May 6, 2014

The Supreme Court in two companion cases this week opened the door wider for prevailing parties in patent cases to recover attorney's fees. One case rejected the Federal Circuit's "overly rigid" test in favor of a much less restrictive test. Its companion changed the standard for review of district court exceptional case decisions, making reversals more difficult to win on appeal.

Initial commentary about these decisions ballyhooed them as welcomed weapons against "patent trolls" that will reduce litigation costs. But, caution is warranted. First, these rules apply to non-practicing and practicing entities alike. Second, these rules apply regardless of whether the prevailing party is the patent owner *or* the accused infringer. Third, these rules will likely increase the costs of individual cases by forcing parties to prepare for the "exceptional case" that may be in any case, and to bring and defend against what may well become "routine" exceptional case motion practice.

Octane Fitness—the "overly rigid" Federal Circuit test rejected

In rejecting the test for an award of attorney's fees mandated by the Federal Circuit since 2005, the Supreme Court held that the prior standard for finding a case "exceptional" under 35 U.S.C. §285 "is unduly rigid, and it impermissibly encumbers the statutory grant of discretion to district courts." *Octane Fitness, LLC v. Icon Health & Fitness, Inc.* (U.S., No. 12-1184, 4/29/14).

Octane Fitness overturned the Federal Circuit's restrictive two-pronged test, which required a showing of *both* objective baselessness and subjective bad faith. The Supreme Court reasoned that "exceptional" as used in Section 285 should have its ordinary meaning:

> "We hold, then, that an 'exceptional' case is simply one that stands out from others with respect to the substantive strength of a party's litigating position (considering both the governing law and the facts of the case) or the unreasonable manner in which the case was litigated."

As a result, "[d]istrict courts may determine whether a case is 'exceptional' in the case-by-case exercise of their discretion, considering the totality of the circumstances."

District judges may now draw on their own reasoning and personal experience—both from private practice and experience on the bench—to assess whether a particular case "stands out from others," without having to delve into the rigid objective/subjective analysis previously mandated by the Federal Circuit.

While the opinion of the Court found the text of Section 285 "patently clear," just what constitutes "one that stands out from others" is far less clear. It is also less than clear who will end up benefitting from this rule—perhaps just lawyers as they now will see more of these motions arguing with hindsight over yet another "totality of the circumstances" test.

Highmark—a new standard of review

To punctuate the point that the "exceptional" case test should not be rigid, in *Highmark Inc. v. Allcare Health Mgmt. Sys., Inc.* (U.S., No. 12-1163, 4/29/14), the Supreme Court held "that an appellate court should apply an abuse-of-discretion standard in reviewing all aspects of a district court's §285 determination." The Court noted that "the text of the statute 'emphasizes the fact that the determination is for the district court,' which 'suggests some deference to the district court upon appeal,'" and that "'as a matter of the sound administration of justice,' the district court 'is better positioned' to decide whether a case is exceptional, because it

lives with the case over a prolonged period of time." (citing *Pierce v. Underwood,* 487 U.S. 552, 559-60 (1988)). Although questions of law may in some cases be relevant to the Section 285 inquiry, "that inquiry generally is, at heart, 'rooted in factual determinations,' *Cooter [& Gell v. Hartmarx Corp.,* 496 U.S. 384, 401 (1990)]."

Thus, the Court jettisoned the Federal Circuit's *de novo* review with the more deferential abuse-of-discretion standard. Again, this ruling applies to both patent trolls and patent practicing entities. Further, the ruling has two edges, applying both to patent owners and to accused infringers.

Practical considerations

Some perspective is warranted. Since the vast majority of patent litigations settle prior to trial, these two decisions will have little impact on those settlements—the statute does not explicitly allow assessing fees for cases that settle—settlements are routine and unexceptional. Only cases that "go the distance" are likely to be impacted. Nevertheless, in the abundance of caution, parties entering into a settlements agreement will likely insist upon a waiver of claims for attorney's fees, costs and other expenses.

A "be careful what you ask for" caution may apply here. Nearly every patent litigator, whether for plaintiff or defendant, pleads "exceptional case" under Section 285. With the new, less restrictive exceptional case test and mandated deference to trial courts, every party should prepare and plan for inevitable motion practice over attorney's fees after a final determination on the merits.

Another practicality in assessing the impact of these decisions is that some litigants have no ability to pay fee awards. For example, collecting fees from a non-practicing entity operating as a shell-company with few assets may be an unsatisfying exercise. Thus, the "most abusive" patent trolls may face little consequence from a Section 285 motion. The same might be said with respect to a defendant that could not pay a judgment in the underlying case.

Nevertheless, while making it considerably easier for courts to impose fees on non-practicing entities, these two decisions will impact all parties—plaintiffs, defendants, competitors and non-practicing entities alike—who advance meritless positions during the course of litigation.

Additionally, these two decisions will inevitably create added considerations and higher stakes in forum selection. District courts that develop track records of "exceptional" case findings may see a reduction in new plaintiff patent suit filings.

Finally, these decisions will necessarily change the dynamic of settlement negotiations, particularly after one party obtains a favorable *Markman* ruling, or other significant rulings. Parties, already held to regular reassessment of their positions, may be facing greater chances of adverse consequences for failure to make such reassessments or doing so poorly.