

The Fallacy of Trademark Residual Goodwill

BY DAVID S. RUDER



David S. Ruder

I. Introduction

When a trademark owner abandons his trademark, what legal rights does he retain to prevent someone else from acquiring and using that mark? A common flawed belief among trademark owners and trademark lawyers is that the owner retains “residual goodwill”—that is, the former trademark owner asserts that he

has the power to bar someone else’s use of his old mark due to a lingering association consumers may continue to have between the mark and the former owner.

The theory behind residual goodwill is that because consumers may associate a discontinued trademark with the producer of a discontinued product, any new user of the trademark would be improperly trading off of the residual goodwill that still exists from when the trademark was used in the marketplace. According to this argument, a new user could employ a discontinued trademark only after consumers have ceased to associate the trademark with the original owner and residual goodwill has dissipated.

There is almost no support whatsoever for the residual goodwill theory in trademark law or practice. Once a trademark is abandoned, it reverts to the public domain and is then available to new users. An innovator may use an abandoned trademark in its original class of goods or services, provided that no false connection is made to the original producer. Residual goodwill, if it even exists, does not give the previous trademark owner any right to prevent the new user’s acquisition and employment of the mark.

II. What Is the Current “Abandonment” System?

Once a trademark is “abandoned” under the trademark laws, no goodwill remains in the trademark, residual or otherwise. The abandoned status allows new users of a trademark to launch a new product or service, and importantly can serve as a defense to a trademark infringement suit. In discussing trademark abandonment, there are two important issues to understand: (1) how exactly a

trademark becomes abandoned under the trademark laws and (2) the impact of abandonment on the trademark.

A. The Abandonment Process

Whenever a trademark is discontinued, there is a very real risk that the trademark will be deemed “abandoned” under the trademark laws. There is an explicit provision in the Lanham Act (the federal trademark statute) describing how a trademark becomes abandoned:

A mark shall be deemed to be “abandoned” . . . when its use has been discontinued with intent not to resume such use. Intent not to resume may be inferred from circumstances. Nonuse for three consecutive years shall be prima facie evidence of abandonment. “Use” of a mark means the bona fide use of such mark made in the ordinary course of trade, and not made merely to reserve a right in a mark.¹

This means that if a marketer stops using a trademark for three years and has not done anything substantial within that time to reintroduce the trademark into commerce, the trademark becomes abandoned. To keep trademark rights alive, marketers must *use* the trademark in commerce.

It used to be that marketers would attempt to make “token” shipments of products in order to keep trademarks in commerce and not risk a trademark becoming abandoned and possibly falling into a new competitor’s hands. Procter & Gamble went as far as to create a “Minor Trademarks Program” that was designed to “rebut any such inference of abandonment” by shipping fifty units bearing a discontinued trademark name to ten

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Keeping Current with the Chair

ROBERT W. SACOFF

Section Policy and Beyond

"I laughed so hard when I read your column, I almost choked on my corn flakes," my friend said when we ran into each other. We were both waiting in line to get into the Supreme Court to hear the arguments in the Victoria's Secret case last fall. I had worked on the *amicus curiae* brief submitted by the ABA, and he had worked on the *amicus* brief submitted by another professional association. I had written the article in question¹ for a Section Chair's Bulletin to explain the interesting process of getting authorization to file an *amicus* brief on behalf of the ABA. That procedure was somewhat more complicated than in my friend's association. I had not intended to make the article amusing, but I told my friend I was happy it made his day, and did not make him choke on his corn flakes.

The purpose of this column is to discuss how Section policy interacts with, and sometimes becomes, ABA policy, and to make it more transparent and accessible to our Section's membership. The ABA Section of Intellectual Property Law, at more than 21,000 members, is the largest professional IP law association in the world. But it is a relatively small segment of the American Bar Association itself, which, at more than 410,000 members, is the largest lawyers' association in the world. Our Section is but one of more than thirty ABA "entities"—Sections, Divisions, Committees, and Forums. Our Section's role in the ABA, and its ability to speak with the voice and force of the ABA, is a distinguishing feature of our group when compared with other leading IP associations. So what are the implications of this symbiotic relationship between Section and parent organization? Formulating ABA policy can seem a bit daunting, as my friend inferred from my article about ABA *amicus* briefs, which, I should mention, can be filed only on behalf of the ABA and not on behalf of individual Sections. But it also can be very worthwhile, because the influence of the ABA can be decisive in Congress and the courts.

Our Section can formulate and express policy at two levels: (1) as Section policy (which, when expressed, must disclaim full ABA consideration or endorsement), and (2) as ABA policy (which carries the full force of the entire association). We can engage in "outside advocacy" based on Section policy if our duly adopted Section resolution gains approval through the procedure known as blanket authority. In that process, we circulate our report(s) and proposed resolution(s) to all the other ABA Sections for review, and if no objections emerge (or when emerging objections are resolved), we have the authority

to advocate our point as Section policy. Often this is how we proceed when testifying before Congress on pending or proposed IP legislation, or before the USPTO.

In contrast, the advantages of advocacy based on full ABA policy are considerable. But greater effort is required to turn Section policy into ABA policy. ABA policy is normally determined by the ABA House of Delegates, with due process for objections to be heard and a full debate to be had. The House is a large body, consisting of 539 members, and our Section's two current delegates to the House are Don Dunner and Jack Goldstein, both former Section Chairs. The House meets only twice a year, at the ABA Annual Meeting in August and at the ABA Midyear Meeting in February. This can present obvious timing challenges when applying for House authorization to file an *amicus* brief within a filing deadline falling between House meetings, as explored in my earlier article. Emergency procedures exist, of course, and in a pinch the ABA Board of Governors or its Executive Committee can act in place of the House, but they do not like to do so if it can be avoided.

So what has this all meant for Section advocacy, and what might it mean in the future? Here are a few examples.

- The House of Delegates, upon our Section's motion, endorsed support for U.S. adherence to the Madrid Protocol in 2001.² Implementing legislation and regulations have now worked their way through Congress and the PTO, with our Section's continuing attention,³ and we are now on the eve of the opening of the Madrid trademark filing system on November 2.⁴

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NEWSLETTER

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From the Editors

Lisa A. Dunner

Fourth Circuit Prevents City of Barcelona from Reverse Domain Name Hijacking



Nick Setty

In this issue, we bring to your attention a recent and interesting case, *Barcelona.com Incorporated v. Excelentísimo Ayuntamiento de Barcelona*,¹ involving a dispute between a private company, Bcom, Inc. (Bcom), and the City Council of Barcelona, Spain (City Council) over the domain name barcelona.com.

After losing a Uniform Dispute Resolution Proceeding (UDRP) by a World Intellectual Property Organization (WIPO) arbitrator's decision,² Bcom brought a declaratory judgment action under the Lanham Act in the U.S. District Court for the Eastern District of Virginia.³ Bcom then appealed that court's denial of its request for declaratory judgment and transfer of the domain name to the U.S. Court of Appeals for the Fourth Circuit.

Among the several issues appealed were whether U.S. or Spanish trademark law should be applied; whether or not any deference should be given to the WIPO decision; and whether or not failure to consider the basis for the WIPO decision would remove the basis for the court's jurisdiction. In looking at these issues, the Fourth Circuit reversed the decision below and held that the owner of the domain name Barcelona.com established a valid claim of reverse domain name hijacking under 15 U.S.C. §1114(2)(D)(v).

Background: *Barcelona.com*

In 1996, Mr. Cobo (Cobo), a Spanish citizen, registered the domain name Barcelona.com in his wife's name with Network Solutions in Herndon, Virginia. Three years later, Cobo and Mr. Hanif (Hanif) developed a business plan to turn Barcelona.com into a tourist portal for Barcelona, Spain. Shortly after developing this plan, they formed Bcom, Inc. under Delaware law to own and run the Barcelona.com website. The company was formed under U.S. law because Hanif believed that would increase their chances of financing the site. However, they were ultimately unable to secure financing to develop the site.

Due to the lack of financing, Cobo and Hanif used the City Council's website to e-mail the mayor of Spain and propose that the City Council purchase the Barcelona.com domain. About a year later, the City Council contacted them to learn more about their plans for the site. Other than Bcom's New York mailing address, Bcom had no physical presence in the U.S.—no office lease, no phone listing, nor any U.S. employees, and its computer server was in Spain.

In May 2000, Bcom received a cease and desist letter from the City Council, notifying Bcom of its 150 trademarks, all issued in Spain—the majority of which included the word “Barcelona.” Shortly after the City Council sent this letter, Cobo transferred the domain from his wife's name to Bcom—something he meant to do after they formed Bcom. Bcom refused to transfer the domain to the City Council, so the City Council invoked the UDRP promulgated by the Internet Corporation for Assigned Names and Numbers (ICANN).

The WIPO Decision

The City Council's complaint sought a transfer of the domain and relied on Spanish law in alleging that Bcom infringed its numerous Spanish trademarks that included the word “Barcelona.” The City Council also stated in the complaint that it agreed to “be subject to the jurisdiction of the registrant's residence, the Courts of Virginia (United States), only with respect to any challenge that may be made by the Respondent to a decision by the Administrative Panel to transfer or cancel the domain names that are [the subject] of this complaint.”⁴

The arbitrator assigned to the proceeding ruled in favor of the City Council by concluding that Barcelona.com was confusingly similar to the City Council's numerous Spanish “Barcelona” trademarks, Bcom had no legitimate interest in the domain, and Bcom registered the domain in bad faith (by virtue of its alleged potential commercial exploitation of the domain). Accordingly, the arbitrator ordered the transfer of the domain to the City Council.⁵

The District Court Case

Within ten business days of the arbitrator's decision,⁶ Bcom filed suit in the U.S. District Court for the Eastern District of Virginia seeking relief under the Anticybersquatting Consumer Protection Act (ACPA).⁷ Specifically, Bcom filed suit under Section 1114(2)(D)(v) of the ACPA which authorizes a domain name registrant to sue trademark owners for “reverse domain name hijacking.” Under this provision, a registrant who is aggrieved by an overreaching trademark owner may commence a suit to declare that the registration of the domain or use of the domain by the registrant is not *unlawful* under the Lanham Act.⁸ This provision is also known as the reverse domain name hijacking provision.⁹

In this proceeding, Bcom sought declaratory relief that its use of the Barcelona.com trademark does not infringe the City Council's trademarks and that the City Council is barred from instituting any action against Bcom for trademark infringement.¹⁰ The City Council answered and included in its answer an affirmative defense that the court lacked jurisdiction for any cause of action other than Bcom's challenge to the UDRP ruling.

Following a bench trial, Judge Hilton ruled in favor of the City Council and ordered the transfer of the domain. While the court acknowledged that the arbitrator's ruling in the UDRP proceeding should not be given any deference, the court nevertheless applied the arbitrator's

reasoning.¹¹ More surprisingly though, the court applied Spanish law in view of its belief that the international nature of the Internet made it unlikely that Congress would limit the courts' consideration of trademark rights under the ACPA to U.S. trademarks only.¹² Accordingly, applying Spanish law, the court found that Bcom's domain was confusingly similar to the City Council's numerous trademarks that include the word "Barcelona" and that Bcom exhibited a bad-faith intent to profit from the use of the Barcelona mark (both through its use and its attempt to sell the domain to the City Council).¹³ The court, therefore, concluded, in part, that Bcom "failed to demonstrate, as required by 15 U.S.C. § 1114(2)(D)(v), that its use of Barcelona.com was not unlawful," a prerequisite to a successful reverse hijacking.¹⁴

The Fourth Circuit Decision

On appeal, the Fourth Circuit examined, among other things, whether U.S. or Spanish trademark law should be applied to the facts of the case; whether or not any deference should be given to the WIPO decision; and whether or not failure to consider the basis for the WIPO decision would remove the basis for the court's jurisdiction.

Relating to the choice of law issue, Bcom contended, and the Fourth Circuit agreed, that the district court erred in applying Spanish law rather than U.S. law.¹⁵ In fact, the Fourth Circuit stated that the "ACPA explicitly requires application of the Lanham Act, not foreign law. . ."¹⁶

In applying U.S. law, the Fourth Circuit then turned to the elements necessary to establish a right to relief under the reverse hijacking provision. Under this provision, a plaintiff must establish (1) that it is a registrant of a domain name; (2) that its domain name was suspended, disabled or transferred pursuant to a UDRP proceeding; (3) that notice of the reverse domain name hijacking action was given to the mark holder; and (4) that the plaintiff's registration or use of the domain name is not unlawful under the Lanham Act.¹⁷

The first three elements were indisputably satisfied, so the court focused on the fourth and final element—that of unlawfulness—which the court considered to be the principal issue on appeal. The Fourth Circuit found that U.S. law should be applied and, in so doing, the court found that Bcom's use and registration was not unlawful. Specifically, the court concluded that under U.S. trademark law (and apparently also under Spanish law), one cannot obtain a trademark interest in a purely descriptive geographical designation (e.g., one that refers only to the City of Barcelona) unless that geographic designation has obtained secondary meaning.¹⁸ Finding no evidence of secondary meaning, the court concluded that "Barcelona" is entitled to no trademark protection.¹⁹ Accordingly, the Fourth Circuit held that there was nothing unlawful about Bcom's use and registration of barcelona.com, and, as a result, the court held that Bcom's reverse domain name hijacking claim was valid.

With respect to the amount of deference that should (or should not) be given to the WIPO decision, the Fourth Circuit concluded that no deference should be given. Moreover, the Fourth Circuit did not buy the City Council's claim that failure to consider the basis for the WIPO

decision would remove the basis for the court's jurisdiction. Instead, the court stated that "while a decision by an ICANN-recognized panel might be a condition of, indeed the reason for, bringing an action under 15 U.S.C. § 1114(2)(D)(v), its recognition *vel non* is not jurisdictional. Jurisdiction to hear trademark matters is conferred on federal courts by 28 U.S.C. §§ 1331 and 1338, and a claim brought under the ACPA, which amended the Lanham Act, is a trademark matter over which federal courts have subject matter jurisdiction."²⁰

In view of its findings, the Fourth Circuit reversed and remanded the district court's ruling for further proceedings to determine and grant the appropriate relief under the Lanham Act.

Implications of This Decision

The Fourth Circuit's decision makes it clear that the ACPA is not only a weapon that benefits trademark owners, but it also protects the interests of aggrieved domain name owners. Moreover, this decision reminds us that UDRP decisions stand alone—they will be given no deference when reviewed by the district court. Importantly, this decision also removed the presumption created by the district court—that cities and municipalities have rights to domain names that incorporate the city or municipality name—that presumption no longer exists under the Fourth Circuit's ruling. Most significantly though, this decision clarified that the ACPA requires application of U.S. law, not foreign law. Given the Fourth Circuit's strong opinion in this regard, it is unlikely that a district court will make this mistake again.

Endnotes

1. 330 F.3d 617 (4th Cir., June 2, 2003).
2. WIPO Case No. D2000-0505.
3. 189 F. Supp. 2d 367 (E.D. Va. 2002).
4. Case No. D2000-0505.
5. *Id.*
6. The UDRP provides that a party aggrieved by the dispute resolution process may file a court challenge within ten business days. ICANN, UDRP ¶ 4(k.)
7. 15 U.S.C. § 1125.
8. Section 1114(2)(D)(v).
9. ICANN defines "reverse domain name hijacking" as use of the UDRP "in bad faith attempt to deprive a registered domain-name holder of a domain name. ICANN, UDRP ¶1. In other words, when a domain-name registrant cybersquats in violation of the ACPA, that person "hijacks" the domain from a trademark owner (who would typically have a right to the domain involving that trademark); but when that trademark owner overreaches in exercising trademark rights under the ACPA, that trademark owner "reverse hijacks" the domain from the domain registrant. Accordingly, Section 1114(2)(D)(v) was enacted to protect domain name registrants against overreaching trademark owners. 330 F.3d at 625.
10. 189 F. Supp. 2d 367.
11. *Id.* at 371.
12. *Id.* at 373.
13. *Id.* at 372.
14. *Id.* at 376.
15. 330 F.3d at 626.
16. *Id.*
17. *Id.*
18. *Id.* at 629.
19. *Id.*
20. *Id.* at 625.

Residual Goodwill

(continued from page 1)

states, and thus achieving interstate commerce.² In 1989, Congress modified the language of the trademark abandonment statute to add the “bona fide” use requirement and specifically forbid token shipments.³

There are ways to satisfy the use requirement and prevent a trademark from being abandoned even when trademarked products are not sold in the marketplace. Courts have held, for instance, that efforts to sell or license a trademark can be seen as use and an intent not to abandon a trademark.⁴ Use can be established if a company services or provides replacement parts to products that are no longer sold.⁵ Companies can also establish use by *trying* to sell a product or business in a difficult economic environment.⁶ There are no cases the author has found, however, where a court determines a trademark has not been abandoned solely because of the existence of “residual goodwill.”⁷

B. The Impact of Abandonment

Unlike patents or copyrights that exist for a set number of years, expire, and then enter the public domain, trademarks operate under the “use it or lose it” standard described above. If a trademark is not used in commerce and is deemed abandoned, then in the words of one court, “the mark reverts back to the public domain whereupon it may be appropriated by anyone who adopts the mark for his or her own use.”⁸ After abandonment, all previous “goodwill” and name association that may have existed are gone, and the trademark is available for a new company or entrepreneur to create new goodwill. After a trademark is abandoned, its former owner has no legitimate grounds for stopping a new user from adopting its old brand name merely by asserting—or even proving—that it has residual goodwill.⁹

This process recently played itself out in the case of the WHITE CLOUD brand formerly marketed by Procter & Gamble. WHITE CLOUD was a brand of toilet tissue originally introduced by Procter & Gamble in 1934.¹⁰ In an effort to focus resources on its larger trademark CHARMIN, in 1992 P&G discontinued the WHITE CLOUD name.¹¹

In 1993, an entrepreneurial firm later named Paper Partners LLC filed an intent-to-use application for the White Cloud trademark with the United States Patent and Trademark Office for “tissue paper, paper bathroom tissue.”¹² After the three-year period of non-use required for abandonment had elapsed, Paper Partners commenced litigation against Procter & Gamble for the rights to use WHITE CLOUD—and prevailed in 1996. Today, WHITE CLOUD has achieved great success as a trademark of toilet tissue and diapers sold exclusively through Wal-Mart. Even though this was a former P&G trademark and P&G products CHARMIN and PAMPERS were adversely affected, after abandoning the trademark there was nothing P&G could do from a trademark perspective to stop Paper Partners’ licensing of WHITE CLOUD.

To the Editors

Dear Lisa and Nick:

I have been involved in patent practice since starting as an examiner in 1962 and working my way across the chief IP positions at Medtronic, Data General, Apple Computer, National Semiconductor, co-founder of Aurigin Systems, and my own practice today.

I want to thank Mark Banner for his article on the rate of reversal of district court claim constructions by the CAFC. It is not surprising that the reversal rate is as high as it is. He points out that we are asking district court judges to rule on “areas of law with which they are unfamiliar” and then he wrongly concludes that they “simply cannot be ‘doing the wrong thing’ nearly half the time.”

Why shouldn’t they be wrong half or more of the time, considering they are ruling in an area they admittedly know little more than an average juror? What the statistics demonstrate is that the chances of district court judges who are dealing with unfamiliar law and technical factual settings, getting it right about 50 percent of the time is about the same result you would get from merely flipping a coin. And those are clearly not acceptable results.

In the 1970s when the groundswell started from people like Don Banner and others in the profession to create a single court which would hear all patent appeals from the district courts, the thing that everyone was missing is that good law and sound decisions emanate from the trial courts. If bad decisions are continually being made at the trial level because we expect good results from judges untrained in patent law and technology, we have not solved the original problem—predictability in patent law.

Creating the CAFC was a step in the right direction but it didn’t go far enough. Maybe the time has come to finish the job of bringing predictability to patent law. The right solution, I believe, is to establish a federal patent trial court that would try all patent cases. Maybe there would be branches of this court located in the main patent centers—Washington, D.C.; Chicago; Texas; and California—for convenience of the parties.

To be appointed a judge to such a specialized court would require minimum standards of training and experience in patent law and technology. Politics should not be a part of the picture in choosing these judges. This is the system in Germany, where patent judges are selected and trained based on their prior experience in patent law and technology.

With a patent trial court made up of knowledgeable patent judges, the number of cases appealed to the CAFC would go down markedly and the patent law should become considerably more predictable than it is today.

Sincerely,

Irving S. Rappaport, Esq.
Palo Alto, CA 94303
USPTO Reg. 22,472

III. The Trademark Abandonment System Works Best

Many lawyers and commentators complain about the inability to use residual goodwill as a way to protect brand names that their clients have discontinued.¹³ Their main argument is that consumers that see a discontinued brand on a new product are at risk of being confused about the product's source.¹⁴ They assert that a new marketer should not have the right to use a discontinued brand until association with the prior user has dissipated. Only after this period of time should the mark be allowed to be reintroduced into commerce. For them, preventing consumer confusion should be avoided at all costs.

While it is true that there may be some confusion in the marketplace when a discontinued brand is reintroduced by a new user, there are five reasons why residual goodwill should not confer any legal rights on a former trademark owner:

A. Residual Goodwill Would Encourage "Warehousing"

If marketers had their choice, they would own as many trademarks as possible—even if the trademarks are not used—for a certain class of goods and use the trademarks as a barrier to new product introductions by competitors. In fact, prior to the Trademark Revision Act of 1988, many companies created clever "token shipment" programs similar to the P&G example cited above. Companies wishing to introduce new products or services into the marketplace were finding it increasingly difficult to find available brand names because of trademarks that were registered by companies but were actually abandoned due to nonuse.¹⁵

The threat of litigation has a chilling effect on potential new market entrants, who may not introduce products, thus harming competition and the economy in general. Those who argue for residual goodwill in the name of protecting consumers from confusion would deprive those same consumers of the benefits of new product choices and lower prices in the marketplace.¹⁶

B. Residual Goodwill Would Destroy the Abandonment Defense

A casualty from the existence of residual goodwill would be a destruction of the abandonment defense to trademark infringement. In a trademark infringement suit, one of the best defenses for an accused defendant infringer is that the plaintiff's trademark is invalid due to abandonment.¹⁷ If a trademark owner could stop a defendant from using a trademark even if the trademark was abandoned, the abandonment defense would be toothless and irrelevant. It is difficult to believe that this is what Congress intended by establishing abandonment as a defense to infringement. If anything, the abandonment defense shows that residual goodwill should not exist at all.

C. Abandonment Encourages Marketers to Keep Brands in Use

If residual goodwill existed, marketers that discontinue brands would have enormous power over potential competitors considering introductions of products with

names similar to or the same as an abandoned trademark. The power would be the same as if the trademark had never been discontinued. Fortunately, the current abandonment procedure provides an incentive for companies to keep brands in use in the marketplace that would not be there otherwise. Consider the following example about Burger King's WHOPPER hamburger.

The WHOPPER is one of the most well-marketed hamburgers in the world. Millions of dollars have been spent advertising the name. If Burger King were to unexpectedly stop selling WHOPPERS in its restaurants today, it would probably take nearly a century before the residual goodwill of the WHOPPER went away (basically, once all of us who have the ability to read this article pass on).

For as long as Burger King retained residual goodwill in the WHOPPER trademark, no burger chain would be able to launch a new WHOPPER. If one tried to do so, it could be stopped by Burger King even though Burger King was not selling the WHOPPER. At the same time, nothing would prevent Burger King from relaunching the WHOPPER a quarter of a century from now, or longer. Even though the Lanham Act specifically states a trademark is abandoned after *three* years of nonuse, Burger King would be able to protect and use the WHOPPER trademark for a lifetime.

Ultimately, because trademark owners cannot rely on residual goodwill to extend their trademark rights, a company that discontinues a brand does not have the same power as a company that uses a brand in commerce. This provides a huge incentive to keep products on the market, thus benefiting consumers and the economy.

D. Measuring Residual Goodwill Is Too Complicated

Recognizing the power problem detailed above, one commentator proposes that instead of looking at whether a trademark owner has the intent to resume use of an unused trademark, "courts should focus on residual goodwill in the context of an unused mark."¹⁸ In this process, courts would look at a variety of factors to determine if a trademark owner should be allowed to keep its trademark even if the trademark has not been used for more than the three-year statutory period.

The main problem with this proposal is that this would be an incredibly complicated process to manage that would do more harm than good. Courts (and companies considering new product introductions) would be put into the position of measuring (1) levels of residual goodwill, (2) the benefits to society from making sure consumers are not confused, and (3) the benefits to society from new product introductions. This would be a time-consuming and subjective process that would vary widely across brands and product categories and would require reams of expensive statistical data. In contrast, the current system is much more straightforward and predictable (three years with no intent to resume use and the trademark is abandoned).

Even the proponent of the above proposal concedes that "courts should not permit residual good will to save a mark forever. There is a point with respect to any mark at which the public interest is no longer served by affording it protec-

tion from abandonment.”¹⁹ Unsettling to most trademark practitioners, however, is that determining the point at which the “public interest” is no longer served by protecting a trademark for abandonment would be left to a judge or jury.

E. Trademark Law Tolerates Confusion

The confusion that might occur from a new user adopting an abandoned trademark is not different from the confusion resulting from other activities about which there is very little concern. For instance, in March 2002, Abbott Laboratories sold the dandruff shampoo SELSUN BLUE to Chattem, Inc. for \$75 million.²⁰ The sale included trademark rights, associated intellectual property, and some manufacturing equipment.²¹ Unless they read the financial or marketing press, it is unlikely that most SELSUN BLUE consumers are aware this transaction occurred. Virtually nobody would argue that consumers’ “confusion” about SELSUN BLUE’s owner presents any real harm in the marketplace, even though there was a change in the source of the product.

Now assume Abbott Laboratories had discontinued SELSUN BLUE in March 2000 and sold the trademark rights to SELSUN BLUE to Chattem for \$1 million with no associated equipment, formulas, or artwork. Chattem would have to develop new packaging, a new formula for the shampoo, and find a manufacturer for the shampoo. Now SELSUN BLUE has been discontinued by one manufacturer and relaunched by an entirely different manufacturer. All that remains the same is the brand name. Confusion about the source of the product would undoubtedly occur in the marketplace. Yet again, very few people would argue that this sale of SELSUN BLUE from Abbott to Chattem should be prohibited to protect consumers from being confused.

One more variation: Now assume Abbott discontinued SELSUN BLUE in March 1998 and abandoned its rights to the SELSUN BLUE trademark. In March 2002 Chattem launches a new line of dandruff shampoo and calls it “SELSUN BLUE.” The development of the packaging, formula, and manufacturing partner would be the same as the sale example above. How is this situation any more confusing to consumers of SELSUN BLUE than the others? It isn’t; yet this is a situation many companies and their lawyers want to stop.

IV. Conclusion

Ultimately, those who argue most passionately for residual goodwill and against trademark abandonment are brand owners and their lawyers who want to eliminate competition. Contrary to their arguments, the trademark abandonment system currently in place is an efficient way to ensure that trademark owners are not in a position to abuse their power and impede competition in the name of

alleged consumer confusion. The current system serves startups and entrepreneurs that are engaged in the valuable process of introducing products in the marketplace and benefiting consumers.

Endnotes

1. Lanham Act, 15 U.S.C. § 1127.
2. *Procter & Gamble Co. v. Johnson & Johnson Inc.*, 485 F. Supp. 1185, 1204–05 (S.D.N.Y. 1979), *aff’d*, 636 F.2d 1203 (2d Cir. 1980).
3. The Trademark Law Revision Act of 1988.
4. *See, e.g., Sands, Taylor & Wood Co. v. Quaker Oats Co.*, 978 F.2d 947 (7th Cir. 1992), *cert. denied*, 507 U.S. 1042 (1993).
5. *See, e.g., Ferrari S.p.A. Esercizio Fabbriche Automobili e Corse v. McBurnie*, 1989 WL 298658, 11 U.S.P.Q.2d 1843 (S.D. Cal. June 1, 1989).
6. *See, e.g., Seidelmann Yachts, Inc. v. Pace Yacht Corp.*, 1989 WL 214497, 14 U.S.P.Q.2d 1497 (D. Md. Apr. 26, 1989), *aff’d*, 898 F.2d 147 (4th Cir. 1990).
7. For instance, a court might remark on the existence of residual goodwill as part of its analysis; but residual goodwill will not confer rights on the former trademark owner if its mark has not been in use. *See, e.g., EH Yacht, LLC v. Egg Harbor, LLC*, 84 F. Supp. 2d 556, 565 (D.N.J. 2000) (continued sales of product ensured that the former trademark owner’s name was still in use).
8. *Dial-A-Mattress Operating Corp. v. Mattress Madness, Inc.*, 841 F. Supp. 1339, 1355 (E.D.N.Y. 1994).
9. A company could potentially stop a secondary user of a trademark from using original packaging or logo artwork that would be protected by copyright law.
10. U.S. Patent and Trademark Office Trademark Registration Number 677,743.
11. Jennifer Reingold, *Darwin Goes Shopping: Fewer Trademarks May Mean Lower Costs and Fatter Profits for Consumer Goods Companies*, TRADEMARKWEEK, Aug. 9, 1993.
12. U.S. Patent and Trademark Office Trademark Registration Number 2,070,125.
13. *See, e.g., Michael S. Denniston, Residual Goodwill in Unused Marks—The Case Against Abandonment*, 90 TMR 615 (2000); Lawrence R. Hefter and Lisa F. Peller, *US Courts in a Quandary Over “Abandoned Trademarks,”* IP WORLDWIDE (June 1999); J. THOMAS MCCARTHY, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 17.03[6] (3d ed. 1996).
14. Although it is the author’s experience that former users are usually more concerned about being mistakenly sued by an angry consumer of a new product or service using the old brand name.
15. *See, e.g., Jerome Gilson, Trademark Protection and Practice (Updated)*, § 45, vol. 9, at 45-26—45-30 (1974).
16. *Newsouth Communications Corp. v. Universal Tel. Co., LLC*, 2002 WL 31246558, *14 (E.D. La. Oct. 4, 2002) (existence of alleged residual goodwill does not allow former trademark owner to “warehouse” name without making actual use of it).
17. Lanham Act, 15 U.S.C. § 115(b)(2).
18. Denniston at 643.
19. Denniston at 640.
20. Press Release, Chattem, Inc., Chattem, Inc. Announces Definitive Agreement to Purchase Selsun Blue from Abbott Laboratories (Mar. 5, 2002).
21. *Id.*

Taken by the Fifth

The Fifth Amendment “Taking Clause” and Intellectual Property

BY PAUL F. KILMER



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Some patent lawyers are familiar with the remedies available under the Tucker Act for unauthorized use of an invention by the United States government or one of its contractors.¹ A few practitioners may even know of the parallel remedies for copyright infringement by the United States government also available under the Tucker Act.²

And a handful of trademark lawyers may have had experience with infringements by federal agencies and the waiver of sovereign immunity in the Lanham Act that permits private rights of action against such government conduct.³

But what about situations in which something other than a patent, trademark, or copyright is involved, such as a trade secret, semiconductor chip mask work, or the right of publicity? And what about situations in which the government involved is a state, not the United States?

What if the government is not the beneficiary of the taking of an intellectual property right (IPR)? For example, where a statute intended to protect public health has the effect of disclosing trade secrets to competitors? Are such cases actionable under the Fifth Amendment Taking Clause?⁴ If so, what circumstances need be present for a private litigant to challenge the authority of the government?

When does a cause of action under the Taking Clause actually arise? Is the threat of a taking enough or must the property already be in the hands of the government, its agent, or a third party before the owner may seek a remedy?

And what about situations in which a party might wish to seek injunctive or declaratory relief rather than money damages? Are such remedies ever available under the Taking Clause, which specifically provides only for “just compensation”?⁵

These questions will not be definitively answered by the recent decision of the U.S. Court of Appeals for the First Circuit in *Philip Morris, Inc. v. Reilly*.⁶ However, *Reilly* provides some of the contours and complexities of the issues with which the courts must grapple in Taking Clause actions.

In *Reilly*, a three-judge panel, split three ways, issued injunctive, not monetary relief, against the prospective taking of a trade secret that might result from a Massachusetts’s statute that could have allowed the ingredients of tobacco products to be made public. A dissent (per Judge Lipez) and so-called lead opinion

(per Judge Torruella) agreed upon a three-part test for assessing IPR Taking Clause actions, and the third judge (Judge Selya) joined the lead opinion in the result only and relied upon a different analysis to find that only a single factor need be present to establish a taking. In the magnitude of its disarray, *Reilly* brings into focus for IPR practitioners those twelve words in the Fifth Amendment to the Constitution “. . . nor shall private property be taken for public use, without just compensation.”⁷

The Life of Reilly

In *Reilly*, a 1996 Massachusetts statute⁸ (the Disclosure Act) was enacted that might have required tobacco companies to submit to a state agency ingredient lists for their products setting forth the relative amount of each substance besides tobacco and water. The tobacco companies claimed that this information constituted trade secrets and presented evidence indicating that their formulas could not be “reverse engineered” with available technology.⁹

The tobacco companies filed a preemptive action to prevent the implementation of the Disclosure Act. The tobacco companies argued, *inter alia*, that the statute would violate the Taking Clause and their constitutional rights under the Due Process Clause of the Fifth Amendment¹⁰ by affecting a taking without providing a meaningful opportunity to be heard.¹¹

The state argued that public health considerations justified the Disclosure Act and its proposed regulations as a proper exercise of traditional “police powers” that fell short of a “taking.” The state’s case included submissions demonstrating that current publicly available ingredient lists did not identify additives by brand or manufacturer and therefore Massachusetts could not effectively study the interaction of additives used in tobacco products. None of the litigants argued that the proposed studies alone were outside of the health and safety realm of the state’s police powers.

The Disclosure Act and the regulations implementing it also left open the possibility that once various tobacco brands had been tested for potential health risks posed by the interaction of their ingredients, the state might publicize the ingredient lists so that consumers would better know which tobacco products were potentially more dangerous than others. However, before any such public disclosure could take place, it was required that: (1) the Massachusetts Department of Public Health (DPH) find that publication of the ingredients “could reduce risks to public health”; (2) the Massachusetts Attorney General determine that disclosure would not be an unconstitutional taking; (3) the DPH provide sixty

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days' notice to the affected tobacco manufacturer before its ingredients list was publicly disclosed; and (4) during the sixty-day notice period, the tobacco manufacturer could withdraw its product from the Massachusetts market and thereby avoid disclosure of its ingredients list.¹² Until all statutory and regulatory requirements for allowing disclosure had been met, the tobacco companies' ingredient lists were to be kept confidential by the state.¹³

The court in *Reilly* was faced with a number of discrete issues which are instructive on virtually every facet of Fifth Amendment "taking" practice. The *Reilly* court also avoided a few issues that may arise in Taking Clause actions, which will also be explored in the following sections.

How Broad Is the "Taking" Power?

Although this issue is at the heart of *Reilly* and all other Taking Clause actions, the breadth of the power of all levels of government to take private property for public use was perhaps best enunciated by Justice Douglas in *Berman v. Parker*,¹⁴ a 1954 Supreme Court ruling on a statute passed by Congress for the redevelopment of substantial areas of the District of Columbia aimed at stemming urban blight in the nation's capital:

Subject to specific constitutional limitations, when the legislature has spoken, the public interest has been declared in terms well nigh conclusive. In such cases, the legislature, not the judiciary, is the main guardian of the public needs to be served by social legislation The role of the judiciary in determining whether that power is being exercised for a public purpose is an extremely narrow one.¹⁵

Public safety, public health, morality, peace and quiet, law and order—these are some of the more conspicuous examples of the traditional application of the police power to municipal affairs. Yet they merely illustrate the scope of the power, and do not delimit it. See *Noble State Bank v. Haskell*, 219 U.S. 104, 111. . . * * * Once the object is within the authority of Congress, the right to realize it through the exercise of eminent domain is clear. For the power of eminent domain is merely the means to the end. See *Luxton v. North River Bridge Co.*, 153 U.S. 525, 529-530; *United States v. Gettysburg Electric R. Co.*, 160 U.S. 668, 679. . . . * * * The rights of . . . property owners are satisfied when they receive that just compensation which the Fifth Amendment exacts as the price of the taking."¹⁶

Although this statement of the breadth of legislative power over private property appears all-encompassing, there are constraints that arise from certain rights guaranteed by the Constitution (such as those contained in certain of the Bill of Rights set forth in the first ten amendments to the Constitution).¹⁷

What Is "Property" Subject to the Taking Clause?

The *Reilly* majority and dissent had no difficulty agreeing that almost any type of IPR, including trade secrets, is a property right protected by the Fifth Amendment.¹⁸ This is consistent with the view of the Supreme Court in *Ruckelshaus v. Monsanto*.¹⁹ The *Monsanto* Court was faced with the issue of whether a

taking occurred under the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), which authorized EPA to use certain data submitted by one applicant for registration of a pesticide in evaluating subsequent applications by other companies and also allowed EPA to publicly disclose some of the submitted data.

The Supreme Court in *Monsanto* began by evaluating whether the trade secret rights at issue were "property" within the meaning of Fifth Amendment. In that its past decisions had recognized rights in various types of intangibles, such as liens and contracts,²⁰ the Court found trade secrets within the ambit of protected property.

However, not every cause of action recognized as part of the law of intellectual property may be pursued against a state under the Taking Clause. Recently, the Supreme Court in *College Savings Bank v. Florida Prepaid Postsecondary Education Expense Board*,²¹ which struck down the portion of the Trademark Remedy Clarification Act that sought to subject states to suits under Section 43(a) for false and misleading advertising, noted that not all rights arising under the broad umbrella of "unfair competition" constitute "property" that may be "taken" by government action. In *College Savings*, the defendant was an arm of the State of Florida that had allegedly made false statements about its own college tuition savings plan to the detriment of the plaintiff, a private bank that competed with state instrumentalities in offering consumers certificates of deposit to finance the cost of college education.²² The Supreme Court noted that the Lanham Act may have provisions that protect property interests (e.g., creating a cause of action for trademark infringement, which implicates the property interest in a trademark), but that false and misleading advertising by a state in relation to its own activities did not impact another's "right to exclude" the state from private property.²³ More broadly, the Court in *College Savings Bank* indicated that a property right did not arise where the interest at stake was "the activity of doing business, or the activity of making a profit."²⁴

In a companion case, *Florida Prepaid Postsecondary Education Expense Board v. College Savings Bank*,²⁵ the Supreme Court struck down a federal law that sought to abrogate state sovereign immunity from patent infringement litigation. However, that holding was made after the Court specifically recognized that patents are a species of property.²⁶

Under *Monsanto* and the *College Savings Bank* decisions, patents, trademarks, copyrights, and trade secrets are "property" interests subject to possible taking by a government. The rights of publicity and privacy, because they are based upon the ability to exclude others from benefiting from the *persona* of another, are also likely to qualify as "property." Similarly, *sui generis* rights included in the patent and copyright laws, such as protection for plant varieties,²⁷ semiconductor mask works,²⁸ boat hull designs,²⁹ and the rights of attribution and integrity that are available to the authors of certain works of visual art,³⁰ all of which include the ability to exclude others from

using the protected right, would appear to be property potentially subject to taking by a government.³¹

Does Sovereign Immunity Need to Be Waived?

As a general rule, the United States government may be sued only by means of a waiver of sovereign immunity.³² Such a waiver is already in place for infringement of patents, copyrights, and trademarks.³³ Likewise, specific waivers of immunity are in place for plant varieties, mask works, and boat hulls.³⁴ Taking actions premised upon the rights of publicity, privacy, and the attribution and integrity of works of visual art could be based upon the general waiver provisions of the Tucker Act, which appear sufficient for that purpose, although unlike the specific waiver provisions applicable to patent, copyrights, and trademarks, additional evidence that government action constitutes a taking may be required.³⁵

Suits against states are trickier. The Eleventh Amendment to the Constitution prohibits suits in federal court against a state government by citizens of another state.³⁶ Supreme Court jurisprudence has both expanded and, based upon application of the Fourteenth Amendment, narrowed the ambit of state government immunity from suit.³⁷ It is now the case that a state may only be sued where: (1) a substantive violation of the Fourteenth Amendment is asserted; (2) Congress has authorized suit in the proper exercise of its power to enforce the Fourteenth Amendment; or (3) the state has waived its sovereign immunity by consenting to suit.³⁸

Recent Supreme Court jurisprudence indicates that Congress may invoke the Fourteenth Amendment as a basis for the waiver of state sovereign immunity only where it has: (1) identified conduct by a state that transgresses the substantive provisions of the Fourteenth Amendment; and (2) the legislation is narrowly tailored to appropriately remedy the unconstitutional conduct by the state.³⁹

It does not appear that the State of Massachusetts questioned whether the *Reilly* action could be brought in a federal court even though issues of state sovereign immunity were implicated in the action.

“Public” or “Private” Use?

Under the Fifth Amendment, the use to which the government subjects the property interest at issue must be “public,” not private. Although *Reilly* does not directly address this issue, the Supreme Court in *Monsanto*, as many courts before it, dealt almost in passing with the question of whether the taking of trade secrets under FIFRA was for “public” or “private” use.⁴⁰

The Supreme Court concluded that only a “conceivable public character” was required to come within the bounds of the Taking Clause and that it was “for Congress to determine” what constitutes a legitimate public purpose.⁴¹ Like the taking power itself, the “public character” requirement is therefore quite broad and can conceivably be molded by legislative history, at least within the bounds of constraints found elsewhere in the Constitution.⁴²

Permitted Regulation or Deprivation of Rights?

The Supreme Court in *Monsanto* concluded that *deprivation* of a property interest by government action may constitute a taking and therefore the taking inquiry does not end merely because the government failed to acquire title to a chattel or occupy land.⁴³ This finding was consistent with prior cases in which the Supreme Court had indicated that there are two branches of Taking Clause cases: (1) physical takings and (2) regulatory takings, with the latter being subject to more detailed judicial analysis as to whether a true taking had occurred.⁴⁴

Physical takings, because they are more readily apparent (e.g., the government takes title to land and knocks down a house to put in a superhighway) are often more focused on valuation (“just compensation”) than whether a taking has occurred or whether the taking is a permitted act of government.⁴⁵ By contrast, regulatory takings are more difficult to assess since, as the Supreme Court has noted, a taking does not always occur “when interference [with a property right] arises from some public program adjusting the benefits and burdens of economic life to promote the common good.”⁴⁶

Justice Holmes observed in the Supreme Court’s 1922 decision in *Mahon*,⁴⁷ that “[g]overnment hardly could go on if to some extent values incident to property could not be diminished without paying for every . . . change in the general law.” Therefore, regulatory requirements such as land use permits and recordation of interests in land do not generally present sufficient intrusions into a property right to constitute a taking under the Fifth Amendment.⁴⁸

However, the Supreme Court in *Monsanto* concluded that trade secrets are a species of property protected under the Fifth Amendment’s Taking Clause whose use *or disclosure* by the government may deprive the owner of all value in the intellectual property. Therefore, where the regulation at issue would lead to a disclosure of the information submitted to the government, the courts should move on to consider additional factors determinative of the taking issue.⁴⁹

The Court in *Monsanto* concluded that a taking of trade secrets would occur where the owner submitted the information under a guarantee that the government would maintain it in secrecy and the government later broke that promise through a revision of law or regulation.⁵⁰ However, *Monsanto* also held that if a company develops trade secret information knowing it will be provided to the government in order to obtain a government benefit and with the knowledge that the government might disclose the trade secret, a taking would not result because the trade secret owner did not have a reasonable expectation of confidentiality when the trade secret was created.⁵¹

In *Reilly*, Judge Torruella’s lead opinion noted that the state may have a legitimate interest that falls short of a taking in forcing the disclosure of some trade secrets.⁵² Prior courts had similarly noted that a statute or regulation that forces the relinquishment of one “strand” or “stick” in a “bundle” of property rights does not necessarily result in a taking as long as the property as a whole remains economically viable.⁵³

Judge Torruella's lead opinion went on to state that "[a] regulatory taking transpires when some significant restriction is placed upon an owner's use of his property for which 'justice and fairness' require that compensation be given."⁵⁴ The exact type and degree of restriction on the use of property that may qualify as a taking is dealt with in the next section.

"Reasonable Investment Backed Expectation," Alone, or Must Economic Impact and the Character of the Government Action Be Considered?

The wheels literally come off in *Reilly* when the three-member court considered what test should be applied to determine whether a taking has occurred and then applies their respective tests to the facts. The lead opinion and the dissent both agree that a three-part ad hoc factual inquiry, derived from *Monsanto*, is determinative, to wit: "(1) what is the economic impact of the regulation; (2) whether the government action interferes with reasonable investment-backed expectations; and (3) what is the character of the government action"⁵⁵ [which the lead opinion later appears to equate with "the public interest" in the alleged taking].⁵⁶

The lead opinion in *Reilly* went on to find that "at least one *per se* rule" applies in the regulatory taking sphere: "[w]hen a regulation denies all economically beneficial or productive uses of land, it is a taking."⁵⁷ However, the lead opinion refused to carry that *per se* rule over into the realm of intangible property or any other form of personality, finding no support for such a holding in the Supreme Court's Taking Clause jurisprudence.⁵⁸ The concurrence, by contrast, found no significant distinction between real property and intangible intellectual property, and would have applied the *per se* rule, finding support in *Monsanto* for this position.⁵⁹

The concurring opinion found that only one factor was dispositive: that the tobacco companies had a reasonable investment-backed expectation when they created their secret combinations of ingredients that the state would protect them under existing Massachusetts trade secrecy law.⁶⁰ The lead opinion criticized this approach at length, noting that it failed to take into consideration factors such as the government's compelling need to protect the public from unreasonable risk of injury that might result from failure to disclose trade secrets in the face of dangers such as the threat posed by toxic substances being released into the environment.⁶¹ Under such compelling circumstances, the lead opinion would not find the government's use of trade secret data to be a taking.⁶² In this regard, the lead opinion in *Reilly* appears more in line with recent Supreme Court precedent.⁶³

Judge Torruella's lead opinion and Judge Lipez's dissent agree that the three-part *Monsanto* ad hoc test must be applied, but they diverge in the application of the test to the facts in *Reilly*. The lead opinion admits that a regulation may not represent a taking merely because it imposes a burden on an investment-backed asset.⁶⁴ The issue for Judge Torruella is whether the government

action (in this case, disclosure of a trade secret) will *destroy* the value of a reasonable investment-backed asset.⁶⁵ Judge Torruella admits that disclosure of information to the government to obtain a government benefit or comply with an existing regulation in a situation in which the government has indicated it may disclose the contents of the submission would not constitute a taking because under such circumstances there is no reasonable investment-backed expectation that the data would be maintained in secrecy.⁶⁶ In other words, if a company has constructive or actual notice that its trade secrets might be made public, then when it either makes a submission to the government or produces additional data or information that it is required to submit under an existing regulatory scheme, the company has no reasonable investment-backed expectation of confidentiality and cannot legitimately claim a taking has occurred when the government later discloses the submitted data or information.

Judge Torruella's lead opinion takes issue with the Disclosure Act in relation to what he characterizes as Massachusetts's effort to redefine property rights "without regard to previously existing [trade secret] protections."⁶⁷ He goes on to admit that if the Massachusetts Disclosure Act had been carefully tailored to allow for disclosure of only "fair information," which he defines as perhaps publishing "one or more ingredients of tobacco products" found to present a health risk (as opposed to publishing a list of all ingredients in a specific tobacco-based product), then it might be permissible to preserve public health and safety rather than constituting a taking.⁶⁸

So that readers of the lead opinion in *Reilly* would not assume Judge Torruella was advocating a "least drastic alternative" review of regulatory taking actions, he specifically noted that "I am not requiring Massachusetts to adopt the narrowest regulation possible to address its laudable goals."⁶⁹ Rather, his concern centered upon two features of the Disclosure Act: (1) the destruction of the property right of the tobacco companies if their trade secret ingredient lists are published⁷⁰ and the attendant destruction of the economic value of tobacco brands;⁷¹ and (2) the low threshold that the Disclosure Act set for allowing publication of the trade secrets (i.e., "Massachusetts can publish their entire ingredient lists if doing so 'could' further public health").⁷²

The dissent of Judge Lipez focused upon the fact that the Disclosure Act had not yet gone into effect and therefore the tobacco companies were mounting a "facial challenge" to the law.⁷³ That is, the actual taking of which the plaintiffs complained had not occurred and the tobacco companies were asserting that implementation in the future would deprive them of a property interest. Of such facial challenges, Judge Lipez noted:

A facial challenge to a legislative Act is . . . the most difficult challenge to mount successfully, since the challenger must establish that no set of circumstances exists under which the Act would be valid.⁷⁴

Judge Lipez then noted that the Disclosure Act indicated "only that Massachusetts may disclose *some* of the

information it receives” (emphasis in original) and that the Act did not, by its terms, mandate disclosure of all ingredient information or even that part of the ingredient information that might contain trade secrets.⁷⁵ On these facts, Judge Lipez would not find a facial taking, noting “the mere possibility of a . . . broad disclosure is not enough to render the Act facially invalid.”⁷⁶

That being said, Judge Lipez agreed with the conclusion of the lead opinion that if the Disclosure Act led to publication of the entire list of ingredients of tobacco products it would constitute a taking of trade secrets.⁷⁷ But if “only certain harmful ingredients” were disclosed, Judge Lipez would find that the state’s interest outweighed the costs to the tobacco companies and no taking would have occurred.⁷⁸ The fact that the state might not publish sufficient information to actually disclose trade secrets of the tobacco companies, combined with the ability of the tobacco companies to challenge proposed public disclosures through “as-applied” litigation (the filing of which would stay public disclosure of the ingredients list at issue) was, in the view of Judge Lipez, sufficient to find that “the Act is not unconstitutional in every application,” thereby defeating the facial challenge by the tobacco companies.⁷⁹

When May Pre-Taking Lawsuits Be Brought?

The *Reilly* court addressed this issue and both the lead opinion and the dissent concluded that where an “unconstitutional taking” is threatened, a preemptive (pre-taking) lawsuit may be brought seeking injunctive or declaratory relief.⁸⁰

Preemptive actions may also be warranted where substantive rights otherwise guaranteed by the Constitution will be violated if the government action is allowed to go forward. For example, claims of discrimination, whether based on theories of equal protection, due process, or otherwise, being outside of the jurisdiction of the Court of Claims, may be candidates for preemptive unconstitutional taking actions.⁸¹ Similarly, if government action is perpetrated in a manner where “just compensation” cannot be given or where the government action threatened a basic constitutional guarantee (such as freedom of speech), a preemptive action would also be warranted.⁸²

“Just Compensation” or Injunctive or Declaratory Relief?

The Fifth Amendment clearly states that the remedy for a taking is “just compensation.”⁸² Yet the courts, including the one in *Reilly*,⁸³ occasionally grant injunctive or declaratory relief against implementation of a statute or regulation that would perpetrate a taking. This conduct by the courts begs the question of when injunctive relief may be appropriate.

The lead opinion of Judge Torruella in *Reilly* attempts to sweep away this issue by indicating that Massachusetts had failed to object to issuance of an injunction and had therefore waived its argument.⁸⁵ This rationale, although an approach taken by other courts, including the Supreme Court,⁸⁶ seems weak because it presumes that once a government has decided to take

private property under its police powers it can be prevented from doing so even though the Constitution states that the government need only pay “just compensation” under such circumstances.

The Supreme Court’s decision in *Monsanto* appears to teach against the “waiver” position adopted in *Reilly*. The Court in *Monsanto* noted that once it is established a taking has occurred for public use, the matter should then be referred to a lower court (there, the U.S. Court of Claims) for a determination of just compensation, and there is no indication in *Monsanto* that such a remedy was requested by the defendant (the United States).⁸⁷

However, beyond “waiver,” *Reilly* and other decisions give some guidance as to when injunctive or declaratory relief may be warranted. *Reilly*’s lead opinion addresses the argument by the state that tobacco companies could avoid the adverse effects of the Disclosure Act by merely “not selling their products in Massachusetts.”⁸⁸ Judge Torruella comes to the conclusion that the product at issue (tobacco) is “legal” in Massachusetts, the Disclosure Act did not make selling the product illegal, and the taking at issue did not result in a benefit being granted to the tobacco companies as a result of submission of their trade secrets to the government but only imposed a loss on them.⁸⁹ Based upon these findings, the lead opinion held that the Disclosure Act was “an unconstitutional taking,” as opposed to a constitutional taking, which would only have required payment of just compensation.⁹⁰

What the lead opinion appears to be saying is that the Disclosure Act was somehow *ultra vires* of the state’s powers to regulate and therefore was an unlawful taking which could not be remedied by just compensation under the Fifth Amendment. In other words, the lead opinion finds that the Disclosure Act was contrary to law (rather than a legally permissible regulation that effected a taking).⁹¹ Unsaid is exactly what law the Disclosure Act violated and how another law (e.g., the right to sell a legal product) could trump the Fifth Amendment to the Constitution.

The use of injunctive relief in *Reilly* might better be justified as either: (1) the only available remedy for an attempt at regulatory taking in which the government had no intention or ability to pay compensation, and therefore the government could not justify its regulation by relying upon the Taking Clause (i.e., the act was *ultra vires* of the Taking Clause);⁹² or (2) as a remedy for denial of “substantive” rather than “procedural” due process rights of the tobacco companies (i.e., *ultra vires* of constitutional guarantees other than the Taking Clause).⁹³

Although the courts have not been explicit on the point, it would appear that in order to be *ultra vires* of the Taking Clause: (1) the legislature must have demonstrated (overtly or by implication) that it did not intend for compensation to be paid as a result of the taking; and (2) compensation must be impossible to reasonably structure without completely undermining or destroying the intent of the enactment, or, perhaps, that paying just compensation would be an immense burden on the government that was not within the contemplation of the legislature when the statute was enacted.⁹⁴

For example, in *Eastern Enterprises*, the statute at issue was intended to force coal companies to compensate miners for lifetime health benefits that were not contemplated during the period of time when the plaintiff (*Eastern Enterprises*) had been in the coal mining business. Based upon these facts, the Supreme Court found that the statute was “improperly crafted” to place a “severe, disproportionate, and extremely retroactive burden” on the plaintiff. Because the statute could not be reasonably interpreted to mean that the federal government would compensate the coal company in order to fund the health benefit (i.e., the statute’s purpose was to impose a regulatory liability on the coal company and that purpose was entirely defeated if the government was forced to fund that liability), an “unconstitutional taking” was found and injunctive relief was imposed.

The conditions that might render an enactment *ultra vires* of substantive due process rights present some complex constitutional issues and for this reason, to date, the Supreme Court and appellate courts have steered away from this concept (mainly by mentioning it and then pointedly not addressing the merits of the claim).⁹⁵

For purposes of background, procedural due process involves issues such as whether the statute or regulations were properly adopted following lawful procedures governing such enactments.⁹⁶ However, if proper procedures were followed, as was the case with the Disclosure Act in *Reilly*, then that law would normally represent a permitted takings by the government.⁹⁷

By contrast, a violation of substantive due process rights may arise even where a statute was enacted in a manner consistent with required procedural due process. Substantive due process absolutely reserves to individuals certain property rights or the ability to engage in certain conduct, despite the government’s desire to the contrary.

A violation of such substantive due process rights would be *ultra vires* and thus the government could not lawfully reach the property right at issue and taking the property right would be unconstitutional. In other words, an unconstitutional enactment by the state or federal governments cannot form the proper basis for a taking under the Fifth Amendment and therefore the “private property” at issue cannot be “taken for public use” and no amount of “just compensation” can save the situation. When properly invoked, therefore, substantive due process rights would cut off the government from acting and can be enforced by injunctive or declaratory relief.⁹⁸

There are two types of substantive due process rights. The first are those clearly recognized in the Constitution (e.g., freedom of speech). These enumerated constitutional rights have generally been extended to cover state action by operation of the Fourteenth Amendment. The second group of substantive due process rights is based upon certain unenumerated rights that courts have found within the context of specific constitutional guarantees.⁹⁹

At first, substantive due process rights included only those enumerated in the Constitution (e.g., freedom of speech, assembly, and the press protected under the First Amendment). However, in the early years of the twentieth

century, certain unenumerated substantive due process rights were recognized under the so-called Fundamental Rights doctrine.¹⁰⁰ The decisions recognizing “fundamental rights” were either severely limited or overruled by later Courts, beginning in 1937.¹⁰¹

However, in the mid-1960s and thereafter, decisions such as *Griswold v. Connecticut*,¹⁰² *Roe v. Wade*,¹⁰³ and, most recently, *Lawrence v. Texas*,¹⁰⁴ have found that substantive due process (or a “penumbra” of substantive rights surrounding the Due Process Clauses of the Fifth and Fourteenth Amendments) includes rights not directly specified in the text of the Constitution.

Applying a pre-1937 “substantive due process” regime to *Reilly*: (1) the state had created and long recognized a property interest in trade secrets; (2) the ingredients of the tobacco products at issue were a trade secret protectable under Massachusetts’s law; (3) the Disclosure Act did not outlaw the sale of tobacco products on public health grounds but instead required possible disclosure and public use of trade secrets; (4) the Disclosure Act did not confer a government benefit on the tobacco companies in exchange for disclosure of the trade secrets; and (5) forcing tobacco companies to withdraw a lawful product from the Massachusetts market in order to avoid disclosure of trade secrets required by an overreaching statute (the Disclosure Act) would deny the tobacco companies the lawful right to sell their products in Massachusetts (a disproportionate harm to the tobacco companies unrelated to the objectives of the Disclosure Act, according to the lead opinion). The result could be characterized as denial of substantive due process—that is, the taking of a property right contrary to law rather than in accordance with a legitimate government purpose (i.e., a possible violation of the formerly recognized substantive due process “right to contract” to sell a legal product).

Despite what might appear to be injunctive or declaratory relief granted on substantive due process grounds, neither *Reilly* nor the Supreme Court has invoked substantive due process as a basis for their holdings in Taking Clause actions.¹⁰⁵ Perhaps this is because the courts do not wish to squarely address the issue of whether recognition of “substantive due process” in *economic* rights such as the ability to sell a dangerous, though legal, product, (like the tobacco products in *Reilly*) might bring the law full-circle back to those Supreme Court decisions which struck down progressive legislation in the early twentieth century and the New Deal of the early 1930s, and were repudiated in the 1937 Supreme Court decision in *West Coast Hotel v. Parrish*.¹⁰⁶ A dramatic expansion of such economic substantive due process rights, enforced by injunctive or declaratory relief, could reverse the course of almost seventy years of social and regulatory legislation by the federal and state governments.¹⁰⁷

What Is the Proper Forum?

Where a litigant is seeking “just compensation” against the federal government in a Taking Clause

action, the proper forum is the U.S. Court of Claims.¹⁰⁸ This is true even if the matter involves “intangible property” and is for “unliquidated damages.”¹⁰⁹

However, where the claim is against a state under the Fourteenth Amendment (as in *Reilly*), or where as litigant seeks injunctive or declaratory relief against the United States government, the proper forum is likely a federal district court with proper jurisdiction.¹¹⁰

Conclusion

In the final analysis, expropriation or regulatory action by the federal or state governments that destroys the private value of an intellectual property right whose normal exercise would result in “excluding” others from the use of an invention, idea, trademark, work, or related intangible property could be subject to a Taking Clause action.

Actions by a government that diminish, but do not expropriate or destroy, the value of the IPR may also constitute takings, either where the government has admitted as much (such as in those sections of the Tucker Act dealing with federal government use of patents and copyrights) or where a court otherwise finds that a taking has occurred. Where there is an issue as to whether a regulatory taking of IPR has occurred, as a general rule the courts are likely to rely upon the three-part ad hoc inquiry found in *Monsanto* and the lead and dissenting opinions in *Reilly* (reasonable investment-backed expectation, economic impact and public interest), rather than the per se “reasonable investment-backed expectation” rule advocated by the dissent in *Reilly* and the D.C. Circuit in *Nixon*.

If only “just compensation” is sought, a Taking Clause action against the federal government will most likely arise through a waiver of sovereign immunity under the Tucker Act and the action must be brought in the U.S. Court of Claims. Taking Clause actions against states will also often arise as a result of a specific waiver of state sovereign immunity and the forum will be dictated by state law, the Eleventh Amendment or more general principles of federal court jurisdiction over the actions of the states.

Where a fundamental right guaranteed by the Constitution or an enactment intended to enforce a fundamental constitutional right is at issue, a waiver of sovereign immunity may not be required and injunctive and declaratory relief may be available.

However, the rules regarding Taking Clause actions are an ever-changing landscape. For example, some courts appear to be edging closer to recognizing certain substantive due process rights of an economic nature. It is therefore difficult to predict how long the current trends will stay in place.

Endnotes

1. 28 U.S.C. § 1498(a).
2. 28 U.S.C. § 1498(b); *See, e.g.*, Steve Altman Photography v. United States, 18 Ct. Cl. 267 (1989) (copyright action).
3. 15 U.S.C. § 1122(a).
4. U.S. CONST. amends. V and XIV.
5. *Id.*

6. Philip Morris, Inc. v. Reilly, 312 F.3d 24 (1st Cir. 1992).
7. U.S. CONST. amend. V.
8. MASS. GEN. LAWS ch. 94, §307B (2002).
9. 312 F.3d at 27.
10. The assertion of a Fifth Amendment violation was predicated on the application of that amendment to the states by means of the Fourteenth Amendment. U.S. CONST. amend. XIV, Clause 1.
11. 312 F.3d at 29.
12. *Id.*
13. *Id.*
14. 348 U.S. 26 (1954).
15. *See* Old Dominion Co. v. United States, 269 U.S. 55, 66; United States ex rel. TVA v. Welch, 327 U.S. 546, 552.
16. *Id.*, 348 U.S. at 32–36.
17. *See* the section below entitled “Injunctive Relief or ‘Just Compensation’.”
18. 312 F.3d at 31–33 and 52–53 (Lipez. J., dissenting).
19. 467 U.S. 986 (1984).
20. Citing *Armstrong v. United States*, 364 U.S. 40 (1960); *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935) and *Lynch v. United States*, 292 U.S. 571 (1934).
21. 527 U.S. 666 (1999) (It should be noted that this was a 5–4 decision).
22. *Id.* at 670–71.
23. *Id.* at 673.
24. *Id.* at 675.
25. *Id.* at 627.
26. *Id.* at 642.
27. 7 U.S.C. ch. 57.
28. 17 U.S.C. ch. 9.
29. *Id.* ch. 13.
30. 17 U.S.C. § 106A.
31. This conclusion is bolstered by the provisions of the Tucker Act, which specifically waive sovereign immunity of the United States in relation to actions brought in relation to plant varieties, mask works and boat hull designs. 28 U.S.C. § 1491(a).
32. *Boyle v. United States*, 200 F.3d 1369, 1372–73 (Fed. Cir. 2000) and *Wechsberg v. United States*, 54 Fed.Cl. 158, 64 U.S.P.Q.2d 1588 (2002).
33. 28 U.S.C. § 1498(a) and (b) and 15 U.S.C. § 1122(a).
34. 8 U.S.C. § 1498(d) and (e).
35. *Id.* § 1491(a). *See* the general discussion of the elements necessary to prove a regulatory taking in the section entitled “‘Reasonable Investment Backed Expectation’, Alone, Or Must Economic Impact and the Character of the Government Action be Considered?,” below.
36. U.S. CONST. amend. XI, provides that “[t]he Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State.”
37. *See, e.g.*, *Seminole Tribes cf. EEOC v. Wyoming*, 460 U.S. 226 (1983) (significantly curtailing the power of Congress to abrogate state sovereign immunity, especially under its Article I powers).
38. *College Savings Bank v. Florida Prepaid Postsecondary Educ. Expense Bd.*, 527 U.S. 627 (1999) (a 5–4 decision).
39. *College Savings Bank*, 527 U.S. at 639 and *City of Boerne v. Flores*, 521 U.S. 507, 519–20 and 530–34 (1997).
40. 467 U.S. at 1014–1016.
41. 467 U.S. at 1014. *See Berman*, 348 U.S. at 33 (1954)
42. *See* the discussion in the section below entitled “Injunctive Relief or ‘Just Compensation’.”
43. 467 U.S. at 1003–1005, citing *United States v. General Motors Corp.*, 323 U.S. 373, 378 (1945).
44. *See* discussion in *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg’l. Planning Agency*, 535 U.S. 302 (2002) and *Yee v. City of Escondido*, 503 U.S. 519, 522 (1992) (discussing the difference between physical occupation and mere regulation); *Goldbatt v. Hempstead*, 369 U.S. 590, 594 (1962) and *Penn. Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922) (“The general rule at least is

that while property may be regulated to a certain extent, if that regulation goes too far it will be recognized as a taking.”).

45. See, e.g., *Kaiser Aetna v. United States*, 444 U.S. 164 (1979) (government grant of public access to private pond found to be a taking tantamount to “an actual physical invasion.”)

46. *Penn Central Transportation Co. v. City of New York*, 438 U.S. 104, 124 (1978).

47. *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 413 (1922).

48. *United States v. Riverside Bayview Homes*, 474 U.S. 121 (1985) (requiring permit to fill privately held wetlands is not a taking; but noting that denying such a permit may entitle owner to just compensation); *Texaco v. Short*, 454 U.S. 516 (1982) (mineral claims may lapse if owner does not comply with regulations regarding such holdings); and *United States v. Locke*, 471 U.S. 84 (1984) (requiring recordation of mining claims is not a taking).

49. 467 U.S. at 1004–1005.

50. *Id.* at 1005–1007.

51. *Id.* at 1008–1010.

52. 312 F.3d at 41–42, citing *Corn Products Ref. Co. v. Eddy*, 249 U.S. 427, 431–32 (1919), which upheld as a permitted non-taking regulation the requirement that ingredient lists be disclosed to prevent consumer fraud.

53. *Andrus v. Allard*, 444 U.S. 51, 65–66 (1979).

54. 312 F.3d at 34; relying upon *Goldblatt v. Hempstead*, 369 U.S. 590, 594 (1962) and *Penn. Coal Co. v. Mahon*, 260 U.S. 393 (1922).

55. 312 F.3d at 34; relying upon *Penn Central*, 438 U.S. at 124.

56. 312 F.3d at 44.

57. *Id.* at 34; relying upon *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1015 (1992).

58. 312 F.3d at 51. See *Nixon v. United States*, 978 F.2d 1269, 1284–85 (D.C. Cir. 1992) (finding no compelling distinction between real and personal property that would render the per se rule inapplicable).

59. 312 F.3d at 50–51.

60. 312 F.3d at 48–51.

61. 312 F.3d at 34 n.5; relying upon statutes such as the Toxic Substances Control Act, 15 U.S.C. § 2601–92. Under that statute, manufacturers of chemicals must submit test data to EPA and there is no exemption for trade secrets.

62. *Id.*

63. *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 535 U.S. 302, 323–24 (holding that the “long-standing distinction between acquisition of property for public use, on the one hand, and regulations prohibiting private uses, on the other, makes it inappropriate to treat cases involving physical takings as controlling precedents for the evaluation of a claim that there has been a regulatory taking . . . we do not apply our precedents from the physical taking context to regulatory taking claims.”).

64. 312 F.3d at 43.

65. *Id.* at 42.

66. *Id.* at 38.

67. *Id.* at 39.

68. 312 F.3d at 40, relying upon *Corn Products*, 249 U.S. at 431–32, which permitted a state to require a complete list of product ingredients to prevent public deception that might otherwise occur through mislabeling and did not find such a regulation to constitute a “taking.” The lead opinion in *Reilly* indicates that disclosure of the complete contents of a product might be “fair information” in one context (such as the food labeling in *Corn Products*) whereas only disclosure of a partial list of ingredients might be justified in another (for example, only those ingredients of tobacco products found to be harmful in *Reilly*).

69. 312 F.3d at 45.

70. 312 F.3d at 45–46. The lead opinion contrasts the complete destruction of the trade secret rights of the tobacco companies with situations in which the economic value of personal property was substantially diminished, but not entirely destroyed, by government regulation. In this section of the lead opinion, primary reliance is placed upon *Andrus v. Allard*, 444 U.S. 51 (1979), which held that a regulation prohibiting the sale of eagle

parts, although severely undermining the economic value of the personal property involved, did not completely destroy its value since, for example, the regulation did not prevent the owners of eagle parts artifacts from displaying those artifacts for a fee. This would appear to be a very slender thread of distinction since the primary worth of artifacts made from eagle parts would be their resale value. A better approach to *Andrus* may be to recognize it as a case in which the government—read “public”—interest at stake in preserving the national symbol of the United States from annihilation by trophy hunters was the dominant factor in the balancing of interests, especially when combined with the difficulty and burden on the government of determining which eagle artifacts had been made before and after the ban in an effort to spare the owners of existing eagle artifacts the burden of the regulation. Under this approach to the three-part test, the government (public) interest was so dominant over the preexisting investment-backed expectations of eagle-parts-artifact owners that the ban was not a taking but instead, under the reasoning of the lead opinion in *Reilly*, a compelling “counterbalance to the private loss involved” such that a taking did not occur.

71. *Id.* In the “Economic Impact” section of Judge Torruella’s lead opinion, he has no difficulty in reaching the conclusion that disclosure of the tobacco ingredients will destroy the “millions of dollars” spent by the tobacco companies in creating their formulas and the “billions of dollars” in value represented by the brands involved.

72. 312 F.3d at 45.

73. 312 F.3d at 52.

74. *Id.*, quoting *Pharm. Research & Mfrs. of Am. v. Concannon*, 249 F.3d 66,77 (1st Cir. 2001) and also relying upon *Yee v. City of Escondido*, 502 U.S. 519, 534 (1992).

75. 312 F.3d at 52–53.

76. *Id.* at 54

77. *Id.* at 52–53.

78. *Id.* at 53.

79. *Id.* at 55–56.

80. *Id.* at 30 and 54 n. 27.

81. See *Mullenberg v. United States*, 857 F.2d 770 (Fed. Cir. 1988) (holding that the Court of Federal Claims does not have jurisdiction over suits against the government for discrimination), cited in *Mients v. United States*, 50 Fed.Cl. 665 (2001).

82. See *Eastern Enterprises v. Apfel*, 524 U.S. 498 (1998).

83. U.S. CONST. amend. V and *Monsanto*, 467 U.S. at 1016 (“Equitable relief is not available to enjoin an alleged taking of private property for public use, duly authorized by law, when a suit for compensation can be brought against the sovereign subsequent to the taking.”).

84. 312 F.3d at 26 and 47 n. 22.

85. *Id.*

86. See *Eastern Enterprises*, 524 U.S. 498, 537 (1998). But see *Monsanto*, 467 U.S. at 1017–20, indicating that once the appropriateness of the taking is determined it is generally proper to refer the matter to the Court of Claims under the Tucker Act.

87. 467 U.S. at 1020.

88. 312 F.3d at 46–47.

89. *Id.* at 47.

90. *Id.*

91. *Id.* It is interesting to note that after discussing the unconstitutional nature of the taking in *Reilly* the lead opinion then states that it need not address the Due Process Clause arguments of the tobacco companies. 312 F.3d at 47. However, it appears that this one-sentence section of the lead opinion is aimed at the procedural due process arguments of the tobacco companies and does not address the substantive due process rights of the companies.

92. See *Eastern Enterprises v. Apfel*, 524 U.S. 498 (1998).

93. See Richard H. Seamon, *An Analysis of Jurisdictional Issues Arising from Eastern Enterprises v. Apfel*, 51 ALA. L. REV. 3 (Spring 2000), discussing relief from *ultra vires* enactments which may rise to the level of violations of substantive due process rights as highlighted by the Supreme Court in *Eastern Enterprises*, 524 U.S. 498 (1998).

(continued on page 20)

Negotiation Ethics: Not an Oxymoron

BY LISA A. DOLAK



Lisa A. Dolak

“Ethics” in the context of negotiations is a bit of a paradox. After all, “selective disclosures” and other techniques of deception generally are accepted as part of the process.¹ Second, absent fraud, the legal obligation to act in good faith attaches only to the performance—not the negotiation—of contracts.²

Third, it would be disingenuous to argue that conducting negotiations with scrupulous honesty and candor is always, or even usually, the most effective way.

Of course, lawyers are required to observe the applicable rules of ethics. The rules themselves, however, redefine what it means to be truthful in the context of negotiations.³ Even when the rules are violated, a lawyer’s misrepresentations or material nondisclosures are difficult to detect and unlikely to result in disciplinary action.⁴ Clearly, there is little incentive to go beyond what the ethics rules require, at least when doing so would disadvantage the lawyer’s client.⁵ In fact, some argue that the obligation of zealous representation requires a “competitive” approach, at least in the absence of the client’s consent to the use of “problem-solving” techniques.⁶

The approach and techniques employed in any given negotiation will, appropriately, depend on a variety of factors, including the client’s instructions, the significance of the matter to the client, the tactics used by the other side, the extent of the client’s participation, and the parties’ relationship and prior dealings. Nevertheless, negotiation counsel must understand the limits set by the rules of ethics. The following questions are designed to test your understanding of the law governing “negotiation ethics.”⁷

1. A lawyer may not represent both the licensor and the licensee in a licensing transaction.

- (a) True
- (b) False

Generally, true. Rule 1.7(a) of the ABA Model Rules of Professional Conduct (Model Rules) prohibits the simultaneous representation of two clients where “the representation of one client will be directly adverse to another client,” or where “there is a significant risk that the representation of one [client] will be materially limited by the lawyer’s responsibilities to another client”⁸

However, notwithstanding the “concurrent conflict of interest” that exists in the situations described in Rule 1.7(a), the representation may proceed if “the lawyer

reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client,” and “each affected client gives informed consent, confirmed in writing.”⁹ The corresponding provisions of the ABA Model Code of Professional Responsibility (Model Code) prohibit simultaneous representations “if the exercise of [the lawyer’s] independent professional judgment in behalf of a client will be or is likely to be adversely affected by the [common representation], or if it would be likely to involve him in representing differing interests,”¹⁰ unless “it is obvious that he can adequately represent the interest of each and if each consents to the representation after full disclosure of the possible effect of such representation. . . .”¹¹

Accordingly, even where common representation in a transaction would give rise to a conflict of interest, as defined by the ethics rules, the clients can “waive” the conflict. The exception, according to Comment 28 to Model Rule 1.7, is where the interests of the parties to the negotiation are “fundamentally antagonistic” to each other.¹² However, “where the clients are generally aligned in interest even though there is some difference of interest among them,” common representation is permissible.¹³

The universe of license transactions includes situations at both extremes. At the “fundamentally antagonistic” end of the spectrum, where common representation would be improper, there is the negotiation to settle a vigorously disputed infringement claim. However, many license transactions involve parties whose interests are largely, if not entirely, aligned. Consider, for example, a trademark license between an intellectual property holding company and its corporate operating affiliate. In such a case, it is likely that there is no conflict at all, and no need for consent. Other license transactions lie on the continuum between the two extremes.

In many cases, the parties’ objectives for the transaction may be best met if only one lawyer is involved. When determining whether to undertake a common representation, counsel should consider several factors. First, of course, the lawyer needs to determine whether a conflict exists, and (if so) whether it is “consentable.” Beyond those issues, however, the Comments to Model Rule 1.7 identify other factors to consider:

- if the common representation fails, “[o]rdinarily, the lawyer will be forced to withdraw from representing all of the clients”¹⁴
- “representation of multiple clients is improper when it is unlikely that impartiality can be maintained”¹⁵
- the clients should be advised that the privilege will not protect their attorney-client communications should litigation ensue between the clients¹⁶

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- absent the clients' (informed) agreement to the contrary, information relevant to the common representation will have to be shared among the clients, and the clients should be so informed at the outset¹⁷

The bottom line, however, is that a lawyer considering undertaking a common representation must carefully evaluate the extent to which the parties' interests diverge, and consider whether proceeding (with the clients' informed consent) is appropriate. As one commentator has noted, representing both parties in a business transaction, even where they have consented, raises difficult questions.¹⁸ For example:

How can the same lawyer ask himself for a copyright infringement indemnification when representing a the [sic] licensee and deny it or limit it when representing the licensor? How can the same lawyer ask himself for audit rights to confirm the proper payment of royalties to a licensor and tell himself they are not necessary on behalf of the licensee?¹⁹

Even when it is appropriate for the one lawyer to consummate a transaction between two parties, the lawyer should be aware of issues beyond the need to comply with Model Rule 1.7 or DR 5-105. For example, suppose a corporate parent asks the lawyer to prepare documents and close a license transaction with one of its subsidiaries, which is not otherwise represented in the transaction. While the mere fact of the corporate relationship does not necessarily make the subsidiary a client of the lawyer and his firm for purposes of conflicts of interest analysis, the lawyer's work on the license transaction in this scenario very well may.²⁰ Thus, until the "representation" of the subsidiary in the license transaction is concluded, the lawyer and his firm are barred from representing parties adverse to the subsidiary, even in unrelated matters.²¹

2. An in-house lawyer, who wears both "business" and "legal" hats for the corporation, and who negotiates with an unrepresented party, must:

- (a) inform the other party that she is a lawyer**
- (b) avoid creating the impression that she is not a lawyer**
- (c) help the other party to understand the applicable law**
- (d) advise the other party to obtain counsel**

Clearly, the lawyer must avoid creating the impression that she is not a lawyer. According to Model Rule 4.3:

In dealing on behalf of a client with a person who is not represented by counsel, a lawyer shall not state or imply that the lawyer is disinterested. When the lawyer knows or reasonably should know that the unrepresented person misunderstands the lawyer's role in the matter, the lawyer shall make reasonable efforts to correct the misunderstanding.²²

Moreover, she should explain that she represents her client, and that the client has interests adverse to those of the other party.²³ She should refrain from advising the other party about the law or other matters, except that she may suggest that the other party obtain counsel.²⁴

3. A lawyer who represents a client in license negotiations with an unrepresented party risks establishing an attorney-client relationship with that party.

- (a) True**
- (b) False**

One very good reason to avoid giving advice to unrepresented parties (other than to suggest that the unrepresented party obtain counsel) is that the unrepresented party could conclude that the lawyer is also acting on his behalf. Whether such a conclusion is reasonable, potentially giving rise to an attorney-client relationship, depends on the sophistication of the unrepresented party and the statements and actions of the lawyer and that party during the negotiations.²⁵ Clearly, a lawyer who unreasonably fails to correct any misunderstandings regarding his allegiance invites trouble. But even where the unrepresented party does not evidence any misconceptions about whom the lawyer represents, he may later claim that the lawyer led him to believe the lawyer was acting on his behalf, for example, by explaining the implications of certain license provisions. And if an attorney-client relationship is created, the lawyer, of course, owes the "unintended" client all of the associated duties (i.e., loyalty, confidentiality, etc.). Consequently, a lawyer who negotiates with an unrepresented party should make clear that he does not represent that party in the negotiation.

4. A lawyer representing a client in a negotiation may affirmatively misrepresent the client's "bottom line."

- (a) True**
- (b) False**

In a Model Rules jurisdiction, Rule 4.1(a) provides the relevant guidance. It provides that "[i]n the course of representing a client a lawyer shall not knowingly . . . make a false statement of material fact or law to a third person."²⁶ However, the commentary to Rule 4.1 defines what is a "fact" for purposes of negotiation. Specifically, according to Comment 2:

This Rule refers to statements of fact. Whether a particular statement should be regarded as one of fact can depend on the circumstances. Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party's intentions as to an acceptable settlement of a claim are in this category. . . .²⁷

Thus, at least to the extent that Model Rule 4.1(a) applies, a lawyer is free to "misrepresent" the client's "number." Several justifications for this rule have been offered.²⁸ First, arguably, the lawyer is not making a statement of fact, but rather a statement regarding his client's intentions.²⁹ Second, exaggerating what the client has indicated is its bottom line is not misleading, because in settling on its number, the client has factored in the amount that it believes the other party is willing to pay or accept.³⁰ The client's "bottom line" thus fluctuates

with the other party's intentions. Third, a rule that did not permit lying about what one's client is willing to pay or accept would be unworkable in the context of negotiations.³¹ And fourth, because such misrepresentations are very difficult to detect, the lawyer who scrupulously obeyed such a rule would be placed at a serious disadvantage.³²

One commentator has argued that misrepresentations relating to the limits of the lawyer's settlement authority fall into the same category, again because the client's instructions as to authority are, no doubt, influenced by what the client believes it can get, and because a lawyer who disregarded a rule requiring honesty would enjoy a significant advantage over a scrupulous adversary.³³ Furthermore, to require sincerity in disclosures relating to the limits of authority would simply encourage lawyers and their clients to agree that the lawyer has no authority, hamstringing negotiations.³⁴

5. A lawyer representing a licensor in a negotiation may misrepresent the size of an offer it has received from another potential licensee.

- (a) True
- (b) False

False. Such a misrepresentation is a statement of fact, and assuming the size (or existence, for that matter) of other offers is material, it is prohibited by Model Rule 4.1 and the corresponding Model Code provision, and not excused by Comment 2, quoted above.³⁵

6. A lawyer for a patent licensor must inform the potential licensee of all potentially invalidating prior art of which it is aware.

- (a) True
- (b) False

Model Rule 4.1(b) governs here. It provides that "a lawyer shall not knowingly . . . fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client . . ." ³⁶ However, Comment 1 to Rule 4.1 provides that "[a] lawyer . . . generally has no affirmative duty to inform an opposing party of relevant facts."³⁷ Thus, Rule 4.1 places the onus on the licensee in Question 6 to ask about known prior art, not on the licensor's attorney to volunteer what she knows.

7. A lawyer for a licensee who learns during negotiations that his client has understated its past sales of infringing product must:

- (a) obey his client's instruction not to reveal the correct figures
- (b) provide the other party with the correct figures
- (c) counsel the client to provide the other party with the correct figures
- (d) withdraw from the representation if the client refuses to correct the record
- (e) answer (a) and answer (c)
- (f) answer (c) and answer (d)

This situation is different from that described in Question 6, because the client, having chosen (even in response to a question) to speak, is obligated to speak the truth, and the lawyer is presumptively obligated by Model Rule 4.1(b) to "avoid assisting a . . . fraudulent act by a client."³⁸ However, Rule 4.1(b) imposes an important limitation on the lawyer's course of action in this situation. It further provides that the lawyer's duty to protect her client's confidences by Model Rule 1.6 trumps her disclosure obligations under Rule 4.1(b).³⁹

Model Rule 1.6 forbids the disclosure of "information relating to the representation of a client unless the client gives informed consent,"⁴⁰ and none of the stated exceptions to the Rule apply in the circumstances.⁴¹ Some jurisdictions, however, have adopted less restrictive versions of Rule 1.6, and permit the disclosure of confidences for the purpose of preventing fraud or financial harm to another.⁴² Thus, the correct answer to Question 7 depends on the law of the relevant jurisdiction. In jurisdictions that apply "pure" Rule 1.6, the lawyer is prohibited from correcting the misstatement, unless the client consents to the disclosure. However, the lawyer must withdraw from the representation if "the representation will result in violation of the rules of professional conduct or other law,"⁴³ and is permitted to withdraw if "the client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is . . . fraudulent."⁴⁴ Furthermore, the lawyer should ("shall," if Model Code provision DR 7-102(B)(1) applies⁴⁵) counsel the client to correct the misstatement.

In addition, ABA Formal Opinion No. 92-366 offers the lawyer the opportunity, in some cases, to alert the client's "victim" to the fraud. Specifically, the ABA opinion allows a lawyer to engage in a "noisy withdrawal"—to disavow any of her work product used by the client to carry out the deception—but only where necessary to prevent the client's use of the work product to perpetrate the fraud.⁴⁶

The same analysis applies whether the client's understatement was intentional or innocent. As noted above, the client had no obligation to volunteer the sales figures in the first place, but having provided them to the other side, whether voluntarily or in response to the other party's inquiry, the client has the legal obligation to correct the misstatement, if the amount of past sales is a material fact on which the other party will rely.

8. A lawyer for a licensee who learns after the transaction has closed that his client has understated its past sales of infringing product may engage in a "noisy withdrawal."

- (a) True
- (b) False

As in the scenario above, the lawyer should advise his client to reveal the misstatement to the licensor. And, the lawyer is permitted to withdraw from the representation.⁴⁷ According to ABA Formal Opinion 92-366, however, a

“noisy withdrawal” is not permitted once the transaction has closed.⁴⁸ However, disclosures made to rectify client fraud are permitted by some states’ ethics rules.⁴⁹

9. A lawyer for a licensee who has agreed to pay the prosecution costs for future patents relating to the licensed technology, but who discovers, before signing the license, that the licensor’s counsel has failed to include this term in the document:

- (a) must remain silent
- (b) must consult with his client to seek permission before calling the error to the attention of the licensor’s counsel
- (c) must inform the licensor’s counsel of her omission
- (d) should inform the licensor’s counsel of her omission

According to ABA Informal Opinion 86-1518, the lawyer should correct the other attorney’s apparent drafting error, and need not consult with his client about the situation.⁵⁰ Although the omission “relates to the representation,” and would appear, therefore, to be protected from disclosure by Model Rule 1.6, the ABA opinion states that calling the error to the attention of the other lawyer is “impliedly authorized in order to carry out the representation”—and is, therefore, permissible.⁵¹

What the lawyer may not do, according to the ABA opinion, is advise the client to take advantage of the other lawyer’s mistake.⁵² To do so “might raise a serious question of the violation” of Model Rule 1.2(d),⁵³ which provides that “[a] lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is . . . fraudulent . . .”⁵⁴ Thus, it has been argued that correcting the other lawyer’s error is “clearly the better practice.”⁵⁵

10. A lawyer who conducts negotiations in a state other than the state(s) in which he or she is licensed risks fee forfeiture.

- (a) True
- (b) False

True—at least in California. In *Birbrower, Montalbo, Condon & Frank, P.C. v. The Superior Court of Santa Clara County*,⁵⁶ a former client succeeded in defending a claim for fees brought by a New York firm whose members had negotiated in California on the former client’s behalf.⁵⁷ The court held that practicing law in California without a California license precluded the firm from recovering attorneys’ fees incurred in the course of the work in California.⁵⁸ However, *Birbrower* does not apply where the out-of-state lawyer’s client is not a California resident.⁵⁹

Conclusion

As the foregoing questions indicate, the ethics rules are, of course, relevant to negotiations. To an extent, the rules permit zealous representation by recognizing the realities of “competitive” negotiation. However, they do

not provide specific guidance for every situation, leaving much to the judgment of the practitioner.

Endnotes

1. See generally Anne M. Burr, *Ethics in Negotiation: Does Getting to Yes Require Candor?*, 56 DISP. RESOL. J. 8, 10–11 (2001); David Geronemus, *Lies, Damn Lies and Unethical Lies*, 6 BUS. L. TODAY 11, 11 (1997).
2. See Burr, *supra* note 1, at 10.
3. See *infra* notes 28–34 and accompanying text.
4. See Charles B. Craver, *Negotiation Ethics: How To Be Deceptive Without Being Dishonest/How To Be Assertive Without Being Offensive*, 38 S. TEX. L. REV. 713, 719 (1997).
5. See Paul Zwier II, *Ethics and Negotiation*, 31 PLI/NY 335, 350–51 (1995).
6. See *id.* at 351.
7. Most state ethics rules are based on either the American Bar Association (ABA) Model Rules of Professional Conduct or the earlier ABA Model Code of Professional Responsibility. This article discusses general ethics principles, and incorporates amendments to the Model Rules through August 2002. As always, specific provisions of the applicable rules should be consulted for guidance on particular fact situations.
8. See MODEL RULES OF PROF’L CONDUCT R. 1.7(a).
9. See MODEL RULES OF PROF’L CONDUCT R. 1.7(b). Rule 1.7(b) also requires that the representation be “not prohibited by law,” and “not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal.” *Id.* Thus, a lawyer engaged in the common representation of multiple clients in a proceeding before a tribunal could not represent those clients in negotiations to settle claims between them in the proceeding. Model Rule 1.0 defines “informed consent” as “the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct.” MODEL RULES OF PROF’L CONDUCT R. 1.0(e). “Confirmed in writing,” according to Model Rule 1.0(b), means “informed consent that is given in writing by the person or a writing that a lawyer promptly transmits to the person confirming an oral informed consent.” MODEL RULES OF PROF’L CONDUCT R. 1.0(b).
10. MODEL CODE OF PROF’L RESP. DR 5-105(A).
11. MODEL CODE OF PROF’L RESP. DR 5-105(C).
12. See MODEL RULES OF PROF’L CONDUCT R. 1.7, cmt. 28.
13. See *id.*
14. See MODEL RULES OF PROF’L CONDUCT R. 1.7, cmt. 29.
15. See *id.*
16. See MODEL RULES OF PROF’L CONDUCT R. 1.7, cmt. 30.
17. See MODEL RULES OF PROF’L CONDUCT R. 1.7, cmt. 31.
18. See Larry M. Zanger, *Ethics in Licensing*, 576 PLI/PAT 797, 805 (1999).
19. *Id.*
20. See Vincent R. Johnson, *Ethics in Licensing*, 496 PLI/PAT 463, 474–76 (1997).
21. See *id.* at 476.
22. See MODEL RULES OF PROF’L CONDUCT R. 4.3.
23. See MODEL RULES OF PROF’L CONDUCT R. 4.3, cmt. 1-2.
24. See MODEL CODE OF PROF’L RESP. DR 7-104(A)(2) (prohibiting the giving of advice to the unrepresented party); see also MODEL RULES OF PROF’L CONDUCT R. 4.3, cmt. 2.
25. See Johnson, *supra* note 23, at 470–72.
26. See MODEL RULES OF PROF’L CONDUCT R. 4.1(a). See also MODEL CODE OF PROF. RESP. DR 7-102(A)(5) (“[i]n his representation of a client, a lawyer shall not . . . [k]nowingly make a false statement of law or fact”).
27. See MODEL RULES OF PROF’L CONDUCT R. 4.1, cmt. 2.
28. See Geronemus, *supra* note 1, at 12–13.
29. See *id.* at 12.
30. See *id.*

Taken by the Fifth

(continued from page 15)

31. *See id.* at 12–13.
32. *See id.* at 13.
33. *See id.*
34. *See id.* The author, though, notes the lack of specific guidance or consensus on this issue. *See id.*
35. *See supra* notes 28–29 and accompanying text.
36. MODEL RULES OF PROF'L CONDUCT R. 4.1(b). *See also* MODEL CODE OF PROF'L RESP. DR 7-102(A)(3) (a lawyer shall not "[c]onceal or knowingly fail to disclose that which he is required by law to reveal").
37. *See* MODEL RULES OF PROF'L CONDUCT R. 4.1, cmt. 1.
38. *See* MODEL RULES OF PROF'L CONDUCT R. 4.1(b).
39. *See id.*
40. *See* MODEL RULES OF PROF'L CONDUCT R. 1.6.
41. Rule 1.6 permits the disclosure of "information relating to the representation" if "the disclosure is impliedly authorized in order to carry out the representation," or if (and to the extent) "the lawyer reasonably believes necessary" to:
 - (1) . . . prevent reasonably certain death or substantial bodily harm;
 - (2) . . . secure legal advice about the lawyer's compliance with these Rules;
 - (3) . . . establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, . . . establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or . . . respond to allegations in any proceeding concerning the lawyer's representation of the client; or
 - (4) . . . comply with other law or a court order.
- Id.*
42. *See* Zwier, *supra* note 5, at 345 n.9. Also, the relevant Model Code provision authorizes a lawyer to "reveal . . . [t]he intention of his client to commit a crime and the information necessary to prevent the crime." *See* MODEL CODE OF PROF'L RESP. DR 4-101(C)(3).
43. *See* MODEL RULES OF PROF'L CONDUCT R. 1.16(a)(1). *See also* MODEL CODE OF PROF'L RESP. DR 2-110(B) (a lawyer "shall withdraw from employment . . . if . . . [h]e knows or it is obvious that his continued employment will result in violation of a Disciplinary Rule") and DR 1-102(A) (a lawyer shall not "[e]ngage in conduct involving dishonesty, fraud, deceit, or misrepresentation").
44. *See* MODEL RULES OF PROF'L CONDUCT R. 1.16(b)(2).
45. *See* MODEL CODE OF PROF'L RESP. DR 7-102(B)(1) (a lawyer who discovers that a client "has, in the course of the representation, perpetrated a fraud on a person or a tribunal shall promptly call on his client to rectify the same").
46. ABA Comm. on Ethics and Professional Responsibility, Formal Op. 92-366 (1992).
47. *See* MODEL RULES OF PROF'L CONDUCT R. 1.16(b)(3) (a lawyer may withdraw if "the client has used the lawyer's services to perpetrate a crime or fraud").
48. *See* ABA Opinion No. 92-366, *supra* note 49.
49. *See* Zwier, *supra* note 45.
50. ABA Comm. on Ethics and Professional Responsibility, Informal Op. 86-1518 (1986).
51. *See id.*
52. *See id.*
53. *See id.*
54. MODEL RULES OF PROF'L CONDUCT R. 1.2(d).
55. *See* Geronemus, *supra* note 1, at 14.
56. 17 Cal. 4th 119 (1998).
57. *See id.* at 140.
58. *See id.* at 139.
59. *See, e.g.,* Gerowitz v. Noll, No. G030308, 2003 WL 1711279, at *2 (Cal. Ct. App. Mar. 28, 2003); Estate of Condon v. McHenry, 65 Cal.App.4th 1138, 1146 (Cal. Ct. App. 1998).

94. For example, in *Reilly*, the lead opinion noted that the trade secret rights in the MARLBORO brand, alone, might be worth "billions of dollars." 312 F.3d at 41. However, the *Reilly* Court does not address the substantive due process issue and it is therefore impossible to accurately ascertain whether the burden of the taking of the tobacco company's trade secrets would have been a factor in the issuance of injunctive relief.

95. *See, e.g., Reilly*, 312 F.3d at 47.

96. 312 F.3d at 26 (characterized in *Reilly* as the need to provide "a meaningful opportunity to be heard.")

97. It would appear that the taking of trade secrets in *Reilly*, like those in *Monsanto*, could be capable of remedy by "just compensation." Although there is no discussion of this issue in *Reilly*, the lead opinion notes that some of the brands at issue are "worth billions of dollars." 312 F.3d at 41. Thus there was a basis for assessing "just compensation" if disclosure of the trade secrets had been made. It would then be up to the state to determine if the contemplated disclosure was worth the required compensation.

98. *See* Seamon, *supra* at n.93.

99. *See, e.g.,* Griswald v. Connecticut, 381 U.S. 479, 481–86 (1965) (Connecticut statute forbidding use of contraceptives found to violate the right of marital privacy which the Court determined to be within the penumbra of specific guarantees of the Bill of Rights); Lawrence v. Texas, 539 U.S. ____ (2003)(Case No. 02-102, Decided June 26, 2003)(striking Texas sodomy law on substantive due process grounds).

100. *See, e.g.,* Lochner v. New York, 198 U.S. 45 (1905)(a decision widely cited by the Supreme Court in the early 1930s to strike down New Deal legislation as violating the "Right to Contract" which that Court found to be encompassed within the 14th Amendment Due Process provisions).

101. *See* West Coast Hotel v. Parrish, 300 U.S. 379 (1937) and Ferguson v. Skrupa, 372 U.S. 726 (1963).

102. 381 U.S. at 481–86 (Connecticut statute forbidding use of contraceptives violates the right of marital privacy which is within penumbra of rights encompassed within the Bill of Rights).

103. 410 U.S. 113 (1973) (finding that certain state criminal abortion laws violated the Due Process Clause of the Fourteenth Amendment, which protects the "right of privacy" against state action)

104. Lawrence v. Texas, 539 U.S. ____ (2003) (Case No. 02-102, Decided June 26, 2003) (striking Texas sodomy law on substantive due process grounds.)

105. In fact, *Reilly's* lead opinion and the Supreme Court in similar situations seem to actively avoid addressing substantive due process issues. 312 F.3d at 56–57, *Eastern Enterprises*, 524 U.S. 498 (1998) and Babbitt v. Youpee, 519 U.S. 234 (1997).

106. 300 U.S. 379 (1937).

107. *Ferguson*, 372 U.S. 726 (1963).

108. 28 U.S.C. § 1491(a). The Court of Claims does not have jurisdiction over "tort" actions or actions involving contracts "implied in law." Leonardo v. United States, 55 Fed.Cl. 344, 65 U.S.P.Q.2d 1915 (Ct. Cls. 2003) (copyright action).

109. *Id.*

110. *See, e.g., Reilly*, 312 F.3d at 26; *Eastern Enterprises*, 524 U.S. at 537; *Duke Power Co. v. Carolina Environmental Study Group, Inc.*, 438 U.S. 59, 71, n.15 (1978) (holding that the Declaratory Judgment Act "allows individuals threatened with a taking to seek a declaration of the constitutionality of the disputed governmental action before potentially uncompensable damages are sustained."); Babbitt v. Youpee, 519 U.S. 234, 243–45 (1997); and *Hodel v. Irving*, 481 U.S. 704, 716–18 (1987); *see, also, Chicago B & Q. R.R. Co. v. Chicago*, 166 U.S. 226 (1897) and *Webb's Fabulous Pharmacies v. Beckwith*, 449 U.S. 155, 159 (1980) (applying the Taking Clause to the states via the Fourteenth Amendment).

From the Chair

(continued from page 2)

- Opposition to USPTO user fee diversion was approved as policy by the ABA in 2000,⁵ and even went one step further. Last year it was made an ABA legislative priority,⁶ and was advocated to Congress as such during ABA Day in Washington last spring and on other occasions. Current pending legislation⁷ contains antidiversion language, though it remains to be seen how this complex and highly political issue will turn out.
- Our advocacy on the Federal Trademark Dilution Act (FTDA) has been greatly enhanced by having ABA policy favoring the interpretation or amendment of the FTDA in accordance with a standard of likelihood of dilution.⁸ This was of course the requisite ABA policy that led to the authorization of our *amicus* brief⁹ in the Victoria's Secret case.¹⁰ And now that the Supreme Court has declined to adopt the likelihood of dilution standard, but instead endorsed an "actual dilution" standard (which was not actually argued by any of the parties to the case), the existing ABA policy enables us to approach Congress to propose an amendment to the FTDA. We are currently studying the advisability of doing so on the sole issue of likelihood of dilution, as compared to a broader approach addressing other important dilution issues that have emerged (e.g., whether dilution by tarnishment is covered by the FTDA,¹¹ and whether famous marks that have become distinctive through use are eligible for protection under the FTDA).¹² Our Trademark Legislation Committee 201 is currently studying this topic, as a good example of how Section and ABA policy is formed from the committee level "up," which also distinguishes our association from some other IP organizations.
- Our Section's Right of Publicity policy,¹³ recommending enactment of a federal right of publicity statute to provide uniformity and certainty, will probably be presented to the House of Delegates for consideration as ABA policy at the 2004 ABA Midyear meeting in February. We scheduled this resolution for consideration last year, but voluntarily withdrew it from the agenda to study and react to some opposition that had unexpectedly emerged from other entities.

These are only examples of the interaction of Section policy and ABA policy. There will undoubtedly be others during the year. I hope this overview provides a useful perspective on policymaking in the ABA from the committee level up to the House of Delegates. The ultimate point comes full circle to encouraging Section members to be active contributors at the committee level. That is where our resolutions originate. They become Section policy either by Council adoption (usually in uncontroversial cases) or at the Section's annual Summer IPL Conference after full debate. But as shown above, the process does not always stop there. To gain maximum credibility and political gravitas, we often advocate Section policy to be endorsed by the ABA as a whole, and the outcomes of those efforts are almost always worthwhile.

Endnotes

1. See www.abanet.org/intelprop/oct02chair.html.
2. "Resolved, that the American Bar Association approves the adherence by the United States to the Protocol to the Madrid Agreement for the International Registration of Trademarks, adopted in Madrid, Spain on June 27, 1989, and the amendment of the Lanham Act, 15 U.S.C. §§ 1051 *et seq.* (1994 & Supp. II 1996), to the minimum extent required for United States adherence."
3. Our Section's recommendations on the proposed implementing regulations were delivered in live testimony to the PTO, and also in a letter submission, which is posted at www.abanet.org/intelprop/response.doc.
4. See the article by Section member Paul Kilmer in the last issue of this newsletter. Kilmer, *The Madrid Protocol—Sea Change or Tempest in a Teapot?*, IPL NEWSL., Summer 2003, at 19.
5. The policy adopted by the ABA House of Delegates reads as follows:

RESOLVED, that the American Bar Association favors in principle that Congress provide that all revenue generated by fees paid by patent and trademark applicants and owners to the United States Patent and Trademark Office remain with the USPTO without limitation, and Specifically, the Association opposes the withholding or diversion of any such revenue to fund any unrelated programs.
6. A description of the Association's legislative priority relating to PTO funding can be accessed on the ABA website at www.abanet.org/poladv/priorities/patent.html.
7. H.R. 1561, as reported by the House Judiciary Committee, contains antidiversion language in Section 5 that would make all PTO user fee revenue immediately available to the PTO upon collection, without the need for the funds to first be appropriated back to the PTO for use.
8. RESOLVED, that the American Bar Association favors in principle that the federal Lanham Act should be amended to provide that questions of trademark dilution, before the federal courts and the United States Patent and Trademark Office, Trademark Trial and Appeal Board, should be uniformly resolved under the standard of whether the junior user's mark is likely to cause dilution of the senior user's mark, rather than under a standard of actual dilution.
9. The brief is posted at www.abanet.org/intelprop/amicubrief.pdf.
10. *Moseley v. V Secret Catalogue*, 123 S. Ct. 1115 (2003), posted at www.abanet.org/intelprop/moseleyvsecret1.pdf.
11. Justice Stevens, writing for the Court, opined in *dicta* that tarnishment may not be actionable under the FTDA because it is not mentioned in the statutory text. "Whether [tarnishment] is actually embraced by the statutory text . . . is another matter. Indeed, the contrast between [the state dilution statutes, which refer to injury to business reputations, and the FTDA, which does not] arguably supports a narrower reading of the FTDA." 123 S. Ct. at 1124.
12. The Second Circuit has interpreted the FTDA to mean that only *inherently distinctive* marks can be protected. In *TCPIP Holding Co., Inc., v. Haar Comm's, Inc.*, 244 F.3d. 88, 98 (2d Cir. 2001), the court held: "Because TCPIP's mark, 'The Children's Place,' as a designator of stores for children's clothing and accessories, is descriptive, and thus, lacks inherent distinctiveness, it cannot qualify for the protection of the Dilution Act." TCPIP states that some of America's most famous marks—"examples are American, United, Continental Airlines, Metropolitan Life, Allied Chemical, and First National Bank of Wherever"—cannot be protected under the FTDA because they are famous only "as a function of their commercial dominance" and lack inherent distinctiveness. 244 F.3d. at 96.

2003 Expert Update

Kumho-Wrestling: Are Your IP Experts in Shape?

BY ALAN RATLIFF



Alan Ratliff

This article presents a combination of short-term and long-term perspectives on the roles of experts in federal intellectual property (IP) cases.

With regard to short-term developments since the 2002 update, there has been a significant increase in substantive *Daubert* decisions relating to experts in federal IP cases. Of the total of approximately 100 substantive IP *Daubert* decisions that have been reported in one form or another, approximately one-half of those have been decided since January 1, 2001.¹ And, during 2002 and the first half of 2003, thirty-six substantive IP *Daubert* decisions have been identified.

The opinions challenged in IP cases are classified into five categories: (1) patent claim construction; (2) patent technical experts relating to infringement or other issues; (3) damages; (4) trademark surveys; and (5) other testing and science.² In about 60 percent of these cases, the experts' opinions were excluded at least in part.³ The chart below summarizes the subject, result, and totals for the current period, and it provides some cumulative totals:

Subject	Admitted	Excluded	Prior Years	Cumulative
Claim Construction	3		10	13
Patent Technical	4	4	11	19
IP Damages	3	8	12	23
Trademark Survey	3	6	18	27
Other Testing/Science	2	3	11	16
2002/2003a	15	21	62	98
PRIOR YEARS	20	30		
TOTAL	35	51		

The current-period *Daubert* decisions are referenced in the body and footnotes of this article, and six of these decisions are examined in detail. Three of these are cases in which opinions were admitted; in the other three, they were excluded. The featured decisions involve patent reasonable royalty damages, trademark infringement survey, trademark dilution survey, trade secret damages, scientific testing used in connection with claim construction, and a patent claim construction technical expert decision discussing the different approach to *Daubert* in bench trials as opposed to jury trials. The remaining decisions are referenced in the footnotes with brief, parenthetical annotations.

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In a section that takes a longer-term perspective, the article concludes with a summary of the recent findings by the RAND Institute for Civil Justice (RAND Study) relating to the effect of *Daubert* on experts in federal court. Among other things, the study presents statistical analyses that compare the frequency, success, and timing of expert reliability challenges in the decade before and after *Daubert*.

Two important findings emerge from this data: (1) Although the cumulative success rate of challenges to experts is, on average, about the same today as it was in the 1980s, the volume of such challenges has increased by nearly a factor of ten; and (2) this period also has seen challenges shift to earlier stages in legal cases; rather than coming "near-to-trial," challenges increasingly are coming soon after expert reports are filed or in connection with summary judgment.

Based on the RAND Study, the decade since *Daubert* certainly has seen an evolution in expert testimony, if not the expert revolution many predicted.

Opinions Admitted⁴

The featured decisions where expert opinions were admitted relate to (1) patent reasonable royalty damages, (2) a trademark survey, and (3) a patent claim construction, although the issue relates primarily to the difference in how courts approach *Daubert* in bench trials as opposed to jury trials.

*Lextron*⁵

The plaintiff patent holder brought an action against the defendants claiming they infringed a patent involving a computerized medical records system that tracks the health histories and medical treatments of livestock. The district court entered judgment for the plaintiff after a jury verdict. On appeal, the defendants claimed that the district court had erred in admitting the reasonable royalty opinions of the plaintiff's damages expert. The Federal Circuit Court found no error and affirmed the judgment.

Based upon a hypothetical negotiation between the parties at the time infringement began, the damages expert for the plaintiff testified at trial that a reasonable royalty for the defendants' infringing systems would amount to \$400 per month per system.⁶ The defendants objected to this testimony on the grounds that, among other things, the expert "based his opinion on inaccurate facts because he relied on the statements of others and did not undertake an independent investigation of the feedlot industry or personally review the parties' financial record."⁷

After briefly summarizing the "landmark" *Daubert* decision and amended Rule 702, the Federal Circuit

observed that the “[d]efendants confuse the requirement for sufficient facts and data with the necessity for a reliable foundation in principles and method, and end up complaining that [the expert’s] testimony was not based on ‘reliable facts.’”⁸ The court explained that “[w]hen, as here, the parties’ experts rely on conflicting sets of facts, it is not the role of the trial court to evaluate the correctness of facts underlying one expert’s testimony.”⁹

The Federal Circuit continued, summarizing its holding concerning the sufficiency of the facts or data as follows:

In this case, the trial court properly did not rule inadmissible [the expert’s] damages testimony simply because it was based on Micro Chemical’s version of the contested facts. The defendants had ample opportunity to rebut [the expert’s] damages theory during cross-examination. They also presented their competing theory through the testimony of their own expert witness, who based his opinion testimony on the defendants’ version of the disputed facts. Under these circumstances, the district court did not abuse its discretion in allowing [the expert] to testify.¹⁰

The Federal Circuit also rejected the defendant’s suggestion that the expert used an “unreliable methodology.”¹¹ The court, articulating its well-established view concerning the approach used to compute reasonable royalty damages, reminds that it has “‘endorsed the conceptual framework of a hypothetical negotiation between patentee and infringer as a means for determining a reasonable royalty.’ . . . [The expert’s] testimony did not run afoul of Rule 702, and the district court did not abuse its discretion in admitting it.”¹²

*Betterbox*¹³

In this trademark case, Betterbox brought a declaratory judgment action against the defendant competitor, Black Box, seeking a ruling that its trademark did not infringe on Black Box’s mark. After a jury verdict, the district court entered judgment for the plaintiff. On appeal, the defendant claimed, among other things, that the district court had erred in admitting the marketing expert’s opinions on likelihood of confusion. The Third Circuit found no error and affirmed the judgment.

At the trial, expert testimony was offered on the likelihood that consumers would be confused about the Betterbox and Black Box marks.¹⁴ The defendant had argued that the plaintiff’s expert was not qualified to testify on this subject and that he had used unreliable methods in reaching his conclusions.¹⁵ After reviewing the expert’s qualifications, the court explained that “‘at a minimum, a proffered expert witness . . . must possess skill or knowledge greater than the average laymen. . . .’”¹⁶ The expert’s qualifications included extensive “practical experience” in the area of marketing and advertising logos and, specifically, twenty years’ experience in the field of direct marketing and mail-order catalogs. The circuit court did not find persuasive the defendant’s argument that the expert’s limited experience of only four years in the specific field of direct marketing of computer products undermined his qualifications, stating “[f]our years of experience at the helm of a company is substantial.”

Additionally, the Third Circuit was not persuaded by the defendant’s arguments that eight years had passed since this specific experience, or that the expert had no experience with the specific product involved in the case. The Third Circuit, thus, concluded that the plaintiff’s expert was sufficiently well qualified to testify.¹⁷ The court also considered the defendant’s argument that the expert “should not have been allowed to testify as an expert because his methodology was deficient.” After briefly summarizing *Daubert* and *Kumho Tire*, the court observed that the expert’s “testimony was based on his ‘personal knowledge or experience,’ . . . rather than a methodology that satisfies the *Daubert* factors.”¹⁸ Schulte testified that he had examined the companies’ catalogs, surveyed colleagues informally, and evaluated the target markets for the catalogs. In doing so, he had focused on the following accepted factors: “[t]he perception of the names,” “[t]he graphic logo design,” and “[t]he presence in the market place and the look and feel of the catalogs.”¹⁹

Although the majority did not elaborate or explain the specific method used by the expert to evaluate these factors (and it appears that the expert may have used professional judgment rather than a statistical methodology),²⁰ the court reminded that it owed great deference to the trial court’s judgment.²¹

*Smithkline Beecham*²²

The plaintiffs, pharmaceutical companies, sued a generic drug manufacturer claiming infringement of a patent for the active ingredient in an antidepressant drug. After a bench trial, presided over by Judge Richard Posner of the U.S. Court of Appeals for the Seventh Circuit, sitting by designation, the district court held that the patent, if construed so as to be sufficiently definite, was not infringed.

During the course of the trial, the defendant objected to the reliability and opinion bases of plaintiffs’ chemistry experts. In its opinion, the court commented that it could have excluded the plaintiffs’ experts under Rule 702, but did not because it was a bench trial.²³ Explaining its conclusion, the court observed that *Daubert* could be applied somewhat differently to bench trials than jury trials:

The primary purpose of the *Daubert* filter is to protect juries from being bamboozled by technical evidence of dubious merit, *Seaboard Lumber Co. v. United States*, 308 F.3d 1283, 1301–02 (Fed. Cir. 2002), as is implicit in the courts’ insistence that the *Daubert* inquiry performs a “gatekeeper” function. See, e.g., *Smith v. Ford Motor Co.*, 215 F.3d 713, 718 (7th Cir. 2000). In a bench trial it is an acceptable alternative to admit evidence of borderline admissibility and give it the (slight) weight to which it is entitled.²⁴

In further support for its decision to admit the experts, the district court went on to discuss Federal Circuit *Daubert* jurisprudence specifically:

In *Seaboard Lumber Co. v. United States*, supra, 308 F.3d at 1302, while pointing to the concern with protecting juries from confusion, did say that the *Daubert* standard must be

followed in bench trials as well. But it did not say that it must be followed rigidly in such trials. Daubert requires a binary choice—admit or exclude—and a judge in a bench trial should have discretion to admit questionable technical evidence, though of course he must not give it more weight than it deserves.²⁵

Concluding its discussion of *Daubert* in bench trials, the court returned to the case at hand:

This at any rate was my approach with respect to [experts], and I do not consider their evidence to have been wholly lacking in credibility or probative value. While the sum of zero plus zero is zero, the sum of one plus one is two; and the convergent result of two weak tests is more robust than the result of each test taken in isolation; so maybe one plus one is three. But if proof by a preponderance of the evidence is modeled as scoring 5.01 points out of 10, then 3 out of 10 won't hack it.²⁶

A formula for success with experts in bench trials? Only time will tell.

Opinions Excluded²⁷

The featured decisions where expert opinions were excluded relate to (1) generally accepted trade-secret damage methodologies, (2) the insufficiency of expert opinions on likelihood of confusion in trademark-dilution cases absent a survey, and (3) the inadequacy of testing to support patent-claim construction.

*Alcatel*²⁸

This lawsuit between plaintiff Alcatel and its competitor Cisco arose out of acts of patent- and copyright-infringement and torts (most specifically, misappropriation of trade secrets) allegedly committed by Cisco and a company that Cisco previously acquired, Monterrey Networks. Alcatel alleged that Monterrey and Cisco systematically misappropriated and used cutting-edge Alcatel technology to develop and market a product called the Wavelength Router, a telecommunications product allegedly designed to compete directly with Alcatel's products. Alcatel further contended that Monterrey's ability to get the Wavelength Router ready to market quickly was critically important to Monterrey.²⁹ First, certain major national customer accounts were contingent upon Monterrey's ability to quickly develop the Wavelength Router and, second, Monterrey's speed to the market increased the likelihood that it would be acquired by Cisco and would increase the price that it would command.³⁰ Monterrey was able to achieve this accelerated product development by hiring Alcatel employees in 1998 who disclosed Alcatel's trade secrets.³¹ During 1999, in two separate transactions, Cisco acquired Monterrey for a little more than \$500 million. Subsequently, in April 2001, due to its failure to complete any sale of the Wavelength Router, Cisco cancelled the project.³²

In connection with summary judgment proceedings, the court was called upon to address the reliability of plaintiff's \$500 million damages claim.³³ Alcatel's damages expert provided calculations based rather simplisti-

cally on an acquisition-price methodology that substantially attributed the entire value of Monterrey to the allegedly misappropriated trade secrets.³⁴ The court commenced its criticism of the damages experts as follows:

This Court has long been suspicious of Alcatel's alleged entitlement to an award of over a half a billion dollars. During a hearing in July 2001 on various pending motions in this case, the Court, *sua sponte*, questioned the propriety of Alcatel's prospective damage theory. To help dispel these concerns, the Court ordered the parties to brief the legal viability of Alcatel's damage theory. Alcatel submitted its brief on August 27, 2001. In its brief, Alcatel argued that it was entitled to recover the value of the trade secrets at the time of the misappropriation. Alcatel further argued that this value could be measured based on a reasonable royalty or unjust enrichment. In response to Alcatel's brief on damages, Cisco filed a motion for summary judgment on September 18, 2001. [Doc. No. 303]. In its motion, Cisco argued that Alcatel's damage theory was untenable because Alcatel had not suffered any lost profits as a result of the alleged misappropriation and that, due to its cancellation of the Wavelength Router, Cisco had not profited from sales based on Alcatel's intellectual property. Accordingly, for these and other reasons, Cisco insisted that Alcatel could not recover pursuant to any conceivable damage theory.³⁵

In a previous ruling, the court had identified one approach to damages that was conceivably available to Alcatel, a reasonable-royalty method. The court held that such an approach is appropriate, for example, where the trade secret has not been destroyed, where the plaintiff is unable to prove specific injury, and where the defendant has not gained any profits by which to value the secrets.³⁶ The court further acknowledged that, where "damages are uncertain," the uncertainty should not "preclude recovery" and the "plaintiff should be afforded every opportunity to prove damages once the misappropriation is shown."³⁷

The court was not persuaded to abandon well-established trade secret damage law, despite giving every benefit of the doubt to Alcatel, and in spite of lengthy contentions by the Alcatel expert concerning the reasonableness of using the Monterrey acquisition price as a basis for valuing the trade secret and using the date of acquisition as the date for valuing the trade secret. Addressing the basis for the expert's opinions:

In the Court's opinion, these assumptions and opinions, all of which serve as the foundation for Alcatel's damage theory, are simply too speculative. A break or non-occurrence in any of the above chain of events would eviscerate the foundation of Alcatel's damages, and consequently, Alcatel's damage theory is rendered exceedingly uncertain.³⁸

The court continued by addressing the expert's methodology:

Aside from the speculative assumptions on which Alcatel's damage theory rests, there is substantial uncertainty as to the amount of damages Alcatel allegedly suffered. In the Court's opinion, the value of the alleged trade secrets cannot be

reasonably extrapolated from the purchase price of Monterey. Because Alcatel is not claiming it suffered lost profits from Monterey's alleged misappropriation or that Monterey or Cisco financially benefitted from direct sales, for example, of the allegedly infringing product, Alcatel's damage theory necessarily seeks to recover the value of the alleged secrets to Monterey/Cisco. Furthermore, this measure is to be calculated based on a reasonable royalty to which the parties would have agreed at the time of the alleged misappropriation. While the Court recognizes that some degree of speculation is inherent in calculating a suppositious licensing agreement between two parties that has never occurred, this hypothetical construct, however, must contain some degree of certitude. After all, the method does not permit the recovery of a simple royalty, but only a reasonable one. In this regard, Alcatel's attempt at recovering the value of the alleged trade secrets based largely on the acquisition price of Monterey, contravenes fundamental notions of reasonableness.³⁹

The court further observed that, the "[e]stimation of damages . . . should not be based on sheer speculation. If too few facts exist to permit the trier of fact to calculate proper damages, then a reasonable remedy in law is unavailable."⁴⁰ Moreover, "evidence by which the jury can value the rights the defendant has obtained," and the value of these rights should not "be based on sheer speculation."⁴¹

Even assuming a valuation approach was generally accepted, the court criticized the application of the methodology, including (1) the expert's use of the acquisition date rather than the misappropriation date to value the trade secrets (problematic both because it ignores events that may have affected value between those dates and takes into account information, including the acquisition price itself, that could not have been known by the parties at the hypothetical negotiation date), (2) the failure to apportion the acquisition price to the trade secrets, (3) no case has held that the acquisition price of a company can provide the measure of a reasonable royalty in the absence of actual lost profits, and (4) purchase price evidence is inadmissible where it is based on speculative profit projections based on "uncertain or changing market conditions, or on changing business opportunities, or on promotion of untested products, or entry into an unknown or unviable markets, or on the success of a new and unproven enterprise."⁴²

Looking, as courts often do, to federal patent law to guide the damages analysis in trade secret cases, the court quoted from a recent federal circuit decision in closing out its critique of the expert's acquisition-price methodology:

The price received by an infringing defendant for the sale of its business is not sound evidence on which to measure damages in a reasonable royalty case. . . . Reasonable royalty damages for patent infringement arise from the fact of infringement, and the portion of the sales price consisting of intangible goodwill is not the sale of infringing goods. It is partial compensation for the sale of a business. . . . [T]he portion of a sales price consisting of goodwill, i.e., compensation in excess of tangible assets, is not sales of infringing goods that can form the base for determination of a reasonable royalty.⁴³

Based on the three-and-half years of litigation in which the plaintiff had the opportunity to develop a supportable

theory of damages and failed to do so, the district court granted summary judgment against Alcatel.

*Pharmacia Corp. v. Alcon Labs, Inc.*⁴⁴

In the injunction phase of this trademark dilution case, the court concluded that, apart from consumer surveys, "lay or even expert opinion about the likelihood of confusion is inadmissible or entitled to little weight."⁴⁵ In this case, the issue dealt with the likelihood of confusion between Travatan and Xalatan. The plaintiff's experts' based their opinions primarily on a subjective evaluation of the marks in light of their experience in the pharmaceutical industry or as an ophthalmologist. The court observed "there are no reported trademark cases in which a court has based its findings of a likelihood of confusion or dilution on the types of 'opinions' on which Pharmacia relies. The bases for these opinions stand in stark contrast to the survey conducted" by defendant's expert "which demonstrates persuasively a confusion rate of 1.5 percent."⁴⁶

Similarly, the court concluded that the professor of pharmacy's opinions on the likelihood of confusion were also entitled to little weight:

His statistical model cannot predict with meaningful reliability in the real world whether Xalatan and Travatan are accurately characterized as an 'Error Pair,' or if instead they represent a 'false positive' — that is, a pair of drug names improperly classified . . . as confusingly similar. Because in the real world there are many, many more non-confusing drug name pairs than confusingly similar ones, it follows from the application of basic statistical principles that the Travatan-Xalatan pair is likely to be a false positive. In any event, [the expert] . . . was unable to opine with any degree of certainty what numbers should be used to determine his model's reliability, much less whether Travatan and Xalatan ever will be confused in the real world.⁴⁷

Noting that the court must assess confusion based on a well-defined set of factors intended to measure what is likely to happen in the real world, the court concluded the professor's model lacked significant probative value for the purposes for which it is offered. Such a "model is entitled to very little weight in a Lanham Act case and cannot serve as the basis for a finding of likely confusion, especially in light of contrary marketplace evidence and the FDA's regulatory determination."⁴⁸

*Arquest*⁴⁹

In a disposable-diaper patent case, the plaintiff filed a declaratory judgment action seeking a determination that patent claims for improvements to disposable diapers were invalid and that the plaintiff's products did not infringe the patent. The plaintiff filed a motion for summary judgment, which the district court granted after determining that the opinions of defendant's proffered expert, a college chemistry teacher, were inadmissible under *Daubert*.

The district court stated that, to avoid summary judgment, the defendant was required to present evidence showing a factual dispute as to whether the elastic member portion of disposable diapers was an additional

absorbent barrier against leakage.⁵⁰ The defendant offered her own tests, one of which used a single drop of water and one of which relied on the elastic member's becoming stained when coffee-dyed water was placed on the material. The plaintiff's expert participated with the plaintiff in conducting the "one-drop" test and concluded that the drop of water had been absorbed. The court restated the test for admissibility of expert opinion testimony under *Daubert* and concluded that the proffered opinion testimony did not meet that test because the proposed opinions were not based on sufficient facts or data.⁵¹ The court also noted that, to the extent a determination as to whether or not the material was absorbent is relevant, it was not a subject for expert testimony.⁵²

Conclusion: The Road Ahead

The RAND Study reviewed data from approximately 400 federal district court opinions between 1980 and 1999.⁵³ According to the data, the judiciary now analyzes reliability and other factors more carefully than it did prior to *Daubert* and applies stricter standards when deciding whether to admit expert evidence.⁵⁴ Such increased scrutiny culminates in more frequent exclusion of key expert testimony or grants of summary judgment.⁵⁵ Contrary to predictions, the RAND Study found no indication that it was easier to admit novel scientific evidence after *Daubert*.⁵⁶ Specifically, the RAND Study noted that *Daubert* has not increased the admissibility of novel scientific theories.⁵⁷

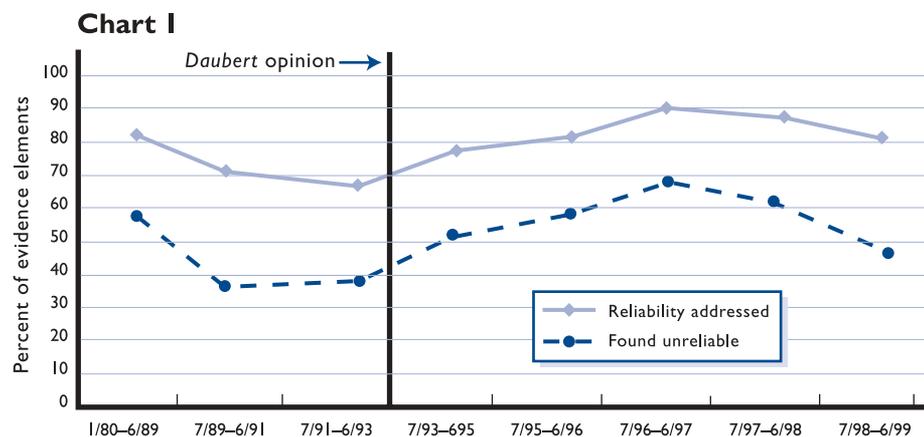
Moreover, a cursory review of the survey results suggests no significant changes in the relative frequency of expert reliability objections or opinion exclusions during the decade before and after *Daubert*.⁵⁸ But such a conclusion would miss the forest for the trees. A closer look demonstrates that the situation has changed significantly, and potentially, for the worst. Chart 1 below illustrates the percentage of reliability challenges asserted in those cases where at least some challenge was made to an expert.

As shown in the chart, during the early 1980s, reliability was addressed in 80 percent of those cases containing an expert element, the same rate of frequency as in late 1999. And, where reliability was challenged, the expert was found unreliable in 60 percent of those cases;

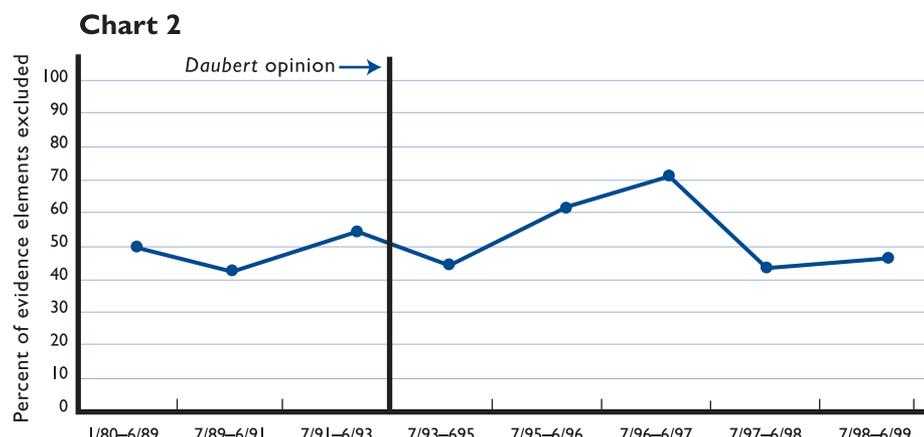
again, this was the same rate in the decade before and after *Daubert*. However, these rates did not remain constant during the twenty-year period considered in the study. Rather, challenges to and exclusions of experts went through a cycle and simply have reached a new equilibrium after nearly a decade of fluctuation.

Further, challenge and exclusion rates fell to all-time lows in the period just before *Daubert* (below 70 percent and 40 percent, respectively) and then rose to all-time highs a few years after *Daubert*, in 1997 (90 percent and 70 percent, respectively). Moreover, what the chart does not reflect—but the full RAND Study discusses—is that the total number of expert challenges increased significantly in the 1990s compared to the 1980s.⁵⁹

Thus, while cursory indications are that little has changed, the challenge and exclusion rates actually have varied wildly (swinging 20 percent to 30 percent), and the absolute number of experts challenged and exclusions based on reliability rose sharply after *Daubert*.⁶⁰ Chart 2 below looks solely at the frequency of partial or complete expert opinion exclusion within the survey population on the whole (as opposed to only those cases raising expert objections, as in Chart 1).



NOTE: Case type, substantive area of evidence, and appellate circuit are held constant



NOTE: Case type, substantive area of evidence, and appellate circuit are held constant

As with Chart 1, the “before and after” *Daubert* frequency of exclusion based on reliability is roughly the same, about 50 percent. Similarly, the low point in exclusions occurred a few years before *Daubert* (just over 40 percent) and the high point occurred in 1997 (70 percent). But as with Chart 1, what is not shown in Chart 2 is that the total number of challenges and exclusions grew significantly in the 1990s.

The last chart we consider is Chart 3 (below), which indicates the number of expert challenges at the summary judgment stage and the relative frequency of exclusion of at least some portion of the expert testimony.

Chart 3

Opinion Date	Summary Judgment Requested	Summary Judgment Granted
1/80–6/89	49	37
7/89–6/93	43	21
7/93–6/95	37	25
7/95–6/97	65	48
7/97–6/99	73	42

NOTE: Case type, substantive area of evidence, and appellate circuit are held constant

This chart serves as the capstone for the conclusions about the growing crisis of experts. Again, a cursory review of this data might suggest little change before and after *Daubert*. For example, examination of the rate of exclusion based on reliability at the summary judgment phase from 1980–1993 and comparison to the most recent period finds that both are approximately 60 percent.⁶¹

However, the more critical indication of change for the worst—and consistent with the previous discussion concerning the increase in total expert challenges observed in the RAND Study—is the increase in expert challenges occurring at the summary judgment phase. As shown, the total number of challenges by summary judgment in the final two years of the RAND Study is 50 percent greater than in the entire decade of the 1980s. This represents roughly an eight-fold increase in the actual frequency of challenges.

Thus, at least two important observations emerge from this scrutiny of available data: (1) experts are challenged (and excluded) in greater numbers since *Daubert*,⁶² and (2) challenges are made more frequently and more successfully much earlier in the cases. What is the road ahead? Will it be the path of least resistance characterized by a continuation of the expensive crap-shoot that is the battle of the experts? Or will it be the road less traveled and a true revolution in the selection, qualification, and use of experts—a revolution that effectively integrates the rules that relate to traditional party-experts with those for court-appointed experts, special masters, and court-appointed technical advisors?⁶³ Only time will tell.

Endnotes

1. There were approximately fifty decisions through 2000, twelve in 2001, and thirty-six in 2002 and the first-half of 2003. For cases through 2001, see Ratliff, *Daubert-proofing Your IP Experts: 2002 Update*, IP LITIGATOR 16–20 (Aug. 2002) and Ratliff, *Kumho Wrestling: Are Your IP Experts In Shape?* TRIAL LAWYER 457–70 (Summer 2000).

2. *Id.*

3. *Id.*

4. Other cases where opinions admitted:

Appellate Court Decisions—Texas Digital Systems, Inc. v. Telegenix, Inc., 308 F.3d 1193, 1219 (Fed. Cir. 2002) (in LED patent dispute, plaintiff’s damages expert was competent and qualified); Techsearch LLC v. Intel Corp., 286 F.3d 1360, 1378–79 (Fed. Cir. 2002) (use of a court appointed expert to explain micro-processing technology approved in patent dispute); Medforms, Inc. v. Healthcare Mgmt. Solutions, Inc., 290 F.3d 98, 110–11 (2d Cir. 2002) (in computer program copyright case, programmer’s opinions on meanings of terms in copyright registrations and significance of programmer to software development were relevant and reliable lay opinions based on personal knowledge); Avery Dennison Corp. v. Four Pillars Enter. Co., 2002 WL 2020041, *4–6 (6th Cir. 2002) (in adhesives formula trade secret/RICO dispute, fact witness technical opinions were relevant and reliable, and damage expert opinions not unreliable even if based on one view of disputed facts).

District Court Decisions—TVT Records v. Island Def Jam Music Group, 2003 WL 1094105, *5–7 (S.D.N.Y. 2003) (in music royalty dispute, CPA was qualified to testify on market performance of a music album); Beacon Mutual Ins. Co. v. OneBeacon Ins. Group, 2003 WL 1618116, *3–4 (D.R.I. 2003) (in trademark dispute relating to trade name OneBeacon, plaintiff’s survey expert qualified and survey reliable); Applera Corp. v. Micromass UK Ltd., 204 F. Supp. 2d 724, 770–71, 781 (D. Del. 2002) (in mass spectrometer patent case, technical expert’s computer simulation was comparable, and jury award was based on lost profits, not allegedly flawed royalty analysis); Orsak, LLC v. Gen. Instrument Corp., 2002 WL 172446, *9 (N.D. Ill. 2002) (in device patent dispute, technical expert scientifically qualified, validity opinions relevant and methods reliable); Sunny Fresh Foods, Inc. v. Michael Foods, Inc., 205 F. Supp. 2d 1077, 1083 n. 1 (D. Minn. 2002) (claim construction technical expert opinions reliable in “ultra-pasteurizing” liquid egg process patent dispute); Minnesota Specialty Crops, Inc. v. Minnesota Wild Hockey Club, 2002 WL 1763999, *2 (D. Minn. 2002) (in trademark case relating to name MINNESOTA WILD, objections to consumer survey sample, tone and content of the questions, and the method of tabulation went to weight, not reliability); Aktiebolag v. Andrx Pharmaceuticals, Inc., 222 F. Supp. 2d 423, 489–503 (S.D.N.Y. 2002) (in gastrointestinal drug patent dispute, defendants’ challenges went to weight not reliability of expert studies, models and experiments); ID Sec. Sys. Canada, Inc. v. Checkpoint Sys., Inc., 198 F. Supp. 2d 598, 619 (E.D. Pa. 2002) (in antitrust case where monopoly allegations based in part on electronic article surveillance tag patents, patent claim expert followed sufficiently rigorous methodology); Poly-Am., Inc. v. Serrot Int’l, Inc., 2002 WL 1996561, *13–14 (N.D. Tex. 2002) (in landfill liner patent dispute, technical expert’s opinions on invalidity and prior art not excluded based on alleged absence of personal knowledge).

5. *Micro Chemical, Inc. v. Lextron, Inc.*, 317 F.3d 1387 (Fed. Cir. 2003).

6. *Id.* at 1390.

7. *Id.* at 1392.

8. *Id.*

9. *Id.*

10. *Id.*

11. *Id.* at 1393.

12. *Id.* at 1394.

13. *Betterbox Communications Ltd. v. BB Techs., Inc.*, 300 F.3d 325 (3d Cir. 2002).

14. *Id.* at 326.
15. *Id.* at 327.
16. *Id.* at 328 (citation omitted).
17. *Id.* at 328–29.
18. *Id.* at 329.
19. *Id.*
20. *Id.* at 334–35.
21. *Id.* at 329.
22. *Smithkline Beecham Corp. v. Apotex Corp.*, 247 F.Supp. 2d 1011 (N.D. Ill. 2003).
23. *Id.* at 1042.
24. *Id.*
25. *Id.*
26. *Id.*
27. Other cases where opinions excluded:

Appellate Court Decisions—*John G. Danielson, Inc. v. Winchester-Conant Properties, Inc.*, 322 F.3d 26, 48 (1st Cir. 2003) (in condominium architectural site plan copyright infringement dispute, defendant’s marketing expert’s opinions not sufficiently supported).

District Court Decisions—*Pickholtz v. Rainbow Technologies, Inc.*, 260 F. Supp. 2d 980, 984 (N.D. Cal. 2003) (in computer security device patent dispute, plaintiff’s technical expert’s opinions not based upon sufficient facts or data); *Augustine Medical, Inc. v. Mallinckrodt, Inc.*, 2003 WL 1873836, *9 (D. Del. 2003) (in convective warming blanket patent and antitrust dispute, monopolization expert’s opinions not based on sufficient facts or data); *Greenwich Indus. v. Specialized Seating, Inc.*, 2003 WL 21148389, *5 (N.D. Ill. 2003) (in B-back chair trade dress dispute, plaintiff’s chair design engineer’s opinions not based on sufficient facts or data, and methods not accepted as reliable); *Dataquill Ltd. v. Handspring, Inc.*, 2003 WL 737785, *4 (N.D. Ill. 2003) (in data entry device patent dispute, technical expert’s opinions on infringement were unreliable); *Sears Roebuck and Co. v. Menard, Inc.*, 2003 WL 168642, *2–3 (N.D. Ill. 2003) (in trademark dispute concerning WHERE ELSE mark, survey flawed); *EZ Dock, Inc. v. Schafer Sys., Inc.*, 2003 WL 1610781, *3 (D. Minn. 2003) (in floating dock patent dispute, plaintiff’s damages expert’s profits opinions were unreliable); *Baker v. Urban Outfitters, Inc.*, 2003 WL 1733778, *5–7 (S.D.N.Y. 2003) (in photographic copyright infringement dispute, photographic pricing expert on damages held unqualified and opinions unreliable); *YKK Corp v. Jungwoo Zipper Co Ltd.*, case not reported but published at www.jurisnotes.com/Cases/YKK.htm (C.D. Cal. Aug. 9, 2002) (in trademark dispute relating to clothing zipper mark, actual confusion survey was unreliable due to selective respondent omissions); *Price v. Code-Alarm, Inc.*, 2002 WL 1870041, *5 (N.D. Ill. 2002) (in car alarm patent dispute, plaintiff’s engineer-damages expert’s opinions excluded as bare conclusions without any analysis); *Albert v. Warner-Lambert Co.*, 234 F. Supp. 2d 101, 105–07 (D. Mass. 2002) (in fraud and misrepresentation dispute for failing to license patented denture cup; plaintiff’s survey in support damages where no history of profits was unreliable “junk science”); *Carroll Shelby Licensing, Inc v. Superformance Int’l, Inc.*, case not reported but published at www.jurisnotes.com/cases/shelby.htm (D.Mass. Aug. 21, 2002) (survey responses unreliable due to combining of responses); *J & J Snack Foods, Corp. v. Earthgrains Co.*, 220 F. Supp. 2d 358, 371–72 (D.N.J. 2002) (in trademark dispute concerning “Break & Bake” mark, survey evidence proffered by plaintiff’s marketing expert and linguist involved incorrect definitions and sample population); *Aktiebolag v. Andrx Pharms., Inc.* (In re Omeprazole Patent Litig.), 2002 WL 193153, *6–7 (S.D.N.Y. 2002) (in gastrointestinal drug patent dispute, science expert’s opinions unreliable or merely legal argument); *LinkCo v. Fujitsu, Ltd.*, 2002 WL 1585551, *1–4 (S.D.N.Y. 2002) (in computer software trade secret case, parties’ CPA and patent lawyer, respectively, damages experts excluded due to analytical gap between bases and opinions; plaintiff’s technical expert’s opinions were cursory, conclusory and did not assist the trier-of-fact); *Nat’l Distillers Products LLC v. Refreshment Brands Inc.*, case not reported but published at www.legaldockets.com/NationalvRefreshment.html (S.D.N.Y. Apr. 15, 2002) (in trademark dispute relating to vodka mark; survey unreliable

as respondents were not the target market for the product); *Elder v. Tanner*, 205 F.R.D. 190, 194 (E.D. Tex. 2001) (in green wood process patent case, plaintiff’s technical experts were qualified and bases for opinions were disclosed, but did not assist the trier-of-fact due to analytical gaps between bases and opinions); *Advanced Display Sys., Inc. v. Kent State Univ.*, 2002 WL 1489555, *7 (N.D. Tex. 2002) (in LCD patent dispute, patentor’s royalty damages expert’s opinions based on 20-20 hindsight, not sufficient facts or data).

28. *Alcatel USA, Inc. v. Cisco Systems, Inc.*, 2002 WL 31950110 (E.D. Tex. 2002).

29. *Id.* at *3.
30. *Id.*
31. *Id.* at *2.
32. *Id.* at *3.
33. *Id.*
34. *Id.*
35. *Id.*
36. *Id.* at *4.
37. *Id.* at *6 (citations omitted).
38. *Id.* at *7.
39. *Id.*
40. *Id.* (citations omitted).
41. *Id.* at *6 (citations omitted).
42. *Id.* at *8–9.
43. *Id.* at *10 (quoting *Transclean Corp. v. Bridgewood Services, Inc.*, 290 F.3d 1364, 1376 (Fed. Cir. 2002)).
44. 201 F. Supp. 2d 335 (D.N.J. 2002).
45. *Id.* at 377
46. *Id.*
47. *Id.* at 377–78.
48. *Id.* (citations omitted).
49. *Arquest, Inc. v. Tracy*, 2002 WL 31744658, *3–4 (N.D. Ill. 2002).
50. *Id.* at *3.
51. *Id.* at *4.
52. *Id.*
53. Katerina M. Eftimoff, RAND Study, *The Decade after Daubert Proves Tough on Expert Witnesses*, LITIGATION NEWS (ABA Section of Litigation) (July 2002) at 1; see also RAND Institute for Civil Injustice, *Research Brief: Changes in the Standards for Admitting Expert Evidence* (2002) at <http://rand.org/publications/RB/RB9037/>.
54. *Id.*
55. *Id.*
56. *Id.*
57. *Id.*
58. RAND Institute for Civil Injustice, *Research Brief: Changes in the Standards for Admitting Expert Evidence* (2002) at <http://rand.org/publications/RB/RB9037/>.
59. <http://rand.org/publications/MR/MR1439/>.
60. *Id.*

61. We note this rate is higher than the roughly 50 percent exclusion rate for the entire population of reliability challenges.

62. This observation is consistent with the trend suggested by the 2000 FJC Study.

63. See, e.g., Federal Rules of Evidence, Rule 706; Federal Rules of Civil Procedure, Rule 56; Robert L. Hess, II, *Judges Cooperating with Scientists: A Proposal for More Effective Limits on the Federal Trial Judge’s Inherent Power to Appoint Technical Advisors*, 54 VAND. L. REV. 547 (2001); Natasha Campbell & Anthony Vale, *Encouraging More Effective Use of Court-appointed Experts and Technical Advisors*, DEFENSE COUNSEL J. 196, 207 (Apr. 2000); Thomas M. Crowley, *Help Me Mr. Wizard! Can We Really Have “Neutral” Rule 706 Experts?*, 1998 DET. C.L. REV. 927, 948 (Winter 1998); Joe S. Cecil and Thomas E. Willging, *The Randolph W. Thrower Symposium: Scientific & Technological Evidence: Accepting Daubert’s Invitation: Defining a Role for Court-Appointed Experts in Assessing Scientific Validity*, 43 EMORY L. J. 995 (1994).

Recent Developments in Intellectual Property Law

BY JOHN C. GATZ, REPORTER



John C. Gatz

Patents

Claim Construction

Waner v. Ford Motor Co., 66 U.S.P.Q.2d 1943 (Fed. Cir. 2003). In this case, the construction of the term “flange” in a claim directed to a fender liner for dual rear wheel tracks was disputed between the parties. The term flange was not specifically defined in the intrinsic record. The dictionary definition of the term flange is a raised or projected edge. The figures of the patent illustrate a raised or projected edge, and there is nothing in the patent specification to indicate that the flange is coplanar with the flat panel. Additionally, the claim language itself makes clear that the flange must exist prior to installation. Nothing in the specification or the drawings suggests that the flange does not exist prior to installation. Because the accused infringer’s (Ford’s) fender liner is a single, planar sheet prior to installation, it does not have the side flange as claimed in the patent. The award of attorney fees to the patentee Waner was reversed by the Federal Circuit. The Federal Circuit affirmed the district court’s grant of partial summary judgment in favor of Ford on Waner’s unjust enrichment claim.

Brookhill-Wilk 1 LLC v. Intuitive Surgical Inc., 67 U.S.P.Q.2d 1132 (Fed. Cir. 2003). The decision between these parties reported at 66 U.S.P.Q.2d 1132 was withdrawn and replaced by this decision that clarified the claim construction. The parties disagreed over the construction of the phrase “remote location beyond a range of direct manual contact.” The Federal Circuit stated that while certain terms may be at the center of the claim construction debate, the context of the surrounding words of the claim must be considered in determining the ordinary and customary meaning of those terms. The accused infringer Intuitive Surgical Inc. construed the term “remote location” to mean a location outside the operating room. The patentee Brookhill-Wilk 1 LLC argued that the term “remote location” encompassed any location of the surgeon that is beyond an arm’s length from the patient.

John Gatz is a member of the firm of Jenkins & Gilchrist in Chicago. Contributors to this department include: Patents—Julio Garceran, Lucent Technologies, Inc.; and John C. Gatz and Cynthia K. Thompson, Jenkins & Gilchrist, Chicago; Copyrights—Zachary Smolinski and Timothy Kowalski, Jenkins & Gilchrist, Chicago; and Gary A. Pierson II, Pattishall, McAuliffe, Newbury, Hilliard and Geraldson; Trademarks—Timothy M. Kenny, Michael A. Collyard, and Elizabeth B. Stinson, Fulbright & Jaworski LLP, Minneapolis; and Alicia Morris Groos, Susan J. Hightower, and Martin Hernandez, Fulbright & Jaworski LLP, Austin; and Kenneth D. Suzan.

The written description of the patent does not include specific distances between the surgeon and patient, but teaches generally that a surgeon using the disclosed assembly may operate without directly touching the patient, the surgical instruments, or the endoscope. The objects of the invention include reducing surgical costs, and facilitating the performance of operations by surgeons from all over the world. The accused infringer argued that the Objects of the Invention section limited the disputed claim phrase. The Federal Circuit, however, stated that the patent does not disavow using the invention within an operating room, and does not specify that the invention is useful only where the surgeon is located at a great distance from the operating room. The prosecution history was irrelevant to the construction of the disputed phrase. The Federal Circuit construed the term “remote location” to encompass locations that are far apart or distant, and those locations that are “separated by intervals greater than usual.” These locations do not need to be outside the operating room. Because the district court’s construction of “remote location” was erroneous and the grant of summary judgment in favor of the accused infringer was based on this claim construction, the Federal Circuit reversed the judgment and remanded the case to the district court for further proceedings consistent with the opinion.

Omega Eng’g Inc. v. Raytek Corp., 67 U.S.P.Q.2d 1321 (Fed. Cir. 2003). In 35 U.S.C. §112, ¶ 6, a patentee is allowed to recite a function to be performed as a claim limitation rather than reciting structure or materials for performing that function. The construction of a means-plus-function limitation follows a two-step approach. First, the court must identify the claimed functions, staying true to the claim language and the limitations expressly recited by the claims. Once the functions performed by the claimed means are identified, the court must then ascertain the corresponding structures in the written description that perform those functions.

The parties disagree on the proper function performed by the means for causing “at least one laser beam to strike the periphery of the energy zone for visibly outlining said energy zone.” The district court construed the function of the phrase “strike the periphery . . . for visibly outlining” as encompassing “the projection of the laser light toward the surface, but does not encompass light striking the center or interior portions of the energy zone.” When construing the functional statement in a means-plus-function limitation, the court must take great care not to impermissibly limit the function by adopting a function different from that explicitly recited in the claim. The district court’s ruling incorporated into the

claim language a novel negative limitation, precluding the laser beam affected by the “means for causing” from striking the center or the interior of the energy zone. This additional negative limitation is not supported in the explicit claim language. The claims do not prohibit the laser beam from striking inside the energy zone. Beyond the words of the claim, the district court did not identify any express disclaimer or independent lexicography in the written description that would justify adding the negative limitation. The Federal Circuit indulges a heavy presumption that claim terms carry their full ordinary and customary meaning unless the patentee unequivocally imparted a novel meaning to those terms or expressly relinquished claim scope during prosecution. Despite the alleged disclaimer of the use of a central laser beam during prosecution, the Federal Circuit has declined to apply the doctrine of prosecution disclaimer where the alleged disavowal of claim scope is ambiguous.

Abbott Labs. v. Syntron Bioresearch Inc., 67 U.S.P.Q.2d 1337 (Fed. Cir. 2003). The plain meaning of “non-diffusively bound” and “non-diffusively immobilized” is a chemical or physical combination of the reagent and the medium such that the reagent does not dissolve and move within the liquid from a region of high concentration to a region of low concentration. None of the pertinent dictionary definitions supports the portion of the jury instruction defining a reagent as non-diffusively bound “only if it is found in such a manner that a sufficient and reproducible amount of reactant remains bound in the reactive zone or zones to conduct both quantitative and qualitative assays.” The plain meaning of the claim recitation, therefore, does not support the district court’s narrow claim construction. The usage of the disputed claim terms in the context of the claims as a whole also does not support the district court’s construction. Thus, the construction adopted by the district court and used to instruct the jury was erroneous because it required a sufficient amount to conduct quantitative assays.

Claim Construction and Infringement

Tehrani v. Hamilton Med. Inc., 67 U.S.P.Q.2d 1015 (Fed. Cir. 2003). The Federal Circuit vacated and remanded the district court’s decision of infringement on summary judgment. The Federal Circuit first considered the claim construction by the district court. In doing so, the Federal Circuit found that the claims directed to an apparatus and method for automatically controlling a respirator for mechanical ventilation required the processing of five data values and use of those data values to calculate tidal volume and breath frequency. The Federal Circuit stated that when a term has multiple dictionary definitions, the intrinsic record must be consulted to identify which meaning is the most consistent with the use of the term by the inventor. The Federal Circuit held that the limitation of “measuring levels” did not require that the levels be measured automatically. “Automatically” was not included in the claim limitation and also was not required by the preamble of the claim. In determining infringement, the Federal Circuit vacated the district court’s findings that the accused infringer’s device nec-

essarily performed the claim limitations. Although there was an association between the function of the infringer’s device and the various claim limitations, the evidence fell short of establishing that these functions met the claim limitations.

Implied License/Preliminary Injunction

Anton/Bauer Inc. v. PAG Ltd., 66 U.S.P.Q.2d 1675 (Fed. Cir. 2003). The asserted claim is directed to a battery pack connection that includes a female plate, a male plate, and releasable locking means. No claim in the Anton/Bauer Inc. patent separately covers the male plate or the female plate. The patentee sells both female plates and battery packs containing male plates. The patentee always sells these as separate products. The female plates can be used with other items, such as video cameras made by other manufacturers. The patentee sells female plates directly to end-users as an after-market product. The accused infringer PAG Ltd. sells a battery pack that can be combined with Anton/Bauer’s female plates. PAG, however, does not make, use, or sell any female plate in the U.S. with a “releasable locking means on said female plate” as required in the patent. The patentee argued that PAG Ltd. was inducing infringement and contributorily infringing its patent.

PAG argued that Anton/Bauer’s customers do not directly infringe the ‘204 patent because of the exhaustion doctrine that results in an implied license, which is a defense to patent infringement. The exhaustion doctrine is based on the proposition that “[t]he unrestricted sale of a patented article, by or with the authority of the patentee, ‘exhausts’ the patentee’s right to control further sale and use of that article by enforcing the patent under which it was first sold.” In other words, sale of an unpatented article exhausts the seller’s right to control the future sale and use of that article. A patentee grants an implied license to a purchaser when (a) the patentee sells an article that has no noninfringing uses, and (b) the circumstances of the sale plainly indicate that the grant of a license should be inferred. The sale of the unpatented female plate by Anton/Bauer is a complete transfer of the ownership of the plate. PAG and Anton/Bauer agree that there are no noninfringing uses of the female plate sold by Anton/Bauer. There is no evidence that Anton/Bauer places express restrictions on using the female plates it sells or that it requires that manufacturers to whom it sells female plates expressly restrict the grant of a license on the sale of the finished product that incorporates the plate. The district court erred in not applying the doctrine of implied license that resulted in an erroneous conclusion of a likelihood of success on the merits of infringement. Therefore, the district court abused its discretion in granting a preliminary injunction and the decision of the district court is reversed.

Inequitable Conduct

Bristol-Myers Squibb Co. v. Rhone-Poulenc Rorer Inc., 66 U.S.P.Q.2d 1481 (Fed. Cir. 2003). A patent application directed to taxol, a cancer chemotherapeutic

agent, was prepared by a French patent agent (Mr. Pilard). Before Mr. Pilard drafted the application, the inventors forwarded him their article (JACS article) directed to the same subject matter. Mr. Pilard drafted claims broader than that disclosed in the JACS article and sent the draft application to the inventors. The inventors made no changes and the application was filed on April 6, 1988. The JACS article was received for publication on April 20, 1988 and published in August 1988. Mr. Pilard sent disclosure information to the U.S. patent attorney (Mr. Mosher) for the U.S. counterpart application, but this information did not include the JACS article. The USPTO examiner assigned to the application asked the PTO Scientific Library to perform a computer search of chemical abstracts using the chemical structure of claim 1. The generated search report listed the JACS article as "Answer 1 of 11" and identified a publication year of 1988. The search report listed another article that was authored by two of the co-inventors that was published in 1987. The examiner listed the 1987 article on a "Notice of References Cited" (Form PTO-892). The examiner did not place his initials next to any of the other listed articles on the search report. The U.S. counterpart application issued as the '011 patent in 1990.

In 1991, Mr. Pilard requested another U.S. patent attorney (Mr. Calvetti) to file a reissue application. Mr. Pilard forwarded several documents, which he deemed "irrelevant," to Mr. Calvetti. One of these documents was the JACS article that was submitted in an IDS in the reissue application and subsequently reviewed by the examiner.

To find inequitable conduct, materiality and intent to mislead must be found by clear and convincing evidence. "Materiality is not limited to prior art but embraces *any* information that a reasonable examiner would be substantially likely to consider important in deciding whether to allow an application to issue as a patent." The Federal Circuit concluded that the district court's finding that the JACS article was material to the prosecution of the '011 patent is not clearly erroneous considering the examiner's obligation to review the application for enablement under 35 U.S.C. § 112. The Federal Circuit stated the JACS article would have raised doubts about producing taxol using specified hydroxy-protecting groups. A reasonable examiner would have wanted to know whether the unsuccessful use of the specified hydroxy-protecting groups discussed in the JACS article affected the ability of a person of ordinary skill in the art to practice the invention, which specifically taught using the same hydroxy-protecting groups, without undue experimentation.

The patentee unsuccessfully argued that: (a) the PTO examiner reviewed the JACS article in the search report—this was rejected because it was not listed or initialized on the Form PTO-892; (b) materiality is lacking because the PTO examiner considered the JACS article during the reissue and did not reject any claims based on it—although this is probative evidence, it does not end the materiality inquiry; (c) other evidence was determinative—this evidence was determined to be "self-serving" because materiality is determined from the

viewpoint of a reasonable patent examiner; and (d) inequitable conduct was contradictory to the district court's holding on enablement—this was also rejected by the Federal Circuit.

In finding intent, the Federal Circuit stated the following: (a) Mr. Pilard intentionally drafted the '011 patent more broadly than the disclosure; (b) he was aware of the JACS article at the time he drafted the patent application and at the time he provided Mr. Mosher materials for filing the application to the '011 patent; (c) he was aware of the PTO duty of disclosure; and (d) his attempted justifications for not disclosing the JACS article were insufficient grounds for not disclosing it to the PTO examiner. The Federal Circuit affirmed the district court's judgment concluding that the '011 and '277 patents were obtained by inequitable conduct and held these patents unenforceable.

Dayco Prods. Inc. v. Total Containment Inc., 66 U.S.P.Q.2d 1801 (Fed. Cir. 2003). To prove inequitable conduct in prosecuting a patent, the accused infringer must provide evidence of affirmative misrepresentations of a material fact, failure to disclose material information, or submission of false material information, coupled with an intent to deceive. Both intent and materiality are questions of fact that must be proven by clear and convincing evidence. The inequitable conduct analysis is performed in two steps. First, a determination is made as to whether the withheld reference meets a threshold level of materiality and intent to mislead. Second, a weighing is done of the materiality and intent in light of all the circumstances to determine whether the applicant's conduct is so culpable that the patent should be held unenforceable. A question exists as to the proper standard of materiality. For many years, materiality for the purposes of an inequitable conduct determination required a showing that a reasonable examiner would have considered such prior art important in deciding whether to allow the patent application. Information did not need to be prior art to be material but, instead, embraced any information that a reasonable examiner would substantially likely consider important in deciding whether to allow a patent application to issue. In 1992, however, the Patent Office amended its rules to provide a different standard for materiality. The new rule reiterated the preexisting duty of candor and good faith, but more narrowly defined materiality, providing for disclosure where the information establishes a *prima facie* case of unpatentability or refutes or is inconsistent with a position the applicant takes. Since 1992, the Federal Circuit has continued to apply the reasonable examiner standard, but only to cases that were prosecuted under the earlier version of Rule 56. The Federal Circuit has not decided whether it should adhere to the preexisting standard for inequitable conduct in prosecutions occurring after the effective date of the new rule. Thus, the Federal Circuit has not decided whether the standard for materiality in inequitable conduct cases is governed by equitable principles or by the Patent Office rules. Because the Federal Circuit concluded that the outcome of this appeal would be the same under either materiality standard, the Federal Circuit leaves the final disposition of that issue for another day.

In this case, the district court granted summary judgment of inequitable conduct relying on: (a) the pendency of a related application that was not disclosed to the examiner; (b) a prior art reference that was not disclosed to the examiner; and (c) the rejection of claims in the related application based on the prior art reference. The Federal Circuit found that, while the related patent application met the threshold level of materiality, the motion for summary judgment did not establish a threshold showing of intent to deceive. With regard to the prior art reference, the Federal Circuit concluded that applying either standard of materiality, it was improper for the district court to conclude that the prior art reference met the threshold level of materiality. The mere fact that the examiner found the prior art reference material is informative, but not dispositive. Whether the prior art reference meets the threshold level of materiality requires a detailed factual analysis of the relevance of the teachings of that reference both with respect to the claims of the patent in suit and with respect to the other prior art references that were before the examiner. On the issue of intent, the district court also erred in concluding that the mere fact that the prosecuting attorney knew of the prior art reference and decided not to submit it to the examiner established intent. Finally, the Federal Circuit addressed whether the rejection of a substantially similar claim in a copending application is material under the reasonable examiner standard. The Federal Circuit held that a contrary decision of another examiner reviewing a substantially similar claim meets the reasonable examiner threshold materiality test of any information that a reasonable examiner would substantially likely consider important in deciding whether to allow a patent application to issue. Moreover, a prior rejection of a substantially similar claim refutes, or is inconsistent with, the position that those claims are patentable. An adverse decision by another examiner, therefore, meets the materiality standard under the amended Rule 56. However, the district court did not address the issue of intent to deceive related to the failure to disclose the examiner's adverse decision. A trial on this issue was, therefore, found to be necessary.

Interferences

Eli Lilly & Co. v. Board of Regents, Univ. of Washington, 66 U.S.P.Q.2d 1161 (Fed. Cir. 2003). Eli Lilly & Co. (Lilly) filed a reissue application and requested an interference to be declared between its reissue application and a patent to the Board of Regents, University of Washington (UW). From the count, Lilly was the presumptive senior party because of an earlier effective filing date.

The Board in determining whether an interference should be declared turned to 37 C.F.R. § 1.601(i). An interference is declared when two parties are claiming the "same patentable invention." Section 1.601(n) defines the phrase "same patentable invention" as follows.

Invention 'A' is the same patentable invention as an invention "B" when invention 'A' is the same as (35 U.S.C. [§] 102) or is obvious (35 U.S.C. [§] 103) in view of invention

'B' assuming invention "B" is prior art with respect to invention 'A.' Invention 'A' is a separate patentable invention with respect to invention 'B' when invention 'A' is new (35 U.S.C. [§] 102) and non-obvious (35 U.S.C. [§] 103) in view of invention 'B' assuming invention "B" is prior art with respect to invention 'A.'

Lilly argued that the proper test for whether two claims have the same patentable invention is a "one-way" test —(a) the claimed invention of Party A is the same patentable invention as the claimed invention of Party B when the claimed invention of Party A anticipates or renders obvious the claimed invention of Party B, or (b) the claimed invention of Party B anticipates or renders obvious the claimed invention of Party A. The director applied a "two-way" test to determine whether two parties are claiming the "same patentable invention"—(a) the claimed invention of Party B (UW) must anticipate or render obvious the claimed invention of Party A (Lilly); and (b) the claimed invention of Party B (Lilly) must anticipate or render obvious the claimed invention of Party A (UW). The Federal Circuit stated because the two-way test is an interpretation of the director's own regulations, the director's interpretation of them is controlling unless "plainly erroneous or inconsistent with the regulation." The director may interpret the phrase "assuming invention B is the prior art with respect to invention A" to mean that both UW and Lilly may be the assumed "prior art" invention B because it is not conclusively known which of the two inventions is the prior art.

The Federal Circuit noted the two-way test applied by the director is underinclusive because it concludes that there is no interference-in-fact even if an interference proceeding would have led to the conclusion that the species was invented before the genus. The Federal Circuit also noted that the one-way test is overinclusive because it concludes that there is an interference-in-fact even if an interference proceeding would have led to the conclusion that the genus was invented before, and separately patentable from, the species. Because both of these are reasonable interpretations of 37 C.F.R. § 1.601(n), the Federal Circuit held that the director's two-way test is not "plainly erroneous or inconsistent with the regulation." The Federal Circuit also stated that there was no need to definitively construe the count because neither proposed claim construction leads to an interference-in-fact.

Inventorship and Unenforceability

Board of Educ. ex rel. Board of Trustees of Florida State Univ. v. American Bioscience Inc., 67 U.S.P.Q.2d 1252 (Fed. Cir. 2003). The Federal Circuit reversed the district court's findings on infringement and unenforceability due to inequitable conduct. The patentee appealed the decision of the court that removed three of the inventors and found the patent unenforceable for inequitable conduct. The Federal Circuit stated that an issued patent creates a presumption that the named inventors are the true and only inventors and, therefore, the burden of showing misjoinder or nonjoinder of inventors is a heavy one. Because there

was no evidence of record that the idea of the patent came from anyone but the co-inventors, the accused infringers did not meet their burden of proving misjoinder. The Federal Circuit stated that “invention does require conception, and there is no evidence that FSU’s [the alleged infringer] inventors conceived of any of the claimed compounds.” The mere fact that the inventors may have had in mind portions of the claimed compound is not the same as conceiving the entire claimed compound.

As to inequitable conduct, the Federal Circuit stated that the determination of inequitable conduct requires the district court to determine whether the conduct met a threshold level of materiality, and that the evidence shows a threshold level of intent to mislead the PTO. The trial court based its findings of inequitable conduct on the misjoinder of the inventors. Because the FSU scientists were not inventors, there can be no inequitable conduct. The patentee was not under any duty to disclose the previous employment of one of the inventors, as the examiner does not normally engage in determining the contributions of individual inventors.

Prosecution History Estoppel

Abbott Labs. v. Baxter Pharmaceutical Prods. Inc., 66 U.S.P.Q.2d 1191 (Fed. Cir. 2003). Abbott Laboratories and Central Glass Company, Ltd. (collectively, Abbott) own a patent directed to storing and using sevoflurane. The patent claims recite “a Lewis acid inhibitor in an amount effective to prevent degradation by a Lewis acid of said quantity of sevoflurane.” The Federal Circuit noted that the term “effective amount” has a customary usage. The patent explained many different factors interact to determine an “effective amount.” Abbott filed an IDS that listed a reference indicating that at least one year before the filing date of the patent, it sold sevoflurane in glass bottles with a water content up to 131 ppm. Baxter Pharmaceutical Products, Inc. and Baxter Healthcare Corporation (Baxter) thus asserted that its generic sevoflurane with a water content of no more than 130 ppm fell within the prior art and did not infringe the patent. The Federal Circuit stated that Abbott’s IDS disclosure to the PTO did not disavow or relinquish all water concentrations below 131 ppm in other conditions. Thus, the district court incorrectly limited the term an “effective amount” of water to more than 131 ppm.

Asserted claims 1 and 6 of the patent recite a list of Lewis acid inhibitors presented in the form of a Markush group. Abbott argued that the phrase “a Lewis acid inhibitor” in claims 1 and 6 means that “more than one inhibitor would still fall within the claim boundaries.” The Federal Circuit disagreed because the claims do not clearly embrace more than one member of the Markush group. The Federal Circuit noted that in an Interview Summary, the examiner stated that he reached agreement with applicants “to narrow the claims to include a specific inhalant anesthetic and specific Lewis acid inhibitors in order to avoid 112 issues,” which was also included in the examiner’s reasons for allowance. Thus, the Federal Circuit indicated that Abbott was limited to the six listed members of these Markush groups.

Because the district court’s construction is flawed, the Federal Circuit remanded for further consideration of literal infringement in view of the amended claim construction. To prove literal infringement, Abbott must show a species selected from the members of the Markush group is present in Baxter’s sevoflurane composition in an amount effective to function as a Lewis acid inhibitor.

Pioneer Magnetics Inc. v. Micro Linear Corp., 66 U.S.P.Q.2d 1859 (Fed. Cir. 2003). To determine whether a claim amendment gives rise to prosecution history estoppel, the court must first determine whether the amendment narrowed the scope of the claims. Then, the court examines the reason why the applicant amended the claim. Where no explanation is established, a court should presume that the applicant had a substantial reason related to patentability for the amendment. In this case, the patentee contends that a “switching” limitation was added through mere inadvertence, unmotivated by the statutory requirements for a patent. In support of this position, the patentee relied in part on a declaration of the prosecuting attorney that the narrowing amendment was added inadvertently. The Federal Circuit did not consider the prosecuting attorney declaration in determining the reason for the amendment. Only the public record of the patent prosecution, the prosecution history, can be the basis for such a reason. Otherwise, the public notice function of the patent record would be undermined.

Having concluded that the district court properly determined that there had been a narrowing amendment for a substantial reason related to patentability, the Federal Circuit turned to the question of whether the patentee can overcome the presumption that it surrendered the equivalent in question. The presumption can be overcome if the equivalent was unforeseeable at the time of the application; the rationale underlying the amendment bears no more than a tangential relation to the equivalent in question; or there was some other reason suggesting that the patentee could not reasonably be expected to have described the insubstantial substitute in question. In this case, the prior art reference disclosed a nonswitching circuit. Therefore, a nonswitching circuit was foreseeable at the time of the amendment. The amendment was clearly not tangential to the equivalent in question because the amendment was made to avoid the very prior art that contained the equivalent. Finally, given the equivalent’s presence in the prior art against the patentee during prosecution, there can be no other reason the patentee could not have described the substitute in question. Thus, the patentee is estopped from arguing that the “nonswitching” circuit is equivalent to the switching circuit in the patent claims.

Res Judicata

Media Tech. Licensing LLC v. Upper Deck Co., 67 U.S.P.Q.2d 1374 (Fed. Cir. 2003). To be given preclusive effect, a judgment must be a final adjudication of the rights of the parties and must dispose of the litigation on the merits. Because this case turns on general principles of claim preclusion, not on any law having special appli-

cation to patent cases, the Federal Circuit applied the law of the regional circuit in which the district court sits—the Ninth Circuit. The Ninth Circuit recognizes that standing is a threshold question that must be resolved before proceeding to the merits of the case. Article II standing, like other bases of jurisdiction, must be present at the inception of the lawsuit. Because standing is jurisdictional, lack of standing precludes a ruling on the merits. Thus, the district court erred in giving preclusive effect to the judgment because its dismissal of the complaint for lack of standing was not a final adjudication on the merits.

Safe Harbor of U.S.C. § 271(e)(1)

Integra LifeSciences I Ltd. v. Merck KGaA, 66 U.S.P.Q.2d 1865 (Fed. Cir. 2003). Integra LifeSciences I Ltd. (Integra) owns several patents. Merck KGaA (Merck) and the Scripps Research Institute (Scripps) performed experiments that Integra believed was a commercial project that infringed its patents. Merck argued that its experiments fell within the safe harbor of U.S.C. § 271(e)(1) of 1984. Specifically, Section 271(e)(1) sought to ensure that a patentee's rights did not de facto extend past the expired patent term because a generic competitor could not enter the market without regulatory approval. Thus, the 1984 Act permitted those competitors to conduct experiments in advance of the patent expiration if those activities were reasonably related to securing regulatory approval.

The issue in this case was whether pre-clinical research conducted under the Scripps-Merck agreement is exempt from liability for infringement of Integra's patents under Section 271(e)(1). Here, the Scripps-Merck experiments did not supply information for submission to the United States Food and Drug Administration (FDA), but instead identified the best drug candidate for future clinical testing under the FDA processes. Merck is not liable for patent infringement if its uses of the Integra inventions fall within Section 271(e)(1). To qualify for exemption, Merck must show its activities were "solely for uses reasonably related to the development and submission of information" to the FDA. Thus, Section 271(e)(1) does not globally embrace all experimental activity that at some point, however attenuated, may lead to an FDA approval process. The Federal Circuit held that Section 271(e)(1) did not include embracing development and identification of new drugs that will, in turn, be subject to FDA approval.

The Federal Circuit also included a lengthy discussion of a hypothetical license that should be taken into account by the district court in considering the damages awarded. Judge Newman, in her dissent, argued that both the common law research exemption and the safe harbor under Section 271(e)(1) applied to the Merck-Scripps "discovery-based research."

Sanctions

Waymark Corp. v. Porta Systems Corp., 67 U.S.P.Q.2d 1303 (Fed. Cir. 2003). The Federal Circuit reversed the district court's award of attorney fees in this trademark and patent infringement case. The district court awarded sanctions under 35 U.S.C. § 285, 15

U.S.C. § 117(a), and 28 U.S.C. § 1927. Applying Federal Circuit law for Section 285 and Eleventh Circuit law for Sections 117(a) and 1927, the Federal Circuit found that sanctions were not warranted. In awarding the fees, the district court relied on three bases: (a) when the plaintiffs instituted the action for trademark infringement, they did not have a federally registered trademark; (b) there was no written exclusive license from the patentee to the plaintiff; and (c) the plaintiff's alleged misleading responses to the alleged infringer's document request. For the first basis, the Federal Circuit found that because the plaintiff sought relief under the Lanham Act, it was not necessary that the trademark be registered. There was no showing that the claimed use of the unregistered mark could not form the basis for a Lanham Act claim. For the second basis, the Federal Circuit held that because only assignments need be in writing and exclusive licenses could be oral, this was not a proper basis for sanctions. Finally, because a written exclusive license did not exist, it cannot be sanctionable for the plaintiff to not produce it.

COPYRIGHTS

Accrued Cause of Action Is Assignable

Silvers v. Sony Pictures Entertainment, Inc., 330 F.3d 1204 (9th Cir. 2003). Plaintiff Silvers authored a script for a movie about the relationship between a mother who discovers that she has cancer and her ex-husband's new wife. Silvers completed the script as a work-made-for-hire for a film company that converted the script in to a made-for-TV movie called "The Other Woman," which aired on CBS in 1995. This film company owned the copyright to the TV movie. In 1998, Sony Pictures released the motion picture "Stepmom" having a similar story line.

After the release of "Stepmom," the film company that owned the copyright in "The Other Woman" executed an Assignment of Claims and Causes of Action assigning to Silvers "all right, title and interest in and to any claims and causes of action against Sony Pictures . . . with respect to the screenplay 'The Other Woman' . . . and the motion picture 'Stepmom'." Subsequently, Silvers sued Sony Pictures for copyright infringement alleging that Stepmom was substantially similar to the script that she had written for the TV movie "The Other Woman."

Sony Pictures sought dismissal of the suit claiming that Silvers lacked standing to bring the copyright infringement suit. The district court denied Sony Picture's motion to dismiss, and the Ninth Circuit affirmed holding that accrued causes of action for copyright infringement may be assigned.

Aimster Injunction Affirmed

In re Aimster Copyright Litigation, 334 F.3d 643 (7th Cir. 2003). Appellant John Deep is the owner of Aimster (now Madster), an Internet service that allows file-swapping among members. Aimster users primarily used the

service to swap copyrighted music files, and Aimster provided computerized tutorials showing how to swap files, using copyrighted music files as examples. Deep was sued as a contributory and vicarious infringer of copyrights by numerous plaintiffs owning popular music copyrights.

The U.S. District Court for the Northern District of Illinois entered a preliminary injunction against Aimster that effectively shut the service down. Deep appealed the injunction, arguing among other things that Aimster did not have control over its users' file-swapping activities, but merely enabled the swapping. Because Aimster had noninfringing uses, Deep argued, an injunction against Aimster due to the infringing uses of its members was misplaced. Deep also argued that an encryption feature of Aimster prevented the service from knowing what its members were swapping.

In an opinion discussing the Supreme Court's analysis of videotaping devices in *Sony Corp of America, Inc. v. Universal City Studios, Inc.*, 464 U.S. 417 (1984), the U.S. Court of Appeals for the Seventh Circuit rejected Aimster's arguments and upheld the injunction, noting that Aimster never produced any evidence that its service was ever used for a noninfringing purpose. The court commented that Aimster's "ostrich-like" refusal to discover the extent of infringing use (i.e., the encryption system) was additional evidence of contributory infringement. Discussing the balance of harm resulting from the injunction, the court determined that the irreparable harm to Aimster from the injunction was either less than or comparable to the harm to the copyright owners due to continued use of Aimster, and the injunction was proper because the plaintiffs have a stronger case on the merits.

Internet Search Engine's Use of Thumbnail Photos Is Fair Use

Kelly v. Arriba Soft Corp., 336 F.3d 811 (9th Cir. 2003). Leslie Kelly is a professional photographer holding copyrights on his photographs of the American West. Arriba Soft operates an Internet search engine that uses small versions of images—"thumbnails"—in its display of search results. Users of Arriba's engine can click on the thumbnails to view larger versions of the images. Kelly sued Arriba for copyright infringement when he discovered his images were being used in the search engine database. The U.S. District Court for the Central District of California determined that Arriba's reproduction and display of Kelly's photographs was *prima facie* copyright infringement, but also determined that Arriba's treatment of the photographs—in both thumbnail and larger forms—was fair use under Section 107 of the Copyright Act. Kelly appealed the decision.

Addressing the fair use factors in the copyright statute, the U.S. Court of Appeals for the Ninth Circuit first determined that Arriba's thumbnails fulfilled the transformative use of "improving access to information on the Internet" versus the "artistic expression" use of the original works. The court said Arriba's use did not supersede Kelly's use, but that Arriba had created a different purpose for the images. The court also deter-

mined that: (a) the "nature of the copyrighted work" factor weighed slightly in favor of Kelly; (b) the "amount and substantiality of the portion used" did not favor either party; and (c) Arriba's thumbnail use of Kelly's full-size images would not harm the market value of Kelly's full-size images.

The Ninth Circuit determined that Arriba's use of thumbnail images was fair use, but found that the district court should not have determined whether the display of larger pictures was fair use and reversed and remanded the district court's full-size image decision. The Ninth Circuit found that the district court improperly expanded both parties' pleadings to reach the question of infringement due to the larger images.

No Restoration of U.S. Copyright under the URAA Where Work Is in the Public Domain in Source Country

Alameda Films SA De CV v. Authors Rights Restoration Corp., 331 F.3d 472 (5th Cir. 2003). Several Mexican film companies sued American film distributors for copyright infringement alleging that the 1994 Uruguay Roundtable Agreement Act (URAA) restored U.S. copyright in vintage Mexican films. The U.S. copyrights in these films were lost due to the foreign authors' failures to comply with U.S. copyright formalities. According to the plaintiff film companies, however, the U.S. copyrights in many of these films were restored when the U.S. adopted the URAA, which eliminated many burdensome formalities previously required for copyrighting foreign works in the U.S. The URAA also provided for the automatic restoration of copyrights in various foreign works that had fallen into the public domain in the U.S. as a result of the foreign authors' failure to follow these formalities. With respect to seven of the films, however, the American film distributors defended on the ground that these films had fallen into the public domain in Mexico and, thus, the U.S. copyrights could not be restored under the URAA.

The Fifth Circuit sided with the film distributors with respect to the seven films. A U.S. copyright under the URAA can be restored if the work is not in the public domain in the source country. In this case, the seven Mexican films at issue were created prior to the effective date of the Mexican statute that eliminated the registration requirement for copyrights protection. These films were never registered in Mexico and, thus, these films fell into the public domain and were not protected by Mexican copyright law.

Rapper's Beats Beat Copyright Rap

Abilene Music, Inc. v. Sony Music Entertainment, Inc., 2003 WL 21415311, 67 U.S.P.Q.2d 1356 (S.D.N.Y. 2003). Abilene Music sued Sony recording artist Dennis Coles (better known as Ghostface Killah) for incorporating into his song "The Forest" a rendition of "What a Wonderful World," to which Abilene holds the copyright. Sony conceded that Abilene established a *prima facie* case of copyright infringement, and the only remaining issue was whether Coles's use of the verse

was a fair use. The U.S. District Court for the Southern District of New York granted Sony's motion for summary judgment and determined Coles's use was fair use under copyright law.

"What a Wonderful World," popularized in a version by Louis Armstrong, portrays the natural world as a utopian wonderland. Coles's "The Forest" uses descriptions of popular cartoon characters engaged in lewd acts to mock the positive view of "Wonderful World." The court determined "The Forest" is a fair use parody of "Wonderful World," relying on the Supreme Court's opinion in the similar case of *Campbell v. Acuff-Rose Music*, 510 U.S. 569 (1994). The contrast between "Wonderful World's" positive, optimistic feel and the drugged-up, seedy nature of "The Forest" led the court to determine that "The Forest" parodies "Wonderful World." The court dismissed Abilene's argument that "The Forest" did not use enough of the original work to be a parody and said that requiring parodists to use a certain amount of an original work would be paradoxical. The court found that "The Forest" used no more of the original work than was necessary to parody it. Addressing the effect of "The Forest" on the market for the original work, the court determined that "The Forest" would have no negative effect on any nonparody version of the original—including a hypothetical nonparody rap version of "Wonderful World."

Redneck Beer Determination Fact-Based

Atkins v. Fischer, 331 F.3d 988 (D.C. Cir 2003). Defendant Fischer conceived of a beverage product called "Redneck Beer." Fischer hired plaintiff Atkins—a provider of services aimed at providing brand identities—to create potential packaging designs for his Redneck Beer product. Fischer and Atkins entered into a two-stage agreement wherein Atkins would first produce a color painting of a Redneck Beer bottle and a Redneck Beer six-pack carrier, and would later finalize the Redneck Beer logo and produce camera-ready art. At the same time, the parties entered into a second agreement whereby Atkins would retain position of "all underlying creative work." Atkins created a design featuring a red bandana at the bottle's neck and a body label of a blue jeans pocket with a red bandana hanging from the pocket. After completion of the first stage, Fischer paid Atkins for the work. The second stage of the agreement was never reached because Fischer claimed he was unhappy with Atkins's work.

Fischer later entered into a manufacturing services agreement with a brewing company for the manufacture and marketing of Redneck Beer. By this time, Fischer had engaged the services of other marketing firms to produce a design for the Redneck Beer bottle and six-pack carrier. Eventually, Fischer began selling Redneck beer in six pack carriers featuring a design of a blue jeans pocket and a red bandana. Atkins then filed suit against Fischer for copyright infringement, and Fischer defended on the ground of an implied license.

An implied copyright license arises where: (1) a person (the licensee) requests the creation of a work; (2) the creator (the licensor) makes the particular work and

delivers it to the licensee who requested it; and (3) the licensor intends that the licensee-requestor copy and distribute the work. There was no dispute as to the first two elements. Regarding the third element, Atkins claimed that her design was to be used only as a sales tool at a convention, but that Fischer's acts in marketing Redneck Beer thereafter exceeded the scope of any implied license. The D.C. Circuit concluded that the question of the parties' intent was a fact question that should have precluded the district court's grant of summary judgment.

TRADEMARKS

Anticybersquatting Consumer Protection Act

Hawes v. Network Solutions, Inc. and L'Oreal, S.A., 67 U.S.P.Q.2d 1277 (4th Cir. 2003). This case involves a domain name dispute between an individual who registered the domain name *lorealcomplaints.com*, the French owner of the trademark L'OREAL, and the domain name registrar that transferred the disputed domain name.

In April 1999, Christopher Hawes (Hawes) registered the domain name *lorealcomplaints.com* with Network Solutions, Inc. (NSI) for the stated purpose of developing a forum in which to communicate with L'Oreal S.A. (L'Oreal) concerning problems with its products. A year later, L'Oreal filed trademark infringement litigation in a French court and obtained an order in its favor transferring the *lorealcomplaints.com* domain name to L'Oreal after Hawes failed to appear before the French court. Before the French court issued its order, and pursuant to NSI's Domain Name Registration Agreement, NSI tendered the domain name to counsel for L'Oreal for deposit with the French court.

In April 2001, Hawes filed the instant action with the U.S. District Court for the Eastern District of Virginia alleging two counts—one count against NSI under the Anticybersquatting Consumer Protection Act (ACPA) for breaching its Domain Name Registration Agreement by transferring *lorealcomplaints.com* to the French court, and one count against L'Oreal under the ACPA seeking transfer of the domain name back to Hawes and a declaratory judgment that Hawes' registration and use of the domain name was not unlawful. The district court dismissed the counts against both NSI and L'Oreal for a lack of subject matter jurisdiction and based on Hawes' failure to state a claim upon which relief may be granted.

Although Hawes's counsel designated both counts as arising under a nonexistent section of the Lanham Act—"§1114(II)"—the Fourth Circuit affirmed the district court's interpretation of Hawes' claim against NSI as arising under 15 U.S.C. § 1114(2)(D)(i)(II)(bb) (containing one of the few exceptions to the limitations of liability provided to domain name registrars under the ACPA) and the claim against L'Oreal as arising under 15 U.S.C. § 1114(2)(D)(v) (allowing a domain name registrant whose domain name has been transferred to bring a federal action seeking a declaration that the domain name registrant's ownership of the disputed domain name was "not unlawful").

The Fourth Circuit reversed the district court's dismissal of both claims for lack of subject matter jurisdiction, stating that federal question jurisdiction was properly founded upon the Lanham Act. Nevertheless, the Fourth Circuit dismissed the count against NSI for failure to state a claim upon which relief may be granted, because registrar liability under 15 U.S.C. § 1114(2)(D)(i)(II)(bb) requires proof that the registrar improperly transferred a domain name "during the pendency of an action," and the "action" contemplated by this section of the Lanham Act had to be a U.S. case, not litigation in a French court. The Fourth Circuit remanded the case against L'Oreal for further proceedings.

Equitable Defenses of Laches and Acquiescence in Opposition and Cancellation Proceedings

Saint-Gobain Abrasives, Inc. v. Unova Industrial Automation Systems, Inc., 66 U.S.P.Q.2d 1355 (T.T.A.B. 2003). Saint-Gobain Abrasives, Inc. (Saint-Gobain) opposed an application and sought to cancel two registrations owned by Unova Industrial Automation Systems, Inc. (Unova) for color marks used on power driven abrasive wheels. Saint-Gobain asserted that Unova's color marks were functional and lack acquired distinctiveness.

Unova moved for dismissal of the action or alternatively for judgment in its favor based in part on the equitable defenses of laches and acquiescence. In a cross-motion, Saint-Gobain moved to strike Unova's two affirmative defenses. Unova argued that under the doctrines of laches and acquiescence Saint-Gobain was barred from attacking Unova's application and registrations due to Saint-Gobain's inexcusable delay in bringing action against Unova's marks.

The Board stated that it is well established that the equitable defenses of laches and acquiescence are not available against claims for genericness, descriptiveness, fraud and abandonment because it is within the public interest to have registrations that are void *ab initio* stricken from the register and that such interest is not waived regardless of the delay. Citing the same reasoning, the Board held that the defenses of laches and acquiescence were unavailable where the proposed grounds for opposition and cancellation is functionality. Additionally, the Board refused to determine whether the defense of laches and/or acquiescence would apply against a claim of a lack of distinctiveness because the parties did not address that specific issue in their briefs.

Fair Use

Horphag Research Ltd. v. Pellegrini, 66 U.S.P.Q.2d 1791 (9th Cir. 2003). Horphag Research, Ltd. (Horphag) brought suit against Larry Garcia (Garcia), an entrepreneur doing business as healthierlife.com, for trademark infringement and trademark dilution based on Garcia's use on his websites of the word "PYCNOGENOL," a trademark owned by Horphag for its pine bark extract product. Garcia's Internet sites, including healthierlife.com, advertised and sold various pharma-

ceutical products, including "PYCNOGENOL" and "Masquelier's: the original French Pycnogenol" and repeatedly used Horphag's trademark PYCNOGENOL as a meta-tag. Following a four-day jury trial, the district court granted Horphag's motions for judgment as a matter of law and awarded attorneys' fees to Horphag, holding that Garcia infringed and unlawfully diluted Horphag's PYCNOGENOL mark. Garcia appealed.

In affirming the district court's judgment with respect to Horphag's trademark infringement claim, the Ninth Circuit began by noting that Garcia's admission of use of Horphag's PYCNOGENOL mark, including use of the mark in the meta-tags for his websites, satisfied the requirements for trademark infringement. The Ninth Circuit then directed its attention to determining whether Garcia adequately presented either a "classic" or a "nominative" fair use defense to infringement under the Lanham Act. The Ninth Circuit concluded that Garcia's use of the PYCNOGENOL mark did not qualify for the classic fair use analysis because the mark did not possess any meaning other than its use as a registered trademark.

In determining whether Garcia would be entitled to the nominative fair use defense, the Ninth Circuit focused on three factors: (1) the product must not be readily identifiable without use of the mark; (2) only so much of the mark may be used as is reasonably necessary to identify the product; and (3) the user must do nothing that would, in conjunction with the mark, suggest sponsorship or endorsement by the trademark holder. The Ninth Circuit held that although Garcia's ability to identify PYCNOGENOL only by using the mark itself satisfied the first requirement, his "unreasonably pervasive" use of the mark in both the text and in the meta-tags of his websites exceeded any measure of reasonable necessity in using the PYCNOGENOL mark and likely suggested that Horphag sponsored or was in some way associated with Garcia's websites and products. Thus, the Ninth Circuit concluded that Garcia could not successfully assert this defense.

The Ninth Circuit vacated the district court's judgment on the trademark dilution claim, and the award of attorneys' fees related to that claim, and remanded for reconsideration in light of the Supreme Court's recent decision in *Moseley v. V Secret Catalogue, Inc.*, 65 U.S.P.Q.2d 1801 (2003).

Liability of Domain Name Registrars for Contributory Trademark Infringement

Size Inc. v. Network Solutions, Inc., 66 U.S.P.Q.2d 1636 (E.D. Va. 2003). This case was before the U.S. District Court for the Eastern District of Virginia on Network Solutions Inc.'s (NSI) motion to dismiss for failure to state a case for which relief can be granted.

In 1996, Size Inc. (Size) registered the Internet domain name *size.com* with NSI. In December 2002, Size began receiving reports from its clients that important information sent to *size.com* e-mail accounts had not been received. When Size contacted NSI, it was informed that NSI had received an e-mail from Size's

registered email address authorizing the transfer of the *size.com* domain to an individual in Russia, named Alexander Ilin (Ilin). After Size had orally informed NSI that it had not authorized the transfer, but before Size had instituted NSI's formal domain name dispute process, Ilin purportedly transferred the domain name to a third party and that third party transferred the domain name registration to a different domain name registrar.

Size commenced the action against NSI arguing that NSI had engaged in contributory trademark infringement of Size's common law trademark for failing to freeze the domain name after Size put NSI on notice that it had not authorized the transfer to Ilin. NSI argued that it was not liable under a contributory infringement theory for supplying a product to a third party with actual or constructive knowledge of the infringement because NSI does not supply a "product." The district court agreed with NSI, concluding that NSI provided a "service," that of translating the domain name into the registrant's IP address. NSI, however, lacked the requisite degree of control over the activity of the domain name registrants to be responsible for the activities of third-party infringers. The district court expressly found that "NSI is simply a routing service" and that NSI had "no direct involvement in the activities of the allegedly infringing third party." Accordingly, the district court dismissed Size's trademark claims, as well as Size's state law claims for breach of contract, conversion, and negligence.

NAFTA Raises Standard for Geographic Misdescriptiveness

In re California Innovations, Inc., 66 U.S.P.Q.2d 1853 (Fed. Cir. 2003). Prior to 1993, marks that were deemed "primarily geographically deceptively misdescriptive"—just like "primarily geographically descriptive" marks—were registrable on the Supplemental Register and could be registered on the Principal Register only if they acquired distinctiveness. In contrast, marks that were deemed "deceptive" were not registrable on either register. Because of this drastic difference in the effect of a finding of deceptiveness under Section 2(a) and geographic deceptive misdescriptiveness under Section 2(e), the Federal Circuit developed very different standards for the two. Specifically, the test for determining a mark to be primarily geographically deceptively misdescriptive consisted of two prongs: (1) the primary significance of the mark was a generally known geographic location, and (2) the public was likely to believe the mark identified the geographic origin of the goods even though they did not come from there. To deny a geographic mark protection as "deceptive" under Section 2(a), however, the PTO had to establish that "(1) the mark misrepresents or misdescribes the goods, (2) the public would likely believe the misrepresentation, and (3) the misrepresentation would materially affect the public's decision to purchase the goods." This additional element of materiality was the key to determining deceptiveness.

On December 8, 1993, the Lanham Act was amended, in compliance with the North American Free Trade

Agreement (NAFTA), to prohibit registration of "primarily geographically deceptively misdescriptive" marks on both the Supplemental and Principal Registers, regardless of acquired distinctiveness.

Whether this amendment changed the standards for finding a mark to be primarily geographically deceptively misdescriptive was the issue in this case. California Innovations applied to register the mark CALIFORNIA INNOVATIONS for insulated bags, wraps, and various other goods that were not made in California. The PTO found that the mark was primarily geographically deceptively misdescriptive, apparently applying the pre-NAFTA standard for such a finding.

The Federal Circuit vacated the PTO's decision and remanded, because "NAFTA and its implementing legislation obliterated the distinction between geographically deceptive marks and primarily geographically deceptively misdescriptive marks," and both types of marks are now "permanently denied registration." The Federal Circuit also stated that the test for rejecting a deceptively misdescriptive mark is no longer simple lack of distinctiveness, but the higher showing of deceptiveness. The Federal Circuit also commented that the relatively easy burden under the old test of showing a naked goods-place association without proof that the association is material to the consumer's decision is no longer justified after NAFTA.

The Federal Circuit summarized the new test for geographic misdescriptiveness as follows:

Thus, due to the NAFTA changes in the Lanham Act, the PTO must deny registration under § 1052(e)(3) if (1) the primary significance of the mark is a generally known geographic location, (2) the consuming public is likely to believe the place identified by the mark indicates the origin of the goods bearing the mark, when in fact the goods do not come from that place, and (3) misrepresentation was a material factor in the consumer's decision.

Although the Federal Circuit remanded the case to the PTO to apply the new standard, it cautioned that "[a]t best, the evidence of a connection between California and insulated bags and wraps is tenuous."

Nominative Use

KP Permanent Make-Up Inc. v. Lasting Impression I Inc., 66 U.S.P.Q.2d 1509 (9th Cir. 2003). This case was brought by KP Permanent Make-Up Inc. (KP) as a declaratory judgment action seeking a determination that the registered mark MICRO COLORS is generic for bottles of pigment injected under skin for cosmetic and medical purposes.

Lasting Impression I Inc. (Lasting Impression) owns an incontestable federal registration for the mark MICRO COLORS & Design for permanent makeup pigments. In January 2000, Lasting Impression sent a cease-and-desist letter to KP demanding KP cease using the mark MICRO COLORS for identical goods. In response, KP brought this declaratory judgment action alleging that MICRO COLORS was generic for the goods at issue and that KP made only fair use of the

term MICRO COLORS. Lasting Impression counter-claimed for trademark infringement, and the parties filed cross-motions for summary judgment.

The district court granted summary judgment for KP after finding that MICRO COLORS was generic or descriptive for skin pigments. On review, the Ninth Circuit determined that the district court failed to observe the presumption of validity provided for registered marks, and erred in requiring Lasting Impression to prove that MICRO COLORS was nondescriptive and nongeneric separate and apart from the mark as a whole.

The Ninth Circuit reversed the district court's granting of summary judgment in favor of KP on the issue of genericness due to a lack of evidence, and granted Lasting Impression's motion for summary judgment on the same genericness issue. The Ninth Circuit determined that summary judgment for KP could not be founded upon the alleged descriptiveness of the MICRO COLORS mark due to the incontestable status of Lasting Impression's registration.

Finally, the Ninth Circuit reversed the district court's grant of summary judgment in KP's favor on its fair use defense, finding that genuine issues of material fact remained regarding whether KP's use of MICRO COLORS gave rise to a likelihood of confusion.

Reverse Passing Off

Dastar Corp. v. Twentieth Century Fox Film Corp., 66 U.S.P.Q.2d 1641 (U.S. 2003). In this case, the Supreme Court said "no" to using the Lanham Act to prevent the unaccredited copying of an uncopyrighted work.

The case involved a television series based on General Dwight D. Eisenhower's book about World War II, entitled "Crusade in Europe." The book was published in 1948, and the TV series (owned and produced by Fox and related entities) was broadcast in 1949. Although the copyright in the book was renewed in 1975, Fox did not renew the copyright in the TV series, which expired in 1977. Anticipating the fiftieth anniversary of the end of World War II, Dastar Corp. (Dastar) obtained tapes of the original "Crusade in Europe" TV series, copied them onto videotape with various additions and modifications, and sold the videos under the name "Campaigns in Europe." Dastar's tapes and advertisements credited itself, its employees and its related distribution company, but gave no credit to the creators of the original book or TV series.

Twentieth Century Fox Film Corp, SFM Entertainment LLC, and New Line Home Video Inc. (collectively Fox) sued Dastar for reverse passing off under Section 43(a) of the Lanham Act. The district court granted summary judgment in favor of Fox, awarding an injunction and double Dastar's profits under 15 U.S.C. § 1117(a). The Ninth Circuit affirmed, holding that Dastar had committed a "bodily appropriation" of Fox's TV series, which was sufficient to establish reverse passing off. The Ninth Circuit rejected Dastar's contention that Fox must make an independent showing of consumer confusion "because the 'bodily appropriation' test subsumes the 'less demanding consumer confusion' standard."

The Supreme Court reversed. Although the Court agreed that the language of Section 43(a) is broad enough to include reverse passing off, it held that Dastar did not commit that tort. The Court reasoned that the term "origin of goods" in Section 43(a) means only "the producer of the tangible product sold in the marketplace, in this case the physical Campaigns videotape sold by Dastar," not "the person or entity that originated the ideas or communications that 'goods' embody or contain." Because Dastar was in fact the "origin" of the videos it sold, it could incur no Lanham Act liability "[f]or merely saying it is the producer of" those videos.

The Court was particularly concerned about extending the Lanham Act into the realm of copyright and patent law. The Court rejected the argument that "communicative products" should be given "special treatment" under Section 43(a) by construing the term "origin of goods" to include the creator of the product's content. The Court was also troubled by the "serious practical problems" that would be posed by requiring attribution of uncopyrighted works under Section 43(a) because without a copyright as the basepoint, it "would be no simple task" to figure out all the parties who should be given attribution as creators.

The Right of Celebrities under the Lanham Act

Parks v. LaFace Records, 66 U.S.P.Q.2d 1735 (6th Cir. 2003). LaFace Records (LaFace) produced a song by a rap duo known as OutKast titled "Rosa Parks" and containing a chorus with the words "everybody move to the back of the bus." Rosa Parks (Parks), who gained prominence as a symbol of the civil rights movement during the 1950s and 1960s for her refusal to follow segregation-era law and move to the back of the bus, brought suit under the Lanham Act and various state law cause of action for misusing her name and identity. The district court granted summary judgment in favor of LaFace, and Parks appealed.

The Sixth Circuit acknowledged that Section 43(a) of the Lanham Act creates a civil cause of action for celebrities because they possess an economic interest in their identities "akin to that of a trademark holder." Such a celebrity must show that the use of her name is likely to cause confusion among consumers as to the connection between the celebrity and the defendant's goods or services. The circuit court found that Parks was a celebrity within the meaning of Section 43(a) and that there was evidence that the title of the song could cause confusion.

LaFace contended that the First Amendment provided it a complete defense. The Sixth Circuit adopted the test in *Rogers v. Grimaldi*, 10 U.S.P.Q.2d 1825 (2d Cir. 1989). Under the *Rogers* test, LaFace would have a valid defense unless: (a) the song had no artistic relevance to the protected interest; or (b) if the song had "some" artistic relevance but the title was "explicitly misleading" about the source or content of the song. The Sixth Circuit reversed the grant of summary judgment because a reasonable jury could have found that the song had no relevance to Parks despite containing the phrase "move to the back of the bus."

The Sixth Circuit's finding was based on the lyrics of the song, which indicated the rap group meant only that other inferior rappers should move to the back of the bus, and statements by the songwriters that the song was not meant to be about Parks or the civil rights movement. The Sixth Circuit concluded that, if on remand, a jury concluded that the song had nothing to do with Parks or her role in the civil rights movement, then the song would have no artistic relevance and the First Amendment would not protect LaFace. The Sixth Circuit also noted that if the jury found that the song had "some" artistic relevance, LaFace would have a complete defense because, as a matter of law, the song title did not "explicitly mislead" consumers into thinking that Parks was the source of the song, even though it contained her name.

Trademark Dilution

Enterprise Rent-A-Car Co. v. Advantage Rent-A-Car Inc., 66 U.S.P.Q.2d 1811 (Fed. Cir. 2003). In this case, the Federal Circuit affirmed the Trademark Trial and Appeal Board's (TTAB) determinations regarding whether an opposition proceeding can be based on trademark dilution claims brought under state dilution statutes, and whether such an opposition can be maintained when the applicant made limited geographical use of the disputed mark before the opposer's mark became famous.

Advantage Rent-A-Car Inc. (Advantage) used the mark WE'LL EVEN PICK YOU UP in a television commercial advertising its car rental services in 1990 in the area of San Antonio, Texas. Later, in 1997 and 1998, Advantage broadcast the same commercial in Arkansas, Louisiana, New Mexico, and in other areas of Texas. In 1994, before the second and more widespread broadcast of Advantage's television commercial containing the WE'LL EVEN PICK YOU UP mark, Enterprise Rent-A-Car Co. (Enterprise) began using the phrases PICK THE COMPANY THAT PICKS YOU UP and PICK ENTERPRISE, WE'LL PICK YOU UP in national advertising. Enterprise obtained three federal registrations covering different versions of its "PICK YOU UP" marks in 1996 and 1997.

Advantage filed suit against Enterprise in the U.S. District Court for the Western District of Texas in 1998, alleging unfair competition and seeking cancellation of Enterprise's registrations. While Advantage's case was pending, Advantage filed an application with the PTO to register the mark WE'LL EVEN PICK YOU UP, and Enterprise promptly opposed this application alleging that Enterprise would be damaged by the dilution of Enterprise's marks. The opposition proceeding was stayed pending the outcome of the district court litigation.

In 1999, the parties entered a partial consent judgment in the district court litigation that disposed of all claims asserted by Advantage and all of Enterprise's counterclaims except for Enterprise's trademark dilution counterclaims. After a bench trial, the district court entered judgment against Enterprise on its dilution

claims based upon a finding that the "PICK YOU UP" marks were not famous or distinctive as defined by the Federal Trademark Dilution Act (FTDA). The Fifth Circuit upheld the district court's determination on appeal; however, the Fifth Circuit also held that Enterprise's state dilution claims were *not* barred due to the mark's lack of fame, because the Texas and Louisiana dilution statutes require only "distinctiveness" but not fame.

Following the Fifth Circuit litigation, the TTAB dismissed Enterprise's opposition to Advantage's WE'LL EVEN PICK YOU UP application, finding that Enterprise's dilution claims under the FTDA were barred by *res judicata*. In response, Enterprise argued that its opposition should proceed on the basis of Enterprise's *state* dilution claims, which were not disposed of in the Fifth Circuit litigation. Enterprise further argued that its dilution claim was not weakened by Advantage's limited geographical use of the WE'LL EVEN PICK YOU UP mark before Enterprise's "PICK YOU UP" marks became famous, because Enterprise could submit evidence that its marks were famous before the opposition was instituted.

The TTAB concluded that it did not have jurisdiction under the Trademark Amendments Act of 1999 to entertain an opposition based on state dilution statutes and declined Enterprise's request to grant geographically limited trademark registrations to the two parties to avoid trademark dilution. The Federal Circuit affirmed the holdings of the TTAB and stated that *any* prior use of a mark, even in a limited geographic area, bars a claim of dilution as a ground for opposition.

Use in Commerce

International Bancorp LLC v. Societe des Bains de Mer, 66 U.S.P.Q.2d 1705 (4th Cir. 2003). International Bancorp LLC and its affiliated companies appealed from the district court's grant of summary judgment that their registration and use of forty-three domain names, all of which incorporate some portion of the term "Casino de Monte Carlo," infringe Societe des Bains de Mer et du Cercle des Etrangers a Monaco's (SBM) rights under the Lanham Act and violate the ACPA, where SBM, a foreign corporation, advertised its trademark CASINO DE MONTE CARLO in the U.S., but only rendered services under the mark outside the U.S.

The Fourth Circuit noted that the critical issue in assessing whether SBM used its mark in commerce was whether the services provided by SBM under the CASINO DE MONTE CARLO mark were rendered in commerce. In reaching its decision, the Fourth Circuit first addressed the scope of the term "commerce" within the Lanham Act, holding—based upon the Lanham Act's own definition of the term—that "commerce" is coterminous with that commerce that Congress may regulate under the Commerce Clause of the U.S. Constitution. Thus, the Fourth Circuit concluded that "commerce" under the Lanham Act necessarily includes all variations of interstate commerce and commerce between the U.S. and other countries.

The Fourth Circuit next turned to the determination of what constitutes “use in commerce” under the Lanham Act. Relying on the statutory definition of “use in commerce” found in the Act, as well as Supreme Court precedent, the Fourth Circuit concluded that a mark is used in commerce only if it accompanies services rendered in commerce.

The Fourth Circuit then determined that SBM used its CASINO DE MONTE CARLO mark by selling and advertising its casino services to U.S. citizens and that its rendering of casino services to citizens of the U.S. constituted foreign trade (i.e., commerce that Congress may lawfully regulate). Thus, the Fourth Circuit concluded—because commerce under the Lanham Act comprises all

commerce that Congress may lawfully regulate—the services rendered by SBM under the CASINO DE MONTE CARLO trademark to U.S. citizens were services rendered in commerce and, consequently, the “use in commerce” requirement set forth in the Lanham Act for the mark’s protectibility was satisfied.

One judge dissented, asserting that the Lanham Act required both elements of “use in commerce” (advertising and the rendering of services) to occur within the U.S. The majority, however, held that such a merging of the two elements is not provided for by the Act. Instead, “commerce” that can satisfy the Lanham Act includes commerce both *in* and *with* the United States.

Chair Appoints Section Nominating Committee

The following Nominating Committee has been appointed by Section Chair, Robert W. Sacoff:

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The Nominating Committee welcomes members’ suggestions for nominees for the offices of Chair-Elect, Vice Chair, Secretary, Financial Officer, and four new members of Council for four-year terms expiring in 2008.

Contact Nominating Committee Chair Edward G. Fiorito with suggestions.

According to Section Bylaws, William L. LaFuze, current Chair-Elect, will automatically assume the office of Section Chair on September 1, 2004.

The Section’s Business Session with Election will be held Saturday, August 7, 2004 at the ABA Annual Meeting in Atlanta, Georgia. All members are invited to attend and vote.

BY SAMSON HELFGOTT, INTERNATIONAL REPORTER



Samson Helfgott

A number of interesting items have come up with respect to the I²P group (International Intellectual Property Group), which are of interest to the entire membership.

Development of the European Patent System

In a report prepared for the thirty-fifth meeting of the Standing Advisory Committee Before the European Patent Office (SACEPO), which was also presented at the US Bar/JPO Liaison Council Meeting in September 2003, EPO provided an update of their current state.

In 2002, for the first time in many years, there was no significant rise in the number of European patent applications filed. Although 175,000 applications were predicted, only 165,000 were registered, including more 111,000 filed by the PCT route. In the first six months of 2003, almost 80,000 applications were filed, about 5.5 percent fewer than in 2002. It is anticipated that for 2003, there will be approximately 71 percent Euro-PCT filings.

The search workload was down 8.5 percent compared with the same period the previous year. However, the workload in substantive examination increased as compared to the first part of the previous year.

Although the opposition rate decreased slightly to 5.4 percent because of the large number of granted patents (specifically 37 percent more than in the previous year), the absolute number of oppositions increased. The total number of oppositions settled by the EPO was fewer than in the previous year. As a consequence, there is a growing increase in the backlog of oppositions. However, the EPO Boards of Appeals had a decline in the number of cases received in 2002 and an increase in the number of cases settled. In general, the backlog within the EPO has started to improve in a number of areas. At the same time, the office's performance productivity rose in just about all areas.

Serious progress occurred with the ongoing extension of the BEST procedure and the introduction of the Joint Cluster Structure. By the end of 2002, about 63 percent of the examiners were working in the BEST mode and some have already started handling opposition files. Because of the BEST implementation harmonizing search and examination practice, it was necessary to introduce a new management structure within DG1/DG2. This entailed the creation of pilot "Joint Cluster" Principle Directorates in various technical areas, which were implemented in early 2003.

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A major issue currently in discussion is the possibility of making the Boards of Appeal independent of the European Patent Office by creating a third organ of the European Patent Organization. There are ongoing discussions on this subject.

With respect to recruitment, the EPO now targets thirty countries. New staff (131 examiners, 72 nonexaminers) was added with another fifty examiners due to start within the coming months. This will lead to an overall of nearly 6,000 staff members from most of the twenty-seven member states. Concerning the financial situation, the operating surplus in 2002 amounted to EUR 45m and in the first six months of 2003, a surplus of EUO 9.5 m was generated which was 7.5 m above plan.

With respect to the enlargement of the Organization, after Bulgaria, the Czech Republic, Estonia, the Slavic Republic and Slovenia, which joined in 2002, Hungary followed in January 2003 and Romania became the twenty-seventh member of the European Patent Organization in March 2003. With Poland, Iceland, Latvia, Lithuania and possibly Malta, which will soon join, there will be at least thirty member states of the European Patent Organization in the very near future. There are four extension states, Albania, Latvia, Lithuania, and the former Yugoslav Republic of Macedonia.

The extension agreement with the State Union of Serbia and Montenegro signed in November 2001, has not yet entered into force. Recently, a cooperation and extension agreement with Croatia was signed.

With respect to PCT matters, now that almost all of the PCT contracting states have agreed to extend Chapter I for thirty months, there has been a reduction of nearly 25 percent on the number of demands filed for International Preliminary Examination. The preparatory work for the creation of the new EISPE system in PCT, which will combine search and examination, will work well with the development of the BEST system and quality of service provided under the PCT is expected to improve.

OHIM UPDATE

The Office for Harmonization in the Internal Market (OHIM) is the administrative agency responsible for both the Community Trademark (CTM) and the newly implemented Registered Community Design (RCD) System. Since it began in 1996, OHIM has received more than 300,000 CTM applications and approved over 180,000 CTMs, refused 10,000 and has had 39,000 applications withdrawn. Of the 85,000 pending CTM applications, 15,000 are in opposition, 1,400 before the Boards of Appeals, 226 before the Court of First Instance and 25 before the European Court of Justice. This year, more than 20,000 CTM applications have been filed though May 2003.

The European Commission has a draft proposal for the EU's Accession to Madrid Protocol. There is general agreement with the proposal, except for language, and the question of whether a Madrid Protocol applicant should be able to "opt back" to EU member states through the Madrid Protocol when a CTM is refused or invalidated. The language question may be resolved by adding Spanish as a Madrid Protocol language. If these issues can be resolved in the near term, the EU could become a member of the Madrid Protocol as early as April 2004. Like the United States' PTO, OHIM plans to implement an all-electronic system for Madrid Protocol communications between its office and WIPO.

There is also a proposal to abolish national searches in the CTM system. Since the final decision must be taken by the Council of Ministers by a unanimous vote, a single member state can block the proposal. Thus, the outcome is not predictable, but alternatives are also being considered, such as giving the option to request searches. The decision on searches will be taken prior to the enlargement of the EU in the middle of 2004. If searches are abolished, then there will be no increase in CTM filing fees following enlargement.

At present, filings by U.S. companies account for at least 25 percent of all CTM filings. Ten new countries will be added to the EU on May 1, 2004. These include Czech Republic, Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia. This will mark the first time OHIM has had to deal with the implications of adding new countries to the EU. The following are highlights of the proposals for the expansion issue.

- CTM and RCD protection will automatically be extended to include the ten new member states upon accession on May 1, 2004, without need for any action by an applicant.
- If there is a conflicting prior mark or design registration in one of the ten new countries, it cannot be used as a basis for invalidating a CTM or RCD in existence at the time of accession.
- If there is a conflicting prior mark or design in one of the ten new countries, the owner of the national mark or design can oppose use of the CTM or RCD in that new member country's territory through an action before a national court.
- CTM applications filed between November 1, 2003 and April 30, 2004 (six months before accession deadline) may be opposed by holders of national trademarks in one or more of the ten new members to the EU. Thus, U.S. filers may wish to take this into account when considering filing strategies for CTM applications.

With respect to the registered Community Designs, OHIM began receiving the applications on January 1, 2003, and began registering these on April 1, 2003. By July, OHIM had registered approximately 3,200 RCDs. U.S. companies account for approximately 10 percent of all RCD filings.

Concerning Unregistered Community Designs (UCDs), pursuant to Article 11 of Council Regulation

(EC) No 6/2002 of December 12, 2001, designs which have only been made public outside the territory of the community shall not be protected as UCDs. In fact, a first disclosure of a design outside the EU before its disclosure in the EU even destroys the possibility of establishing a UCD. Paragraph 2 of Article 11 provides that "a design shall be deemed to have been made available to the public within the community if it has been published, exhibited, used in trade or otherwise disclosed in such a way that, in the normal course of business, these events could reasonably have become known to the circles specialized in the sector concerned, operating within the Community." As the legal basis for this interpretation, paragraph 5 of a new Article 110a was added to Council Regulation No 6/2002 pursuant to the Treaty of Accession by the ten new countries to the EU. This appears to eliminate the possibility that disclosure in trade shows in the U.S. or elsewhere outside the community would constitute a qualifying disclosure based on the rationale that one specialized in the field could have attended and gained knowledge of the design at the trade show, no matter where it might be located.

PCT SAFE Goes Live at RO/IB of PCT

The International Bureau as Receiving Office (RO/IB) has announced (see PCT Gazette No. 34/2003, at 19,248) that, as of August 25, 2003, it is prepared to receive international applications in electronic form *provided that* they are filed by users already registered with the International Bureau as Receiving Office for that purpose under the PCT-SAFE pilot (see PCT Gazette No. 46/2002, page 23268). Dutch electronics giant Philips (Koninklijke Philips Electronics N.V.) became the first to file a fully electronic international application with RO/IB using PCT-SAFE (Secure Applications Filed Electronically) software. The availability of this upgraded secure electronic filing facility means that PCT users are able to file their international applications either online or using physical media such as CD-R.

The PCT-SAFE software, which is expected to be available to all users of the by the end of 2003, offers PCT applicants significant benefits. Users will be able to submit validated applications without the printing, copying and mailing normally associated with such a transaction. PCT-SAFE also will allow users to receive almost immediate notification of application receipt and processing. The PCT-SAFE development was made possible through the adoption by the industrial property offices of the PCT contracting states of a legal framework and technical standard necessary for the implementation of electronic filing and processing of international applications, and its subsequent promulgation.

How does it work? To facilitate the transition to PCT-SAFE for current PCT users who prepare the request part of the international applications using the PCT-EASY software, the new system has been built upon an enhanced version of that software. With the PCT-SAFE software, it is possible for applicants to continue to create and file PCT-EASY type applications

(paper plus diskette). As the electronic application is completed, the system validates the entered data and presents applicants with a “traffic light” system indicating any fields that have been incorrectly or inconsistently completed and that may result in defects in the international application once it is filed. Applicants also select whether the international application is to be filed using physical media or online. Depending on the filing method selected, a completed international application in electronic form is either saved on a physical media, which will be filed, or electronically transmitted directly to the specified receiving Office.

New easy to use software for the authoring of the application body—the PCT-SAFE Editor—is included in the PCT-SAFE software. The PCT-SAFE Editor enables users to prepare the body of a PCT application in the required electronic format (extensible Markup Language (XML)), without any need to understand this format. XML is an industry standard computer readable format that is very useful for searching, storing, and exchanging patent information. When operating the Editor, applicants have the option of converting an application body created using a word processor, or to prepare the application body from scratch within the Editor. Once created by the PCT-SAFE Editor, the applicants combine it with the request by indicating its location using the PCT-SAFE software used for preparing the request. With RO/IB, applicants also have the option to prepare components of the application body in PDF format.

What are the additional benefits to users compared with paper filing? The use of PCT-SAFE delivers a number of benefits to PCT applicants. These include:

- The fact that the PCT-SAFE product has been based so closely on the PCT-EASY should mean that the 40 percent of PCT users who currently use PCT-EASY and the PCT authorities that accept such filings will find the transition to PCT-SAFE quite easy.
- The validation software within PCT-SAFE creates documents that meet PCT requirements allowing users to be confident that their applications are correctly formatted.
- An online submission reduces printing, copying and mailing costs of applications.
- The use of XML formatting means that the documents submitted are fully searchable, both during the PCT procedure and once they enter the public domain.

Finally, and perhaps most importantly, the use of electronic online transmission shortens the process of filing and applicants are almost immediately assured that their international application has been received and is being processed.

Is the PCT-SAFE system really safe for the submission of patent applications? Applicants submitting an international application online will first need to apply for a digital certificate. It will be possible to obtain this certificate either directly from WIPO (normally in a matter of minutes) or from any other national industrial property office whose certificate is recognized

in accordance with the PCT electronic filing standard and accepted by the chosen receiving Office. The digital certificate is used by the system in digitally signing the international application and in creating a secure connection with the receiving office for the transmission of the international application package. The secure connection ensures that the application is not legible during transmission, and the digital signature ensures that any alteration of the package is detectable. A high degree of integrity and security is therefore assured for PCT-SAFE data.

How can I obtain it? Toward the end of 2003, PCT-SAFE software will be free of charge and available for download from the PCT-SAFE website at www.wipo.int/pct-safe or on a CD which can be obtained by contacting the PCT-SAFE Help Desk at pct-safe.help@wipo.int or by writing to the PCT-SAFE Help Desk, WIPO, 34 chemin des Colombettes, P.O. Box 18, CH-1211 Geneva 20, Switzerland.

If you are interested in learning more about PCT-SAFE, please visit the PCT-SAFE website at www.wipo.int/pct-safe.

Patent Marking in China

Marking of patented products and/or their packaging in China is recommended (particularly in light of new provisions exempting innocent infringers from payment of damages), but not compulsory. Regulation 83 of the implementing Regulations to the Chinese Patent Law (2000) requires that such marking be in the manner prescribed by the State Intellectual Property Office. Until recently, no such manner had been prescribed, but there has been rectified with the issuance of the Provisions Regarding the Manner of indicating Patent Markings and Patent Numbers, which came into effect on July 1, 2003. These provisions are:

1. The type of patent (i.e., invention, utility model, or design) must be indicated in Chinese;
2. Products obtained by use of a patented method, or their packaging, must be marked in Chinese with the statement: “This product is a product obtained by use of a patented method”;
3. The patent number must be the exact number issued by the State Intellectual Property Office; and
4. Words or graphics used in conjunction with the above markings must not mislead the public in any way.

Australia Introduces Information Disclosure Statements

Regulations have been passed to now require Information Disclosure Statements in Australia. Only prior patent office search results are required. For UK and EPO searches, the code indicating the degree of relevance is also required. The results of any official search completed before the *grant* of the Australia patent are required. These must be submitted by the later of the six months of the request for examination, six months of completion of the search result, or February 1, 2004.

It is important to note that the obligation to disclose continues for search results completed up to the date of sealing of the Australian patent. It is therefore important

to continuously update the IDS in Australia. It is not necessary to provide copies of the citations, only the number of the citation so it can be identified. Furthermore, only official searches conducted by patent offices are required to be submitted.

It is not necessary to provide search results where no citations were identified. Also, where the citations were previously provided in a patent application of a divisional or a divisional of a divisional, it need not be submitted again. However, this does not go beyond two generations of divisionals. Also, where the search results were submitted in relation to the main invention of a patent of addition, it does not again have to be submitted.

The penalty for noncompliance is that an amendment will not be allowed in order to avoid such prior art that should have been disclosed but was not.

European Community Patent

On March 3, 2003, the European Union reached agreement on a common political approach concerning the proposed Community Patent. This approach includes the main outlines of the system of jurisdiction, the language regime, costs, the role of national patent offices and the distribution of fees.

Jurisdictional System—Litigation concerning Community Patent will be exclusively dealt with by a unitary Court for the Community Patent. At first instance, it shall take place before a judicial panel called the Community Patent Court, which is to be established according to the European Community Treaty. It shall be attached to the European Court of First Instance of the European Community and have its seat at Luxembourg. Appeal against decisions of the Community Patent Court shall be with the Court of First Instance. The Community Patent Court shall be established at the latest by 2010.

Language Regime—Up to the grant of the Community Patent, the European Patent Convention's language regime will apply. However, wherein an application is filed initially in a non-EPO language, the cost of the translation of such application into one of the EPO's official languages will have to be carried by the system itself.

After grant, a translation of the claims of the Community Patent into all of the European Country languages will have to be filed with the EPO. Translation costs are to be carried by the applicant. The Council indicated that the words "upon the grant of the patent" would mean within a reasonable time from the date of the grant of the patent. In this period of time during which translations are to be provided, the granted patent shall be valid regardless of the availability of the translations of all the claims into all official community languages at that time. The Council noted that the German delegation considered a reasonable time would be within two years from the date of the grant of the patent.

Based upon current estimates, including costs for translations into eighteen separate languages, the cost of a Community Patent would be less than an average EPO application requiring even six translations of the entire specification.

Renewal fees for Community Patents must not exceed the level of the corresponding fees for an average European Patent. Procedural fees for processing a Community Patent application will be the same regardless of where the application is filed and where the search is carried out.

Roll of National Patent Offices—The European Patent Office exclusively will be responsible for the examination of applications and the grant of Community Patents. National Patent Offices that do not have an EPO language as official language may carry out novelty searches on behalf of the EPO if the applicant so requests. Other National Patent Offices may do so only if they have experience of cooperation with the European Patent Office and need such search work to maintain a critical mass of their own work. In both cases, the cooperation between the European Patent Office and the National Patent Offices is to be based on a Partnership Agreement defining particular relevant quality standards.

Distribution of Fees—The EPO's share of renewal fees from Community Patents will be 50 percent. The remaining 50 percent will be distributed among EU member states in accordance with a distribution key to be fixed by the EU Council.



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