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# Is the Federal Circuit's Test for Enhanced Damages too Rigid?

*Halo Electronics Inc. v. Pulse Electronics, Inc.*, S.Ct. No. 14-1513 (cert. granted)  
*Stryker Corp. v. Zimmer Inc.*, S.Ct. No. 14-1520 (cert. granted)

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# Overview

The U.S. Supreme Court has agreed to consider whether the Federal Circuit's two part test for allowing enhanced damages in patent cases is too restrictive on the discretion of the district courts.

# 35 U.S.C § 284

Upon finding for the claimant the court shall award the claimant damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court.

When the damages are not found by a jury, the court shall assess them. **In either event the court may increase the damages up to three times the amount found or assessed.** Increased damages under this paragraph shall not apply to provisional rights under section 154(d) of this title.

The court may receive expert testimony as an aid to the determination of damages or of what royalty would be reasonable under the circumstances.

# Current Test

- Two part test
  - Patentee must establish
    - (1) by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent, and
    - (2) only if (1) is satisfied, that this objectively-defined risk was either known or so obvious that it should have been known to the accused infringer.



*Halo Electronics Inc. v. Pulse Electronics, Inc.,*  
S.Ct. No. 14-1513 (*cert. granted*)



# Questions Presented

- First Question

- Whether the Federal Circuit erred by applying a rigid, two part test for enhancing patent infringement damages under 35 U.S.C. § 284, that is the same as the rigid two-part test this Court rejected last term in *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 134 S. Ct. 1749 (2014) for imposing attorney fees under the similarly-worded 35 U.S.C. § 285

- Second Question

- Related to “sell” or “offer to sell”
  - *Cert* was not granted as to this question

# Parties

- Petitioner

- Halo Electronics, Inc.

- Halo supplies electronic components
    - Has several patents directed to surface mount electronic packages containing transformers for mounting on printed circuit boards inside electronic devices including computers and routers

- Respondents

- Pulse Electronics, Inc. and Pulse Electronics Corp.

- Pulse supplies electronic components including surface mount electronic packages
    - Most delivered abroad, but some delivered to companies in the U.S.

# Pulse's activities

- Domestic
  - Pricing negotiations occurred in U.S. with Cisco
  - Pulse shipped products to U.S. customers
  - Products shipped abroad were incorporated into products coming back into the U.S.
- Abroad
  - Purchase orders were received at sales offices abroad based on negotiated prices
  - Products were shipped from manufacturing facilities abroad to purchasers abroad



# Timeline

- 1998 - Pulse allegedly knew of Halo patents
- 2002 - Halo sends two letters offering licenses without accusing of infringement
  - Pulse engineer spends two hours reviewing patents and determined invalid over Pulse products
  - Does not seek opinion of counsel
- 2007 - Halo sues Pulse for patent infringement
- 2010 - Dist. Ct (Nev.) grants summary judgment motion that Pulse's products delivered outside of U.S. do not infringe

## Timeline (continued)

- 2012 – Jury Trial
  - Pulse directly infringed on products shipped to the U.S.
  - Pulse induced infringement with products shipped outside of U.S. but ultimately imported into U.S.
  - **Highly probable that infringement was willful**
  - Halo patents not invalid for obviousness
  - Awards 1.5 million in reasonable royalty

# Timeline (continued)

- 2012 – Post Trial
  - Dist. ct. concludes that objective component of willfulness inquiry is not satisfied because Pulse “reasonably relied on at least its obviousness defense” and unsuccessful obvious defense was not “baseless”
  - Pulse’s infringement was not willful
- 2013 - Halo appeals to Federal Circuit
- 2014 – Opinion of Court Issued

## Timeline (continued)

- March 23, 2015 – Petition for panel hearing and rehearing *en banc* denied
- June 22, 2015 – Petition for Writ of Certiorari
- August 24, 2015 – Brief in Opposition
- September 3, 2015 – Reply of Petitioner



## Timeline (continued)

- October 19, 2015 – Petition granted limited to question 1 presented
  - Consolidated with *Stryker Corp. v. Zimmer, Inc.*
- February 23, 2016 – Oral Arguments

# Federal Circuit

- Willfulness (citing *In re Seagate Tech. , LLC* 497 F.3d 1360 (Fed. Cir. 2007) (*en banc*))
  - First, must show by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent
  - Second, if threshold objective standard is satisfied, the patentee must also demonstrate that this objectively-defined risk (determined by the record developed in the infringement proceeding) was either known or so obvious that it should have been known to the accused infringer
- Objective prong subject to *de novo* review (citing *Bard Peripheral Vascular, Inc. v. W.L. Gore & Assocs., Inc.*, 682 F.3d 1003 (Fed. Cir. 2012))

# Halo's Arguments

- Pulse did not rely on any invalidity defense pre-suit when selling accused products because defense was developed after suit filed in 2007
- Engineer's review in 2002 was only cursory and did not consider review in assessing whether infringing a valid patent
- Dist. ct. erred in holding objective prong not met simply because Pulse raised a non-frivolous obviousness defense

# Pulse's Arguments

- Dist. ct. properly considered post-suit obviousness defense to evaluate objective risk
- 2002 letters did not allege infringement
- Obviousness defense presented at trial raised substantial question of invalidity



# Holding

- In light of the record as a whole, panel agreed with the dist. ct. that Pulse's obviousness defense was not objectively unreasonable
- Accordingly, never gets to second prong of test

# Concurring Opinion

- Believes that it is time for full court to reevaluate standard for imposition of enhanced damages in light of Supreme Court's recent decisions in *Highmark Inc. v. Allcare Health Management Systems, Inc.*, 134 S. Ct. 1744 (2014) and *Octane Fitness*
- Two prong test for willfulness is analogous to test Fed. Cir. used for the awards of attorneys' fees under 35 U.S.C. § 285
- Both tests predicated on interpretation of *Professional Real Estate Investors, Inc. v. Columbia Pictures Industries, Inc.* ("PRE"), 508 U.S. 49 (1993)
  - *Octane Fitness* held that interpretation of *PRE* was incorrect as standard was crafted as narrow exception for "sham" litigation to avoid chilling exercise of First Amendment right to petition government for redress of grievances with the threat of antitrust liability

# Concurring Opinion (continued)

- Essentially provides roadmap to challenge appropriateness of the two prong test

*Stryker Corp. v. Zimmer Inc.,*  
S.Ct. No. 14-1520 (*cert. granted*)





# Questions Presented

- First Question

- Has the Federal Circuit improperly abrogated the plain meaning of 35 U.S.C. § 284 by forbidding any award of enhanced damages unless there is a finding of willfulness under a rigid, two-part test, when this Court recently rejected an analogous framework imposed on 35 U.S.C. § 285, the statute providing for attorneys' fee awards in exceptional cases?

- Second Question

- Does a district court have discretion under 35 U.S.C. § 284 to award enhanced damages where an infringer intentionally copied a direct competitor's patented invention, knew the invention was covered by multiple patents, and made no attempt to avoid infringing the patents on that invention?
  - *Cert* was not granted as to this question

# Parties

- Petitioners

- Stryker Corp., Stryker Puerto Rico, Ltd. and Stryker Sales Corp. (collectively (Stryker))
  - Provides orthopedic pulsed lavage devices
  - Several patents directed to pulsed lavage devices issued between 2000 and 2006 based on application filed in 1993

- Respondents

- Zimmer, Inc., Zimmer Surgical, Inc., and Zimmer Orthopaedic Surgical Products
  - Provides portable pulsed lavage devices
  - In 1998 developed Pulsavac Plus range of products. Peak of \$55 million in annual sales in 2007

# Timeline

- 2010 – Stryker sues Zimmer for patent infringement
  - Dist. ct. of Western District of MI grants partial summary judgment of infringement on two patents
  - Jury trial on infringement of 1 claim in another patent, invalidity defenses
    - Found products infringed claim and all asserted claims were valid
    - Awarded \$70 million in lost profits
    - Found willfully infringed all three patents
- 2013 – Post Trial
  - Dist. ct. issues order rejecting Zimmer's JMOL including issue of willful infringement

## Timeline (continued)

- 2013 – Zimmer appeals to Federal Circuit
- 2014 – Opinion Issued
- March 23, 2015 – Revised Opinion Issued and denies petition for rehearing *en banc*
- June 22, 2015 – Petition for Writ of Certiorari
- July 24, 2015 – Brief in Opposition
- August 6, 2015 – Reply of Petitioner



## Timeline (continued)

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- Objective prong subject to *de novo* review (citing *Bard Peripheral Vascular, Inc. v. W.L. Gore & Assocs., Inc.*, 682 F.3d 1003 (Fed. Cir. 2012))

# Holding

- Dist. ct. failed to undertake an objective assessment of Zimmer's specific defenses to Stryker's claims.
  - Summarily asserted that jury heard testimony that Zimmer "all but instructed its design team to copy Stryker's products"
  - Pioneering nature of patents and secondary considerations made it dramatically less likely that Zimmer's invalidity arguments were reasonable
- An objective assessment of the case shows that Zimmer presented reasonable defenses to all of the asserted claims.
  - Infringement came down to claim construction in two patents where Zimmer's interpretation of the terms was not unreasonable based on plain meaning of the term
  - Invalidity with respect to third patent was based on combination of references used by Examiner in a related application

*Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, 134 S. Ct. 1749 (2014)





# Question presented

- Does the Federal Circuit's promulgation of a rigid and exclusive two-part test for determining whether a case is "exceptional" under 35 U.S.C. § 285 improperly appropriate a district court's discretionary authority to award attorney fees to prevailing accused infringers in contravention of statutory intent and this Court's precedent, thereby raising the standard for accused infringers (but not patentees) to recoup fees and encouraging patent plaintiffs to bring spurious patent cases to cause competitive harm or coerce unwarranted settlements from defendants?

## 35 U.S.C. § 285

- The court in exceptional cases may award reasonable attorney fees to the prevailing party.

# Exceptional Case

- According to *Brooks Furniture Mfg., Inc. v. Dutailier Int'l, Inc.*, 393 F.3d 1378 (2005), a case was deemed exceptional under 35 U.S.C. § 285 in two limited circumstances:
  - When there has been some material inappropriate conduct, typically during litigation or securing the patent
  - When the litigation is both brought in subjective bad faith and objectively baseless
    - Objectively baseless – so unreasonable that no reasonable litigant could believe that it would succeed
    - Subjective bad faith – only if plaintiff actually knows that it is objectively baseless
- Must show by clear and convincing standard because of presumption that assertion of infringement is made in good faith

# Holding

- Plain meaning - Exceptional case is simply one that stands out from others with respect to the substantive strength of a party's litigating position (considering both the governing law and facts of the case) or the unreasonable manner in which the case was litigated
- Dist. cts. can determine whether case is exceptional considering the totality of the circumstances
- Proof of entitlement of fees is preponderance of evidence standard



# Rationale

- Historically, 35 U.S.C. § 285 was interpreted under a totality of circumstances test, including by the Federal Circuit
- First category is largely independently sanctionable conduct
  - Statute does not impose sanctionable standard on the meaning of exceptional
- Second category is based on improper understanding of *PRE*
  - Standard for *PRE* finds no basis in 35 U.S.C. § 285
    - Involved an exception to antitrust law that defendants are immune from antitrust liability for engaging in conduct, including litigation, aimed at influencing decision making by the government, namely if litigation was a “sham litigation” in an attempt to directly interfere with business relationships of a competitor
    - Narrow exception to avoid chilling the exercise of the First Amendment to petition the government to address grievances
    - Fee shifting provisions less likely to chill the exercise of the First Amendment

# Consolidated Cases



# Question Presented

- Halo
  - Whether the Federal Circuit erred by applying a rigid, two part test for enhancing patent infringement damages under 35 U.S.C. § 284, that is the same as the rigid two-part test this Court rejected last term in *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 134 S. Ct. 1749 (2014) for imposing attorney fees under the similarly-worded 35 U.S.C. § 285
- Stryker
  - Has the Federal Circuit improperly abrogated the plain meaning of 35 U.S.C. § 284 by forbidding any award of enhanced damages unless there is a finding of willfulness under a rigid, two-part test, when this Court recently rejected an analogous framework imposed on 35 U.S.C. § 285, the statute providing for attorneys' fee awards in exceptional cases?

# Halo's Arguments on Writ

- 35 U.S.C. § 284 gives dist. ct. flexibility to balance all relevant facts when deciding to enhance damages
- Federal Circuit has no support for its application of 35 U.S.C. § 284
- U.S. Supreme Court should restore enhanced patent damages law to the flexible inquiry under 35 U.S.C. § 284



# Flexibility

- 35 U.S.C. § 284 text is plain and broad
  - The court may increase the damages up to three times the amount found or assessed
- Evolution of damages text
  - 1790 Patent Statute – limited to actual damages
  - 1793 Patent Act – at least three time the price patentee has sold or licensed
  - 1800 Patent Act – a sum equal to three times actual damages
  - 1836 Patent Act – power of court to render judgment for any sum above the amount found by verdict, but not to exceed three times the amount thereof based on circumstances
  - 1870 Patent Act – similar to 1836
  - 1946 Patent Act – similar to 1870
  - 1952 Patent Act – current language

# Flexibility (continued)

- Text is “inherently flexible”
  - *Octane Fitness* found similar text in 35 U.S.C. § 285 “inherently flexible”
  - Gives courts the freedom to consider all relevant circumstances in determining whether to enhance damages
- Supreme Court has approved enhancement whenever circumstances require it
  - Instances of bad faith infringement
  - Infringer imposes unnecessary expense and burden on the patent holder
  - Even if patent’s validity “is by no means free from doubt” if there are other aggravating circumstances

# Flexibility (continued)

- Factors considered before Federal Circuit adopted two part test in *In re Seagate*
  - Deliberate copying
  - Once knew of patent protection, investigated scope of patent and formed good-faith belief that it was invalid or not infringed
  - Behavior as party to litigation
  - Defendant's size and financial condition
  - Closeness of the case
  - Duration of misconduct
  - Remedial action take
  - Defendant's motivation for the harm
  - Attempt to conceal misconduct
- Based on *Read Corp. v. Portec, Inc.*, 970 F.2d 816 (Fed. Cir. 1992)



# Lack of Support

- Federal Circuit departed from the statutory text and historical application in series of decisions culminating in *In re Seagate*
  - First limited enhancement to cases of only willful infringement
    - *Jurgens v. CBK, Ltd.*, 80 F.3d 1566 (Fed. Cir. 1996)
  - *In re Seagate* imported test for willfulness based on a case interpreting Fair Credit Reporting Act (*Safeco Insurance Co. of Am. v. Burr*, 551 U.S. 47 (2007))
    - Similar error corrected by U.S. Supreme Court in *Octane Fitness*
  - Setting willfulness as necessary predicate conflicts with U.S. Supreme Court precedent which considers whether acted in good faith or has caused unnecessary expense and injury
- Bypasses historic totality of circumstances test thereby allowing even most malicious infringer to avoid enhancement by developing a non-sham defense



# Lack of Support (continued)

- No legal basis exists for automatically allowing willful infringer to avoid enhancement simply because of a later developed, reasonable defense that is ultimately unsuccessful
- Clear and convincing evidence standard is not supported
  - 35 U.S.C. § 284 imposes no heightened burden
  - Departs from typical burden in civil cases which is preponderance of the evidence standard – *Octane Fitness*
- Federal Circuit's review of objective recklessness *de novo* is counter to plain language of 35 U.S.C. § 284 “may” increase damages

# Proper Standard

- Restore enhanced damages under 35 U.S.C. § 284 to flexible standard consistent with text
  - Consider *Read* factors
  - Dist. ct. review under abuse of discretion standard

# Stryker's Arguments on Writ

- Stryker's Arguments are very similar to those presented by Halo
- In discussing *Read* factors, Stryker indicates how factors can still protect infringers that acted in good-faith
  - Deliberate copying
  - Once knew of patent protection, investigated scope of patent and formed good-faith belief that it was invalid or not infringed
  - Behavior as party to litigation
  - Defendant's size and financial condition
  - Closeness of the case
  - Duration of misconduct
  - Remedial action take
  - Defendant's motivation for the harm
  - Attempt to conceal misconduct

# United States *Amicus* Brief

- Text and history of 35 U.S.C. § 284 make clear that enhanced damages are appropriate to punish intentional, willful or otherwise egregious conduct
  - Draws a distinction between ordinary infringement
- *In re Seagate* practical effect is to bar a district court from awarding enhanced damages even against an infringer that deliberately copies a patented device, while subjectively believing that conduct constitutes unlawful infringement, so long as the infringer can manage a non-frivolous defense at trial



# United States *Amicus* Brief

- Facts relevant to enhanced damages must be proved under preponderance of the evidence standard that generally governs patent litigation
- Dist. ct. grant or denial for enhanced damages should be reviewed under abuse of discretion standard

# Questions and Discussion

