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Bright Ideas

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Message From the Chair


Paul M. Fakler

Outside my window, the leaves are various shades of yellow, red, and orange. Some have already fallen to the ground, but many will continue to adorn the trees for a while before they, too, fall. This backdrop reminds me of two fundamental and important things: (1) the principle of impermanence and (2) the Intellectual Property Law Section's annual Fall Meeting. The Fall Meeting was held this year from October 7-10 in lovely Cooperstown, New York. Kudos to Debra Resnick and Erica Klein for producing one of the best substantive programs we have ever presented. Every one of the panels was informative, timely, and interesting, and many attendees commented on their high quality. A recurring theme was that even the panels relating to intellectual property disciplines in which a given attendee did not practice (you know, the panels during which you "co-vertly" open your laptop and catch up on e-mail or revise that brief you are working on) were fascinating and held everyone's attention. This combination of well-selected topics and engaging speakers led to something we always strive for in our programs: a level of interactivity and audience involvement that I find rare at CLE programs produced by other organizations.

One of the greatest features of the Fall Meeting, and particularly of this one, is that participants spend an extended weekend together in a wonderful environment wherein the CLE programming is mixed with social events for the whole family. This allows for an even higher degree of interactivity, as questions and issues raised in the substantive program spill over to smaller discussions over a local beer or glass of wine. Section members who attend the Fall Meeting get to know one another (and often one another's families) due to this wonderful mix of substantive programming and fun social events. I believe these elements of camaraderie and fun really distinguish our group from other bar associations, and this year's Fall Meeting set a new high-water mark for our Section.

I have received a large number of wonderful notes from participants who—unsolicited—took the time to share their enjoyment of the program and their pledge to

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become more involved in future Section activities. I attribute this unprecedented level of positive feedback to (1) Debra and Erica's hard work as co-chairs; (2) the talents of the superb speakers; and (3) the nature of our Section, which places a premium on combining commitment to substantive expertise with a friendly and fun approach to our events.

Another hallmark of our Section is that, in addition to our tried-and-true events like the Fall Meeting, we continually strive to create new programs we believe will be of interest to our members. One such new event, the Section's first annual General Counsel Forum, took place on September 28. This inaugural Forum was titled "How General Counsel Can Increase Revenue and Market Share With and Effective IP Strategy." It was conceived and executed by our Immediate Past Section Chair Joyce Creidy. The Forum brought together a number of General Counsel from many midsize-to-large companies and various in-house intellectual property law specialists to help the General Counsel in attendance better understand the value added by expending resources in the intellectual property areas relating to their businesses. Based upon the feedback we received from attendees, the Forum was a roaring success. We look forward to next year's Forum and to other new events through which we are trying to encourage greater involvement in our Section by in-house counsel.

As this issue goes to press, we are preparing for numerous other great events, including the Litigation Committee's roundtable forum on injunctive relief in trademark infringement cases after the Second Circuit's recent *Salinger* decision, in which the court changed its traditional standard for preliminary injunctions in copyright (and by implication other intellectual property) cases. Our Section is also, for the first time, collaborating with the United States Patent and Trademark Office on a program for visiting judges from various Latin American countries, giving the judges instruction on how various intellectual property rights are enforced in the United States. Of course, we are also closing in on our Annual Meeting, which will be held as part of the larger New York State Bar Association's Annual Meeting in January.

As we continue to expand the number and nature of our programs and events, it is more important than ever that you become more actively involved in our Section. We work hard to keep the cost of our events reasonable (particularly in relation to the CLE credits offered) and to make them informative and fun. Attend a meeting or event, join a Committee of interest to you, if you have not already. If you have joined a Committee, call one of the Chairs and ask how you can get more involved. Like the many Fall Meeting attendees who sent me their personal reflections on the Meeting, you will be glad you did. And don't forget to register for the Annual Meeting in January as soon as the registration materials are posted! I look forward to seeing as many of you there as possible.

Paul M. Fakler

Recent Damages Trends in Patent Infringement Litigation

By Nagendra Setty, Jay Smith, and Debra Resnick

I. Introduction

In recent years, Congress has been under increased pressure to reform the Patent Act. Among other principal areas of reform, many entities and individuals have petitioned Congress to rein in perceived excesses in patent infringement damages awards. Not to be upstaged by their Article I counterparts, the Federal Circuit, as well as district courts nationwide, seem to have become increasingly involved in changing the patent damages landscape.

Part II of this article discusses recent decisions that have questioned a broad application of the "entire market value" rule for assessing patent damages. Part III discusses post-*eBay*[1] cases involving the calculation of ongoing royalties in lieu of a permanent injunction. Part IV addresses the Supreme Court's *Quanta Computer v. LG Electronics*[2] decision and its effects on financial aspects of settlement agreements and licensing negotiations. Part V explores current case law regarding the use of settlement negotiations and license agreements in assessing damages. Part VI discusses the recent spate of false marking cases. And finally, Part VII focuses on recent legislative patent reform efforts and proposed changes to patent damages.

II. Judges Rein in Expansive Use of the Entire Market Value Rule

Recently, various courts have shown an increased willingness to restrict a plaintiff's ability to rely on the so-called "entire market value rule" to enlarge the base of accused products on which the patentee may recover damages for infringement.

The entire market value rule "allow[s] recovery of lost profits or a reasonable royalty based not only on the profit from the patented part, but also on non-patented parts [of an accused product]."[3] As evidence of its prominence (some might say infamy) in the calculation of patent damages, Chief Judge Paul Michel of the Federal Circuit spoke directly on the issue at the Spring 2009 American Intellectual Property Law Association meeting. Taking issue with the comments of academics who argue that courts need to be able to better "apportion" damages, Chief Judge Michel emphasized that the entire market value rule is not required when calculating royalty damages.[4] Rather, a jury may base its royalty calculation on an enlarged royalty base under the entire market value rule only where the patentee makes three showings:

> (1) the infringing components must be the basis for customer demand for the entire machine including the parts beyond the claimed invention; (2) the individual infringing and non-infringing components must be sold together so that they constitute a functional unit or are parts of a complete machine or single assembly of parts; and (3) the individual infringing and non-infringing products must be analogous to a single functioning unit.[5]

Below, we highlight several recent decisions that have addressed and defined application of the entire market value rule in patent infringement litigations.

A. *Lucent* and *Cornell University*

In *Lucent Technologies, Inc. v. Gateway, Inc.*,[6] the Federal Circuit affirmed a district court grant of judgment as a matter of law (JMOL), reversing a $1.5 billion judgment against Microsoft.[7] On Microsoft's JMOL motion, the district court found that the jury acted against the clear weight of the evidence when, applying the entire market value rule, it used as a royalty base the value of every computer sold with Windows Media Player installed rather than merely the value of the patented technology, i.e., MP3 audio technology utilized by Windows Media Player.[8] To include patented and unpatented components together in a royalty calculation, the patented component must be "the basis for customer demand or 'substantially create the value of the component parts.'"[9] Despite Lucent's attempt to prove that consumers strongly desired MP3 audio technology, the district court held that Lucent failed to adduce sufficient evidence that the MP3 technology was *the basis* for customer demand that could "establish the required nexus between the patented features and the value of the entire computer."[10]

Similarly, in March 2009, Judge Randall R. Rader of the Federal Circuit, sitting by designation in the Northern District of New York, reduced a royalty damages award from $184 million to $54 million based on a misapplication of the entire market value rule.[11] In *Cornell University v. Hewlett-Packard Co.*, the jury awarded damages using the value of an entire computer component, the "CPU brick," as the royalty base, even though the patent at issue covered only a small invention used within the "CPU brick," a "method for instruction issuance within a computer processor."[12] Indeed, the court had previously rejected plaintiff's attempt to use an even larger unit—"servers and workstations"—as the basis for the royalty.[13]

Post-trial, the court determined that even the "CPU brick" was overbroad where a "processor" was the smallest unit incorporating the patented invention. Although

Judge Rader recognized that the entire market value rule "permits damages on technology beyond the scope of the claimed invention," he granted the defendant JMOL and calculated the royalty base using the "processor" unit.[14] The court disapproved of the plaintiff "simply stepp[ing] one rung down the [defendant's] revenue ladder from servers and workstations to the next most expensive processor-incorporating product without offering any evidence to show a connection between consumer demand for that product and the patented invention."[15] The court also rejected the plaintiff's attempt to use the more "accurate" sales figures for servers and workstations, since "the damages equation is not based on [the defendant's] earnings, but instead on the compensation due to [the plaintiff] for infringement."[16] The court ultimately found that the defendant was entitled to JMOL, or alternatively, remittitur of the award using the hypothetical processor revenue as the royalty base.[17]

Following *Cornell University*, several decisions emanating from the Eastern District of Texas have adopted the same approach with respect to plaintiffs seeking damages under the entire market value rule, and all have found that the entire market value rule was misapplied by the plaintiff. In *IP Innovation LLC v. Red Hat, Inc.*[18] for example, Chief Judge Rader, sitting by designation, granted the defendants' motion to preclude testimony of the plaintiff's damages expert, Joseph Gemini, to the extent his testimony was based on the entire market value rule. Although Mr. Gemini included 100 percent of the defendants' total revenues from sales of subscriptions to the accused operating systems in his proposed royalty base, his

> methodology [] does not show a sound economic connection between the claimed invention and this broad proffered royalty base. The claimed invention is but one relatively small component of the accused operating systems. The evidence shows that the workspace switching feature represents only one of over a thousand components included in the accused products…. Most of [defendants'] accused sales come from their Server products, the majority of which are not connected to a display and thus do not take advantage of the workspace switching feature. Mr. Gemini made no effort to factor out of his proffered royalty base these products which do not even feature the claimed invention. Once again, this blatant oversight shows that Mr. Gemini did not use the type of reliable economic principles and methods required by Rule 702 for an economic damages expert.[19]

In an unpublished decision in *Fenner Inv., Ltd. v. Hewlett-Packard Co.*,[20] Magistrate Judge Love held that although reliance on the entire market value rule to calculate damages may have been appropriate, the testimony of Fenner's damages expert had to be excluded on the ground that it failed to demonstrate that the patented invention was the basis for consumer demand for the accused products and failed to "identify and support an appropriate 'multiplier' that takes into account the relative significance of the patented inventions and their contribution to the overall value of the accused products."[21]

Several weeks later, in *Laserdynamics, Inc. v. Quanta Computer, Inc.*,[22] Judge Ward reduced a jury verdict of $52 million to $6.2 million and gave the plaintiff ten days to choose between the reduced award or a new trial on damages. The patent at issue covered computer technology that enabled recognition of a CD or DVD. During trial, the plaintiff's damages expert, Dr. Emmett Murtha, invoked the entire market value and testified the royalty should be 6 percent on stand-alone disc drives and 2 percent on assembled computers containing the disc drive. The jury's verdict was based on Dr. Murtha's entire market value rule analysis.[23]

Judge Ward found that there was no basis for the application of the entire market value and that the price of the finished computer should not have been included in the royalty base:

> At best, Dr. Murtha testified that almost all computers sold in the retail market include optical disc drives and that customers would be hesitant to purchase computers without an optical disc drive. This evidence notwithstanding, there was no evidence from which the jury could conclude that the patented features of the invention formed the basis for the customer's demand for the entire computer.[24]

Indeed, the "claimed invention embodied in the disc-drive is but one relatively small component of the entire assembled computer,"[25] and LaserDynamics pointed to no evidence that Quanta sold more of the assembled computers because it included drives practicing LaserDynamics' patent.[26]

The Federal Circuit and Eastern District of Texas are not alone in adhering to a strict application of the entire market value rule, albeit with sometimes differing results. For example, in *Funai Electric Co., Ltd. v. Daewoo Electronics Corp.*,[27] the Federal Circuit upheld a determination by the district court that the plaintiff had submitted evidence to prove that its patented technology was the basis for customer demand, such that damages properly could be based on the entire lost sales value.[28]

In an unpublished decision out of the District of New Hampshire in *Marine Polymer Technologies, Inc. v. HemCon, Inc.,*[29] the court denied the defendant's motion for remittitur of an almost $30 million verdict based on a reasonable royalty of 30 percent of the entire market value of the infringing products. The court found that plaintiff Marine Polymer presented evidence regarding the importance of its patented technology in defendant HemCon's products and its significance to market demand. Although HemCon sought to undermine that evidence, its damages expert failed to support the theory that HemCon's manufacturing process, rather than the infringing component of its products, fueled the demand for its products.[30] In *Cordis Corp. v. Boston Scientific Corp.,*[31] pending in Delaware, Judge Robinson denied the defendant's motion to preclude damages based on the entire market value rule, finding that "literally, without the patented feature, [Boston Scientific] would not have a product to sell."[32]

B. *American Seating*: "Functional Unit" Analysis for "Convoyed" Sales

In *American Seating Co. v. USSC Group, Inc.*, the Federal Circuit ratified a trial court's decision to set aside a jury's damages award based on so-called "convoyed sales." The court explained that an award of lost profits may only include sales of non-infringing items sold together with, or "convoyed" with, an infringing product if the two items "were considered to be components of a single assembly or parts of a complete machine, or they together constituted a functional unit."[33] As the court previously stated in *Rite-Hite Corp. v. Kelley Co., Inc.,*[34] a jury cannot award lost profits for non-infringing items if they were bundled together with the patented product "only as a matter of convenience or business advantage."[35] American Seating originally won a damages award for infringement of its patent covering wheelchair tie-down devices, which were usually (but not always) sold with the unpatented passenger seats.[36] The Federal Circuit affirmed, noting that the "passenger seats command a market value and serve a useful purpose independent of the patented product."[37]

C. Microsoft Appeals $358 Million Award to Alcatel-Lucent

While the Federal Circuit reviewed the grant of JMOL in *Lucent Technologies v. Microsoft*, the parties continued to wage war on a slightly different front. In a separately tried case, Alcatel-Lucent accused Microsoft of infringing several patents, including one (known as "the Day patent" after one of its named inventors) claiming a method for entering information into forms on computer-based fields using predefined onscreen rules. According to Alcatel-Lucent, several Microsoft products infringed the Day patent, including Microsoft Outlook's calendar function. Specifically, Alcatel-Lucent claimed that the "date-picker" menu within Outlook's "new appointment" form, a function that Alcatel-Lucent conceded is not required to operate Outlook's calendar, infringed the Day patent. At trial, Alcatel-Lucent sought a reasonable royalty using the sales of Outlook as the royalty base. Despite Microsoft's protest that the evidence did not demonstrate the accused feature served as the basis for customer demand for Outlook, the jury awarded Alcatel-Lucent close to $358 million in damages (later increased to $512 million by the district court to account for interest).

Microsoft appealed, arguing that the trial court erred in allowing the jury to consider Alcatel-Lucent's entire market value rule argument that the patented feature was the basis for customer demand because the evidence Alcatel-Lucent advanced, such as Microsoft marketing material, failed to demonstrate the connection. Instead, Microsoft contended that the court should have instructed the jury to base its damages award only on the value of the patented technology, not on the entire value of the accused products. For its part, Lucent argued that the jury's verdict was not necessarily based on the entire market value rule, and even if it was, the evidence supported a nexus between the patented technology and demand for the accused products.

The Federal Circuit heard argument on the case in June 2009. During argument, Chief Judge Michel observed that "[t]here still seems to be massive unclarity about how reasonable royalty damages are to be calculated."[38] He also intimated that the Federal Circuit might be amenable to modifying the entire market value rule to include a burden-shifting standard, under which the patentee would initially bear the burden to establish that the entire market value rule applies a presumption the alleged infringer could then rebut.[39]

The Federal Circuit issued its decision on September 11, 2009.[40] With respect to the entire market value rule, the court noted the complexity of the Outlook program, which comprised "hundreds, if not thousands or even more, features."[41] On that basis, the court found it "inconceivable to conclude, based on the present record, that the use of one small feature, the date-picker, constitutes a substantial portion of the value of Outlook…. Here, numerous features other than the date-picker appear to account for the overwhelming majority of the consumer demand and therefore significant profit."[42] The court ultimately held the jury's award to be "based mainly on speculation or guesswork" and "against the clear weight of the evidence,"[43] and it remanded to the district court for a new trial on damages.[44] In so doing, the court again cautioned district court and litigating parties from unwarranted reliance on the entire market value rule where the evidentiary prerequisites have not been satisfied.[45]

D. Microsoft's Appeal of $240 Million Award to i4i Limited Partnership

In *i4i Limited Partnership v. Microsoft Corp.,*[46] software maker i4i Limited Partnership accused Microsoft of infringing U.S. Patent No. 5,787,449 ("'449 patent"), based on the custom XML editor used in various editions of Microsoft Word ("Word").[47] The '449 patent claims a method for "editing documents containing markup languages like XML."[48] At trial, the jury found Microsoft liable for infringing the '449 patent and awarded $200 million in damages as well as $40 million in enhanced damages for Microsoft's willful infringement and for litigation misconduct. On appeal, Microsoft challenged the damages award on three grounds: (1) the admission of certain expert testimony; (2) the sufficiency of the evidence supporting the damages award; and (3) the award of $40 million in enhanced damages.[49]

The Admission of Expert Testimony. Microsoft challenged the admissibility of the testimony of i4i's damages expert, Dr. Michael Wagner, under Rule 702 of the Federal Rules of Evidence.[50] In considering whether expert testimony was "properly admitted" under Rule 702, a court must use the standard stated in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*,[51] which requires that expert evidence "be not only relevant, but reliable."[52]

Dr. Wagner argued for a damages award of $200 million, based on a hypothetical negotiation between the parties at the beginning of Microsoft's infringement. He arrived at the $200 million by using a royalty rate of $98 multiplied by the number of infringing Word products sold annually, which was 2.1 million.[53] He calculated the base royalty rate using an "appropriate benchmark" to value Microsoft's use of the claimed invention, and he chose a product called XMetaL, which has a retail price of $499, to determine the rate.[54] Dr. Wagner "multiplied the price of XMetaL ($499) by Microsoft's profit margin (76.6%)" and "applied the 25-percent rule to this number, which assumes the inventor will keep 25% of the profits from any infringing sales," resulting in a $96 base royalty rate.[55] Dr. Wagner then applied the factors set out in *Georgia-Pacific Corp. v. U.S. Plywood Corp.* to adjust the baseline royalty upward from $96 to $98.[56]

On appeal, Microsoft pointed to certain "weaknesses" in the damages calculation, but the Federal Circuit found that Microsoft's arguments questioned "Wagner's conclusions, not his methodology" and that *Daubert* and Rule 702 protect against "unreliable or irrelevant opinions" but are "not guarantees of correctness."[57] Based on this rationale, the court held that "the district court did not abuse its discretion in finding Wagner qualified to apply the methodology" because "Microsoft's quarrel with the facts Wagner used go to the weight, not admissibility, of his opinion."[58]

The Federal Circuit next addressed Microsoft's dispute concerning certain facts underlying the calculation of the reasonable royalty rate.[59] Microsoft disputed the relevancy of the i4i's chosen benchmark product, the resulting base royalty rate, and the survey utilized to estimate infringing use.[60] The court affirmed Dr. Wagner's calculus for choosing XMetaL as a benchmark, which included Microsoft's use of XMetaL prior to developing its own XML editor, the relatively inexpensive price of the product, and its identification as one of Microsoft's principal competitors in the custom XML market.[61]

The court also affirmed Dr. Wagner's conclusion that the value of the patented technology should be pegged to XMetaL's $499 retail price because Dr. Wagner's calculus "only considered users who really needed" the custom XML editor and would have purchased one commercially "despite any superfluous features," thus driving customer demand for the product.[62] The court next affirmed Dr. Wagner's use of the $96 base royalty rate as the start of his analysis. Dr. Wagner testified that he thought this value was necessary due to "Microsoft's business strategy," which involves sacrificing the price charged for incremental upgrades in order to maximize the sales of these products and "incentivize users to upgrade."[63]

Finally, the court affirmed the admission of the survey evidence offered by i4i, which was a conservative survey limited to "estimating infringing use by businesses." Dr. Wecker, i4i's survey expert, explained that his survey was a randomized survey of 988 large and small companies. He explained that he received 46 responses to the survey, with only 19 companies reporting using Word in an infringing manner. He then assumed that all non-responding companies did not use Word in an infringing manner. He thus was able to determine "that 1.9% (19/988) of all copies of Word sold to businesses between 2003 and 2008 were used in an infringing manner," and 1.9 percent of the sales amounted to "1.8 million infringing uses," which was adjusted to 2.1 million based on "infringing uses between the end of the survey and the start of trial."[64]

Based on its consideration of the facts underlying Dr. Wagner's opinion, the Federal Circuit found that "[t]he existence of other facts…does not mean that the facts used failed to meet the minimum standards of relevance and reliability" because under Rule 702 "the question is whether the expert relied on facts sufficiently related to the disputed issue," which was the calculation of a reasonable royalty for the '449 patent.[65] In finding that Dr. Wagner "based his calculation on facts meeting these minimum standards" and that "these facts had a sufficient nexus to the relevant market, the parties, and the alleged infringement," the court found "it is not the district court's role under *Daubert* to evaluate the correctness of facts underlying an expert's testimony."[66] The court stated that the appropriate means of testing questionable evidence is through the use of "vigorous cross examination, [the] presentation of contrary evidence, and careful instruction on the burden of proof."[67] Finding that Microsoft tested i4i's expert testimony, the Federal Circuit held "the district court did not abuse its discretion in admitting Wagner's expert testimony on damages."[68]

The court also affirmed i4i's use of survey evidence, holding that "the district court did not abuse its discretion in admitting the survey" because "[g]iven the survey's importance, evidence about its methodology and findings could certainly help the jury evaluate the expert testimony."[69]

Implications for the Entire Market Value Rule. The Federal Circuit held that Dr. Wagner's calculation of the base royalty rate using the price of a competitor's commercial product was admissible. In reaching this holding, the court applied the standard used in entire market value rule cases, which allows a plaintiff to use the value of an entire product to calculate its base royalty if the plaintiff can show that the patented technology is the basis for customer demand. Absent such proof, as discussed above, courts will not hesitate to reject damages based on the entire market value rule.

Post-*i4i* plaintiffs will be able to offer evidence valuing the patented technology based on either the allegedly infringing product *or* a competitor's existing commercial application of similar technology. Plaintiffs may want to consider whether "similarity" will be enough versus a test more analogous to license comparison—"comparability." Perhaps "sufficiently comparable" versus "similar" technology.

The $200 Million Damages Award. In attempting to rein in the perceived excesses in patent damages awards, courts evaluate the reasonableness of damages awards in view of the sufficiency of the evidence in support of the awarded amount. The most important factor in each of these cases is the party's preservation of its right to challenge the sufficiency of the evidence by filing for a pre-verdict JMOL on damages or otherwise properly reserving its right to appeal. The *i4i* case will serve as a cautionary tale for the unwary counsel who fails to fully realize until it is too late the implication of certain strategic decisions made at trial.[70]

The Federal Circuit affirmed the district court's $200 million damages award, expressly rejecting Microsoft's argument that the court should reduce the award by following its recent decision in *Lucent Technologies, Inc. v. Gateway, Inc.*[71] The Federal Circuit held that Microsoft "waived its ability" to challenge the sufficiency of the evidence "because Microsoft did not file a pre-verdict JMOL on damages."[72]

Based on the procedural posture of the case, the Federal Circuit reviewed Microsoft's reasonableness argument under the "highly deferential" and "much narrower" standard applied to denials of motions for a new trial, which allows for the damages award to be set aside "only upon a *clear showing* of excessiveness."[73] To make this showing the appellant has to prove that the damages award "exceed[s] the maximum amount calculable from the evidence."[74] In addition, under this deferential standard, the court must affirm the judgment unless the appellant can show that "there was no evidence to support the jury's verdict."[75]

Finding that the damages award was "supported by the evidence presented at trial," the Federal Circuit held that "[g]iven the intensely factual nature of a damages determination and our deferential standard of review, we are not in a position to second-guess or substitute our judgment for the jury's."[76]

The $40 Million Enhanced Damages Award. Microsoft also appealed the district court's decision to grant enhanced damages under 35 U.S.C. § 284. Finding that the factors in *Read Corp. v. Portec, Inc.*[77] supported enhancement, the Federal Circuit held that "[o]n this record, we cannot conclude that the district court abused its discretion in weighing the evidence or applying the *Read* factors."[78] The court found that "the standard for deciding whether—and by how much—to enhance damages is set forth in *Read*, not *Seagate*[,]" and "[u]nder the *Read* factors the district court properly considered Microsoft's size and financial condition, as well as whether Microsoft investigated the scope of the patent."[79] In addition, the court held that while it is "improper to enhance damages based solely on litigation misconduct, …the district court considered Microsoft's litigation misconduct only after finding that the other *Read* factors favored enhanced damages[.]"[80]

III. Injunctions and Ongoing Royalties after *eBay*

In *eBay Inc v. MercExchange, LLC*,[81] the Supreme Court held that patentees are not automatically entitled to the entry of a permanent injunction against future infringement by parties adjudged to be past infringers.[82] Instead, district courts are to consider requests for injunctions under the traditional four-factor test, evaluating irreparable harm, the adequacy of legal remedies, the balance of hardships, and the public interest. In his concurring opinion, Justice Kennedy noted that injunctions may not be appropriate in suits brought by "firms [that] use patents not as a basis for producing and selling goods but, instead, primarily for obtaining licensing fees."[83]

Indeed, in the early post-*eBay* cases, courts generally have followed Justice Kennedy's suggestion, denying injunctions to non-practicing entities and instead ordering infringers in those cases to pay ongoing royalties for their continued infringement.[84] In recent cases, however, courts have not hesitated to deny both an injunction and future royalties absent proof of entitlement, irrespective of whether the parties are competitors.[85] Since *eBay*, based on the authors' research, there have been decisions addressing permanent injunctions in 108 patent infringement actions. Injunctions were granted in 70 of those actions: 63 injunctions when the parties were competitors and 7 when the parties were not competitors. The following discussion, which focuses on how courts recently have determined an appropriate ongoing royalty rate, demonstrates that reasoning particular to the circumstances of the case must support an ongoing royalty rate.

A. *Paice*: Sufficient Reasoning Required for Ongoing Royalty Rate

In *Paice LLC v. Toyota Motor Corp.*, the Federal Circuit affirmed that a district court may impose an ongoing royalty where it finds that a permanent injunction is not appropriate, but only if the court has sufficient evidence and reasoning to support the royalty rate.[86] In *Paice*, the district court, sua sponte, imposed an ongoing royalty calculated by dividing the jury's award for past damages by the number of infringing cars sold, to establish a $25 per car royalty.[87] On appeal, Paice argued that the district court did not have authority to set an ongoing royalty, and if it did, the Seventh Amendment required a jury trial to determine the amount of damages.[88]

The Federal Circuit first emphasized that ongoing royalties should not be the "matter of course whenever a permanent injunction is not imposed" but may be necessary in some cases.[89] With respect to the district court's $25 per car rate, the Federal Circuit remanded, noting that the district court had failed to explain its reasoning for settling on that rate. Although noting that the district court could "allow the parties to negotiate a license amongst themselves," the Federal Circuit remanded to give the district court a chance to receive additional evidence, reevaluate the ongoing royalty rate, and provide its reasoning.[90] As for Paice's Seventh Amendment argument, the court found Paice had failed to demonstrate the constitutional requirement of a jury, since "not all monetary relief is properly characterized as 'damages.'"[91]

Judge Rader, concurring, argued that rather than allowing negotiation between the parties, the court "should require the district court to remand this issue to the parties, or to obtain the permission of both parties before setting the ongoing royalty rate itself."[92] He noted that all the evidence presented at trial addressed "Toyota's past infringement" instead of damages for post-judgment acts of infringement.[93] Thus, because "pre-suit and post-judgment acts of infringement are distinct, [these activities] may warrant different royalty rates given the change in the parties' legal relationship and other factors."

Determining an ongoing royalty rate on remand, the court used a modified *Georgia-Pacific* analysis that preserved the fictional hypothetical negotiation between a willing licensor and willing licensee and focused only on the *Georgia-Pacific* factors that were most applicable to the circumstances surrounding an ongoing royalty rate.[94] The court acknowledged that "a post-judgment ongoing royalty negotiation is logically different from the pre-trial hypothetical negotiation discussed in *Georgia-Pacific*," as the "willing licensee" has become an adjudged infringer.[95]

The court imposed a new, increased ongoing royalty rate of $98 per vehicle and based the increase largely on changed legal and factual circumstances of the two parties, namely the verdict of infringement and increased demand for hybrid vehicles.[96] Rejecting Toyota's position that the royalty for post-judgment infringement should be equal to that pre-judgment, the court explained that the parties' bargaining positions had changed, and "injunction or no injunction, pre-suit and post-judgment licensing negotiation are necessarily different" primarily because "ongoing infringement by the adjudged infringer is willful."[97]

Considering a variety of new evidence, the court concluded that the "changed factual and legal circumstances…justified application of the 25% Rule of Thumb to Toyota's profit margin of 9%, thereby yielding a royalty rate of 2.25%."[98] However, based on the lower rate the jury awarded and the fact that Toyota makes less profit from hybrid vehicles than non-hybrids, the court reduced this rate by 1/3 to 1.5%. Using the accused vehicle's hybrid powertrain as the royalty base (valued at $6,500 per-vehicle), the court opted for a reasonable ongoing royalty rate of $98.[99]

B. *Amado*: Royalty Should Account for Changed Circumstances

Further informing the district court's analysis of *Paice* on remand was the Federal Circuit's 2008 decision in *Amado v. Microsoft Corp.* In *Amado*, the court reiterated that a district court must articulate reasoning for setting a particular royalty rate that takes into account all of the case's unique circumstances, particularly Judge Rader's pre-verdict/post-verdict distinction.[100] After staying an injunction pending appeal, the district court had set an amount in escrow that was triple what the jury had found for post-injunction infringement.[101] Since the escrow award "did not expressly consider that Microsoft's infringing sales took place following the grant of an injunction that was stayed," the Federal Circuit remanded the case, instructing the district court to provide a full explanation of its reasons for setting a particular royalty rate.[102]

When a district court decides that an injunction is warranted, even if that injunction is stayed pending appeal, the Federal Circuit stated, "the assessment of damages for infringements taking place after the injunction should take into account the change in the parties' bargaining positions, and the resulting change in economic circumstances, resulting from the determination of liability…as well as the evidence and arguments found material to the granting of the injunction and the stay."[103] Such "resulting change[s] in economic circumstances" include "the infringer's likelihood of success on appeal, the infringer's ability to immediately comply with the injunction, the parties' reasonable expectations if the stay was entered by consent or stipulation, etc."[104]

C. Ongoing Royalty Calculations After *Paice* and *Amado*

There have been few published decisions discussing the calculation of ongoing royalties after an injunction has been denied, possibly because parties have heeded Judge Rader's "advice" in *Paice* and negotiated an appropriate royalty rate.[105] Not surprisingly, such negotiations are often fruitless, and the court ends up setting the rate.

In determining an appropriate ongoing royalty rate in *Boston Scientific Corp. v. Johnson & Johnson*,[106] the court began with the assumption that the jury's finding of liability "would have strengthened Cordis' [the successful counterclaim plaintiff] bargaining position had the parties negotiated a license agreement after the jury verdict."[107] Although the court agreed with the district court's conclusion after remand in *Amado* that a strict application of *Georgia-Pacific* factors should not be used in determining a post-infringement royalty rate, as it would "'run [] the risk of skewing the analysis towards a pre-judgment framework' in contravention of the Federal Circuit's mandate,"[108] because "both experts…framed their analysis in terms of those factors," the court decided to use the *Georgia-Pacific* factors but to consider whether certain factors should be weighed differently in the context of post-verdict royalties.[109] After the hypothetical negotiation analysis resulted in a range of 5.1 percent to 14.8 percent, the court considered eight other *Georgia-Pacific* factors[110] to arrive at an ongoing royalty rate of 5.1 percent.

A 23 percent ongoing royalty was awarded in *Creative Internet Advertising Corp.v. Yahoo! Inc.*[111] After a trial in the Eastern District of Texas, where a jury awarded Creative Internet damages based on a 20 percent royalty rate, the court denied the plaintiff's request for a permanent injunction. Creative Internet then filed a motion for ongoing royalties, which Yahoo! opposed on the ground that it had removed the infringing portion of its Yahoo! Messenger program. Deeming the issue of "determining an ongoing royalty when Defendant argues that infringement has stopped"[112] to be one of first impression, the court "looked to analogous factual situations where the plaintiff requests an injunction that protects its right to exclude the adjudicated product, as well as 'colorable variations thereof.'"[113]

The court found that Creative Internet had the burden of proving that the new version of the Yahoo! Messenger was no more than a "colorable variation" of the older infringing product.[114] After reviewing both parties' arguments, the court ruled that "the 'logic' underlying the 'new' Messenger version continues to fall within the scope of the adjudicated product"[115] and that Yahoo! therefore had to pay an ongoing royalty.

The court then applied the modified *Georgia-Pacific* analysis used in *Paice* to arrive at the ongoing royalty rate. Factors considered by the court in increasing by 3 percent the rate awarded at trial included the change in legal relationship between the parties, Yahoo!'s decision not to design around or otherwise stop infringing, and the Federal Circuit's "instruct[ion] that post-verdict infringement should typically entail a higher royalty rate than the reasonable royalty found at trial."[116]

In *Presido Components Inc. v. American Technical Ceramics Corp.*[117] the court reluctantly examined certain *Georgia-Pacific* factors, finding that only Factor 3 (nature and scope of the license) and Factor 4 (the licensor's established licensing policy) were anything other than neutral.[118] The court awarded an ongoing royalty rate of 12 percent in light of the verdict of liability and "because granting a license would require Presidio to give up its valuable business consideration of refusing to license the *'356 patent* as well as the right to offer an exclusive license to a third party in the future."[119] Although at trial Presidio was awarded lost profits, the court noted that "had it been faced with [a reasonable royalty] issue at trial, it very well may have been inclined to adopt a figure somewhere between the 2 to 4% rate suggested by [defendant] and the 12% rate suggested by Presidio."[120]

With respect to the ongoing royalty rate, the court held that any "rate below 12% will give [defendant], who is now a willful infringer, a windfall at Presidio's expense. On the other hand, the Court is not convinced that the parties' positions warrant a departure from what Presidio's own damages expert considered to be a reasonable rate pre-trial."[121]

After failed negotiations *Soverain Software LLC v. Newegg Inc.*,[122] Eastern District of Texas Judge Davis considered the following factors in setting an ongoing royalty rate: Newegg's willful continued infringement; Newegg's becoming "the second largest online-only retailer and announcing its plans for an initial public offering"; the costs of Newegg's proposed design-around; and Soverain's successful expansion of its licensing program.[123] Although the court found that the parties' changed financial positions "appear to cancel each other out because each party is more successful today than they were at the time of the hypothetical negotiation, [it could not] ignore Newegg's adjudged infringer status in determining an appropriate ongoing royalty."[124]

In arriving at an appropriate rate, the court used Soverain's proposal of $0.20 as a starting point. "Even taking into account Newegg's adjudged infringer status, the jury's award of only $0.088 per transaction (1.88% of Newegg's profits) counsels against an ongoing royalty of $0.20 per transaction (4.27% of Newegg's profits)."[125] As Soverain did not account for Newegg's proposed design-arounds in its $0.20 proposal, the court reduced Soverain's proposal by 25 percent and concluded that $0.15 per transaction was an appropriate ongoing royalty.[126]

IV. Changes in Settlement Negotiations Resulting from *Quanta*

The Supreme Court's recent decision in *Quanta Computer, Inc. v. LG Electronics, Inc.*[127] held that the exhaustion doctrine blocked LG's infringement suit against third-party computer manufacturers because LG had "authorized" the manufacturers' supplier, Intel Corporation, to sell LG's patented technology.[128] The opinion has had a noticeable effect on patent settlement and licensing negotiations.

In *Quanta*, the Supreme Court addressed two issues regarding the patent exhaustion doctrine: (1) whether the doctrine applies to method patents and (2) to what extent a product must embody a patent in order to trigger the doctrine.[129] LG licensed a portfolio of patents to Intel allowing Intel to manufacture and sell computer parts using LG patents.[130] Computer manufacturers, including Quanta Computer (collectively Quanta), purchased computer parts from Intel.[131] When LG sued Quanta for infringement, Quanta countered that the doctrine of exhaustion—"the traditional bar on patent restrictions following the sale of an item"[132]—should block the action.[133] The Federal Circuit held that exhaustion did not apply to method patents[134] and, alternatively, that exhaustion "did not apply because LG did not license Intel to sell the Intel Products to Quanta for use in combination with non-Intel products."[135]

The Supreme Court unanimously reversed, holding that patent exhaustion applied to method patents and that exhaustion applies if a third party uses a technology in a way that "substantially embodies" the method patents held by the patent holder.[136] It did not matter whether Quanta's final step involved adding or removing material as long as the final step was "common and noninventive."[137]

Importantly, the Court found that exhaustion applied "[b]ecause Intel was authorized to sell its products to Quanta."[138] Specifically, LG "authorized" Intel to sell its products embodying the LG patents, and "[n]othing in the license agreement restricts Intel's right to sell its microprocessors and chipsets to purchasers who intend to combine them with non-Intel parts."[139] Although the LG-Intel agreement required Intel to give notice to customers that LG did not license those customers to practice LG's patents, LG never alleged a breach of that provision.[140] Whether Quanta received implied licenses to the LG patents was "irrelevant," since Quanta asserted "its right to practice the patent based not on implied license, but exhaustion. And exhaustion turns only on Intel's own license to sell products practicing the LG Patents."[141] The Court explicitly did not express an opinion on whether LG could recover contract damages.[142]

When licensing a patent or portfolio in either commercial or litigation contexts, it is common for the licensee to seek an "end-to-end" license. This is a license that protects the licensee's supply chain—manufacturers, vendors, component makers—and distribution chain—distributors, customers, etc. In crafting license grants that reasonably allow the licensee to make the licensed product or have it made and then sold through its distribution channels to end users, many licensors have become concerned about generally "authorizing" such third parties under *Quanta*.

The concern reduces to whether a licensor can allow a distributor to sell the licensed products that licensee "A" provides to the distributor without generally inoculating that distributor under the licensed patents when selling products that others manufacture. There are ways to guard against such unintended consequences in a license scenario, including limited authorization clauses and the like, and a seasoned practitioner will likely be aware of other paths. This article merely identifies this potential licensing pitfall, as the unwary can potentially authorize a much broader array of downstream activities, with significant financial implications.

V. Use of Settlement Negotiations and License Agreements to Determine a Reasonable Royalty

In *ResQNet.com, Inc. v. Lansa*[143] the Federal Circuit vacated a damages award as "inconsistent with sound damages jurisprudence" because "the district court's award relied on speculative and unreliable evidence divorced from proof of economic harm linked to the claimed invention…."[144]

Although a reasonable royalty is derived from a hypothetical negotiation between the parties, the court stated that the district court's reasonable royalty analysis requires it to "hypothesize, not to speculate."[145] This analysis should "concentrate on compensation for the economic harm caused by infringement of the claimed invention."[146] The Federal Circuit found that the evidence "unrelated to the claimed invention does not support compensation for infringement."[147]

The court determined that the bulk of the licenses relied on by ResQNet's damages expert were problematic, stating that he "used licenses with no relationship to the claimed invention to drive the royalty rate up…."[148] The court expressly rejected the district court's consideration of five of the licenses, which it described as "re-bundling licenses," because these licenses "furnished finished software products and source code, as well as services such as training, maintenance, marketing, and upgrades…."[149] The court also observed that none of those licenses "mentioned the patents in suit or showed any other discernible link to the claimed technology."[150] The court concluded that "[i]n simple terms, the '075 patent deals with a method of communicating between host computers and remote terminals—not training, marketing, and customer support services. The re-bundling licenses simply have no place in this case."[151]

The court rejected the use of such "speculative evidence" to calculate a reasonable royalty, holding that "the district court erred by considering ResQNet's re-bundling licenses to significantly adjust upward the reasonable royalty without any factual findings that accounted for the technological and economic differences between those licenses and the '075 patent."[152] The court observed that "the most reliable license in this record arose out of litigation."[153] While citing its jurisprudence recognizing the "skew[ed]" royalty rates that often result from licensing agreements arising out of litigation,[154] the court nevertheless indicated that, on remand, the district court should "consider the panoply of 'events and facts that occurred thereafter and that could not have been known to or predicted by the hypothesized negotiators.'"[155] In so doing, the court effectively suggested that the district court take into consideration the litigation-based license in recalculating a reasonable royalty.[156]

In dissent, Judge Newman disagreed that the licenses relied upon by the plaintiff's expert were insufficiently related to the technology at issue to support the expert's proposed royalty rate.[157] He further opined that the majority's suggestion that the district court could rely upon a settlement agreement to determine a royalty risked the possibility that putative infringers will elect to infringe as "a handy means for competitors to impose a 'compulsory license' policy upon every patent owner," and he stated that the majority's holding did not comport with the theory of the hypothetical negotiation.[158]

In June 2010, the Federal Circuit, citing *Lucent* and *ResQNet*, reiterated that the first *Georgia-Pacific* factor requires comparisons of past licenses to the infringement to account for the technological and economic differences between them and rejected a lump sum award that was unsupported by any of the thirteen licenses offered at trial.[159]

District courts considering the question have reached different conclusions regarding the admissibility of settlement agreements. The Eastern District of Texas has issued several decisions on this issue. In *IP Innovation LLC v. Red Hat, Inc.* Chief Judge Rader, sitting by designation, rejected the expert's reliance on industry licenses that encompass "much more than the desktop switching feature at issue in this case…[and where there is no evidence that they] are in any way comparable to the patents-in-suit."[160]

In *Tyco Healthcare Group LP v. E-Z-EM, Inc.*,[161] Judge Ward determined that the *ResQNet* decision "cause[d] the Court to shift its approach toward the discoverability of settlement negotiations," and he ordered the production of documents relating to settlement negotiations that could inform the calculation of a reasonable royalty.[162] While Judges Davis and Folsom have reached the same conclusion based on the facts presented to them,[163] Magistrate Judge Love granted two motions seeking to exclude evidence of settlement agreements, finding that the agreements in question would be unduly prejudicial to the plaintiff and that *ResQNet* did not alter the pre-*ResQNet* approach of generally disallowing the use of settlement negotiations to determine a reasonable royalty rate.[164]

Courts outside the Eastern District of Texas also have grappled with nuances of this issue. In an unpublished decision out of the Northern District of Illinois in *Abbott Laboratories v. Sandoz, Inc.*,[165] Sandoz claimed that Abbott's damages expert put in issue three settlement agreements allowing generic versions of the drug to be sold royalty-free by stating that he considered the agreements when conducting his damages analysis. Relying on *Century Wrecker Corp. v. E.R. Buske Mfg.*,[166] the court denied Abbott's motion to bar production of these agreements, finding that since the plaintiff's expert specifically relied upon the settlement agreements in his damages calculation, Sandoz could present those agreements to rebut Abbott's expert.[167] Recently, in *Phillip M. Adams & Associates, LLC v. Asustek Computer, Inc.*,[168] on a motion by the defendants to exclude a consent judgment entered into by Sony with respect to infringement issues, the plaintiff argued that the defendants put the judgment in issue, as their experts' reports relied upon prior settlement agreements to show they did not establish a royalty rate for the patent at issue.[169] Although the Utah court excluded the objected-to portions of the judgment, it agreed with the plaintiff and held that "if such arguments are raised by Defendants at trial, Plaintiff is entitled to explore why the Sony settlement and license supports its theory of damages."[170]

Regardless of whether the district courts construe the holding of *ResQNet* broadly or narrowly, the decision has opened the door to consideration of settlement agreements in calculating a reasonable royalty, and this type of evidence is likely to become increasingly important in the damages phase of patent infringement cases.[171]

VI. False Patent Marking Damages

Section 292 of the Patent Act provides that "[w]hoever marks upon, or affixes to, or uses in advertising in connection with any unpatented article, the word 'patent' or any word or number importing that the same is patented for the purpose of deceiving the public…shall be fined not more than $500 for every such offense."[172] Historically, courts have differed over what constitutes each "offense" authorizing the fine of up to $500.

On one end of the spectrum, some courts have construed "offense" broadly and imposed only a single $500 fine, regardless of the number of falsely marked articles.[173] On the opposite end of the spectrum, some courts have imposed a $500 fine for each falsely marked article, creating the potential for enormous damages awards.[174] Many courts have fallen somewhere in the middle, assessing more than a single $500 fine but not imposing a separate fine for each falsely marked article. For example, courts have held that the defendant's continuous act of falsely referring to its product as patented over a period of over 10 years warranted a $325,000 fine, calculated by the number of weeks (650) times $500 each.[175] Likewise, one court imposed a fine for each shipment of falsely marked goods.[176]

In 2008 in *The Forest Group, Inc. v. Bon Tool Co.*, the Southern District of Texas decided that "continuous markings" over a given time count as one offense only, meaning a plaintiff could only recover a maximum of $500.[177] In deciding damages for false marking, the court found the First Circuit's 1910 decision in *London v. Everett H. Dunbar Corp.* persuasive.[178] *London* had reasoned that Congress could not have intended a greater fine for falsely marking many small items than for falsely marking a limited number of expensive items.[179] The court concluded that Congress did not intend "that penalties should accumulate as fast as a printing press or stamping machine might operate."[180] Agreeing with *London*, the *Forest Group* court granted Bon Tool a penalty of only $500 because Forest "made a single decision to mark its non-conforming [items]."[181]

On appeal, the Federal Circuit reversed, finding that every article falsely marked with an inapplicable patent number constitutes a discrete "offense" under the statute.[182] The court recognized that its decision might prompt a "cottage industry" among plaintiffs seeking large false-marking damages, but it also pointed to the district courts' statutory discretion to set the amount of the fine per offense.[183] According to the Federal Circuit, this grant of discretion to the district courts allowed them "to strike a balance between encouraging enforcement of an important public policy and imposing disproportionately large penalties for small, inexpensive items produced in large quantities."[184]

On remand, the district court in *Forest Group* fined the defendant $180 for each of 38 articles falsely marked. In reaching the $180 figure, the court opted to fine the defendant the maximum amount charged by the defendant for each of the falsely marked products, reasoning that the total amount of the fine would serve the purpose of deterring the defendant (and others) from engaging in future false marking.[185]

Well over 400 false marking suits have been filed since *Forest Group* by putative plaintiffs in search of large damages awards, and the Federal Circuit's June 10, 2010 decision in *Pequignot v. Solo Cup Co.*,[186] which clarified a higher standard of wrongful intent to prove false marking,[187] has apparently not quelled such filings. In fact, the Federal Circuit's August 31, 2010 ruling that to prove standing a plaintiff need not allege any injury to any identifiable person but rather must allege merely that the defendant's conduct violated the false marking statute,[188] has led to a significant spike in filings. The short-term effects of these decisions has led to differing decisions across the country, but hopefully the passage of time, and possibly Congressional reform, will provide clearer guidance for courts and litigants alike.

VII. Patent Damage Reform Legislation

In March 2009, Congressional sponsors introduced identical patent reform legislation in both the House and Senate, including several proposals to amend patent damages law.[189] These bills, known as the Patent Reform Act of 2009, attempt, *inter alia*, to codify the entire market value rule and a rule for calculating reasonable royalties that looks at the price of licensing "similar non-infringing substitutes in the relevant market," but these provisions were subsequently struck from the Senate's version of the bill.[190]

As of June 2009, provisions in the bill would codify that proof of willful infringement "may increase damages up to 3 times the amount of damages found."[191] An infringer has acted willfully only if the patentee "proves by clear and convincing evidence" that the infringer acted with objective recklessness by continuing infringement after receiving sufficient written notice from the patentee, intentionally copying technology with knowledge of a patent, and continuing conduct post-infringement verdict that is not colorably different from pre-verdict conduct.[192]

In other remaining provisions, the legislation prescribes a procedure meant to give judges a broader role in identifying the legal standards for calculating damages that the court will present to the jury.[193] This procedure requires the court to identify the "methodologies and factors" relevant to determining damages.[194] The factfinder may consider only these factors when determining damages.[195] Before trial, the parties must submit their proposed factors for jury instructions "in writing and with particularity…specifying the relevant legal and factual bases for their assertions."[196] Before introducing any evidence, the court, "by motion of either party or sua sponte," must decide whether a given factor has a "legally sufficient evidentiary basis."[197] The court may only permit evidence relevant to the factors the court "determines may be considered in making the damages determination."[198]

VIII. Conclusion

The Federal Circuit is gradually holding patentees to more rigorous standards of proof in claiming large damages awards in patent infringement cases. Certainly, erasing the "entire market value rule" altogether will be a difficult and perhaps unnecessary jurisprudential task, effectively undoing decades of precedent. As such, it will be interesting to see if and how the Federal Circuit continues to narrow application of the rule to ameliorate the excesses many judges and practitioners have observed in recent damages awards.

Endnotes

1. *eBay Inc. v. MercExchange, LLC*, 547 U.S. 388 (2006).
2. *Quanta Computer, Inc. v. LG Elec., Inc.*, 553 U.S. 617, 128 S. Ct. 2109 (2008).

3. *King Instruments Corp. v. Perego*, 65 F.3d 941, 951 n.4 (Fed. Cir. 1995).

4. *Federal Circuit Chief Judge Challenges Testimony at Congressional Hearings on Patent Reform*, Patent, Trademark & Copyright Daily (May 15, 2009).

5. *Cornell Univ. v. Hewlett-Packard Co*., 609 F. Supp. 2d. 279, 286 (N.D.N.Y. 2009) (citations omitted).

6. 543 F.3d 710 (Fed. Cir. 2008).

7. *Id.* at 716-17. The Federal Circuit did not reach the damages issue because it affirmed the JMOL on other grounds.

8. *Id.*

9. *Lucent Techs. Inc. v. Gateway, Inc*., 509 F. Supp. 2d 912, 935 (S.D. Cal. 2007) (quoting *Rite-Hite Corp. v. Kelley Co., Inc.*, 56 F.3d 1538, 1549 (Fed. Cir. 1995)), *aff'd*, 543 F.3d 710 (Fed. Cir. 2008).

10. *Id.*

11. *Cornell Univ*., 609 F. Supp. 2d at 286.

12. *Id.*

13. *Id.*

14. *Id.*

15. *Id.*

16. *Id.*

17. *Id.*

18. 2010 U.S. Dist. LEXIS 28372 (E.D. Tex. Mar. 2, 2010).

19. *Id.* at *7. The court also court noted that Mr. Gemini's testimony should have been excluded because "he arbitrarily picked a royalty rate that is much higher than the existing royalty rates for licenses to the patents-in-suit…. At least two of these agreements were entered into outside of the context of litigation and thus appropriate as touchstones for determining the appropriate royalty rate in this case. Mr. Gemini disregarded these licenses because Xerox [the previous owner of the patent] entered into these agreements in the mid-1990's, a decade before the alleged hypothetical negotiation date. However, these licenses are far more relevant than the general market studies on which Mr. Gemini primarily relied in his expert report." *Id.* at *10-*11.

20. Memorandum Opinion and Order, Civil Action No. 6:08-CV-273 (E.D. Tex. Apr. 16, 2010).

21. *Id.* at 2-3.

22. 2010 U.S. Dist. LEXIS 56634 (E.D. Tex. June 9, 2010).

23. *Id.* at *10.

24. *Id.*

25. *Id.*

26. *Id.* The court did uphold the royalty rate for the disk drives, however, finding them to not be "clearly excessive." Applying the royalty rate to the disk drives only, the court remitted the damage award to $6.2M. *Id.* at *13.

27. 2010 U.S. App. LEXIS 18237 (Fed. Cir. Sept. 1, 2010).

28. *Id.* at *43.

29. Order, Civil Action NO. 06-cv-100-JD (D. N.H. Aug. 3, 2010).

30. *Id.* at 9-10.

31. 2010 U.S. Dist. LEXIS 7197 (D. Del. Jan. 28, 2010).

32. *Id.* at *11.

33. *American Seating Co. v. USSC Group, Inc*., 514 F.3d 1262, 1268 (Fed. Cir. 2008) (quoting *Rite-Hite Corp. v. Kelley Co. Inc.,* 56 F.3d 1538, 1550 (Fed. Cir. 1998)).

34. 56 F.3d 1538 (Fed. Cir. 1998).

35. *American Seating*, 514 F.3d at 1268 (citing *Rite-Hite*, 56 F.3d at 1550).

36. *Id.* at 1266.

37. *Id.* at 1269.

38. Erin Coe, *Fed. Circ. May Take Damages Issue Into Own Hands*, Law 360 (July 21, 2009).

39. *Id*.

40. *See Lucent Techs., Inc. v. Gateway, Inc.*, 580 F.3d 1301 (Fed. Cir. 2009). Chief Judge Michel authored the opinion.

41. *Id.* at 1332.

42. *Id.*; *see also id.* at 1337-38 ("Consistent with this description of Outlook, Lucent did not carry its evidentiary burden of proving that anyone purchased Outlook because of the patented method.").

43. *Id.* at 1335.

44. *Id.* at 1340. Microsoft petitioned for a writ of certiorari on other grounds, which the Supreme Court denied on May 24, 2010. *Microsoft Corp. v. Lucent Techs., Inc.*, 130 S. Ct. 3324 (2010).

45. *See* Lisa M. Tittemore, *Federal Circuit Holds Litigants to Strict Evidentiary Standards in Proving Patent Infringement Damages*, Sunstein Intellectual Property Update (Sept. 2009), *available at* http://www.sunsteinlaw.com/publications-news/news-letters/2009/09/200909_Tittemore.html.

46. 598 F.3d 831 (Fed. Cir. 2010). The Federal Circuit rendered an initial decision in this case on December 22, 2009, at 589 F.3d 1246. On March 10, 2010 and after rehearing, the court withdrew its first opinion and substituted the decision at 598 F.3d 831. The substituted opinion contains an additional section addressing Microsoft's challenge to the district court's denial of a post-trial motion for judgment as a matter of law on the evidentiary sufficiency of the jury's finding of willful infringement. *See* 598 F.3d at 859-60 (including new Section VI entitled "Willfulness"). The court denied Microsoft's petition for rehearing en banc on April 1, 2010, and Microsoft requested and received from the Supreme Court on June 14, 2010 an extension of time through August 27, 2010 to file a petition for a writ of certiorari. On August 27, 2010, Microsoft filed a petition for a writ of certiorari with the Supreme Court after the Federal Circuit denied its request for an en banc rehearing.

47. 598 F.3d at 839.

48. *Id*.

49. *Id*.

50. An expert witness with "scientific, technical, or otherwise specialized knowledge," may testify and form an opinion "if (1) the testimony is based on sufficient facts or data, (2) the testimony is the product of reliable principles and methods; and (3) the witness has applied the principles and methods reliably to the facts of the case." Fed. R. Evid. 702 (*quoted in i4i*, 598 F.3d at 852 n.2).

51. 509 U.S. 579 (1993).

52. *Id.* at 589 (*quoted in i4i*, 598 F.3d at 852).

53. *i4i*, 598 F.3d at 852-53.

54. *Id.* at 853.

55. *Id*.

56. *Id.* at 853-54; *see also Georgia-Pacific Corp. v. U.S. Plywood Corp.*, 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970), cited in *i4i*, 598 F.3d at 853 n.3 ("These factors include: (1) royalties the patentee has received for licensing the patent to others; (2) rates paid by the licensee for the use of comparable patents; (3) the nature and scope of the license (exclusive or nonexclusive, restricted or nonrestricted by territory or product type); (4) any established policies or marketing programs by the licensor to maintain its patent monopoly by not licensing others to use the invention or granting licenses under special conditions to maintain the monopoly; (5) the commercial relationship between the licensor and licensee, such as whether they are competitors; (6) the effect of selling the patented specialty in promoting sales of other products of the licensee; (7) the duration of the patent and license term; (8) the established profitability of the product made under the patent, including its commercial success and current popularity; (9) the utility and advantages of

the patent property over old modes or devices; (10) the nature of the patented invention and the benefits to those who have used the invention; (11) the extent to which the infringer has used the invention and the value of that use; (12) the portion of profit or of the selling price that may be customary in that particular business to allow for use of the invention or analogous inventions; (13) the portion of the realizable profit that should be credited to the invention as opposed to its non-patented elements; (14) the opinion testimony of qualified experts; and (15) the results of a hypothetical negotiation between the licensor and licensee.").

57. *i4i*, 598 F.3d at 854.
58. *Id*.
59. *Id*.
60. *Id*.
61. *Id*.
62. *Id*. at 854-55.
63. *Id*. at 855.
64. *Id*.
65. *Id*. at 855-56.
66. *Id*. at 856.
67. *Id*.
68. *Id*.
69. *Id*.
70. *See also Wordtech Systems v. Integrated Networks Solutions, Inc.*, 2010 U.S. App. LEXIS 12260 (Fed. Cir. June 16, 2010) (finding waiver of right on appeal to claim that evidence was insufficient to support a finding of any "hypothetical royalty" or to establish "the amount of [defendant's] sales revenues" because the issue was not raised before the district court).
71. 580 F.3d 1301 (Fed. Cir. 2009), *cited in i4i*, 598 F.3d at 856-57.
72. *i4i*, 598 F.3d at 856-57.
73. *Id*. at 857 (emphasis in original) (citation omitted).
74. *Id*.
75. *Id*.
76. *Id*. at 858.
77. 970 F.2d 816 (Fed. Cir. 1992).
78. *i4i*, 598 F.3d at 858.
79. *Id*. at 859 (citing *In re Seagate Tech., LLC*, 497 F.3d 1360, 1371 (Fed. Cir. 2007)).
80. *Id*.
81. 547 U.S. 388 (2006).
82. *Id*.
83. *Id*. Justice Kennedy also noted that injunctions might not be appropriate "when the patented invention is but a small component of the product the companies seek to produce and the threat of an injunction is employed simply for undue leverage in negotiations."
84. Erin Coe, *Injunctions Harder to Win In Post-EBay Courts*, LAW 360 (Jan. 26, 2009); *but see Commonwealth Sci. and Indus. Research Org. v. Buffalo Tech. Inc*., 492 F. Supp. 2d 600, 605 (E.D. Tex. 2007) (awarding injunction to research institution, a non-practicing entity); *Kowalski v. Mommy Gina Tuna Res.*, 2009 U.S. Dist. LEXIS 26216 (D. Haw. Mar. 30, 2009) (injunction granted despite plaintiff not practicing the patent or having a history of licensing or litigating the patent).
85. *See, e.g., IGT Corp. v. Bally Gaming Int'l*, 2009 U.S. Dist. LEXIS 120065 (D. Del. Dec. 22, 2009); *Medtronic Sofamor Danek USA v. Globus Med., Inc.*, 2009 U.S. Dist. LEXIS 61332 (E.D. Pa. July 17, 2009).
86. *Paice LLC v. Toyota Motor Corp*., 504 F.3d 1293, 1315 (Fed. Cir. 2007).
87. *Id.* at 1303, 1314. *See also Paice LLC v. Toyota Motor Corp*., 609 F. Supp. 2d 620, 625 (E.D. Tex. 2009) (describing the court's reasoning in setting a $25 royalty rate).
88. *Id.* at 1316.
89. *Id.* at 1314-15.
90. *Id.*
91. *Id.* at 1316 (citing *Root v. Ry*., 105 U.S. 189, 207 (1881) (prohibiting court from assessing damages but allowing court to require an accounting of profits)); *cf. Bowen v. Massachusetts*, 487 U.S. 879, 910 (1988) (construing payment of money as not being "money damages" because they were "specific relief").
92. *Id.* at 1316 (Rader, J., concurring).
93. *Id.* at 1317.
94. *Paice*, 609 F. Supp. 2d at 624.
95. *Id.*
96. *Paice*, 609 F. Supp. 2d at 625 (citing the increased advantage of hybrid technology due to rising oil prices and new fuel efficiency legislation, and the increased reputation of "green" companies).
97. *Id.*
98. *Id.* at 630.
99. *Id.*
100. *Amado v. Microsoft Corp*., 517 F.3d 1353, 1361-62 (Fed. Cir. 2008).
101. *Id.* at 1361.
102. *Id.* (citing *Paice*, 504 F.3d at 1315).
103. *Amado*, 517 F.3d at 1362. *See also Soverain Software LLC v. Newegg Inc.*, 2010 U.S. Dist. LEXIS 89269, at *52 (E.D. Tex. Aug. 11, 2010); *Paice*, 609 F. Supp. 2d at 628.
104. *Amado*, 517 F.3d at 1362.
105. *See, e.g., Ricoh Company v. Quanta Computer, Inc.*, 2010 U.S. Dist. LEXIS 38220 (W.D. Wis. Apr. 19, 2010).
106. 2009 U.S. Dist. LEXIS 35372 (N.D. Cal. Apr. 19, 2009).
107. *Id.* at *16
108. *Id.* at *14 (internal citation omitted).
109. *Id.* at *16.
110. *Id.* at *19-*24 (Factor 1 (royalties received for licensing of patent in suit), Factor 2 (rates paid by licensee for use of other patents), Factor 12 (portion of profits or of selling price in the particular business), Factor 4 (licensor's entitlement to maintain his patent monopoly), Factor 5 (commercial relationship between the parties), Factors 8 and 9 (established profitability of the product made under the patent and the marginal utility of the patented invention over the old modes), and Factor 13 (apportionment)).
111. 674 F. Supp. 2d 847 (E.D. Tex. 2009).
112. *Id.* at 853.
113. *Id.* (internal citations omitted).
114. *Id.* at 858.
115. *Id.* at 860.
116. *Id.* at 861 (*quoting, Amado v. Microsoft*, 517 F.3d at 1362 n.2).
117. 2010 U.S. Dist. LEXIS 79039 (S.D. Cal. Aug. 5, 2010).
118. *Id.* at *17. The court thought it was "unclear" whether the *Georgia-Pacific* factors should control post-trial, but believed that "an examination of the relevant *Georgia-Pacific* factors could be helpful in determining an appropriate royalty rate post-judgment." *Id.* at *17 n.7.
119. *Id.* at *23.
120. *Id.*
121. *Id.*

122. *Id.* at *53.

123. *Id.* at *53-54.

124. *Id.* at *54.

125. *Id.* at *55.

126. *Id.* at *56.

127. 533 U.S. 617 (2008).

128. 128 S. Ct. at 2117-18.

129. *Id.*

130. *Id.* at 2114.

131. *Id.*

132. *Id.* at 2117.

133. *Id.* at 2114.

134. *Id.* at 2115.

135. *Id.*

136. *Id.* at 2113, 2119 (test is whether the technology's "only reasonable and intended use [is] to practice the patent" and whether the technology "embodie[s] essential features of [the] patented invention").

137. *Id.* at 2120.

138. *Id.* at 2122.

139. *Id.* at 2121 ("Exhaustion is triggered only by a sale authorized by the patent holder.").

140. *Id.* at 2122.

141. *Id.*

142. *Id.* at 2119 n.6.

143. *ResQNet.com, Inc. v. Lansa, Inc.*, 594 F.3d 860 (Fed. Cir. 2010).

144. *Id.* at 868.

145. *Id.* at 869.

146. *Id.*

147. *Id.*

148. *Id.* at 870.

149. *Id.*

150. *Id.*

151. *Id.* at 871.

152. *Id.* at 873.

153. *ResQNet*, 594 F. 3d at 872.

154. *Id.* (citing, *inter alia*, *Hanson v. Alpine Valley Ski Area, Inc.*, 718 F.2d 1075, 1078-79 (Fed. Cir. 1983)).

155. *Id.* (citation omitted).

156. *See id.* at 882 (Newman, J., concurring in part and dissenting in part) ("This court today holds that only the royalty in the settlement agreement can be considered in the hypothetical license negotiation."). The Federal Circuit did not refer to century old Supreme Court precedent on this issue. In both *Cornely v. Marckwald*, 131 U.S. 159, 161 (1889), and *Rude v. Westcott*, 130 U.S. 152 (1889), the Supreme Court held that litigation-related settlements in patent infringement actions "cannot be taken as a standard to measure the value of the improvements patented, in determining the damages sustained by the owner of the patent in other cases of infringement. Many considerations other than the value of the improvements patented may induce the payment in such cases." *Id.* at 164. "In order that a royalty may be accepted as a measure of damages against an infringer, who is a stranger to the license establishing it, it must be paid or secured before the infringement complained of; it must be paid by such a number of persons as to indicate a general acquiescence in its reasonableness by those who have occasion to use the invention; and it must be uniform at the places where the licenses are issued." *Id.* at 165.

157. *Id.* at 876 (Newman, J., concurring in part and dissenting in part).

158. *Id.* at 880.

159. *Wordtech Systems, Inc. v. Integrated Networks Solutions, Inc.*, 609 F.3d 1308, 1319-20 (Fed. Cir. 2010).

160. 2010 U.S. Dist. LEXIS 28372, at *9-*10.

161. 2010 WL 774878 (E.D. Tex. Mar. 2, 2010).

162. *Id.* at *2.

163. *See Reedhycalog UK, Ltd. v. Diamond Innovations Inc.*, 2010 U.S. Dist. LEXIS 78138 (E.D. Tex. Aug. 2, 2010) (Davis, J.), and *Datatreasury Corp. v. Wells Fargo & Co.*, 2010 WL 903259 (E.D. Tex. Mar. 4, 2010) (Folsom, J.); *cf. In re U.S. Bank Nat'l Ass'n*, 2010 WL 1169943 (Fed. Cir. Mar. 15, 2010) (declining to issue writ of mandamus reversing Judge Folsom's determination that settlement agreements were admissible under *ResQNet*).

164. *See Software Tree, LLC v. Red Hat, Inc.*, 2010 U.S. Dist. LEXIS 70542, at *14 (E.D. Tex. June 24, 2010) (refusing to compel discovery of negotiations pertaining to settlement agreements, especially when three of the four settlement agreements in question were between plaintiff and former defendants in the case)*; Fenner Inv.*, 2010 WL 1727916, at *3 (distinguishing *ResQNet* on grounds that the defendants' expert sought to consider the settlement agreements under a different prong of the *Georgia-Pacific* analysis than that addressed in *ResQNet).*

165. No. 05 C 5373 (N.D. Ill. May 24, 2010).

166. 1995 U.S. Dist. LEXIS 14136 (N.D. Iowa Sept. 25, 1995).

167. *Abbott Laboratories*, Slip Op. at 5-6.

168. 2010 U.S. Dist. LEXIS 78857 (D. Utah Aug. 4, 2010).

169. *Id.* at *12.

170. *Id.* at *13-*14.

171. *See* Brian Pandya, *Why Pay More? Using Patent Settlements to Calculate Reasonable Royalty Rates*, Law.com (May 31, 2010) (observing that the *ResQNet* decision should prompt parties seeking to maximize the value of a patent to be cautious of entering into low-value settlement agreements early in litigation).

172. 35 U.S.C. § 292(a) (2000). Non-practicing entities have recently seized hold of false patent marking as a potential new source of revenue. *See, e.g., Pequignot v. Solo Cup Co.*, 2009 U.S. Dist. LEXIS 26020 (E.D. Va. 2009) (denying Solo Cup's motion to dismiss based on alleged unconstitutionality of false marking statute via violation of separation of powers); *see also* Donald W. Rupert, *Trolling for Dollars: A New Threat to Patent Owners*, 21 Int. Prop. & Tech. L.J. 1, 4 n.19 (2009).

173. *See Undersea Breathing Sys., Inc. v. Nitrox Techs., Inc.*, 985 F. Supp. 752, 782 (N.D. Ill. 1997); *Sadler-Cisar v. Commercial Sales Network, Inc.*, 786 F. Supp. 1287, 1296 (N.D. Ohio 1991) ("[C]ontinuous markings over a given time constitute a single offense. Defendants are therefore liable for only one 'offense' under the statute and are hereby fined $500.00."); *Joy Mfg. Co. v. CGM Valve & Gauge Co., et al.*, 730 F. Supp. 1387, 1394, 1399 (S.D. Tex. 1989); *Precision Dynamics Corp. v. Am. Hosp. Supply Corp.*, 241 F. Supp. 436, 446-47 (S.D. Cal. 1965); *Cornick v. Stry-Lenkoff Co.*, 134 F. Supp. 126, 131 (W.D. Kent. 1955) ("The corporate defendant falsely marked its marking tags [and[is therefore subject to the fine of $500.").

174. *Enforcer Prods., Inc. v. Birdsong*, 98 F.3d 1359 (Fed. Cir. 1996) (affirming the apparent assessment of a $50 fine for each individual flea trap product or product packaging appellants falsely marked).

175. *Icon Health & Fitness, Inc. v. The Nautilus Group, Inc.*, No. 1:02 CV 109 TC, 2006 WL 753002, at *4 (D. Utah Mar. 23, 2006).

176. *Krieger v. Colby*, 106 F. Supp. 124, 131 (S.D. Cal. 1952)

177. *The Forest Group, Inc. v. Bon Tool Co.*, No. H-05-4127, 2008 WL 2962206, at *6 (S.D. Tex. 2008).

178. *Id.* at *5 (citing *London v. Everett H. Dunbar Corp.*, 179 F. 506 (1st Cir. 1910)).

179. *Id.*

180. *Id.*

181. *Id.*

182. *Forest Group, Inc. v. Bon Tool Co.*, 590 F.3d 1295, 1301 (Fed. Cir. 2009) ("[T]he statute's plain language requires the penalty to be imposed on a per article basis.").

183. *Id.* at 1303-04.

184. *Id.* at 1304.

185. *See* Memorandum & Order, *The Forest Group, Inc. v. Bon Tool Co.*, No. H-05-4127, Slip Op. at 4-5 (S.D. Tex. Apr. 27, 2010).

186. 608 F.3d 1356 (Fed. Cir. 2010).

187. *Id.* at 1363-64.

188. *Stauffer v. Brooks Brothers, Inc.*, 2010 U.S. App. LEXIS 18144, at *17-*18 (Fed. Cir. Aug. 31, 2010).

189. William McQuillen, *Patent Bill Gets Judiciary Approval, Moves to Senate*, Bloomberg (Apr. 2, 2009).

190. *See* Patent Reform Act of 2009, S. 515, 111th Cong. § 284 (2009) with amendments (showing the provisions struck from the bill), *available at* http://www.govtrack.us/congress/billtext.xpd?bill=s111-515 (*last visited* June 18, 2009).

191. *Id.* at § 284(c).

192. *Id.* at § 284(c)(2)(A)-(C).

193. *See* McQuillen, *supra* note 189 (summarizing the purpose of the judge's role provisions in the bill and the political concession behind the change).

194. S. 515, 111th Cong. § 284(b)(1).

195. *Id.*

196. *Id.* at § 284(b)(2).

197. *Id.* at § 284(b)(3).

198. *Id.*

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Open Source Software: To Patent or Not To Patent?

By Martin F. Noonan

I. Introduction

According to conventional wisdom, patents and open source software are fundamentally incompatible.[1] This conventional wisdom is based on the principle that a patent holder is required to grant a royalty-free patent license when distributing any open source software that embodies the patent holder's patented technology. This requirement, however, does not make patents and open source software incompatible. On the contrary, patents can complement a business model based on the distribution of open source software. To understand how, we must first look at the nature of both open source software and patents.

II. The Nature of Open Source Software and Patents

Understanding open source software requires first understanding what source code is and how access to source code fundamentally changed software distribution. Source code is the "human-readable form of computer programs that allows programmers to understand and modify computer programs for themselves, as opposed to 'object code' which is the machine language version of computer programs that is very difficult for programmers to understand or modify."[2] Under a traditional software licensing model, software developers (primarily software companies) only distribute their software in object code format to their end users. Because end users do not have access to the source code, they cannot modify the software unless they reverse engineer the software to obtain the source code. The accompanying software license, however, generally prohibits both reverse engineering and any modifications to the software.

In the 1980s, a new software licensing model was introduced: open source software. Some software developers had become frustrated with the inability to have access to and modify the source code of software they were licensing. In response, some of these developers formulated a new software licensing model and called it "open source." Under the open source software licensing model, software developers distribute not only object code but also the source code to end users. But to fully allow end users the right to modify the software they were licensing, changes in the software licenses that governed that software also were made. These changes resulted in a new category of software license: the open source software license.

Open source software licenses are fundamentally different than traditional software licenses. Although there are currently over 1,400 unique open source licenses, in general open source licenses allow the end user a royalty-free right to view, use, and *modify* the source code for the end-user's own purpose[3]—all without obtaining permission from the author.[4]

In contrast, an end user can make use of modifications to patented technology only by obtaining permission (i.e., a license) from the patent holder. Patents give patent holders a great deal of control over their patented technology. Specifically, patents give the patent holder an exclusive right to make, use, sell, offer to sell, and import the patent holder's patented technology.[5] To exercise any of these rights requires a license from the patent holder. Therefore, if a patent holder includes patented technology in software that is governed by an open source license, the patent holder must grant a royalty-free patent license to the end user for the patented technology.

An open source license, however, does not affect whether a software developer can or even should apply for patent protection. An open source license only affects how a patent holder may be able to use his patent rights.[6] To effectively use both open source software and patents together, a software developer must recognize that although open source licenses generally require a royalty-free grant of a patent license, the license grant is limited to an end user who uses the software that is licensed under the open source license. The license grant is not a universal grant to the public at large. In other words, the software developers' patented technology does not become part of the public domain. This important distinction allows patents not only to complement an open source license but also to safeguard a business model that is built on the open source license.

III. Patents Can Complement an Open Source Business Model

Patents can play a key role in securing and protecting certain business models based on open source software. Patents and the selection of an appropriate open source license, however, must be considered early in the development of the business model to ensure the success of the business model. The key is recognizing the protection patents can afford a patent holder and understanding the reach of the open source license that governs the software.

To understand this dynamic between patents and open source licenses, let's explore one of the 1,400 open source licenses in greater depth. The open source license that is most often used by software developers is the General Public License (GPL). The most important aspect of the GPL is that it requires that any modifications to the open source software that are made and then distributed to an end user also must be governed by the GPL. In other words, any resulting software also must be distributed as open source software under the terms and conditions of the GPL. This requirement is referred to as “copy-left” and more derogatorily as “viral.” The term viral is used because the open source software can cause proprietary software to become open source software. In other words, the open source software can infect (like a virus) the proprietary software.

Because of this “copy-left” requirement, the GPL is favored by the open source community but disfavored by proprietary companies. The GPL is favored by the open source community because it ensures that people who use the open source software must keep any improvements to the open source software as open source software. The open source community wants to avoid people using and improving the open source software without having to disclose the improvements back to the open source community, i.e., taking advantage of open source software without contributing back to the open source community.

In contrast, proprietary companies are reluctant to use GPL software in products that are distributed to their end users because of the “copy-left” requirement of the GPL. If a proprietary company modifies open source software that is governed by the GPL and distributes the modified software to an end user, the proprietary company would be required to provide the end user with a copy of the source code for the modifications. Proprietary companies, however, maintain the commercial viability of their software products by retaining exclusive rights to their source code. Under the GPL, end users (including competitors) not only would obtain access to the source code but also rights to modify the source code. Competitors could study the modifications the proprietary company made, make further modifications, or even develop a competing product.

With this understanding, it appears unlikely that any viable business model could be based on open source software. Nevertheless, patents and a business model referred to as “dual-licensing” can allow a proprietary company to exploit the advantages of open source software while still maintaining the proprietary nature of the company’s software. Under a dual-licensing model, the software is simultaneously licensed under an open source license and a traditional commercial license. For example, a software company could develop open source software and make it available to the public under the GPL and under a commercial software license. Under the GPL, the license to the software would be royalty-free. This makes the software compelling to the open source community, the academic world (e.g., professors and their students), and cost-conscious engineers trying to solve their company’s engineering challenges.

If the software is compelling enough, it will become widely adopted. Proprietary companies then will be compelled to use the software or at least make sure their products and services are compatible with the software. Such proprietary companies then could purchase a license to the software under the commercial software license. By doing so, the companies would avoid the “copy-left” requirements of the GPL, and the software company would generate revenue from the commercial software license.

One major limitation of this approach involves a sophisticated competitor. The competitor can obtain the source code for the software product under the GPL and then develop a competing software product that incorporates all the innovation of the original software without using any of the source code of the original software. This would enable the competitor to avoid the requirement of having to release its new software under the GPL. If the competitor takes this approach, the original company would have no recourse. Although the original company developed the software and built the demand and market for the software, the sophisticated competitor could easily force the original company out of the market.

Patents would prevent that. If the original software contained technology that was patentable (i.e., novel, useful, and nonobvious), the original software company could apply for and obtain patents on the technology. If that occurs, when the competitor develops a competing product, the competitor may avoid copyright infringement and may avoid the reach of the GPL, but the competitor would not be able to avoid the patents. By obtaining patents on technology embodied in the software, a software company can build demand and a market for software protected using open source software and then monetize that demand and market by using a commercial revenue-generating software license.

Patents have additional value as well. For example, the software company can assert the patents against other parties that use the patented inventions in products and services other than the original software. Remember, the patent license granted in the GPL is limited to parties that use the software governed by the GPL. If the parties are not using the GPL software, then the patent license provided in the GPL does not apply to them.

In addition, patents also can enable the software company to assert the patents against any company that uses the GPL version of the software but that does not comply with the GPL. If a company is not in compliance with a condition (as opposed to a covenant) of the GPL, then that company would be outside the scope of the patent license provided by the GPL.[7] As a result, a patent holder could sue for patent infringement. Although the software company can also assert a breach of the GPL for failing to comply with the GPL, the remedies and certainties associated with patent infringement make a patent infringement lawsuit a better alternative.

IV. Recent Example

A recent case highlights how patents can reinforce a business model built on open source software. In August 2010 Oracle America, Inc. filed a patent infringement lawsuit against Google, Inc. alleging that Google's Android operating system infringes seven Oracle patents.[8] The patents being asserted by Oracle were acquired earlier this year when Oracle Corporation acquired Sun Microsystems, Inc..

In the mid- to late 1990s, Sun developed the Java programming language and Java platform (collectively "Java"). One of the advantages of Java was that it allowed software developers to develop software applications that could be used across multiple hardware devices and operating systems without having to customize the software applications for each hardware device or operating system. In other words, Java was hardware- and operating-system independent.

Sun recognized that the Java technology contained patentable subject matter and, accordingly, filed for and obtained several patents on the technology. These patents are the patents-in-suit in *Oracle v. Google*. Initially, though, Sun licensed Java under a traditional proprietary software license and successfully licensed Java to companies such as IBM, Microsoft, Oracle Corporation, Netscape, and others. Eventually, Sun adopted a different licensing strategy.

In 2006, Sun elected to "dual license" Java.[9] Sun continued to sell traditional commercial software licenses for Java, but Sun also licensed Java under the GPL. The selection of the GPL for Java was carefully planned. It appears that Sun recognized that the open source community and the academic world would embrace Java under the GPL. This would enable Java to become further adopted by the technical community. It also appears that Sun recognized that the viral nature of the GPL would cause proprietary companies to avoid using Java under the GPL. Under the dual license approach, however, Sun gave such proprietary companies the option to license Java under the proprietary software license in order to avoid the viral nature of the GPL.

Proprietary companies thus had a choice. If they licensed Java under the GPL, they would avoid paying licensing fees to Sun but would be required to disclose any modifications they made to end-users. However, if they licensed Java under the commercial software license, they would pay licensing fees to Sun but would be able to keep any modifications they make proprietary.

The basis of Oracle's complaint is that Google chose another option. Google developed its own operating system that consists of Java applications running on a Java-based framework.[10] By doing so, it appears that Google was attempting to develop an operating system that was similar to Java but not so similar as to be subject to the GPL. As discussed above, this is a major limitation in some business models built on open source software. Because the source code is required to be made available to end users, a sophisticated competitor can develop a competing software product that incorporates all the innovation of the software without using any of the source code of the original software. This approach can be an effective way to avoid both (i) a claim for breach of the GPL and (ii) a claim for copyright infringement for using an unauthorized copy (or a derivative work) of the software. This approach, however, may not be an effective way to avoid a claim of patent infringement. Unlike copyrights, which protect a particular expression of an implementation of a software product, patents can protect the idea and innovation embodied in the software. Time will tell if Google not only successfully designed around the GPL and Sun's copyrights but whether it also successfully avoided Sun's patents.

V. The Role of Attorneys

Attorneys play a critical role in determining if software should be released under an open source license and if certain technology should be patented. The first step in this process is to define the key business objectives of a company. With an understanding of the business objectives, attorneys can assist the company's executives in shaping various business models to achieve those objectives. As demonstrated above, some business models can effectively use both open source software and patents to build and protect a market for a given software product. The open source software can help build a customer base, and patents can ensure that competitors cannot leverage the open source software to develop and build competing products.

Specifically, attorneys can assist company executives in selecting the open source license that will most effectively achieve the company's business objectives. As stated above, there are over 1,400 different open source licenses. Some licenses are appropriate for some business models but not for others. Attorneys can advise company executives on both the advantages and disadvantages of the various open source licenses.

Attorneys also can work with the product development community to ensure that the products are developed in a manner that not only achieves the desired business model but also is in compliance with the open source license. Selecting the open source license is critical, but so is ensuring that the products are developed in a manner that complies with the open source licenses. Non-compliance with the open source license can have unintended consequence that could destroy a company's business model. Often, the advantages and disadvantages of open source software depend on how the open source software is used in a product. Attorneys can advise the product development community on the proper use of open source to leverage the advantages and to avoid the disadvantages.

Finally, attorneys can assist executives in developing a patent filing program that complements the company's open source business objectives. Such a patent filing program should be the same type of filing program that should be developed for protecting business objectives built on commercial software. The attorneys and company executives should: (1) develop a patent budget for the filing program; (2) identify the core technologies that will result in "blocking patents"; (3) identify complementary technologies that may result in future improvements to the products; and (4) identify technologies a competitor might use to design around the company's products. Within the constraints of the patent budget, attorneys then can work with both company executives and product development community to file for, prosecute, and obtain patents on the right combination of blocking patents, complementary patents, and design-around patents.

IV. Conclusion

Patents and open source software are not incompatible. Depending on the open source license and business model a company chooses, patents still can be an effective tool for protecting the company's intellectual property in the software. Therefore, a company's decision to release software as open source does not answer the question "To patent or not to patent?" Instead, further analysis is required to determine if a patent can complement the open source license to protect the company's business model.

Endnotes

1. *See* Arnoud Engelfriet, *Patent Risks of Open Source Software*, Ius mentis (Oct. 1, 2005), *available at* http://www.iusmentis.com/computerprograms/opensourcesoftware/patentrisks/.
2. Laura Majerus, *Court Evaluates Meaning of "Derivative Work" In An Open Source License*, Fenwick & West Intellectual Property Bulletin (Fall 2002).
3. *See* Andrew T. Pham and Matthew B. Weinstein, *Living With Open Source: Implementing, Managing and Enforcing A Uniform Policy For Your Enterprise*, Les Nouvelles: Journal Of The Licensing Executives Society (March 2010).
4. Laura Majerus, Patent Rights And Open Source—Can They Co-Exist? (Fenwick & West 2006).
5. 35 U.S.C. § 271(a).
6. *See* Majerus, *supra* note 4.
7. *See Jacobsen v. Katzer*, 535 F.3d 1373 (Fed. Cir. 2008).
8. *See* Complaint, *Oracle America, Inc. v. Google, Inc.* Case No. 3: 10-cv-03561-WHA (N.D. Cal. filed Aug. 12, 2010).
9. *See* David Kravets, *Oracle-Google Suit Attacks Open Source Software*, Wired (Aug. 16, 2010), *available at* http://www.wired.com/threatlevel/2010/08/oracle-attacks-opensource/.
10. *See* Complaint, *supra* note 8, at ¶ 12.

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Federal Court of Canada Holds "Business Methods" Patentable

By Geoffrey North

I. Introduction

In a decision reminiscent of the U.S. Supreme Court's recent ruling in *In re Bilski*, the Federal Court of Canada, in its highly anticipated decision in *Amazon.com v. The Commissioner of Patents*,[1] held that patents relating to "business methods" can constitute patentable subject matter. The decision, written by the Honourable Mr. Justice Michael Phelan and handed down on October 14, 2010, discusses differing laws and disparate judicial decisions respecting the patentability of "business method" patents across the globe, and it is required reading for anyone wishing to implement a cogent global IP strategy.

II. Background

A. The invention

Amazon.com, Inc. filed Canadian patent application no. 2,246,933 entitled "Method and system for placing a purchase order via a communications network" (the "'933 application") on September 11, 1998. The '933 application sets out a method and system that allows a purchaser to place an order for items over the Internet. This method and system of conducting Internet commerce differs from that known in the art. In the known system, a server computer may provide an electronic version of a catalogue that lists available items. A potential purchaser may browse through the catalogue using a browser and select various items to be purchased. This selection generally is based on the "shopping cart" model: when the purchaser selects an item, the server metaphorically adds that item to a shopping cart. When the purchaser is done selecting items, all the items in the shopping cart are "checked out," and the server computer system then prompts the user for information to complete the order, including, for instance, the purchaser's name, credit card number, and shipping address. The server then typically confirms the order by sending a confirming Web page to the purchaser's computer system and schedules shipment of the items.

Although intuitive, this shopping-cart model has a downside in that it requires many interactions by the purchaser. The overhead involved in confirming the various steps of the ordering process and waiting for, viewing, and updating the purchaser-specific order information can be cumbersome. Also, each time an order is placed, sensitive information is transmitted over the Internet and is susceptible to being intercepted and decrypted.

In the '933 application, however, Amazon.com provides a method and system for single-action ordering of items in a client/server environment that reduces both the number of purchaser interactions needed to place an order and the amount of sensitive information that is transmitted. Specifically, the server system uses a client identifier sent from the purchaser's computer to associate the purchaser's computer with the purchaser's payment and shipment information (purchaser-specific account information). The server stores the client identifier in the purchaser's computer in a "cookie" when the purchaser enters his identification, billing, and shipping information (purchaser-specific account information), usually at the time of the purchaser's first visit.

On a subsequent visit to the Web site by the purchaser's computer, the server recognizes the client identifier in the "cookie" as belonging to that purchaser. The purchaser may then browse items and decide to buy an item by clicking on only one button, which sends the request to order the item along with the client identifier.

The effect of this single action is to order the item instantly. The server system will receive the purchase request, automatically retrieve the purchaser's account information (which is now stored in the vendor's computer system) using the client identifier, and combine the retrieved account information to generate the order. Only one click of the purchaser's mouse is required. The order is made without the need to "check out" or enter any more information, and, as such, no sensitive information is transmitted via the Internet.

B. Decisions of the Examiner and the Patent Appeal Board

The patent examiner at the Canadian Intellectual Property Office (CIPO) rejected the application for being an obvious ordering method and system. The examiner also found that the subject matter of the claims was directed to non-patentable subject matter under section 2 of the Patent Act[2] on the ground that the essence of the claimed invention did not fall into one of the categories of "invention" ("any new and useful art, process, machine, manufacture or composition of matter, or any new and useful improvement in any art, process, machine, manufacture or composition of matter").

Having been rejected by the examiner, the '933 application was considered by the Patent Appeal Board and the Commissioner of Patents, and a decision was rendered on March 5, 2009 (Decision No. 1290). The Board concluded that the prior art did not disclose performing a single action to instantly order an item as set out in the claims. The Board also found there was no suggestion in the prior art to modify a subscription-based shopping model such that with one click an identifier (cookie) is sent in conjunction with the product ordering information, thus retrieving purchaser-specific account information, so that the order is instantly placed. According to the Board, "The advantages of such a streamlined ordering process pointed to by the Applicant are indicative of some ingenuity (or inventive step)."[3] As a result, the Board disagreed with the examiner and found that the skilled technician would not have been led directly and without difficulty to conceive of what had been claimed in the '933 application, i.e., it was not obvious.

However, the Board agreed with the examiner that the invention was directed to non-statutory subject matter on the ground that the substance of the claimed invention was not technical in nature. According to the Board:

> [W]here the claimed invention, in form or in substance, is neither a physical object (a machine, manufacture or composition of matter) nor an act or series of acts performed by some physical agent upon some physical object to produce in that object some change of either character or condition (art or process), it is not patentable….[C]ertain types of subject matter are excluded from patentability in Canada. A claimed invention which in form or in substance amounts to a business method is excluded from patentability.[4]

For this broad statement excluding business methods from patentability, the Board relied upon a statement made by a Justice of the Supreme Court of Canada in reasons dissenting in part from those of the majority in *Monsanto Canada Inc. v. Schmeiser*.[5] This was a noteworthy stance for the Board to take given that the previous Manual of Patent Office Practice (MOPOP) had stated that business methods were not "automatically excluded from patentability." The Board also relied upon statements made by the Federal Circuit in *In re Bilski*,[6] and decisions from the U.K. to support its position.

III. The Decision of the Federal Court of Canada

A. Adoption of international principles

Justice Phelan noted that this case highlighted the challenges in looking to foreign case law or international legal principles to assist in interpreting the Canadian patent regime:

> In an area of the law where advancing human ingenuity often creates novel legal questions to which there may be no immediate answer in Canadian jurisprudence, it can be useful to look to other regimes. However, this must be done mindfully. Despite the international conventions and principles of reciprocity, regimes can be fundamentally different. Something which may be patentable in one country, will not be here, or vice-versa. Also, it may be patentable for an entirely different reason. While international jurisprudence can provide guidance, these cases and the particular Canadian context of the question before the Court (i.e. what is patentable subject matter) must correspond to Canadian law. Some jurisdictions will be more applicable than others given the history, language and prior interpretation of their patent legislation.[7]

His Honour noted, for instance, that under the English and European systems which implement the European Patent Convention (EPC) there is no definition of "invention" but, instead, a series of exclusions. In this respect, article 52(2)(c) of the EPC specifically states that "schemes, rules and *methods for* performing mental acts, playing games or *doing business, and programs for computers*" shall not be regarded as inventions. In addition, a review of U.K. case law revealed that the exclusions in the U.K. and European regimes are largely concerned with policy. In Canada, on the other hand, the Commissioner of Patents has no discretion to refuse a patent on the basis of public policy considerations independent of any express provision in the Act, the Commissioner has to justify any refusal. International jurisprudence is therefore "at most a potential guide when applied correctly and mindfully"[8] in Canada.

B. Definition of "art" and "process"

Justice Phelan noted that in Canada it is generally accepted that "method" and "process" are the same thing and that "art" may include either. There are three important elements in the test for "art": (i) it must not be a disembodied idea but have a method of practical application; (ii) it must be a new and inventive method of applying skill and knowledge; and (iii) it must have a commercially useful result. The practical application requirement ensures that something that is a mere idea or discovery is not patented—it must be concrete and tangible. This requires some sort of manifestation or effect or change of character.

However, Justice Phelan noted that it is important to remain focused on the requirement for practical application rather than merely on the physicality of the invention. One must not "restrict the patentability of practical applications which might, in light of today's technology, consist of a slightly less conventional 'change in character' or effect that [is] through a machine such as a computer."[9] While not everything under the sun is patentable, the definition of "invention" in the Patent Act is broad and encompasses "unforeseen and unanticipated technology."[10]

C. Application to the '933 application

The Court found that a purposive construction of the "system claims" at issue clearly disclosed a machine that is used to implement Amazon.com's one-click ordering system. The described components were found to be essential elements in implementing the online ordering process and not merely a "mathematical formula" that could be carried on without a machine or simply a computer system. A machine as such is patentable under section 2 of the Patent Act.

As to the process claims at issue, the Court found they claim an invention that uses stored information and "cookies" to enable customers to order items over the Internet simply by clicking on them. This novel online ordering system added to the state of knowledge in this area. As Justice Phelan noted:

> The new learning or knowledge is not simply a scheme, plan or disembodied idea; it is a practical application of the one-click concept, put into action through the use of cookies, computers, the internet and the customer's own action. Tangibility is not an issue. The "physical effect," transformation or change of character resides in the customer manipulating their computer and creating an order. It matters not that the "goods" ordered are not physically changed.
>
> It is undisputed that this invention has a commercially applicable result and is concerned with trade, industry and commerce. Indeed, its utilization in this very realm seems to be at the root of the Commissioner's concern.[11]

In view of the foregoing, Justice Phelan also found the process claims to be patentable as an art or process. The Court therefore found that the '933 application disclosed patentable subject-matter, contrary to the decision of the Commissioner of Patents. His Honour, however, would not grant a patent as requested by Amazon.com, since the Court was not asked to assess the validity of the claims in other respects. As such, the Court quashed the decision of the Commissioner of Patents, and the application was sent back for expedited reexamination.

As an important aside, it is interesting to note that Justice Phelan also made the following comments:

> There may be (and the Court is not suggesting that there are) other reasons why the Commissioner might have rejected this patent. *One might question the sufficiency of disclosure in the system claims but no one has claimed that it was insufficient*. That matter was not considered by the Commissioner.[12]

Subsection 27(3) of the Patent Act states that the specification of an invention must: (a) correctly and fully describe the invention and its operation or use as contemplated by the inventor; (b) set out clearly the various steps in a process, or the method of constructing, making, compounding, or using a machine, manufacture, or composition of matter, in such full, clear, concise, and exact terms as to enable any person skilled in the art or science to which it pertains, or with which it is most closely connected, to make, construct, compound, or use it; (c) in the case of a machine, explain the principle of the machine and the best mode in which the inventor has contemplated the application of that principle; and (d) in the case of a process, explain the necessary sequence, if any, of the various steps, so as to distinguish the invention from other inventions.

In accordance with section 84 of the Patent Rules, the claims must be clear and concise and must be fully supported by the description independently of any document referred to in the description. As such, a person skilled in the art must be able to understand what the invention is, what it does, and how to make it work based on the specifications alone when read in light of their common general knowledge.

According to the MOPOP, if the desired result requires a novel and nonobvious application of hardware or software, a greater level of detail regarding how this result is to be achieved is necessary. Computer-implemented inventions are often described in terms of a flow chart that illustrates the algorithm or logic tree on which the operation of the invention is based. Where the algorithm or logic performed by the computer lies at the heart of the invention, a full description of the algorithm or logic tree must be provided.

Moreover, in order for the person skilled in the art to be able to put each step in the flow chart into operation, the description must be enabling. That is, the person skilled in the art must be able to do this without recourse to inventive ingenuity or undue experimentation. The description, therefore, must provide any information necessary to enable the algorithm to be practiced. As stated in the MOPOP, "Where very little explanation is given regarding how a step in a method is to be implemented by a computer, this will generally be understood as an indication that the applicant, rightly or wrongly, does not consider the implementation of that step to require inventive effort on the part of the person skilled in the art."[13]

Unfortunately, patent applications regarding computer-implemented inventions are all too often bereft of sufficient disclosure and therefore are open to attack. Applications for computer-implemented inventions should be drafted with a sufficiently detailed description of the hardware, program modules, and data structures involved, along with flow charts describing the algorithms or computer logic used to implement the invention. If one wishes to implement a cogent global IP strategy with respect to computer-implemented business method patents, one must be concerned not only with patentability of the subject matter in various jurisdictions but also with whether the application provides a sufficiently enabling disclosure.

Endnotes

1. 2010 FC 1011.
2. R.S.C. 1985, c. P-4.
3. PAB Decision No. 1290, at para. 95.
4. Ibid. at paras. 139-140.
5. 2004 SCC 34, at para.133.
6. 88 U.S.P.Q.2d 1385 (Fed. Cir. [2008]).
7. 2010 FC 1011, at para. 32.
8. Ibid. at para. 37.
9. Ibid. at para. 53.
10. Ibid. at para. 54.
11. Ibid. at paras. 75-76.
12. Ibid. at para. 79.
13. MOPOP, s. 16.05.01, "Written description and enablement."

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Chloé v. Queen Bee: Second Circuit Expands Reach of New York Long-Arm Statute in Online Counterfeiting Case

By Itai Maytal

I. Introduction

As e-commerce continues to grow, so have counterfeit markets. The Internet provides counterfeiters with the marketing and distribution tools needed to expand their illicit and profitable trade anywhere in the world, without requiring a physical presence to sell their knock-off goods. Because of this virtual, borderless reality, frustrated trademark owners seeking to enforce their rights in court are often faced with jurisdictional challenges from online counterfeiters.

Sometimes these challenges succeed, forcing trademark owners to chase infringers to their home jurisdictions—however remote and costly that might be—in pursuit of uncertain relief. It has been unclear, however, under what circumstances trademark owners could bring trademark infringement actions against out-of-state online merchants without having those actions dismissed on jurisdictional grounds.

Recently, the Second Circuit, in *Chloé v. Queen Bee of Beverly Hills, LLC*,[1] provided local trademark owners some clarity on this issue by interpreting expansively the reach of New York courts over out-of-state trademark infringers and their employees. The court held that a single sale and shipment of the plaintiff's branded good into New York by a defendant, whether that sale is infringing or not, combined with the defendant's use of an interactive website that sold goods carrying the marks of others in the forum, satisfied New York's long-arm statute and the Due Process Clause of the U.S. Constitution.[2] In arriving at this conclusion, the court noted the need to "update [the Court's] jurisprudence on personal jurisdiction in the age of internet commerce."[3]

This article examines the Second Circuit's "update" and offers insights into its potential impact on trademark owners.

II. Factual and Procedural Background

Chloé SA ("Chloé") is a French fashion house that sells and markets, among other things, luxury women's handbags and purses bearing the CHLOÈ word mark (Registration #3,291,996).[4] The company's exclusive licensee in the United States is Chloé NA, a division of a Delaware corporation operating out of New York.[5]

In November 2005, Chloé NA became aware of an online retail discount designer named Queen Bee of Beverly Hills LLC ("Queen Bee") during a lawsuit it brought against a counterfeit handbag vendor that named Queen Bee as its supplier.[6] Queen Bee is an Alabama corporation that had show rooms in Beverly Hills, California and Huntsville, Alabama.[7] It did not maintain any offices or employees in New York.[8] On its two identical websites, Queen Bee described itself as a "leading wholesale and retail designer boutique, offering the latest trends in authentic European designer accessories."[9] It advertised "trunk shows" across the country and offered to sell and ship handbags purportedly manufactured by various name brand designers—including Chloé—anywhere in the continental United States and to select locations worldwide.[10]

Chloé investigated Queen Bee and learned that the company was selling unauthorized copies of Chloé handbags for $1,200, plus shipping, which was approximately $400 less than what the handbags sold for in authorized Chloé boutiques.[11] In response, Chloé's attorneys in New York orchestrated what is commonly described in the trademark community as a "trap sale."[12] A paralegal with Chloé's firm named Rosa Santana was directed to place an online order for a Chloé "Paddington" bag from the Queen Bee site and have it delivered to her Bronx, New York address.[13] The bag, which a Chloé investigator concluded was counterfeit, arrived with a FedEx shipping label bearing the Beverly Hills, California address of Simone Ubaldelli, a principal of Queen Bee.[14] During the ensuing lawsuit, Ubaldelli did not dispute that the bag purchased by Chloé's agent was counterfeit and was not manufactured, produced, or in any manner authorized by Chloé.[15]

In April 2006, Chloé sued Queen Bee and five other defendants, including Ubaldelli, a California resident, in the Southern District of New York for trademark infringement under sections 32(1) and 43(a) of the Lanham Act and New York General Business Law § 349 as well as for common-law trademark infringement and unfair competition.[16] The case proceeded only against Ubaldelli after the other defendants defaulted, settled, or went into bankruptcy. The suit against Queen Bee was stayed when Queen Bee filed for bankruptcy.[17]

In the course of jurisdictional discovery, questions arose as to whether New York courts could properly exercise personal jurisdiction over Ubaldelli and Queen Bee. Chloé learned that Queen Bee had shipped more than seventy Chloé handbags in the United States, but the only one shipped to New York appeared to be the one purchased by Chloé's agent, Ms. Santana, the paralegal with Chloé's firm.[18] At the same time, Chloé discovered that Queen Bee had shipped at least fifty-two non-Chloé branded items to New York customers.[19] It also was revealed that Queen Bee's principal, Ubaldelli, had supervised and directed those sales.

At the close of discovery, Ubaldelli moved to dismiss for lack of personal jurisdiction, while Chloé cross-moved for partial summary judgment on liability.[20] Ubalelli argued that the sale and delivery of a single admittedly counterfeit bag to the plaintiff's investigator could not support jurisdiction in New York because it was a "manufactured contact" or a purchase not made by an actual customer but rather by an agent of the plaintiff. Ubaldelli also asserted that the sale was only a one-time Internet-based sale from a company with no physical presence in the state. In response, Chloé argued that personal jurisdiction was proper based on the single purchase by its counsel's paralegal and because the "offers of sale" of counterfeit Chloé bags on the Queen Bee website were accessible to New York residents.[21]

The district court granted Ubadelli's motion to dismiss, concluding that the court did not have personal jurisdiction over him based on a "single internet-based sale of a counterfeit retail product."[22] The court dismissed as moot Chloé's motion for partial summary judgment. The court found that the trademark infringement claim did not arise from an infringing sale where there could be a likelihood of confusion at the "point of sale" or "postsale."[23]

The court also found that the sale of a counterfeit Chloé bag to an agent of the plaintiff in New York was "manufactured" and thus could not by definition generate any confusion for the purchaser, since Ms. Santana knew she was buying a knock-off bag.[24] Accordingly, the court held that it would violate due process to "permit a plaintiff to manufacture personal jurisdiction by purchasing an allegedly infringing product in a plaintiff's forum of choice."[25] The court discounted the sale and shipment by Queen Bee of non-Chloé goods into New York because, while they indicated purposeful availment of the New York forum "for some business activity," they did not sufficiently arise out of or relate to the sale of Chloé goods by Ubaldelli, which was the only infringing activity alleged by Chloé.[26]

The district court also declined to exercise personal jurisdiction over Ubaldelli based on Queen Bee's "commercial interactive website," even though it permitted users to view allegedly infringing products and place orders for those products. The district court evaluated the website according to the "sliding scale of interactivity,"[27] which generally holds that a wholly "passive" website is insufficient to support personal jurisdiction over its owner, but an "interactive website" in combination with other relevant forum contacts may be sufficient for jurisdiction.[28] Under this approach, the district court found that while the Queen Bee site did offer Chloé handbags, it could not support jurisdiction because it was not aimed or directed at New York users, and no New York residents had purchased counterfeit merchandise from Queen Bee, with the exception of the plaintiff's agent, Ms. Santana.[29]

On June 29, 2009, the district court supplemented its rationale for granting Ubaldelli's motion to dismiss in response to plaintiffs' motion to certify the dismissal as final.[30] Based on its review of various Supreme Court precedents, the court found that the single Internet purchase by Chloé's agent from the Queen Bee site did not manifest a "continuing relationship," "prior negotiations," or "contemplated future consequences" sufficient to support personal jurisdiction.[31] The court also noted that it would offend traditional notions of fair play and substantial justice to subject Ubaldelli, a California resident, to jurisdiction in New York when there was "no obvious reason why New York has a greater interest in hearing trademark actions than other federal and state courts."[32] The plaintiffs appealed.

III. Second Circuit Ruling

The Second Circuit reversed, holding that Ubaldelli's single act of shipping a Chloé-branded bag into New York, combined with the sale of at least fifty non-Chloé items to New Yorkers through the Queen Bee interactive website, gave rise to personal jurisdiction under the state's long-arm statute, CPLR 302(a)(1), and did not violate the Due Process Clause.[33] The court based its conclusion on Ubaldelli's connections to the act in question and to the business activities of Queen Bee in New York.

Relying on Ubaldelli's role at Queen Bee as the primary purchaser of infringing handbags and on the fact that his Beverly Hills address was on the FedEx package containing the Chloé-branded bag shipped to New York, the Second Circuit first determined that "the evidence supported the conclusion that Ubaldelli either physically shipped or was responsible for the shipment of the counterfeit handbag from California to New York."[34] The court also imputed to Ubaldelli Queen Bee's other business activities in New York—namely the shipment of fifty-two non-infringing goods into New York and an interactive website that permitted the sale of Chloé-branded goods to New York consumers—based on the fact that Ubaldelli shared profits from Queen Bee sales, had joint access to its bank account, used its revenue to pay his rent, and shared in the decision-making and execution of Queen Bee sales.[35]

Having established Ubaldelli's connection to the allegedly infringing activity, the court proceeded to the two-step inquiry for finding personal jurisdiction over a non-domiciliary in a case involving a federal question.[36] In the first step, a court must determine whether the laws of the forum state, here New York's long-arm statute, confers jurisdiction over the defendant.[37] If so, the court then considers whether the exercise of jurisdiction is consistent with the Due Process Clause of the Fourteenth Amendment.[38] This requires determining whether the defendant had "minimum contacts" in the forum state to justify the court's exercise of personal jurisdiction, whether specific or general. It also requires asking whether the exercise of jurisdiction is reasonable in that it does not "offend traditional notions of fair play and substantial justice."[39]

The court concluded that Ubaldelli had transacted business within the state under section 302(a)(1) of New York's long-arm statute.[40] That provision states that a court "may exercise personal jurisdiction over any non-domiciliary…who in person or through an agent…transacts any business within the state or contracts anywhere to supply goods or services in the state."[41] The court noted that the New York law is a "single act statute," such that proof of one transaction in New York is sufficient to invoke jurisdiction even when the defendant never enters New York.[42] However, because Queen Bee operated a "highly interactive website" offering counterfeit Chloé bags and sold and shipped a non-trivial number of branded goods into the state, the court declined to resolve whether a single act of shipping a counterfeit Chloé bag was by itself sufficient to support personal jurisdiction.[43] The Second Circuit wrote that "[v]iewed in their totality, these contacts sufficiently demonstrate [defendant's] availment of the benefits of transacting business in New York" under the New York long-arm statute."[44]

In addition to finding jurisdiction was authorized under New York's long arm statute, the Second Circuit also held that personal jurisdiction over Ubaldelli comported with due process. In its "minimum contacts" analysis, the court found that Ubaldelli had "purposefully availed himself of the privileges of conducting activities within the forum state…by [Queen Bee's] develop[ing] and serv[ing] a market for its products in [New York]."[45]

Unlike the district court, the Second Circuit refused to limit the relevant minimum contacts between Queen Bee and New York to the "narrow subset of one sale that involved a Chloé handbag shipped to Plaintiffs' law firm."[46] Instead, it included in its analysis the more than fifty additional sales of non-Chloé designer handbags in New York.[47] The court held that the district court's characterization of these sales as constituting only "some business activity" "too narrowly construe[d] the nexus requirement which merely requires the cause of action to relate to defendant's minimum contacts with the forum."[48] Further, that Ubaldelli did not maintain a "continuous relationship" with any particular New York consumer—a fact of significance to the district court—was irrelevant.[49] While such a relationship may be a sufficient condition for asserting jurisdiction, the court found, it is not a necessary one.[50]

Finally, the court of appeals rejected the district court's reasonableness analysis after applying the five-factor test set of *Asahi Metal Industry Co., Ltd. v. Superior Court of California, Solano County*.[51] The *Asahi Metal* test requires courts to consider (1) the burden on the defendant, (2) the interests of the forum state, and (3) the plaintiff's interest in obtaining relief. It also must consider (4) the interstate judicial system's interest in obtaining the most efficient resolution of controversies and (5) the shared interest of the several states in furthering fundamental substantive social policies.[52]

The court concluded that any burden on Ubaldelli from litigating cross-country from California to New York would be equally burdensome for the plaintiffs and was, in any event, reduced by "modern communication and transportation."[53] It also found that New York had a particular interest in providing redress for its residents, notwithstanding the fact that trademark claims can be brought in any forum. Further, Chloé had a particular interest in obtaining relief in New York given that its headquarters and some of its witnesses were there. Thus, the court concluded that "Ubadelli's generalized complaints of inconvenience arising from having to defend himself from suit in New York do not add up to a compelling case that the presence of some other considerations would render jurisdiction unreasonable."[54]

IV. Impact of the Decision

Having won the right to proceed in its action against Ubaldelli, it remains to be seen whether Chloé ultimately will prevail on the merits of its counterfeiting claim. What is clear, though, is that the Second Circuit has significantly expanded long-arm jurisdiction, at least in New York, over Internet counterfeiters in such cases. Now, when faced with e-commerce sites hawking counterfeit goods, trademark owners can reliably use investigators to determine the extent of the illicit activity and confirm online sales of knock-offs without necessarily jeopardizing the jurisdictional basis of actions they may bring in New York. They may now be able to obtain specific personal jurisdiction over an out-of-state online defendant if they can show, in addition to a single act of shipping a counterfeit good, that the counterfeiter site engaged in non-trivial online business sales in the state, infringing or otherwise, of branded goods.

Exercising jurisdiction over such Internet merchants may not necessarily be unfair, given the control they generally have in limiting their online presence. As the International Trademark Association argued in an amicus curiae brief it filed in support of Chloé's appeal, if an Internet merchant chooses to avoid a jurisdiction, it can do so by providing a passive, informational site or by blocking sales to that jurisdiction.[55] Conversely, the merchant can elect to service a national market, to advertise, sell, and ship its goods throughout the country. In that scenario, the merchant should pay a jurisdictional price; otherwise, its conduct would go legally unchecked in the markets in which it operates.[56]

Still, the Second Circuit's interpretation of the nexus requirement for jurisdiction may have exposed more online merchants to claims in the New York forum than is necessary to combat counterfeiting. Without addressing how so-called "manufactured contacts" should be treated for purposes of trademark infringement claims, the court stated that "an employee's single act of shipping a bag—*any* bag, not necessarily a counterfeit one—into the State of New York, combined with the employer's other business activity involving the State of New York, gives rise to an inference that the defendant 'purposefully avail[ed] himself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws'."[57] The strange implication of this statement seems to be that a trademark infringement claim can arise from the online purchase in the forum of a good later found to be non-infringing from a site that otherwise sells legitimate goods with different marks. Supporters of the Chloé decision may argue that this concern confuses the jurisdictional question with the merits of the claim. On the other hand, detractors may argue the decision will needlessly increase the cost of doing business for legitimate businesses as they are haled into fora to which they are only obliquely connected. Ultimately, future decisions will determine the seriousness of these concerns and whether the law should change in response to them.

Notwithstanding its expansive reading of the New York long-arm statute, the Second Circuit did not revamp the law to the extent INTA and the plaintiffs would have preferred. The court declined to decide whether an out-of-state defendant's single act of selling and shipping one infringing good into New York is sufficient to support personal jurisdiction.[58] However, in keeping with a number of district court decisions, the court acknowledged in dictum the possibility that such facts could satisfy the New York long-arm statute.[59] In so doing, the Second Circuit seems to have invited brand owners to test jurisdiction under these facts in future trademark actions.

Two New York district courts already have applied the Second Circuit's dictum—perhaps too loosely—in their personal jurisdiction analyses.[60] In one case, the court allowed the plaintiff to proceed on the basis of only a few online sales made in the forum.[61] Presumably, more New York courts will make similar rulings when pressed by trademark plaintiffs, given the limited sympathy the Second Circuit seems to have with counterfeiters.

V. Conclusion

The Internet has largely obviated the need for a brick-and-mortar presence in most markets. More entities now do business online and, to the dismay of trademark owners, so do counterfeiters. They sell their illicit wares through auction sites, stand-alone e-commerce sites, and email solicitations from virtually anywhere in the world. Recognizing the enforcement problems this creates for trademark owners, the Second Circuit has now secured, at least in New York, greater access to the forum's courts in trademark infringement actions. Future cases may expose the excesses of the Chloé decision as it relates to out-of-state non-infringers haled into New York courts on thin trademark infringement claims and oblique connections to the forum. Until then, trademark owners should take note of the *Chloé* decision and be further emboldened to pursue their claims against out-of-state counterfeiters and other types of infringers who attempt to avoid liability by operating solely in the virtual marketplace.

Endnotes

1. *Chloé v. Queen Bee of Beverly Hills, LLC*, 616 F.3d 158 (2d Cir. 2010). ("Chloé III").
2. *Id.* at 162.
3. *Id.* at 165.
4. U.S. Patent and Trademark Office, Electronic Word Mark Search = Chloé, *at* http://www.uspto.gov (last visited October 10, 2010).
5. *Chloé III*, 616 F.3d at 162.
6. *Id.*
7. *Id.*
8. *Id.*
9. *Chloé v. Queen Bee of Beverly Hills, LLC*, 571 F. Supp. 2d 518, 521 (S.D.N.Y. 2008)("*Chloé I*").
10. *Id.*
11. *Chloé III*, 616 F.3d at 162.
12. *Chloé I*, 571 F. Supp. 2d at 522.
13. *Id.*
14. *Chloé III*, 616 F.3d at 162.
15. *Chloé I*, 571 F. Supp. 2d at 522.
16. *Chloé III*, 616 F.3d at 163.
17. *Id.* at 161 n.1.
18. *Id.* at 163.
19. *Id.*
20. *Chloé I*, 571 F. Supp. 2d at 521.
21. *Id.*
22. *Chloé v. Queen Bee of Beverly Hills, LLC*, 630 F. Supp. 2d 350, 351 (S.D.N.Y. 2009)("*Chloé II*")(Describing the holding of *Chloé I*).
23. *Chloé I*, 571 F. Supp. 2d at 526.
24. *Id.*
25. *Id.*
26. *Chloé I*, 571 F. Supp. 2d at 523 n.3. (noting that "Plaintiffs' cause of action for infringement of the Chloé trademark does not arise out of or relate to Queen Bee's sales of Gucci, Prada, Fendi, or other designers' merchandise.").
27. *Id.* at 526 (citing *Best van Lines, Inc. v. Walker*, 490 F.3d 238, 252 (2d Cir. 2007). The "sliding scale" was originally proposed in *Zippo Manufacturing Co. v. Zippo Dot Com, Inc.*, 952 F. Supp. 1119 (W.D. Pa. 1987).
28. *Id.* at 528 (citing *Energy Brands, Inc. v. Spiritual Brands Inc.*, 07 Civ. 10644(DC), 2008 WL 2747276, at *7-*8 (S.D.N.Y. July 16, 2008)).
29. *Id.* at 530.
30. *Chloé II*, 630 F. Supp. 2d at 351.

31. *Chloé II*, 630 F. Supp. 2d at 353 (citing *Travelers Health Association v. Virginia*, 339 U.S. 643 (1950), *McGee v. International Life Insurance Co.*, 455 U.S. 220 (1957), and *Burger King Corp. v. Rudzewicz*, 471 U.S. 462 (1985)).

32. *Id.* at 356.

33. *Chloé III*, 616 F.3d at 162.

34. *Id.* at 165.

35. *Id.* at 169.

36. *Id.* at 163.

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.* at 170. The Second Circuit declined to analyze the jurisdictional question under CPLR 302(a)(3) even though Queen Bee did not dispute its products were counterfeit and that it advertised its goods on its website, as the court concluded it could find jurisdiction under section 302(a)(1) and because the court recently certified the question of its applicability to the New York Court of Appeals. *See id.* at 169 n.3 (referring to *Penguin Group (USA) Inc. v. American Buddha*, 609 F.3d 30 (2d Cir. 2010)). The question before the New York Court of Appeals focused on how the ease of infringement via the Internet should change long-arm jurisdiction analysis.

41. *Id.* at 169.

42. *Id.* at 170.

43. Acknowledging the holdings of district court within the circuit, the court of appeals held in dicta that a "single act" of selling counterfeit goods into New York could satisfy the long-arm statute under section 302(a)(1). *See, e.g.*, *Baron Phillippe de Rothshild, S.A. v. Paramount Distillers, Inc.*, 923 F. Supp. 433 (S.D.N.Y. 1996); *Mattel, Inc. v. Adventure Apparel*, 00-cv-4085, 2001 WL 286827 (S.D.N.Y. Mar. 22, 2001). While it did not apply this rationale here, by making this observation the Second Circuit seems to have encouraged future brand-owner plaintiffs to bring trademark infringement claims under this jurisdictional theory.

44. *Id.* at 170-71.

45. *Id.* at 171.

46. *Id.* at 167.

47. *Id.*

48. *Id.*

49. *Id.* at 172.

50. *Id.*

51. *Asahi Metal Industry Co., Ltd. v. Superior Court of California, Solano County*, 480 U.S. 102 (1987).

52. *Id.* at 113.

53. *Id.* at 172.

54. *Id.* at 173.

55. Brief of Amicus Curiae International Trademark Association in Support of Vacatur and Remand, 09-3361-cv (2d Cir. Aug. 5, 2010).

56. *Id.*

57. *Chloé III*, 616 F.3d at 165 n.3.

58. *Id.* at 170.

59. *Id.*

60. See *Pearson Education v. Textbooks Discounters*, No. 10-CV-324, 2010 WL 3528866, at *2 (S.D.N.Y. Aug. 20, 2010) (finds personal jurisdiction over trademark defendant in part under the Chloé dicta that stated "the sale of even a single item over the internet that is shipped into New York can give rise to personal jurisdiction"); *O'Brien & Gere Engineers, Inc. v. Innis Arden Golf Club*, No. 5:10-CV-410, 2010 WL 3526207, at *5 (N.D.N.Y Sept. 3, 2010) (denying jurisdiction while misconstruing Second Circuit holding in Chloé to allow for personal jurisdiction through "an employee's single act of shipping a handbag to New York").

61. *Pearson Education*, 2010 WL 3528866, at *2.

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Scenes from the Intellectual Property Law Section

FALL MEETING

October 7–10, 2010

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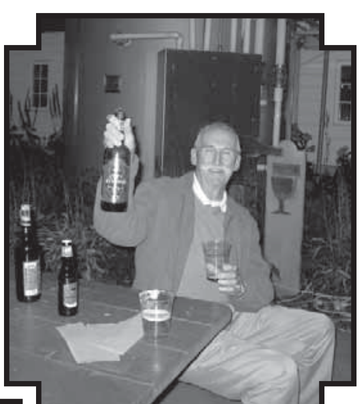


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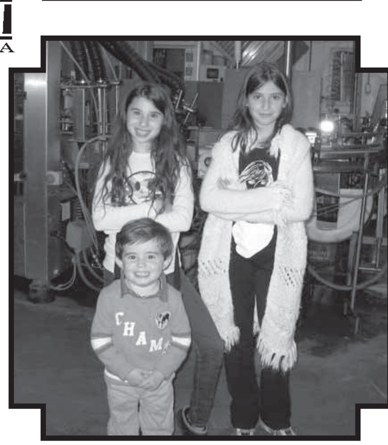











Advertising and the Environment: The New FTC Green Guides

By Marc A. Lieberstein and Barry M. Benjamin

I. Introduction

Advertising and the environment have become close friends over the past fifteen years. Companies are now, more than ever, promoting the "green" qualities and characteristics of their products. This article discusses how the Federal Trade Commission is seeking to regulate such promotional claims, and how companies can take steps to ensure that they and their competitors are in compliance with the law in order to avoid deceiving consumers.

1992 was a crucial year in the development of law and regulations relating to the environment and environmental claims. ECO-92, the United Nations Conference on Environment and Development, was held in Rio de Janeiro, and although it was not the first international meeting on the subject, it became famous due to the high attendance by heads of state.[1] Reducing human impact on the environment and conserving it for future generations had finally become a concern for the global capitalist world, which was exposed to a new term: "sustainable development."

Thereafter, interest in the environment increased substantially. Companies gradually started to change their practices, using renewable raw materials as well as incorporating renewable energy and developing manufacturing and logistical processes that cause less harm to the environment. A new market of consumers interested in "ecologically correct" or "green" products emerged as well. To appeal to this new market, companies began to advertise the environmental benefits of their products and manufacturing methods. The concept of "green" became fashionable—even ubiquitous—in the news and entertainment media, in response to the demands of a new market thirsty for "environmentally correct" products.

Advertisers quickly took note of this new messaging and began to develop new words and phrases to attract attention to their new crop of "green" products and their suppliers and created new marketing communication strategies to attract consumer attention. Along with new trademarks, many products began to carry symbols (e.g., chasing arrows in a mobius loop circle, representing recyclable) and expressions such as "eco-friendly"; "environmentally friendly, safe or green"; "ozone free"; "degradable"; "biodegradable"; "photodegradable"; and "recyclable", all indicating their "green" quality. The problem was that consumers did not necessarily understand these new words and phrases to mean what the advertiser intended, and advertisers did not necessarily have adequate substantiation for the claims the words and phrases were communicating to consumers. This conflicted with the basic tenets of advertising law that consumer impression, not literal truth, is the touchstone of an advertising claim and that an advertiser must have substantiation for all express and implied claims conveyed to consumers by a product's advertising.

II. Environmental Claims and the Green Guides

In view of the increasing use of marketing communication strategies highlighting, and sometimes improperly claiming, the "green advantages" of products and services, in 1992 the FTC issued its Guides for the Use of Environmental Marketing Claims, commonly known as the Green Guides.[2] The purpose of the Guides was to establish a set of guidelines to ensure that corporations do not deceive consumers through improper environmental claims. On October 6, 2010, the FTC issued a proposed revised version of the Green Guides. The proposed new Guides can be accessed on the FTC website at www.ftc.gov.[3] As part of its revision effort, the FTC relied on public workshops, comments, and a study of consumers' perceptions of environmental claims. The FTC requested public comments on the proposed revisions through December 10, 2010, after which the agency will decide what changes to make final.

Even though the Green Guides are only administrative interpretations of the law, the FTC has been using them as a basis for enforcement actions. In addition, marketers use the Green Guides as a safe harbor against FTC action: as long as advertising stays within the meaning of those expressed in the Green Guides, the advertising should not be deemed deceptive.

The Green Guides are animated by a set of four principles, separate and apart from any particular advertising claim. These principles are important to understanding the rationale behind the specifics of the Green Guides and the manner in which the FTC may take action when it deems appropriate. The principles are:

Principle #1: Qualifications and Disclosures. Qualifications and disclosures must be sufficiently clear when such statements are necessary to prevent a claim from being deceptive. This is a general principle for all advertising disclosures: disclaimers should not contradict or negate the main claim of the advertisement.

Principle #2: Distinction Between Benefits of Product, Package, and Service. Marketers must make clear whether a claim applies to a product, to its packaging, or to a service. For example, in 1994, the seller of plastic tableware was targeted by the FTC because it labeled its packages "recyclable" with the three-chasing arrow depiction. The label failed to specify whether it referred to the packaging or the product—the FTC assumed both, but neither actually complied with the Green Guide's definition of "recyclable."

Principle #3: Overstatement of Environmental Attribute. Claims must not overstate an environmental benefit. As with any advertising claim, it is the consumer impression that matters, not whether the claim is strictly true. For example, if through a new manufacturing process the use of recycled content increases from 2 percent to 3 percent and the advertiser indicates on the package "50% more recycled content than before," the statement, although true, gives the consumer the false impression that the advertiser significantly increased the use of recycled materials.

Principle #4: Comparative Claims. An advertisement that compares a product to another must be clear what the baseline for comparison is. For example, if a water bottle advertises that it uses "30% less plastic" the claim may be deceptive because it is not clear what the basis for the comparison is—a prior version of the bottle or a competitor's.

III. 1998-2010: Pre-Revised Green Guides

Before discussing the specifics of the revised Green Guides, it is important to note the evolution of the thinking behind green advertising law between 1998, the last time the original Green Guides were revised, and 2010, when the new proposed revised version was released. The marketplace experienced an explosion of green advertising claims. Into the vacuum of FTC guidance during this time period entered some private actors concerned about false green claims in the marketplace. The overriding concern is that when false claims pervade the marketplace, the credibility of true, genuine "eco-friendly" green claims suffers from the prevalence of false claims and from the inability of consumers to distinguish between the two.

One such private actor's guidance became particularly persuasive. Terra Choice, an organization concerned with environmental marketing, has issued insightful guidance about green claims called the "Seven Sins of Greenwashing." These "sins" are:

Sin of the Hidden Trade-Off. Suggesting a product is "green" based on a narrow set of attributes, without attention to other important environmental attributes. Paper is not necessarily environmentally preferable just because it comes from a sustainably harvested forest—other relevant factors in the paper-making process include energy, greenhouse gas emissions, and water and air pollution, which may be equally or more significant.

Sin of No Proof. Making a claim that cannot be substantiated by easily accessible supporting information or by a reliable third-party certification.

Sin of Vagueness. Making a claim that is so poorly defined or broad that its real meaning is likely to be misunderstood by the consumer. For example, "All-natural" when arsenic, uranium, mercury, and formaldehyde are all naturally occurring yet poisonous.

Sin of Irrelevance. Making a claim that may be truthful but is unimportant or unhelpful to consumers attempting to purchase environmentally friendly products.

Sin of Lesser of Two Evils. Making a claim that may be true within a product category but risks distracting the consumer from the greater environmental impact of the category as a whole, e.g., "Fuel efficient SUV" and "Organic cigarettes."

Sin of Fibbing. Making claims that are simply false. For example, some companies advertise their products as "certified organic" when no such certification was made.

Sin of Worshiping False Labels. Making a claim, either through word or image, that gives the impression of a third-party endorsement where no endorsement was made. For example, a brand of aluminum foil uses certification-like images that bear the name of the company's own in-house environmental program, without further explanation.

IV. The FTC's Revised Green Guides

The process undertaken by the FTC to revise the Green Guides was quite extensive, examining both sides of the advertising equation—the advertising claims made by industry and the impression conveyed to consumers by those claims. The FTC hosted a series of three workshops to which they invited consumer groups, industry actors, and others to provide input and opinion about various environmental-oriented industry claims. They also conducted an extensive Internet surfing period, during which they catalogued green advertising claims. In addition, in order to comprehend how consumers understood green claims, the agency conducted consumer perception studies, underscoring that the basis of advertising law is consumer impression, not the literal truth or falsity of any particular advertisement or claim.

Preventing consumer deception remains paramount in the revised Green Guides, and the proposed revisions include guidance on claims both addressed and unaddressed by the existing Green Guides. Claims addressed by the existing Green Guides which have been updated include general environmental benefit claims, use of certification and third-party seals of approval, and use of terms that convey a "green-friendly" benefit, such as "degradable," "compostable," "recyclable," and "non-toxic." Claims not addressed by the existing Green Guides for which guidance is proposed include "made with renewable materials," "made with renewable energy," and carbon offset claims.

An extensive examination of the proposed revised Green Guides is beyond the scope of this article, but a brief overview of certain proposals is instructive. First, the FTC stresses that the Green Guides apply to business-to-business marketing, dispelling the notion held by some that they applied only to consumer-oriented marketing.

The proposed revised Green Guides also caution against making unqualified, general claims that a product is "environmentally friendly" or "green." The previous Guides had allowed marketers to make such unqualified claims so long as they could substantiate all express and implied claims. If substantiation was not available, marketers were to qualify the general claims. However, in its research in connection with the proposed revised Guides, the FTC found that consumers interpret unqualified "eco-friendly" claims as meaning the products have far-reaching environmental benefits and specific attributes such as being biodegradable, non-toxic, or made with renewable energy. Since few, if any, products have all of the attributes that consumers interpreting "eco-friendly" claims believe them to have, the FTC considers these general claims to be nearly impossible to substantiate. Moreover, because a significant number of consumers perceive these general "green" claims as suggesting the product has no environmental impact, and because all products have some environmental impact, it is highly unlikely that a marketer could substantiate that a product has no or negligible negative environmental impact. Thus, in a departure from the previous Guides, the proposed revised Guides advise marketers not to make unqualified general environmental benefit claims.

The FTC found, however, that qualifying a general environmental benefit claim can reduce consumers' misperceptions regarding a product's specific, unstated benefits or the absence of a negative environmental impact. Accordingly, the proposed Guides state that marketers must use clear and prominent language to convey that a general environmental claim refers only to a specific and limited environmental benefit. Nonetheless, the Guides warn that explanations of specific environmental attributes will not qualify a general claim if the advertisement's context implies other deceptive claims and that some qualifications can result in additional claims that cannot be substantiated. Thus, marketers should avoid unqualified general environmental benefit claims and should be careful when qualifying those claims.

The proposed revised Guides also emphasize that certifications and seals are covered by the FTC's Endorsement Guides. The proposed Guides provide new and expanded examples and analysis showing marketers how to avoid pitfalls using certifications / seals, noting that an unqualified certification (one that states no basis for the certification it embodies) likely constitutes a general environmental benefit claim. Accordingly, marketers should use clear and prominent language limiting the claim to particular attribute(s) for which they have substantiation. And, notably, third-party certification does not obviate a marketer's obligation to use clear limiting language with regard to any such claims.

The proposed Guides also provide updates on how to properly use relevant words and phrases used in product labeling, including "degradable," "compostable," "ozone-safe / friendly," "recyclable," "free of / non-toxic," and "made with renewable materials / energy," as well as clarification on how to use the concept of carbon offsets in advertising materials.

It is also important to note that the FTC expressly did not address certain green marketing claims. Specifically, the FTC did not provide guidance on use of the words "sustainable," "natural," or "organic," because it did not have a sufficient basis for providing any guidance as to these terms and because in certain instances (e.g., "organic") other federal agencies provide guidance as to their use. It is also understandable that the FTC would not provide guidance for a term when there is no general consumer understanding of what it means. Marketers therefore use these terms at their peril. Without a concrete consumer understanding of what these terms mean, it will likely be difficult for an advertiser to provide substantiation for their use.

V. Conclusion

U.S. companies that make "green" claims concerning their products or operations must be aware of the Green Guides and their provisions that seek to avoid consumer deception. Where transgressions occur, there are a number of judicial and regulatory avenues for forcing companies and advertisers to comply with applicable standards and to pay damages in appropriate circumstances.

Endnotes

1. *See* United Nations Website, Earth Summit, *available at* http: / / www.un.org / geninfo / bp / enviro.html (last visited June 24, 2010).
2. 16 C.F.R. Part 260; *see* 57 FR 36363 (1992).
3. The updated Guides have basically included more specific information regarding renewable material content claims, renewable energy claims, and carbon offset claims.

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The Ethical Quandary of Pretext Investigations in Intellectual Property Practice and Beyond

By Teige P. Sheehan

I. Introduction

In order for attorneys to provide competent legal services, it is necessary to acquire information that is material to clients' interests. In the context of litigation, of course, procedural rules pertaining to discovery provide mechanisms for exchanges of information between parties. However, there are many circumstances in which formal discovery procedures are unavailing. Clients may need to verify suspicions of a violation of their legal rights before determining whether to pursue litigation or some other course of action, but information necessary to make the determination may purposefully be suppressed. Or they may contest a proffered valuation of assets that are the subject of licensing negotiations or other business transactions but lack closely held information necessary to resolve their concerns. Or they may anticipate that prejudicial information may not be provided during discovery notwithstanding mechanisms to compel complete disclosure through court order, etc.

In turn, attorneys and their clients may contemplate using investigative techniques that involve deception to induce parties to disclose prejudicial information by misrepresenting the identity and/or purpose of the individual eliciting the disclosure. Attorneys' participation in, or supervision of, such "pretext investigations" poses complications when juxtaposed with the New York Rules of Professional Conduct ("NY Rules").[1] Although deceptive tactics involving misrepresentation may not necessarily be illegal, the NY Rules facially proscribe such conduct as unethical when engaged in by attorneys either directly or by others acting under attorneys' direction or supervision.

Nevertheless, pretext investigations are hardly rare. On the contrary, they are commonplace in civil and criminal matters.[2] Many state and federal courts have affirmatively condoned such tactics in certain circumstances, as have various bar associations throughout the country in ethics opinions. Some states have gone further, amending their ethics rules to permit pretext investigations. Indeed, in several jurisdictions, the bodies responsible for enforcing attorney rules of professional conduct themselves engage in such deceptive tactics in investigating possible malfeasance. Although explicitly permissive treatment of pretext investigations remains the minority position, and some authorities continue to explicitly prohibit them, there is a growing recognition among the bar that the prevailing rules need to address the permissibility of such practices with more clarity and certainty.

This article presents the current state of the conflict between the NY Rules and pretextual investigative practices that have been condoned by authorities in New York State. Part II summarizes the NY Rules, which facially proscribe such conduct. Part III discusses New York court and ethics opinions condoning attorney use of pretext investigations and how the NY Rules were construed in those opinions. As we will see, intellectual property attorneys in particular have been exempted from the NY Rules' apparent prohibition on the use of pretext investigations, although for reasons that are not entirely clear doctrinally. Part IV describes additional opinions and rules from other jurisdictions that have addressed this issue. The conclusion summarizes the analysis, highlights the need for more clarity on this issue, and presents some general guidelines intellectual property attorneys could weigh when considering how to comply with the NY Rules in employing pretext investigations.

II. The NY Rules Facially Proscribe Attorney Implementation of Pretext Investigations

Several NY Rules explicitly prohibit attorneys from engaging in misrepresentation and deceptive conduct, either personally or by proxy, which in general are inherent characteristics of pretext investigations. Other NY Rules limit the individuals with whom attorneys are permitted to communicate, again either personally or by proxy, restricting who may be a subject of investigations, pretextual or otherwise.

Rule 4.1 states that "[i]n the course of representing a client, a lawyer shall not knowingly make a false statement of fact or law to a third person." Notably, in the rules recommended by the NYSBA Committee on Standards of Attorney Conduct (COSAC) and approved by the NYSBA such a statement constitutes an ethical violation only if it consists of "a false statement of *material* fact or law,"[3] in accordance with the Model Rules of Professional Conduct promulgated by the American Bar Association (ABA). By omitting the word "material" from the adopted rule, the New York courts rejected the proposition that a factual misrepresentation is unethical only if it is "significant to the issue or matter at hand,"[4] or "[o]f such a nature that knowledge of [it] would affect a person's decision-making."[5]

For purposes of pretext investigations, however, whether Rule 4.1 permits material misrepresentations is moot. The identity of an individual attempting to elicit information from a party in such circumstances is objectively significant, and the expectation that knowledge of her identity and purpose would unfavorably impact the decision to provide information is the very purpose of engaging in such tactics.[6] Thus, even if New York had adopted the Model Rules' more permissive formulation, Rule 4.1 on its face would appear to prohibit the use of pretext investigations.

Furthermore, NY Rule 8.4(c) prohibits lawyers and law firms from "engag[ing] in conduct involving dishonesty, fraud, deceit or misrepresentation." By definition and necessity, pretext investigations involve dishonesty, deception, and misrepresentation, if not outright fraud, and thus appear to be prohibited by Rule 8.4(c). It has been suggested that the "catch-all" provision of 8.4(c)[7] is not applicable to pretext investigations, which fall within the more directly targeted ambit of Rule 4.1.[8] Ultimately, the resolution of this question may be strictly academic and of little help to practitioners, who in theory could suffer the consequences of violating Rule 4.1 whether or not the same conduct also constitutes a violation of Rule 8.4(c).

Rule 5.3(b) functions in combination with Rule 4.1 to further restrict the use of pretext investigations: "[A] lawyer shall be responsible for conduct of a nonlawyer employed or retained by or associated with the lawyer that would be a violation of [the NY Rules] if engaged in by a lawyer, if…the lawyer orders or directs the specific conduct or, with knowledge of the specific conduct, ratifies it." Thus, insofar as Rule 4.1 prohibits a lawyer from engaging in misrepresentation, Rule 5.3(b) prevents circumvention of this prohibition through performing pretext investigations through another, by proxy. Rule 8.4(a) also prohibits a lawyer or firm from violating the Rules "or do[ing] so through the acts of another."

Whereas Rules 4.1, 5.3(b), and 8.4 prohibit a lawyer from employing misrepresentation directly or indirectly, Rules 4.2 and 4.3 further circumscribe the permissibility of investigations by limiting whom lawyers may communicate with. Rule 4.2 states that "[i]n representing a client, a lawyer shall not communicate or cause another to communicate about the subject of the representation with a party the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the prior consent of the other lawyer or is authorized to do so by law."

Perhaps because Rule 8.4(a) prevents circumvention of the ethical rules by proxy, COSAC's proposed Rule 4.2(a) did not of itself make it a violation for an attorney to "cause another to communicate" with a represented party,[9] but the New York courts inserted that clause directly into the Rule, presumably to eliminate any doubt. Although Rule 4.2(b) states that "a lawyer may cause a *client* to communicate with a represented person…and may counsel the client with respect to those communications" (emphasis added), Rule 4.3(a) notwithstanding, it also requires advance notice of the communication be given to the party's counsel.[10] Thus, even if Rules 4.1, 5.3(b), and 8.4(c) do not prevent the use of pretext investigations, this notice requirement would undermine pretext investigations that were somehow shoehorned into any reading of a "safe harbor" into Rule 4.2(b).

Where a party is a corporation, as opposed to a natural person, a relevant question is which of its employees or other agents also qualify as parties for the purposes of Rule 4.2. The New York Court of Appeals formulated the following test for determining who qualifies as a party under these circumstances: "corporate employees whose acts or omissions in the matter under inquiry are binding on the corporation (in effect, the corporation's 'alter egos') or imputed to the corporation for purposes of its liability, or employees implementing the advice of counsel."[11]

However, pretextually investigating an employee of a corporate party who does not meet any of these descriptions, and thus technically is not a party, still may fall within the proscriptions of Rule 4.3, which states that "[i]n communicating 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." The NYSBA comment to Rule 4.3 makes clear that "a lawyer will typically need to identify the lawyer's client and, where necessary, explain that the client has interests opposed to those of the unrepresented person."[12] As addressed above, Rules 5.3(b) and 8.4(a) would prohibit a lawyer from circumventing Rule 4.3 by proxy, thus rendering any attempted pretext ineffectual.

III. Court and Ethics Opinions in New York Have Condoned Pretext Investigations in Some Circumstances

In light of the above analysis, it may come as a surprise that authorities in New York have in recent years permitted attorneys' use of pretext investigations, although neither the NYSBA nor the Court of Appeals has issued an opinion explicitly condoning them. The New York County Lawyers' Association (NYCLA) issued an opinion in 2007 holding that although the use of pretext investigations is "generally unethical" under the NY Rules, they are ethically permissible "under certain exceptional conditions," to be interpreted "narrowly."[13] The opinion applied the term "dissembling" to describe what occurs in the context of a pretext investigation, defined as "giv[ing] a false impression about (something); … cover[ing] up (something) by deception."[14] Dissemblance, the NYCLA argued, is "distinguished…from dishonesty, fraud, and deceit by the degree and purpose of the dissemblance."[15] After surveying the treatment of this issue in various opinions issued in other states analyzing the applicability of ethics rules, the NYCLA concluded that pretext investigations are permissible when:

> (i) either (a) the investigation is of a violation of civil rights or *intellectual property*

> *rights* and the lawyer believes in good faith that such violation is taking place or will take place imminently or (b) the dissemblance is expressly authorized by law; and
>
> (ii) the evidence sought is not reasonably available through other lawful means; and
>
> (iii) the lawyer's conduct and the investigators' conduct that the lawyer is supervising do not otherwise violate the [NY Rules, such as Rules 4.2 and 4.3] or applicable law; and
>
> (iv) the dissemblance does not unlawfully or unethically violate the rights of third parties.
>
> Moreover, the investigator must be instructed not to elicit information protected by the attorney-client privilege.[16]

Out of context, designating intellectual property rights violations as warranting the use of pretext investigations might seem curious. However, federal courts had previously permitted pretext investigations in the context of enforcing copyrights and trademark rights. In *Gidatex v. Campaniello Imports, Ltd.*[17] the court denied a motion to preclude evidence that had been obtained during a pretext investigation aimed at uncovering violations of trademark rights in 1999. The plaintiff's attorney sent undercover investigators to defendant's place of business to pose as customers, speak with salespeople, and secretly tape record the conversations.[18] Although the court found that counsel's conduct technically corresponded to conduct proscribed by the NY Rules, including those forbidding contact with represented parties, it nevertheless concluded that "his actions simply do not represent the type of conduct prohibited by the rules."[19] Ultimately, the evidence gathered during the investigation was deemed admissible because "the remedy of preclusion would not serve the public interest or promote the goals of the disciplinary rules."[20]

A "public interest" exception to the NY Rules is not without corollary in New York State courts. For example, in 2003, the Kings County Supreme Court held that an attorney did not violate ethics rules when he assisted his client in surreptitiously recording telephone conversations with the defendant, her employer.[21] The recordings revealed another employee of the defendant using obscenities and racial slurs.[22] While acknowledging the deception involved, the court held that because the public policy interest of combating racial bias was served by the conduct, an exemption from condemnation was warranted.[23] Subsequently, although stating that "[u]ndisclosed taping smacks of trickery" and, in general, is "ethically impermissible as a routine practice," the Association of the Bar of the City of New York created an exception, holding that "[a] lawyer may…engage in the undisclosed taping of a conversation if…disclosure of the taping would impair pursuit of a generally accepted societal good."[24] By extension, similar rationales could be extended to exempting otherwise ethical pretext investigations from condemnation.

Gidatex is not the latest federal court opinion issued in New York to condone pretext investigations of suspected violation of intellectual property rights. In *Cartier v. Symbolix, Inc.* the same court summarily dismissed an argument by the defendant in a trademark suit that a claim for injunctive relief should be denied because the plaintiff's attorney had gathered evidence through use of a pretext investigation, an issue the court characterized as "collateral to the subject matter of [the] litigation—trademark infringement."[25]

Nor was it the first federal court to do so. In *Apple Corps Ltd., MPL v. Int'l Collectors Society*[26] the court condoned pretexting in the investigation of suspected violations of trademark rights and copyrights. The plaintiff's counsel directed investigators to call the defendant and purchase materials covered by the plaintiff's trademarks and copyrights—which the defendant was forbidden to sell to them under a prior consent decree—without disclosing their identity or their ultimate purpose in placing the orders.[27] The court held that the controlling ethical rules did not apply to a "lawyer's use of an undercover investigator to detect ongoing violations of the law…especially where it would be difficult to discover the violation by other means."[28]

Perhaps importantly, the court held that counsel did not violate the prohibition on contact with a represented party because the corporate defendant's salespeople whom the investigators contacted were not deemed parties.[29] The court also held that the controlling rule analogous to NY Rule 4.3, prohibiting a lawyer from contacting an unrepresented person "[i]n dealing on behalf of a client" also was not violated.[30] The court construed the quoted language to mean that the rule was violated only if the communication is by someone "acting as a lawyer."[31] Because the investigators were not functioning as attorneys but merely as customers, the court held, the rule against communication with unrepresented persons was not triggered.[32]

Thus, NYCLA Op. 737's application of public interest exceptions to the apparent prohibitions on pretext investigations, in particular with regard to intellectual property disputes,[33] was not unprecedented. However, to the extent the opinion relied on court precedents to explicitly allow pretexting in investigating an intellectual property rights violation (provided the additional requirements are also met), it is somewhat overinclusive. *Gidatex*, *Cartier*, and *Apple Corps* involved investigating intellectual property rights pertaining to trademarks and copyrights, but no court or other ethics opinions specifically address dissemblance in other intellectual property matters, such as those involving trade secrets or patent rights.

Misappropriation of trade secrets, such as by obtaining them through fraudulent misrepresentation or engaging in industrial espionage, is itself proscribed by New York law.[34] Furthermore, Rule 8.4(b) prohibits lawyers from "engag[ing] in illegal conduct that adversely reflects on the lawyer's honesty, trustworthiness or fitness as a lawyer," and Rule 4.4(a) holds that "[i]n representing a client, a lawyer shall not…use methods of obtaining evidence that violate the legal rights of [a third] person." Thus, by engaging in a pretext investigation aimed at obtaining another's trade secrets, on behalf of a client or otherwise, an attorney would all but surely violate Rules 8.4(b) and / or 4.4(a), irrespective of Rules 4.1–4.3, 5.3(b), and 8.4(c). Conversely, however, a party that suspects its own trade secrets have been stolen, such as by a current or former employee, might consider launching a pretext investigation into the suspected misappropriation. As an aspect of intellectual property practice, would it be a violation of the NY Rules if a party's attorney were involved in such an investigation?

As for enforcing patent rights, pretext investigations may not be necessary for determining whether, for example, a party is infringing a product patent through importation or sales of infringing goods. In such a case, a patentee could simply purchase the goods through normal channels of commerce and determine through direct examination whether its patent reads on the product. However, it may be far more difficult to determine whether a process patent is being infringed. The process used by a suspected infringer may be maintained in secret, in which case the patentee's counsel may contemplate employing a pretext investigation.[35] Moreover, prior to filing or even drafting a patent application, use of pretext investigations may be contemplated as part of landscape searching. Notably, both the Federal Circuit[36] and the New York Appellate Division, First Department[37] have held that New York attorneys are subject to the ethics rules of New York State when representing clients before the USPTO, notwithstanding the USPTO's own ethics rules.[38]

No published opinions specifically address whether such examples of pretext investigations pertaining to patent or trade secret intellectually property rights violations are permissible under the NY Rules, notwithstanding NYCLA Op. 737's gloss on the issue.[39] Focusing on such particulars, however, suggests an inverse opinion from that suggested above: that NYCLA Op. 737 may be *underinclusive* in singling out suspected violations or impending violations of intellectual property rights or civil rights as those which warrant pretext investigations.[40] Barry Temkin, who participated in writing NYCLA Op. 737 as Chair of the NYCLA Professional Ethics Committee,[41] has argued convincingly for a reevaluation of the rules pertaining to pretext investigations.[42] He observes that judging the permissibility of such tactics by "the subject matter of the underlying claim or investigation" is "highly subjective, value-laden, and political."[43] From this perspective, the question is not which types of intellectual property matters warrant the use of pretext investigations but, rather, why should such tactics be forbidden in the investigation of other areas of law if permitted for intellectual property attorneys?[44]

Beyond civil litigation and transactional practice, law enforcement has long involved the use of misrepresentation in the form of informants and sting operations. In 2001, the U.S. District Court for the Western District of New York denied a criminal defendant's motion to suppress evidence,[45] obtained by informants at the apparent direction of FBI counsel.[46] The magistrate judge's report and recommendation, relied on in denying the motion to suppress, stated that there was "no authority for [the] conclusion" that "government attorneys could not supervise investigations involving undercover agents and informants who cannot reveal their true identity and purpose to the targets of the investigation."[47] Such conflict between ethical rules governing private attorneys in civil practice and even criminal defense and government lawyers involved in law enforcement has been the subject of substantial commentary,[48] as discussed below.

IV. Opinions from Other Jurisdictions on the Permissibility of Pretext Investigations

In Oregon, a 2000 Supreme Court attorney disciplinary proceeding that barred the use of pretext investigations and refrained from exempting law enforcement attorneys from the proscription paralyzed operative undercover criminal investigations, prompting a revision of the state's ethics rules.[49] The case is illustrative of the confusion prevalent in this area. An attorney, Daniel Gatti, represented chiropractors charged with racketeering and fraud.[50] Realizing that his clients had been the subjects of pretext investigations by the Oregon Department of Justice, he filed a complaint with the Oregon Bar, alleging violations of the state's ethical rules.[51] He was subsequently notified that the Oregon State Professional Responsibility Board had concluded that the dissemblance involved in the pretext investigation did not violate any ethical codes and that it had closed its file on his complaint.[52]

Subsequently, Gatti himself implemented a pretext investigation to assess his suspicions that an insurer and a medical review service company had engaged in fraud in denying an insurance claim of one of his clients. He telephoned a medical reviewer and an officer and director of operations for the medical service review company, representing that he was a chiropractor, eliciting information, and recording some of the calls.[53] For this conduct, Gatti himself was sanctioned by the Wisconsin Supreme Court, with a public reprimand.[54] In its opinion, the court considered and rejected a U.S. Attorney's amicus argument that it should create a "prosecutorial exception" to the ban on pretext investigations.[55] Rather, the court declined to recognize "an exception for *any* lawyer to engage in dishonesty, fraud, deceit, misrepresentation, or false statements," an exception which, it held, could only properly be made by an amendment to the state's rules of ethics.[56]

As a result, in 2002 Oregon amended its ethics rules to permit pretext investigation not only by law enforcement attorneys but by all lawyers.[57] Thus, although Oregon's Rule 8.4(a)(3) holds that it is "professional misconduct for a lawyer to…engage in conduct involving dishonesty, fraud, deceit or misrepresentation that reflects adversely on the lawyer's fitness to practice law," Rule 8.4(b) adds that "it shall not be professional misconduct for a lawyer to advise clients or others about or to supervise lawful covert activity in the investigation of violations of civil or criminal law or constitutional rights, provided the lawyer's conduct is otherwise in compliance with these Rules of Professional Conduct."[58]

The Oregon State Bar Association Board of Governors subsequently issued an ethics opinion elaborating on the circumstances under which pretext investigations would be permissible: the lawyer must rationally believe that there is a violation of civil or criminal law or constitutional rights to investigate and must not directly engage in dissembling.[59] Interestingly, however, the opinion also highlighted the fact that even under the revised Oregon Rule 8.4(b), the result in *Gatti* would not have been different.[60] Whereas the rule "is meant to permit a lawyer only to provide advice and supervision regarding covert activity, not to participate directly in that activity,"[61] Gatti had directly participated.[62]

A similar course of events transpired in Wisconsin. Attorney Stephen Hurley's client was accused of several crimes, including possession of child pornography.[63] Believing his client had been falsely accused, Hurley initiated a pretext investigation whereby an investigator convinced the accuser to surrender his computer, in which Hurley anticipated finding evidence that would exculpate his client.[64] In February 2007, the Wisconsin Office of Lawyer Regulation (OLR) filed a complaint against Hurley for his involvement in the pretext investigation.[65] The referee appointed to hear the matter recommended that Hurley not be found in violation of the Wisconsin's Rules.[66]

In support of her recommendation, the referee noted Mr. Hurley's "conflicting obligations": to zealously defend his client or to conform to a vague rule that had never before been used to condemn such pretext investigations.[67] In February 2009, the Wisconsin Supreme Court dismissed the OLR's subsequent appeal of the referee's report and recommendation, favorably citing her reasoning and noting that the OLR director and Dane County District Attorney both had admitted that "prosecutors frequently supervise a variety of undercover activities and sting operations carried out by nonlawyers who use deception to collect evidence, including misrepresentations as to identity and purpose."[68]

Also relevant to the court's determination was that in July 2007, after the OLR had initiated its proceedings against Mr. Hurley but before the referee had issued her report and recommendation,[69] Wisconsin Rule 4.1(b) was amended to state that "a lawyer may advise or supervise others with respect to lawful investigative activities." As the Committee Comment to the amended rule explained:

> Paragraph (b) has no counterpart in the [ABA] Model Rule…. As a general matter, a lawyer may advise a client concerning whether proposed conduct is lawful…. This is allowed even in circumstances in which the conduct involves some form of deception, for example the use of testers to investigate unlawful discrimination or the use of undercover detectives to investigate theft in the workplace. When the lawyer personally participates in the deception, however, serious questions arise…. Paragraph (b) recognizes that, where the law expressly permits it, lawyers may have limited involvement in certain investigative activities involving deception.
>
> Lawful investigative activity may involve a lawyer as an advisor or supervisor only when the lawyer in good faith believes there is a reasonable possibility that unlawful activity has taken place, is taking place or will take place in the foreseeable future.[70]

In ruling for Hurley, the Wisconsin Supreme Court noted that "the OLR [did] not contest that Attorney Hurley's conduct would violate the current version of the rule."[71]

Note that, as in Oregon, the permissibility of attorney participation in pretext investigations in Wisconsin requires that the attorney not participate directly in dissembling.[72] Although this contingency may have merit insofar as it seeks to spare attorneys from perceptions of unclean hands, it nevertheless suggests an elision of the doctrinal force of NY Rule 8.4(a) and its ilk, which prevent circumvention of the Rules by proxy, a point I elaborate on in the conclusion.

In any case, the tension between allowing government attorneys to circumvent ethical proscriptions on pretext investigations, while giving full force to the prohibitions on private attorneys, has played a central role in challenging the sustainability of such prohibitions.[73] Additional jurisdictions have issued opinions explicitly exempting government lawyers from prohibitions on pretext investigations.[74] Notably, NYCLA Op. 737 explicitly refrained from "address[ing] the…question of direction of investigations by government lawyers supervising law enforcement personnel where additional considerations, statutory duties and precedents may be relevant."[75] For its part, the NYSBA has suggested that communications with represented parties may be permitted as lawful if they consist of "investigative activities of lawyers representing governmental entities, directly or through investigative agents."[76]

Of particular interest are opinions holding that bar associations authorized to administer discipline to attorneys for ethical violations may themselves employ dissemblance in investigating lawyers' conduct. For example, the Virginia State Bar Ethics Counsel has held that bar investigators may engage in dissemblance in investigating suspected unauthorized practitioners of law (e.g., contacting them under a guise of requesting legal services).[77]

In a particularly apt case, a former D.C. Bar counsel, in investigating an attorney's attempt to sell a witness to the plaintiff's counsel in a pending lawsuit, "deputized" the plaintiff's counsel, who reported the attempt and encouraged him "to continue negotiations…to explore fully the ethical implications of [the attorney's] conduct."[78] The judge who delivered the opinion of the three-judge panel argued to exclude evidence against the witness-proffering attorney obtained after the reporting plaintiff's counsel had been "deputized" because the attendant dissemblance constituted an ethical violation.[79] Another judge on the panel agreed that the Bar Counsel violated ethics rules but refrained from opining on the admissibility of the evidence, as it was not necessary to reach a determination in the case.[80] The remaining judge argued that the Bar Counsel's participation in dissembling did not constitute a violation of the rules of ethics and recommended that the Board of Professional Responsibility "submit to the court proposed rules amendments to make clear Bar Counsel's authority to conduct post-complaint covert investigation and evidentiary rules deemed just."[81]

The fact that in that case a Bar Counsel engaged in dissembling, and three appellate judges could not agree on whether the conduct was permissible, speaks to the bar's continuing need for clarity and guidance on this issue. Indeed, to give the impression that authorities nationwide have embraced the use of pretext investigations by attorneys would be misleading. A number of court and ethics opinions have expressly declined to endorse such conduct.[82] Thus, examples of favorable treatment notwithstanding, uncertainty as to the permissibility of such tactics abounds.

V. Conclusions

As Chief Justice Roger B. Taney observed in 1856, "it is difficult, if not impossible, to enumerate and define, with legal precision, every offence for which an attorney or counsellor ought to be removed."[83] Corresponding sentiments clearly are shared by current members of the bar in New York and elsewhere in wrestling with the ethics of pretext investigations. And yet, navigating the rules governing pretext investigations is perilous for attorneys and clients alike. It is apparent that more consistency and clarity would be of benefit to the bar to avoid the "dog law" abhorred by Jeremy Bentham: a system akin to the way people train dogs by waiting for them to do something wrong and then beating them.[84] Much as the ABA Section on Intellectual Property Law advised the ABA's Ethics 2000 Commission to amend the Model Rules to clarify the permissibility of attorneys engaging in pretext investigations,[85] further guidance from state and national bar associations on this issue increasingly appears needed.

As Barry Temkin has argued, the formalistic and somewhat arbitrary nature of basing the permissibility of pretext investigations on a lawyer's status (e.g., whether a private or governmental attorney, counsel for a criminal defendant or for law enforcement or prosecution, attorney for a holder of intellectual property rights or for someone accused of infringement, or representatives of parties with altogether different interests) is giving way to a more functionalistic analysis based on the attorney's conduct.[86] Temkin suggests five factors that should govern the analysis:

> (a) the directness of the lawyer's involvement in the undercover subterfuge; (b) the significance and depth of the deception; (c) the necessity of the deception; (d) the existence of alternative means to uncover the sought-after evidence; and (e) whether the conduct violates other rules and principles, such as the no-contact rule of ABA Model Rule 4.2.[87]

He also argues that the ABA should amend the Model Rules to permit pretext investigations under circumstances that take these factors into consideration (i.e., when the investigation is necessary, other means of procuring the desired information are not available, the attorney does not participate directly in the dissemblance, and other ethical rules are not violated).[88]

It is worth noting that U.S. District Court judges in New York and New Jersey have expressed a relatively permissive attitude toward intellectual property attorneys' use of pretext investigations.[89] Thus, where litigation of intellectual property rights in those districts is contemplated, the risk of evidence preclusion as a result of engaging in pretext investigations may be less than in other jurisdictions.

Nevertheless, unless and until the New York courts adopt these or other recommendations, practitioners in the state should be mindful that engaging in pretext investigations could amount to violating the NY Rules.

The courts of New York State are not bound to apply the NY Rules in conformity with federal court interpretations. Moreover, neither state nor federal courts are likely to give unconditional approval to such practices, and it remains to be seen whether the Appellate Division committees that are responsible for enforcing attorney discipline would permit them at all, absent direction from the courts. Thus, practitioners should use caution and prudence in deciding whether and how to employ pretext investigations to avoid serving as a test case—and failing the test.

The guidelines of NYCLA 737 would seem to provide a reasonable basis upon which to ground such tactics,[90] at least until a higher controlling authority in the state issues a ruling or opinion on the matter. Paramount concerns should be attention to avoiding unauthorized communication with parties so as not to violate NY Rules 4.2 or 4.3 and exercising diligent supervision over any investigators who act at the attorney's direction to ensure that they are aware of, and conform to, their ethical obligations.

Avoiding direct participation in pretext investigations is also advisable, considering the hostility of court and ethics opinions to such involvement by attorneys. However, should the NY Rules ultimately be amended to accommodate some forms of pretext investigations, it is questionable whether direct attorney involvement should be precluded while indirect involvement is permitted. Currently, attorneys are prevented from circumventing the NY Rules by engaging others to do what they are not themselves permitted to do. If permitting the use of pretext investigations is indeed justified, why should attorneys be forbidden from engaging in them directly?

More to the point, if direct attorney engagement in the dissembling of pretext investigations is deemed inappropriate, how is it any less unfavorable to allow them to do so indirectly, through the acts of another? Allowing pretext investigations only by proxy would be somewhat of an anomaly among the rules, signaling at once the disapprobation, yet permissibility, of certain conduct and creating tension with the repeated admonitions against circumventing the NY Rules by acting through an agent.

By way of comparison, recall that NY Rule 4.2 prohibits lawyers from directly communicating with represented parties, but it does allow them to "cause" their clients to do so and to "counsel" their clients with respect to such communications, a rare example of allowing attorneys to do something through another what they are not allowed to do themselves.[91] In that case, the disparity is supported by significant, independent policy considerations. Adverse clients' direct communication with each other has long been considered helpful in the resolution of disputes, an end furthered by the assistance of their attorneys, whereas prohibiting lawyers from communicating directly with represented parties "carr[ies] on the long tradition of protecting the client-lawyer relationship against the risk of interference and overreaching by lawyers for parties with adverse interests."[92] By contrast, the existence of independent grounds for both permitting pretext investigations and preventing attorney involvement in them is less evident, provided that existing rules are otherwise complied with.

Of course, to ask whether attorneys should be permitted to directly participate in pretext investigations is premature, given that not even proxy investigations have yet been sanctioned. It is to be hoped that greater clarity and certainty on this important and difficult question will be forthcoming.

Endnotes

1. The New York Rules of Professional Conduct, codified at 22 N.Y.C.R.R. Part 1200, became effective on April 1, 2009. The NYSBA published comments to the rules intended to aid attorneys' interpretation and compliance, though the comments were not officially adopted by the courts. *See* New York State Bar Association, *Final New York Rules of Conduct With Comments* (2009), http://www.nysba.org (follow "For Attorneys" hyperlink; then follow "Professional Standards for Attorneys" hyperlink; then follow "Final New York Rules of Conduct with Comments" hyperlink) [hereinafter "NY Rules Comments"]. The NY Rules are formatted as, and borrow extensively from, the American Bar Association Model Rules, after which they largely modeled. *See* New York State Bar Association, *Proposed Rules of Professional Conduct*, vi (2008), http://www.nysba.org (follow "Sections/Committees" hyperlink; then follow "Committee on Standards of Attorney Conduct" hyperlink; then follow "Proposed Rules of Professional Conduct–Approved Nov. 3, 2007" hyperlink) [hereinafter "COSAC Report"]. In adopting this formulation, New York rejected its former Code of Professional Responsibility (NY Code). *Id.* However, the NY Rules retain much of the substance of the NY Code. Roy Simon, *Comparing the New NY Rules of Professional Conduct to the NY Code of Professional Responsibility (Part I)*, N.Y. Prof. Resp. Rep., Feb. 2009, at 1, http://nysba.org (follow "For Attorneys" hyperlink; then follow "Professional Standards for Attorneys" hyperlink; then follow "Chart correlating new NY Rules of Professional Conduct to former Disciplinary Rules" hyperlink). Thus, for currentness and simplicity, when citing to materials that refer to provisions of the NY Code, i.e. opinions and articles written before the NY Rules went into effect, this article will substitute references to the NY Rules corresponding to such provisions of the NY Code (*see id.* at 2–8, providing a table for correlating each NY Rule to a corresponding provision, if any, in the NY Code).
2. David B. Isbell & Lucantonio N. Salvi, *Ethical Responsibility of Lawyers for Deception by Undercover Investigators and Discrimination Testers; An Analysis of the Provisions Prohibiting Misrepresentation Under the Model Rules of Professional Conduct*, 8 Geo. J. Legal Ethics 791, 794 (1995).
3. COSAC Report, *supra* note 1, at 160.
4. Black's Law Dictionary 629 (8th ed. 2004).
5. *Id.* at 998.
6. Isbell & Salvi, *supra* note 2, at 813.
7. Restatement (Third) of The Law Governing Lawyers § 5 cmt. c (2000).
8. Isbell & Salvi, *supra* note 2, at 817 (arguing that construction of the term "misrepresentation" as used in Rule 8.4(c), considered within the context of the rest of the rule, should be limited to "apply only to misrepresentations that manifest a degree of wrongdoing on a par with dishonesty, fraud, and deceit," and, furthermore, not to

encompass misrepresentations prohibited by Rule 4.1, to avoid redundancy in the Rules as a whole).

9. COSAC Report, *supra* note 1, at 161.

10. *See also* NYSBA Rules Comments, *supra* note 1, Rule 4.2 cmt. 11 ("[a]gents for lawyers, such as investigators, are not considered clients within the meaning of this Rule.").

11. *Niesig v. Team I*, 76 N.Y.2d 363, 374 (1990). Note, however, that in a subsequent holding, the New York Court of Appeals held that, in applying this test, "so long as measures are taken to steer clear of privileged or confidential information, adversary counsel may conduct ex parte interviews of an opposing party's *former* employee," so long as counsel "conform[s] to all applicable ethical standards when conducting such interviews" (emphasis added). *Muriel Siebert & Co., Inc. v. Intuit Inc.*, 8 N.Y.3d 506, 511-12. *See* Patrick M. Connors, *The Desert Island Disciplinary Rule*, 239 N.Y. L.J. 3 (2008) (describing *Siebert* in more detail, as well as other cases in which the New York Court of Appeals has interpreted this rule).

12. *See* NYSBA Rules Comments, *supra* note 1, Rule 4.3 cmt. 1.

13. New York County Lawyers Ass'n Comm. on Prof'l Ethics, Formal Op. No. 737, 6 (2007), *available at* http://www.nycla.org/siteFiles/Publications/Publications519_0.pdf [hereinafter "NYCLA Op. 737"].

14. *Id.* at 2 (quoting Black's Law Dictionary 506 (8th ed. 2004)).

15. *Id.*

16. *Id.* at 5-6 (emphasis added).

17. *Gidatex*, 82 F. Supp. 2d 119, 126 (S.D.N.Y. 1999).

18. *Id.* at 120.

19. *Id.* at 126.

20. *Id.*

21. *Mena v. Key Food Stores Co-op., Inc.*, 195 Misc. 2d 402, 403 (2003). At plaintiff's request, her counsel advised her of the legality of secretly tape recording "obscenities, foul language, racial slurs and epithets directed at women and African-Americans" that she alleged were "common parlance" in the defendant's offices. *Id.* at 403. Counsel also obtained the services of, and paid, a private investigator to help plaintiff secretly record in-person and telephone conversations with defendant's employees, and at least partly aided the plaintiff in proper use of recording equipment. *Id.* & n.1.

22. *Id.* at 403.

23. *Id.* at 407.

24. Ass'n for the Bar of the City of New York Committee on Prof. and Jud. Ethics, Formal Op. No. 2003-02 (2003), http://www.nycbar.org/Ethics/eth2003-2.html. *Cf.* False Denial of Secret Tape-Recording Didn't Violate General Rule on Deceit, 25 Laws. Man. on Prof. Conduct (ABA/BNA) 691 (2010) (describing a Vermont case where lawyers were held not to be in violation of Vermont's equivalent of NY Rule 8.4(c) by secretly taping a phone conversation, but to be in violation of equivalent Rule 4.1 for falsely denying the act of recording when asked); *In re* Attorney ST, 621 So.2d 229, 233 (Miss. 1993) (similar holding).

25. *Cartier*, 386 F. Supp. 2d 354 (S.D.N.Y.2005), 386 F. Supp. 2d at 362.

26. *Apple Corps Ltd.*, 15 F.Supp.2d 456 (D.N.J. 1998),15 F. Supp. 2d at 476.

27. *Id.* at 462.

28. *Id.* at 475.

29. *Id.* at 474.

30. *Id.* at 476.

31. *Id.*

32. *Id.*

33. NYCLA Op. 737, *supra* note 13, at 5-6.

34. Michael J. Hutter, *The Case for Adoption of a Uniform Trade Secrets Act in New York*, 10 Alb. L.J. Sci. & Tech. 1, 20 (1999).

35. Jeff Moore, *Sources for Patent Infringement Investigations and Patent Search Services on the Internet* (1998), http:// www.ipmall.info/hosted_resources/bp98/moore.htm.

36. *Kroll v. Finnerty*, 242 F.3d 1359, 1365 (2001).

37. *Buechel v. Bain*, 275 A.D.2d 65, 74 (2000).

38. Representation of Others Before the PTO, 37 C.F.R. pt. 10 (2009).

39. *See supra*, notes 13–16 and accompanying text.

40. *Id.*

41. Barry R. Temkin, *Lying By Proxy: Permissible Trickery and Deception By Undercover Investigators*, Oct. 13 2009, at S8 n.12.

42. Barry R. Temkin, *Deception in Undercover Investigations: Conduct-Based vs. Status-Based Ethical Analysis*, 32 Seattle U. L. Rev. 123, 164 (2008).

43. *Id.*

44. *Id.* at 126.

45. *United States v. Parker*, 165 F. Supp. 2d 431, 439 (W.D.N.Y. 2001).

46. *Id.* at 476.

47. *Id.* at 476-77.

48. Steven C. Bennett, *Ethics of "Pretexting" in a Cyber World*, 41 McGeorge L. Rev. 271, 274 (2010); Megan Browdie & Wei Xiang, Comment, *Chevron Protects Citizens: Reviving the Citizens Protection Act*, 22 Geo. J. Legal Ethics 695, 714 (2009) ; Jeremy Feinberg, *Report on Pretexting–Recent Cases & Ethics Opinions*, N.Y. Prof. Resp. Rep., June. 2009, at 1, 5-6; William H. Fortune, *Lawyers, Covert Activity, and Choice of Evils*, 32 J. Legal Prof. 99, 103 (2008); Isbell & Salvi, *supra* note 2, at 800–01; Gerald B. Lefcourt, *Fighting Fire With Fire: Private Attorneys Using the Same Investigative Techniques as Government Attorneys: The Ethical and Legal Considerations for Attorneys Conducting Investigations*, 36 Hofstra L. Rev. 397, 397–98 (2007); Douglas Richmond, *Deceptive Lawyering*, 74 U. Cin. L. Rev. 577, 591-93 (2005); Temkin, *supra* note 41; Temkin, *supra* note 42, at 143-48.

49. Temkin, *supra* note 42, at 139-140.

50. *In re Gatti*, 8 P.3d 966, 969 (Or. 2000).

51. *Id.*

52. *Id.*

53. *Id.* at 970.

54. *Id.* at 979.

55. *Id.* at 974-75.

56. *Id.* at 976 (emphasis in original).

57. Temkin, *supra* note 42, at 140.

58. In response, Iowa adopted a comment to its Rule 8.4, consisting of language that closely parallels that in Oregon Rule 8.4(b). *See* Iowa Rules of Professional Conduct Rule 8.4 cmt. 6; Tempkin, *supra* note 42, at 155; 16 Iowa Practice Series § 12:4(e) (2009).

59. Formal Op. No. 2005-173, at 482, 483, 485 (2005) [hereinafter "Op. No. 2005-173"].

60. *Id.* ad 483-84.

61. *Id.* ad 484.

62. *Gatti*, 8 P.3d at 970. *Cf. In re Ositis*, 40 P.3d 500, 503-04 (2002) (holding that an attorney had violated Oregon's rules as they existed prior to adoption of current Rule 8.4(b) by directing an investigator to obtain information from a party adverse to his client through dissemblance). In Op. No. 2005-173, the Oregon Board of Governors opined that under current Rule 8.4(b), *Ositis* might have been decided differently because, unlike in *Gatti*, he had not participated directly in any dissemblance (Op. No. 2005-173, *supra* note 59, at 484).

63. Office of Lawyer Reg. v. Hurley, No. 2007AP478-D, slip op. at 2 (Wis. Feb. 11, 2009).

64. *Id.* at 2–3.

65. *Id.* at 3.

66. *Id.*

67. *Id.*

68. *Id.*

69. *Id.* at 4.

70. Wisconsin Rule 4.1, Committee Comment [hereinafter “Wisconsin Committee Comment”].

71. *Hurley*, at 4.

72. Wisconsin Committee Comment, *supra*, note 70.

73. *See supra* note 48.

74. Utah State Bar Ethics Advisory Opinion Committee, Op. No. 02-05 (2005); D.C. Bar Ethics Op. 323 (2002) (which, in support of its holding, cites comment 12 to D.C. Rule 8.4, which reads “[t]he rule is not intended to enlarge or restrict the law enforcement activities of the United States or the District of Columbia which are authorized and permissible under Constitution and the laws of the United States or the District of Columbia. The ‘authorized by law’ proviso to Rule 4.2(a) is intended to permit government conduct that is valid under this law.”).

75. NYCLA Op. 737, *supra* note 13, at 3.

76. NYSBA Rules Comments, *supra* note 1, Rule 4.2 cmt. 5.

77. Virginia State Bar Ethics Counsel Legal Ethics Op. 1845 (2009). *See also* William Wernz, *‘Pretexting,’ Prevaricating and Getting the Facts*, MINNESOTA LAWYER, Oct. 30, 2006, at 1, 2 (“The Minnesota Office of Lawyers Professional Responsibility itself has been known to call the office of a disbarred lawyer, to determine whether the disbarment has actually taken effect—‘Hello, I’m Lynda Olson, and I’m wondering whether Mr. Doe is available for representation in a family law matter.’”).

78. *In re Sablowsky*, 529 A.2d 289, 290 (D.C.C.A. 1987).

79. *Id.* at 291.

80. *Id.* at 294 (Rogers, J., concurring).

81. *Id.* (Nebeker, J., concurring).

82. *See, e.g., In re Wood*, 526 N.W.2d 513 (Wis. 1995) (sanctioning an attorney, who was plaintiff in small claims court, for, among other things, using a pretext investigation to acquire information about the defendant’s automobile insurance policy; though the Wisconsin Rules have since been amended to permit pretext investigations in some circumstances, the fact that the attorney in *In re Wood* could have obtained the insurance policy information through normal discovery procedures, a fact highlighted in the court’s opinion (*id.* at 506), would likely find disfavor by the court even today); *Midwest Motor Sports, Inc. v. Arctic Cat Sales, Inc.*, 144 F. Supp. 2d 1147, 1158 (D.S.D. 2001) (sanctioning attorneys for violating South Dakota’s equivalent of NY Rule 4.2 (prohibiting attorney contact with a represented party) by directing a pretext investigation; interestingly, no violation of South Dakota’s equivalent to NY Rule 4.1 (prohibiting misrepresentation) was discussed in the opinion); *In re Air Crash Disaster*, 909 F. Supp. 1116, 1122, 1123-24 (N.D. Ill. 1995) (under similar circumstances, sanctioning attorneys for violating Illinois’ equivalent of NY Rule 4.2 and, in addition, 4.3 (prohibiting contact with unrepresented persons)); *Curatola v. Am. Electric Power*, 2008 WL 2120840, *3-*4 (S.D.Ohio 2008) (sanctioning an attorney for violating Ohio’s equivalent to NY Rule 4.2 by initiating a pretext investigation to an adversary in a civil litigation suit, though the severity of the sanction was mitigated in part because the court found that the attorney did not intend for the inappropriate contact to occur); Philadelphia Bar Ass’n Prof. Guidance Committee, Ethics Op. No. 2009-02 (2009) (holding that an attorney may not engage in the dissemblance of hiring a third party to “friend,” through social networking websites, an adversarial witness in a lawsuit); *In re Pautler*, 47 P.3d 1175, 1178, 1182 (Colo. 2002) (a Deputy District Attorney was sanctioned for inducing a murderer and rapist to surrender peacefully by posing as a public defender on the telephone, deemed violations of Colorado’s equivalents of NY Rules 4.3 and 8.4(c)).

83. Ex parte Secombe, 60 U.S. (19 How) 9, 14 (1856).

84. 5 JEREMY BENTHAM, THE WORKS OF JEREMY BENTHAM 235 (1843), referred to in *In re* Sablowsky, 529 A.2d at 294 (Nebeker, J., concurring).

85. ABA Comm’n on Evaluation of Rules of Prof. Conduct, Meeting Minutes, Aug.6–Aug. 8, 1999, http://www.abanet.org/cpr/e2k/080699mtg.html.

86. Temkin, *supra* note 42, at 175.

87. *Id.*

88. *Id.*

89. *See supra* notes 17–20, 25–32 and accompanying text.

90. *See* NYCLA Op. 737, *supra* note 13, and associated text.

91. *See supra* note 10 and accompanying text.

92. COSAC Report, *supra* note 1, at 163.

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The Legal Framework for Trademark Licensing Agreements in Brazil

By Otavio Padilha Velasco

I. Introduction

The Brazilian legal system is rooted in Roman Civil Law. Legal rules are derived primarily from the Constitution, which is supplemented by more specific codes, laws, statutes, and administrative acts. Many pieces of legislation may touch trademark licensing relationships under Brazilian law—the Constitution, Civil Code, Industrial Property Law, Consumer Code, Taxation Code, Penal Code, treaties, etc. Given this complex legal framework, the purpose of this article is to provide basic procedural knowledge relevant to trademark licensing in Brazil.

II. The Role Played by the Brazilian Trademark Office

The Brazilian Constitution and Law 9,279/96 (IP Law) provide that a trademark is property granted by the State after a "first to file" system prosecution at the Brazilian Patent and Trademark Office (BPTO). The BPTO also assists the Brazilian Tax and Financial Authorities in order to avoid undue remittances abroad and to confirm that taxes are being correctly calculated and paid. The BPTO does not authorize the remittance of royalties if the licensed trademark is neither duly registered nor filed. Because Brazil has not yet adhered to the Madrid Protocol, the filing of trademarks still must take place in the BPTO in order to be protected in Brazil.

If a trademark is not used within five years from the date of registration, the registration may be attacked by third parties and may be cancelled due to lack of use. Once the trademark is duly registered, or at least pending, the trademark licensing agreement must be recorded at the BPTO for the following purposes:

1. To put third parties on notice. If the agreement is not recorded, parties will not have prima facie rights if enforcement is necessary. In practical terms, the chances of prevailing in a legal or administrative procedure against a third party are reduced by failure to record, particularly in cases involving parallel importation, since the infringer is not presumed to know of an unrecorded license agreement.

2. To enable payment of royalties abroad. Taking into account that IP rights are intangible, the BPTO cooperates with the Brazilian Tax and Financial Authorities to avoid undue payments abroad and to ensure that taxes are properly charged and paid.

3. To authorize the licensee to deduct from taxes amounts remitted. A portion of the royalties paid for the license of trademarks can be deducted by the licensee from its income taxes as a business expense.

During the recording procedure, the BPTO usually also will analyze other matters. For example, if the licensor is a parent company with more than a fifty percent interest in the licensee, the remittance of royalties and resulting tax deduction are limited to one percent of the gross revenue derived from the licensee's exploitation of the trademark. If the trademark is directly related to a patent or to technological know-how, the limitation may vary between one percent and five percent, depending on the field of business as provided for by Ministerial Ordinance 436/58.

On the other hand, if the licensee is not controlled by the licensor, remittance of royalties is unlimited as long as the amount agreed to by the parties is in accordance with the price commonly used in the particular market. The deduction, however, still will be limited by Ministerial Ordinance 436/58.

III. Recommended License Terms

Some basic clauses that should be contemplated in licensing agreements include:

- Grant of a trademark license. For recording purposes, the BPTO will require the number of the pending applications/registrations licensed.
- Right to assign/sublicense. If not expressly authorized, the trademark cannot be assigned nor sublicensed.
- Description of the activities to be performed by the licensee.
- Specification of the licensor's obligations.
- Specification of the licensee's obligations.
- Training; know-how; marketing; quality control.
- Remuneration, including advertising fees, minimum insurance, and rent of equipment or place of business.
- Territorial limitation/exclusivity.
- Period of contract and renewal.
- Licensee's limitations on the use of trademarks and know-how and on the commercialization of products/services.

- Rules concerning termination of the contract; bankruptcy; jurisdiction over disputes; enforcement, and
- Status of the licensee after the expiration of the agreement regarding know-how / industrial secrets and competing activities in relation to the licensor.

IV. The New Civil Code: Principles of Good Faith and Social Purpose

The most important recent development in the New Civil Code (NCC) related to contract law has been the introduction of two principles developed by the local courts that govern the execution and efficacy of commercial agreements. These are the Principle of Good Faith and the Principle of the Social Purpose. The adoption of these principles in the NCC provides judges adjudicating disputes with a basis for thoroughly examining commercial agreements and reviewing clauses based on the need to satisfy the general interest of the parties implied in the agreement. This is new in Brazilian contract law, since under the prior Civil Code, mere compliance with written obligations would suffice to meet the purpose of agreement. The new law obliges the parties to adopt the duty of loyalty and good faith in relation to the other party.

The Principle of Good Faith, provided for by articles 113 and 442, is considered an implied covenant of commercial agreements. It is viewed as the duty of the contracting parties to cooperate with each other in order to advance specific interests in a manner that they could not if acting alone. There is, therefore, a general duty of collaboration and an expectation of loyalty on the part of the parties in the negotiation, execution, and termination of the agreement.

Indeed, considering that all agreements have a clear objective, it is reasonable to expect certain specific patterns of behavior from each of the parties that go beyond the "duty of no harm" or avoiding conduct calculated to seriously damage or destroy a relationship. This behavior is based on the obligation to collaborate (positively) and to take steps to reach the outlined objectives. It is expected that during the negotiation and operation of the agreement, the parties will take all steps necessary to prevent damage to any of the parties.

The Principle of Social Purpose, introduced in article 421 of the NCC, is conceptually related to the Principle of Good Faith. It derives from the concept of cooperation of the contracting parties to reach the economic goals set by the parties in the negotiation and execution of the agreement. Under this principle, in case of disputes, judges may modify some provisions of the agreement if it is shown that the terms and conditions of the agreement affect the balance of rights and obligations assumed by the parties, including fees that may financially overburden one of them.

V. Consumer Protection

Another important body of law for entrepreneurs interested in investing in the Brazilian market to be aware of is the Consumer Protection Code (*Código de Defesa do Consumidor* (CDC)), which is intended primarily to protect consumers against abuses and to assure harmony and transparency in consumer relations. As the Brazilian Labor Code (*Consolidação da Leis Trabalhistas* (CLT)) was implemented to stabilize relations between workers and their employers, the CDC is based on the premise that the consumer relation is unequal, favoring the product / service supplier.

Consumer protection is a principle of economic order established in article 170, item VI of the Brazilian Constitution, reflecting the proposition that the relationship between the supplier and the purchaser is essential in a "consumption society" for the competitiveness of the companies and the development of the Brazilian capitalist system based on the well-being of individuals and the maxim of justice.

A. Adhesion contracts

Aiming to prevent abusive contracts, article 51 of the CDC contains several provisions intended to protect the consumer. For example, the supplier cannot (i) transfer its legal responsibilities to third parties; (ii) invert the burden of proof in a lawsuit; (iii) unilaterally change prices; or (iv) unilaterally terminate an agreement without vesting the consumer with the same right.

The CDC also provides that the clauses of this type of contract must be written in a clear and comprehensible manner. Any provisions that restrict any right held by the consumer must be drafted so as to emphasize the restriction, thus allowing for easy and immediate comprehension.

Further, article 423 of the NCC provides that any ambiguous and conflicting clauses established in the adhesion agreements shall be construed in favor of the consumer, confirming the provisions established in Section III of the CDC.

B. Statutory warranty

Another important aspect of Brazilian consumer protection law is the difference between a contractual warranty and a statutory warranty. While the former is the warranty set forth in the contract (i.e., voluntarily provided by the supplier), the latter is established by law and belongs to the consumer irrespective of any other covenant. Under the statutory warranty, the purchaser is entitled to the repair or exchange of the product purchased or, in the case of a service, to have the service redone. The period established in the CDC to exercise such rights is 90 days in the case of durable goods and 30 days in the case of non-durable goods. Any contractual provision establishing a shorter period shall be deemed void.

C. Liability *strictu senso*

Brazilian consumer protection law adopted the liability *strictu senso* principle relating to indemnification for the damages caused by or derived from consumer relations. This means that irrespective of fault, the supplier must repair the damage caused to the consumer by the supplier or by the products or services provided. In practical terms, the consumer may make a damages claim against any of the companies engaged in placing the product or service in the market (manufacturer, distributor, seller—all defined in the CDC as suppliers). The company that bears the loss caused to the consumer is entitled to proceed in court against the other suppliers that jointly were responsible for causing the damage.

Liability *strictu senso* excludes liability where the entrepreneur's products or services did not cause damage to the consumer, namely: (i) upon proof that the entrepreneur's company did not participate in the placement of the product / service in the market; (ii) despite having placed the product / service in the market, upon proof that no defect exists; (iii) upon proof that the defect was caused exclusively by the consumer. These rules reflect the premise that the supplier must assume risks inherent to its business and, thus, in no cases other than these three may liability for indemnification be excluded. These are rules of public order and, as such, must be complied with by foreign companies that are engaged in activities within Brazil.

VI. Conclusion

This brief overview of aspects of Brazilian commercial law should help U.S. lawyers to better understand the legal parameters bearing upon trademark licensing agreements in Brazil and to assist clients seeking to enter the Brazilian market.

Otavio Padilha Velasco is a lawyer with Soerensen Garcia Advogados Associados in Rio de Janeiro, Brazil.

First Annual General Counsel Intellectual Property Forum

The First Annual General Counsel Intellectual Property Forum got off to a great start on September 28, 2010. In another program conceived by former IP Law Section Chair Joyce Creidy (Thomson Reuters), the Forum targeted an underrepresented target group within the Section: in-house counsel. The program was titled "How General Counsel Can Increase Revenue and Market Share With an Effective IP Strategy" and offered 1.5 CLE credits.

The Forum was an opportunity for GCs to discuss intellectual property as a means to increase revenue and market share for a sustainable competitive advantage in the worldwide marketplace. The purpose was to discuss how implementing a deliberate policy for development, protection, management, and monetization of IP can make the difference between a company being just a player and being a leader. The Forum noted how GCs can add significant value to a company's bottom line by taking a tactical approach to utilizing a company's IP to its fullest potential.

The discussion was moderated by Michelle Francis, former Global Head of IP for News Corporation and currently Principal at The Francis Company, and the speakers were Margaret Walker, Associate General IP Counsel for Xerox Corporation, and Tim Lynch, Managing Director of IP Transactions and Vice President of Legal for Eastman Kodak.

The panelists and attendees noted the tension between legal protection and revenue generation. Michelle pointed out that a forward-thinking GC can get educated about IP and have conversations at a high level within his or her company to talk about what the GC sees as possible. And then the GC can set up businesspeople in the right way (including rejiggering budgets, setting up efficient processes, and having appropriate staffing) to move forward. If GCs think like businesspeople they can structure processes within a legal framework.

Margaret gave the trademarks perspective from her experiences at Xerox, with her theme being to listen to your IP attorneys. Xerox went through tough times in early 2000 and had to put a security interest on its trademarks to secure a loan. The key for Xerox was to license the XEROX mark to create an annual income annuity. Margaret stressed the need for a strong protfolio that is well maintained with good goods and services descriptions. Margaret also noted that education of clients on the importance of IP, and trademarks in particular, is key.

Tim discussed Eastman Kodak's 8000-patent portfolio, with 1000 patents related to digital photo or digital capture that have been monetized through licensing such that the two main licenses generate $950 million per year for Kodak. In terms of market share, these patent licenses have allowed Kodak to be in 85 percent of industry cellphones, video cameras, or single-purpose digital cameras. Tim noted that these revenues and market share were all because back in 1975 someone at Kodak made sure these inventions were protected with patents even though at the time the patents were filed the company was focused on film and did not want to pursue digital to the detriment of film. It was this forward-thinking protection of digital inventions that led to the current success. Tim noted that Kodak did consider other options to licensing its technology to third-party competitors but realized that blocking in consumer electronics generally did not work, and getting an injunction was nearly impossible. Tim said Kodak is constantly auditing its IP to decide whether there is any value in each item or whether to sell off an asset, and recognizes these are difficult decisions that require judgment as to whether to wait and see if an idea takes off.

This topic generated much discussion among the other panelists, as well as the attendees. Xerox and other companies represented noted that auditing your company's IP portfolio is critical and that consultants can be hired to mine portfolios and package assets for sale.

The GCs who attended thought the Forum presented an important topic and great brainstorming event. The IP Law Section is looking forward to its Second Annual GC IP Forum next year with even more in-house GCs in attendance. Thank you to Joyce and to the IP Solutions business of Thomson Reuters for another successful Section event! And special thanks to Naomi Pitts for all her hard work in putting this program together.

Other Recent Intellectual Property Law Section Events

September, 2010—December, 2010

Greentech Committee

On September 14, 2010, the Greentech Committee, co-chaired by Rory J. Radding and Gaston Kroub, met at Morrison & Foerster LLP to discuss "Getting the Greenlight for Green Trademarks."

On November 8, 2010, the Greentech Committee, co-chaired by Rory J. Radding and Gaston Kroub, met at Morrison & Foerster LLP, where Alex Sousa discussed "Protecting and Licensing Green Energy Technologies."

Fall Meeting

On October 7-10, 2010 the Section held its Annual Fall Meeting, co-chaired by Debra I. Resnick and Erica D. Klein, at The Otesaga in Cooperstown, New York. The two-day program, entitled "Money Makes the World Go Round," offered 11 credit hours of MCLE on the following topics: Priceless: When Money Isn't Enough; Keeping the Green: Lessons Learned from Joint Defense Litigation; From Rags to Riches: Brand Rehabilitation and Re-Establishment Ethics in the New Economy; Spreading the Wealth: The Power and Pitfalls of Use and Misuse of Intellectual Property in the Current Economic Landscape; The Global IP Economy: Will Disharmony Prevail? (Don't) Show Me the Money: Recent Damages Trends in Patent Infringement Litigation; and Getting to Green: Taking an Idea from Invention to Market. See pages 30-35 for photos of this event.

Litigation Committee

On November 3, 2010, the Litigation Committee co-chaired by Marc Ari Lieberstein and Eric Roman, held a Roundtable at Kilpatrick Stockton LLP entitled "First Patents, Then Copyrights, Now Trademarks? A Look at *Salinger v. Colting* and Its Future Effect—or Lack Thereof—on Trademark Cases in the Second Circuit." The panelists, Robert N. Potter and Andrew I. Gerber, discussed the *Salinger v. Colting* decision itself and its impact on injunctions in copyright cases; the presumption of irreparable harm in copyright and patent cases; and whether the test from *Salinger v. Colting* will apply to trademark plaintiffs seeking injunctive relief.

Diversity Initiative Committee

On November 19, 2010 the Diversity Initiative Committee, chaired by Joyce L. Creidy, met to discuss a new Special Committee to Study Diversity in the IP Section, led by Annette Kahler. The meeting was hosted by Joyce L. Creidy at the offices of Thomson Reuters.

Trade Secrets Law Committee

On December 14, 2010, the Trade Secrets Law Committee, chaired by Douglas A. Miro, held a Roundtable sponsored by Kilpatrick Stockton LLP entitled "Trade Secrets and Departing Employees." The presenters, Mark W. Robertson and Robert D. Goldstein, discussed using the Computer Fraud and Abuse Act (CFAA) to protect information stored on computers from being stolen by departing employees or being hacked by former employees and whether the inevitable disclosure doctrine justifies barring an employee from taking a new job even in the absence of a non-compete clause.

Transactional Law Committee

On Tuesday, December 14, 2010, the Transactional Law Committee, co-chaired by Erica D. Klein and Robin E. Silverman, met at the offices of Kramer Levin Naftalis & Frankel LLP for an introductory meeting and to exchange ideas on the role and activities of the Committee.

For further information on upcoming Section events and committee meetings, please visit our website http://www.nysba.org/ipl.

Trade Winds

Trade Winds offers Section members a way to keep up on the comings and goings of their colleagues and upcoming events of interest. Has there been a change in your practice? Any recent or forthcoming articles or lecture presentations? Won any awards recently? Please e-mail submissions to Jonathan Bloom at jonathan.bloom@weil.com.

Welcome New Members:

Matthew F. Abbott
Joan C. Acosta
Cary Adickman
Nicholas Fremont Aldrich
Nathaniel Alejandro
Diane Florence Artal
Chelsey Axel
Brian Joseph Bair
Brittany Anne Ballard
Joseph M. Ballerini
Suraj Kumar Balusu
Samuel M. Bayard
Aaron Baynard
Mark Belkin
Elise Bensimon
Vipra Bhardwaj
Susan Eileen Billheimer
Jaimie Michael Bordman
William Joseph Bratton
Megan C. Bright
Kimberly Chela Brown
Christopher Martin Bruno
Michael Buccino
Laurin Trisha Buettner
Litusha Burns
Marla R. Butler
Derrick Carman
Eric Peter Carnevale
James Robert Carpenter
Juliana Barbedo Carvalho
Rebecca Schneider Casas
Lisa Marie Cattan
Henry Chen
Siew Yen Chong
Chang-ning Chou
Deirdre A. Clarke
Akiva Meir Cohen
Kathleen M. Conkey
Thomas Andrew Connors
Andrea Baur Cornwell
Alexander S. Coven
Gregory William Cram
James W. Dabney
Jay S. Davis
Christopher DeLuca
Girvani Dhyani
Philip Gareth Dickson
Keachea Nicole Dixon
Melissa Kay Dobson
Stephen Richard Donnelly
Daniel Francis Dovi
Joseph Anthony Dunne
Jared Eber
Jason L. Ederer
Daan G. Erikson
David Faham
Derek John Famulari
Paul J. Farrell
Mitchell A. Frank
James Samuel Friedman
Eric Brandon Fugett
John Cornell Fuller
Nicholas J. Gallo
Melanie G. Gelfand
David Scott Gelin
Kenneth P. George
David Gerard
Adam Scott Gershenson
Alice Goldmann
Shadaia Maleka Gooden
Barry Mark Greenbaum
Paul Greenberg
Scott D. Greenberg
Thomas Matthew Grove
William Hair
Tracy S. Harrienger
Jeanne Heffernan
Rosa Henriquez
Chris Henry
Christopher P. Hill
Liel Hollander
Fawn M. Horvath
Hillary Hera Hughes
Frank Sebastian Ioppolo
Briana Frances Isiminger
Elana Tori Jacobs
Swatee Jasoria
Aaron David Johnson
Kevin Brad Jordan
Joseph Kamien
Siddhartha Kamisetti
Hasanmeet Kaur
Paul B. Keller
Michael L. Kenny
Dmitriy A. Kheyfits
Esther Kim
Nicholas Jae-Ryoung Kim
Mark N. Kittel
Simone Marie Kovacic
Adam E. Kraidin
Paavana Lakshmi Kumar
Vincent Kung
David Robert Kurlandsky
Susan Schultz Laluk
Paul Thomas Lavoie
David P. Lazenski
Jeong-Ah Joy Lee
Rina E. Lee
Anna Leipsic
Adrienne Lester
Nan Sze Ling
Bobby Ljiljanic
Peter John Lord
Jane Love
Justin A. Maclean
Amit Manu Mahtani
Erika Maurice
Gerard Xavier McCarthy
Conor Vincent McDonald
Bernadette Karen McGann
Joseph O. McPartland
Joanna Merrill
Jayashree Mitra
John Moehringer
Diane Reese Moriarty
Robert H. Morse
Gregory Sonam Mullens
Jennifer Newman
Martha H. Nimmer
Karl Huy Ninh
David L. Nocilly
Eric Null
Arlene D. O'neill
Kenichi Osawa
Martin B. Pavane
Daniel James Perez
Michele Christine Perino
Joseph Petro
Frederick J.M. Price
Shannon Hennessy Pulaski
Tara Ryan Rahemba
Andrew Rausa
Sharon D. Reiche
Heather Joy Reid
Ari L. Reiser
Jordan L. Reitzfeld
Jason Rindenau
Christine Rodil Rivera
Lawrence Rosenthal
Matthew F. Rothstein
Yukiko Ryonai
David Jonathan Saenz
Benjamin Sahl
Shawn Schatzle
Jeremy Schlosser
Gary A. Schonwald
Gary Serbin
Robert Morrow Shaw
Karen Chia-en Shen
Danielle A. Shultz
Elizabeth Silva
Bradley Silver
Joel C. Simon
Sarika Singh
Alexander C. Sirkman
Kaylan Sobel
Alexis N. Stevens
Petra Stewart
Angel Nicole Stull
Caroline Sun
Jeffrey A. Tochner
Kaede Toh
Leon Tsinberg
Irina Vainberg
Meghan Marie Van Horn
Dena Verhoff
Caleb Vesey
Joyce Helen Alexandra Von Natzmer
Yariv Waks
Janet Walker
Jason Weaderhorn
Matthew Weaver
James D. Weinberger
Jonathan S. Wiggins
Theodore Charles Wills
Karen N. Wilson
Jennette Wiser
Stacy Wu
Stephen R. Yoder
Edward Yoo
Sonny Zhiyu Zhan

NEW YORK STATE BAR ASSOCIATION

Annual Meeting of the Intellectual Property Law Section

Tuesday, January 25, 2011 Hilton New York 1335 Avenue of the Americas, New York City	
MORNING PROGRAM, 8:45 a.m. Gramercy Suites A & B, 2nd Floor	**AFTERNOON PROGRAM, 1:50 p.m.** Gramercy Suites A & B, 2nd Floor
LUNCHEON, 12:35 p.m. Murray Hill Suite A, 2nd Floor	**COCKTAIL RECEPTION, 5:20 p.m.** Nassau Suite, 2nd Floor

IMPORTANT INFORMATION

Under New York's MCLE rule, this program has been approved for a total of up to 8.0 credit hours including 6.5 in areas of professional practice and 1.5 in ethics. Other than the ethics portion of the program, this meeting will not qualify for credit for newly admitted attorneys because it is not a basic practical skills program.

Discounts and Scholarships: New York State Bar Association members and non-members may apply for a discount or scholarship to attend this program, based on financial hardship. ***This discount applies to the educational portion of the program only.*** Under that policy, any member of our Association or non-member who has a genuine basis of his her hardship, if approved, can receive a discount or scholarship, depending on the circumstances. A request for a discount or scholarship must be received **ten days prior** to the start of the program. For more details, please contact Linda Castilla at New York State Bar Association, One Elk Street, Albany, New York 12207.

Section Chair
Paul M. Fakler, Esq.
Arent Fox LLP
New York City

Program Co-Chair
Philip Furgang, Esq.
Furgang & Adwar L.L.P.
New York City

Program Co-Chair
Charles E. Miller, Esq.
Dickstein Shapiro LLP
New York City

8:45 - 9:00 am **Welcoming Remarks**
Paul M. Fakler, Esq., Section Chair
Philip Furgang, Esq. and Charles E. Miller, Esq., Program Co-Chairs

9:00 - 9:50 am **Intellectual Property Litigation Year in Review - Part I: Patent Law**

A review of U.S. Appellate Court cases (decided in 2010) with a focus on patentability of biotech inventions, patent description requirements and infringement issues.

Moderator: **Philip Furgang, Esq.,** Furgang & Adwar L.L.P., New York City
Panelists: **Ira Jay Levy, Esq.,** Goodwin Proctor LLP, New York City
Stephen Rabinowitz, Esq., Fried Frank Harris Shriver & Jacobson LLP, New York City

9:50 - 10:40 am **Intellectual Property Litigation Year in Review - Part II: Trademark and Unfair Competition Law**

A review of Appellate Court trademark and unfair competition cases decided in 2010 with a focus on distinctiveness of marks, likelihood of confusion, dilution, trade dress, registration, affirmative defenses, monetary and equitable remedies, insurance issues and abandonment.

Speaker: **Kenneth B. Germain, Esq.,** Wood, Herron & Evans, L.L.P.
University of Dayton, School of Law, Cincinnati, Ohio

10:40 - 10:50 am **Coffee break** - Co-Sponsored by Hiscock & Barclay LLP and Dickstein Shapiro LLP

NYSBA

10:50 - 11:45 am **Current Developments in IP Legislation**

Seldom has Washington seen more IP legislative activity and political infighting than in 2010 -- patent reform, anti-counterfeiting, fashion designs, PTO fee setting authority, false marking legislation, PTO rulemaking .....and the list goes on. With the start of the 112th Congress in 2011, the action is likely to continue unabated. Our panel will address the hot button issues of today and things to watch out for in the future that confront and which will affect everyone in the IP community.

Moderator: **Charles E. Miller, Esq.,** Dickstein Shapiro LLP, New York City
Panelists: **David Boundy, Esq.,** Cantor Fitzgerald, New York City
Dana R. Colarulli, Esq., U.S. Patent and Trademark Office, Washington, DC
David L. Marcus, Esq., Comcast Cable Communications, Philadelphia, Pennsylvania

11:45 am - 12:35 pm **International Counterfeiting - A Plague on the House of IP**

Counterfeiting has become a cross-border phenomenon affecting a wide spectrum of products from clothing - to software - to pharmaceuticals, just to name a few. The cost of these elicit activities to legitimate owners and users of intellectual property has reached staggering proportions and threatens the well-being of industries and people everywhere. Our panel of experts on this ever growing problem will share important insights and information that everyone in the IP community should become familiar with.

Moderator: **Gina Hough, Esq.,** Anderson Kill & Olick, LLP, Washington, DC
Panelists: **Andrea Charters, Esq.,** Rosetta Stone Ltd., Arlington, Virginia
Bret Parker, Esq., Elizabeth Arden, Inc., New York City
Lisa Rogan, Esq., Acushnet Company, Fairhaven, Massachusetts

12:35 - 1:50 pm **Lunch - Hon. Paul R. Michel,** Former Chief Judge (*retired*) of the U.S. Court of Appeals for the Federal Circuit, Washington, DC

1:50 - 2:40 pm **IP Alternative Dispute Resolution - Is it Ready for Prime Time?**

Disputes arise across a broad spectrum of relationships and substantive areas of the law involving intellectual property issues. Our panel will address alternatives to litigation that can best serve the interests and needs of entities both large and small in resolving many of these disputes. They will describe the special advantages of mediation and arbitration in the various contexts in which disputes usually arise.

Moderator: **Thomas L. Creel, Esq.,** Law Offices of Thomas L. Creel PC, New York City
Panelists: **Cheryl H. Agris, Esq.,** Law Offices of Cheryl H. Agris, Pelham
Stephen P. Gilbert, Esq., Bryan Cave LLP, New York City
Charles E. Miller, Esq., Dickstein Shapiro LLP, New York City

2:40 - 3:30 pm **Red State, Blue State: Lawyers, Politics & Moral Counseling**

A film "Red State, Blue State: Lawyers, Politics & Moral Counseling" (with appearances by R.E.M., Ken Starr, and others), will be the starting point for a discussion of critical issues of ethics and professionalism. The film uses the question of why lawyers are more politically liberal than non-lawyers as a way to explore the basis for the dominant view that lawyers should keep their personal moral beliefs separate from their representation of clients. The film considers whether this separation contributes to job dissatisfaction, as well as to complicity with client wrongdoing, and asks if society, clients, and lawyers would benefit if there were a way for lawyers to practice law and take into account moral responsibility.

Speaker: **Prof. Russell C. Pearce,** Fordham University Law School, New York City

3:30 - 3:55 pm **Technology Forecast: Ethical Storm Brewing Over Attorneys Computing in the Cloud and on the Gound**

Are confidential information and privileged material safe in the cloud? What are the ethical and professional concerns over use of servers located somewhere out on the Internet to store your data and run programs? What are counsels' responsibilities in assuring that discarded hard drives, flash drives, PDA, phones and other storage devices are wiped clean of data, including return of leased equipment? What are the risks of using WiFi hotspots at cafés, airports and hotels? What are the ethical concerns about using hotel faxes or outside vendors for copying and scanning? The panel discusses the application of these circumstances to the recently adopted Rules of Professional Conduct.

Panelists: **Richard L. Ravin, Esq.,** Hartman & Winnicki, P.C., Paramus, New Jersey
Ray Mantle, Esq., Office of Ray A. Mantle, Neptune Beach, Florida

3:55 - 4:05 pm **Coffee break** - Sponsored by Kilpatrick Townsend LLP

4:05 - 5:20 pm **Profiting From and Protecting Your Intellectual Property Investments in China**

This topic will reveal what businesses in the United States need to know about venturing into China. From starting up a business to protecting and enforcing intellectual property rights in China, our panelists will discuss best practices and recent updates in China law which will enable those who enter the China market to profit from their investment.

Panelists: **Christopher J. Woods, Esq.**, Kilpatrick Townsend LLP, New York City
Wayne H. Elowe, Esq., Kilpatrick Townsend LLP, Atlanta, Georgia
David J. Johns, Esq., W.L. Gore & Associates, Inc., Flagstaff, Arizona
James J. Zhu, Ph.D., Jun He Law Offices, Palo Alto, CA/Beijing, China

5:20 - 5:25 pm **Annual Law Student Writing Competition**
First Prize: $2,000
Second Prize: $1,000

5:25 - 5:30 pm **Closing Remarks**
Paul M. Fakler, Esq., Section Chair
Philip Furgang, Esq. and Charles E. Miller, Esq., Program Co-Chairs

5:30 - 7:00 pm **Networking Cocktail Reception** - Sponsored by Thomson CompuMark/Thomson Reuters
All Attendees and Speakers are Invited

Accommodations for Persons with Disabilities: NYSBA welcomes participation by individuals with disabilities. NYSBA is committed to complying with all applicable laws that prohibit discrimination against individuals on the basis of disability in the full and equal enjoyment of its goods, services, programs, activities, facilities, privileges, advantages, or accommodations. To request auxiliary aids or services or if you have any questions regarding accessibility, please contact Linda Castilla at 518-487-5562.

For overnight room accommodations, please call the Hilton New York at 1-800-445-8667 and identify yourself as a member of the New York State Bar Association. Room rates are $249.00 for single/double occupancy. Reservations must be made by Monday, December 20, 2010. You also can reserve your overnight room on the web at www.nysba.org/10accomm.

For questions about this specific program, please contact Linda Castilla at 518-487-5562. **For registration questions only, please call 518-487-5621. Fax registration form to 866-680-0946.**

Intellectual Property Law Section

Tuesday, January 25, 2011
Hilton New York
1335 Avenue of the Americas, New York City

Morning Program, 8:45 a.m.
Gramercy Suites A & B, 2nd Floor

Luncheon, 12:35 p.m.
Murray Hill Suite A, 2nd Floor

Afternoon Program, 1:50 p.m.
Gramercy Suites A & B, 2nd Floor

Cocktail Reception, 5:20 p.m.
Nassau Suite, 2nd Floor

MEMBERSHIP APPLICATION

New York State Bar Association

INTELLECTUAL PROPERTY LAW SECTION

Membership in the New York State Bar Association's Intellectual Property Law Section is a valuable way to:

- enhance professional skills;
- keep up-to-date with important developments in the legal profession;
- join colleagues in exciting Section events.

OPPORTUNITIES FOR EDUCATION

The Intellectual Property Law Section offers both the experienced and novice practitioner excellent opportunities to enhance their practical and legal knowledge and expertise. Through Section activities, including conferences on intellectual property (an annual Winter event), members may examine vital legal developments in intellectual property law. The Section's Web site provides current information regarding Section events and offers "members only" access to current issues of *Bright Ideas* and current Committee bulletins providing updates on intellectual property law. The Section sponsors continuing legal education (CLE) credit-bearing programs for Section members at reduced rates. Recent programs offered by the Section related to computer software and biotechnology protection, conducting intellectual property audits, and practical considerations in trade secret law. Now, with Mandatory Continuing Legal Education (MCLE) requirements, Intellectual Property Law Section membership is more valuable than ever before! The Section also sponsors joint programs with Law Schools including an annual writing contest for law students wherein the winning articles appear in an issue of *Bright Ideas*.

OPPORTUNITIES FOR PROFESSIONAL DEVELOPMENT

Intellectual Property Law Section committees address unique issues facing attorneys, the profession and the public. The Section offers opportunities to serve on committees such as Copyright Law; Diversity Initiative; Ethics; Greentech; International IP Law; Internet & Technology Law; Legislative / Amicus; Litigation; Meetings and Membership; Patent Law; Pro Bono and Public Interest; Trademark Law; Trade Secrets; Transactional Law; and Young Lawyers.

Committees allow you to network with other attorneys from across the state and give you the opportunity to research issues and influence the laws that can affect your practice. Committees are also an outstanding way to achieve professional development and recognition. Law students are automatically members of the Young Lawyers Committee. Section members may join more than one committee.

A VOICE IN THE ASSOCIATION

The Intellectual Property Law Section takes positions on major professional issues that affect practitioners and advocates those positions within the New York State Bar Association, the legislature, and the public.

See page 57 to become a member of the Intellectual Property Law Section

COMMITTEE ASSIGNMENT REQUEST

Please designate, from the list below, those committees in which you wish to participate. For a list of Committee Chairs and their e-mail addresses, please refer to page 59 of this issue.

___ Copyright Law (IPS1100)
___ Diversity Initiative (IPS2400)
___ Ethics (IPS2600)
___ Greentech (IPS2800)
___ International Intellectual Property Law (IPS2200)
___ Internet and Technology Law (IPS1800)
___ Legislative / Amicus (IPS2300)
___ Litigation (IPS2500)
___ Patent Law (IPS1300)
___ Pro Bono and Public Interest (IPS2700)
___ Trademark Law (IPS1600)
___ Trade Secrets (IPS1500)
___ Transactional Law (IPS1400)
___ Young Lawyers (IPS1700)

Please e-mail your committee selection(s) to Naomi Pitts at: npitts@nysba.org

* * *

To be eligible for membership in the Intellectual Property Law Section, you first **must** be a member of the NYSBA.

❒ As a member of the NYSBA, I enclose my payment of $30 for Intellectual Property Law Section dues. (Law student rate: $15)

❒ I wish to become a member of the NYSBA and the Intellectual Property Law Section. I enclose both an Association and Section application with my payment.

❒ Please send me a NYSBA application. No payment is enclosed.

Name ____________________

Office ____________________

Office Address ____________________

Home Address ____________________

E-mail Address ____________________

Office Phone No. ____________________

Office Fax No. ____________________

Home Phone No. ____________________

Please return payment and application to:

Membership Department
New York State Bar Association
One Elk Street
Albany, New York 12207
Telephone: 518/487-5577
FAX: 518/487-5579
http://www.nysba.org/membership

ANNOUNCING THE

Intellectual Property Law Section's

ANNUAL LAW STUDENT WRITING COMPETITION

To be presented at the **Annual Meeting of the Intellectual Property Law Section, January 24, 2012, New York, NY** to the authors of the best publishable papers on subjects relating to the protection of intellectual property **not published elsewhere, scheduled for publication, or awarded another prize.**

First Prize: $2,000

Second Prize: $1,000

COMPETITION RULES ARE AS FOLLOWS:

To be eligible for consideration, the paper must be written solely by students in full-time attendance at a law school (day or evening program) located in New York State or by out-of-state students who are members of the Section. One hard copy of the paper and an electronic copy in Word format on a 3.5" H.D. or CD disk must be submitted by mail, postmarked no later than December 7, 2011 to the person named below. As an alternative to sending the disk or CD, the contestant may e-mail the electronic copies, provided that they are e-mailed before 5:00 p.m. EST, December 7, 2011.

Papers will be judged anonymously by the Section and must meet the following criteria or points will be deducted: no longer than 35 pages, double-spaced, including footnotes; and one file with a cover page indicating the submitter's name, law school and expected year of graduation, mailing address, e-mail address, telephone number, and employment information, if applicable.

Winning papers may be published in the Section's publication *Bright Ideas*. Reasonable expenses will be reimbursed to the author of the winning paper for attendance at the Annual Meeting to receive the Award.

The judges reserve the right to: not consider any papers submitted late or with incomplete information, not to publish papers, not award prizes, and/or to determine that no entries are prizeworthy or publishable.

Entries by hard copy and e-mail to: Naomi Pitts, NYSBA, One Elk Street, Albany, NY 12207 (e-mail: npitts@nysba.org). Comments and/or questions may be directed to the Co-Chairs of the Young Lawyers Committee: Lara R. Corchado, 333 4th Street, Brooklyn, NY 11215-2845, (646) 220-8895, lcorchado@gmail.com or Natallia Azava, Law Offices of Peter Thall, 110 West End Avenue, Suite 7K, New York, NY 10023, (212) 245-6221, nazava@thallentlaw.com.

Winners of the 2009 Annual Law Student Writing Competition

First Place
Nonna G. Akopyan
Pace University School of Law

Second Place
Sean Scuderi
St. John's University School of Law

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The Intellectual Property Law Section encourages members to participate in its programs and to contact the Section Officers or Committee Chairs for information.

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Submission of Articles

Anyone wishing to submit an article, announcement, practice tip, etc., for publication in an upcoming issue of *Bright Ideas* is encouraged to do so. Articles should be works of original authorship on any topic relating to intellectual property. Submissions may be of any length.

Submissions should preferably be sent by e-mail to Jonathan Bloom, Editor-in-Chief, at the address indicated on this page. Submissions for the Spring/Summer 2011 issue must be received by February 18, 2011.

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