

Supreme Court Chooses the Middle Ground In the *eBay* Case

By Alexander Poltorak

The landmark decision of the Supreme Court in *MercExchange LLC v. eBay*, 547 U.S. __ (2006), has left many inventors and patent owners disappointed, as the Supreme Court sided with eBay and set aside the prior decision of the Court of Appeals for the Federal Circuit (“CAFC”). A closer reading of the decision, however, seems to indicate a balanced approach that gave both sides something to brag about.

A jury in the Eastern District of Virginia found that MercExchange’s patent for an electronic exchange was valid, and that online auctioneer eBay and its affiliate Half.com had willfully infringed it though eBay’s fixed-price “Buy-it-Now” feature. They awarded MercExchange damages in the amount of \$35 million. Following the jury verdict, the judge denied MercExchange’s motion for a permanent injunction. The CAFC reversed that ruling, applying its “general rule that courts will issue permanent injunctions against patent infringement absent exceptional circumstances.” The Supreme Court remanded the case to the District Court, stating that the District Court and the CAFC both erred by departing from the four-factor test in opposite directions.

FOUR-FACTOR EQUITABLE TEST APPLIES TO PATENT CASES

The courts have long applied the following four-factor test to the question of equitable injunctive relief:

- 1) irreparable injury;
- 2) whether remedies such as monetary damages are adequate;
- 3) the balance of hardships between the patent owner and infringer; and
- 4) whether a permanent injunction would disserve the public interest.

District courts have discretion in granting or denying injunctive relief. Any abuse of such equitable discretion may be appealed to and reviewed by an appellate court. The Supreme Court held that these well-established principles apply equally to patent cases. The Supreme Court cited its earlier decision in *Weinberger v. Romero-Barcelo*, 456 U.S. 305 (1982), in which it held that, “a major departure from the long tradition of equity practice should not be lightly implied.” The justices found nothing in the Patent Act that

continued on page 6

In This Issue

Supreme Court Chooses Middle Ground in <i>eBay</i>	1
Patent Process Inventions	1
Are Patent Cases Too Complex?	3
Retroactive Licenses and Claim Settlements	5

warranted such a departure. To the contrary, the published unanimous opinion written by Justice Clarence Thomas cites that the Patent Act “expressly provides that injunctions ‘may’ issue ‘in accordance with the principles of equity.’ 35 U.S.C. §283.”

PROPERTY RIGHTS OF PATENTS ARE ‘SUBJECT TO’ THE REST OF THE STATUTE

The Supreme Court’s decision addressed the question of property rights of a patent. The Court recognized that “the Patent Act declares that ‘patents shall have the attributes of personal property,’ §261, including ‘the right to exclude others from making, using, offering for sale, or selling the invention,’ §154(a)(1).” The Supreme Court disagreed with the CAFC, however, that “this statutory right to exclude alone justifies its general rule in favor of permanent injunctive relief.” The Supreme Court observed that “the creation of a right is distinct from the provision of remedies for violations of that right.” Justice Thomas observed that, “The Patent Act itself indicates that patents shall have the attributes of personal property ‘[s]ubject to the provisions of this title,’ 35 U.S.C. §261, including, presumably, the provision that injunctive relief ‘may’ issue only ‘in accordance with the principles of equity,’ §283.” Thus, relying on the language of the Patent Act, the Supreme Court made a distinction between the right to exclude (the property right) and a permanent injunction as the remedy for its violation. Although patents do have the attributes of personal property, that does not trump the four-factor test.

SIMILARITY WITH COPYRIGHT LAW

The Supreme Court drew a parallel with copyright law where a similar situation occurs. A copyright owner, just like a patent owner, has the right to exclude. The Copyright Act, just like the Patent Act, states “that courts ‘may’ grant injunctive relief ‘on such terms as

it may deem reasonable to prevent or restrain infringement of a copyright.’ 17 U.S.C. §502(a).” Over the years, there came before the Supreme Court a number of cases in which an “invitation” had been made to “to replace traditional equitable considerations with a rule that an injunction automatically follows a determination that a copyright has been infringed.” The Supreme Court has steadfastly rejected these “invitations.” The *eBay* decision is consistent in this position, which is not surprising given the shared origin of patent and copyright statutes in the U.S. Constitution.

THE DECISION

In its decision, the Supreme Court scolded both the District Court and the Court of Appeals for taking extreme positions and erring in opposite directions.

Although the District Court applied the four-factor test, its holding would have excluded from the injunctive relief remedy “a broad swath of cases.” In a victory for independent inventors, universities, and patent holding companies, the Supreme Court rejected the District Court’s conclusion that “a ‘plaintiff’s willingness to license its patents’ and ‘its lack of commercial activity in practicing the patents’ would be sufficient to establish that the patent holder would not suffer irreparable harm if an injunction did not issue.”

Justice Thomas wrote for the unanimous Court: “some patent holders, such as university researchers or self-made inventors, might reasonably prefer to license their patents, rather than undertake efforts to secure the financing necessary to bring their works to market themselves. Such patent holders may be able to satisfy the traditional four-factor test, and we see no basis for categorically denying them the opportunity to do so.” The Court cited its earlier opinion in *Continental Paper Bag Co. v. Eastern Paper Bag Co.*, 210 U.S. 405 (1908), “which rejected the contention that a court of equity has no jurisdiction to grant injunctive relief to a patent holder who has unreasonably declined to use the patent.”

In the opinion of the Supreme Court, the Court of Appeals went to the other extreme when it enunciated a general rule “that a permanent injunction will

issue once infringement and validity have been adjudged.”

According to the Supreme Court, the CAFC did not properly apply the four-factor equity test in this case, and therefore it vacated the CAFC’s decision and remanded the case to the District Court for fact-finding to determine if the plaintiff satisfied the four-factor test.

The Supreme Court did not take a position on whether or not permanent injunction is warranted in the *eBay* case or any other specific patent case. It only concluded 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.”

CONCURRING OPINIONS

The Concurring Opinions filed by Justices John G. Roberts and Anthony Kennedy shed some light on the dispute between these two camps, which perhaps explains why the published decision and the unanimous opinion is so short and matter-of-fact — this is all the justices could agree on.

Chief Justice Roberts, joined by Justices Antonin Scalia and Ruth Bader Ginsburg, wrote a concurring opinion in which he defends the long tradition of granting injunctive relief upon a finding of infringement. He wrote, “From at least the early 19th century, courts have granted injunctive relief upon a finding of infringement in the vast majority of patent cases.” He further noted that, “This ‘long tradition of equity practice’ is not surprising, given the difficulty of protecting a right to exclude through monetary remedies that allow an infringer to use an invention against the patentee’s wishes — a difficulty that often implicates the first two factors of the traditional four-factor test.” In support of the import of consistency and seeing cases in a historical context, Justice Roberts invokes “the basic principle of justice that like cases should be decided alike.” Seemingly urging judges to apply the four-factor test in this historical context, he quoted Justice J. Holmes who wrote, “a page of history is worth a volume of logic.”

continued on page 7

Justice Kennedy, joined by Justices John Paul Stevens, David Souter and Stephen Breyer, took issue with Justice Roberts' reverence to history. They took the position that the world has changed and the courts need to proactively adapt to the changing legal and economic realities of the present day. They took a stab at "patent trolls" noting the emergence of a new industry "in which firms use patents not as a basis for producing and selling goods but, instead, primarily for obtaining licensing fees." Citing the FTC report on patents and competition, Justice Kennedy writes in his concurring opinion that, "For these firms, an injunction, and the potentially serious sanctions arising from its violation, can be employed as a bargaining tool to charge exorbitant fees to companies that seek to buy licenses to practice the patent."

In the opinion of Justice Kennedy, "When the patented invention is but a small component of the product the companies seek to produce and the threat of an injunction is employed simply for undue leverage in negotiations, legal damages may well be sufficient to compensate for the infringement and an injunction may not serve the public interest."

He also took issue with business method patents: "In addition, injunctive relief may have different consequences for the burgeoning number of patents over business methods, which were not of much economic and legal

significance in earlier times." He concluded that, "The potential vagueness and suspect validity of some of these patents may affect the calculus under the four-factor test."

THE MEANING FOR PATENT OWNERS

This long-anticipated decision will likely have a limited effect on the outcome of patent cases. First, only a very small percentage of patent cases ever reaches trial. Historically, only 3% to 4% of filed cases are tried — most are settled or resolved on motion.

Based on the analogy with the copyright law drawn by the Supreme Court, one can anticipate that, like copyright cases, most patent cases will result in a permanent injunction, once infringement is established.

On the other hand, the law may develop in a different direction if some judges take to heart the dicta in the concurring opinion of Justice Kennedy and deny injunction to non-practicing entities, to owners of business method patents, and in those cases where the patented invention is but a small component of a larger system.

However, even if an injunction is not granted, in the absence of a compulsory license, the prevailing patent owner can file a subsequent case in which the issues of validity and infringement will be likely *res judicata*. Such a case will likely proceed quickly to a hearing in damages and a finding of willful infringement. Furthermore, since a reasonable royalty is determined based on hypo-

thetical negotiations between the patent owner and the infringer as of the date of commencement of the infringement, this date in the subsequent trial arguably shifts to the date of the first act of infringement after the previous trial. The patent owner, having established the value of the patented technology, patent validity, and the fact of infringement in the first trial, can be reasonably expected in hypothetical negotiations to demand significantly higher royalty rate than before resulting in a finding of a higher reasonable royalty under *Georgia Pacific*. This may compel an infringer to negotiate a license rather than wait to be sued again and possibly face higher royalty rates and treble damages.

Although most non-practicing patent owners, such as patent holding companies, independent inventors, and universities, do not wish to enjoin infringers from practicing their invention, which would deny them income from royalty payments if these infringers were to license their patents, the threat of injunction is what often brought the infringers to the negotiating table. Two things can be said with certainty to follow from this Supreme Court decision: It will promote litigiousness as the alleged infringers, emboldened by now less likely prospect of injunction, will become more recalcitrant; and, secondly, it will drive down settlement amounts since the risk factors in the equation have now changed.

