

April 30, 2014

Practice Group(s):
IP Litigation

Supreme Court Redefines Framework for Determining Whether a Patent Case is Exceptional and Warrants an Award of Attorney's Fees

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On April 29, 2014, the Supreme Court delivered much-anticipated decisions in the *Octane* and *Highmark* cases and redefined the framework for determining whether a patent lawsuit is “exceptional,” justifying an award of attorney’s fees. The decisions come at the crux of a nationwide debate about how best to quell frivolous patent litigation, and the accused infringers in both cases urged the Supreme Court to refine the “exceptional case” law in order to dis-incentivize meritless patent cases. Against this setting, the *Octane* and *Highmark* cases presented two issues to the Supreme Court:

1. What standard should draw the line between a losing case and an exceptional one?
2. What deference should appellate courts give to a district court’s decision that a case is (or is not) exceptional?

Octane

Octane presented the first issue, leading the Court to reset the standard for determining when a case is exceptional.¹

The District Court Grants Summary Judgment, but Does Not Find the Case Exceptional Under the Brooks Furniture Standard

Octane prevailed on summary judgment, but the district court did not find the case exceptional under the Federal Circuit’s *Brooks Furniture* standard, which required demonstrating by clear and convincing evidence that a case fell into one of two categories:

- One that involved “material inappropriate conduct” such as “willful infringement, fraud or inequitable conduct in procuring the patent, misconduct during litigation, vexatious or unjustified litigation, conduct that violates Fed. R. Civ. P. 11, or like infractions”; or
- One that was both (1) “objectively baseless,” meaning that it was “so unreasonable that no reasonable litigant could believe it would succeed,” and (2) “brought in subjective bad faith.”²

Octane argued that the *Brooks Furniture* standard was too inflexible and prevented the Court from considering a broader range of factors—e.g., that the patentee had the patent “sitting on a shelf” and did not practice it, and initially chose an inconvenient venue.³ *Octane* urged the Court to change the standard to allow district courts to consider a wider net of equitable factors on the grounds that under the current “exceptional case” regime “prevailing accused infringers have no hope of recouping fees even if they win, [and] federal courts serve as the playing field for extortion.”⁴

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The Supreme Court Rejects the Brooks Furniture Standard

In its April 29, 2014 decision, the Supreme Court unanimously agreed that the *Brooks Furniture* framework was too rigid; indeed, it found *Brooks Furniture* to be “so demanding that it would appear to render § 285 [the exceptional case statute] largely superfluous.”⁵ With respect to the first *Brooks Furniture* category, the Supreme Court noted that it required independently sanctionable conduct, and thus precluded a district court from awarding fees where the conduct is not necessarily independently sanctionable, but still so exceptional as to justify fees. The Court likewise found the second *Brooks Furniture* category too inflexible because it mandated a finding of both “objective baselessness” and “subjective bad faith,” even when one or the other alone would justify an exceptional case finding.⁶

The Court further highlighted that the root of the *Brooks Furniture* standard was inapposite to patent litigation. *Brooks Furniture*'s framework stems from the “sham litigation” exception to antitrust immunity under the *Noerr-Pennington* doctrine for filing a lawsuit. The Court, however, found no reason to import the standard for determining whether one should lose the protection of antitrust immunity into the standard for determining whether one should pay attorney's fees for an exceptional patent case. The Court concluded that the exception for antitrust immunity called for a different standard because the threat of antitrust liability and treble damages “far more significantly chills the exercise of the right to petition” the courts than “the mere shifting of attorney's fees.”⁷

The Supreme Court Establishes a New Standard for Exceptional Case Determinations

In establishing the new “exceptional case” standard, the Supreme Court focused on the meaning of the word “exceptional” today, and in 1952 when the word appeared in section 285—that is, “uncommon,” “rare,” or “not ordinary.” In view of this definition, the Court reasoned that a case is exceptional because it “is simply one that stands out from others with respect to the substantive strength of a party's litigating position (considering both the governing law and the facts of the case) or the unreasonable manner in which the case was litigated,” and that district courts can determine whether a case “stands out” under the totality of the circumstances.⁸ Moreover, the Court rejected the requirement to demonstrate an entitlement to attorney's fees by clear and convincing evidence, because nothing in the statute required such a high burden of proof. The Court held instead that “preponderance of the evidence” was appropriate.⁹

Highmark

In *Highmark*, the Court determined a second issue in the “exceptional case” law: whether appellate courts should review exceptional case determinations *de novo*, or, as the Court ultimately held, for abuse of discretion.

District Court Finds Patentee's Conduct Exceptional and Awards Attorney's Fees

Highmark, Inc. filed a declaratory judgment action to determine invalidity, non-infringement, and unenforceability as to one of Allcare Health Management Systems, Inc.'s patents.¹⁰ Following summary judgment in Highmark's favor, the District Court concluded that the case was exceptional and awarded attorney's fees, finding that Allcare engaged in “vexatious, and at times, deceitful conduct,” including “maintain[ing] infringement claims well after such

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claims had been shown by its own experts to be without merit and did so as a tactic to provide leverage against Highmark's pending claims."¹¹

The Federal Circuit Applies De Novo Review and Reverses the Exceptional Case Finding

The Federal Circuit partially reversed the district court's fee award, holding that under the second category of the (now rejected) *Brooks Furniture* framework, the objective baselessness inquiry is "a question of law based on underlying mixed questions of law and fact and is subject to *de novo* review."¹² It therefore reviewed the district court's determination of objective reasonableness "without deference."¹³ By reviewing the case *de novo*, the Federal Circuit relied on its own theory—which Allcare never advanced—to preclude an exceptional case finding.¹⁴ Notably, Judge Mayer dissented from the Federal Circuit's opinion, asserting that deference was particularly appropriate in the exceptional case context: "As an appellate court, we are ill-suited to weigh the evidence required to make an exceptional case determination. . . . [The district court's] intimate familiarity with the facts of the case, and the parties involved, place it in a far superior position to judge whether or not a litigant's claims of infringement were objectively baseless."¹⁵

Highmark then filed a petition for rehearing en banc, which was denied over the dissent of five judges who emphasized the inconsistency between the panel majority's decision and Supreme Court precedent.¹⁶

The Supreme Court Unanimously Agrees that Abuse of Discretion, and Not De Novo Review, is the Appropriate Standard of Review

Before the Supreme Court, Highmark urged that the Federal Circuit should have given the district court's opinion deference.¹⁷ *De novo* review, Highmark argued, makes it easier to overturn fee awards, rather than impose them, because a fresh look at the case allows patentees to come up with newly minted legal arguments on appeal and overturn the exceptional case finding.¹⁸ Industry organizations, such as the American Intellectual Property Law Association ("AIPPLA"), argued that a decision from the Supreme Court was necessary to, among other things, (1) deter litigants from "abusive and improper litigation practices"; (2) "alleviate the costs of patent litigation"; and (3) foster innovation.¹⁹ The United States likewise agreed that the Supreme Court's intervention was necessary.²⁰

Allcare argued that there was no evidence that changing the standard of review would ultimately change the result when reviewing exceptional case determinations on appeal.²¹ In support of Allcare's position, the Boston Patent Law Association ("BPLA") argued that the "Federal Circuit's breadth of experience with patent cases since 1982 gives it unique perspective and, with it, the ability to distinguish between claims and defenses that have no merit from those that are legitimate, if novel or aggressive."²²

The Supreme Court, however, did not address these policy arguments. It reviewed the *Highmark* case in connection with *Octane*, and unanimously concluded that, in view of the newly articulated exceptional case standard discussed above, the Federal Circuit erred when it reviewed the District Court's decision *de novo*.²³ Because the finding of whether a case is exceptional is "a case-by-case exercise" of a district court's discretion, the decision is to be reviewed on appeal for abuse of discretion.²⁴

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Conclusion

The Supreme Court's unanimous *Octane* and *Highmark* decisions set a new framework for "exceptional case" determinations. A party can now demonstrate, by a preponderance of the evidence, that a case is exceptional based on the "totality of the circumstances" at hand, and the district court's "exceptional case" decision is reviewed for abuse of discretion at the appellate court level.

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¹ *Octane Petitioner's Br. at 9*; see also *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, No. 12-1184, slip. op. at 1, 3-4 (Apr. 29, 2014).

² *Brooks Furniture Mfg., Inc. v. Dutailier Int'l, Inc.*, 393 F.3d 1378, 1381-1382 (Fed. Cir. 2005); *iLOR, LLC v. Google, Inc.*, 631 F.3d 1372, 1378 (Fed. Cir. 2011). In the *Kilopass* case decided while *Octane* was before the Supreme Court, the Federal Circuit held that subjective bad faith did not require actual knowledge of objective baselessness; instead, subjective bad faith could be demonstrated through "reckless conduct," and "objective baselessness alone can create a sufficient inference of bad faith." *Kilopass Tech., Inc. v. Sidense Corp.*, 738 F.3d 1302, 1310-1314 (Fed. Cir. 2013).

³ *Octane Petitioner's Br. at 12*.

⁴ *Id.* at 4.

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⁵ *Octane*, slip op. at 11. Justice Scalia joined the opinion with the exception of footnotes regarding the history and purpose of the exceptional fees statute.

⁶ *Id.* at 8-9.

⁷ *Id.* at 10.

⁸ *Id.* at 7-8.

⁹ *Id.* at 13.

¹⁰ *Highmark, Inc. v. Allcare Health Mgmt. Sys., Inc.*, 706 F. Supp. 2d 713, 717 (N.D. Tex. 2010)

¹¹ *Id.* at 737.

¹² *Id.* at 1309 (quoting *Bard Peripheral Vascular, Inc. v. W.L. Gore & Assocs., Inc.*, 682 F.3d 1003, 1004-06 (Fed. Cir. 2012)).

¹³ *Id.*

¹⁴ *Id.* at 1313-15.

¹⁵ *Id.* at 1321 (Mayer, J., dissenting).

¹⁶ See *Highmark, Inc. v. Allcare Health Mgmt. Sys., Inc.*, 701 F.3d 1351 (Fed. Cir. 2012) (denial reh'g en banc).

¹⁷ *Highmark Petitioner's Br.* at 2-3.

¹⁸ *Id.* at 3.

¹⁹ *Highmark, AIPLA Amicus Br.* at 28, 31, 34.

²⁰ *Highmark, United States Amicus Br.* at 8-10.

²¹ *Allcare Respondent's Br.* at 4.

²² *Highmark, BPLA Amicus Br.* at 3.

²³ See *Highmark, Inc. v. Allcare Health Mgmt. Sys., Inc.*, No. 12-1163, slip. op. at 1 (Apr. 29, 2014).

²⁴ *Id.* at 4 (citing *Pierce v. Underwood*, 487 U.S. 552, 558 (1988)).