

Patent Litigation: Is The Party Over?

Monday, July 30, 2007 — Patent protection is nothing new. America’s Founding Fathers knew all about the subject when they drafted the Constitution, and they specifically gave Congress the power “to promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries.” But until late in the twentieth century, no one seemed to care all that much about patent protection.

That started changing in the 1970s, as companies discovered the value of patents in an increasingly knowledge-based economy and law firms — especially big law firms — realized they could earn millions of dollars litigating patent infringement cases. For example, Polaroid won a billion-dollar judgment against Kodak in 1985 for infringement of Polaroid’s patent for instant photography. With so much at stake, patent law was transformed from a sleepy backwater of the law into a white-hot practice area.

The increase in patent litigation also stemmed from the creation of the Federal Circuit Court of Appeals, to which Congress gave exclusive appellate jurisdiction over patent claims in 1982. The Federal Circuit turned out to be very protective of patent holders. Furthermore, the Supreme Court rarely stepped into patent disputes because patent law was regarded as the exclusive province of lawyers with science degrees and, with the Federal Circuit’s exclusive appellate jurisdiction over patent claims, no meaningful circuit conflicts arose for the Supreme Court to resolve. As a result, patent litigation has flourished on the Federal Circuit’s watch, with the number of patent lawsuits at least tripling since 1970.

But things have started changing rapidly during just the first two terms of the Roberts Court, as the Supreme Court has rejected a number of the Federal Circuit’s most important legal doctrines, all of which protected patent holders. The Supreme Court’s willingness to grant certiorari in complex patent cases, and the zeal with which it has checked the Federal Circuit’s patent-friendly jurisprudence, suggests that the patent boom may be about to subside.

The Supreme Court’s assault on the rights of patent holders began in a limited way in the 2002 case of *Holmes Group v. Vornado*,⁽¹⁾ when the Court held that a case arises under federal patent law — and therefore is subject to the Federal Circuit’s exclusive appellate jurisdiction — only when the plaintiff’s well-pleaded complaint “establis[hes] either that federal patent law creates the cause of action or that the plaintiff’s right to relief necessarily depends on resolution of a substantial question of patent law.”⁽²⁾

By applying the well-pleaded complaint rule in this context, the Court checked the Federal Circuit’s efforts to claim exclusive jurisdiction over any case that included a patent law question, including requests for declaratory relief where the defendant counter-claimed for patent infringement (the facts of the *Holmes Group* case). The Court thereby prevented parties from forcing more cases into the patent-friendly confines of the Federal Circuit.

The assault accelerated during the past two terms, as the Supreme Court struck down three staples of the Federal Circuit's patent jurisprudence. In *KSR v. Teleflex*,⁽³⁾ the Court unanimously rejected the Federal Circuit's test for measuring the obviousness of inventions, which focused on whether some teaching, suggestion or motivation (the "TSM" test) existed at the time the invention was conceived that would have led an average person in the field to envision the creation.

In its place, the Court adopted a commonsense inquiry that considers any evidence of obviousness and makes it easier to challenge a patent as void for obviousness.⁽⁴⁾

The Court also made it easier to challenge the validity of a patent in *MedImmune v. Genentech*.⁽⁵⁾ For years, the Federal Circuit had closed the courthouse doors to licensees that tried to challenge the validity of the licensed patent, finding that, so long as the licensee was meeting its obligations under its license, it could not demonstrate an Article III case or controversy.

The Federal Circuit required that patent licensees materially breach their licenses before they could challenge the validity of the licensed patent. The Supreme Court rejected that technical application of the Article III case or controversy requirement, echoing its reasoning in *Lear v. Adkins*⁽⁶⁾ that "[l]icensees may often be the only individuals with enough economic incentive to challenge the patentability of an inventor's discovery. If they are muzzled, the public may continually be required to pay tribute to would-be monopolists without need or justification."⁽⁷⁾

Finally, in *eBay v. MercExchange*,⁽⁸⁾ the Court struck down the Federal Circuit's "general rule that courts will issue permanent injunctions against patent infringement absent exceptional circumstances." That standard conflicted with the Supreme Court's traditional rule that permanent injunctive relief is only available to a plaintiff that shows that: (1) it has suffered irreparable injury; (2) its legal remedies are inadequate; (3) the balance of hardships justifies equitable relief; and (4) the public interest would not be disserved by the injunction.

Unlike the Federal Circuit, the Supreme Court found nothing special about patents that justified a presumption in favor of granting permanent injunctive relief to patent holders. In addition, several justices were skeptical of the Federal Circuit's eagerness to grant injunctions to patent holders in light of the fact that some firms have sought patents "not as a basis for producing and selling goods but, instead, primarily for obtaining licensing fees."⁽⁹⁾ In their view, those firms could use the easily obtained injunction simply as a bargaining tool to charge exorbitant licensing fees.

It is surprising enough for the Supreme Court to issue so many key decisions in one area of law in such a short period, especially in such a specialized area. But the uniformity of the decisions and the way the Court has criticized the Federal Circuit says even more about the Court's frustration with the patent boom.

For example, during the *KSR* oral argument, Justice Antonia Scalia derided the TSM test as "gobbledygook" and "irrational." Chief Justice Roberts echoed that sentiment and hypothesized that the TSM test's only purpose was its profitability for the patent bar. Those comments reflect a level of unhappiness the Court rarely shows toward a single circuit. And while the Court has tempered that criticism in its written opinions, several justices continue to express concern that zealous patent protection has "discourage[d] research by impeding the free exchange of information . . . , by leading [researchers] to conduct costly and time-consuming searches of existing or pending patents, by

requiring complex licensing arrangements, and by raising the costs of using the patented information, sometimes prohibitively so.” (10)

The Supreme Court has also implicitly recognized that too much patent protection is inappropriate in today’s global economy. The very fact that the Court has granted certiorari in so many patent cases, after years of abstention, makes this clear, but this theme became even clearer when the Court decided *Microsoft v. AT&T Corporation* (11) in April. There, the Court reversed the Federal Circuit’s judgment that Microsoft infringed an AT&T patent when it sent the code for its Windows software to computer manufacturers in Europe. United States patent law provides that, while no infringement occurs when a patented product is made and sold in another country, infringement does occur when a party supplies “components” of a patented product from the United States to a foreign manufacturer for assembly abroad. (12)

The Supreme Court, in an opinion by Justice Ginsburg, determined that the Windows software only developed into a “component” when it was “expressed as a computer-readable ‘copy,’ e.g., on a CD-ROM.” (13) Thus, the software code that Microsoft transmitted to Europe did not constitute a component that could have infringed on AT&T’s patent.

However, Justice Stevens (the lone dissenter) pointed out that the fact that software code is intangible should not preclude it from being considered a component. A component is merely an element or ingredient of a larger object. The fact that software code “is an idea without physical embodiment” (14) does not change the fact that the code is the essential ingredient in the Windows recipe, an element that manufacturers must have to install Windows on any computer. Nevertheless, the majority read and applied the patent law narrowly to avoid extending its reach to business activities that occurred predominantly overseas and it emphasized that any doubts about Microsoft’s actions were resolved by the presumption against extraterritorial application of American law, a form of judicial restraint the Federal Circuit had ignored.

In all of these cases, the Court eliminated a rule that encouraged patenting or protected patent holders, and the Court has made no secret of its concern that patent holders’ rights are too expansive. That was most clear in *KSR*, where the Court criticized the Federal Circuit’s formalistic TSM test as potentially hampering the inventive process instead of promoting it. There, the Court recognized that “[a]pplication of the [obviousness] bar must not be confined within a test or formulation too narrow to serve its purpose.” (15)

The larger problem for patent lawyers is that the Supreme Court seems to believe that the Federal Circuit has not served its purpose and that has caused the Court to intervene in this highly specialized area of law. After all, Congress created the Federal Circuit in 1982 to promote uniformity and stability in the law and to eliminate the forum shopping that occurred when patent cases traveled through the regional circuits, not to give patent holders a home-court advantage.

With the stakes so high, the Supreme Court will continue to police the Federal Circuit’s opinions for decisions that unreasonably favor patent holders. The Federal Circuit may try to ward off review by limiting rules that seem suspect, as it did after the Supreme Court granted certiorari in the *KSR* case, broadening its concept of the TSM test to retain flexibility and “require consideration of common knowledge and common sense.” (16)

However, the Supreme Court seems determined to limit patent holders' rights. Naturally, patent litigation may stay hot for years, as parties test out the Supreme Court's new rules and evaluate how the lower courts apply them and, given the increasing importance of intellectual property in our economy, patent litigation is not destined to return to being a quiet backwater of the law. But with an increasingly skeptical Supreme Court taking the place of the friendly Federal Circuit, patent holders are likely to bring fewer infringement claims in the future. That means less business for patent litigators in the long run — and the likely end of the patent boom as we know it.

— By Rex S. Heinke and Scott J. Street

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Notes

1. *Holmes Group, Inc. v. Vornado Air Circulation Sys., Inc.*, 535 U.S. 826 (2002).
2. *Id.* at 830.
3. *KSR Int'l Co. v. Teleflex Inc.*, 127 S. Ct. 1727 (2007).
4. *Id.* at 1739 – 43 (2007).
5. *MedImmune, Inc. v. Genentech, Inc.*, 127 S. Ct. 764, 777 (2007).
6. *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969).
7. *Id.* at 670.
8. *ebay Inc. v. MercExchange, LLC*, 126 S. Ct. 1837 (2006).
9. *Id.* at 1842 (Kennedy, Stevens, Souter, and Breyer, JJ., concurring).
10. *Lab. Corp. of America Holdings v. Metabolite Labs., Inc.*, 126 S. Ct. 2921, 2922 (2006) (Breyer, Stevens, and Souter, JJ., dissenting from cert. dismissal).
11. *Microsoft Corp. v. AT & T Corp.*, 127 S. Ct. 1746 (2007).
12. 35 U.S.C. § 271(f)(1) (2000).
13. *Microsoft*, 127 S. Ct. at 1755.
14. *Id.*
15. *KSR*, 127 S. Ct. at 1746.
16. *DyStar Textilfarben GmbH & Co. Deutschland KG v. C.H. Patrick Co.*, 464 F.3d 1356, 1367 (Fed. Cir. 2006) (original emphasis).