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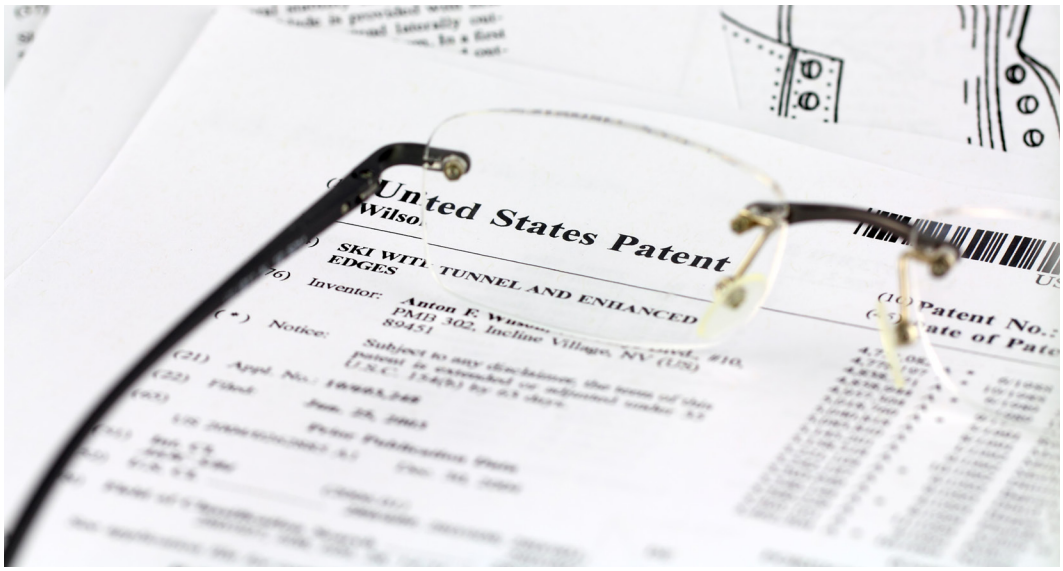
New Hope for Patent Owners: Supreme Court Eases the Path to Enhanced Damages



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UNDER THE NEW STANDARD, DISTRICT COURTS WILL HAVE CONSIDERABLY MORE DISCRETION TO FIND THAT AN ACCUSED INFRINGER ACTED WILLFULLY AND ENHANCE DAMAGES UP TO THREE TIMES THE AMOUNT OF COMPENSATORY DAMAGES.

On June 13, in *Halo Electronics, Inc. v. Pulse Electronics, Inc.* (available at http://www.supremecourt.gov/opinions/15pdf/14-1513_db8e.pdf), No. 14-1513 (U.S. June 13, 2016), the U.S. Supreme Court established a new standard for determining when a district court may award enhanced damages in patent infringement cases. The decision followed the same approach adopted in *Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, 134 S. Ct. 1749 (2014), where the Court concluded that the broad statutory language governing when a court may award attorney's fees was at odds with the U.S. Court of Appeals

for the Federal Circuit's more narrow test for awarding attorney's fees. Under the new standard for enhanced damages in patent cases, district courts will have considerably more discretion to find that an accused infringer acted willfully and enhance damages up to three times the amount of compensatory damages.

The Court's Analysis

Similar to the section governing the award of attorney's fees, the patent statute provides no guidance as to when enhanced damages are appropriate and, instead, simply states that district courts "may increase the damages up to three times the amount found or assessed." 35 U.S.C. § 284. The Supreme Court's unanimous opinion, authored by Chief Justice Roberts, began by summarizing the long history of awarding enhanced damages in patent infringement cases in the United States where the defendant's infringement was "wanton," "malicious," "intentional" or "in bad faith." *Halo*, No. 14-1513, slip op. at 2-4. In contrast to compensatory damages, enhanced damages have previously been described as "vindictive and punitive" and were permitted under earlier versions of the patent statute "according to the circumstances of the case." *Id.* at 3 (internal quotations omitted). The Supreme Court's recent decision explained that lower courts had consistently awarded enhanced damages when they determined that the accused infringer acted deliberately, willfully or in bad faith.

The question presented to the Court in *Halo* and the companion case, *Stryker Corp.* v. *Zimmer, Inc*., No. 14-1520, was whether the Federal Circuit erred in applying a rigid two-part test for deciding when enhanced damages are appropriate under 35 U.S.C. § 284. In both cases, the Federal Circuit found that enhanced damages were not appropriate, relying on the test it articulated in its 2007 *en banc* decision in *In re Seagate Technology, LLC*, 497 F.3d 1360 (2007). Under the *Seagate* test, enhanced damages could only be awarded when a patent owner showed, by clear and convincing evidence, that the accused infringer "acted despite an objectively high likelihood that its actions constituted infringement of a valid patent" ***and*** that the risk of infringement "was either known or so obvious that it should have been known to the accused infringer." *Halo*, No. 14-1513, slip op. at 5. The Court concluded the *Seagate* test was inconsistent with the language of the patent statute (which provides district courts with discretion to award enhanced damages), as well as 180 years of cases establishing that enhanced damages should be awarded when there is "egregious infringement behavior." *Id*. at 8-9.

As a matter of substance, the Court first took issue with the requirement under *Seagate* of finding "***objective*** recklessness" in addition to a ***subjective*** element that the infringer acted despite the fact that the infringer knew or should have known of such an infringement risk. *Id*. at 9-10 (emphasis added). Under *Seagate*, an accused

infringer could avoid enhanced damages if they were able to develop an objectively sound noninfringement or invalidity defense even after litigation ensued, for example. Additionally, an infringer could avoid enhanced damages even if such a defense was not known to the accused infringer at the time it was infringing and regardless of whether the defense was ultimately successful. *Id.* The Court criticized the *Seagate* test because it could "insulate[] the infringer from enhanced damages, even if he did not act on the basis of the defense or was even aware of it." *Id.* at 10. Instead, the Court stated, the test for enhanced damages should focus on culpability for egregious behavior "measured against the knowledge of the actor at the time of the challenged conduct." *Id.* The opinion stressed that the language of the statute itself provided the district court with discretion on the issue of enhanced damages. Thus, while a finding of "egregious conduct" is not a prerequisite to awarding enhanced damages, "such punishment should generally be reserved for egregious cases typified by willful misconduct" and not for "garden variety cases." *Id.* at 11.

The Court also rejected the requirement under *Seagate* of proving willfulness by clear and convincing evidence. *Id.* at 12. Consistent with the Court's follow-on decision to *Octane Fitness* in *Highmark Inc.* v. *Allcare Health Management System, Inc.*, 134 S. Ct. 1744 (2014) (addressing the appellate review standard for an award of attorney's fees), the Court noted that there is no basis for requiring a heightened standard of proof for enhanced damages. Citing its reasoning in *Octane*, the Court again reiterated that "patent-infringement litigation has always been governed by a preponderance of the evidence standard." *Halo*, No. 14-1513, slip op. at 12.

Finally, the Court rejected the Federal Circuit's standard of appellate review on the issue of enhanced damages. *Id.* at 12-13. Again relying on its reasoning in *Octane* and *Highmark*, the Court rejected the Federal Circuit's "tripartite framework" of review under the *Seagate* standard, in which the determination of objective recklessness was reviewed *de novo*, the determination of subjective knowledge was reviewed for substantial evidence, and the ultimate determination on enhancement was reviewed for abuse of discretion. *Id.* The Supreme Court held that the district court's discretion on whether or not to enhance damages should be reviewed on appeal for abuse of discretion.

Concurring Opinion

Several amici who submitted briefs in the case were concerned with the effect that loosening the standards for willfulness may have on innovation and competitiveness. A concurring opinion authored by Justice Breyer and joined by Justices Kennedy and Alito addresses many of these concerns. The concurring opinion notes, for example, that there are many scenarios where a business owner may elect not to respond or act on a notice letter from a patent owner, who may never intend to enforce its patents in

litigation. That business owner may not be engaging in reckless behavior justifying an award of enhanced damages. *Id.*, slip op. at 4 (Breyer, J., concurring). Further, Justice Breyer notes that not all small businesses may be able to afford obtaining an opinion of counsel and that a failure to obtain an opinion need not prescribe a finding of enhanced damages. *Id.* at 2-3 ("an owner of a small firm, or a scientist, engineer, or technician working there, might, without being 'wanton' or 'reckless,' reasonably determine that its product does not infringe a particular patent, or that that patent is probably invalid."). The concurrence also notes that, due to the Federal Circuit's expertise on patent issues, there may be instances where a district court improperly awards enhanced damages because it erroneously misapprehended the reasonableness of a patent defense. *Id.* at 5. In such a case, the Federal Circuit would be within its purview to find an abuse of discretion. *Id*. Justice Breyer's concurrence may provide accused infringers with some comfort in its observation that enhanced damages should be not be abandoned, but rather carefully applied "to ensure that they only target cases of egregious misconduct." *Id.* at 5.

Given the new standard articulated in *Halo*, the task will largely fall on the district courts to sort out what behavior will be deemed "egregious," warranting enhanced damages, and what behavior will be characterized as merely routine or "garden variety" infringement.