

## Under Threat

Supreme Court should tell judges to balance equities before squashing infringers with injunctions.

BY ANDREW J. PINCUS

**P**atent law is big news today. Before the BlackBerry infringement case was settled this month, millions of Americans trembled on the edge of their seats, fearing the abrupt cutoff of instant communication with friends, colleagues, and clients. Settlement of the action was featured on the television news and the front pages of national newspapers.

This week the Supreme Court is hearing oral argument in *eBay Inc. v. MercExchange L.L.C.*, a case raising the very question that, press reports suggest, played a major role in the final days of the BlackBerry litigation: What standard should trial courts apply in determining whether to grant injunctive relief in patent infringement cases? Are successful plaintiffs automatically entitled to an injunction, regardless of the equities of the case?

BlackBerry's manufacturer, Research in Motion Ltd. (RIM), had lost at trial to NTP Inc. Despite further legal efforts, which even saw the Patent Office raising doubts about the validity of NTP's patents, the district judge appeared to indicate that he would soon grant NTP's motion for a permanent injunction. So RIM settled, for \$612 million.

The online auction house eBay—like RIM, a high-tech success story—was sued for infringement by MercExchange over patents related to fixed-price purchasing. The jury found for MercExchange. But the district judge declined to grant its motion for an injunction after weighing the traditional equitable factors: the risk of irreparable harm, the adequacy of legal remedies, the balance of the parties' relative hardships, and the consequences of injunctive relief for the public interest.

The U.S. Court of Appeals for the Federal Circuit reversed. The court held that a permanent injunction “will issue once infringement and invalidity have been adjudged” except in “rare instances” where such relief would “frustrate an important public need” such as the protection of public health.

Now the Supreme Court must decide whether the Federal Circuit erred in setting forth such a rigid standard.

### A TAX ON INNOVATION

Widespread interest in the BlackBerry and eBay cases reflects a simple fact: Intellectual property-dependent industries contribute a growing portion of our gross domestic product. As companies jockey for a share of this newly created wealth, the number of high-stakes legal disputes rises. Nowhere is this more common than in technology industries, where rapid innovation tests the ability of the Patent Office to keep abreast of developments, to distinguish true innovation from prior art, and to define patents clearly with language that is inherently imprecise.

The result is that more than ever before, patent litigation must separate legitimate claims of infringement from unjustified lawsuits seeking illegitimate recoveries, recoveries that amount to a tax upon innovation.

The rules governing infringement claims are now receiving greater scrutiny. If infringement actions were nearly friction-free—if the litigation process guaranteed accurate outcomes with very low transaction costs—then the practical impact of the rules would be irrelevant. But litigation is not friction-free. The Supreme Court has recognized—in the context of other high-profile private claims, such as securities class actions and private antitrust suits—that the real-world effects upon litigants and potential litigants must be taken into account in fashioning litigation rules.

The debate in the eBay case is therefore occurring on two levels: first, a discussion of the statutory language, precedent, etc.; and second, arguments about the practical impact of the different injunction standards being urged upon the Court. The case has attracted a phalanx of amici, including the solicitor general, technology firms, pharmaceutical companies, universities, bar associations, and law professors.

### GRANT WITH DISCRETION

With respect to the statutory language, the Federal Circuit

was plainly wrong in asserting that a permanent injunction is a foregone conclusion once a judge or jury has found infringement. Section 283 of the Patent Act provides that district courts “may” grant injunctions “in accordance with the principles of equity.”

The governing Supreme Court precedents clearly establish that this discretionary language requires courts to assess the traditional equitable factors. As the solicitor general stated in his amicus brief, Section 283 “directs the district courts, when adjudicating private patent rights, to issue injunctions in accordance with the familiar four-factor test.”

When applying these four factors in determining whether to grant an injunction, the Supreme Court instructed in *Hecht Co. v. Bowles* (1944) that district courts can and should consider all of the facts of each situation “to do equity and to mould each decree to the necessities of the particular case.” The *Hecht* Court said that “flexibility rather than rigidity” distinguishes equity jurisprudence.

Today the technology sector, where not just the eBay and BlackBerry cases but many of the highest-profile infringement actions arise, provides a case study in the types of circumstances that courts should consider before granting an injunction.

#### HIGH-TECH COMPLEXITIES

Technology products typically consist of hundreds or even thousands of patented components. (By contrast, consumer products in the chemical and tool sectors are typically protected by only a handful of patents.) One reason for this phenomenon is the extraordinary complexity of high-tech products. Another is the incremental nature of high-tech innovation. A new version of a software program or a new computer virtually always builds upon pre-existing technology, adding features based on new inventions but incorporating prior technology as well.

Notwithstanding the business’s best efforts, it is often extraordinarily difficult to identify all the existing patents, not to mention the pending patent applications, that may be relevant to each of those hundreds of components that make up a new product. Moreover, infringement claims are easy to assert but difficult to disprove, especially in the context of sophisticated technology. This allows for the assertion of extremely tenuous claims.

If a hardware or software company becomes aware of the possibility of an infringement claim *before* it designs a new product, it can choose to design around the allegedly patented technology or obtain a license to use it. At that point, the cost of a license reflects the relative difficulty of designing around the technology as well as the strength of the potential infringement claim. A strong patent that is difficult to design around can command a relatively high fee, while a weak one that is easy to design around cannot.

The situation becomes dramatically different when, as is too often the case, the patentee raises the possibility of an infringement claim *after* a company has already initiated production or invested substantial time and resources in research and development. Backtracking to design around the now-integrated technology will almost certainly involve substantial expense, waste, and delay. The Federal Trade Commission observed in a major 2003 report on the patent system that “redesigning a product

after significant costs have been sunk is usually not economically viable.”

That is especially true if, as has occurred with increasing frequency, the infringement claim is asserted against an industry standard *after* that standard has been adopted. Consider the case of one small company that recently asserted ownership of patents covering part of XML, a method for storing and sharing electronic information that is a formal specification of the World Wide Web Consortium. Another firm now claims to own a patent covering certain technology underlying JPEG, a standard method of sharing images on the Internet that was developed by the Joint Photographic Experts Committee.

#### UNFAIR LEVERAGE

If the district court won’t take into account facts such as these before granting an injunction, the potential infringement plaintiff gains extraordinary and unfair leverage. When an injunction is always or nearly always available, the potential plaintiff can demand a licensing fee that reflects not just the ordinary market value of the license, but also a company’s sunk costs and the losses that an injunction would inflict. So long as an injunction will issue automatically upon a finding of infringement, this extreme bargaining inequality exists even if the allegedly patented technology is only an insignificant part of the product and the manufacturer could have designed around the technology if it had only known.

The BlackBerry case demonstrates that the risk to a company can be so great that the company has little ability to withstand a plaintiff’s demands. The threat of disruption of the company’s business effectively forces the company to reach an agreement—precisely what press reports indicate happened in the BlackBerry case.

The risk has been exacerbated by the growth of patent “trolls,” which are firms that acquire patents solely to demand royalties and then sue if their demands are not met. To maximize their litigation leverage, these firms virtually always wait to raise claims until after a product is brought to market or an industry standard is adopted—precisely the situation in which the risk of unfairness is greatest. And the cost of abusive claims falls upon all of us: By increasing the burden for innovative companies, patent trolls effectively levy a tax on innovation.

This illegitimate leverage can be reduced significantly if district courts are required to evaluate the specific facts and weigh the particular equities of each case before granting an injunction, even against an adjudged patent infringer.

For example, irreparable harm will be easy to establish when the patentee practices its own patent and competes with the infringing company or has granted an exclusive license to a third party that does so. On the other hand, if the patentee is willing to grant a nonexclusive license to anyone on essentially identical terms, it will have a harder time demonstrating that monetary damages are not an adequate remedy.

In assessing the balance of the hardships, the court also must examine such factors as whether the defendant made significant investments before it learned of the alleged infringement, whether the injunction would require the defendant to redesign its product in a way that would eliminate interoperability, and

whether the injunction will serve merely to increase the patentee's negotiating leverage. With respect to the public interest, the court must examine not just the public's interest in the enforcement of patent rights, but also the potential burdens of an injunction, including the disruption of a technology already in widespread use.

In deciding the eBay case, the Supreme Court should recognize that applying the traditional rule of equity, assessing all relevant facts to reach a just result, is the fairest approach to determining whether an injunction is appropriate in a patent

infringement case. And it is the only approach that will protect legitimate claims while deterring abusive lawsuits that harm our entire economy.

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