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INFRINGEMENT ASSERTIONS IN THE NEW WORLD ORDER

Wednesday, Oct 17, 2007 — The recent Supreme Court and Federal Circuit decisions in MedImmune, eBay, and Seagate have significantly impacted the analysis, risk calculus, and practices of an accused infringer who receives a typical patent assertion letter. These cases, and their progeny, also have the potential to alter the common practice of patentees sending such notice letters in the first place.

In Part I, this guest column examines the historical approach that has been commonly used by patentees to put potential targets on notice of a patent claim without risking a declaratory judgment, as well as the risks that would attach once such a notice was received.

In Part II, it explains how recent Supreme Court and Federal Circuit decisions have changed the law in critical respects affecting these prior practices.

In Part III, it addresses the new options available to potential targets in light of this recent Supreme Court and Federal Circuit precedent.

Part I. Patent Infringement Assertions - The Imbalance In Power Between Patentee and Alleged Infringer

Traditionally, it has been the practice of patentees to send assertion letters identifying the patent at issue and seeking to engage in licensing discussions.

Viewed from the perspective of the patentee, the purpose of such letters was two-fold. First, as a legal matter, it was a way to put accused infringers on actual notice of its patent rights, for purposes of damages and willful infringement.

In some circumstances, in order to commence the period under which a patentee could collect damages, a patentee would have to send a written notice letter to an accused infringer that specifically identifies the relevant patent and makes a charge of infringement with sufficient detail for the recipient to understand what specific products are implicated by the patent claims.

Second, as a practical matter, it was a way to initiate licensing discussions without actually starting a lawsuit. A carefully crafted notice letter could also ensure that the patentee would not open itself up to a Declaratory Judgment lawsuit brought by the accused infringer.

For a large company, it is not uncommon to receive many such assertions every month. Viewed from the perspective of the recipient of such a letter responsible for deciding how to respond to such letters, this situation was fraught with risk.

First, for purposes of willful infringement and whether an award of enhanced damages may ultimately be awarded, receipt of such a letter was considered to trigger a “duty of care” to investigate the assertion and ordinarily to procure advice from competent counsel of the issue, a process that requires the devotion of time, resources, and money.

Second, assuming the letter was carefully crafted to not expressly threaten litigation, but was couched as a request to engage in licensing discussions, the recipient would not even be in a position to seek a declaratory judgment action in a location of its choosing, absent establishing a “reasonable apprehension” of the patentee bring suit.

Third, if negotiations did ensue, the patentee had potent negotiating weapons at its disposal, including the twin threats of an almost certain injunction and the very real possibility of treble damages for willful infringement, if the infringement charge were ultimately successful.

Finally, if litigation were ultimately initiated by the patentee, the accused infringer would be faced with the Hobson’s choice of whether to waive the attorney-client privilege by relying on the opinion of counsel to defend against the charge of willful infringement (with the attendant uncertainty of whether such waiver would extend to conversations with and work-product of trial counsel), or whether to not rely on the opinion of counsel, thus preserving the privilege, but increasing the risk of being held to be a willful infringer.

The collective impact of these circumstances allowed patentees to collect large sums of money based on even dubious infringement assertions and patents of questionable validity.

In recent years, there have been a number of highly publicized infringement actions where dubious patents asserted by patent licensing entities were found to be willfully infringed and the infringers were permanently enjoined.

For example, in NTP’s infringement action against Research In Motion, the maker of the popular Blackberry device, the public was horrified at the thought of an injunction against the use of Blackberries and astonished to learn that NTP received \$400 million to settle the case and avoid this outcome. (Adding insult to injury, certain of the patents that were found valid and infringed have since been found invalid in subsequent reexamination proceedings by the U.S. Patent and Trademark Office.) Against that background, our story begins.

Part II. Recent Changes In The Law Cooperate To Change This Imbalance

Three recently decided lines of cases cooperate to change this historical imbalance and level the playing field between patentee and accused infringer.

*** Injunctions ***

First, in the Supreme Court’s decision in *eBay, Inc. v. MercExchange L.L.C.*, 126 S. Ct. 1837 (2006), the Court eliminated the leverage of the almost certain remedy of a permanent injunction held by all patentees.

The eBay Court recognized that the Patent Law stated that a court “may” grant an injunction, not that it must. Specifically, the Court rejected the rationale that because a patent is a property right that confers the patentee with the right to exclude, irreparable harm should be presumed and injunctions against adjudicated infringers should be a near-certainty in patent cases.

Instead, the Court held that the traditional four-factor test for injunctive relief must be applied in patent cases, including a determination of: (i) whether the patentee would be irreparably harmed in the absence of an injunction; (ii) whether adequate remedies at law (such as monetary damages) exist; (iii) the balance of the hardships; and (iv) the public interest. In order to be entitled to a permanent injunction, the patentee bears the burden of satisfying this test.

The Court also directly addressed non-practicing patentees, i.e., licensing entities, questioning whether such entities, which have demonstrated the desire to license the patent for lump-sum payments and who have no competing product, could demonstrate irreparable harm.

Subsequent District Court decisions applying eBay have held that such plaintiffs, including those entities referred to as “patent trolls,” are generally not entitled to injunctive relief. For example, in each of *z4 Technologies, Inc. v. Microsoft*

Corp., 434 F. Supp. 2d 437 (E.D. Tex. 2006), *Finisar Corp. v. DirecTV Group, Inc.*, No. 1:05-cv-264, 2006 U.S. Dist. LEXIS 76380 (E.D. Tex. July 7, 2006) and *Paice LLC v. Toyota Motor Corp.*, No. 2:04-cv-211, 2006 WL 2385139 (E.D. Tex. Aug. 16, 2006), as well as the remanded *MercExchange, LLC v. eBay, Inc.*, 500 F. Supp.2d 556 (E.D. Va. 2007), the District Court denied plaintiff's request for a permanent injunction, based largely on findings that there was no irreparable harm and that remedies at law would be adequate to compensate the plaintiff-patentee.

In each of those cases, the patentee did not compete with the accused infringer in the market for the infringing product and had exhibited a willingness to license its patents for monetary considerations.

It should also be noted that recently the Federal Circuit has also shown a greater sensitivity to decisions concerning injunctions, expressly recognizing that the right to exclude others from practicing the invention is not the same thing as a right to put your competitor out of business.

Earlier this year, in *Vonage v. Verizon*, the Federal Circuit agreed to stay a permanent injunction against Vonage, pending appeal. The stay gave Vonage additional time to try to develop a design-around for its future products.

It also allowed Vonage to pursue its appeal. If the stay were not granted, it would have been devastating to Vonage's continued viability. In a later decision in the same case, *Vonage v. Verizon*, No. 2007-1240, Slip. op. (Fed. Cir. Sept. 26, 2007), the Court noted in a footnote that while "Verizon had a cognizable interest in obtaining an injunction to put an end to infringement of its patents; it did not have an interest in putting Vonage out of business." Slip op., p. 25 n.12.

*** Duty to Avoid Infringement ***

Second, in the Federal Circuit's en banc decision in *In re Seagate Technology L.L.C.*, Misc. Docket No. 830, 2007 U.S. App. LEXIS 19768 (Fed. Cir. Aug. 20, 2007), the Federal Court drastically altered the standard of care necessary to exercise to avoid enhanced damages.

The en banc holding in *Seagate* completes the evolution of the willful infringement standard that began in *Underwater Devices, Inc. v. Morrison-Knudsen Co.*, 717 F.2d 1380, 1390-91 (Fed. Cir. 1983).

In *Underwater Devices*, the Federal Circuit held that notice of another's patent rights triggers a duty of due care to determine whether or not the accused infringer is infringing and that demonstrating that this duty of care was met will defeat a charge of willful infringement. *Id.*

The continuing viability of the affirmative duty of care standard for willful infringement was considered and re-affirmed by the en banc Federal Circuit as recently as 2004 in *Knorr-Bremse Systeme Fuer Nutzfahrzeuge GmbH v. Dana Corp.*, 383 F.3d 1337, 1343-44 (Fed. Cir. 2004) (en banc).

In *Knorr-Bremse*, the Federal Circuit re-affirmed the duty of care standard, but held that there is no adverse inference of willfulness associated with not producing an exculpatory opinion; rather, the determination as to willful infringement is made based on the totality of the circumstances.

More recently, in *In re EchoStar Communications Corp.*, 448 F.3d 1294 (Fed. Cir. 2006), the Federal Circuit addressed the proper scope of the waiver of work-product that results when an accused infringer relies on an opinion of counsel to defend against a willfulness claim.

The *EchoStar* Court held that when an opinion of counsel is relied upon to defend against a charge of willful infringement, there is a subject matter waiver of communications with counsel on the same subject.

The *EchoStar* Court further held that attorney work-product that is never communicated to a client does not fall within the scope of the waiver of work-product. However, the *EchoStar* decision left a few troubling issues unsettled. Specifically, while it reasoned that the proper waiver was a subject-matter waiver and rejected the assertion that waiver of work-product should not extend to advice and work-product given after the initiation of litigation, it did not squarely address the specific issue of waiver as to trial counsel.

In Seagate, the en banc Federal Circuit not only considered the specific issue of waiver as to trial counsel, but it also questioned and ultimately overturned the duty of care standard that had first been announced in Underwater Devices.

Specifically, the Federal Circuit overturned its twenty-year precedent that placed a “duty of care” on an accused infringer to avoid infringement and replacing it with a requirement that the patentee demonstrate by clear and convincing evidence that the accused infringer acted “objectively reckless.”

Under the newly announced standard, obtaining a formal opinion is no longer required, and the subjective state of mind of the accused infringer is no longer at issue. In addition, the Court expressly stated that in the ordinary course, post-complaint activities should not be the focus of a willfulness charge.

This new standard will make willfulness far more difficult to prove, and should also result in less pleading of willfulness. This will significantly reduce the threat of treble damages.

The Seagate decision also makes clear that, as a general proposition (assuming no “chicanery” on the part of the accused infringer), if an accused infringer does choose to rely on an opinion of counsel, there is no waiver of attorney-client privilege or work-product as to trial counsel.

*** Declaratory Judgments ***

Third, the Supreme Court’s decision in MedImmune, Inc. v. Genentech Inc., 127 S. Ct. 764 (2007) and the subsequent Federal Circuit cases applying MedImmune, such as Sandisk and Guardian, have changed the jurisdictional standing requirements that govern Declaratory Judgment Actions.

Prior to MedImmune, the Federal Circuit held that in order to bring a Declaratory Judgment Action, there had to be a “reasonable apprehension of suit.”

Under this prior test, a patentee could draft a carefully crafted notice letter which could start the damages pending under 35 U.S.C. 284 without risking a declaratory judgment action by the accused infringer.

In MedImmune, the Supreme Court ruled that a licensee need not repudiate its license in order to have standing to bring a Declaratory Judgment Action against the patentee.

In a footnote, the Supreme Court brought into question the Federal Court’s test for when a declaratory judgment action was appropriate, noting that the Federal Circuit’s “reasonable apprehension of suit” test “conflicted with” and “is also in tension with” certain Supreme Court precedent. MedImmune, 127 S. Ct. at 774 n.11.

In subsequent Federal Circuit cases, the Federal Circuit recognized that MedImmune abrogated the “reasonable apprehension of suit” test, and has made clear that a declaratory judgment plaintiff no longer needs to establish a reasonable apprehension of suit in order to establish that there is an actual controversy between the parties.

Rather, according to MedImmune, the proper inquiry into declaratory judgment jurisdiction is whether there is a justiciable controversy within the meaning of Article III of the Constitution, including standing and ripeness.

This can be satisfied by demonstrating under all the circumstances an actual or imminent injury that can be redressed by judicial relief and that is of “sufficient immediacy and reality to warrant the issuance of a declaratory judgment.”

The Federal Circuit’s application of MedImmune has made it clear that a course of conduct can establish that there is an actual controversy between the parties sufficient to confer declaratory judgment jurisdiction even without the accused infringer having reasonable apprehension of suit.

For example, in SanDisk Corp. v. STMicroelectronics, Inc., 480 F.3d 1372 (Fed. Cir. 2007), the Federal Circuit held that Declaratory Judgment jurisdiction existed based on pre-suit patent assertion correspondence even though the

patentee had not threatened the accused infringer with an infringement suit and indeed affirmatively stated it had no plan whatsoever to sue the alleged infringer.

Similarly, in *Sony Electronics Inc. v. Guardian Media Technologies, Ltd.*, No. 2006-1363, 2007 U.S. App. LEXIS 18465 (Fed. Cir. Aug. 3, 2007), the Federal Circuit held that Declaratory Judgment jurisdiction existed based upon pre-suit patent assertion correspondence even though the patentee stated that it was at all times willing to negotiate a “business resolution” with the alleged infringer.

This change in Declaratory Judgment jurisprudence is significant, because it obviates the concept of “carefully crafted notice letters” and confers more of the power of choosing the forum and timing of initiating litigation to the accused infringer.

Part III. The New World Order

In contrast to the traditional power imbalance described in Section II above, an accused infringer in receipt of a patent assertion letter now has a number of arrows in his sling.

First, under eBay and its progeny, the threat of injunctive relief has been vastly reduced and all but eliminated in the ordinary course where the patentee is a patent holding company. The elimination of this risk goes a long way towards allowing a more accurate assessment and response to such threats.

Second, based on Seagate, there is no longer any affirmative duty to obtain an opinion for the purpose of defending against a willful infringement charge.

Accordingly, the troubling issues of waiver as to attorney-client communications and attorney work-product are unlikely to ever arise, and, if they do, the Federal Circuit has held that absent extraordinary circumstances the scope of the waiver does not extend to communications with and work product of trial counsel.

Under the new willfulness standard — the patentee must prove that the accused infringer was objectively reckless — it still behooves the accused infringer to do a reasonable investigation to form an objectively reasonable basis for deciding not to license the patent at issue.

And of course prudence may suggest obtaining an opinion of counsel for this purpose. But the tougher willfulness standard drastically reduces the risk of treble damages based on a finding of willful infringement.

Moreover, the Seagate Court limited that the circumstances in which a willfulness claim could be made, e.g., noting that a willfulness claim could not ordinarily be based on post-complaint conduct, unless a preliminary injunction were sought and obtained.

Third, the post-MedImmune line of Federal Circuit cases provide an accused infringer with the option of responding affirmatively by initiating a Declaratory Judgment Action, foreclosing the ability of patentee’s to threaten moving forward or to sue in venues that are considered to be more friendly towards patentees.

These same developments, however, could alter the very practice of patentees sending assertion letters in the first place. Specifically, patentees might begin to sue first and then negotiate, rather than writing an early notice letter, in order to preserve their choice of forum, as has become a standard operating procedure in the Eastern District of Texas.

Furthermore, patentees could also now have the incentive to act more aggressively by seeking preliminary injunctions in order to maintain the leverage of post-complaint willfulness charges. While it is unclear if this will happen with greater frequency, this course of action was expressly suggested by the Federal Circuit in Seagate.

Specifically, in *Seagate*, when the Federal Circuit commented that the post-complaint activities should not be the focus of a willfulness charge, it also suggested that patentees who believed an infringers ongoing post-complaint activities would be willful, could combat any such behavior by seeking a preliminary injunction.

The *Seagate* Court noted, however, that “[a] patentee who does not attempt to stop an accused infringer’s activities in this manner should not be allowed to accrue enhanced damages based solely on the infringer’s post-filing conduct.” In *re Seagate*, 2007 U.S. App. LEXIS 19768, at *30.

*** Conclusion ***

In the New World Order created by this triumvirate of cases, the traditional patentee practice of engaging in carefully crafted letter-writing campaigns may change.

While there is no doubt that assertion letters will continue to be written, and that licenses will likely result from many such letters, the calculus entailed in responding to such letters has changed dramatically.

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