

**Featured Professionals**

Thomas R. Hipkins

## Avoiding Punitive Damages in Patent Infringement Cases: Staying on the Right Side of the Now-Blurred Line

**Legal Update**

09.19.2016

By Thomas R. Hipkins

The United States Supreme Court's recent *Halo Electronics v. Pulse Electronics* case made it easier for a patent holder to win punitive damages in a patent infringement case. Halo rejected the Court of Appeals for the Federal Circuit's two-part test for deciding whether to award punitive damages as being too rigid. Halo instead gave district courts broad discretion to weigh the facts of each case in determining whether punitive damages are appropriate. In view of this change, companies wanting to avoid punitive patent infringement damages would be wise to revisit their policies on assessing patent infringement risk during product development.

### Background – § 284 and *Seagate*

Punitive damages in patent infringement cases are authorized by statute. Section 284 of the Patent Act provides that, in infringement cases, courts "may increase the damages up to three times the amount found or assessed."

Since 2007, courts had determined whether to increase damages under § 284 based on the rule articulated by the Federal Circuit in *In re Seagate*. The *Seagate* rule required patent holders to prove both of the following elements by clear and convincing evidence:

- (1) the accused infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent
- (2) the risk of infringement was either known or so obvious that it should have been known by the accused infringer

*Seagate* caused a steep decline in the number of punitive patent infringement damages awards.

# Avoiding Punitive Damages in Patent Infringement Cases: Staying on the Right Side of the Now-Blurred Line

## *Halo* – The Parties

The *Halo* decision actually addressed two separate lawsuits that presented the same issue. In one, Halo Electronics won a jury verdict of patent infringement against Pulse Electronics. The jury also found a high probability that the infringement was willful. But the district court did not award punitive damages because Pulse's defense at trial was not objectively baseless, meaning that Halo had not shown objective recklessness under the *Seagate* test. The Federal Circuit affirmed.

In the second lawsuit addressed in the *Halo* decision, Stryker won a jury verdict against Zimmer for willful infringement. The district court awarded \$76.1 million in compensatory damages and another \$152.2 million in punitive damages, citing evidence that Zimmer copied Stryker's products and then chose a high-risk/high-reward strategy of competing immediately and aggressively in the marketplace while opting to worry about the legal consequences later. On appeal, the Federal Circuit vacated the punitive damages award because Zimmer had asserted reasonable defenses at trial, meaning that Stryker had not satisfied the *Seagate* test's objective prong.

## *Halo* – Rejecting *Seagate* and Charting a § 284 Path Forward

In *Halo*, the Supreme Court rejected the Federal Circuit's *Seagate* test as being too rigid and not consistent with the text of § 284. The Court's primary concern was with the *Seagate* rule's objective recklessness requirement. An infringer who clearly subjectively believed its actions carried a serious risk of patent infringement would be shielded from punitive damages if there happened to have been factors that made its actions not objectively reckless. The Court found the *Seagate* rule's objective recklessness requirement to be inconsistent with § 284.

The *Halo* Court emphasized the importance of timing: What did the accused infringer believe about the infringement risk *at the time of the accused infringement*? What the accused infringer did not know (or have reason to know) at the time of the accused infringement is not relevant for purposes of § 284. The Court was especially critical of the *Seagate* rule's consideration of infringement defenses developed after the accused infringement in preparation for trial:

"The existence of such a defense insulates the infringer from enhanced damages, even if he did not act on the basis of the defense or was even aware of it. Under that standard, someone who plunders a patent—infringing it without any reason to suppose his conduct is arguably defensible—can nevertheless escape any comeuppance under § 284 solely on the strength of his attorney's ingenuity."

The *Halo* Court found that whether to award punitive damages under § 284 is best left to the discretion of district courts. This is consistent with the Supreme Court's 2014 *Octane Fitness* case, which gave district courts broad discretion in deciding whether to require a losing party in a patent infringement lawsuit to pay the winning party's attorney's fees. The Court instructed district courts to consult "nearly two

# Avoiding Punitive Damages in Patent Infringement Cases: Staying on the Right Side of the Now-Blurred Line

centuries” of precedent and to reserve punitive damages for only the most egregious infringers—those whose conduct is “characteristic of a pirate.”

## Remand to the Federal Circuit

Since *Halo* was decided, the Federal Circuit has revisited both the Halo/Pulse case and the Stryker/Zimmer case. In the Halo/Pulse case, the Federal Circuit provided additional details on Pulse’s initial analysis of Halo’s patents:

“The president of Pulse contacted a Pulse engineer, who spent about two hours reviewing the Halo patents and concluded that they were invalid in view of prior Pulse products. Pulse did not seek an opinion of counsel on the validity of the Halo patents at that time and continued to sell its surface mount electronic package products. A Pulse witness later testified that she was ‘not aware of anyone in the company ... that made a conscious decision’ that ‘it was permissible to continue selling’ those products.”

The Federal Circuit remanded both cases to their respective district courts to determine, in their discretion, whether to award punitive damages.

## Going Forward – Avoiding Punitive Patent Infringement Damages After *Halo*

It will be interesting to see what the district courts do in the Halo/Pulse and Stryker/Zimmer cases on remand. Did Pulse do enough—a non-lawyer employee concluding that the Halo patents were invalid after a brief review—to avoid punitive damages? Will the Stryker/Zimmer district court reinstate the \$152.2 million in punitive damages?

But the precedential value of what the district courts do will be minimal. District courts deciding whether to award punitive damages will not be bound by what happens in the Halo/Pulse or Stryker/Zimmer cases on remand but will have discretion to act based on the facts of the cases before them.

In addition, in trying to discern what front-end actions are likely to avoid punitive patent infringement damages, we will not be able to rely on uniform, nationwide standards established by the Federal Circuit. The Federal Circuit will review district courts’ § 284 decisions for abuse of discretion. It is possible that the Federal Circuit will establish basic guidelines by reversing a district court for awarding punitive damages when the accused infringer clearly took great care to avoid infringement or for not awarding punitive damages when the accused infringer clearly acted like a pirate. But the vast gray area in between will be left up to the discretion of the various district court judges.

The most straightforward way of minimizing the risk of getting hit with punitive damages for patent infringement is to seek the advice of patent counsel as soon as you become aware of a potentially problematic patent. If your patent counsel

# Avoiding Punitive Damages in Patent Infringement Cases: Staying on the Right Side of the Now-Blurred Line

determines that each claim of the patent is not infringed by your product or invalid (or both) and explains in detail how he/she reached that conclusion (orally or, preferably, in writing), the patent holder will be hard pressed to convince a district court judge that your actions in reliance on the opinion of counsel were “characteristic of a pirate.” Plus, the benefits of asking patent counsel about potential infringement risk extend beyond establishing an evidentiary record for refuting a future request to enhance damages. You may be able to identify infringement issues early on and take corrective action to avoid a dispute altogether.

What is clear is that *Halo* has done away with the safety net that, under *Seagate*’s objective prong, allowed companies to postpone analysis of potentially problematic patents until they were accused of infringement. Under *Halo*, noninfringement or invalidity theories developed after the accused infringement in the course of litigation —theories of which the accused infringer was not aware when deciding whether or not to proceed with the accused conduct—will carry no weight in district court § 284 determinations.

## Conclusion

By entrusting § 284 decisions to the discretion of district court judges, *Halo* blurs the line between what warrants punitive patent infringement damages and what does not. Companies would be wise to revisit how they assess potentially problematic patents in their product development processes to ensure the best chance of staying on the right side of the line.