



FENWICK & WEST LLP

# eBay v. MercExchange

## Supreme Court to Reconsider Injunction Remedy in Patent Cases

BY C.J. ALICE CHEN AND DARREN E. DONNELLY

The U.S. Supreme Court will soon reconsider the long-lived standards for granting permanent injunctions in patent infringement cases in *eBay Inc. v. MercExchange L.L.C.*, 401 F.3d 1323 (Fed. Cir. 2005).

The question the case poses—whether patentees not practicing their patents are automatically entitled to an injunctive remedy—is of great consequence to both patent owners and the infringers they confront. Such “non-practicing entities” or, pejoratively, “patent trolls,” have led many to complain for patent reform. Nonetheless, under the Federal Circuit’s current rule, if found to infringe a valid patent, a nonpracticing entity will be entitled to enjoin the infringer absent the injunction posing a threat to public health or safety or other exceptional reason.

This remedy stems from the right to exclude others from practicing the invention, which is the basis of the patent grant itself. In its certiorari petition, eBay questions whether automatically enforcing this right with a permanent injunction truly furthers the patent system’s fundamental policy of promoting the progress of science and useful arts. The petition and amici supporting it argue an injunction provides a nonpracticing entity with unjustified leverage in negotiating license fees for use of their inventions.

The rule that patentees — be they nonpracticing entities or not — are effectively entitled to permanently enjoin infringement is not new. The U.S. Supreme Court interpreted the patent grant early on to be a “complete monopoly ... a right so explicitly given and so complete that it would seem to need no further explanation than the word of the statute.” *Continental Paper Bag Co. v. E. Paper Bag Co.*, 210 U.S. 405 (1908). The Federal Circuit interprets *Continental Paper Bag* to mean that equity favors issuing a permanent injunction for patent infringement unless that injunction will harm a public interest, e.g., by threatening public health. *eBay Inc. v. MercExchange*.

eBay argues the statute, which invokes general principles of equity, is not so absolute. Section 283 of the Patent Act allows courts to issue injunctions “in accordance with the principles of equity” and “on such terms as the court deems reasonable.” 35 U.S.C. Section 283. eBay persuaded the district court that the traditional four-factor test — irreparable injury, adequacy of remedy at law, public interest and balance of hardships — applied in its favor.

The Eastern District of Virginia found specifically: (1) MercExchange would not suffer irreparable injury because it did not commercialize the invention, had no plans to do so and was willing to license or sell its patents; (2) MercExchange had an adequate remedy at law because money damages would fully compensate it for its loss of licensing revenue; (3) the public interest “equally supports granting an injunction to protect the plaintiff’s patent rights, and denying an injunction to protect the public’s interest in using a patented business-method that the patent holder declines to practice”; and (4) the balance of hardships slightly favored defendants. *eBay Inc. v. MercExchange L.L.C.*, 275 F. Supp. 2d 695 (E.D. Va. 2003).

The Federal Circuit reversed. It held that the statutory right to exclude was available to patentees whether or not they practiced their patented invention and, thus, an injunctive remedy also was available to “both groups.”

It further found that the lower court’s “general concern regarding business-method patents, however, is not the type of important public need that justifies the unusual step of denying injunctive relief,” and “[i]f the injunction gives the patentee additional leverage in licensing, that is a natural consequence of the right to exclude and not an inappropriate reward to a party that does not intend to compete in the marketplace with potential infringers.”

eBay’s certiorari petition asked the U.S. Supreme Court to consider “[w]hether the Federal Circuit erred in setting

forth a general rule in patent cases that a district court must, absent exceptional circumstances, issue a permanent injunction after a finding of infringement.”

On Nov. 28, the Court granted eBay’s petition, adding an additional question for briefing: whether the court should reconsider its precedents, such as *Continental Paper Bag*, on when permanent injunctions are appropriate in patent infringement cases. See No. 05-130.

eBay’s certiorari petition may presage arguments on the merits. It urges that the Federal Circuit’s automatic injunction gives patentees an enhanced negotiation stance not intended by the patent grant. It notes the Federal Circuit currently distinguishes between those who do, and do not, practice patented inventions in the context of the damages remedy — allowing lost profits for patentees with lost sales of commercial products and reasonable royalties for nonpracticing entities. eBay further argues that the current rule improperly shifts the burden of proof to the defendant to show the need for not issuing an injunction, whereas the party requesting relief usually has the burden to show the need for, and entitlement to, such relief.

A host of amici curiae supported eBay’s certiorari petition. The Computer & Communications Industry Association cites to this automatic injunction rule as one in a number of ways the Federal Circuit has promoted patents in a manner that aggravates many current problems with the patent system, including “low quality, portfolio racing, high transactions costs, widespread inadvertent infringement [and] opacity of patent information.”

In addition to echoing eBay’s textual argument, an amicus brief by 35 intellectual property law professors makes the policy argument that nonpracticing entities use the high cost of switching technologies, exceeding the value of the patented invention, to drive unfair settlements under the current rule and that full consideration of the four equitable factors will curtail this abuse.

The current rule that injunctions will issue as a matter of course has had wide-ranging effects. Startups are funded with the understanding that their intellectual property could have independent value to an acquirer. Generations of patent counsel have so advised their clients who have committed resources to the disclosure and patenting of inventions that may not be included in commercial products. Universities and other research institutions often rely on

industrial partners to fund research that then are licensed back to practice patented inventions.

Many expect the dispute to pit the interests of information technology industries against those of research institutions and pharmaceutical companies, and the community will watch with interest as amici weigh in on the merits.

The current rule is not without support. The Constitution’s grant of power to Congress itself is for “securing ... to inventors the exclusive right to their ... discoveries” and every U.S. patent states that it “grant[s] ... the right to exclude others.” Section 283’s language underlying eBay’s challenge is little changed from the prior patent statute, the Supreme Court’s interpretation of which helped create the current rule a century ago.

If the Supreme Court decides to deny patent trolls an injunctive remedy, crafting a rule that nonetheless preserves that remedy for other interests deemed worthy of it may prove challenging.

Industries founded on costly, long-term research could present substantial arguments that uncertainty in whether market exclusivity will exist at the end of the day may overturn the economic foundation of that research — something the patent system should promote. Pharmaceutical companies could argue, for example, that, but for the expected monopoly profit on drugs, costly development, trials and government approval may not be undertaken.

In litigation, the expectation of an injunction often motivates settlement, as noted in submissions in support of certiorari. Without that expectation, the alleged infringer chooses between paying a reasonable royalty by litigating, but possibly paying nothing if the patent is found invalid or not infringed, and paying that reasonable royalty up front in settlement. Practically, a rule denying nonpracticing entities injunctions could create incentives to flaunt patent rights and for the contrived working of a patent by nonpracticing entities for the purposes of litigation, which also could concern the court.

If the Supreme Court decides to readjust the rule from *Continental Paper Bag*, the degree of guidance it gives to district courts will be closely watched. For example, a rule that decides between a patent owned by a research university that is licensed to an industrial partner and one owned by a “patent troll” with the same licensee enlisted for the purposes of litigation, could be quite involved.

High-profile cases many view as emblematic of patent system woes highlight that broad discretion could lead to perhaps-troubling unpredictability. For instance, where Eolas Technologies (a university spin-off) and NTP (successor to an unsuccessful market entrant) — litigants against Microsoft and Research in Motion, respectively — fall along the spectrum could be unclear at the outset of litigation.

Public dissatisfaction with the patent system's current operation may motivate the Supreme Court to rewrite the rule from *Continental Paper Bag*. With the economic interests and public policies at stake, however, crafting a new rule balancing them may prove challenging indeed.

**C.J. Alice Chen** is an associate and **Darren E. Donnelly** is a partner in the litigation group at Fenwick & West in Mountain View.

**If you have questions please contact:**

C.J. Alice Chen, Associate, Litigation Group  
[achen@fenwick.com](mailto:achen@fenwick.com), 650-335-7163

Darren E. Donnelly, Partner, Litigation Group  
[ddonnelly@fenwick.com](mailto:ddonnelly@fenwick.com), 650-335-7624

©2006 Fenwick & West LLP. All Rights Reserved.

THIS UPDATE IS INTENDED BY FENWICK & WEST LLP TO SUMMARIZE RECENT DEVELOPMENTS IN THE LAW. IT IS NOT INTENDED, AND SHOULD NOT BE REGARDED, AS LEGAL ADVICE. READERS WHO HAVE PARTICULAR QUESTIONS ABOUT THESE ISSUES SHOULD SEEK ADVICE OF COUNSEL.