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Lies, Damn Lies and Fraud: *BSkyB v. HP Enterprise Services UK Limited*

By Anthony Sourgnes, London

On January 26, 2010, Mr. Justice Ramsey handed down his much-awaited decision in one of the most high-profile pieces of IT litigation in recent years. The litigation—which concerned the implementation of a new CRM system—was heard over 109 hearing days in 2008; the decision runs to approximately 470 pages. Although it offers little that is innovative from a legal perspective, the decision is a good example of how English courts approach the issues of pre-contractual misrepresentation and fraud. It is also a salutary reminder to suppliers and customers alike regarding the potentially far-reaching consequences of statements made in the often tense period leading up to the decision to award a major contract.

Facts

Following a competitive tendering process in 2000, EDS was awarded a contract by Sky—the satellite broadcaster—to design, build, implement and manage a new CRM system. Difficulties set in early, project time frames slipped and the project was in part de-scoped and Sky took over the role of prime system integrator from EDS. Although initially due to go live in March 2002, the relevant functionality was only completed in 2006, by which time, according to Sky, the project budget had blown out from £47.6 million to approximately £265 million. Sky claimed damages in excess of £700 million.

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Pre-Contractual Misrepresentations

(i) Were pre-contractual representations excluded?

A threshold issue arose regarding whether the terms of the agreement entered into between the parties excluded the liability of EDS for pre-contractual misrepresentation. The pre-contractual representations alleged by Sky to have been made by EDS were essentially that EDS had adequate resources necessary for the project, that EDS had carried out a proper estimate of project costs and that EDS had carried out a proper analysis of the amount of time required to carry out the project. Each of these pre-contractual representations was found by the judge to be material to Sky's selection of EDS rather than a rival solution.

Applying standard English law principles of contractual interpretation, the judge found that the "entire agreement" clause contained in the agreement did not operate to exclude claims a party may have had in relation to pre-contractual interpretation. Although the clause did operate to "supersede" prior representations, there was no clear statement of a contractual renunciation of the right of the claimant party to rely on statements made in the course of the negotiations. That right not having been clearly excluded by contractual agreement, Sky was entitled to claim damages arising out of what it alleged to be pre-contractual misrepresentations.

(ii) What were the relevant representations?

Sky claimed that EDS had made a number of representations and that those representations had been made falsely or fraudulently. The principal representations were as follows:

- that: (i) EDS had the personnel with the necessary skills and experience available and reserved for the project and (ii) that EDS personnel with appropriate skill could be made available as and when their particular skills were required and that EDS was ready to start work in July 2000 using such personnel as might be required for the initial stage ("Representations as to Resources").
- that EDS had carried out a proper analysis as to the time to deliver the project and that EDS had reasonable grounds for holding the opinion that the project could be delivered within the timescales referred to in their tender response (i.e., a "go-live" within nine months of project initiation and project completion within 18 months) ("Representations as to Timing").
- that EDS had carried out a proper estimate of the costs for delivering the project and that EDS had reasonable grounds for holding the opinion that the project could be delivered within that budget ("Representations as to Costs").

In addition to the above, Sky also claimed EDS had made representations regarding use of proven technology and methodologies.

(iii) Findings on the representations as to resources

Key to the judge's finding as to what representations, if any, had been made by EDS prior to signature of the Agreement were two statements. The first was the following phrase contained in a letter sent to Sky: "We have the resources and ability to deliver the systems and services you require to meet the financial and budgetary targets you have met." The second was the following phrase appearing in a pre-contractual e-mail: "EDS is ready to start this project as of Monday, July 17. We have the resources reserved for this project."

The judge focused on two issues: (i) was it represented that personnel "were available" or was it only that they "could be made available?" and (ii) was the representation that personnel had "been reserved" a reference to all the personnel for the project only or only those required for the start or initial stage?

The judge found that:

- The reference to EDS having the resources "available" meant no more than that EDS had global resources available to deliver the project;
- The reference to "resources and ability" amounted to no more than a general representation that EDS was making about the organisations having resources which could be made available for the project;
- the reference to the phrase that "EDS has the resources reserved for this project" should not be read out of the overall context in which it was made. In the context in which it was made, the judge found that Sky understood that all the resources for the project could not be reserved at the tender response stage; and
- the nature of large IT projects, during which work definition develops in the course of a project, and the inherent "cone of uncertainty" which will exist at the start of the project, "necessarily means that on large and complex IT projects there is no ability to have resources available or reserved for the whole of that project."

Accordingly, the judge found that there was no representation by EDS that the personnel required for the project, with the necessary skills and experience in the relevant technologies and methodologies, were available and had been reserved for the project. What EDS had represented was that personnel with experience gained from comparable projects could be made available to be used on the project as and when they and their particular skills might be required, a representation which the judge found not to have been false.

(iv) Findings on Representations as to Timing

The judge found that EDS had represented that it had carried out a proper analysis of the amount of elapsed time required to complete the project and had further represented that EDS had reasonable grounds for holding the opinion that it could and would deliver the project within the timescales referred to in its tender response. The judge found that representation to be false, since no "proper analysis" had been carried out nor were there "reasonable grounds" for EDS holding that opinion.

The judge further found that representation to have been made dishonestly by an officer of EDS who knew the representation to be false. The officer in question—the managing director of the relevant business division of EDS and the person who had overall control of EDS's bid response—was found by the judge to have lied under oath and, during the course of the bidding process, had acted dishonestly and with subterfuge. That was a key finding of the judge, and underpinned his ultimate finding that EDS would be liable for the tort of deceit for that misrepresentation.

The finding of fraud opens up the possibility for the judge to award substantial damages to Sky without being constrained by the contractual limitation of liability cap of £30 million.

(v) Findings on Representations as to Costs

The judge found that EDS had indeed made the Representation as to Costs. However, the judge found that, in putting in an estimate of £54 million in its tender response, EDS had carried out a proper estimate of the costs for completing the project and had reasonable grounds for holding the opinion that they could and would deliver the project within that budget.

Breach of Contract Claims

In addition to liability for pre-contractual misrepresentations, the judge also found that EDS was in breach of contract in that:

- EDS failed to resource the project adequately;
- EDS was seriously in delay in carrying out and achieving the project milestones; and
- EDS had not carried out sufficient work to capture the project requirements and had not carried out adequate stress and integration testing to identify potential problems during the roll-out of the solution

The claims for breach of contract were subject to the contractual limitation of liability cap of £30 million.

Other Findings

The judge also made findings on a number of other issues, the most interesting of which are summarized below.

(i) Impact of contractual exclusions and limitations of liability on the existence of a tortious duty of care

One issue which arose was the extent to which a duty of care could be imposed upon a non-contracting EDS entity ("EDSC") involved in the pre-contractual discussions in favour of Sky and another Sky entity involved in those discussions. The judge found that the only duty of care with respect to negligent misstatement or misrepresentation was as between EDS and Sky and was subject to the contractual limitation of liability clause.

In determining that EDSC did not owe a duty of care to Sky or the other Sky entity participating in the pre-contractual discussions which circumvented the contractual exclusion or limitation of liability agreed as between Sky and EDS, the judge stated as follows:

> *"[…] in considering whether a contractual provision affects the existence or the scope or extent of a duty of care, the test will be whether the parties have so structured their relationship that it is inconsistent with any such assumption of responsibility or with it being fair, just and reasonable to impose liability. In particular, a duty of care should not be permitted to circumvent or escape a contractual limitation of liability for the act or omission that would constitute a tort."*

That statement is somewhat puzzling, in that presumably any duty of care on the part of EDSC for negligent misrepresentation/misstatement, would have arisen prior to EDS and Sky entering into the Agreement. It seems logically inconsistent to hold that a subsequent contractual term will negate the existence of an antecedent duty of care in tort.

(ii) Mitigation

As the project ran further into trouble, the parties agreed that Sky would take over the role of systems integrator from EDS as part of Sky's actions to mitigate the loss it was suffering. Expert evidence from both parties concurred that, in performing the systems integrator role, Sky performed less well and took longer to deliver the system than a competent systems integrator. EDS sought to rely upon this as a basis for arguing that Sky had acted unreasonably.

The judge rejected EDS's argument. The fact that Sky had not adopted steps that a reasonably competent systems integrator might have adopted does not mean that Sky had acted unreasonably. Both parties accepted that, in taking over the project, Sky had acted reasonably. The onus was thus upon EDS to establish that Sky's actions were unreasonable. The evidence was that Sky had retained expert advice and support and, in doing so, had acted reasonably. The fact that those steps taken by Sky meant that the project might take longer or cost more could not, on its own, amount to a failure on the part of Sky to act reasonably.

This finding underlines the proposition that, although the duty to mitigate losses is an important principle of English contract law, neither the content of the duty to mitigate, nor steps required to be taken by a party in mitigation of its losses, are particularly onerous.

Next Steps

Because of the findings of fraud and deceit, EDS can expect to have substantial damages awarded against it. EDS will not be able to rely on its contractual exclusion of liability clause to limit its exposure to those damages. Incidentally, the judge made an order that EDS make an interim payment on account of the damages to which Sky is entitled in the amount of £200 million—one would therefore expect the final damages order to be significantly higher than this figure.

Vendors would do well to support more substantively representations they make in the course of bidding for outsourcing mandates. The decision in *BSkyB v. EDS* confirms that English courts will look closely at statements which, whilst amounting to exercises in salesmanship, nevertheless have a material impact on a customer's supplier selection decision. On the other hand, customers should not be surprised by a lack of firm commitments coming from vendors in early stages of discussion as vendors are likely to be more cautious in the statements they make to customers. The case also highlights the importance of ensuring that "entire agreement" or "merger" clauses are appropriately drafted if the parties intend to exclude liability for non-fraudulent pre-contractual representations.

Willful Patent Infringement After *Seagate*

By Eric Krause and Thomas Flynn, Palo Alto

Trial courts may increase assessed damages for patent infringement up to three times the amount awarded in certain situations.[1] Although this is discretionary with the court, generally, "enhanced damages requires a showing of willful infringement" of a valid patent.[2] Under *In re Seagate Technology*, proving willfulness is a two-step process.[3] First, the "patentee 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."[4] Second, "[i]f this 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."[5] The determination of willful infringement "is best made after a fully developed trial record."[6]

While *Seagate* set forth a new willfulness test, the Federal Circuit explicitly left further application to the district courts. As a result, much of the willfulness jurisprudence remains undeveloped. Nevertheless, district courts have moved toward establishing bright line tests which may help defendants assess their business exposure in patent cases.

1 35 U.S.C. §284.

2 *Beatrice Foods Co. v. New England Printing & Lithographing Co.*, 923 F.2d 1576, 1578 (Fed. Cir. 1991).

3 497 F.3d 1360, 1371 (Fed. Cir. 2007). *Seagate* abandoned the prior standard which created "an affirmative duty to exercise due care to determine whether or not" one is infringing when on notice of another's patent rights. *Underwater Devices, Inc. v. Morrison-Knudsen Co.*, 717 F.2d 1380, 1389-90 (Fed. Cir. 1983).

4 *Seagate*, 497 F.3d at 1371.

5 *Id.*

6 *Abstrax, Inc. v. Dell, Inc.*, 2009 WL 3255089, at *3 (E.D. Tex. Oct. 7, 2009) (approving magistrate judge's recommendation that defendant's motion for summary judgment of no willfulness be denied).

The Objective Prong of the Willfulness Analysis

The first step in the *Seagate* test is objective, and "[t]he state of mind of the accused infringer is not relevant to this objective inquiry."[7] The objective prong requires the factfinder to take an objective view of the totality of the circumstances surrounding infringement.[8] Relevant considerations under the objective prong include "both legitimate defenses to infringement claims and credible invalidity arguments" because these "demonstrate the lack of an objectively high likelihood that a party took actions constituting infringement of a valid patent."[9]

Decisions following the Federal Circuit's decision in *Seagate* have examined whether a defendant's legitimate defenses to infringement claims and credible invalidity arguments preclude a finding of willfulness. While the Federal Circuit clarified that "both legitimate defenses to infringement claims and credible invalidity arguments" could negate willfulness, it defined neither "legitimate" nor "credible."[10] However, district court decisions have provided additional guidance.

In evaluating such defenses, district courts have looked to the persuasiveness of the non-infringement or invalidity arguments, regardless of whether they prevailed in court. For instance, in the Eastern District of Texas, although the defendant did not prove invalidity at trial, the court noted that the defendant's position was "hardly objectively unreasonable" and would preclude a willfulness finding.[11] On the other hand, simply because an argument survives summary judgment and goes to trial does not mean it automatically becomes a "close question" precluding a willfulness finding. In finding that a jury could have reasonably found for either party on the question of equivalence, the Federal Circuit noted that "the fact that an issue was submitted to a jury does not automatically immunize an accused infringer from a finding of willful infringement."[12] Instead, a court must consider whether the arguments were persuasive and demonstrated that the infringement question was a close one requiring an "intensely factual inquiry."[13]

Many courts seem to rely on the objective prong when denying a claim of willfulness or denying a motion for summary judgment of willfulness.[14] This reliance may be because the analysis of the subjective prong under the *Seagate* test is not as defined as the objective prong. This is discussed more below.

The Subjective Prong of the Willfulness Analysis

District courts, post-*Seagate*, focus on the subjective prong less frequently than they deal with questions related to *Seagate*'s objective prong. This, coupled with *Seagate*'s stated intent to "leave it to future cases to further develop the application of this standard" means that there is little guidance on the substantive question.[15]

However, the Federal Circuit has stated that any evidence of copying, should it exist, would be relevant only to the subjective prong of the *Seagate* test.[16] For instance, where the plaintiff argued that the defendant copied the invention directly from the patent-in-suit, the court held that this evidence was relevant only to the subjective prong, since it demonstrated what the accused infringer knew or should have known about the likelihood of its infringement.[17]

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7 *Seagate*, 497 F.3d at 1371.

8 *Arlington Indus., Inc. v. Bridgeport Fittings, Inc.*, 610 F. Supp. 2d 370, 389 (M.D. Penn. 2009). At least one district court, the Eastern District of Texas, has found that the objective prong is limited to an examination of the facts and circumstances surrounding the accused infringer at the time it initiates the allegedly infringing activity. *i4i Ltd. P'ship v. Microsoft Corp.*, 2009 WL 2449024, at *9 (E.D. Tex. Aug. 11, 2009). *But see Uniloc USA, Inc. v. Microsoft Corp.*, 640 F. Supp. 2d 150, 177 n.33 (D.R.I. 2009) (disagreeing with the *i4i* court because "such a 'before and after' line is [not] so easily drawn, or for that matter appropriate, to measure the objective likelihood (or lack thereof) that a party acted to infringe a valid patent").

9 *Black & Decker, Inc. v. Robert Bosch Tool Corp.*, 260 F. App'x 284, 291 (Fed. Cir. 2008). This case is frequently cited by alleged infringers in willfulness cases. However, many patent holders discredit *Black & Decker* because it was not published in the Federal Reporter.

10 *Id.*

11 *TGIP, Inc. v. AT&T Corp.*, 527 F. Supp. 2d 561, 579 (E.D. Tex. 2007); *see also Henrob Ltd. v. Bollhoff Systemtechnik GmbH & Co.*, 2009 WL 3199812, at *7-8 (E.D. Mich. Sept. 29, 2009) (finding no willfulness because of defendant's "persuasive," although ultimately unsuccessful, non-infringement arguments); *ResQNet.com, Inc. v. Lansa, Inc.*, 533 F. Supp. 2d 397, 420 (S.D.N.Y. 2008) (finding that although defendant failed to prove non-infringement or invalidity of the patent-in-suit, its arguments were "substantial, reasonable, and far from the sort of easily-dismissed claims that an objectively reckless infringer would be forced to rely upon").

12 *DePuy Spine, Inc. v. Medtronic Sofamor Danek, Inc.*, 567 F.3d 1314, 1337 (Fed. Cir. 2009).

13 *Id.*

14 *See,* e.g., *Depomed, Inc. v. Ivax Corp.*, 532 F. Supp. 2d 1170, 1186 (N.D. Cal. 2007) (court examined whether a party would have 'ample time to investigate and discover the relevant patent' based on the time between the patent's issuance and the start of infringing activity). In some cases, courts have applied factors that seem more appropriate to a subjective prong analysis than to their "objective" prong discussion.

15 *Seagate*, 497 F.3d at 1371. Because the willfulness analysis is intensely factual, the Federal Circuit likely found the district courts best suited to develop its application.

16 *DePuy Spine*, 567 F.3d at 1336.

17 *Id.*; *see also Creative Internet Adver. Corp. v. Yahoo!, Inc.*, 2009 U.S. Dist. LEXIS 65690, at *6 (E.D. Tex. July 30, 2009).

In the District Court of Delaware, where the alleged infringer received no notice of the patent, the patentee argued that it could "reasonably be inferred that a company so thoroughly invested in [the technology at issue] would have carefully studied the prior art before seeking a patent for and investing in" that business model.[18] The court said that this reading of *Seagate* was "overly broad" and that to allow such a reading would essentially return to the negligence standard *Seagate* rejected.[19]

Although cases analyzing the subjective prong of *Seagate* are few, many have examined the threshold for the defendant's knowledge of the patent-in-suit. Because this is a highly factual inquiry, no clear rule exists. However, the standard is stringent. The District Court of Rhode Island acknowledged its "gatekeeping role," warning that it would not accept "inference upon inference [which] could not, as a matter of law, [leave] jurors with a 'clear conviction or firm belief'" that the defendant knew it infringed.[20] Nonetheless, courts have drawn some clear lines. For instance, the Eastern District of Texas rejected the argument that anything short of a cease and desist letter is inadequate to alert the defendant to the objectively high risk of infringement.[21] Additionally, mere publication of a patent is insufficient to show defendant's knowledge.[22]

Conclusion

Perhaps the most important change in recent willfulness jurisprudence is *Seagate*'s shifting of the affirmative duty of due care from the accused infringer, who was all but required to obtain and rely on opinion of counsel, to the patentee, who now faces a clear and convincing standard for proving willful infringement. Under the new test, articulated in *Seagate*, the patentee has to prove willfulness under both an objective prong and a subjective prong. However, the law is not yet clear on the analysis for either prong. The Federal Circuit deliberately left the development of the proper analysis under the subjective prong to future cases. There has been little development, however, as the cases that have been decided have tended to focus on the objective prong, often confusingly applying factors that seem more appropriate to a subjective analysis to their "objective" prong discussion.

It will take time to determine how courts deal with changes to the willfulness analysis, and although the abandonment of an affirmative duty of due care is an important change, a final picture of how willfulness will be handled after *Seagate* has yet to emerge. Until the case law is clear, companies and their counsel should exercise caution when considering another's patents. For instance, companies should be especially careful in studying the prior art before investing in a business model. This kind of watchfulness is the best way to protect against the threat of litigation until the new willfulness standard is better settled.

US Barred from Accessing the SWIFT Data by the European Parliament

By Bertrand Liard and Gustave Hottegindre, Paris

The Society for Worldwide Interbank Financial Telecommunications ("SWIFT") is a financial transmission company organized under Belgian law which at the present holds more than 80 percent[23] of the worldwide market for electronic financial transfers and on a daily basis processes significant volumes of crucial information, not least of which includes the banking coordinates of issuers and receivers for transactions falling within its purview. This highly sensitive information has been used, for several years, by the government of the United States (US); more particularly, by the US Treasury Department in the framework of the Terrorism Finance Tracking Programme ("TFTP").

The TFTP was created following the attacks of September 11, 2001 for the purpose of identifying and prosecuting the financial support of terrorism. Subsequent to the revelation of TFTP's existence by the US press in 2006, and so as to provide for the US government's

18 *Cordance Corp. v. Amazon.com, Inc.*, 639 F. Supp. 2d 406, 415 (D. Del. 2009).

19 *Id.* (granting Amazon.com's motion for summary judgment of no willfulness).

20 *Uniloc USA, Inc.*, 640 F. Supp. 2d 150, 179 (D.R.I. 2009).

21 *i4i Ltd. P'ship v. Microsoft Corp.*, 2009 WL 2449024, at *11 (E.D. Tex. Aug. 11, 2009).

22 *Uniloc USA, Inc.*, 640 F. Supp. 2d at 178 (finding that the mere publication of a patent does not establish defendant's knowledge—otherwise, "every accused infringer with an internet connection or Washington DC metro pass (enabling travel to the PTO) would become a willful infringer").

23 *See*: http://www.europarl.europa.eu/news/expert/background_page/019-68530-032-02-06-902-20100205BKG68527-01-02-2010-2010-false/default_p001c001_fr.htm.

continued access to SWIFT data, an international framework was rendered necessary. In addition, SWIFT has recently replaced its US-based data centre with a Swiss-based data centre. The establishment of a Swiss-based data centre has resulted in the US government no longer possessing direct access to stored SWIFT data. So as to allow the US continued direct access to SWIFT data a further agreement (SWIFT Agreement) has been negotiated between the EU and the US.

The Content of the SWIFT Agreement

In its resolution of September 17, 2009, and as a result of its direct concern to EU citizens, the European Parliament highlighted the need to formalize the US government's access to data held by SWIFT by way of international agreement.

On November 30, 2009, the SWIFT Agreement (with a term of nine months) was signed between the EU and the US with a proposed date of entry into force of February 1, 2010. The SWIFT Agreement is based on the principle of reciprocity and has as its primary objectives that (i) SWIFT financial transmission network data be made available to the US Treasury Department for the purposes of detecting and preventing terrorism and (ii) any relevant information obtained by the US government as a result of the SWIFT Agreement must be made available to the respective authorities of the Member Countries responsible for combating terrorism. The SWIFT Agreement, moreover, specifies that the data provided to the US Treasury Department must be processed exclusively for the purposes of detection and prevention of terrorism or its financing and that no profiling may be carried out on the basis of this data.

The SWIFT Agreement was not therefore intended to implement a new programme or to grant the US authorities with additional access to European personal data, but in fact formalised and ensured the continuation of the TFTP.

The European Parliament's Right of Oversight under the Lisbon Treaty

The Lisbon Treaty, which came into force on December 1, 2009, grants new prerogatives to the European Parliament including the right to approve international agreements negotiated in the areas of judicial cooperation in criminal matters. This right applies not only to agreements that were under negotiation at the date of the Lisbon Treaty's entry into force, but also to agreements duly signed but not yet entered into effect, as was the case with the SWIFT Agreement.

In application of these new prerogatives, the European Deputies voted (378 in favour, 196 against) on Thursday 11 February 2010 to adopt a resolution refusing to approve the conclusion of the SWIFT Agreement (the "Resolution"). This rejection by the European Parliament prevents the SWIFT Agreement from entering into force.

The Reasons for the Refusal by the European Parliament

By their vote, the European Deputies reaffirmed the principles advanced in their resolution adopted on September 17, 2009. The European Parliament stated that it "*recalls its determination to fight terrorism and its firm belief in the need to strike the right balance between security measures and the protection of civil liberties and fundamental rights, while ensuring the utmost respect for privacy and data protection; reaffirms that necessity and proportionality are key principles without which the fight against terrorism will never be effective.*"[24]

The European Parliament further added that any transfer of European personal data to a country outside of the EU for security purposes must comply with the applicable national and European laws in terms of data protection, more particularly with Directive 95/46/CE of October 24, 1995 concerning the protection of individuals with regard to the processing of personal data and the free circulation of such data.

By its Resolution, the European Parliament thus decided to follow the opinion which Peter Hustinx, the European Data Protection Supervisor ("EDPS"), rendered on January 25, 2010. In his official capacity, Peter Hustinx stated that the SWIFT Agreement was "very privacy-intrusive since it interferes with the private life of all Europeans" and that it was insufficiently precise concerning the protection of personal data. In particular, he noted that "many data subjects' rights—as for example rectification, information, compensation for unlawful processing, redress—are either disregarded or have no concrete and clear way to be enforced." He further added that "the evidence provided so far to the EDPS does not entirely show the necessity [of the SWIFT Agreement] and the real added value with respect to more targeted existing instruments" such as, in particular, the agreement on mutual legal assistance between the EU and the US which entered into force on January 1, 2010.

24 The full text of the resolution is available at: http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2009-0016+0+DOC+XML+V0//EN.

The European Parliament also followed the position of the Article 29 Working Group[25] and the opinion of the President of the French *Commission Nationale de l'Informatique et des Libertés* (CNIL), Alex Türk. The later in a recent letter addressed to the President of the Committee on Civil Liberties, Justice and Home Affairs of the European Parliament, highlighted that the guarantees negotiated between the European and US authorities concerning banking details (in particular pursuant to the agreement on mutual legal assistance between the EU and the US) could be undermined by the conclusion of the SWIFT Agreement.[26]

The Consequences of the Veto by the European Parliament

The Resolution should incentivise the European Commission and the European Council to commence work on concluding a new, long-term, agreement with the US concerning the prevention of terrorism financing.

The entering into force of the Lisbon Treaty provides for the full participation by the European Parliament in the drafting/contemplation of any new international agreement. In this respect, the European Deputies have taken care to note in the Resolution that any new agreement with respect to the SWIFT data will have to find the correct balance between the prevention of terrorism on one side and the requirements of the European Union Charter of Fundamental Rights as well as the European data protection rules on the other.

In Re Bose Corporation: Federal Circuit Clarifies Trademark Fraud Precedent

By Daren M. Orzechowski and Adam E. Wactlar, New York

It is not uncommon for companies with established brands and existing trademark portfolios used in traditional retail methods to expand their businesses into digital marketplaces. This expansion provides companies with an opportunity to evaluate their operations vis-à-vis existing or applied-for trademark registrations. Unfortunately, when it comes to Internet marketing, a large number of companies do not engage in this evaluation exercise and still apply to register marks in an overly broad grouping of product and service classes. The Federal Circuit's decision in *In re Bose Corporation*[27] serves as a cautionary tale for trademark applicants and registrants and presents a prudent opportunity to remind clients about best practices in registering and managing their trademarks.

In *In re Bose*, the Federal Circuit clarified the requirements for a finding of fraud on the Patent and Trademark Office ("PTO") in connection with claims for cancellation. Bose, a consumer electronics dealer best known for its speaker and audio products, brought an opposition proceeding against the HEXAWAVE trademark application by Hexawave, Inc., a manufacturer of wireless communications products. Hexawave counterclaimed for cancellation of Bose's WAVE mark, asserting that Bose committed fraud on the PTO in its registration renewal by claiming continued use on all goods covered by the WAVE registration when Bose knew that it had stopped manufacturing certain goods.

In January 2001, Bose had filed a Section 8 affidavit of continued use and Section 9 renewal application, signed by its general counsel, Mark Sullivan, stating that Bose was still using the WAVE mark in commerce for various goods, including audio tape recorders and players. During the course of proceedings, the Trademark Trial and Appeal Board ("TTAB") found that Bose stopped manufacturing and selling tape recorders and players sometime between 1996 and 1997. Mr. Sullivan testified that when he executed the WAVE renewal, he believed the mark was still used in commerce in connection with audio tape recorders and players because Bose continued to repair those products and shipped them back to customers.

25 This Working Group was created by Directive 95/46/CE of 24 October 1995.

26 *See*: http://www.cnil.fr/la-cnil/actu-cnil/article/article/2/swift-nouvelle-donneapres-le-rejet-de-laccord-par-le-parlement-europeen.

27 580 F.3d 1240 (Fed. Cir. 2009).

The TTAB cancelled the WAVE mark in its entirety, including in connection with goods other than audio tape recorders and players, finding that repairing and transporting goods did not constitute use in commerce and that Mr. Sullivan's belief that it did was not reasonable. In support of its holding, the TTAB relied on its prior decision in *Medinol v. Neuro Vasx, Inc.*,[28] which held that a "trademark applicant commits fraud in procuring a registration when it makes material representations of fact in its declaration which it knows or should know to be false or misleading." Under *Medinol*, fraud could be found if false misrepresentations were made to the PTO, even if accidental, and the registrant or applicant should have known they were false. Since the TTAB decided *Medinol* in 2003, it has found fraud in several cases based upon a simple showing of material mistake made in a statement to the PTO that resulted in registration or renewal of a trademark. Such was the case in the decision against Bose.

The Federal Circuit reversed and remanded, holding that the TTAB had erroneously lowered the standard from fraud—a statement an applicant or registrant *knowingly* makes with intent to deceive—to the simple negligence standard in *Medinol*. The Federal Circuit went on to explain that it is a higher burden to prove an intent to deceive than the standard for negligence or gross negligence, and accordingly rejected the standard set in *Medinol*. In holding that the intent to deceive is an "indispensible" requirement to find fraud, the Federal Circuit found that such a standard comports with previous Federal Circuit precedent and precedent of several other Courts of Appeals. As it pertained to Bose, since there was no clear and convincing evidence in the record that Mr. Sullivan intended to deceive the PTO, Mr. Sullivan's misunderstanding did not rise to the level of deceptive intent and did not constitute fraud. The Federal Circuit went on to find that although the WAVE registration should not be cancelled in its entirety, it should be modified to reflect "commercial reality" since the mark was no longer being used in commerce with tape recorders and players.

Practical Implications and Best Practices

At first glance, in reaffirming the strict standard for finding a registrant committed fraud on the PTO, the *In re Bose* decision may look like a green light for a return to the practice of broad applications and renewals. A closer review, however, cautions that applicants and registrants should still take care to tailor applications to goods or services with which they are using/intend to use a mark and confine renewals to those goods or services still being used in commerce. Although trademark owners can rest easier in knowing that an honest and inadvertent mistake in a representation to the PTO will not necessarily lead to a finding of fraud and consequent cancellation of a registration, fraudulently procured registrations or renewals will still be subject to cancellation. The Federal Circuit held that the "should have known" standard is insufficient to find fraud but did not opine as to what kinds of evidence would be sufficient to find an intent to deceive. Future decisions may make fraud practically easier to prove than *In re Bose's* exacting language may indicate. Specifically, the burden of an applicant or registrant to inquire further when presented with an ambiguity is not settled.

As *In re Bose* clarifies, there is a significant evidentiary requirement to prove fraud on the PTO in order to cancel a mark. Accordingly, already-registered marks that were perhaps procured by fraud or based on a failure to properly investigate use of the mark may be even more costly if those registrations cannot be cancelled. The evaluation of whether or not a fraud argument will prevail has changed and parties will need to consider whether in challenging an existing registration they can meet the heightened burdens of proof. The result may very well be that until further case law develops, those who were merely negligent in their pre-filing investigation may be able to maintain their registrations despite the fact that there were incorrect statements made to the PTO. Unfortunately, this might have the effect of precluding other legitimate trademark owners from using their marks in certain classes of goods or services.

While *In re Bose* corrects what was perhaps an unfair legal standard, it should not lead to a relaxed approach to trademark prosecution. As an initial consideration before applying for any mark, an applicant should still first clear the proposed mark through customary clearance searches before committing any resources to advertising or marketing goods or services under that mark. In addition, some minimal investigation should be conducted by the individual signing any declaration submitted to the PTO concerning use of, or an intent to use, the subject mark in connection with the cited goods and services.

28 67 U.S.P.Q.2d 1205 (T.T.A.B. 2003).

ICANN's IDN ccTLD Fast Track Process: A Challenge in any Language

By Daren M. Orzechowski and Boris Sharapan, New York

Introduction

Every website's URL address ends with a top-level domain ("TLD"), which are the two or more letters that appear after a domain name such as ".com", ".net", and ".info". These TLDs are referred to as generic top-level domain names ("gTLDs"). However, rather than using gTLDs, most countries use a country code top-level domain ("ccTLD") such as ".de" for Germany, ".cn" for China, and ".ru" for Russia. All gTLDs and ccTLDs are managed by registry operators, organizations that maintain their respective registry databases.

Several gTLDs and ccTLDs allow registrations of internationalized domain names ("IDNs") for second level domains ("SLDs"). An SLD is what appears after the "www." For example, "google" is the SLD of www.google.com. IDN SLDs contain non-Latin characters, such as Chinese, Arabic and Russian characters, all of which are part of the Unicode character set. For example, www.музыка.net ("music" in Russian) and www.direktflüge.de ("direct flights" in German) are URL addresses that have IDN SLDs.

On October 30, 2009 the Internet Corporation for Assigned Names and Numbers ("ICANN") announced the launch of the IDN ccTLD Fast Track Process.[29] This process, which formally launched on November 16, 2009, is described by ICANN as "a method by which the Internet communities that are ready to do so can obtain new internationalized country code top-level domains (IDN ccTLDs) representing the name of their country or territory. The IDN ccTLDs are available for countries or territories with official languages based on scripts other than Latin."[30] This program will allow nations to apply for IDN ccTLDs to be managed by government supported registry operators. Thus, countries like China will soon have a ccTLD in their native language (".中国"), no longer restricted by the Latin alphabet ccTLD version of ".cn". This initiative will make the Internet more accessible to the billions of people who do not speak a Latin-based language. As a result, Internet users will soon be able to register and access websites using their native languages for both the SLD and TLD.

The benefits of this initiative, however, may come at a significant cost and burden to trademark owners. History is a strong indicator of the problems that trademark owners may face as a result of the IDN ccTLD Fast Track Process. For example, the introduction of IDN SLDs in 2003 resulted in numerous homograph spoofing concerns for trademark owners. Similarly, the launch of IDN ccTLDs may pose a new set of homograph spoofing and cybersquatting threats.

Homograph Spoofing

One major concern with Unicode is that scammers have easily faked legitimate domain names. Before ICANN's 2003 IDN initiative, only 37 characters were used for domain names (A-Z, 0-9 and "-"). Even these 37 Latin characters created some confusion; the letter "O" looks similar to the number "0", and "I" could easily be mistaken for an "l". The introduction of IDNs, which use over 100,000 Unicode characters, created even more confusion. For example, the following two domain names appear to be the same: Tax.com and Tax.com. However, only the first one is the real Tax.com domain because it is written using Latin letters while the second is comprised of Cyrillic letters, which happen to look identical to Latin letters. Since these domains contain different Unicode characters, an Internet browser will interpret each as a distinct domain name despite their similarity. This is called homograph spoofing. While Internet browsers attempt to protect Internet users with anti-spoofing software, scammers are constantly conjuring up new ways to stay ahead of the software. The launch of IDN ccTLDs will undoubtedly increase the prevalence of homograph spoofing. As the number of IDN ccTLDs grows, many trademark owners may find themselves unable to meaningfully monitor and prevent the multiple IDN variations of their trademarks.

No Registration Guarantee to Prevent Cybersquatting

Previous registrations of a domain name containing a recognized trademark with a countries' ccTLD do not guarantee automatic rights to the new version of that country's IDN ccTLD. For example, Company X's registered ownership of www.companyx.ru (Russia)

29 For more information, visit ICANN's website, specifically, http://www.icann.org/en/topics/idn/fast-track/.

30 *See* https://www.icann.org/en/topics/idn/fast-track/faq-en.htm#general4.

does not necessarily mean Company X will have first priority for www.companyx.pф (Russia's new IDN ccTLD, which stands for Russian Federation). This uncertainty is due to the fact that a ccTLD operator, such as ".ru", may not be selected by ICANN as the operator of that country's new IDN ccTLD, such as ".pф". The new operator could very well be a totally unrelated party. Thus, trademark owners must be prompt and vigilant in registering domain names incorporating their marks with the new IDN ccTLD operators at the risk of losing ownership rights or priority in several IDN ccTLDs. This risk is compounded by the fact that national registries generally lack the standard practices necessary to protect the genuine interests of trademark owners.

Practice Pointers and Best Practices

Registering and maintaining domains with the new IDN ccTLDs will increase the costs associated with preserving a trademark's online presence, but avoiding the problems associated with cybersquatting and spoofing can outweigh such added costs.

However, racing to capture the many combinations and options created by this opening up of IDN ccTLDs may prove overwhelming and uneconomical to many trademark owners.

As has always been the case, selective registration of domain names must be made after commercial considerations and competition analyses have been completed. These analyses unfortunately just got more complicated. A prudent first step is to analyze the countries and territories that do not use the Latin alphabet and determine whether such markets are commercially significant to a trademark owner. If such jurisdictions are not clearly significant to the brand owner, then pursuing registration of variations of certain IDN ccTLDS will not be economically justified. If there is a business case for registration, then those domain names concerning the company's trademarks should be protected, bearing in mind issues such as phonetic variation and homograph spoofing.

Antitrust Scrutiny of IP Licensing in Competitor Collaborations

By Noah Brumfield and Kenneth Maikish, Palo Alto

Currently, the Supreme Court is considering the issue of trademark licensing restrictions that may shed additional light on the liability standard under the antitrust laws when competing firms license IP, whether it be trademarks or technology, through a joint venture or other collaboration. The case, *American Needle Inc. v. National Football League*, also attempts to clarify when joint venture members may be liable for "conspiring" well-after agreeing to a joint venture or collaboration. The case concerns a single licensing decision taken by the NFL more than 40 years after the formation of its joint licensing arm, NFL Properties.

When competitors consider forming a joint venture to license IP or bring a new product to market, they rarely think about drawing the attention of government antitrust regulators. Antitrust litigation represents one of the most complicated and costly procedures in the US civil court system so businesses should know the rules before participating in joint licensing with competitors. Unfortunately, the courts have offered little guidance on when a joint venture's decisions might run afoul of antitrust laws.

The Sherman Act is the primary antitrust law that governs both agreements between two or more companies and the conduct of a single monopolist; agreements often face greater scrutiny and lower thresholds for liability than single firm conduct. The risks are particularly heightened when the challenge concerns an agreement between competitors or potential competitors. Consequently, when the actions of a joint venture and its members are challenged, the question often turns to whether the joint venture's actions are defined as concerted actions between the members or the action of a single entity—the joint venture itself. Section 1 of the Sherman Act regulates agreements, potentially including conduct acted on jointly. If the venture's actions are the actions of all the members acting in concert with each other, then Section 1 applies and those members could end up in a lengthy court battle. But, if the venture is a single entity then its actions, by definition, cannot violate Section 1 of the Sherman Act, and would only be subject to the more lenient standards applicable to single-firm conduct relevant to monopolies under Section 2 of the Sherman Act.

The central issue in *American Needle, Inc. v. National Football League* is whether the individual teams "conspired" to limit competition in the licensing of their marks.[31] In response, the NFL has argued that the NFL and its membership—the individual teams—should not be subject to the heightened scrutiny that applies to agreements among competitors. The NFL argues it ultimately cannot be liable for conspiring because the NFL constitutes a "single-entity" for antitrust purposes when it engages in the activities for which the venture was formed: the production and promotion of football.

Implicitly recognizing the potential broader ramifications of a decision in this case, the US Solicitor General petitioned the US Supreme Court to deny certiorari, arguing that the "sports-league context is not a suitable one in which to address broader questions concerning the application of single-entity principles to joint ventures generally."[32] But the Supreme Court agreed to hear the case and is expected to issue an opinion offering important guidance to businesses involved in or considering collaborations with a competitor that involve the bundling of IP.

Background

The NFL is an unincorporated, nonprofit association of 32 football teams—each an independent, for-profit entity.[33] The NFL controls many aspects of the league such as scheduling, television licensing and approval of all assignments and sales of member teams; the teams also share revenues.[34] The teams initially formed a licensing entity called NFL Properties so that they could issue a "blanket" license of all the teams' respective IP in one bundle.[35] Later, the teams agreed to make the NFL Properties the "near-exclusive" licensing entity for each of their marks, retaining only the right to advertise locally and use the marks in the teams' own publications. The licensing entity agreed to evenly split the revenue amongst the teams.[36]

American Needle (among others) obtained a blanket license from NFL Properties to manufacture NFL apparel during the '80s and '90s. This changed in 2000, when the teams collectively approved a ten-year exclusive license with Reebok covering the NFL and all team marks and logos.[37] Shortly after, American Needle brought the current action against the NFL and each of the 32 teams for a violation of Section 1 of the Sherman Act.[38] The district court granted summary judgment to the NFL because the defendants "act as a single entity in licensing their intellectual property."[39]

Arguments before the Supreme Court

The NFL argues on appeal that a joint venture's agreements and actions are only subject to the Sherman Act's Section 1 scrutiny of agreements at the formation of the joint venture. The government is able to review the agreement at formation and if the agreement is found to be procompetitive then all later joint venture actions are not the decisions of the individual members, but the decision of a unitary body—the joint venture—and are immune from Section 1 scrutiny.[40] NFL Properties was created to promote football, and the undisputed evidence establishes that the purpose of collective licensing is to promote football.[41] Therefore, the NFL contends that an NFL licensing decision is not an agreement among competitors regulated by the conspiracy standards of the Sherman Act because it is "venture activity" and not concerted action.[42]

American Needle argues that the joint licensing by competing NFL teams is alleged to be a horizontal agreement among competitors.[43] The NFL's conduct and conduct of joint ventures in general, is therefore subject to heightened scrutiny under Section 1 scrutiny because the participants are separately owned and controlled.

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31 *American Needle Inc. v. National Football League, et al.*, No. 08-661 (US argued Jan. 13, 2010).

32 Brief for the United States as Amicus Curiae at 7, *American Needle Inc. v. National Football League, et al.*, No. 08-661 (US argued Jan. 13, 2010).

33 Brief of Petitioner at 2, *American Needle Inc. v. National Football League, et al.*, No. 08-661 (US argued Jan. 13, 2010) [hereinafter Brief of Petitioner].

34 Id. at 3.

35 While each team is assigned official colors to use in developing its marks and logos, and changes to the logos or marks must be approved by the NFL, each team owns its own marks. Id. at 4; Brief for the NFL Respondents at 7, *American Needle Inc. v. National Football League, et al.*, No. 08-661 (US argued Jan. 13, 2010) [hereinafter Brief of NFL].

36 Brief of Petitioner, supra note 3, at 5.

37 The deal included a provision, insisted upon by the Dallas Cowboys, which allowed a team to elect to control the merchandising of its own apparel in exchange for an annual minimum contribution to the teams' shared revenue pool. The Cowboys elected to exercise this option. *Id.* at 7.

38 Originally, American Needle brought suit under Section 2 as well, but that claim was dismissed and is not up on appeal.

39 *American Needle Inc. v. New Orleans Louisiana Saints, et al.*, 496 F. Supp.2d 941, 944 (N.D. Ill. 2007).

40 Brief of NFL, supra note 5, at 25.

41 *American Needle Inc. v. National Football League*, 538 F. 3d 736, 739 (7th Cir. 2008).

42 Brief of NFL, supra note 5, at 27.

43 Brief of Petitioner, supra note 3, at 10.

The NFL emphasized that because the teams alone cannot produce their joint product—a football season—they are not "independent sources of economic power," but merely units of the NFL.[44] So, according to the NFL, their collaboration cannot be subject to Section 1 scrutiny when they produce and take action ancillary to the promotion of NFL football.[45]

In response, American Needle argued that even if the licensing is done for the purpose of promoting football, "a restraint cannot be justified by reference to the benefits of a joint venture unless it is 'reasonably necessary to achieve [the] joint venture's efficiency-enhancing purposes.'"[46] That is, even though an individual team cannot create a football season, each team can license its own IP. So, the argument continues, the decision to issue a blanket license is separate from the NFL's primary purpose and its licensing agreement is not immune from Section 1 just because the joint venture was formed for a procompetitive reason.

American Needle seeks a remand to the district court for furthering fact-finding on the issue of whether the teams are capable of competing against each other in the licensing market.[47] They contend that if teams can compete as licensors then the NFL Properties license is an inefficient and illegal restraint.

Implications for IP Collaborations

Many important business and technological advances are made possible through collaboration between competitors. At a fundamental level, collaborations enable the efficient use of scarce resources and know-how. Even among competitors, they have many procompetitive benefits, including bringing better products to market cheaper and faster.

Formal and informal joint ventures are common in the IP context. For example, patent pools break up patent thickets allowing a licensee to negotiate a single license for all patents necessary to produce a product. Without the pool, inefficient separate negotiations can drive up prices and transaction costs. The music business creates efficiency by offering blanket licenses that cover the broadcast of millions of songs without which radio and music streaming might be prohibitively expensive.

The antitrust laws recognize the inherent procompetitive nature of such collaborations. When a joint venture is formed, government regulators will analyze the agreement under the rule of reason, which is used to determine the overall competitive effect.[48] This "rule of reason" analysis focuses on the state of competition with, as compared to without, the challenged agreement.

The issue in *American Needle* is analogous to the issue of competing technologies in patent pools. If one of the patents in the pool is a substitute for another patent, then the pool might limit competition and a plaintiff challenging the pool license may argue it is anticompetitive. Others would argue, as Justice Scalia reiterated at the oral argument, that this question is irrelevant to the question of concerted action in the joint venture context.[49] Either the joint venture acts as a single entity or it does not; if the action is unitary then inquiries into the action's impact on competition are unnecessary. Justices Kennedy and Breyer suggested that each decision must be reviewed for its anticompetitive effect.[50] In a patent pool, under this line of argument, the fact that substitute IP exists in a pool could be evidence that the members are independent sources of economic power and thus not a single entity.

Finding Equipoise After an Initial Agreement to Collaborate on IP Creation and Licensing

This case also highlights the tension in antitrust when companies are targeted with claims long after parties agree to collaborate. The statute of limitations for civil claims is four years. Here the challenge to NFL Properties' licensing was brought over 40 years after its creation. American Needle benefited as a licensee under NFL Properties' prior licensing arrangement and only challenged the NFL's joint licensing when NFL Properties decided to grant Reebok an exclusive license.

If every decision made by a joint venture is deemed concerted action made by separate entities, then joint venture members are going to be spending precious time and resources on lengthy discovery and litigation procedures. Several large businesses submitted an amicus brief stressing the importance of this case to

44 Brief of NFL, *supra* note 5, at 14.

45 The case of *Copperweld Corp. v. Independence Tube Corp.* is cited heavily by both sides and its application is the subject of ongoing debate—however, one of its central holdings is that only "independent sources of economic power" can by subject to Section 1 scrutiny. 467 US 752, 771 (1984).

46 Reply brief of Petitioner at 12, *American Needle Inc. v. National Football League, et al.*, No. 08-661 (US argued Jan. 13, 2010), quoting *Major League Baseball Props., Inc. v. Salvino, Inc.*, 542 F.3d 290, 339 (2d Cir. 2008) (Sotomayor, J., concurring in the judgment).

47 At the District Court, American Needle was allowed discovery solely on the single-entity question. *See American Needle Inc. v. New Orleans Louisiana Saints, et al.*, 496 F. Supp.2d 941 (N.D. Ill. 2007).

48 Agreements of a type that always or almost always tends to raise price or to reduce output are per se illegal. These are naked agreements to fix prices, rig bids, or divide markets among competitors.

49 Transcript of Oral Argument at 20, *American Needle Inc. v. National Football League, et al.*, No. 08-661 (US argued Jan. 13, 2010).

50 *Id.* at 19 – 21.

the general business community. The amici pleaded with the Court not to subject joint venture decisions to Section 1 scrutiny: "The Section 1 rule of reason litigation in which joint ventures are frequently engaged has long been recognized as among the most costly and burdensome litigation in a civil justice system widely criticized for its overwhelming cost and burden."[51]

And, with treble damages, the potential liability is significant for both the venture and its members. The potential for antitrust challenges injects uncertainty and risk into collaborative efforts by companies long after their underlying agreement to collaborate.

Post *Quanta*: Recent Developments on the Patent Exhaustion Doctrine

By Bijal V. Vakil and Kao-yu Hsu, Palo Alto

The longstanding doctrine of patent exhaustion, also known as the first sale doctrine, is a judicially created rule designed to limit a patent holder to a single royalty per patented device.[52] It provides that the initial authorized sale of a patented item terminates all patent rights to that item. That is, once a patent owner engages in or authorizes an unrestricted sale of the patented device, the patentee's right to exclude others from use of the patented device is exhausted.

On June 9, 2008, the Supreme Court, in *Quanta Computer, Inc. v. LG Electronics, Inc.*[53] clarified the reach of the exhaustion doctrine. In this case, the court considered whether LG's patent rights were exhausted by its license agreement with Intel, and Intel's subsequent sale of its products to Quanta under such license. Despite LG's efforts to craft a limited license intended to exclude unlicensed Intel customers from the scope of the license, the Supreme Court unanimously concluded that "[t]he 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."[54]

While the Court addressed several questions of patent exhaustion in *Quanta*, it also left others unanswered. Below, we analyze a number of recent district court cases and shed light on some of the open issues left by *Quanta*.

May a Conditional Sale Still Defeat Patent Exhaustion Under *Mallinckrodt*?[55]

Before *Quanta*, patentees had the ability to avoid the exhaustion doctrine by imposing certain condition on sales of their products.[56] *In Mallinckrodt*, exhaustion was held inapplicable to the sale of patented medical devices accompanied by a "single-use-only" notice. The landscape for conditional sales has changed post-*Quanta*. For example, the District Court for the Eastern District of Kentucky declined to follow *Mallinckrodt* and held that *Quanta* overruled *Mallinckrodt* sub silentio.[57] *In Static Control Components v. Lexmark Int'l*, Lexmark also employed single-use restrictions on sales of its toner cartridges so that it could still target those who refilled and resold used toner cartridges to end-users. Nonetheless, the court held that as a result of *Quanta*, Lexmark could no longer impose post-sale restrictions on its toner cartridges to circumvent exhaustion.[58]

In *Monsanto v. Scruggs*,[59] the District Court for the Northern District of Mississippi applied *Quanta* in a different way. While it agreed that *Quanta* bans the patentee's post-sale control on use of the article, the court nonetheless allowed Monsanto to restrict farmers' post-sale use of seeds sold by Monsanto's seed

51 Brief of Mastercard Worldwide and Visa Inc. as Amici Curiae in Support of Respondents at 13, *American Needle Inc. v. National Football League, et al.*, No. 08-661 (US argued Jan. 13, 2010).

52 *See Adams v. Burke*, 84 US 453 (1873).

53 *Quanta Computer, Inc. v. LG Electronics, Inc.*, 128 S.Ct. 2109 (2008).

54 *Id.* at 2122.

55 *Mallinckrodt, Inc. v. Medipart, Inc.*, 976 F. 2d 700 (Fed. Cir. 1992).

56 The theory behind this rule is that the patentee may not have received the full value of the patented goods in an expressly conditional sale. Namely, the offered price reflects only the value of the "single use" rights conferred by the patentee. *See B. Braun Med. Inc. v. Abbott Labs.*, 124 F.3d 1419, 1426 (Fed. Cir. 1997).

57 *Static Control Components Inc. v. Lexmark International, Inc.*, 615 F. Supp.2d 575, 585 (E.D. Ky. 2009).

58 "Lexmark attempts to reserve patent rights in its products through post-sale restrictions on use imposed on its customers. This is what *Quanta* says Lexmark cannot do." *Id.* at 584.

59 *Monsanto Company v. Scruggs*, 2009 WL 536833 (N.D. Miss.).

partners.[60] Likewise, in *Monsanto v. Bowman*, the court also held that, even after *Quanta*, Monsanto may invoke patent law to control farmers' post-sale use of seeds purchased from seed companies which have only limited licenses to sell.[61]

In sum, despite varying interpretations of *Quanta*, these courts all seem to agree that there is a line between "post-sale conditions on use" and "conditions restricting the licensee's right to sell."[62] While *Quanta* blocks the patentee from limiting post-sale use of goods, the patentee is free to employ any restrictions on a licensee's right to sell. By selling patented articles via a supplier who only has a limited license, the patentee may still control the buyer's post-sale use of the article because the supplier cannot convey what he does not have, to the buyer.[63]

Can an Authorized Sale Outside the US Trigger the Exhaustion Doctrine After *Quanta*?

In Fuji Photo Film v. Jazz Photo,[64] the Federal Circuit held that the exhaustion doctrine is not triggered by any authorized sale outside of the United States. Although this issue was never addressed in *Quanta*, the District Court for the Northern District of California recently concluded that *Fuji Photo* was overruled by *Quanta* and that exhaustion can be triggered by authorized foreign sales as well.[65] *In Fujifilm v. Benun*, however, the District Court of New Jersey rejected such a broad view and still upheld *Fuji Photo* as the controlling law after *Quanta*.[66]

Likewise, Federal Circuit Judge Rader also reaffirmed *Fuji Photo* at the district court as he sat in the district court by designation.[67] In *Cornell Univ. v. Hewlett-Packard*, by citing *Quanta*, Judge Rader held that exhaustion requires a showing of an authorized sale of a patented article within the United States. He continued, however, that "this standard is not rigid.... The requirement that the sale be in the United States can be satisfied when the contracting and performance occur in the United States, even where some parts of the transaction occur abroad."[68]

Is a Covenant Not To Sue a Possible Solution to Circumvent *Quanta*?

In its amicus curiae brief, Motorola strongly urged the *Quanta* Court to limit its holding to products sold pursuant to a license, and leave the question of what impact a covenant not to sue may have on exhaustion for another day.[69] Although the Court eventually expressed no opinion on whether a covenant not to sue is tantamount to a license for the purpose of patent exhaustion, the Federal Circuit spoke on this issue less than one year after *Quanta*.

In *Transcore v. Electronic Transaction Consultants*, the Federal Circuit ruled that an unconditional covenant not to sue in effect authorizes sales by the covenantee for the purpose of exhaustion.[70] It reasoned that the difference between a covenant not to sue and a license is only one of form, not substance—both properly viewed as "authorizations." The Federal Circuit also held that, for exhaustion, what matters is whether the covenantee's sales were authorized, not whether the covenant was intended (either expressed or implied) to extend to customers.

The *Quanta* court clearly tried to reset a basic tone for patent exhaustion and reinforce the notion that a patent holder is merely entitled to a single royalty per patented device. The overall impact of *Quanta* is still evolving. Thus, it is important for both licensors and licensees to keep tracking the latest decisions and strategize their licensing policy accordingly. For example, after *Transcore*, either covenants not to sue or non-assertion clauses may no longer be an option for patent holders to get around *Quanta*. Also, to retain its rights to pursue downstream customers, the patentee should avoid, or at least narrowly define, the license granted to upstream suppliers. And for cross-border business transactions, making or performing the contract in the United States is a better approach in order to take the full advantage of *Quanta*.

60 The license between Monsanto and its seed partners only permits the sale of seeds containing its patented biotechnology to growers who additionally agreed to Monsanto's license restrictions. *Id.* at *1.

61 The court distinguished *Quanta* by stating that exhaustion was found to apply there because LG failed to employ sufficient conditions on its patent license to Intel. *See Monsanto Company v. Bowman*, 2009 WL 324103 (S.D. Ind.).

62 *See Static Control*, 615 F. Supp.2d at 584-585; also *Monsanto*, 2009 WL 536833 at *1.

63 The theory of this fine line is mainly based on the *Quanta* court's reaffirmation of its own precedent, *General Talking Pictures v. Western Electric*, 304 US 175 (1938), which allowed a patentee to lawfully restrict its licensee from making initial sales to commercial users.

64 *Fuji Photo Film Co., Ltd. v. Jazz Photo Corp.*, 394 F. 3d 1368 (Fed. Cir. 2005).

65 *LG Electronics, Inc. v. Hitachi, Ltd.*, 2009 WL 667232 (N.D. Cal.).

66 Notwithstanding the position adopted in LG Electronics, the controlling rule of law remains that "US Patent rights are only exhausted when the patentee, or its licensee, sells the patented article in the United States." *See Fujifilm Corp. v. Benun*, 2009 WL 2232523 (D.N.J.).

67 *Cornell Univ. v. Hewlett-Packard Co.*, 2008 US Dist. LEXIS 60209 (N.D.N.Y. Aug. 1, 2008).

68 *Id.* at *2 (citing *Litecubes, LLC v. Northern Light Prods., Inc.*, 523 F.3d 1353, 1369-71 (Fed. Cir. 2008)).

69 Brief of Amicus Curiae Motorola, Inc. in Support of Petitioners, *Quanta Computer, Inc. v. LG Electronics, Inc.*, 128 S.Ct. 2109 (2008) (No. 06-937).

70 *Transcore, LP v. Electronic Transaction Consultants Co.*, 563 F.3d 1271, 1274 (Fed. Cir. 2009).

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