

United States

Analysing the impact of the Supreme Court's *eBay* decision

It has been more than a year since the Supreme Court issued its opinion in *MercExchange v eBay*. In that opinion, the court overturned the Federal Circuit's ruling that once infringement is found in a patent case, the general rule is "that courts will issue permanent injunctions against patent infringement absent exceptional circumstances".

The *eBay* decision

In overturning the Federal Circuit, the Supreme Court held that a patent holder seeking a permanent injunction must satisfy a four-factor equitable test that the US courts have historically applied when considering requests for injunctive relief:

- Did the plaintiff suffer irreparable injury?
- Would remedies at law (eg, financial damages) adequately redress the injury?
- Does the balance of hardships favour injunctive relief?
- Would equitable relief serve the public interest?

As the Supreme Court rejected the Federal Circuit's general rule regarding injunctions, the case was vacated so that the district court could apply the four-factor test.

Although the court's decision was unanimous, concurring opinions reflected a theoretical split between the justices regarding the hypothetical types of patentee that might be entitled to injunctions. Justice Thomas observed that patentees who work in university settings often lack the resources to commercialise their inventions and must therefore rely on licensing to realise the value of their patents. Therefore, such patentees should not be categorically denied injunctions. Justices Kennedy, Stevens, Souter and Breyer concurred in the opinion, noting that the modern economics of patents have changed and that many non-invention practising patent holders use their patents solely for licensing fees,

sometimes at "exorbitant" rates. In those cases, the Kennedy concurrence observed that "legal damages may well be sufficient to compensate for infringement and an injunction may not serve the public interest".

Kennedy and his concurring colleagues questioned whether financial damages might not be sufficient for these types of company: "When the patented invention is but a small component of the product the companies seek to produce and the threat of an injunction is employed simply for undue leverage in negotiations, legal damages may well be sufficient to compensate for the infringement and an injunction may not serve the public interest." Kennedy also noted the new economic reality of business method patents, with their "potential vagueness and suspect validity", as potentially affecting the outcome of the four-factor test in such cases – that is, perhaps injunctive relief should not be granted when the underlying patents are on shaky ground.

Chief Justice Roberts, in a concurrence joined by two other justices, suggested that the courts take a lesson from the history books. Notably, this lesson points in a different direction to the Kennedy concurrence. Roberts held that although the four-factor test should be applied, the reason that injunctions are generally granted in patent infringement cases is that it makes sense. The patent laws grant patentees the right to exclude others from practising the invention during the life of the patent (ie, through infringement suits) and it is difficult to protect that right through a financial award.

In the months following the Supreme Court's opinion, commentators argued about the potential impact of the opinion on patent injunctions. Most agreed that it would be up to the district courts to apply the four-factor test on a case-by-case basis.

The application of *eBay*

Cases involving non-competitors

Since *eBay*, district court decisions have largely

confirmed that competitors in industry have a significantly greater chance of obtaining an injunction than non-competitors (sometimes referred to as patent trolls).

Prior to the *eBay* ruling, patent holders enjoyed an almost automatic right to injunctive relief upon the finding that a valid patent was infringed. In *eBay* the Supreme Court modified that right by requiring plaintiffs to demonstrate, through four equitable factors, the fairness of an injunction on a case-by-case basis.

The post-*eBay* decisions dealing with the injunction issue commenced with *z4 Technologies Inc v Microsoft Corp* (ED Tex, No 6:06-CV-142, 6/14/06) in the US District Court for the Eastern District of Texas. In that case, Judge Davis ruled that the principles of equity set forth in the four-factor test did not call for an injunction against Microsoft, notwithstanding a jury finding Microsoft liable for wilfully infringing z4's patents relating to product activation software. The ruling appeared to signal a major shift in patent litigation practice as it was the first indication of how the *eBay* ruling could potentially affect defence strategies in patent litigation.

The facts of the *z4 Case* are instructive. In April 2006 a Texas jury found that Microsoft and Autodesk had wilfully infringed two of z4's patents covering methods for limiting the unauthorised use of computer software. Both Microsoft and Autodesk use the anti-piracy program in some of their products. The jury ordered the two companies to pay z4 \$133 million in damages.

z4 requested that an injunction be entered against Microsoft. In refusing z4's request, the court applied the traditional four-factor test recommended by the High Court, concluding that z4 would not suffer irreparable harm in the absence of a permanent injunction. The court began its analysis by rejecting z4's argument that a verdict of infringement raises a rebuttable presumption of irreparable harm. Instead, the court diligently analysed the facts relating to each of the four equitable factors, providing a roadmap of possible considerations in future hearings relating to questions of injunctive relief.

Davis ruled that because Microsoft used the infringing technology as only a small component of its own software, z4 would not lose profits, brand-name recognition or market share as a result of Microsoft's infringement: "[I]t is not likely that any consumer of Microsoft's Windows or Office software purchases these products for their product activation functionality." In justifying the denial of an injunction, Davis also cited Kennedy's comment in *eBay* that if a patented invention is but a small component of the infringing product, monetary damages should be sufficient compensation. In this case, the large damages award (one of the largest

ever in a patent case in this jurisdiction) convinced the court that monetary compensation was adequate. The court rejected the argument that the existence of a right to exclude (a basic right of patent ownership) implied that monetary damages were inadequate to compensate for patent infringement. The court acknowledged the possible scenario of a violation of the right to exclude resulting in damages not compensable by monetary award, but found that this was not such a case. Significantly, Davis explained that if z4 were directly competing with Microsoft in the product activation software market, irreparable harm might exist because Microsoft might be selling product to potential z4 customers.

Analysing the final two equitable factors, the court concluded that the balance of hardships tilted in favour of Microsoft. The court largely based this finding on the possibility of Microsoft having to redesign and re-release all its Office software products, which are currently distributed in 450 variations in 37 languages. Its Windows product currently has 600 variations in more than 40 languages. The court ruled that the hardship of redesigning these software products outweighed any hardships that z4 would suffer in the absence of an injunction.

Finally, Davis's ruling cited possible harm to the public interest if the court were to enjoin Microsoft: "Microsoft's Windows and Office software products are likely the most popular software products in the world. Accordingly, the public interest is likely to be disserved if a permanent injunction were entered against Microsoft."

Applying the four equitable factors to the circumstances presented here, the court concluded that imposition of a permanent injunction was not appropriate. The ruling signalled a change in the US law surrounding injunctions in patent cases. Prior to the *eBay* ruling, BlackBerry maker Research In Motion failed to persuade a court to stop an injunction based on the inconvenience that its millions of users would have faced had the company been enjoined from offering its wireless email service.

Several other district courts have similarly denied applications for post-*eBay* permanent injunctions where the adjudged infringer was not a competitor of the prevailing patentee.

Cases involving competitors

In contrast, the district courts have been much more willing to enjoin infringing activities where the adjudged infringer has directly competed with the party seeking the permanent injunction.

TiVo v Echostar, also from the Eastern District of Texas,

provides a good example. In that case Tivo moved for a permanent injunction following a finding of infringement, seeking to prevent Echostar from selling its infringing cable box digital video recorders (DVRs).

Echostar's direct competition with TiVo was a crucial factor in Judge Folsom's decision to grant the permanent injunction. Indeed, Folsom stated that a "key consideration in finding that the plaintiff suffers irreparable harm" was the loss of market share in a newly established and highly competitive market. The court found it important that DVR consumers were "sticky customers" who tended to remain with the company from which they first obtained a DVR. As a result, the injury caused by the infringement resulted in long-term customer loss.

It is clear from Folsom's opinion that irreparable injury can be established in highly competitive markets where one competitor successfully demonstrates that another competitor is infringing its patents. Indeed, several other district courts have granted permanent injunctions post-*eBay* following a finding of infringement and validity in situations where the infringer was a direct competitor.

For a short time it appeared that the rules regarding injunctions were becoming clear. However, a recent case, again from the Eastern District of Texas, raises new questions. The Commonwealth Scientific and Industrial Research Organisation (CSIRO), which is Australia's primary governmental research group, holds and licenses hundreds of US patents in many different fields, including wireless networking. CSIRO does not manufacture products, so its function is purely research, testing and licensing.

CSIRO obtained a patent relating to a process it had created that corrected a major technical defect that had hindered efforts to develop wireless technology. CSIRO actively licensed its technology, which became a core part of 802.11a and 802.11g wireless standards. Both standards remain popular today.

CSIRO sought to enforce its patent against a number of major companies in the wireless networking field, including Belkin, Dell, Apple, Microsoft, Intel, Netgear, Hewlett-Packard and D-Link. Buffalo Technologies Inc manufactures wireless network products, including routers, antennas and adaptors that use the 802.11a and 802.11g standards. Buffalo's products are sold to a variety of distributors and at retail outlet stores.

In 2006 CSIRO sued Buffalo in the Eastern District of Texas, alleging infringement of its patent. In November 2006 Davis found the patent infringed by Buffalo invalid. CSIRO subsequently moved for a permanent injunction. Given CSIRO's business model, many were dubious of its chances.

Buffalo opposed CSIRO's motion by arguing that because Buffalo was not a direct competitor, it could not prove irreparable harm under the *eBay* enquiry. Davis rejected this position and granted the injunctive relief. In doing so, Judge Davis first quoted from *eBay*, which warned against "creating broad classifications": "[S]ome patent holders, such as university researchers or self-made inventors, might reasonably prefer to licence their patents, rather than undertake efforts to secure the financing necessary to bring their work to market themselves. Such patent holders may be able to satisfy the traditional four-factor test, and we see no basis for categorically denying them the opportunity to do so."

Davis then explained that CSIRO had demonstrated that its harm was not merely financial. Having its patents challenged in litigation not only impugned CSIRO's reputation as a leading scientific research entity, but also forced CSIRO to divert millions of dollars away from research and into litigation costs. According to Davis, these lost opportunities cost CSIRO in potentially valuable fields that it could otherwise have pursued, thus leading to irreparable harm.

This reasoning was significant because it gave hope to non-patent practising universities and research organisations, which often conduct business in a manner similar to CSIRO. Davis' opinion restored to universities and research organisations much of the bargaining power that many thought had been taken away by the *eBay* ruling.

Unclear future

The law relating to patent injunctions is still developing. For example, the ruling in the *CSIRO Case* is too narrow to result in an injunction for non-practising licensing organisations or for venture capital groups that acquire and enforce patents. The 'diversion of resources' argument accepted by Davis is unlikely to apply to organisations that cannot demonstrate substantial ongoing research activities.

Nevertheless, there are potential arguments that have yet to be considered by the courts relating to irreparable injury suffered by individual inventors whose patents are infringed. For example, evidence that others in an industry may refuse reasonable offers of a licence and continue to infringe a valid patent may be enough, in certain circumstances, to demonstrate irreparable harm.

The law relating to injunctions in patent cases will undoubtedly continue to evolve as new factual scenarios and new arguments are presented by creative patent holders.

Blair Jacobs focuses his practice on IP litigation. He has achieved favourable results for both plaintiffs and defendants in patent infringement, trade secret, trademark, copyright and other commercial disputes. Mr Jacobs represents clients in a variety of technical areas, including fibre-optic telecommunications equipment, photolithographic equipment for imaging semi-conductor devices, internet technologies, iris recognition security devices, computer hardware and software, medical devices and pharmaceutical drugs. He graduated from the University of Richmond School of Law.

Blair M Jacobs

Partner, Washington DC

Tel +1 202 383 0773

Email blair.jacobs@sablaw.com

Sutherland Asbill & Brennan LLP

United States

