

University of Missouri School of Law Scholarship Repository

Faculty Publications

Faculty Scholarship

2014

The Standard for Awarding Attorney Fees Under 35 U.S.C. Section 285 to Prevailing Parties in Patent Litigation - Octane Fitness, LLC v. ICON Health & Fitness, Inc. and Highmark, Inc. v. Allcare Health Management Systems

Dennis D. Crouch

University of Missouri School of Law, crouchdd@missouri.edu

Jafon Fearson

Follow this and additional works at: <https://scholarship.law.missouri.edu/facpubs>

 Part of the [Intellectual Property Law Commons](#)

Recommended Citation

Dennis D. Crouch and Jafon Fearson, The Standard for Awarding Attorney Fees Under 35 U.S.C. Section 285 to Prevailing Parties in Patent Litigation - Octane Fitness, LLC v. ICON Health & Fitness, Inc. and Highmark, Inc. v. Allcare Health Management Systems, 41 *Preview of United States Supreme Court Cases* 226 (2014).

Available at: <https://scholarship.law.missouri.edu/facpubs/773>

This Article is brought to you for free and open access by the Faculty Scholarship at University of Missouri School of Law Scholarship Repository. It has been accepted for inclusion in Faculty Publications by an authorized administrator of University of Missouri School of Law Scholarship Repository. For more information, please contact bassettcw@missouri.edu.

The Standard for Awarding Attorney Fees Under 35 U.S.C. § 285 to Prevailing Parties in Patent Litigation

CASE AT A GLANCE

The Supreme Court granted certiorari in two patent infringement cases that both concern shifting of attorney fees under the “exceptional case” standard of 35 U.S.C. § 285. The Federal Circuit has traditionally been resistant to fee shifting awards—especially in cases where an accused infringer is the prevailing party. In *Octane Fitness*, petitioner asks the Court to lower the standard for proving an exceptional case. In *Highmark*, petitioner asks for deference to lower court exceptional case findings.

Octane Fitness, LLC v. ICON Health & Fitness, Inc. and Highmark, Inc. v. Allcare Health Management Systems
Docket Nos. 12-1184 and 12-1163

Argument Date: February 26, 2014
From: The Federal Circuit

by Dennis Crouch and Jafon Fearson
University of Missouri School of Law, Columbia, MO

INTRODUCTION

In the United States, each party to litigation ordinarily pays its own attorney fees regardless of the case outcome. In the patent litigation context, this changes as 35 U.S.C. § 285 provides an avenue for awarding “reasonable attorney fees to the prevailing party” in “exceptional cases” at the discretion of the lower court. However, discretion only goes so far, and the Federal Circuit’s standard for classifying an “exceptional case” has been critiqued as too rigid, tough, and pro-patentee. It is those same complaints that led to reversal by the Supreme Court in a number of other patent cases such as *KSR Int’l. v. Teleflex Inc.*, 550 U.S. 398 (2007) (obviousness) and *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388 (2006) (injunctive relief).

In both *Octane Fitness* and *Highmark*, the Federal Circuit sided with the patentees who lost their infringement actions. In *Octane Fitness*, the Federal Circuit confirmed that the case was not “exceptional,” while in *Highmark*, a divided Federal Circuit reversed an exceptional case finding based upon a de novo appellate review that gave no deference to the district court’s finding that the lawsuit was objectively baseless.

Patent litigation is incredibly expensive, and most patent infringement actions rely on alternative litigation financing such as contingency fee. These two factors suggest that changing the likelihood of fee shifting is a form of tort reform that may greatly alter the risk calculus and the market for patent litigation.

Although separate, the Supreme Court has paired these cases for oral arguments.

ISSUES

In *Octane Fitness*, the question presented is: Does the Federal Circuit’s promulgation of a rigid and exclusive two-part test for determining whether a case is “exceptional” under 35 U.S.C. § 285 improperly appropriate a district court’s discretionary authority to award attorney fees to prevailing accused infringers in contravention of statutory intent and this Court’s precedent, thereby raising the standard for accused infringers (but not patentees) to recoup fees and encouraging patent plaintiffs to bring spurious patent cases to cause competitive harm or coerce unwarranted settlements from defendants?

In *Highmark*, the question presented is: Is a district court’s exceptional case finding under 35 U.S.C. § 285, based on its judgment that a suit is objectively baseless, entitled to deference?

FACTS

ICON originally sued Octane for infringing its patent covering a particular configuration of an elliptical exerciser. U.S. Patent No. 6,019,710. After two years of pretrial litigation, the district court awarded Octane summary judgment of noninfringement. However, the district court refused to then award attorney fees under § 285 based upon the Federal Circuit’s *Brooks Furniture* standard. *Brooks Furniture Mfg., Inc. v. Dutailier Int’l, Inc.*, 393 F.3d 1378 (Fed. Cir. 2005). On appeal, the Federal Circuit affirmed the denial of fees—holding that the court was not prepared “to revisit the settled standard for exceptionality.”

Highmark centers on a computerized health management system covered by Allcare’s U.S. Patent No. 5,301,105. The lawsuit arose when Highmark filed action seeking a declaratory judgment of noninfringement, invalidity, and unenforceability, and Allcare

counterclaimed with allegations that Highmark infringed claims 52, 53, and 102 of the '105 patent. On summary judgment, the district court agreed with Highmark that the challenged claims were not infringed and also awarded attorney fees based upon an exceptional case finding—stating that Allcare had engaged in “the sort of conduct that gives the term ‘patent troll’ its negative connotation.” On appeal, the Federal Circuit confirmed the noninfringement holding but partially reversed the fee award since Allcare’s infringement theory vis-à-vis claim 52 was “not objectively baseless” and none of Allcare’s litigation actions rose to actionable litigation misconduct. Ultimately, the Federal Circuit remanded the case to the district court “for a calculation of attorneys’ fees based on the frivolity of only the 102 claim allegations.” The Federal Circuit gave no deference to the district court conclusion that all of Allcare’s infringement allegations were objectively baseless. Rather, the Federal Circuit reviewed that issue de novo. Although the request for en banc review was denied, five of the eleven voting judges would have reheard the case. One dissent noted that the majority decision “establishes a review standard for exceptional case finding in patent cases that is squarely at odds with the highly deferential review adopted by every regional circuit and the Supreme Court in other areas of law.”

CASE ANALYSIS

The primary focus of both appeals is the exceptional case determination with *Octane* addressing the substantive requirements necessary to prove an exceptional case and *Highmark* addressing the procedural standard of review and level of deference given to the lower court.

U.S. patent infringement litigation typically follows the traditional American Rule that each party is responsible for its own attorney and expert witness fees. The patent statute does provide for a reasonable fee shifting award, but only to the “prevailing party” and only in “exceptional cases.” 35 U.S.C. § 285. The Federal Circuit has established a four-step process for evaluating claims under § 285 that involves determining (1) the prevailing party; (2) whether the case is exceptional; (3) if exceptional, whether a fee award is appropriate; and (4) the amount of the award, if any.

In its 2005 *Brooks Furniture* decision, the Federal Circuit laid down its structure for the exceptional case test. There, the court seemingly spelled out a limited set of actions sufficient to prove an exceptional case. In particular, the court noted that an exceptional case award may only be based upon either (1) material inappropriate conduct; or (2) objectively baseless litigation brought in subjective bad faith. According to the Federal Circuit:

A case may be deemed exceptional when there has been some material inappropriate conduct related to the matter in litigation, such as willful infringement, fraud or inequitable conduct in procuring the patent, misconduct during litigation, vexatious or unjustified litigation, conduct that violates Fed.R.Civ.P. 11, or like infractions . . . Absent misconduct in conduct of the litigation or in securing the patent, sanctions may be imposed against the patentee only if both (1) the litigation is brought in subjective bad faith, and (2) the litigation is objectively baseless.

The test for baseless litigation is derived from the Supreme Court *Noerr-Pennington* line of cases that protect parties who petition the government from being charged with anticompetitive behavior—even when seeking anticompetitive action from the government. That doctrine has been extended to shield private tort actions as well—absent sham litigation. See *Prof'l Real Estate Investors v. Columbia Pictures Indus.*, 508 U.S. 49 (1993) (only sham litigation if both objectively and subjectively baseless).

The language of § 285 has remained unchanged since its enactment as part of the major patent reforms of 1952. The predecessor statute, passed a few years earlier in 1946, was substantially similar but had two major differences. In particular, the 1946 act expressly gave the court “discretion” to award attorney fees to the prevailing party, while the 1952 act removed the “discretion” language and instead indicated that the fee may be awarded “in exceptional cases.” The Senate Report associated with the 1946 act indicates that the statute is not intended to make fee awards an “ordinary thing in patent suits” but instead to reserve such awards for “gross injustice.”

It is not contemplated that the recovery of attorney’s fees will become an ordinary thing in patent suits, but the discretion given the court in this respect, in addition to the present discretion to award triple damages, will discourage infringement of a patent by anyone thinking that all he would be required to pay if he loses the suit would be a royalty. The provision is also made general so as to enable the court to prevent a gross injustice to an alleged infringer.

S. Rep. No. 1503, 79th Cong., 2d Sess. (1946). When the 1952 act was passed, the House Committee Report briefly mentioned the “exceptional case” amendment to the statute—indicating that the phrase “in exceptional cases” has been added as expressing the intention of the present statute as shown by its legislative history and as interpreted by the courts.”

In its briefing, *Octane* argues that the *Brooks Furniture* test is overly constrictive on district court discretion and flawed. In particular, *Octane* argues that the First Amendment concerns that motivate *Noerr-Pennington* are not present in the fee-shifting context and that the result of the *Brooks Furniture* test is a disparate treatment that disfavors awarding fees to accused infringers who prevail at trial in violation of the principles laid down by the Supreme Court in *Fogerty v. Fantasy, Inc.*, 510 U.S. 517 (1994) (holding that plaintiffs and defendants must be treated alike under an analogous fee-shifting provision in copyright law). In the end, *Octane* argues that the test should revert back to an Equitable Discretion Test (EDT), which allows district courts to consider the totality of the circumstances when determining exceptional case fee awards.

In response, *ICON* argues *Octane* has mischaracterized *Brooks Furniture* and that the test is not so restrictive. In particular, *ICON* notes that, under the *Brooks Furniture* test, accused infringers who prevail in litigation can prove an exceptional case by a variety of mechanisms that go well beyond the strict baseless litigation standard. *Brooks Furniture* specifically calls out litigation misconduct, inequitable conduct by the patentee, as well as “vexatious or unjustified litigation” as justification for an exceptional case

finding. More broadly, *Brooks Furniture* identifies the possibility of exceptional case awards based upon any “material inappropriate conduct related to the matter in litigation.” However, ICON agrees that the current test is more restrictive than pure equitable discretion. According to ICON, applying that test would effectively read the phrase “exceptional cases” out of the statute, eliminating a key limitation imposed by Congress.

In deciding patent cases, the Supreme Court frequently considers whether principles in other areas of intellectual property law provide guidance. Here, Octane suggests that the Court consider both trademark and copyright law. The Lanham Act’s fee shifting statute for trademark infringement is textually identical to patent law’s § 285 and the “exceptional case” limitation has been interpreted at the circuit court level as providing equitable discretion to district courts instead of being limited by any rigid formula. *Noxell Corp. v. Firehouse No. 1 Bar-B-Que Restaurant*, 771 F.2d 521, 526 (D.C. Cir. 1985). The *Noxell* case is particularly important here because it was penned by Justice Ginsburg (then Judge Ginsberg) and joined by Justice Scalia (then Judge Scalia) who were colleagues on the D.C. Circuit Court of Appeals before being elevated to the Supreme Court. In *Noxell*, the appellate panel held that bad faith was not necessary for an exceptional case finding. Similarly, Octane argues that in *Fogerty*, the Supreme Court gave equitable discretion to district courts in awarding fees. ICON attempts to distinguish those cases by pointing to the “surprising lack of agreement” as to the meaning of “exceptional case” and by highlighting the less restrictive language of the copyright statute.

Both parties also claim legislative history support. Octane asserts that Congress intended a broad conferral of equitable discretion upon the district courts to grant fee awards to wrongfully accused defendants to prevent “gross injustice[s],” and that the *Brooks Furniture* test conflicts with decades of judicial interpretation of § 285, predating establishment of the Federal Circuit. ICON argues, however, that when Congress actually intends to give district courts discretion in a broad range, it does so expressly and does not confine the exercise of discretion to “exceptional cases.” ICON further points to the fact that Congress affirmatively removed the statute’s pre-1952 reference to discretion in favor of the more particular exceptional case test.

The United States filed an amicus brief strongly in support of Octane. The government relies on legislative history and similar areas of the law such as the Copyright Act and the Lanham Act in its argument that § 285 should be construed to allow a district court to authorize a fee award to a prevailing defendant when it determines—based on its analysis of the totality of circumstances present in each case—that such an award is necessary to prevent gross injustice to that defendant. The United States argues that the Federal Circuit’s *Brooks Furniture* test has diminished § 285’s effectiveness as a tool to discourage abusive patent litigation and mitigate injustice suffered by prevailing parties in particular cases.

At least one amici, the New York IP Law Association, takes a middle ground approach—agreeing with Octane that the bar is too high, but argues against a purely discretionary and nonstructured totality of the circumstances test. A group of companies represented by 3M and General Electric, as amici, also suggest that any approach to

an exceptional case test should focus on bad actions rather than on broad classes of actors, such as nonpracticing entities, and that any test should be balanced.

To be sure, there are instances (some extremely well-publicized) of patent litigation abuse involving non-practicing patent owners who use the courts in an effort to collect large numbers of nuisance settlements. Yet this problem, in the experience of Amici Companies, is no more serious than that created by many infringing defendants who routinely fight off meritorious patent suits by pressing scores of frivolous defenses and counterclaims, and who otherwise rely upon dilatory tactics to force unjust settlements. Accordingly, the focus should be on curbing litigation misconduct wherever it occurs. An evenhanded standard, flexibly applied, allows just that.

In the exceptional case procedural dispute, petitioner Highmark argues that a district court’s determination that a case was “objectively baseless” and thus amenable to an award of attorney fees should receive deferential appellate review rather than the de novo standard applied by the Federal Circuit. Highmark’s principle argument is that the case is controlled by the prior Supreme Court decisions of *Pierce v. Underwood*, 487 U.S. 552 (1988), and *Cooter & Gell v. Hartmarx*, 496 U.S. 384 (1990). In *Pierce*, the Court considered the proper standard of review for fee awards under the Equal Access to Justice Act (EAJA). EAJA authorizes attorney fees when the United States’ position is not “substantially justified,” and Highmark argues that *Pierce*’s proposition that a position is not substantially justified if it has no “reasonable basis in both law and fact,” is a standard effectively identical to the Federal Circuit’s § 285 test, which deems a position objectively baseless if “no reasonable litigant could believe it would succeed.” In *Cooter*, the Court considered the standard of review for decisions imposing Rule 11 sanctions. Prior to *Cooter*, the courts of appeals applied three different standards of review to different kinds of Rule 11 questions—clear-error review regarding the factual basis for a claim, de novo review of findings about whether a claim was “warranted by existing law,” and abuse-of-discretion review of the amount of sanctions imposed. The Federal Circuit adopted this same trifurcated standard for § 285, and Highmark argues that *Cooter* squarely rejects this approach. Highmark further asserts that the Court held that “all aspects” of a district court’s decision to impose Rule 11 sanctions—including its “legal conclusions”—should be reviewed under a unitary, abuse-of-discretion standard. Highmark argues that both *Pierce* and *Cooter* address fee and sanction standards directly analogous to the “objective baselessness” test, and that the Supreme Court in both cases held that appellate courts should review awards under such provisions for abuse of discretion.

Allcare responds that *Pierce* and *Cooter* actually work in its favor. Allcare asserts that *Pierce* noted that smaller dollar amounts counsels in favor of deferential review, while larger awards might suggest a more intensive review; and because patent cases commonly involve large potential damage awards, giving them de novo review does not raise the same concerns as raised in *Pierce* (that providing de novo review would result in the generation of additional appeals that would not otherwise be pursued). Allcare also argues that *Cooter* contradicts Highmark’s position because one of the factors

in favor of deferential review was that the district court was “best situated” to consider the “local bar’s litigation practices” as to when a Rule 11 sanction is warranted. Allcare argues that this is contrary to Congress’s express determination that local variations in the approach to patent litigation are undesirable, by its very creation of the Federal Circuit.

Highmark also argues that the Federal Circuit’s consideration in undertaking de novo review of objective-baselessness findings—namely, that some such findings may turn on legal issues—is flawed in light of *Pierce*; that *Pierce* called for deference even when the lower court determination was “based upon evaluation of the purely legal issue governing the litigation.” Relying again on the Federal Circuit’s role in promoting patent law uniformity, Allcare responds that the uniformity purpose can only be served if the Federal Circuit applies de novo review to questions involving the interpretation of the patent laws. The Federal Circuit decides many more patent cases than any individual district court and therefore, Allcare argues, it is much better suited to decide whether a litigant’s ultimately unsuccessful position was nonetheless an objectively reasonable one.

As in *Octane*, the United States filed an amicus brief supporting the petitioner in *Highmark*. Here, the government argues that an appellate court should review a district court’s exceptional case finding under 35 U.S.C. § 285 with deference, using an abuse-of-discretion standard. The United States offers three guideposts in support of its position: (1) Congress has long vested district courts with broad discretion to determine when fee awards are necessary to prevent gross injustice in appropriate patent cases—as evidenced by the 1946 version of the fee-shifting provision; (2) a sixty-year tradition of deferential review strongly supports an abuse-of-discretion standard; and (3) in both *Pierce* and *Cooter*, the Supreme Court concluded that deferential review was appropriate because baselessness determination involves a fact-intensive analysis that the trial court is best positioned to conduct. However, the government does offer that even under the abuse-of-discretion standard, appellate courts remain free to reverse decisions premised on a pure error of law.

SIGNIFICANCE

Because of the high cost of patent litigation, a reduced standard for fee shifting has the potential of having a large impact on the litigation landscape. And, accused infringers are looking to fee shifting as a mechanism for reducing patent enforcement by nonpracticing entities. However, it is unclear whether an equally applied lower standard would have that result because defendants would also face the risk of being assessed fees. Several years ago, Professor Jay Kesan wrote about fee shifting in patent cases and concluded that there is no deserving theoretical reason for believing the British rule (liberally awarding fees) better promotes efficient primary behavior and that only when the analysis is limited to very specific cases, can it sometimes be shown that the British or American rule is more efficient. Jay P. Kesan, *Carrots and Sticks to Create a Better Patent System*, 17 *Berkeley Tech. L.J.* 763 (2002). However, an unbalanced standard of practice—especially one directed against nonpracticing entities—is likely to have a greater impact. Further, to the extent wide deference is given to district court judges on this issue, we should expect a greater degree of forum shopping and venue battles as parties seek audience before judges more favorable to their particular cause.

In its briefing, ICON suggests that any policy-based shift in the rule should be left to Congress. In fact, several bills are pending in Congress that would shift fees even further than that contemplated by petitioners here. The leading proposal overwhelmingly passed in the House with bipartisan support, is supported by President Obama, and is now being considered in the Senate. See *Innovation Act*, H.R. 3309. The proposed legislation would rewrite § 285 to affirmatively require an award of reasonable fees to the prevailing party unless the court finds that “the position and conduct of the non-prevailing . . . parties were reasonably justified in law and fact” or that special circumstances would make an award unjust. Based upon its strong support, the bill has a substantial likelihood of passing in the Senate this term. If so, the Supreme Court decisions here would have little precedential value beyond the already pending lawsuits. However, a substantial contingent of patent litigators are hoping that Supreme Court action here will temper the fervor for legislative reform.

One spillover in the case may be in the area of willful patent infringement. Under the patent statute, a willful infringer can be assessed with a punitive award of treble damages. In parallel to the exceptional case rule, willfulness requires a finding of both objective and subjective recklessness (or willfulness). There is some likelihood that a shift on the standard of review for exceptional cases will lead to a shift on the willfulness side as well. In its amicus brief, Google cautioned against such a linkage. However, that issue will likely be reserved for future cases.

Dennis Crouch is an associate professor at the University of Missouri School of Law in Columbia, Missouri. He publishes widely on intellectual property law issues, including in his popular blog, *Patently-O*. He can be reached at crouchdd@missouri.edu. Jafon Fearson is a second-year law student at the University of Missouri School of Law. He received his bachelor of science in biomedical engineering and will be graduating from MU LAW in May 2015.

PREVIEW of United States Supreme Court Cases, pages 226–230.
© 2014 American Bar Association.

ATTORNEYS FOR THE PARTIES In *Highmark v. Allcare*
For Petitioner Highmark, Inc. (Neal Kumar Katyal, 202.637.5528)

For Respondent Allcare Health Management System, Inc. (Donald R. Dunner, 202.408.4000)

AMICUS BRIEFS

In Support of Petitioner Highmark, Inc.
Blue Cross Blue Shield Association (Brian Himanshu Pandya, 202.719.7000)

United States (Donald B. Verrilli Jr., Solicitor General, 202.514.2217)

Yahoo!, Inc., the New York Times Company, Netapp, Inc., Medtronic, Inc., General Mills, Inc., EMC Corporation, and Boston Scientific Corporation (Jeffrey A. Lamken, 202.556.2000)