Publication Detail

Related Practice Groups

Appellate and Constitutional Law

Intellectual Property

See more Appellate and Constitutional Law Publications

See more Intellectual Property Publications

Supreme Court Decision Removes One Procedural Obstacle to Federal Lawsuits Challenging Patents

January 11, 2007

In a recent decision of note, the U.S. Supreme Court ruled patent licensees in good standing may challenge the validity of the patent, or assert non-infringement, without first terminating their license agreements. The Court's January 9, 2007 decision in *MedImmune, Inc. v. Genentech, Inc.* allows litigants to seek relief in the form of a declaratory judgment without subjecting themselves to an infringement action that could potentially be crippling. This holding, while particularly significant in potentially exposing more patents to challenges, could also be significant for commercial litigation more generally, because it expands the opportunity to seek a declaration of rights from a federal court *before* damages claims are asserted. The Court's decision left open several significant issues that may still limit declaratory relief, which undoubtedly will generate future litigation.

In 2004, the Court of Appeals for the Federal Circuit, the intermediate court that decides all patent appeals, held that entering into a patent license had precluded the licensee from challenging the patent as invalid - even if the license agreement contained no such explicit restriction. Federal courts' jurisdiction is limited to "Cases" and "Controversies" by Article III of the Constitution. The Federal Circuit had ruled that there cannot be a "case" or "controversy" between a licensor and licensee about the validity of the patent being licensed. If a licensee wanted to challenge the validity of the patent, the Federal Circuit held, it had to first repudiate its license agreement and risk being sued for infringement. Then, if the patent holder sues, the former licensee can counterclaim that the patent is invalid or unenforceable.

Last February, the Supreme Court agreed to decide whether this absolute jurisdictional barrier was correct. In this case, MedImmune had obtained a license from Genentech to manufacture products covered by Genentech's patents and pending applications, in exchange for a royalty. After the license agreement was signed and one of Genentech's pending patents issued, Genentech concluded that one of MedImmune's products, a respiratory drug, was covered by the new patent, and demanded royalties. Genentech threatened to bring an infringement lawsuit if MedImmune refused to pay. MedImmune believed that the Genentech patent was

invalid and unenforceable, and in any event that its product was non-infringing. Nonetheless, not wishing to risk a patent infringement action in which it could face treble damages, liability for attorney's fees, and an injunction forbidding it to sell its product (which accounted for eighty percent of its sales), it paid royalties pursuant to the license, under protest. MedImmune then sued Genentech in federal court, asking for a declaratory judgment that the Genentech patent was invalid, unenforceable, or not infringed. Applying its precedent, the Federal Circuit found no "case" or "controversy" and refused to entertain the lawsuit. The Supreme Court granted MedImmune's petition for certiorari.

In an 8-1 opinion by Justice Antonin Scalia, the Supreme Court ruled for MedImmune. The Court rejected the Federal Circuit's rule and held that licensees can sue for a declaratory judgment, without needing to give up their licenses first. Justice Clarence Thomas was the sole dissenter.

The federal Declaratory Judgment Act allows litigants to obtain an adjudication of their rights without waiting to be sued. For example, a citizen who believes a criminal law is unconstitutional, or preempted by federal law, can sue for a declaratory-judgment to that effect; the citizen does not first have to violate the law and risk prosecution. As long as there is a genuine likelihood that the law would be enforced against that citizen, there is a ripe controversy and the federal courts have jurisdiction.

The Court held in MedImmune's case that the same rule applies in the context of litigation between private parties. If MedImmune could not raise its invalidity, unenforceability, and noninfringement arguments without breaching its license agreement, then it would be forced to take an enormous risk: the respiratory drug in question accounted for 80 percent of its business, and the trebled damages liability could be crippling. Under these circumstances, the Court wrote, litigants need not "bet the farm." Plaintiffs can challenge criminal statutes without violating them, even if the only penalty for violation is a small fine; MedImmune faced "the threat of treble damages and loss of 80 percent of [its] business," which the Supreme Court found "every bit as coercive" as a criminal fine. In other words, the Court concluded that a licensee who pays royalties under a license agreement out of fear of a patent infringement action is being coerced in a way that creates an actual controversy, and therefore confers jurisdiction to seek a declaratory judgment. Accordingly, the Court held that MedImmune had established a genuine controversy with Genentech about the validity of the patent, even though MedImmune had continued to pay royalties to Genentech throughout the dispute.

The Court did strike some significant cautionary notes: First, the holding was limited to the question of federal jurisdiction. Whether MedImmune and similar licensees can *prevail* in declaratory-judgment lawsuits against their licensors is another question, and the Court noted that some license agreements, or even some state contract-law doctrines, may specifically prevent the licensee from bringing a lawsuit to challenge the licensed patent. In that instance, the Supreme Court said, the licensor would "win [the] case *on the merits*," not based on jurisdiction. Thus, a contractual term precluding challenges to the validity of the patents might still result in the licensee losing its case on the merits. The MedImmune agreement apparently did not have an express no-challenge provision, and the Court saw no implicit prohibition; indeed, the Court held that a prohibition on challenging the licensor's patents "can hardly be implied from the mere promise to pay royalties on patents."

Second, the Court noted that declaratory judgments are not always readily available. Ever since the Declaratory Judgment Act was enacted, federal district courts have enjoyed wide discretion to decline declaratory-judgment cases even if they do present a ripe and actual controversy. Although the Supreme Court has listed certain factors that district courts consider in deciding whether to grant a declaratory judgment, the trial courts' discretion is broad, and their decisions to decline jurisdiction are difficult to challenge on appeal. Accordingly, some licensees may not be able to rely on the declaratory-judgment procedure; in that case, they

may have to repudiate their license agreements, defend infringement suits, and assert invalidity and unenforceability as counterclaims. The Supreme Court remanded MedImmune's case to let the district court make its discretionary determination.

The *MedImmune* decision's immediate significance is for patent litigants, who previously had been restricted by the Federal Circuit's holding that licensees must repudiate their agreements, and risk a lawsuit, as the price of admission to federal court. Patents may now be subject to more potential challenges, even by licensees that continue to pay royalties under license agreements. But the decision may also have farther-reaching consequences for any litigant seeking an alternative to high-stakes litigation. Bringing an action for declaratory relief, rather than waiting to be sued or prosecuted, may offer a lower-risk strategy for obtaining a binding determination of one's own legal rights. The Supreme Court's decision appears to make that procedural device available to more litigants.

Gibson, Dunn & Crutcher has one of the country's preeminent practices in both intellectual property and appellate litigation, with lawyers nationwide assisting corporations with their most sensitive and challenging matters. Our lawyers regularly handle complex intellectual-property matters in federal courts nationwide, including the Supreme Court, where Gibson Dunn's client prevailed last Term in Laboratory Corp. of America Holdings v. Metabolite Laboratories*. Our lawyers are available to assist in addressing any questions you may have regarding these issues. Please contact the Gibson Dunn attorney with whom you work, Mark A. Perry (202-887-3667, mperry@gibsondunn.com) or William M. Jay (202-955-8256, wjay@gibsondunn.com) in the firm's Washington, D.C. office, David A. Segal (949-451-3973, dsegal@gibsondunn.com) in the Orange County office, or the following attorneys.*

Appellate and Constitutional Law Group:
Theodore J. Boutrous, Jr. - Los Angeles (213-229-7804, tboutrous@gibsondunn.com)
Miguel A. Estrada - Washington, D.C. (202-955-8257, mestrada@gibsondunn.com)
Daniel M. Kolkey - San Francisco (415-393-8240, dkolkey@gibsondunn.com)
Theodore B. Olson - Washington, D.C. (202-955-8668, tolson@gibsondunn.com)

Intellectual Property Group:
Wayne M. Barsky - Los Angeles (310-557-8183, wbarsky@gibsondunn.com)
Glenn K. Beaton - Denver (303-298-5773, gbeaton@gibsondunn.com)
Josh Krevitt - New York (212-351-2490, jkrevitt@gibsondunn.com)
Denis R. Salmon - Palo Alto (650-849-5301, dsalmon@gibsondunn.com)

© 2007 Gibson, Dunn & Crutcher LLP