

# Recent Decisions In The United States

A recurring feature

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## SUPREME COURT FINDS INTERNET FILE-SHARING SERVICES LIABLE FOR INDUCING COPYRIGHT INFRINGEMENT

In analyzing whether a distributor of software was liable for copyright infringement by users of the software, the U.S. Supreme Court recently adopted the inducement law used in patent infringement cases, and concluded that based on this standard, anyone who distributes a device with the objective of promoting its use to infringe a copyright, as shown by clear expression or other affirmative steps taken to foster infringement, is liable for the resulting acts of infringement by third parties.

This case, *Metro-Goldwyn-Mayer Studios Inc. v. Grokster, Ltd.*, No. 04-480 (June 27, 2005), related to software products provided by the defendants that allow computer users to share electronic files through peer-to-peer networks. The plaintiffs sued defendants for the copyright infringement committed by users of their software in transferring copyrighted files over these networks. Peer-to-peer networks require no central computer server to mediate the exchange of files. Because of this decentralization, the defendants were not aware of exactly what files were copied and when those files were copied. The plaintiffs introduced evidence, however, showing that the principal object of the business models of the defendants was the use of the software to download copyrighted works. In addition, studies by the plaintiffs revealed that over 90% of the files being transferred using the defendant's software were copyrighted.

Before reaching the Supreme Court, the case was first heard in a District Court and then appealed to the Court of Appeals. In the first instance, the District Court found that the users of defendants' software were infringing plaintiffs' copyrights. The court found, however, that the defendants could not be liable for this infringement because they had no actual knowledge of specific acts of infringement. This decision was affirmed by the Court of Appeals for the Ninth Circuit. Relying on the Supreme Court's decision in *Sony Corp. of America v. Universal City Studios*, the Court of Appeals held that distribution of a commercial product capable of substantial non-infringing uses could not give rise to contributory liability for infringement unless the distributor had actual knowledge of specific instances of infringement and failed to act on

that knowledge. Because the defendants' software was capable of non-infringing uses and because the defendants had no actual knowledge regarding the acts of infringement, the Appeals Court found that they could not be liable for copyright infringement.

The Supreme Court began its review of the case by revisiting its decision in *Sony Corp.* In that case, copyright holders sued Sony for secondary liability of infringement by distributing VCRs. The Supreme Court found that Sony could not be liable because the devices had significant non-infringing uses. The Court noted that the *Sony* case barred liability based on presuming or imputing intent to cause infringement solely from the design or distribution of a product capable of substantial lawful use, which the distributor knows is in fact used for infringement. The decision, however, did not mean that whenever a product is capable of substantial lawful use, the producer can never be held secondarily liable, particularly when actual intent to cause infringing use can be shown.

The Supreme Court next noted that at common law a defendant who not only expected but invoked infringement of a copyright could be liable for infringement. The Court also noted that in the related field of patent law, inducement to infringe was well recognized and statutorily established. The Supreme Court, therefore, chose to adopt the patent law inducement doctrine and apply it to copyright cases, and it held that anyone who distributes a device with the objective of promoting its use to infringe copyright, as shown by clear expression or other affirmative steps taken to foster infringement, is liable for the resulting acts of infringement by third parties.

Applying this standard to the present case, the Supreme Court found that significant evidence existed proving that the defendants had affirmatively sought to encourage infringement. Specifically, each company showed itself to be aiming to satisfy a known source of demand for copyright infringement; neither company attempted to develop any tools to diminish infringing activity; and the commercial sense of their enterprises turned on high-volume use, which the record showed was infringing. Therefore, the Court overturned the decision of the Court of Appeals.

## PATENT OWNERS WHO MISMARK A PRODUCT AS PATENTED ARE NOT GUILTY OF FALSE MARKING UNLESS THEY INTEND TO DECEIVE THE PUBLIC

U.S. patent law provides that a party who falsely marks a product as patented will be subject to a fine for each incidence of false marking. In *Clontech Labs, Inc. v. Invitrogen Corp.*, No. 03-1464, 04-1099 (Fed. Cir. May 5, 2005), the Federal Circuit concluded that the patent marking statute is not a statute of strict liability but requires some proof that articles were mismarked for purposes of deceiving the public.

This case arose out of a lawsuit filed by Clontech against Invitrogen for false patent marking. The patents involved in this case were all directed to RNase H deficient Reverse Transcriptase polypeptides (“RTs”). Invitrogen markets Rnase H deficient RTs, kits including these Rnase H deficient RTs, AND cDNA libraries made using Rnase H deficient RTs. All of these products were marked as covered by Invitrogen’s Rnase H deficient RTs patents.

The trial court held that Invitrogen had falsely marked its Rnase H deficient RTs, kits, and cDNA libraries, and found that none of the patents were directed to cDNA libraries. In addition, the court found that all the patent claims included the limitation “substantially no Rnase H activity” and that a 2000 test performed by Invitrogen established that its Rnase H deficient RTs did not meet this limitation. Therefore, the court found that all of these products were deliberately mismarked.

On appeal, the Federal Circuit first reviewed the false marking statute and noted that mismarking occurs if the article in question is not covered by at least one claim of each patent marked on the article. The Court, however, held that mismarking alone is insufficient to establish false marking. Rather, the statute requires that a party have an intent to deceive the public. Therefore, if a patentee can show it had a reasonable belief that the article were properly marked, it cannot be liable for false patent marking.

Next, the Federal Circuit held that the trial court clearly erred when it concluded that the results of the 2000 tests put Invitrogen on clear notice that its Rnase H deficient RTs and kits were not covered by its patents. The Court found that Invitrogen had put forth un rebutted testimony that the 2000 tests did not establish that Invitrogen’s products failed to meet the limitation of “substantially no Rnase H activity.” Therefore, the Federal Circuit reversed the trial court’s finding of false marking with respect to these products.

With respect to the cDNA libraries, the Federal Circuit affirmed the finding of false patent marking. For these products, Invitrogen did not contend that its patents covered these products or that it had a good faith belief that they did cover these products. Therefore, Invitrogen was guilty of false patent marking with respect to these products.

## SOFTWARE COPIES MADE OUTSIDE THE U.S. FROM A MASTER VERSION EXPORTED FROM THE U.S. ARE DEEMED SUPPLIED FROM THE U.S. FOR PURPOSES OF INFRINGEMENT LIABILITY

Section 271(f) of the U.S. patent laws makes it an act of infringement to supply all or a substantial portion of the components of a patented invention from the U.S. in such a manner as to induce the combination of those components outside the U.S. in a way that would infringe the patent if the combination occurred in the U.S. In *AT&T Corp. v. Microsoft Corp.*, No. 04-1285 (Fed. Cir. July 13, 2005), the Court of Appeals for the Federal Circuit found that under §271(f), exporting a master version of software from the United States constitutes supplying a component from the United States, and therefore, can result in liability for patent infringement for every copy of that software made abroad.

This case relates to Microsoft’s Windows® software. Microsoft supplies a limited number of master versions of its software to entities outside the U.S., who then generate multiple copies of the software for installation on foreign computers. The master versions of the software incorporate certain codecs, which when installed on a computer, were alleged to infringe AT&T’s patent. In the district court, Microsoft moved for partial summary judgment on the issue of its liability under §271(f) for foreign sales of computers with the Windows® software. Microsoft argued that software was not a “component” of a patented invention within the meaning of the statute and that, even if it were a component, no components had been supplied from the United States because all the copies that are installed on foreign computers are made abroad.

On appeal, the Federal Circuit first noted that in another case it had recently determined that software may be a “component” of a patented invention. Specifically, in *Eolas Techs. Inc. v. Microsoft Corp.*, the court had held that nothing in the statute limited its application to “machines” or physical structures. (See April 2005 Issue of *LES Nouvelles* for further information on this case). Therefore, the only issue was whether or not software replicated abroad from a master version exported from the United States would be considered “supplied” from the United States.

In resolving this issue, the Federal Circuit began by noting that the “supplying” of software commonly involves generating a copy. In fact, “copying... is part and parcel of software distribution.” Therefore, the court held that for software “components,” the act of copying is subsumed in the act of “supplying.” Therefore, sending a single copy abroad with the intent that it be replicated invokes § 271(f) liability for those foreign made copies.

The court also noted that § 271(f) was passed specifically to close a loophole and was clearly intended to have an extraterritorial effect. Microsoft’s argument, however,

would subvert this goal, because it would permit technical avoidance of the statute by ignoring the advances in a field of technology and its associated industry practices that developed after the enactment of the statute. Therefore, this view could not be correct.

### **THERE IS A BROAD EXEMPTION TO INFRINGEMENT LIABILITY FOR USES OF PATENTED INVENTIONS IN ACTIVITIES RELATED TO THE FEDERAL REGULATORY PROCESS**

Section 271(e)(1) of the U.S. patent laws provides an exemption from infringement liability for the use of a patented invention solely for uses reasonably related to the development and submission of information to federal entities, such as the FDA. In *Merck KGaA v. Integra Lifesciences, Ltd.*, No. 03-1237 (June 13, 2000), the Supreme Court held that § 271(e)(1) protects the use of patented compounds in preclinical studies as long as there is a reasonable basis to believe that the compound could be the subject of an FDA submission and the experiments will produce the types of information relevant to an FDA submission.

This case related to several patents owned by Integra related to the RGD peptide. Merck had provided funding to a doctor at the Scripps Research Institute investing tumor growth. In his research, the doctor experimented with RGD peptides supplied by Merck to inhibit tumor growth. During the course of his research, the doctor experimented with several different RGD peptides, many of which were never submitted to the FDA as a possible drug candidate. After learning of this activity, Integra sued Merck, Scripps, and the doctor for patent infringement based on their use of the RGD peptides in their experiments.

In the hearing of the case in the first instance at the district court, the parties tried the issue of whether the defendants' activities were protected by § 271(e)(1). The jury found that they were not, and on a motion for judgment as a matter of law, the district court agreed that the evidence was sufficient to show that any connection between the experiments and FDA review was insufficiently direct to qualify for the § 271(e)(1) exemption. The defendants appealed, and the Court of Appeals for the Federal Circuit affirmed the decision of the district court on this point. The Federal Circuit found that the defendants' activities was not clinical testing to supply information to the FDA, but only general biomedical research to identify new compounds.

The Supreme Court began its review of the case by noting that § 271(e)(1) provides a wide berth for the use of patented drugs in activities related to the federal regulatory process. In the court's view, the statute protects all uses of patented inventions that are "reasonably related to the development and submission of *any* information" to the FDA (emphasis in original). Therefore, the court held that this necessarily includes preclinical information. Moreover, the type of protected testing includes not only testing related to the safety of drugs in humans, but all testing that would be of interest to the FDA in making its analysis. This includes preclinical *in vitro* and *in vivo* studies.

The Supreme Court also held that the testing need not be on drugs that ultimately become the subject of an FDA submission. The Court noted that in the majority of testing, most scientists have no way of knowing whether an initially promising candidate will actually prove successful until after it has been tested. Therefore, to limit the application of § 271(e)(1) to only those drugs that ultimately result in FDA submissions would effectively limit the safe harbor to generic versions of brand name drugs. Thus, the Court held that a drug will be protected by § 271(e)(1) if a drug maker has a reasonable belief that a patented compound may work to produce a particular effect, and uses the compound in research that, if successful, would be included in an FDA submission.

### **PATENT RIGHTS MAY BE EXHAUSTED EVEN WHEN A LICENSOR EXPRESSLY RESERVES THE RIGHT TO SUE THE LICENSEE'S CUSTOMERS**

The fact that a licensor has expressly reserved the right to sue a licensee's customers for infringement does not prevent exhaustion of those rights unless the licensor requires the licensee to condition its sales of the products to those customers. In *Minebea Co., Ltd. v. Pabst*, No. Civ. A. 97-0590 (D.D.C. June 24, 2005), the District Court for the District of Columbia held that despite such an express reservation, the licensee was authorized to sell the products at issue unconditionally, and therefore, the licensor's patent rights would be exhausted unless the those products had a reasonable noninfringing use.

This case related to several disk drive patents owned by Pabst and to disk drive motors sold by Minebea. Pabst and Minebea had entered into a settlement agreement in 1995. As part of that agreement Pabst expressly warranted not to sue Minebea for contributory infringement or inducement of infringement of its disk drive patents based on the sale by Minebea of disk drive motors. Pabst, however, expressly reserved the right to sue Minebea's customers who incorporated those motors in a disk drive. After Pabst asserted these patents against Minebea's customers, Minebea filed suit for a declaratory judgment that the patents were invalid and that Minebea's customers did not infringe those patents.

On summary judgment, Minebea argued that its sale of disk drive motors exhausted Pabst's patent rights based on the 1995 settlement agreement. In deciding the motion, the Court found that in order to prove exhaustion, Minebea needed to show that: (1) it had authority to sell the motors; (2) there were no conditions on its sale of motors; (3) the motors have no substantial noninfringing use; and (4) the sale of the motors occurred under the United States patents.

In determining whether Minebea had authority to sell the motors, the court looked to the 1995 settlement agreement as well as several other agreements between the parties. The court found that the agreement waived Pabst's right to sue Minebea for patent infringement based on the sale of its motors. By waiving this right, Pabst had, therefore, authorized Minebea to manufacture

and sell such motors.

The court next looked to whether the sale was, in fact, unconditional. The court began by noting that the parties to the settlement agreement had anticipated that Pabst would retain the right to sue Minebea's customers. The court held, however, that this reservation did not make Minebea's authority to sell its motors "conditional." The court found that Pabst could have included in the agreement a requirement that Minebea's sales to its customers be conditioned in some way, but did not. Therefore, Minebea's sales to its customers were unconditional, and the fact that they were unconditional, was not a breach of the settlement agreement. Therefore, even though the parties had clearly intended that Pabst be able to sue Minebea's customers, the law of patent exhaustion required a different result.

With respect to the remaining two issues, the court found that issues of fact remained as to whether Minebea met those requirements. Specifically, the court noted that Pabst introduced evidence that the motors could be used in other devices, which would not infringe its patents. Therefore, there was an issue of fact as to whether the motors had a substantial noninfringing use. Finally, with respect to whether the sales were made under a U.S. patent, the court noted that for the sales to be under a U.S. patent they had to be made in the U.S. Since there was evidence that at least some of the sales occurred outside the U.S., the court held that an issue of fact remained as to this point as well.