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UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

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KNORR-BREMSE SYSTEME FUER NUTZFAHRZEUGE GMBH,

Plaintiff-Cross Appellant,

v.

DANA CORPORATION,

Defendant-Appellant,

and

HALDEX BRAKE PRODUCTS CORPORATION  
AND HALDEX BRAKE PRODUCTS AB,

Defendants-Appellants.

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*En Banc Appeal*

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**BRIEF OF *AMICUS CURIAE* PUBLIC PATENT FOUNDATION**

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November 3, 2003

CERTIFICATE OF INTEREST

Counsel for *amicus curiae* Public Patent Foundation certifies the following:

1. The full name of every party or amicus represented by me is:

Public Patent Foundation

2. The name of the real party in interest (if the party named in the caption is not the real party in interest) represented by me is:

Public Patent Foundation

3. All parent corporations and any publicly held companies that own 10 percent or more of the stock of the party or amicus curiae represented by me are:

None

4. The names of all law firms and the partners or associates that appeared for the party or amicus now represented by me in the trial court or agency or are expected to appear in this court are:

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## STATEMENT OF INTEREST

Amicus Curiae Public Patent Foundation (“PubPat”) is a not-for-profit corporation that represents the public’s interest in having free markets and civil liberties unrestrained by wrongly issued patents and unsound patent policy. PubPat provides those persons and businesses otherwise deprived of access to the system governing patents with representation, advocacy and education.

This brief is submitted in response to the Court’s September 29, 2003 Order with the consent of the parties.\*

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\* No part of this brief was authored by counsel for any party and no party, person, or organization contributed besides *amicus curiae* and its counsel.

## ARGUMENT

### I. THE *UNDERWATER DEVICES* DUTY CONFLICTS WITH SOUND PATENT POLICY

#### A. Intentional Ignorance of Patents Undermines Patent Quality

Our patent system is in crisis because the PTO is granting too many patents that should never have been issued. *See* David Streitfeld, *Note: This Headline is Patented*, L.A. Times, February 7, 2003 (quoting James Rogan, Director of the PTO, “This is an agency in crisis, and it's going to get worse”; further stating “‘Crisis is a strong word,’ the American Intellectual Property Law Association has noted in correspondence, ‘but we believe that it aptly describes the situation’”); John R. Allison & Mark A. Lemley, *Empirical Evidence on the Validity of Litigated Patents*, 26 AIPLA Q.J. 185, 205-206 (1998) (demonstrating that 46% of patents litigated to judgment on validity issues are held invalid).

The crisis in patent quality is devastating to innovation and competition. *See* *To Promote Innovation: The Proper Balance of Competition and Patent Law & Policy*, Federal Trade Commission, October 2003, available at <http://www.ftc.gov/reports/index.htm> (“FTC Report”) at 37, 54, Ch. 5 at 12. A wrongly issued patent “withdraws what is already known into the field of its monopoly and diminishes the resources available to skilful men.” *Great Atlantic & Pacific Tea Co. v. Supermarket*

*Equipment Corp.*, 340 U.S. 147, 152-153 (1951). The *Underwater Devices* duty to seek an exculpatory opinion of counsel upon mere awareness of a patent exacerbates the patent quality crisis.

One reason the PTO issues invalid patents is that it is not aware of material prior art. Searching prior art in the areas of software, the Internet and business methods is particularly challenging. See FTC report at 40, 46. The PTO therefore increasingly depends on applicants' duty to identify for the examiner all material prior art of which they are aware. The *Underwater Devices* rule discourages applicants who also practice related technology from searching for prior art patents to disclose to the Patent Office, because they might, in the process, become aware of patents that trigger the duty to avoid infringement by seeking an opinion of counsel. See FTC Report Chapter IV at 29, Chapter V at 49. See, e.g., Edwin H. Taylor and Glenn E. Von Tersch, *A Proposal to Shore up the Foundations of Patent Law that the Underwater Line Eroded*, 20 *Hastings Comm. & Ent. L. J.* 721, 737 (1998); Dennis Fernandez, *Move Over Letterman, Top 10 Most Common IP Management Mistakes for New Companies*, 4 *No. 3 Patent Strategy & Mgmt.* 3 (2003).

Encouraging ignorance of patents undermines one of patent laws' most important purposes, to teach the public the useful knowledge contained



in patents. As a result, when these companies apply for patents, they disclose fewer prior art patents, resulting in examiners being less aware of the state of the art, causing them to allow applications that should be rejected. The Court should clarify the *Underwater Devices* rule so as encourage companies to search and read patents.

B. The *Underwater Devices* Duty Disproportionately Affects Small Businesses

In addition to exacerbating the patent quality crisis, the *Underwater Devices* duty is unfairly burdensome for small businesses. Originally stated in cases involving large, sophisticated defendants with good reasons to take a specific patent seriously, the “duty to avoid infringement” has become equated with a “duty to hire outside patent counsel” whenever a patent comes to a company’s attention, regardless of the company’s resources or any other circumstances. See Mark A. Lemley & Ragesh K. Tangri, *Ending Patent Law’s Willfulness Game*, forthcoming 2003, 18 Berkeley Tech. L.J. \_\_\_, n. 16 and accompanying text; *Vulcan Eng’g. Co., Inc. v. Fata Aluminium, Inc.*, 278 F.3d 1366, 1378 (Fed. Cir. 2002) (due care exercised “usually by seeking the advice of competent and objective counsel and receiving exculpatory advice”). This is fiscally difficult for many small businesses, often the leaders in advancing technology, who must bear a greater exposure to willful infringement than their larger competitors.

Reading the duty to avoid infringing patents to require every company, regardless of size, to hire patent counsel to prepare an opinion for each patent learned of, is simply unfair and unrealistic. Instead, the Court should make it clear that the duty to avoid infringement arises from a totality of the circumstances, and that the actions required by the duty depend on those circumstances, including the size of the company, the nature of the patent, the specificity of the infringement allegations, and the company's ability to understand the patent and form opinions about validity and infringement without counsel.

#### C. Predator Patentees Extort Small Businesses Which Cannot Afford to Challenge Patent Validity

Today, holders of wrongly issued patents on aspects of e-commerce, software and business methods use the threat of receiving enhanced damages to extort royalties where none are justified. Contingency fee attorneys send out patent notice letters to entire industries, including small businesses, offering licenses for amounts much less than the exposure the recipients face in litigation. *See* FTC Report, Chapter 4 at 40. Such letters are skillfully crafted to trigger the recipient's duty to avoid infringing the patent (exposing the recipient to enhanced damages for willfulness), while not providing declaratory judgment jurisdiction for the recipient to challenge the patent's validity if she wanted.

Rather than risk having to pay enhanced damages, many businesses chose to pay royalties for patents that may very well not be valid or infringed, solely because the royalties demanded are much less than the cost of litigation, and often even less than the cost of an opinion. *See E-commerce Patent Threat*, Chicago Tribune, January 13, 2003, available at <http://www.chicagotribune.com/technology/chi-0301130012jan13,1,2608471.story?coll=> (quoting Sharon Barner, of Foley & Lardner, "that's a significant amount of money when you can settle for \$10,000 or \$15,000."). The availability of enhanced damages and attorneys fees creates an additional "in terrorem" effect forcing recipients of patent notices to write checks instead of reexamination requests or complaints for declaratory judgment of patent invalidity. *See* FTC Report, Chapter IV at 30. The Court should clarify the *Underwater Devices* rule so as encourage companies to challenge questionable patents.

## II. THE ADVERSE INFERENCES ARE IRRATIONAL AND UNJUSTIFIABLY PREJUDICIAL

A patentee bears the burden of proving willful infringement by clear and convincing evidence. *Crystal Semiconductor Corp. v. TriTech Microelects. Int'l., Inc.*, 246 F.3d 1336, 1351 (Fed. Cir. 2001). When a factfinder infers that legal advice was or would have been adverse, however, that burden effectively shifts to the accused infringer. *See* John Dragseth,

*Coerced Waiver of the Attorney-Client Privilege For Opinions of Counsel in Patent Litigation*, 80 Minn. L.Rev. 167, 186-189. Thus, under today's law, a patentee need only show that the infringer knew of the patent and has not produced an exculpatory opinion in order to win on willfulness, because the negative inferences provide the rest of the patentee's prima facie case.

The adverse inferences, however, are just not logical in many cases. In *Kloster Speedsteel*, the Court drew an adverse inference because the defendant had much more information about the patent, the asserted claims, and the basis for the infringement allegation than most companies have when they simply become aware of a patent. Further, the defendant in that case was an international company with the financial ability and patent acumen to hire multiple patent firms in Europe and America, turn to the International Patent Institute in the Hague for certain kinds of research, and develop a worldwide strategy. *Kloster Speedsteel AB v. Crucible, Inc.*, 793 F.2d 1765 at 1578 (Fed. Cir. 1986). Under those circumstances, the Court found defendant's failure to produce exculpatory evidence supported an adverse inference.

But, under different circumstances, an adverse inference would not be rational. There are many reasons why a company might be aware of a patent but not obtain a legal opinion. One is cost. See Ira V. Heffan, *Willful Patent*

*Infringement*, 7 Fed. Cir. Bar J. 115 (1997) at 150 (patent opinions costing up to fifty thousand dollars were financial burden for small businesses). Depending on the nature of the patent and the clarity of the claims, it may not be immediately obvious that there is any risk of infringement. The company, knowing the relevant art in its own field, may be aware of prior art that would invalidate the claims, as the company understands them. Or it may reasonably believe it has a good defense not dependent on patent law. *See State Contracting & Eng'g. Corp. v. Condotte America, Inc.*, 2003 WL 22288180 \*7 (Fed. Cir. 2003) (defeating willfulness because defendant had reasonable belief license covered use of patented technology). *See also Delta X Corp. v. Baker Hughes Prod. Tools, Inc.*, 984 F.2d 410, 419 (Fed. Cir. 1993).

Similarly, a litigant may have good reasons to choose not to waive privilege even if it has an exculpatory opinion. The opinion might disclose business strategies. *See Dragseth* at 187. The opinion might be obsolete in view of subsequent discovery, prior art searches or claim construction rulings. Lemley & Tangri, *Willfulness Game* at 31 n. 87; John F. Lynch, *Risky Business: Coping With a Charge of Willful Infringement*, 4 Sedona Conf. 5:31 at 51 (2003). Such good faith actors do not willfully infringe

patents, and, as such, they should not be exposed to enhanced damages. The adverse inferences, however, do just that.

### III. RAISING A SUBSTANTIAL DEFENSE SHOULD DEFEAT A FINDING OF WILFULLNESS

Precluding a finding a willfulness if an infringer presents a substantial defense would comport with sound patent policy and this Court's precedent. *See Paper Converting Mach. Co. v. Magna-Graphics Corp.*, 745 F.2d 11, 20 (Fed. Cir. 1984) (“[a]n increase in damages for willfulness...is generally inappropriate when the infringer mounts a good faith and substantial challenge to the existence of infringement”); *State Contracting*, 2003 WL 22288180 \*7 (Fed. Cir. 2003) (where defendants raised a substantial defense [...] plaintiff could not prove willfulness by clear and convincing evidence). *See also Read Corp. v. Portec*, 970 F.2d 816 at 829 n.9 (Fed. Cir. 1992) (“A good test that the advice given is genuine and not merely self-serving is whether the asserted defenses are backed up with *viable proof during trial which raised substantial questions*, as here”) (emphasis added). Such a rule comports with sound patent policy because it encourages accused infringers to raise validity and infringement issues, does not prefer certain patentees over others, and does not overly reduce the deterrent against willful infringement.

Under a “Substantial Defense” rule, parties having a good faith belief that an asserted patent is invalid or not infringed would be encouraged to raise such issues instead of licensing the patent out of a fear of being held liable for enhanced damages. In doing so, they would serve the public in at least two ways.

First, accused infringers who prove a patent invalid perform an important public service by correcting the PTO’s errors on their own nickel. *See Lear v. Adkins*, 395 U.S. 653, 670 (1969) (if those “with economic incentive to challenge the patentability of an inventor’s discovery” do not do so, “the public may continually be required to pay tribute to would be monopolists without need or justification”); *Pope Mfg. Co. v. Gormully*, 144 U.S. 224, 234 (1892) (“[i]t is as important to the public that competition should not be repressed by worthless patents as that the patentee of a really valuable invention should be protected in his monopoly”); *see also* FTC Report, Chapter IV at 28. Even those who try but fail to prove a patent invalid perform a public service by narrowing uncertainty as to the patent’s validity, thus encouraging others to respect it. *Kloster Speedsteel*, 793 F.2d at 1581. Therefore, a “substantial defense” should preclude willfulness if an accused infringer presents a good faith argument that a patent is invalid.

The litigants most likely to vigorously challenge a patent's validity are those who have no noninfringement argument because market forces require them to directly copy the patented technology. Such litigants include generic drug manufacturers and information technology companies complying with industry standards. These companies are friends of the consumer. Their copying does not demonstrate laziness, free riding, or lack of creativity. Rather, when they directly copy technology claimed in an invalid patent, they return to the public domain technology impermissibly taken from it. A rule creating greater exposure for "direct copyists" would treat invalidity as an inferior defense to noninfringement, because it would not immunize from enhanced damages parties who (i) have a good faith belief they are not infringing valid patents and (ii) present substantial defenses. As such, a "substantial defense" rule is preferable because it would leave courts discretion to consider the totality of the circumstances and not require them to prefer certain substantial defenses over others.

Second, litigants who raise substantial noninfringement defenses serve the public because their efforts lead to a judicial opinion declaring the patent's metes and bounds, on which the public may rely. Claim construction is often difficult, as demonstrated by the fact that this Court reverses over 30% of district court claim constructions. *See* FTC Report at



53; Christian Chu, *Empirical Analysis of the Federal Circuit's Claim Construction Trends*, 16 Berkeley Tech L.J. 1075 (2001); see also Kimberly A. Moore, *Are District Court Judges Equipped to Resolve Patent Cases?*, 15 Harv. J. L & Tech 1 (2001). As not even judges always correctly construe claim terms, even after full briefing and an adversarial hearing, this Court has recognized that it is unfair to punish parties, even those with specialized counsel, if they err. See *Antonious v. Spalding & Evenflo*, 275 F.3d 1066, 1073 (Fed. Cir. 2002) (reversing sanction where claim construction was wrong but not frivolous). Similarly, it is unfair to expose a party to treble damages simply because its good faith claim construction is wrong. Therefore, a “substantial defense” should exist if an accused infringer presents a good faith argument that a patent is not infringed under a proposed claim construction that is not frivolous, especially if the court finds a disputed claim term ambiguous.

Last, a “Substantial Defense” rule would not meaningfully diminish the deterrent to intentional infringement. The courts could still punish true scofflaws who fail to mount substantial defenses. While it is true that a “substantial defense” rule would reduce the patentees’ opportunities to receive the windfall of enhanced damages, patentees could still seek compensatory damages and injunctive relief, the latter being a much more

important remedy for most patentees than enhanced damages. The rule also would improve patent quality by removing the reasons to avoid patent awareness, and treat small business fairly.

### CONCLUSION

The Court should hold that it is inappropriate to draw an adverse inference regarding willful infringement from a party's not waiving privilege in or not producing exculpatory opinions of counsel. The Court should hold that the duty to avoid infringement does not require obtaining a legal opinion upon merely learning of a relevant patent, without more. Finally, the Court should find that a party that presents a substantial defense should not be found willful.

Dated: November 3, 2003

Respectfully submitted,

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I hereby certify that this brief is double-spaced (except for headings), appears in 14-point Times New Roman type, and contains 2,478 words according to the word processor used to prepare it. It therefore complies with FRAP and Federal Circuit Rules 28, 29 and 32 and this Court's September 29, 2003 Order limiting it to 2,500 words or less.

Dated: November 3, 2003

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Elizabeth H. Rader

## DECLARATION OF AUTHORITY

I, Elizabeth H. Rader, declare as follows:

1. I am an attorney admitted to practice before the United States Court of Appeals for the Federal Circuit.
2. Pursuant to Federal Circuit Rule 47.3(d), I have actual authority to sign this brief and the accompanying Entry of Appearance on behalf of *amicus curiae* Public Patent Foundation.
3. I am entering appearance in this matter and have attached Entry of Appearance (Form 5) for that purpose.

I declare, under the penalty of perjury, that the foregoing is true and correct. Executed this 3rd day of November 2003 at Palo Alto, California.

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NOTICE OF ENTRY

FORM 5

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