Client Alert

April 29, 2014

Supreme Court Unanimously Overrules the Federal Circuit's Fee-Shifting Framework in Patent Cases

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Today, the Supreme Court issued two unanimous decisions that considerably relax the standard for awarding attorney's fees against plaintiffs who bring meritless patent suits. These decisions are timely given the ongoing debate in Congress regarding the inclusion of a "fee-shifting" provision in the pending patent reform legislation.[1]

Under 35 U.S.C. § 285, a district court has discretion to award attorney's fees to a prevailing party in a patent case if the court determines that the case is "exceptional." Under the standard crafted in *Brooks Furniture Manufacturing., Inc. v. Dutailier International, Inc.*, attorney's fees previously were awarded against the patentee only if the suit was (1) objectively baseless, and (2) brought in subjective bad faith, absent misconduct during litigation or inequitable conduct before the Patent and Trademark Office.[2]

The Supreme Court's decision in *Octane Fitness, LLC v. ICON Health & Fitness, Inc.* overrules *Brooks Furniture*, holding that its standard for an award of fees was "unduly rigid." The Court held that, as used in §285 of the patent code, "an 'exceptional' case is simply one that stands out from others with respect to the substantive strength of a party's litigating position (considering both the governing law and the facts of the case) or the unreasonable manner in which the case was litigated." The Supreme Court vacated and remanded the case for consideration under this standard.

In *Highmark, Inc. v. Allcare Health Management Systems, Inc.*, the companion case to *Octane,* the Supreme Court held that the statutory text compelled that "an appellate court should apply an abuse-of-discretion standard in reviewing all aspects of a district court's § 285 determination."

DETAILED DISCUSSION

Octane Fitness, LLC v. ICON Health & Fitness, Inc.

In *Octane Fitness*, the defendant prevailed on summary judgment and moved the district court for an award of attorney's fees under § 285, pointing to specific infringement assertions and proposed claim constructions by ICON that Octane argued were "unreasonable and unsupportable."[3] The district court denied the motion, finding that Octane had failed to meet both the objective and subjective requirements to prove the case as "exceptional."[4] The court also briefly addressed the poor showing of subjective bad faith. The court dismissed a proffered email exchange between ICON sales executives as "stray comments by employees with no demonstrated connection to

[1] Prior client alerts on this issue can be found here.

[2] *See* 393 F.3d 1378, 1381 (Fed. Cir. 2005); *see also Beckman Instruments, Inc. v. LKB Produkter AB*, 892 F.2d 1547, 1551 (Fed. Cir. 1989).

[3] *See ICON Health & Fitness, Inc. v. Octane Fitness, LLC*, No. 09-319, 2011 WL 39000975, at *1-2 (D. Minn. Sept. 6, 2011).

[4] *Id.* at *1.

the lawsuit" and also rejected the disparate sizes of the parties and ICON's decision not to commercialize as purported evidence of subjective bad faith.[5]

On cross-appeal before the Federal Circuit, Octane argued that the district court applied an overly restrictive standard in refusing to find the case exceptional under § 285.[6] The Federal Circuit rejected this argument, concluding that the record does not show error in the trial court's decision to deny the motion and "[w]e have no reason to revisit the settled standard for exceptionality."[7]

Today's unanimous decision by Justice Sotomayor reversed the Federal Circuit's formulation of the standard for "exceptional" case.[8] First, the Court explained that the text of § 285 makes "patently clear" that the power to award attorney's fees in patent litigation is reserved for "exceptional" cases.[9] Because the Patent Act does not define "exceptional," the Court turned to the ordinary meaning of the word to conclude that, when Congress recodified the fee-shifting provision in the Patent Act as § 285, the word "exceptional" meant "uncommon," "rare," or "not ordinary."[10] Thus, the Court held that an "exceptional" case is "simply one that stands out from others with respect to the substantive strength of a party's litigating position…or the unreasonable manner in which the case was litigated."[11] Analogizing to copyright law, the Court clarified that the determination under § 285 is a case-by-case exercise that should consider the totality of circumstances.[12]

In rejecting *Brooks Furniture* as "overly rigid," the Court first explained that the Federal Circuit's formulation "superimposes an inflexible framework onto statutory text that is inherently flexible."[13] The Court took issue with how the framework would require either (1) independently sanctionable conduct, or (2) a showing that plaintiff's case was objectively baseless *and* brought in subjective faith.[14] Instead, the Court clarified that a district court may award fees even in cases where a party's unreasonable conduct is "exceptional" even if "not necessarily independently sanctionable."[15] Furthermore, "a case presenting either subjective bad faith or exceptionally meritless claims" may also warrant a fee award.[16] The Court rejected ICON's argument that the dual requirement of subjective bad faith and objective baselessness follows from the Court's decision involving an exception to the *Noerr-Pennington* doctrine of antitrust law.[17] The Court reasoned that Section 285 shares neither common roots with the antitrust

[5] *Id.* at *4.

[6] *ICON Health & Fitness, Inc. v. Octane Fitness, LLC*, 496 Fed. App'x 57, 65 (Fed. Cir. 2012).

[7] *Id.*

[8] 572 U.S. ____ (2014).

[9] *Id.* (slip op. at 7).

[10] *Id.*

[11] *Id.* at 7-8.

[12] *Id.* at 8.

[13] *Id.*

[14] *Id.* at 8-9.

[15] *Id.* at 9.

[16] *Id.*

[17] *Id.* at 10.

context of the *Noerr-Pennington* doctrine nor the First Amendment concerns that the "sham exception" to that doctrine was crafted to address.[18]

Furthermore, the Court observed that the *Brooks Furniture* framework is "so demanding that it would appear to render § 285 largely superfluous."[19] The Court declined to construe "exceptional" so narrowly as to read out the fee-shifting provision in effect.[20] Finally, the Court rejected the Federal Circuit's requirement that patent litigants establish entitlement to attorney's fees by clear and convincing evidence. The Court found that § 285 "imposes no specific evidentiary burden, much less such a high one."[21] Given that patent-infringement litigation has always been governed by a preponderance of the evidence standard, this standard should apply in fee-shifting determinations to "allow[] both parties to 'share the risk of error in roughly equal fashion.'"[22]

Highmark, Inc. v. Allcare Health Management Systems, Inc.

In *Highmark*, the trial court entered summary judgment of non-infringement in favor of Highmark.[23] Highmark moved for an award of attorney's fees. The trial court found the case "exceptional" under § 285 and awarded attorney's fees, emphasizing Allcare's (1) failure to have an attorney, "let alone a patent attorney," investigate its counterclaims before filing; (2) continued assertion of infringement claims well after such claims had been shown by its own experts to be without merit; (3) assertion of defenses it and its attorneys knew to be frivolous; and (4) misrepresentations to the Western District of Pennsylvania in connection with a motion to transfer.[24]

On appeal, a divided Federal Circuit panel affirmed the district court's finding of an "exceptional" case based on Allcare's allegations of infringement of one particular patent claim, but the appellate court reversed the district court's finding that Allcare's other claims and conduct during litigation supported an exceptional case finding.[25]

In *Highmark*, Justice Sotomayor again penned a unanimous opinion that reversed the Federal Circuit's decision. The Court held that "an appellate court should apply an abuse-of-discretion standard in reviewing all aspects of a district court's §285 determination."[26]

PRACTICAL IMPLICATIONS

The issue of fee-shifting has been hotly debated as a potential legislative reform to help curb frivolous patent litigation. The Supreme Court's decisions today ease the way for the award of attorney's fees to the prevailing party in patent cases deemed "exceptional." The decisions also restore the discretion of fee awards back into the hands of district courts by giving district courts more flexibility to deviate from the "American rule" that generally governs attorney's fees in U.S. litigation. District courts are no longer bound to the rigid formulation under *Brooks Furniture* but rather have the breathing room necessary to a more hands-on approach to case administration.

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[18] *Id.*

[19] *Id.* at 10-11.

[20] *Id.* at 11.

[21] *Id.*

[22] *Id.*

[23] *See Highmark, Inc. v. Allcare Health Mgmt. Sys.*, 706 F. Supp. 2d 713, 716 (N.D. Tex. 2010).

[24] *Id.* at 735-37.

[25] *Id.* at 1319.

[26] 572 U.S. ____ (2014).

Although the "ordinary meaning" clarification of "exceptional" still leaves much to be determined by the district courts, the Supreme Court has made clear that the bar to fee awards is lower than the standard that was previously applied. For example, conduct that falls short of Rule 11 sanctions may nevertheless warrant fee-shifting, and a strong showing of subjective bad faith *or* exceptionally meritless legal positions may also suffice to warrant a fee award. The lower burden of proof established in *Octane* will further enable litigants to prevail under this new legal standard." The lowered bar, both in legal standards as well as evidentiary burden of proof, makes the threat of attorney's fees a more realistic deterrent to meritless suits designed to extort licensing fees or injure competition as a strategic weapon.

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