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CHALLENGING PENDING PATENTS:

Weigh Your Options Carefully

By Nina Schuyler

A recent U.S. Supreme Court decision, *MedImmune, Inc. v. Genentech, Inc.*, has shifted the balance of power between licensees and licensors, removing a big hurdle for licensees seeking to challenge a patent's validity. A licensee is no longer required to terminate its license agreement before seeking a declaratory judgment that a pending patent is invalid, unenforceable or not infringed. While legal experts predict more patent litigation as a result, they don't foresee a deluge.

"Patent litigation is costly and very disruptive to business," says Alan H. Norman, a partner at Thompson Coburn LLP whose practice centers on intellectual property. "There will be more patent litigation, but the floodgates haven't been opened."

Before filing such a suit, a number of factors need to be weighed, including the high cost of litigation and how the market will be reconfigured if the patent is declared invalid.

The New Legal Landscape

In 1997, Genentech and MedImmune, Inc. entered into a license agreement under which MedImmune obtained a license to use Genentech's existing patent, "Cabilly I," and a pending patent, "Cabilly II." When the second patent was issued in 2001, Genentech notified MedImmune that its product, "Synagis," was covered by the patent and MedImmune owed royalties in accordance with the agreement. MedImmune believed the patent was invalid and unenforceable, but continued paying royalties to avoid a patent infringement

lawsuit, which could result in treble damages and attorneys' fees. MedImmune sued Genentech, asking the district court for a declaratory judgment stating the second patent was not enforceable or valid. The judge refused because MedImmune had not stopped paying royalties, so there was no breach of the license agreement, and, consequently, there was no "actual controversy" between the two parties as required by the federal Declaratory Judgment Act (28 USC Section 2201). The Federal Circuit Court affirmed.

The Supreme Court reversed, holding that a patent licensee need not breach its license agreement—such as refusing to pay royalties—in order to file a declaratory judgment action regarding noninfringement, invalidity or unenforceability. "Promising to pay royalties on patents that have not been held invalid does not amount to a promise not to seek a holding of their invalidity," wrote the Court.

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“In this decision, the Supreme Court said you don’t have to risk opening yourself up to treble damages in order to challenge the validity of a patent,” says David B. Jinkins, a partner at Thompson Coburn who focuses on intellectual property litigation. “If you believe a patent is invalid, it’s now easier to file suit.”

What Should You Do?

Whether to file a declaratory judgment action is a complex decision, driven by both legal and economic considerations. Say you find yourself in a situation like MedImmune’s. First, consult a patent attorney, who will determine if royalties need to be paid. If a valid patent covers the product, royalties should be paid. But if the product is not covered or the patent is invalid, in-house counsel need to consider several factors before stopping payments or filing a declaratory judgment action.

Even if a patent is invalid, it might be in the licensee’s best interest to keep the patent alive. “Let’s say MedImmune had a good royalty rate and an exclusive license agreement, which meant it could stop other companies from getting into the market,” says Jinkins. “In that scenario, MedImmune might not want to challenge the patent.”

If counsel concludes that the company’s product does not infringe the patent and a declaratory judgment action seems the best choice, should royalty payments continue? The *MedImmune* case holds you can continue to pay royalties and file a suit, but “even if the licensee wins the litigation, the licensee most likely won’t get the royalty payments back,” says Norman.

Counsel have other costs to consider: Patent litigation is expensive. “A typical suit that goes through trial can cost several million dollars in attorneys’ fees,” says Jinkins. Such suits can require experts and review of hundreds of thousands of documents.

Also weigh royalties paid per unit under the license agreement versus the treble damages possibility should the licensee lose the declaratory judgment action. For instance,

under a license agreement, a licensee may pay \$10/unit in royalties. But if the case is lost, a patent attorney may estimate the jury or court will say a reasonable royalty is \$100/unit. “In that scenario, the licensee will decide to continue paying royalties and not challenge the patent because the exposure is too high,” says Norman.

ACROSS THE BOARD: More Declaratory Judgment Actions?

Justice Thomas was the lone dissenter in this 8-1 decision, and he predicted the decision would have far-reaching consequences. In his dissent, Thomas wrote:

“...the majority has given every patent licensee a cause of action and a free pass around Article III’s requirements for challenging the validity of licensed patents. But the reasoning of today’s opinion applies not just to patent validity suits. Indeed, today’s opinion contains no limiting principle, whatsoever.”

Interestingly, making these similar exposure considerations in a case where “the patent holder’s claim may be so far off that it’s likely the patent holder won’t file suit,” says Norman, the licensee shouldn’t make payments, nor should it file a declaratory judgment action.

What Happens Next

A settlement of litigation often results in a license agreement, says Norman. After this particular Supreme Court decision, when parties negotiate the agreement, the patent holder will most likely want a provision that narrows the circumstances in which a licensee can file a declaratory judgment action.

It is also likely the patent holder will include in the agreement a provision for higher royalties, since it’s now easier to file a suit and challenge a licensing agreement. On the other hand, licensees may be more willing to enter into patent license agreements since it is now easier to take licensors to court.

The Supreme Court decision also left open the question: Where there is an existing product, an existing patent and a license agreement, can a licensee in such a scenario file a declaratory judgment action to challenge the patent’s validity? “We don’t know that yet,” says Norman, “but we’re sure to find out.”

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