 2011) (Prado, J.).

Plaintiff Tewari developed a "zero oxygen" meat-packing method and disclosed the technology involved in multiple 2004 patent applications. In 2005, defendant Mountain States/Rosen (MTSR) signed a non-disclosure agreement with Tewari in efforts to determine if the plaintiff's method could increase the shelf-life of MTSR's case-ready cuts of lamb. Tewari claimed that it revealed trade secrets to MTSR during the demonstration of his method and that MTSR later misappropriated those trade secrets.

The district court initially rejected the defendant's argument that the prior disclosure in the 2004 patent application destroyed the secret, on the ground that a patent application does not disclose a trade secret. However, on a motion for reconsideration, the court ruled that any information disclosed in the 2004 patent applications were no longer trade secrets when the NDA was signed in March 2005, relying on *Group One v. Hallmark*, and granted summary judgment to MTSR. The district court determined that the difference between what was disclosed in the 2004 patent applications and the 2005 meeting with the defendant was "merely a customization" based on MTSR's needs and using MTSR's equipment, and therefore Tewari had no trade secret to protect.

The 5th Circuit, sitting *de novo*, agreed with the district court that any information disclosed in the 2004 patent applications were no longer trade secrets. However, the court determined that the district court incorrectly ruled that Tewari's unique combinations of previously disclosed elements could not constitute trade secrets.

Although no post-2000 Texas case directly addresses whether a published patent application destroys the secrecy of its contents for trade secret purposes, the 5th Circuit relied on the weight of authority from the other jurisdictions. A

published patent application is not “secret.” The plaintiff’s 2004 applications were published a year prior to the meeting with MTSR, and any contents disclosed would no longer qualify as trade secrets.

Tewari, in an affidavit, defined multiple trade secrets that it argued were not disclosed in the 2004 applications. They involved combinations of the disclosed information as well as new adaptations. The 5th Circuit, relying on its opinion in *Water Services*, explained that a trade secret can exist in a combination of characteristics and components, each of which, by itself, is in the public domain, but the unified process, design or operation of which in unique combination, affords a competitive advantage and is a protectable secret. Even though the district court rejected Tewari’s alleged trade secrets as “customization” or “trial-and-error” processes, the 5th Circuit cited to *Ventura Manufacturing*, which specifically granted trade-secret protections to a trial-and-error process. As such, Tewari created a fact dispute as to whether it had trade secrets that it disclosed to the defendant.

Because the district court incorrectly defined Tewari’s trade secrets and failed to consider that a unique combination of previously disclosed elements constituted protectable trade secrets, the 5th Circuit reversed the summary judgment on the plaintiff’s trade secret misappropriation and breach of fiduciary duty claims and remanded the case.

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