



SUPREME COURT EXTENDS EXHAUSTION DOCTRINE	1
PARENT CORPORATION CANNOT RECOVER LOST PROFITS OF SUBSIDIARY	4
PARTY SEEKING THE BENEFIT OF PRIORITY BEARS THE BURDEN OF PROOF	6
FEDERAL CIRCUIT DEFINES LOCAL STORAGE	7
FEDERAL CIRCUIT DEFINES PARTIALLY HIDDEN TO NOT INCLUDE COMPLETELY HIDDEN	8
FEDERAL CIRCUIT FINDS INEQUITABLE CONDUCT FOR MISLEADING DECLARATION FACTS	9
DC CIRCUIT FINDS FAILURE TO DISCLOSE PATENTS TO STANDARD SETTING ORGANIZATION DID NOT PRESENT AN ANTITRUST INJURY	12
11TH CIRCUIT FINDS USE OF TRADEMARKS IN METATAGS IS AN INFRINGING USE IN COMMERCE	13
SPECIAL OFFER ON INTELLECTUAL PROPERTY AND GOVERNMENT CONTRACTS TREATISE	16
USPTO PROPOSES NEW FEES FOR 2009	17
STEIN MCEWEN & BUI IS PLEASED TO WELCOME NEW ATTORNEY	17
FEATURE COMMENT:	18

SUPREME COURT EXTENDS EXHAUSTION DOCTRINE

SUPREME COURT FINDS SALE OF DEVICE EXTENDS PATENT EXHAUSTION TO UNLICENSED METHOD CLAIMS

In *Quanta Computer, Inc. v. LG Electronics, Inc.*, 553 U.S. ___; 86 USPQ2d 1673 (June 9, 2008), the Supreme Court held that the doctrine of patent exhaustion applies to unlicensed patented methods used by a sold patented device and that LG's sale of such devices to Intel, who then sold such devices to Quanta, exhausted LG's patent rights against downstream purchasers. The unanimous decision, authored by Justice Thomas, overruled the decision by the Federal Circuit which had held that method patents were not within the scope of the patent exhaustion doctrine.

BACKGROUND

LG possessed three patents addressing optimization of memory access by a computer processor (the "LG Patents"). The patents included system claims to a system for ensuring retrieval of current data, a system for the ordering of read and write requests, and a system for managing data traffic on wires connecting computer components (known as a "bus"), and also contained methods claims for the use of the system. LG entered into a licensing agreement with Intel, authorizing them to practice the system claims (the "License Agreement"). However, LG stipulated that Intel give notice to its customers that the license did not extend to products made by combining an Intel chip with a non-Intel product, but did not otherwise limit the downstream sale of the Intel chips. This stipulation was contained in a separate agreement from the licensing agreement, the "Master Agreement," and explicitly

stated that a breach would not affect the License Agreement.

Quanta Computer purchased processor chips from Intel and built computer systems incorporating the chips. Intel provided Quanta with the required notice and Quanta proceeded to construct computer systems combining the Intel chips with non-Intel components (such as memory, hardware busses, etc). LG then sued Quanta, alleging infringement of the LG Patents.

The District Court initially ruled in favor of Quanta, granting summary judgment because the doctrine of patent exhaustion prevented LG from asserting its rights to the patents against Quanta. On reconsideration, the District Court denied summary judgment for Quanta because the LG Patents contained method claims not covered by the licensed system claims. The Federal Circuit affirmed-in-part and reversed-in-part, agreeing with the District Court that the doctrine of patent exhaustion does not apply to method patents (patents claiming how to make or use a product, as opposed to the product itself). The Federal Circuit also noted that LG did not license Intel to sell the product for the purposes of combination with non-Intel products such that there was no authorized sale.

QUESTION OF CERTIORARI

Quanta filed a petition for certiorari, which was granted, on the following question:

Whether the Federal Circuit erred by holding, in conflict with the decisions of this Court and other courts of appeals, that respondent's patent rights were not exhausted by its license agreement with Intel Corporation, and Intel's subsequent sale of product under the license to petitioners.

THE DOCTRINE OF PATENT EXHAUSTION

The Supreme Court reviewed the longstanding doctrine of patent exhaustion, which provides that the initial authorized sale of a patented item terminates all patent rights to that item. *Id* at 5; see *Bloomer v. McQuewan*, 14 How. 539 (U.S. 1853). “Where a person has purchased a patented machine of the patentee or his assignee, this purchase carries with it the right to the use of that machine so long as it is capable of use.” *Adams v. Burke*, 17 Wall. 453 (U.S. 1873). The Court further reviewed their last decision on the doctrine of patent exhaustion was in *United States v. Univis Lens Co.* 316 U.S. 241 (1942). In that case, Univis possessed a patent for a special type of lenses. Univis sold lens blanks to wholesalers, which the wholesalers would then sell to finishing retailers. The finishing retailers would then grind down the blanks to produce a patented lens. Univis attempted to collect further patent royalties from these finishing retailers. The Supreme Court held that the sale of the lens blanks exhausted the patents on the finished lenses. As summarized by the Court, *Univis* stands for the proposition that “the traditional bar on patent restrictions following the sale of an item applies when the item sufficiently embodies the patent—even if it does not completely practice the patent—such that its only and intended use is to be finished under the terms of the patent.” *Quanta* at 8.

PATENT EXHAUSTION AND METHOD CLAIMS

LG argued, and the District Court and Federal Circuits held, that the doctrine of patent exhaustion does not apply to method claims. The Supreme Court disagreed for reasons based upon precedent and pointed out the disastrous effects of such an exclusion.

Quanta argued that both the Supreme Court and the Federal Circuit had applied exhaustion to method claims in the past. The Supreme Court recognized that it has “repeatedly held that method patents were exhausted by the sale of an item that embodied the method.” *Id* at 9. For example, the Court noted that, in *Ethyl Gasoline Corp. v. United States*, the Court had held that the sale of a motor fuel produced under one patent also exhausted the patent for a method of using the fuel in combustion motors. 309 U.S. 436, 446, 457 (1940); *Quanta* at 9.

Going further, the Court stated that excluding method claims from the doctrine of patent exhaustion would seriously undermine the doctrine. If such an exclusion were allowed, patentees seeking to avoid exhaustion would seek to claim a method instead of an apparatus. Converting an apparatus claim into a method claim is relatively simple, so the effect of such an exclusion would effectively neutralize the doctrine. The Court

further did not see a significant difference between method and apparatus claims that would require an exclusion, and refused to categorically exclude method claims from the doctrine of patent exhaustion when there is a sale of a device covered by corresponding apparatus claims.

TRIGGERING EXHAUSTION

Having determined that exhaustion applies to method claims, the Court turned to discussing the extent to which a product must embody a patent in order to trigger exhaustion. Quanta argued that the Court should apply *Univis*, as the Intel chips here played an analogous role to the lens blanks in that case. LG sought to distinguish *Univis* on three grounds: *Univis* should be limited to physical aspects, the lens blanks and final lenses in *Univis* were covered by the same patent whereas the Intel chips and systems incorporating the chips were covered by different patents, and that *Univis* shouldn’t apply as the components here represented parts off a combination patent.

The Court agreed with Quanta, and applied *Univis* to the facts of the case. Like the lens blanks in *Univis*, the only reasonable and intended use of the Intel chips was to practice the LG Patents and the chips sufficiently embodied essential features of the patented invention. *Id* at 12. *Univis* held that “the authorized sale of an article which is capable of use only in practicing the patent is a relinquishment of the patent monopoly with respect to the article sold.” *Univis* at 249. The Court held that an incomplete article substantially embodies a patent if the only remaining step necessary to fully practice the patent is the application of common processes or the addition of standard parts. *Quanta* at 14. Everything ‘inventive’ about the patent is included in the Intel chips; all that remained for Quanta to do was put it to use by attaching the chips to the standard system components it was designed to use.

Intel’s chip practiced the LG Patents, like the lens blanks in *Univis*. Quanta simply finished the product by attaching the required components to it, like the finishing retailers polishing the lens.

The Court rejected LG’s attempts to distinguish *Univis*. With regards to limiting the holding to physical changes, the Court held that the important component is the nature of the final step, not whether it consists of adding or deleting material. When the final step to completely practice the patent is common and non-inventive (i.e. grinding the lens or attaching standard components to the processor chip), the incomplete article substantially embodies the patent.

As for LG's argument that multiple patents covered different elements of the system, the Court agreed with the general principle that practicing one patent should not exhaust another patent. However, as the Court concluded, the Intel chip substantially embodied the patent LG sought to assert against Quanta and exhausted LG's rights through the authorized sale of the chip. While Intel's chip practiced many other patents fully, there is no reason why it could not also practice (substantially embody) the LG patent in question. The Court dismissed LG's combination patent argument as it did not see the combination of components to be the inventive step here.

EXHAUSTION THROUGH AUTHORIZED SALE

The Court noted that a patentee's rights are exhausted against a buyer when the patentee sells a patented product to him. Further, a patentee's rights are exhausted against parties who later buy the product from that buyer, provided the patentee authorized the buyer to sell the product. Here, the Court found that LG authorized Intel to sell chips practicing LG's patents. Even though LG required Intel to provide a notice that no license would extend to parties combining the Intel chip with non-Intel parts, Intel was otherwise unconditionally authorized to sell the chips. There was no breach by Intel as Intel did provide the required notice to LG, thus the sale was authorized per the contract.

LG asserted that Quanta possessed no license to practice its patents, but Quanta argued exhaustion of the patents by sale, not that it was licensed to practice the patent. The existence of exhaustion turns solely on Intel's right to sell the patented invention, and the license agreement between Intel and LG makes it clear that Intel's sale was authorized. Because the Court found that it is the incomplete article (the Intel chips) that practices the patent, and not the final product (Quanta's computer system), the Court found LG's claims barred by exhaustion. Intel practiced the patent, not Quanta. Quanta's combination of the Intel chip was simply standard finishing which did not amount to "making" a patented article.

POTENTIAL LICENSING EXCEPTION

While finding the LG patents were exhausted through Intel's authorized sale, the Court specifically noted that its opinion is directed at patent law. "The authorized sale of an article that substantially embodies a patent exhausts the patent holder's rights and prevents the patent holder from invoking *patent law* to control post-

sale use of the article." *Id* at 19 (emphasis added). The Court also noted that LG is only barred from seeking damages under patent law, but declined to extend their decision to the contractual consequences. *Id* at 18 n. 7. The Court's dicta seemed to suggest that a patentee's restitution in similar situations to this lies in the terms of the licensing contracts, with damages being limited to contractual damages.

CONCLUSION

Intel's chips "substantially embodied" the LG patents because they had no non-infringing use and included all the inventive aspects of the patents. *Id* at 19. Intel's authorized sale to Quanta took its products outside the scope of the patent monopoly, barring LG from asserting its patent rights against Quanta through the doctrine of patent exhaustion. *Id*. The chips made by Intel were analogous to *Univis'* lens blanks, the sale of which was authorized by LG. LG's rights against finishers of Intel's products are exhausted by the doctrine of patent exhaustion under *Univis*.

SIGNIFICANCE FOR PATENT OWNERS

Quanta represents a significant limitation to the exhaustion doctrine as it removes one possible set of remedies (i.e., those based upon patent infringement) for unlicensed use of a patented product. Through *Quanta*, the Court clarifies that the sale of a product will remove any patent-based infringement theory to the extent that the patent has no other purpose but to be incorporated into the product or a non-inventive use of the product in a particular system. While seemingly beneficial to end users, the Court does make clear that not all remedies are removed. Instead, the Court specifically notes that breach of contract remedies should be available. Thus, while treble damages may not be available due to patent exhaustion, specific performance, damages and other breach of contract claims would survive. Moreover, given the Court's emphasis on the fact that the License Agreement did not prohibit the sale of the chips where the customer combined the chips with non-approved products and only required a notice to be provided with the chips, it would be expected that licensors may attempt to cure this deficiency to ensure that the contract does not extend to such situations (thereby emphasizing the unauthorized nature of the initial sale). As such, it would be expected that patent owners will increasingly look to licensing restrictions to govern end user use of patented items, and will be less reliant on merely selectively licensing patents.

PARENT CORPORATION CANNOT RECOVER LOST PROFITS OF SUBSIDIARY WHEN SUBSIDIARY IS NON-EXCLUSIVE LICENSEE OF PARENT'S PATENT

In *Mars, Inc v. Coin Acceptors, Inc.*, Nos. 07-1409, -1436 (Fed. Cir. June 2, 2008), Mars, Inc., a U.S. based candy company producing popular treats such as M&Ms and Milky Way bars, developed and obtained patents on a technique for identifying coins deposited in a vending machine. Mars does not produce any vending machines itself but created a wholly-owned subsidiary, Mars Electronics International (MEI), to produce the machines. Mars licensed MEI to use its patents in the design of its vending machines.

Mars maintained consolidated financial statements reflecting the incomes of all its subsidiaries. However, Mars licensed MEI to use its patents on a royalty basis per gross sales. Thus Mars would receive revenue regardless of whether MEI turned a profit or not. As will be described below, the Federal Circuit found this fact particularly compelling in finding that there was not a significantly direct flow of profits from MEI to Mars.

A competing vending machine manufacturer, Coin Acceptors, Inc. ("Coinco"), began producing vending machines which infringed Mars' patents. Mars sued Coinco for this infringement in 1990. The District Court, after consolidating, found that Coinco infringed both of Mars' patents and entered final judgment on liability in 2005. Coinco appealed and the Federal Circuit affirmed the liability holding. The District Court then began to calculate damages.

Calculation of damages was shaped by several factors. First, one of the two patents expired in 1992. Second, Coinco introduced a non-infringing alternative in 1994, so the parties agreed that lost profits did not apply after 1994. Third, in 1996 Mars transferred its entire interest in the patents to MEI. Fourth, the second patent expired in 2003.

Mars sought lost profits for sales prior to 1994, or at a minimum a reasonable royalty on such sales. Mars further sought a reasonable royalty on sales after 1994 until 2003. Coinco acknowledged that Mars was entitled to a reasonable royalty prior to 1994, but disputed Mars' other claims.

The District Court ruled that Mars could not recover on a lost profits theory as Mars itself did not lose any sales and there was no evidence that MEI's profits flowed inexorably to Mars. Mars sought to add MEI as a co-plaintiff, but the court denied this motion because MEI

lacked standing to seek damages, at least prior to the 1996 transfer. On a motion for reconsideration, the District Court found that Mars lacked standing to pursue the claims from 1996 onward, after it transferred its interests to MEI. The District Court allowed MEI to immediately transfer the interests back to Mars in order to re-establish standing under *Schreiber Foods, Inc. v. Beatrice Cheese, Inc.*, 402 F.3d 1198 (Fed. Cir. 2005). Mars accomplished this through a document asserting that MEI transferred the rights to litigation of the patents back to Mars.

After a four day bench trial, the District Court found that a 7% royalty was reasonable and found \$14,376,062 in damages.

Four issues were addressed by the Federal Circuit on appeal: (1) whether Mars was entitled to lost profits; (2) whether MEI lacked standing prior to 1996; (3) whether Mars had standing to seek damages after 1996; and (4) whether the 7% royalty was reasonable.

LOST PROFITS

The Federal Circuit began its consideration by recognizing that patent infringement is a tort, and that the purpose of damages is to restore the victim to the position he would be in had the tort not occurred. *Brooktree Corp. v. Advanced Micro Devices, Inc.*, 977 F.2d 1555, 1579 (Fed. Cir. 1992); *see also Aro Mfg. Co. v. Convertible Top Replacement Co.*, 377 U.S. 476, 507 (1964) ("had the infringer not infringed, what would the [Patentee] have made?"). There was no dispute that Coinco's actions harmed Mars; the dispute was over whether Mars could recover under lost profits.

After a lengthy discussion of compensation theories, the Court addressed whether or not Mars could claim MEI's lost profits. Mars argued that, due to MEI being a wholly owned subsidiary and the consolidated financial statements, the profits of MEI flowed inexorably to Mars. The Federal Circuit did not agree. Uncontradicted testimony in the record showed that Mars and MEI had a traditional royalty-bearing license agreement. Such royalty payments were the only payments on record which Mars received from MEI. The court saw no evidence that the profits of MEI flowed inexorably to Mars. *Mars* at 11. As such, the Court determined that the harm suffered by Mars was lost royalty payments, for which the appropriate recompense is a reasonable royalty by the infringer.

The court affirmed the District Court's holding on this point.

The Court declined the opportunity to address whether or not a parent company can recover lost profits of a subsidiary when the profits do flow inexorably from the subsidiary to the parent as that is not the case here. *Id.* at 12.

1. MEI'S STANDING PRIOR TO 1996

In order to seek lost profits, Mars attempted to add MEI as a co-plaintiff. The District Court denied this motion, as MEI lacked standing. The Federal Circuit affirmed.

Only a patent owner or an exclusive licensee can have constitutional standing to bring an infringement suit; a non-exclusive licensee does not. *Sicom Sys., Ltd. v. Agilent Techs., Inc.*, 427 F.3d 971, 976 (Fed. Cir. 2005). MEI did not possess standing to sue prior to 1996 because it was neither owned the patents in question nor was it the exclusive licensee. Mars had licensed another of its subsidiaries, MEI-UK, to practice the patent in the U.S., making MEI a non-exclusive licensee.

Thus the court determined that the District Court had correctly denied Mars' motion to add MEI as a co-plaintiff for damages occurring prior to the 1996 transfer.

2. MARS' STANDING AFTER 1996

When Mars transferred its interests in the patents to MEI in 1996, it lost standing to seek infringement. Under *Schreiber*, Mars could correct this jurisdictional defect by reacquiring the title to the patent. *See Schreiber*, 402 F.3d at 1204 ("Here *Schreiber* reacquired its stake in the litigation by reacquiring the '860 patent (and causes of action thereunder) before the entry of judgment. The jurisdictional defect that had existed was cured before the entry of judgment and thus the judgment was not void" (emphasis added)). Therefore, the Federal Circuit turned to analyzing whether the 1996 agreement transferred title to MEI and if the agreement in 2006 transferred it back.

The 1996 transaction by its terms transferred Mars' "entire interest" in the patents to MEI. The Federal Circuit recognized that it is well known that a transfer of one's entire interest equates to a full assignment of the patent and a transfer of title. *Mars* at 17. As a result, the court found that Mars lacked standing as of 1996, confirming the District Court's finding.

Turning to the 2006 retransfer from MEI to Mars, the court relied upon the plain and common meaning of the words in the contract. Under New York corporate law, which governed that contract, words are given their plain meaning and a dictionary is often used to

determine such meaning. After defining the terms used in the document, the court determines that the document assigns the right to sue for past infringement to Mars, but not title. *Id.* at 19. The court saw no provision in the contract which purports to transfer full title back to Mars.

Mars argued that, as the patent had expired, the only remaining right associated with the patent was the right to sue for past damages. As such, they argued, transfer of that right should amount to a transfer of title. The court rejected this argument, stating that the title to an expired patent contains more than the right to sue. *Id.* at 20. Seeing nothing in the contract which would transfer full title to Mars, the Federal Circuit held that Mars failed to satisfy *Schreiber* and lacked standing from 1996 through 2003.

REASONABLE ROYALTY

Coinco argued that the District Court erred in setting the royalty rate. One of its arguments was that the royalty which the court settled upon was higher than the cost of developing non-infringing alternatives. Specifically, Coinco claimed that no rational entity would infringe if the cost exceeded the cost of developing an alternative. The court rejected this argument as a matter of law. *Id.* at 22; *see also Monsanto Co. v. Ralph*, 382 F.3d 1374, 1383 (Fed. Cir. 2004). In a related argument, Coinco argued that a reasonable royalty can never result in the infringer operating at a loss. This argument was also dismissed as a matter of law. *Id.* at 24; *see Monsanto*.

CONCLUSION

The Federal Circuit affirmed the District Court's holding that Mars could not recover MEI's lost profits, as the profits did not flow inexorably to Mars and the financial relationship between Mars and MEI was a traditional royalty-based license relationship. The District Court's denial of Mars' motion to add MEI as a co-plaintiff was also affirmed because MEI lacked standing, as they were neither the owner of the patent nor the exclusive licensee. The Federal Circuit reversed the decision of the District Court and held that Mars lacked standing from 1996 to 2003 and was not entitled to recover damages from that time period. The Court affirmed the royalty set by the District Court and remanded the case for a recalculation of damages.

SIGNIFICANCE TO PATENT OWNERS

Mars continues the Federal Circuit's view that lost profits damages should rarely be granted, and further shows the limitations of attempting to obtain lost profits damages where a subsidiary is the entity actually losing

the sales, but the parent is enforcing the patent. As such, while it is often convenient to hold intellectual property at a parent corporation level, such convenience can come at the price of limiting damages

which could possibly be obtained if the damaged subsidiary actually owns the intellectual property and is allowed to assert damages for infringement.

FEDERAL CIRCUIT AFFIRMS THAT THE PARTY SEEKING THE BENEFIT OF PRIORITY BEARS THE BURDEN OF PROOF THAT CLAIMS ARE ENTITLED TO PRIORITY

In *PowerOasis, Inc. v. T-Mobile USA, Inc.*, 522 F.3d 1299; 86 U.S.P.Q.2D 1385 (Fed. Cir. 2008) (non-precedential), PowerOasis possessed two patents with the purpose of providing a “vending machine” that enables a customer to connect a laptop to a communications channel. *Id.* at 2. PowerOasis brought suit in the District Court for the District of New Hampshire alleging that T-Mobile’s internet “Hot-Spot” system infringed its patent.

PowerOasis’ original application in 1997 described a “vending machine” which would allow a consumer to connect his laptop to a telecommunications network. The figures and descriptions in the original application make it very clear that the “vending machine” was to be some component external to the consumer’s laptop. The continuation-in-part (CIP) filed in 2000 removed this external restriction, introducing examples which included an interface on the consumer’s laptop, and led to the issuance of U.S. Patents Nos. 6,466,658 and 6,721,400. PowerOasis alleged infringement of the ‘658 and ‘400 patents by T-Mobile. T-Mobile introduced prior art which had been carried out for more than a year prior to the filing of the CIP in 2000. PowerOasis claimed that the prior art was no bar, as the CIP should have the benefit of the date of the filing of the original application in 1997 and the prior art had not been carried out for a year prior to that date.

In deciding this case, the Federal Circuit addressed which party bears the burden of proof for establishing the effective filing date of claims in a continuation-in-part. If the claims in the CIP are fully described in an earlier filing, they are eligible to benefit from the date of the earlier filing. As such, the outcome of the case revolved around the effective filing date of the CIP filed by PowerOasis which matured into the two patents at issue. T-Mobile identified prior art that would invalidate the patents (under 35 U.S.C. § 102(b)) if the CIP retained its own filing date (June 15, 2000). However, PowerOasis argued that the CIP should be presumed to have the filing date of the original application (February 6, 1997) for purposes of priority in date, thereby requiring T-mobile to provide evidence of

a lack of written description in the original application. The District Court held that the CIP was not entitled to the benefit of the earlier filing date because the original application did not provide a written description of the invention claimed in the CIP as required by 35 U.S.C. § 112. As such, the District Court held that the PowerOasis patents were invalidated by the prior art presented by T-Mobile. The Federal Circuit affirmed this holding.

The Federal Circuit began its analysis by recognizing the well established fact that a patent is presumed valid and that a party wishing to assert otherwise bears the burden of persuasion. *See Ralston Purina Co. v. Farm-Mar-Co, Inc.* 772 F.2d 1570 (Fed. Cir. 1985). Moreover, there is a heightened presumption where the attack on validity is an issue already resolved during prosecution as there is a presumption that the issue was correctly resolved during the examination process. As such, in *Ralston Purina*, there was a presumption that the claims were entitled to a parent application priority date as the examiner and the Board of Patent Appeals and Interferences had addressed the issue specifically relative to considered prior art.

PowerOasis argued that this presumption of validity should extend to issues of priority in time in other circumstances, but the Federal Circuit rejected this argument. Specifically, the Federal Circuit noted that the rationale behind the presumption of validity does not extend to issues of timing in the case of CIPs because patent examiners do not generally consider the timing issues of CIPs unless the issue is raised in regards to specific prior art references. Timing issues related to CIPs only arise during litigation, and it is not part of the United States Patent and Trademark Office’s standard procedure to make unnecessary priority determinations. Without a presumption of priority in time, the Federal Circuit held that the party relying upon validity bears the burden of showing that the CIP should date back to the earlier filing.

The party asserting invalidity still must show by clear and convincing evidence that the patent is invalid, but, once a prima facie case is made, the party relying on validity must present evidence to the contrary. T-Mobile met its burden here by presenting 35 U.S.C. §102(b) prior art which would invalidate the patent if the CIP had an effective date of 2000. Once T-Mobile satisfied its burden by establishing a prima facie case, the burden shifted to PowerOasis to show that the CIP benefitted from the date of the earlier filing.

After discussing the burden of proof, the court moved on to the standard for determining whether the CIP benefitted from the filing date of an earlier filed application. “It is elementary patent law that a patent application is entitled to the benefit of the filing date of an earlier filed application only if the disclosure of the earlier application provides support for the claims of the later application, as required by 35 U.S.C. § 112.” (quoting *In re Chu*, 66 F.3d 292, 297 (Fed. Cir. 1995)). To satisfy this requirement, the written description of the earlier filing must make it clear to those skilled in

that art that the inventor possessed the invention claimed in the later filing at the time of the earlier filing. This requirement is not fulfilled by inventions which may be obvious over what is disclosed; only by what is expressly disclosed.

The Federal Circuit agreed with the District Court that the CIP filed by PowerOasis failed to meet this standard. The original application (filed in 1997) did not support the terms included in the CIP (filed in 2000). The modifications in the CIP substantially changed the content of the original application, expanding it from a “unitary vending machine” to a number of different platforms, including a customer laptop. As the CIP was not fully supported by the written description in the original filing, the CIP was not entitled to benefit from the filing date of the original application. The District Court held, and the Federal Circuit affirmed, that the relevant claims in patents ‘658 and ‘400 were invalid due to the 35 U.S.C. §102(b) prior art presented by T-Mobile.

FEDERAL CIRCUIT DEFINES LOCAL STORAGE IN THE CONTEXT OF NETWORKS TO BE LIMITED TO STORAGE AT A COMPUTER

In *Mangosoft, Inc. v. Oracle Corp.*, 525 F.3d 1327; 86 USPQ2d 1939 (Fed. Cir. May 14, 2008), Mangosoft, Inc. and Mangosoft Corporation (collectively, “Mangosoft”) appeal from the District Court’s summary judgment order holding that Oracle Corporation (“Oracle”) did not infringe Mangosoft’s U.S. Patent No. 6,148,377 (“the ‘377 patent”). The Federal Court affirmed this holding.

The ‘377 patent relates to “computer networking systems and methods that provide shared memory systems and services,” ‘377 patent col.1 ll.4-6. It creates a decentralized storage system that pools together and shares the storage capacities of individual computers (or nodes) on the network to form a “virtual memory space.” See *id.* col.2 ll.21-28. In 2002, Mangosoft filed suit against Oracle, accusing Oracle’s Real Applications Clusters (“RAC”) software of infringing upon some 38 claims of the ‘377 patent and a related patent.

Upon a Markman hearing in 2004, the District Court distinguished “local” memory devices from “shared,” “networked,” or “remote” memory devices, and rejected Mangosoft’s request to construe “local” to “simply requir[e] a computer memory device that is somehow ‘linked’ to a computer (whether directly or indirectly).” *Mangosoft, Inc. v. Oracle Corp.*, No. 02-CV-

545, slip op. at 18-20 (D.N.H. Sept. 21, 2004). Based on this order, Mangosoft amended its list of asserted claims to include only three claims on the ‘377 patent. The District Court concluded that, as a matter of law, Oracle did not infringe any of the asserted claims, and in so holding, the District Court agreed with Oracle that “the memory space shared in RAC clusters does not span local persistent memory devices.” Summary Judgment Opinion at 8, 14-15.

The issue on appeal turns on what it means for a storage device to be “local” to a particular computer or node in a computer network. Mangosoft claimed that in construing the term “local,” the District Court improperly relied on a technical dictionary definition and incorrectly required that the connection be “direct” and “unique.” However, the Federal Court accepted Oracle’s claim that the District Court’s construction of “local” was supported by claim language, specification, prosecution history, and reliable extrinsic evidence.

First, the District Court’s construction of the term “local” was consistent with the language of claim 1, whereas Mangosoft’s construction gave it too much of an expansive meaning, unsupported by the intrinsic record. Further, Mangosoft’s proposed construction of a “local” memory device to mean one that “can be contributed to

the shared addressable memory space by a particular node” rendered the word “local” superfluous as the language of claim 1 independent of the word “local” already required a connection of some sort between a computer and a hard disk. The District Court’s construction, on the other hand, gave “local” its ordinary meaning.

Second, the ‘377 patent’s specification disclosed that an “object of the invention is to provide computer network systems that... dynamically exploit[] *distributed* resources,” col.2 ll.3-6 (emphasis added), in contrast to centralized storage, and several lines of the specification characterized local persistent memory devices as being unique to individual nodes on the network. Furthermore, the specification’s figures and descriptions consistently represented “local” persistent memory devices as being directly attached to individual computers, which specifically contrasted local devices with “network memory devices.”

Third, the prosecution history supported the District Court’s construction. Mangosoft contended that based on cancellations and amendments that it had made to the patent application, the ‘377 patent did not incorporate the limitation that local devices “each [be] coupled to a respective one of said plural computers.” However, Mangosoft had incorporated the term “local” in claim 2 of the original application and had represented to the examiner that in cancelling claim 2, it had generally incorporated those cancelled terms into claim 1. The doctrine of prosecution disclaimer... preclud[es] patentees from recapturing through claim interpretation specific meanings disclaimed during prosecution.” *Omega Eng’g, Inc. v. Raytek Corp.*, 334 F.3d 1314, 1323 (Fed. Cir. 2003), so Mangosoft could not argue that the subject matter incorporated from the

cancelled claim 2 of the original application should be ignored.

Fourth, the District Court’s construction was also consistent with the extrinsic evidence of the technical dictionary definition offered by Oracle. Reference to dictionaries is not prohibited as long as the ultimate construction given to the claims in question is grounded in the intrinsic evidence and not based on definitions considered in the abstract. See *Phillips v. AWH Corp.*, 415 F.3d 1303 at 1318 (Fed. Cir. 2005). The District Court’s use of the technical definition was simply a starting point, and its claim construction was fully consistent with and supported by the intrinsic record.

Based on the claim language, specification, prosecution history, and reliable extrinsic evidence of the ‘377 patent application and the term “local,” the District Court correctly construed the claim term. The Federal Circuit, thus, affirmed the grant of Oracle’s motion for summary judgment of non-infringement.

SIGNIFICANCE TO PATENT APPLICANTS

Mangosoft presents a reminder to patent applicants that, during the drafting of the application, the specification needs to provide evidence of broader interpretations than might otherwise be afforded a claim. Such additional examples help to ensure that drawings and statements about objects of the invention are not used to unduly limit a claim feature. However, as noted below in *Helmsderfer v. Bobrick Washroom Equipment, Inc.*, No. 2008-1027 (Fed. Cir. June 4, 2008), such additional examples become more difficult to describe generically, thereby leading to further complications if the claim language is not chosen carefully.

FEDERAL CIRCUIT DEFINES PARTIALLY HIDDEN TO NOT INCLUDE COMPLETELY HIDDEN

In *Helmsderfer v. Bobrick Washroom Equipment, Inc.*, No. 2008-1027 (Fed. Cir. June 4, 2008), John A. Helmsderfer and Brocar Products (collectively “Brocar”) owns U.S. Patent No. 6,049,928 (the ‘928 patent). The ‘928 patent is directed to baby diaper changing stations that are resistant to vandalism, making them especially suitable for use in public restrooms.

Brocar filed suit in the District Court for the Southern District of Ohio against Bobrick Washroom Equipment, Inc., BWA South Company, Inc., Target Sales and Marketing, LLC, and Patterson Case Associates, Inc. (collectively “Bobrick”), alleging that Bobrick’s stainless

steel baby changing stations infringed claims 6 and 7 of the ‘928 patent.

Upon a *Markman* hearing in August 2007, the District Court entered a judgment of noninfringement based on its construction of the claim term “partially hidden from view,” which refers to the platform top surface when the table is in its closed position, folded up against the wall. The District Court construed the term as “hidden from view to some extent but not totally hidden from view.” Brocar appealed this claim construction to the Federal Circuit.

On appeal, Brocar contended that the District Court erred in that term should have been defined as

“positioned so at least some of the top surface is blocked from being seen,” so as not to exclude totally hidden from view.

The Federal Circuit noted that a claim term will be taken to carry its plain meaning unless the patentee acts as its own lexicographer and assigns to the term a unique definition that is different from its ordinary and customary meaning and clearly expresses this intention in his written description.

Brocar did not claim that it acted as its own lexicographer. Instead, Brocar argued that the plain meaning of “partially” includes completely. As evidence, Brocar asserted that the written description of the top surface as “generally hidden from view” supports its proposed construction. However, the Federal Circuit noted that different claim terms are presumed to have different meanings. *Applied. Med. Res. Corp. v. U.S. Surgical Corp.*, 448 F.3d 1324, 1333 n.3 (Fed. Cir. 2006); *CAE Screenplates Inc. v. Heinrich Fiedler GmbH*, 224 F.3d 1308, 1317 (Fed. Cir. 2000). There was no evidence that the terms have the same meaning to rebut the presumption. As such, Brocar could have used “generally hidden from view” rather than “partially hidden from view” to describe the platform top surface, and the terms would not be construed to have the same meaning.

Brocar also argued that the District Court gave too much weight to extrinsic evidence in claim construction. In rejecting this argument, the Federal Circuit held that a court may look to extrinsic evidence so long as the extrinsic evidence does not contradict the meaning otherwise apparent from the intrinsic record. *See Intel*

Corp. v. VIA Techs., 319 F.3d 1357, 1367 (Fed. Cir. 2003). Here, the meaning was not apparent from the intrinsic record because the specification did not define “partially.” Therefore, it was appropriate for the District Court to look to dictionaries for context. Further, the Federal Circuit agreed that the three dictionaries that it cited clearly contrast Brocar’s definition of “partially.”

Also, Brocar noted that the claim construction would exclude the preferred embodiment. Citing *Primos Inc. v. Hunter’s Specialties Inc.*, 451 F.3d 841, 848 (Fed. Cir. 2006) and *Vitronics Corp. v. Conceptor, Inc.*, 90 F.3d 1576, 1583 (Fed. Cir. 1996), the Federal Circuit agreed that caselaw does generally prefer that the claim construction encompass the preferred embodiment. However, the Court noted that various non-asserted claims do encompass the preferred embodiment such that it is only claims 6 and 7 that do not encompass the preferred embodiment. As such, the Court found that the difference in language deliberately did not encompass the preferred embodiment so as to allow claims of varying scope.

Lastly, the Federal Circuit noted that courts may not rewrite claim language; they must give effect to the terms chosen by the patentee. *Tex. Instruments, Inc. v. U.S. Int’l Trade Comm’n*, 988 F.2d 1165, 1171 (Fed. Cir. 1993). Therefore, the Federal Circuit affirmed that the ordinary and customary meaning of the term “partially” excludes “totally,” and that the District Court was correct in construing the term “partially hidden from view” to mean “hidden from view to some extent but not totally hidden from view.”

FEDERAL CIRCUIT FINDS INEQUITABLE CONDUCT FOR MISLEADING DECLARATION FACTS

In *Aventis Pharma S.A. v. Amphastar Pharmaceuticals, Inc.*, No. 2007-1280 (Fed. Cir. May 14, 2008), Aventis Pharma S.A. and Aventis Pharmaceuticals, Inc. (collectively, “Aventis”) appealed the District Court for the Central District of California’s finding of inequitable conduct and holding of unenforceability of Aventis’ Patent No. RE 38,743 (the ‘743 patent) and Patent No. 5,389,618 (the ‘618 patent). The Federal Circuit affirmed.

BACKGROUND

The ‘734 patent and ‘618 patent are directed to the composition of low molecular weight heparins (“LMWHs”). These LMWHs comprise the drug Lovenox® (marketed as Clexane® in Europe), which helps to prevent blood clotting, while minimizing the chance of hemorrhage, especially in high-risk surgery.

In the first office action, the patent examiner rejected the claims under 35 U.S.C. §§ 102(b)/103 over several references, including European Patent 40,144 (EP ‘144), stating that each of the prior art references teaches sulfated heparinic admixtures within the molecular weight (MW) range of the claims and is considered to be inherently the same as the claimed admixtures. The examiner noted the fact that the PTO does not have testing facilities, so it is the responsibility of the Applicant to convincingly demonstrate that the claimed product provides an unexpected or unobvious property, different from prior art products.

Aventis then offered an example to the specification, supporting its assertion that the claimed LMWHs exhibit a significantly longer half-life than formulations prepared in accordance with EP ‘144, and because it is

well established that compounds are inseparable from their properties, the evidence of a difference in a property (here, half-life), serves as evidence of a difference in structure. Nonetheless, the examiner issued a second office action maintaining the rejection citing the same reasons from the first office action. She reiterated that any properties would be inherent in the prior art compounds because they have the same structure as the claimed compounds.

Aventis amended its claim and submitted a declaration from Dr. Uzan, who distinguished the claimed formulations from the formulations in EP '144. Upon the third office action, the examiner withdrew several 102/103 rejections over other prior art references but continued to reject the claims over EP '144 for the reasons already in the record. Aventis argued in its response that EP '144 does not suggest compounds containing polysaccharides of the claimed MW in the claimed proportions and that the examiner improperly relied on inherency to reject the claimed compounds over EP '144. Aventis also averred that the claimed compounds had been shown to differ from the compounds of EP '144 in both structure and property based on Dr. Uzan's declarations about the difference in half-lives. At this point, the '618 patent was allowed.

Amphastar Pharmaceuticals, Inc. ("Amphastar") and Teva Pharmaceuticals USA, Inc. ("Teva") each filed an Abbreviated New Drug Application with the FDA to obtain approval to generic market versions of Lovenox®, and in so doing, challenged Aventis' '743 and '618 patents. Aventis sued Amphastar and Teva in the District Court for the Central District of California for infringement of the '618 patent. Amphastar filed a motion for summary judgment on its affirmative defense and counterclaim that the '618 patent is unenforceable due to inequitable conduct.

First, the District Court found that the Aventis' representation of the improved half-life of the patented compound as compared to the EP '144 compound was material to patentability as the examiner ultimately allowed the '618 application after the final representation that the difference in mean half-life was statistically significant. Second, the court found a strong inference of intent to deceive because it found no credible explanation for comparing half-lives at different doses, and comparisons at the same dose showed little difference in half-life. Upon weighing the evidence of materiality and intent, the District Court granted summary judgment against Aventis and held the '618 patent unenforceable.

On appeal, Aventis argued that the District Court erred in finding materiality because if the dose information

were material to patentability, the examiner would have requested it because: (1) she was presented with half-life data that enable her to compare various doses, (2) Dr. Uzan informed the examiner that the half-life comparison was done at different doses, (3) those of skill in the art frequently compare half-lives at different doses, and (4) half-life is independent of dose. *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, 176 Fed. Appx. 117, 120 (Fed. Cir. 2006). To support its first two reasons, Aventis relied on the statement in the Dr. Uzan's declaration that "[t]his represents an increase in 250% in the half life and is very significant because *it enables the same effect to be achieved with lower dosages*"; Dr. Uzan's testimony that he believed this to mean "that the comparison is a comparison between two doses of which one is lower than the other, *id.* at 120-21; Dr. Uzan's submission of the half-life data for the claimed compound at 60 mg as well as 40 mg, *id.* at 123. The court did not accept Aventis' reasons and concluded that the withholding of the EP '144 dosage information prevented the examiner from considering information important to patentability and constituted a failure to disclose material information. *Id.* at 122. However, this court also reversed the grant of summary judgment of unenforceability of the '618 patent and '743 patent and remanded to the District Court for determination of whether there was intent to deceive. *Id.* at 12. It noted, in particular, that the reasonableness of the comparison at different doses is relevant to determining whether there was an intent to deceive in withholding the dosage of the EP '144 composition. *Id.* at 122-23.

Following remand, the District Court held a bench trial on the issue of intent. The court again considered the explanations offered by Aventis for Dr. Uzan's failure to disclose the dose of the EP '144 composition in its half-life comparisons and was not persuaded that he presented the half-life comparisons to show only a difference in property and not also a difference in composition. *Aventis Pharma S.A. v. Amphastar Pharms., Inc.*, 475 F. Supp. 2d 970, 975 (C.D. Cal. 2007). The court determined that but for Dr. Uzan's intentional omissions, the probability was high that the '618 patent would not have issued, and it held the '618 patent and the '743 patent unenforceable due to inequitable conduct. *Id.* at 994.

Its second time on appeal, Aventis offered a new justification, alleging that Dr. Uzan's half-life comparisons were intended to show a difference in properties in response to the obviousness rejection under 35 U.S.C. § 103, not to demonstrate a compositional difference to address the anticipation rejection under 35 U.S.C. § 102, as the District Court

concluded. Aventis bases this on the premise that while a half-life comparison must be done using equivalent doses to establish a compositional difference, a half-life comparison may be done using different doses if the purpose is to establish a difference in property. In fact, Aventis argues, that it is more appropriate to use the “clinically relevant dose” of each compound to demonstrate a difference in property.

MATERIALITY

With respect to materiality, Aventis contends that the District Court made two clearly erroneous findings of fact: (1) that the central question relating to patentability was compositional differences, and (2) that the purpose of Dr. Uzan’s half-life comparisons was to show compositional differences. Aventis contended that anticipation was the only rejection of record, even though there was an obviousness rejection present throughout prosecution and that the District Court erred in concluding that the “issue of obviousness necessarily folds into, and is subsumed, by inherency.” Aventis III, 475 F. Supp. 2d at 982 n.10. Although the District Court incorrectly suggested in a footnote that obviousness is subsumed by inherency, the Federal Circuit sees this merely as recognition by the court that the notion of inherency was part and parcel of the examiner’s rejections. *Id.* at 979. Furthermore, several statements in the opinion clearly indicate that the court was aware of the obviousness rejection. *Id.* at 980. The Federal Circuit does not find clear error in the District Court’s ultimate decision, recognizing the court’s understanding that the PTO did not have the facilities to test the products and that Aventis did not provide evidence of a difference in property to show a compositional difference. Second, the Federal Circuit does not agree with Aventis that the District Court clearly erred in its determination that the half-life comparisons were, at least in part, intended to show compositional differences because Dr. Uzan’s example and all of the evidence directed at the EP ‘144 reference appears without distinction between the § 102 and § 103 aspects of the rejection. Therefore, the District Court properly found that the half-life comparisons were intended to address both the anticipation and obviousness rejections, and the failure to disclose the dosage information evidenced intent to deceive.

Aventis further urges that the examiner clearly withdrew the § 102 rejection based on the MW distribution data, and the half-life data in the second Uzan declaration was intended only to overcome the § 103 rejection. Therefore, it avers that the anticipation rejection was not still pending at the time of the third office action. The Federal Circuit notes, however, that

although the court may have erred in concluding that the anticipation rejection was still pending in the third office action, that conclusion was not critical to the court’s ultimate determination that there was intent to deceive, based on evidence prior to the third office action. Therefore, the District Court did not clearly err in determining that the half-life comparisons were, in part, intended to show compositional differences to address the anticipation rejection under 35 U.S.C. § 102 and, thus, rejecting Aventis’ argument that they were intended only to show differences in property, such that dosage was immaterial.

Aventis then argued that the District Court clearly erred in excluding evidence that comparison of half-lives at different doses was the standard practice in the LMWH field. The Federal Circuit finds no abuse of discretion by the court’s exclusion of the evidence because evidence of industry practice of clinically-relevant doses would only be pertinent if there was a finding that the half-life comparisons were used to address obviousness and not anticipation because Aventis has conceded that half-life comparisons must be at the same dose to show compositional differences. Further, the court noted that neither the claims nor the specification were limited to prevention of deep venous thrombosis in high-risk surgical patients and that the patented composition could be used at several different doses for several different indications.

INTENT

The District Court heard Dr. Uzan’s testimony that he did not have deceptive intent and considered this along with all the other relevant evidence, yet the court determined that it did not outweigh the cumulative evidence evincing an intent to deceive. Therefore, it maintained that the District Court did not err in concluding that the other evidence outweighed Dr. Uzan’s testimony.

Lastly, the Federal Circuit upheld the District Court’s finding that Dr. Uzan failed to disclose the dosage information because in the least, the information was provided in a very misleading way. Dr. Uzan’s failure to disclose the information was also not found purely due to inadvertence. Unlike any of the inadvertent omissions made in prosecution, there is sufficient evidence of concealment to warrant a determination that the dose information was intentionally withheld.

DISSENT

Judge Rader dissented because he did not find that the record showed clear and convincing evidence of intent to deceive the PTO. Specifically, Judge Radar pointed

out that the inequitable conduct claim is used too frequently and improperly. Even if Dr. Uzan was negligent, this does not show culpable intent to deceive based on *Kingsdown Med. Consultants, Ltd. V. Hollister, Inc.*, 863 F.2d 867, 876 (Fed. Cir. 1988) (en banc). Rader also pointed out that Dr. Uzan, a world-class scientist, would not likely risk his reputation and tarnish his career for a single example in the prosecution of a patent for an invention in which he was not even involved. Also, Dr. Uzan's candor in revealing the error himself and correcting it before it resulted in an issued patent was inconsistent with deceptive intent.

SIGNIFICANCE TO PATENT APPLICANTS

Aventis represents a continuation of the Federal Circuit's recent trend to ignore, for purposes of inequitable conduct, any need for intent in determining

fraud on the patent office. Instead, as noted by the dissent, the Federal Circuit focuses almost exclusively on materiality, thereby encouraging frivolous inequitable conduct charges. *Aventis* also provides a cautionary note about the need for declarations to be as precise as possible since any error in the declaration could result in a charge of inequitable conduct. Specifically, the Federal Circuit is holding that declarations are inevitably material to the Examiner such that, even without intent to deceive, any error in the declaration amounts effectively to inequitable conduct by the patentee. As such, *Aventis* serves as notice to inventors to carefully review a declaration presenting facts to an Examiner to ensure that the facts in the declaration are both technically accurate and not misleading as to the outstanding rejections for which the facts are being presented.

DC CIRCUIT FINDS FAILURE TO DISCLOSE PATENTS TO STANDARD SETTING ORGANIZATION DID NOT PRESENT AN ANTITRUST INJURY

In *Rambus Inc. v. FTC*, 522 F.3d 456 (D.C. Cir 2008), Rambus appealed the finding of the Federal Trade Commission (FTC) that Rambus engaged in an unfair method of competition and unfair or deceptive acts or practices prohibited by § 5(a) of the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. § 45(a). Specifically, the FTC had found that Rambus had engaged in unfair competition by deceptively failing to disclose its patents and patent applications relating to standards being set by a standard setting organization (SSO) in relation to synchronous dynamic random access memory (SDRAM): the Joint Electron Device Engineering Council (JEDEC).

Rambus had participated in the JEDEC in developing the standard, but had withdrawn prior to finalization of the standard. The rules of the JEDEC required participating members to disclose intellectual property encompassing the standards being developed. During this participation, Rambus did not disclose the existence of various patent applications related to the standard under discussion as the claims at the time of participation did not cover the standard. However, after withdrawal, Rambus presented new claims in the pending application which did encompass the standard. After the standard was finalized, Rambus asserted that compliance with the SDRAM standard would infringe its patent rights relating to the undisclosed inventions.

The FTC filed a complaint under § 5(b) of the FTC Act, 15 U.S.C. § 45(b), charging that Rambus engaged in unfair methods of competition and unfair or deceptive acts or practices in violation of the Act. See 15 U.S.C. § 45(a). Specifically, the FTC alleged that Rambus' failure to disclose its intellectual property violated the JEDEC disclosure requirements, and resulted in Rambus' ability to monopolize the SDRAM market through unfair means. Rambus had contended that it had complied with the specific JEDEC rules in regards to what intellectual property was required to be disclosed and, therefore, did not engage in the type of deceptive behavior needed to show unfair competition under 15 U.S.C. § 45(b).

After conducting a trial before an administrative law judge (ALJ), the ALJ issued an Initial Decision agreeing with Rambus. Specifically, the ALJ found that any failure to disclose was due to the specific JEDEC policies not requiring such disclosure and therefore Rambus' non-disclosure was not in violation of the JEDEC policies. However, after appealing to the Commission, the Initial Decision was reversed and Rambus was found to have engaged in deceptive behavior. Specifically, the Commission found that the JEDEC policies and rules, while not a model of clarity, at least impliedly required the disclosure and such was presumed by the members. Moreover, the deceptive intent provided for the monopolization because, had JEDEC been aware of the patent applications, JEDEC either would have excluded the patented technologies from the standard or at least

required Rambus provide assurances of “reasonable and nondiscriminatory” license fees. As a remedy, the Commission ordered that the patented technology be made available for license at a preset license rate, depending on the type of JEDEC compliant DRAM involved.

On appeal, Rambus challenged the finding that the JEDEC rules required disclosure of the patent applications in question. Also, Rambus challenged that there was an antitrust violation because there was insufficient evidence that the JEDEC either would have excluded the patented technologies from the standard or at least required Rambus provide assurances of “reasonable and nondiscriminatory” license fees. In regards to the license fees, Rambus argued that the required license would not have been an antitrust violation, and there was insufficient evidence that JEDEC would have simply excluded the patented technology.

The D.C. Circuit noted that not all monopolies are illegal as only those acquired by unlawful means are considered anticompetitive. In defining what constitutes unlawful acquisition of a monopoly, the DC Circuit relied upon its prior decision in *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001) (en banc) (*per curiam*) in defining the test. Under this test, there needs to be a finding on the following:

First, “to be condemned as exclusionary, a monopolist’s act must have ‘anticompetitive effect.’ That is, it must harm the competitive process and thereby harm consumers. In contrast, harm to one or more competitors will not suffice.” *Microsoft*, 253 F.3d at 58; see also *Trinko*, 540 U.S. at 407; *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993); *Covad Commc’ns. Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 672 (D.C. Cir. 2005). Second, it is the antitrust plaintiff—including the Government as plaintiff—that

bears the burden of proving the anticompetitive effect of the monopolist’s conduct.

While criticizing the Commission’s findings of fact on the issue of whether disclosure was necessary, the D.C. Circuit accepted the Commission’s conclusion that the failure to disclose the patent applications was in violation of the JEDEC rules for purposes of appeal. The D.C. Circuit then found that, even assuming the disclosure was required, the Commission improperly assumed that the anticompetitive effect existed for both likely outcomes had the patent applications been properly disclosed (i.e., preventing JEDEC from excluding the patented technology or requiring a license). Moreover, the Commission had specifically found that the FTC had not provided sufficient evidence that JEDEC would have excluded the patented technology from the standard, which the D.C. Circuit found would have been an antitrust effect harmful to competition. As such, the only viable antitrust effect was that JEDEC would have been required Rambus to provide the license.

The D.C. Circuit then found that, whereas in the Microsoft case there was evidence of an effect caused by Microsoft’s deceptive intent (i.e., tricking developers in working on proprietary Java applications when the developers were intending to work on platform independent Java applications), the only competitive harm resulting from Rambus’ deceptive actions was a raise in prices. However, relying on *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128 (1998), the D.C. Circuit found that the mere raising of prices was not an anticompetitive effect. Specifically, even assuming Rambus had disclosed the patents, this disclosure would also have resulted in a price increase such that there was no discernable injury. As such, the D.C. Circuit vacated the Commission’s ruling due to the failure to find evidence of an anticompetitive effect due to Rambus’ failure to disclose the patent applications in question.

11TH CIRCUIT FINDS USE OF TRADEMARKS IN METATAGS IS AN INFRINGING USE IN COMMERCE

In *North American Medical Corporation v. Axiom Worldwide, Inc.* 522 F.3d 1211; 86 USPQ2d 1462 (11th Cir. 2008), Axiom Worldwide (“Axiom”) appealed the District Court for the Northern District of Georgia’s grant of preliminary injunction in favor of North American Medical Corp. (“NAM”) enjoining Axiom from engaging in alleged acts of trademark infringement and false advertising. The Eleventh Circuit affirmed in part and vacated and remanded in part.

BACKGROUND

NAM designs and manufactures physiotherapeutic spinal devices used to treat lower back pain, which are commonly known as traction devices. NAM owns and uses registered trademarks for “Accu-Spina” and “IDD Therapy.” Axiom competes with NAM and manufactures a physiotherapeutic device known as the DRX 9000.

NAM alleged that Axiom infringed NAM’s trademarks by using the “Accu-Spina” and “IDD Therapy” marks on

Axiom's website within meta tags. Meta tags are words or phrases included in a website's code intended to describe the contents of the website with which the meta tags are associated. Such included meta tags are often used by internet search engines to associate a user's search terms with relevant websites but are not displayed thereon. NAM further alleged that Axiom made false statements about the DRX 9000 in stating (1) that Axiom and NASA or the DRX 9000 and NASA were affiliated and (2) that the DRX 9000 was FDA approved.

The District Court granted NAM's request for a preliminary injunction thereby enjoining Axiom from using NAM's trademarks within meta tags on Axiom's websites and from making the challenged statements about the DRX 9000. Further, the District Court found that Axiom's use of NAM's trademarks created a likelihood of confusion among consumers and that Axiom's statements about the DRX 9000 were literally false and material to consumers' purchasing decisions. This decision was appealed to the Eleventh Circuit.

On appeal, Axiom argued that NAM failed to establish a likelihood of success on the merits of either the trademark infringement or the false advertising claims and, assuming *arguendo* that NAM had established such likelihood of success, that the District Court erred in presuming that any plaintiff with a viable unfair competition claim will always suffer irreparable harm if a preliminary injunction is not issued.

LIKELIHOOD OF SUCCESS: TRADEMARK INFRINGEMENT

Under Eleventh Circuit precedent, a preliminary injunction may be granted only if NAM established "(1) a substantial likelihood of success on the merits of the underlying case, (2) [NAM] will suffer irreparable harm in the absence of an injunction, (3) the harm suffered by [NAM] in the absence of an injunction would exceed the harm suffered by [Axiom] if the injunction issued, and (4) an injunction would not disserve the public interest." *Johnson & Johnson Vision Care, Inc. v. 1-800 Contacts, Inc.*, F.3d 1242, 1246 (11th Cir. 2002).

In order to prevail on a claim of trademark infringement under the Lanham Act, the Eleventh Circuit required that NAM establish: "(1) that [NAM] possess[es] a valid mark, (2) that the [Axiom] used the mark, (3) that the [Axiom's] use of the mark occurred "in commerce," (4) that the [Axiom] used the mark "in connection with the sale... or advertising of any goods," and (5) that [Axiom] used the mark in a manner likely to confuse consumers." Slip op. at 7, citing *1-800 Contacts, Inc., v. WhenU.com, Inc.*, 414 F.3d 400, 406-07 (2d Cir. 2005).

Specifically, Axiom argued that the use of NAM's trademarks within meta tags of Axiom's websites does not constitute a "use in commerce" under the Lanham Act and, even if such use as meta tags is a "use in commerce," that such use is not likely to confuse consumers. The Eleventh Circuit "readily conclude[d]" that Axiom's use of NAM's trademarks as meta tags was an infringing use as Axiom used the trademarks in an "effort to promote and advertise its products on the Internet." Slip op. at 9. Further, Internet search results displayed NAM's trademarks along with a description of Axiom's website. The Eleventh Circuit distinguished *1-800 Contacts* because there (1) the defendant used the plaintiff's web address and not plaintiff's protectable trademark, and (2) the defendant did not cause the plaintiff's trademark to be displayed to the consumer. Here, Axiom used NAM's registered trademarks in meta tags and the registered trademarks were displayed along with descriptions of Axiom's website when searched using an Internet search engine. The Eleventh Circuit went on to substantially criticize the Second Circuit's analysis in *1-800 Contacts* as incorrectly analyzing the elements of trademark infringement, rendering the conclusions therein reached suspect. Specifically, the Second Circuit reasoned that because the defendant did not display the plaintiff's trademark, there could be no possibility of confusion.

The Eleventh Circuit disagreed with the Second Circuit's analysis in that, while the lack of display is worthy of consideration, it not dispositive of the likelihood of confusion analysis as the elements governing the confusion analysis are specifically separated and each deserves individual attention. With regard to likelihood of confusion, the Eleventh Circuit analyzed the following seven factors:

- (1) the strength of [NAM's] mark;
- (2) the similarity between [NAM's] mark and the allegedly infringing mark;
- (3) the similarity of the products and services offered by [NAM] and [Axiom];
- (4) the similarity of the sales methods;
- (5) the similarity of advertising methods;
- (6) [Axiom's] intent; and
- (7) actual confusion.

Alliance Metals, Inc., of Atlanta v. Hinely Indus., Inc., 222 F.3d 895, 907 (11th Cir. 2000). In the above case, Axiom only challenged that the meta tags caused the Internet search results, which was rejected by the Court, and that the District Court's reliance on

Brookfield Communications, Inc., v. West Coast Entertainment Corp., 174 F.3d 1036 (9th Cir. 1999), and *Promatek Industries, Ltd. v. Equitrac Corp.*, 300 F.3d 808 (7th Cir. 2002) with respect to meta tags and search engines was misplaced.

In *Brookfield*, the Ninth Circuit enjoined a defendant from including a competitor's trademark for confusingly similar terms in the meta tags of the defendant's website. There, the Ninth Circuit characterized the infringing use of a trademark in a meta tag as generating initial interest confusion, assuming that the allegedly infringing use was not actually displayed by the defendant. The Seventh Circuit faced similar facts in *Promatek*, which led to a similar conclusion of initial interest confusion sufficient to support a finding of likelihood of confusion.

However here, the Eleventh Circuit distinguishes *Brookfield* and *Promatek* as NAM has demonstrated a likelihood of actual source confusion, i.e., a consumer is likely to be confused as to whether Axiom and NAM are affiliated or whether Axiom's and NAM's products come from a same source. Because Internet search results displayed a description of Axiom's website in which NAM's trademarks were highlighted, the Eleventh Circuit found that Axiom's use of NAM's trademarks in meta tags caused a likelihood of actual consumer confusion as to source.

Further, Axiom argued that its use was no different than a store placing the store's generic competing product next to a brand name product on the store's shelf. However, because Axiom's use of NAM's trademarks as meta tags caused Internet search engines to suggest that the competing products had a same source, were affiliated, or were both sold by Axiom, the Eleventh Circuit concluded that Axiom's use caused a likelihood of actual source confusion. Therefore, the Axiom's analogy was misplaced.

LIKELIHOOD OF SUCCESS: FALSE ADVERTISING

In order to prevail on a false advertising claim under the Lanham Act in the Eleventh Circuit, NAM must demonstrate: "(1) the ads of [Axiom] were false or misleading, (2) the ads deceived, or had the capacity to deceive, consumers, (3) the deception had a material effect on purchasing decisions, (4) the misrepresented product or service affects interstate commerce, and (5) [NAM] has been - or is likely to be - injured as a result of the false advertising." Slip op. at 23, citing *Johnson & Johnson*, 299 F.3d at 1247.

The Eleventh Circuit held that the District Court did not clearly err when finding that Axiom's claims of affiliation with NASA and the DRX 9000 being FDA

approved were literally false and that the ads were material to consumers' purchasing decisions. As such, the District Court did not clearly err in finding that NAM demonstrated a likelihood of success on the merits of the false advertising claims.

PRESUMPTIONS OF IRREPARABLE HARM

The Eleventh Circuit vacated the District Court's grant of preliminary injunction with respect to both the trademark infringement and false advertising claims, despite NAM's demonstration of a likelihood of success on the merits, because the District Court improperly relied upon a presumption of irreparable harm for both the trademark infringement and false advertising claims.

In vacating the preliminary injunction with respect to NAM's false advertising claims, the Eleventh Circuit notes that the District Court relied upon an incomplete recitation of the law. Specifically, proof of falsity of advertising is sufficient to sustain irreparable injury for purposes of a preliminary injunction when the challenged advertising makes a misleading comparison to a competitor's product. However, if the false advertising is non-comparative and makes no direct reference to a competitor's product, irreparable harm is not presumed. Slip op. at 28, citing *J. Thomas McCarthy, McCarthy on Trademarks and Unfair Competition*, Sec. 23.37 (4th e. 2003); *Energy Four, Inc., v. Dornier Medical Systems, Inc.*, 765 F. Supp. 724, 734 (N.D. Ga. 1991) (*internal quotations omitted*). Below, the District Court incorrectly presumed irreparable harm despite Axiom's false advertising being non-comparative and making no direct reference to NAM's products. As such, the Eleventh Circuit vacated the preliminary injunction with respect to the false advertising claims and remanded for determination as to whether NAM will suffer irreparable harm in the absence of a preliminary injunction.

With regard to presuming irreparable harm on the trademark infringement claims, the Eleventh Circuit noted that it had previously acknowledged and extended a presumption of irreparable harm once a plaintiff has established a likelihood of success on the merits of a trademark infringement claim. However, the Eleventh Circuit relied on the recent Supreme Court decision in *eBay Inc., v. MercExchange, L.L.C.*, 547 U.S. 388, 126 S.Ct. 1837 (2006).

In *eBay*, a District Court refused to grant the plaintiff's motion for permanent injunction after a jury had found that the defendant had infringed plaintiff's patents. The Federal Circuit reversed the District Court and

articulated a categorical rule that permanent injunctions shall issue once infringement is established. The Supreme Court reversed the Federal Circuit and upheld the District Court's denial of permanent injunction. "The [Supreme] Court stressed that the Patent Act indicates that injunctive relief may issue only in accordance with the principles of equity." Slip op. at 30, quoting *eBay* at 393 (internal quotes omitted).

The Eleventh Circuit extended the *eBay* patent ruling (with respect to a permanent injunction) to the current trademark claims (with respect to a preliminary injunction) by relying on the similarity between the language of the Lanham Act and the Patent Act. Because the language of the two acts is so similar and no obvious distinction between preliminary and permanent injunctive relief can be made, the principles of equity should prevail.

However, the Eleventh Circuit did not state that the District Court erred in extending the presumption of harm to NAM's trademark infringement claims. The Eleventh Circuit only held that the Supreme Court's ruling in *eBay* should apply to NAM's trademark infringement claims. As such, the Eleventh Circuit vacated the preliminary injunction with respect to the trademark infringement claims, remanded for further development of the case with respect to the Supreme Court's decision in *eBay* and stated that the District Court may very well reach the conclusion that a preliminary injunction is appropriate.

SIGNIFICANCE TO TRADEMARK OWNERS

The use of meta tags has presented a particular problem for trademark owners since consumers are driven to particular websites through the meta tags. While certain courts have allowed relief under the rubric of initial interest confusion, the Eleventh Circuit more directly attacked the practice of meta tag use as presenting infringement either directly or through false association. As such, the theories espoused by the Eleventh Circuit should provide a more direct mechanism to resolve infringement occurring through meta tags.

Additionally, the Eleventh Circuit's decision also highlights the importance of presenting evidence of irreparable harm in trademark cases. While presumptions of irreparable harm used to exist, after *eBay*, courts may require evidence of irreparable harm beyond mere use of the mark. However, such evidence should be easier to present in the context of trademark infringement as trademark licensing is not as common as licensing is in the patent world, and importantly, allowing confusion to continue for trademark infringement is arguably more societally harmful since it allows deception of the public as opposed to a mere infringement of a private property right as in patent infringement.

SPECIAL OFFER ON INTELLECTUAL PROPERTY AND GOVERNMENT CONTRACTS TREATISE

Slated for release in August of 2008 by Oxford University Press, *Intellectual Property In Government Contracts: Protecting And Enforcing IP At The State And Federal Level* is being coauthored by James G. McEwen in collaboration with two pre-eminent intellectual property practitioners whose combined experience spans the private and government sectors. *Intellectual Property in Government Contracts* provides a comprehensive survey of U.S. federal and state intellectual property procurement laws and gives valuable advice to government and private-sector attorneys on aspects of intellectual property, government procurement, and litigation from the perspectives of both the government and the contractor communities.

IP attorneys will find an extensive overview of U.S. federal and state procurement systems, strategies for preserving IP rights in the procurement process, and the practical guidance needed to avoid the pitfalls of

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The treatise will provide a roadmap for high-tech contractors doing business with the government sector in the United States, and will include an examination of methods proven to ensure compliance with government provisions.

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USPTO PROPOSES NEW FEES FOR 2009

In order to account for changes in the Consumer Price Index (CPI), the United States Patent and Trademark Office, (USPTO) has proposed new fees for patent filings. The fees generally reflect a 4% projected change in the CPI for 2009. 73 Fed. Reg. 31656 (June 3, 2008). These new fees should go into effect on October 1, 2008. The proposed changes in the patent fees are as follows. All other fees will generally remain unchanged.

Description	2008-2009 Proposed Fee	2007-2008 Fee
Basic filing fee - Utility	320.00	310.00
Utility Search Fee	530.00	510.00
Utility Examination Fee	220.00	210.00
Independent claims in excess of three	220.00	210.00
Claims in excess of 20	52.00	50.00
Basic filing fee - Design	220.00	210.00
Design Examination Fee	140.00	130.00
Basic filing fee - Reissue	320.00	310.00
Reissue Examination Fee	640.00	620.00
Reissue Search Fee	530.00	510.00
Provisional application filing fee	220.00	210.00
Utility issue fee	1500.00	1,440.00

Description	2008-2009 Proposed Fee	2007-2008 Fee
Design issue fee	850.00	820.00
Statutory disclaimer	140.00	130.00
Extension for response within second month	470.00	460.00
Extension for response within third month	1080.00	1,050.00
Extension for response within fourth month	1690.00	1,640.00
Extension for response within fifth month	2300.00	2,230.00
Notice of appeal	530.00	510.00
Filing a brief in support of an appeal	530.00	510.00
Request for oral hearing	1070.00	1,030.00
Filing of PCT application-USPTO ISA-national stage	320.00	310.00
National Stage Search Fee - search report prepared and provided to USPTO	430.00	410.00
National Stage Search Fee - all other situations	530.00	510.00
National Stage Examination Fee - all other situations	220.00	210.00

STEIN McEWEN & BUI IS PLEASED TO WELCOME NEW ATTORNEY: QUASIM A. SHAH

Quasim A. Shah joins the firm as an associate. Mr. Shah received a Bachelor of Science degree in Electrical Engineering from George Mason University in 2000 and a J.D. from Georgetown University Law Center in 2005. He is currently an active member of the District of Columbia Bar.

Mr. Shah has worked as an Electrical Engineer for the U.S. Department of Defense and two hardware companies, as a Network Engineering Consultant to the U.S. Government and as a Project Manager for an energy infrastructure development firm. He has experience designing and implementing telecommunications networks, hardware and protocols and has developed an expertise in TCP/IP and data communications for wired

and wireless networks. Mr. Shah has experience in drafting amendments for patent applications and responses to U.S. Patent Office Actions and in providing research and analysis on patent litigation issues.

As an engineering student, Mr. Shah was a member of the George Mason chapter of Eta Kappa Nu (Electrical Engineering Honor Society) and worked as a Junior Engineer for the Department of Defense, conducting research on ATM and other telecommunications networks. While in law school, Mr. Shah researched public intellectual property trusts and was a member of the Georgetown Student Intellectual Property Association.

FEATURE COMMENT: TRAPS FOR THE UNWARY: AN OVERVIEW OF PATENT ISSUES FOR THE COMMERCIAL COMPANY ENTERING INTO FEDERALLY SPONSORED RESEARCH AND DEVELOPMENT PROJECTS

BY JAMES G. McEWEN, STEIN, McEWEN & BUI, LLP.¹

BACKGROUND

For the uninitiated, contracts and agreements with the Federal Government present a dizzying array of acronyms and terms which seemingly add a layer of confusion above the already-complex subject of patent rights for parties under research and development agreements. However, it is important to realize that, generally, contracts with the Federal Government are similar to commercial contracts (i.e., consideration, offer, and acceptance). Thus, while generally similar in terms of appearance, the difference in a government contract becomes apparent when you realize one important fact: the contract is with the rule maker who may or may not have consented to suit according to the particular circumstance. As a result, a Government contract can be thought of in terms of a controlled taking since the Government creates laws that govern all contracts, and is therefore in a better position as a contracting party to create mandatory clauses, and to ensure their inclusion in all contracts.

For instance, in a contract between private parties, if one party fails to include a clause, that clause is not part of the contract. In contrast, since certain clauses are required by law, where a Government contract is concerned, omitted clauses can be included as if in the contract since the contract is otherwise *ultra vires*.²

In the context of intellectual property, many intellectual property rights are governed by such laws or by strong Federal procurement policies, and are thus “read in” to all contracts.³ Therefore, unlike

commercial contracting, one cannot assume that since a Government contract lacks a provision that the missing provision will not be later automatically included.

This requirement is especially strong in the context of intellectual property. For instance, when inventions are created or made under a procurement agreement with the Government, such inventions are generally referred to as “subject inventions.” These inventions are defined by law in the Bayh-Dole Act,⁴ which requires Government rights in certain inventions made in conjunction with a Government contract.⁵ Similar statutes apply in the context of other intellectual property, most notably for technical data for contracts with the Department of Defense⁶. However, since patents represent a core protection for many companies whose existence is based on exclusive use of knowledge and who are interested in working with the Government, it is important for these companies to recognize the Government’s requirements for patents, and how to account for these requirements in a manner that fits their particular marketing model.

Christian doctrine. Pursuant to this Doctrine, important regulations are read into contract or conflicting terms are removed. Since intellectual property provisions represent important procurement policy objectives, as evidenced in terms of their treatment in the Federal Acquisition Regulations and Congressional and Executive interest on the subject, these provisions would likely satisfy the requirements for inclusion using the Christian Doctrine since an improper inclusion/exclusion would be *ultra vires*. E.g., *FilmTec Corp. v. Hydranautics*, 982 F.2d 1546, 25 USPQ2d 1283 (Fed. Cir. 1992) (Patent title automatically divested mid-litigation due to finding invention was “subject invention” under Saline Water Conversion Act (since repealed)).

⁴ The Bayh-Dole Act refers to Chapter 18 of 35 U.S.C.

⁵ Under 35 U.S.C. §201(e), subject invention “means any invention of the contractor conceived or first actually reduced to practice in the performance of work under a funding agreement.” The Government obtains rights in subject inventions either directly through 35 U.S.C. §202 or through a series of Executive Orders implemented in the Federal Acquisition Regulations. See Federal Acquisition Regulation (FAR) 27.302(a) (discussing the interplay of the Presidential Memorandum on Government Patent Policy to the Heads of Executive Departments and Agencies dated February 18, 1983, and Executive Order 12591 and Chapter 18 of 35 U.S.C.).

⁶ 10 U.S.C. 2320-2321.

¹ The opinions in this article do not represent the official positions of Stein, McEwen & Bui, LLP. Portions of this article utilize research included in *Intellectual Property In Government Contracts: Protecting And Enforcing IP At The State And Federal Level*, slated for release in August of 2008 by Oxford University Press.

² *Federal Crop Ins. Corporation v. Merrill*, 332 U.S. 380 (1947). See also the Christian doctrine as outlined in *G.L. Christian and Associates v. United States*, 312 F.2d 418 (Ct. Cl. 1963).

³ While not all forms of intellectual property have a law on point, such clauses are very likely going to be read into these contracts under the

A. INTELLECTUAL PROPERTY CLAUSES GOVERNED STRICTLY

Consistent with commercial contracts, intellectual property clauses are governed strictly. As such, where a patent is developed under a Government contract, that contract's terms will govern the respective rights of the parties. Thus, it is these terms and conditions which have an effect on subsequent licensing. However, since these clauses have the veneer of law, Courts are more likely to enforce the clauses even where the contractual remedy appears harsh.

For example, in *Campbell Plastics Engineering & Mfg., Inc., v. Army*,⁷ the Government took title to a contractor's patent for the contractor's failure to report a subject invention pursuant to the timing requirements governed by FAR 52.227-11 and by statute (35 U.S.C. §202). This clause, like many of the patent rights clauses, have been in effect for a number of years without such a ruling.⁸ Indeed, there appeared to be a feeling that such clauses were not of importance. As such, this holding was a shock to many in the procurement community who had never considered the remedies these intellectual property clauses have with respect to contractor-owned intellectual property. Importantly, from a licensing standpoint, a potential licensee performing due diligence needs to check whether the patent owner performed the required contractual duties for reporting the subject invention since, as demonstrated in *Campbell Plastics*, the failure to perform these duties can result in the loss ownership itself.

These intellectual property clauses, which are in most procurements, are standardized and have multiple requirements for reporting, notices, dispute resolution, and later rights to use. Moreover, these requirements cannot be waived merely because they are believed oppressive at a later time. Also, any attempt to deviate from a standard intellectual property scheme must be done properly and carefully since, unlike pure commercial contracts where implied and apparent authority can still bind the parties, anyone lacking *actual* authority lacks the ability to bind the Government to a contract. Thus, in the same way it is important to ensure that a Government official signing a procurement vehicle has the actual authority to do so, it is important that there is a statutory basis for a

⁷ 389 F.3d 1243; 73 U.S.P.Q.2d 1357 (Fed. Cir. 2004).

⁸ Versions of this clause and its requirements predate the enactment of Bayh-Dole, with some of the first versions being found dating back to the late 1950's, and are in the earliest versions of the Defense Acquisition Regulations. E.g., ASPR 7-302.23(a) (December, 1969).

procurement vehicle with deviations from the standard intellectual property provisions.

B. OVERVIEW OF PATENT CLAUSES

For patents, the standard requirements are embodied in the Bayh-Dole Act at 35 U.S.C. §200-204 and in the Federal Acquisition Regulations (FAR) at section FAR 227 and 52.227-11 and Defense Federal Acquisition Regulation Supplement at section DFARS 252.227-7038 (collectively referred to as Bayh-Dole rights or clauses hereafter). There are strong public policies implicated by these requirements. Specifically, the Government's contribution is often most important in two different phases of development: the conceptual phase and the prototyping phase. As such, Bayh-Dole rights are generally created for patented inventions where the Government entered into a contract to conceive of the invention, as well as for when the invention was actually created (as opposed to merely being a plan to be built).⁹ The strong policy next requires that such inventions are used to benefit the American tax payer by allowing the Contractor the right to retain title of the invention with the exclusive right to commercialize the invention. Where the Contractor fails to live up to these expectations, the Government will take title to or license the invention itself.

Since being promulgated, the military industrial complex has dwindled to only a few main contractors. Thus, there is a new incentive to attract non-traditional contractors for procurements. Moreover, many Government labs have closed such that the Government is required to rely more on extramural research to accomplish agency missions, which necessarily requires flexibility for intellectual property provisions. Also, both Government and private industry are realizing a need to more effectively leverage their intellectual property, which necessarily requires both parties to be flexible in their approach to public-private collaborations for different needs. As a result, the standard procurement terms and conditions have grown more flexible, and a whole host of procurement vehicles now exist which provide the contracting authority with actual authority to deviate from standard procurement terms and conditions for intellectual property.¹⁰

While many types of intellectual property are created during research and development, patents are the most prominent type since patents are granted to encourage and protect ideas themselves. In contrast, copyrights are granted to protect only a particular expression, such

⁹ 35 U.S.C. 202.

¹⁰ Examples include Other Transaction Agreements, CRADAs, Venture Funding through programs such as In-Q Tel, and Prize Authorities.

as the software resulting from a project, and provide very thin protection only to that particular expression. Trademarks solidify a consumer's understanding as to the source of a product or service, but do not confer ownership over the substance of the developed product itself and do not prevent others from copying the results. Lastly, while trade secrets are available to protect the specifics of the developed product, trade secrets only protect unknown information of demonstrable value and do not protect the product if there is independent development or where the product is reverse engineered. Thus, patents are often the tangible result of a concerted research and development program.

Moreover, patents have become a powerful tool for attracting investment since a grant of a patent enjoys a presumption of validity and an extent as broad as the claims. This is a particular advantage since over other types of intellectual property (most notably trade secrets) which do not hold a presumption of validity. Lastly, and perhaps most importantly, patents hold the threat of a permanent injunction which is a far more devastating remedy in many cases than mere damages. While this threat of injunction has been somewhat mitigated by the Supreme Court's recent decision in *eBay v. Mercexchange*, the injunctive remedy is the traditional norm as acknowledged by the Supreme Court's decision.¹¹

In view of these many advantages, most commercial and all Government development agreements address patent rights in one form or another. Generally, these describe treatment for improvements developed during the agreement, which parties own or license the patent, and intellectual property indemnification or joint defense for the developed product. In the context of Government research and development, these terms and conditions are substantially uniform such that a party can determine in advance the Government's typical position. However, while each situation holds special and unique requirements¹², there are general terms and conditions that one needs to be aware of before entering into a research and development contract with the Federal Government. These general terms and conditions are set forth separately below.

1. TIMING AS AFFECTS RIGHTS

The Government typically obtains patent rights based upon the timing of an event. Specifically, under 35 U.S.C. 200-202 as implemented in FAR 52.227, the

¹¹ 126 S. Ct. 1837 (2006).

¹² For instance, requirements vary according to the type of contractor, the particular agency who is party to the contract, and the type of contractual vehicle employed.

Government obtains license or ownership rights in subject inventions. Subject inventions are defined to include inventions first conceived or *actually* reduced to practice (i.e., built) while conducting research and development during a procurement contract.¹³

A few consequences of this phraseology are important. As defined, subject inventions are independent of *constructive* reductions to practice (i.e., when a patent application is filed) as well as being independent of delivery of the patentable invention. In addition, since the test for subject inventions is event based, the test is independent of funding so long as the work is within the statement of work of the procurement contract. This situation is in contrast to how the Government obtains rights in trade secrets and copyrights (i.e., technical data and computer software), which is generally based on funding.¹⁴ As such, it is conceivable that inventions conceived and first reduced to practice outside of a government contract can be considered a "subject invention."¹⁵

Once a subject invention is created, the Government will typically only obtain a non-exclusive license to use the invention for Government purposes unless the work is being performed outside of the United States.¹⁶ Further, the Government typically only obtains a license right as opposed to *ownership* to the subject invention. Thus, the mere fact that the invention is classified as a subject invention does not preclude enforcement of the patented invention in the commercial marketplace.

2. UNIQUE MONITORING AND DISCLOSURE REQUIREMENTS

In order to identify and track subject inventions, the Government requires the contractor provide record keeping in order to ensure that the Government obtains the benefit of the acquired right. While seemingly reasonable, these reporting requirements can be seemingly onerous to a small business lacking a formal invention disclosure and evaluation plan. The entire reporting system is predicated on the business having such a plan, and the patent clauses actually require the contractor to ensure that such a plan exists in order to

¹³ Procurement contracts include grants, contracts, and cooperative agreements. Procurement contracts do not include other contracts, such as Cooperative Research and Development Agreements (CRADAs) and Other Transactions.

¹⁴ While beyond the scope of this article, additional information on rights in technical data and computer software can be found in DFARS 252.227-7013 & 252.227-7014, as well as in the FAR Part 27 generally.

¹⁵ E.g., *Mine Safety Appliances Co. v. United States*, 150 U.S.P.Q. 453 (Ct. Cl. 1966) (first reduction to practice of helmet within statement of work sufficient to be a subject invention even though occurred between contract phases since was "close and umbilical connection" to work).

¹⁶ FAR 27.303(c) and FAR 52.227-13.

adequately track and report inventions. Indeed, the assurance that such a plan exists is a condition of compliance with the clause in the first place and can be grounds for withholding of final payment.¹⁷ However, it is important to recognize that such a plan need not be ornate so long as there is some contact for patent issues to help identify patentable inventions, which is something most businesses involved in research and development have either formally or informally.

Within the tracking system are multiple required notifications related to ensuring that the Government is made aware of the existence of the subject invention, and which allow the Government an option to take over responsibility for obtaining a patent on the subject invention if the contractor declines to do so. Specifically, the contractor is required to report each subject invention as soon as possible, and usually within two (2) months.¹⁸ Moreover, after reporting the existence of the subject invention, the contractor is required to inform the Government, within eight months after disclosure, whether the contractor will be keeping ownership of the invention (i.e., title) and in which countries. After electing to keep title, the contractor is required to complete the filing within one year of election or prior to a potential patent bar date.¹⁹ Lastly, after filing, the contractor is required to report each filing abroad and if a maintenance fee will not be paid. The failure to render any of these notices in time allows the Government the contractual option to take the title from the contractor upon written request to do so. While the government is not required to take title, this provision has been found enforceable and does allow the Government an option to take title to protect the Government's interest.²⁰

The reporting and disclosure provisions are often supplemented by annual and final reports, either as part of the clause used for large contractors, or as supplements for small contractors.²¹ These additional reports summarize the inventive activity for the year or, in the cases of a final report, for the entire contractual effort. As such, these summary reports are required

even where no inventions have been created, requiring contractors to submit negative reports confirming that nothing has been reported. These reports also help confirm whether the contractor is compliant with other patent rights provisions requiring the contractor to ensure that a process is in place to ensure timely reporting of subject inventions. Since no patent title is at risk where no invention is made, the Government uses withholding of final contract payment as an incentive to comply with this requirement. Such payment withholdings can be up to \$50,000 and can substantially delay final closeout of contracts.²² Thus, failing to sufficiently inform the Government that nothing patentable was developed can result in significant administrative and financial hardship.

C. WHEN ARE STANDARD BAYH-DOLE CLAUSES USED?

1. IS THERE A PROCUREMENT CONTRACT?

While pervasive, it is important to note that these clauses are not required in all contracts. For instance, standard Bayh-Dole clauses are only required in "procurement contracts." As defined in 35 U.S.C. §200, procurement contracts only includes grants, contracts, and cooperative agreements. Thus, standard Bayh-Dole clauses are not required in other types of agreements, notably Other Transactions and Cooperative Research and Development Agreements (CRADAs). As such, where procurement is using another contractual vehicle specifically designed to allow flexibility for intellectual property, the Government is generally allowed and encouraged to deviate from the standard Bayh-Dole clauses in order to attract more non-traditional contractors.²³ Thus, where these clauses appear in non procurement agreements, the contractor can (and should) object.

2. IS THERE RESEARCH AND DEVELOPMENT BEING PERFORMED?

Further, even where there is a procurement contract, the standard Bayh-Dole clauses are only appropriate where the procurement contract is for research and development.²⁴ While this is generally the case for grants and cooperative agreements, most contracts are not for research and development and are only mechanisms to purchase standards goods or services. In

¹⁷ DFARS 252.227-38(k) allowing withholding of final payment for failing to "establish, maintain, and follow effective procedures for identifying and disclosing subject inventions"

¹⁸ If the inventor identifies as subject invention: within 2 months. If the contractor later determines is subject invention: within 6 months.

¹⁹ The more applicable bar dates are, generally, publication of technical reports and offers for sale of the subject invention under 35 U.S.C. §102. Since the filing must be made prior to either occurrence, patent applications are often filed well before this one year deadline.

²⁰ *In re Campbell Plastics Engineering & Mfg. Inc.*, ASBCA No. 53319 (2003), affirmed *Campbell Plastics Engineering & Mfg., Inc., v. Army*, 389 F.3d 1243; 73 U.S.P.Q.2d 1357 (Fed. Cir. 2004).

²¹ See DFARS 252.227-7038 for large businesses, and DFARS 252.227-7039 for small businesses.

²² DFARS 252.227-7038, FAR 52.227-11.

²³ See David S. Bloch and James G. McEwen, "OTHER TRANSACTIONS" WITH UNCLE SAM: A SOLUTION TO THE HIGH-TECH GOVERNMENT CONTRACTING CRISIS, 10 TEX. INT. PROP. L.J. 195 (2002), Other Transactions Guide for Prototype Projects (January 2001)

²⁴ FAR 27.300 envisions inclusion "if a purpose of the contract or subcontract is the conduct of experimental, developmental, or research work."

these cases, unless the statement of work includes research and development, the standard Bayh-Dole clauses should not be used and should be objected to at least on the grounds that the reporting requirements are an unnecessary administrative burden.²⁵

D. MARCH IN RIGHTS

While many of the reporting requirements required for standard Bayh-Dole clauses are generally similar to those used in commercial joint development agreements, one of the more controversial provisions in the Bayh-Dole clauses is very different: the march-in provision. Under the march-in provision, the Government can take and license a contractor's patented subject invention in very limited circumstances.²⁶ Specifically, the Federal agency has the right to grant a license to the patented subject invention where the contractor is not taking adequate steps to "achieve practical application of the subject invention" or where the Contractor is not complying with public use or preferences for exclusive licensing to U.S. industries. Alternately, the Government can use the march in rights to license a patented subject invention in emergencies, such as to "alleviate health or safety needs." This provision reflects the importance that is placed upon ensuring that, where the Government helped at critical stages in the development of a patented subject invention, the American taxpayer receives the maximize return on investment in terms of commercialization of the invention or increased access in times of need.

While perhaps a reasonable provision from a public policy perspective, this provision is contrary to the security in ownership for patents required in the commercial world. Moreover, while march-in rights have never been used successfully for the purposes of obtaining rights, commercial contractors recognize that there is a potential for abuse. Indeed, there are periodic attempts by public interest groups to have the Government invoke these march in rights in relation to medical devices and drugs. However, since this clause is not negotiable in procurement contracts, there is

little that a contractor can do to remove this clause in a procurement contract.²⁷

E. MISCELLANEOUS PROVISIONS

While the main elements, such as the march-in rights, of the standard Bayh-Dole clauses are better known, the standard Bayh-Dole clauses typically will include miscellaneous provisions which are less well known. These provisions are unexpected and can be as troublesome from a contractor point of view as the march in rights or the definition of the subject invention. As such, these miscellaneous provisions deserve at least a brief mention.

1. COMMERCIALIZATION REPORTS

Incidental to the march in rights are provisions regarding required reporting (at the option of the Government) of commercialization for the subject invention. These reports require reporting commercial sales, gross revenue, development status, and "such other data and information as the agency may reasonably specify." Thus, the Bayh-Dole clauses require the contractor to turn over sensitive and proprietary information, which is both burdensome to compile and risky since there is always a risk of accidental disclosure.

2. PREFERENCE FOR U.S. INDUSTRY

Moreover, the contractor, prior to granting an exclusive license, needs to require the exclusive licensee to manufacture the subject invention substantially in the United States. It is unclear what "substantially" means in the context of manufacturing the subject invention since it is unclear if final assembly of imported components is compliant. Such a requirement may be difficult to fulfill for certain industries and, while a waiver may be obtained, the accidental failure to comply with this preference for U.S. manufacture could result in the Government exercising its march in rights for the licensed subject invention. As such, this provision represents a trap for the unwary contractor hoping to utilize subject inventions as part of a licensing campaign.

3. SUBCONTRACTS

Recognizing that many research and development contracts involve subcontractors, the Bayh-Dole clauses include a requirement to include the same clauses in subcontracts involving research and development. The flowdown clauses are required to stipulate that the

²⁵ Moreover, where the clause is removed and the removal is later found to be improper, the Government would still likely be protected since, as noted above, such clauses would likely be read into the contract. *C.f. FilmTec Corp. v. Hydranautics*, 982 F.2d 1546, 25 USPQ2d 1283 (Fed. Cir. 1992) (in deciding title required under Saline Water Conversion Act, title obtained from inventor even though no evidence inventor required to assign rights to employer.)

²⁶ 35 U.S.C. §203.

²⁷ It should be noted that this march in provision is very often included, in some form, in other, non-procurement contracts since the provision has such a strong public policy basis. However, the march in provision in these non-procurement contracts can at least be more narrowly crafted to reflect the true investment by the Government.

prime contractor does not receive the benefit of the Government's rights in subject inventions. However, while not the beneficiary of the subject invention, the prime is also required to ensure that the subcontractor complies with the clause included in the subcontract. Since the prime is responsible, the Government will invoke its withholding right to ensure the prime forces the subcontractor to perform the necessary reporting under the clause.

contract vehicles in which the Bayh-Dole clauses are not mandatory.

F. AUTHORIZATION AND CONSENT

While there are many issues of concern to contractors in relation to the Bayh-Dole clauses, not all of the patent clauses are as burdensome to contractors. Especially for research and development contracts, the standard terms and conditions do have beneficial clauses of interest to the contracting community. One such clause is an authorization and consent clause, contained in FAR 52.227-1, by which the Government assumes the liability for the contractor's having used a third party's patented invention. When this provision is included, the third party has no recourse against the contractor, and instead must file a claim under 28 U.S.C. §1498(a). Moreover, the contractor is not generally liable for the infringement during a research and development contract.²⁸ As such, contractors performing research and development work are able to avoid substantial liability and the threat of injunction due to patent infringement when performing a research and development contract on behalf of the Government. Given the benefit of these particular clauses, even contractors performing work under non-procurement agreement should consider having these standard provisions included.

CONCLUSION

When entering into a standard procurement vehicle with the Government to perform, even tangentially, research and development, it is important to recognize that the Government requires the contractor to take certain actions to protect the Government and the taxpayer. While certain of these provisions are relatively intuitive and exist in normal commercial contracting, other provisions require advanced planning in order to ensure compliance. Moreover, contractors need to realize that these other provisions reflect a number of social and public policies, and will be enforced in court if there is a dispute. However, with sufficient planning, contractors can implement internal patent policies which account for these various requirements or have the choice of only performing work using alternate

²⁸ FAR 27.201-2(b) & 27.203-1(b)(1).

**STEIN, McEWEN
& BUI LLP**

About us ...

ADDRESS:

1400 EYE STREET, N.W.
SUITE 300
WASHINGTON, DC
20005

PHONE:

202.216.9505

FAX:

202.216.9510

E-MAIL:

EMAIL@SMBIPLAW.COM

Stein, McEwen & Bui, LLP is a full service intellectual property law firm with an emphasis on intellectual property creation and maximization. With a diverse clientele, including large multinational corporations, as well as small to midsize domestic and international companies, the attorneys of Stein, McEwen & Bui, LLP have worked with and counseled clients on the use of intellectual property as a tool for maximizing the protection of their research and development efforts.

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