The Supreme Court Appears Likely to Place the Burden of Proof in Declaratory-Judgment Actions on the Patentees

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On November 5, the U.S. Supreme Court heard argument in Medtronic, Inc. v. Boston Scientific Corporation (No. 12-1128) — a case that will determine whether the patent holder or the patent licensee bears the burden of proof in an action seeking a declaratory judgment of non-infringement. Although the Court’s decision is not expected for some time, the justices’ questions during oral argument suggest they are likely to place that burden on the patentee. This burden-allocation rule — which would reverse a contrary decision by the U.S. Court of Appeals for the Federal Circuit that placed the burden of proof on the patent licensee — could have significant implications for intellectual property rights holders. Companies that grant licenses to their intellectual property portfolio, particularly as a resolution to patent disputes, should consider potential modifications to their licensing arrangements in order to mitigate the impact of the Supreme Court’s likely decision.

Background
The case arises from a patent dispute between Medtronic, Inc., a medical equipment manufacturer, and Mirowski Family Ventures, LLC (“MVF”), a company holding patents to a cardiac stimulation device. Medtronic obtained a license that permitted it to practice certain MVF patents, in exchange for royalties. The license provided that if MVF (or other licensors) believed any new Medtronic device infringed one of the licensed patents, they could notify Medtronic of the infringement, forcing Medtronic to start paying the royalty for the new device or to have the license terminated. If Medtronic chose to pay the royalty, it nevertheless retained the right to challenge the patent holder’s claim of infringement through a declaratory-judgment action.

In 2007, MVF notified Medtronic that some of its products infringed two of the licensed MVF patents. In response, Medtronic filed a complaint seeking a declaratory judgment of non-infringement as to the asserted patents, while continuing to pay the disputed royalties into an escrow account. Medtronic’s lawsuit was made possible by the Supreme Court’s decision in MedImmune, Inc. v. Genentech, Inc., issued earlier that year. MedImmune held that a patent licensee may file a declaratory-judgment action challenging a patent’s validity without stopping royalty payments (and, consequently, risking liability for patent infringement). Medtronic and MVF disagreed as to who should bear the burden of providing infringement at trial: Medtronic contended that the burden should remain with MVF, as the patentee, while MVF argued that the burden should lie with Medtronic, as the licensee under the license and plaintiff in the declaratory-judgment action.
The district court agreed with Medtronic, concluding that the burden of proving infringement should always reside with the patentee. The Federal Circuit took the opposite stand. While the Federal Circuit acknowledged that the patentee normally bears the burden of proving infringement, it crafted an exception for the specific facts at hand. Namely, in declaratory-judgment actions initiated by the patent licensee where the license prevents the patentee (i.e., licensor) from bringing an infringement counterclaim, the licensee bears the burden of proof. Medtronic successfully petitioned the Supreme Court for certiorari. Medtronic argued that the Federal Circuit’s decision ignored the settled rule that a declaratory-judgment action is simply a procedural device that does not change the traditional burden allocation under the patent law, which places the burden of proving infringement on the patentee. The U.S. Solicitor General and the U.S. Patent and Trademark Office, appearing as amici curiae, supported Medtronic. In addition to endorsing Medtronic’s legal argument, the Solicitor General also warned that the Federal Circuit’s rule would deter licensees from using the declaratory-judgment mechanism, undermining the public’s interest in a prompt and conclusive settlement of patent disputes.

Supreme Court’s Oral Argument

At oral argument, the justices appeared deeply skeptical of the rule fashioned by the Federal Circuit. A number of justices seemed to accept the central premise of Medtronic’s argument — that the Declaratory Judgment Act is a purely procedural mechanism and, therefore, cannot reverse the normal burden-of-proof allocation under substantive patent law. As Justice Scalia emphasized, the Supreme Court “said time and time again that [the Declaratory Judgment Act] doesn’t alter the burden of proof.” The Declaratory Judgment Act, he stressed, enables a licensee to obtain a judicial determination with respect to any infringement without having to incur penalties for non-payment of royalties, but “its purpose is not to shift the burden of proof.”

This view was echoed by Justice Kagan, who disagreed with MVF’s argument that placing the burden of proof in declaratory-judgment actions on the patentee would create “a patent law exception” to the traditional default rule that the plaintiff bears the burden of proof. “It’s not a patent law exception,” she observed. “It’s the recognition that a procedural device that simply changes the nominal status of the parties doesn’t change the substantive rules, and that the burden of proof counts as a substantive issue.” Justice Ginsburg pointed out that the Court’s precedent reaffirming the general rule that the plaintiff must bear the burden of proof — Schaffer v. Weast, 546 U.S. 49 (2005) — was not a declaratory-judgment case, and that the general rule is subject to exceptions. Chief Justice Roberts similarly observed that MVF’s reliance on the general default rule “overlook[ed] the elephant in the room” — the fact that “the relief [the plaintiff licensee was] seeking is protection against the relief that [the patentee] would be seeking but for the declaratory judgment action.”

The justices were similarly skeptical of the Federal Circuit’s distinction between this case and a traditional declaratory action on the basis that Medtronic’s license prevented MVF from filing an infringement counterclaim (because, as long as Medtronic was paying the royalty on the disputed patent, no infringement occurred). As Justice Scalia observed, “it is often the case in declaratory judgment actions that the defendant in the action cannot counterclaim.” Therefore, he asked, “why should the fact that the other side doesn’t have a counterclaim change anything?” Justice Breyer similarly stressed that the only reason MVF cannot bring an infringement counterclaim is because Medtronic has “already agreed that if he loses his suit, he’ll pay [MVF] the money.” In a related point, Justices Kennedy and Kagan observed that MVF would have been able to counterclaim for infringement if Medtronic refused to pay the royalty. Therefore, Justice Kagan noted, the same rule
should apply where, subsequent to the Supreme Court’s MedImmune decision, a licensee seeks a declaratory judgment of non-infringement while continuing to pay the royalty, thereby foreclosing a patent infringement counterclaim.12

The justices also probed the practical consequences of the burden-allocation rule. Justice Scalia appeared concerned that the Federal Circuit’s rule would undermine judicial efficiency by depriving the original declaratory-judgment action of preclusive effect. As he observed, any unsuccessful declaratory-judgment plaintiff could then refuse to pay the royalty and relitigate the infringement issue in any subsequent infringement action, where the burden of proof would shift to the patentee.13 Justice Breyer focused on whether placing the burden of proof on the licensee would unduly disadvantage the party challenging the patent, since the patent holder may be better placed to know how the infringing product violates the patent.14

Both Medtronic’s counsel (former Solicitor General Seth Waxman) and Assistant to the Solicitor General Curtis Gannon, who supported Medtronic, sought to allay concerns that placing the burden of proof on the patent owner would discourage patent holders from enter into licensing agreements as a way to avoid or settle patent disputes. They argued that patent owners would nevertheless retain significant incentives to enter into licensing arrangements, and that they could structure licensing agreements so as to discourage any declaratory-judgment challenges by the licensees or to make the royalty obligations independent from infringement.15

**Possible Outcomes and Practical Implications**

The oral argument strongly suggests that the Supreme Court will reverse the Federal Circuit and hold that the patentee bears the burden of proof in a declaratory-judgment action for non-infringement brought by the licensee. Most of the justices who spoke during the argument appeared to share Medtronic’s view that, as a purely procedural device, the Declaratory Judgment Act cannot reverse the traditional patent-law burden of proof, which resides with the patent holder. The justices appeared unconvinced by the distinction drawn by the Federal Circuit between a declaratory action where the patentee can counterclaim for infringement and a case where the existing license precludes the patentee from filing such a counterclaim.

There is some question as to potential breadth of the Court’s opinion. The precise case before the Court involves a license agreement that required the patentee-licensor to notify the licensee about any perceived infringement, permitted the licensee to seek declaratory judgment while continuing to pay the disputed royalty, and precluded the licensor from filing a counterclaim. Several justices — such as Justices Kennedy, Sotomayor, and Kagan — questioned whether their decision should turn on those case-specific facts, or whether the burden-allocation rule the Supreme Court fashions should apply to other types of licensing agreements as well.16 On the other hand, other justices — notably, Justice Scalia — did not appear to view the case as dependent on the particular terms of the licensing arrangement, but as governed by the general burden-allocation rules for declaratory actions. The Solicitor General endorsed that view.17

Irrespective of its precise scope, the Court’s decision will make it easier for patent licensees to seek declaratory judgment of non-infringement against the patentees-licensors. Although, as Justice Alito observed, the burden-allocation rule will likely be decisive only where the evidence is in relative equipoise,18 it could be outcome determinative in a close case.19 Moreover, the burden-allocation rule may influence the procedure of the declaratory-judgment litigation. District courts may require the party with the burden of proof to be the first to set forth its contentions with respect to infringement.
More importantly, companies that license their intellectual property portfolios — and, in particular, companies that enter into a licensing arrangement to settle a patent dispute — may consider taking steps to reduce any possible incentives for the licensees to bring declaratory-judgment actions. A number of such steps were, in fact, discussed during the argument before the Supreme Court. Specifically, the patent owners may consider the following when structuring their licensing arrangements or dispute-settlement agreements:

- Making the royalty obligations independent from infringement, such as requiring that such licenses be fully paid-up upfront or structuring payments as a percentage of net sales.
- Providing for an automatic increase of the royalty payments in the event the licensee brings a declaratory-judgment action against the licensor.
- Specifying that the filing of a declaratory-judgment action would represent a breach of the license agreement, permitting the patentee to seek appropriate remedies allowed by patent law (such as damages and injunctive relief).
- Providing for license termination if the licensee seeks to reopen issues resolved by the license agreement, permitting the patentee to bring an infringement action.

The Court’s decision is also likely to leave open the question of whether the patentees and the licensees can contract for a different burden-allocation rule in any declaratory-judgment action — a question that Medtronic said the Court need not reach — although some courts have questioned private parties’ ability to contract around such background provisions.

If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings Washington, D.C. lawyers:

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4 Argument Tr. 44:21-45:6; id. at 45:9-17.
5 Argument Tr. 40:18-22.
6 Argument Tr. 30:6-9; id. at 50:16-21.
7 Argument Tr. 44:9-13.
8 Argument Tr. 28:20-22; see also id. at 29:13-19.
9 Argument Tr. 29:6-7.
10 Argument Tr. 31:4-6.
11 Argument Tr. 37:4-8 (Kennedy, J.); id. at 37:14-23 (Kagan, J.); see also id. at 27:21-28:2 (Kennedy, J.).
12 Argument Tr. 37:19-38-2.
13 Argument Tr. 33:4-35:15.
14 Argument Tr. 31:24-32:9; 39-1-40:5.
16 Argument Tr. 6:14-7:2 (Kennedy, J.); id. at 7:10-17 (Kennedy, J.); id. at 11:4-21 (Kagan, J.); id. at 16:11-13 (Sotomayor, J.).
17 Argument Tr. 16:14-19 (argument of Curtis E. Gannon).
18 Argument Tr. 4:16-21.
19 Argument Tr. 4:24-5:6 (argument of Seth P. Waxman).