

Enforcement of Intellectual Property Rights Before the U.S. International Trade Commission:

What's in your non-practicing entity's patent portfolio?

By Charles F. Schill and Jamie B. Beaber¹



Charles F. Schill

1330 Connecticut Ave., NW
Washington DC 20036
Office Tel: 202.429.8162
Fax: 202.429.3902
cschill@steptoe.com

In today's high-tech and increasingly competitive global economy, protecting intellectual property rights is the paramount corporate concern for an increasing number of non-practicing entities. The clash between the predominately manufacturing-based economies of the United States and other developed countries that existed three decades ago and the technology-based sector that rapidly emerged in the late 1980s is over – and the technology sector has won. This shift in the economies of the United States and other developed countries from economies that were primarily focused on tangible assets to economies today that are primarily focused on intangible assets has made enforcing intellectual property rights big business and also has, and will continue to have, a dramatic affect on U.S. international trade laws. One such law, Section 337 of the Tariff Act of 1930, as amended (19 U.S.C. § 1337) – a powerful trade and quasi-intellectual property statute administered by the U.S. International Trade Commission that provides domestic industries with an effective means to protect intellectual property rights from infringing imports – once unavailable to non-practicing entities, has quickly become the statute of choice for a growing number of non-practicing entities seeking to broadly enforce their patent portfolios.

While the *in rem* nature of Section 337 actions, the nationwide jurisdiction of the Commission, and the speed at which such investigations proceed have an obvious appeal to non-practicing entities seeking to broadly and efficiently enforce their intellectual property rights against infringing imports, the domestic industry standing requirement of Section 337 historically relegated such entities to filing multiple federal district court suits at a significant cost disadvantage.

A series of legislative and judicial events beginning in 1988, however, have reshaped Section 337 and created a growing preference for the Commission forum. These legislative and judicial events have not only made Section 337 available to non-practicing entities, but they also have reduced the requisite showing necessary to establish standing before the Commission, while, at the same time, heightening the bar for non-practicing entities to avail themselves to comparable relief before federal district courts. These reforming events include: (1) legislative amendments to Section 337's domestic industry requirement contained in the Omnibus Trade and Competitiveness Act of 1988; (2) a clear trend by the Commission toward interpreting those legislative amendments more broadly; and (3) the U.S. Supreme Court's decision in *eBay, Inc. v. MercExchange*.²



Jamie B. Beaber

1330 Connecticut Ave., NW
Washington DC 20036
Office Tel: 202.429.6286
Cellular Tel: 202.904.7284
Fax: 202.261.7543
jbeaber@steptoe.com

Opening the Door of the U.S. International Trade Commission to Non-practicing Entities

As a trade statute, Section 337 is designed to protect U.S. industries from unfairly traded imports. Accordingly, to invoke the jurisdiction of the Commission in a patent-based proceeding under Section 337, a patent owner must establish that “an industry in the United States, relating to the articles protected by the patent . . . , exists or is in the process of being established.”³ Under Commission precedent, this domestic industry standing requirement consists of a technical prong and an economic prong.⁴ The economic prong of the requirement is satisfied if the economic activities enumerated in the statute occur in the United States at a significant or substantial level. The technical prong of the requirement is satisfied if the patent owner’s economic activities relate to the patent and/or articles protected thereunder.

Prior to passage of the Omnibus Trade and Competitiveness Act of 1988, the Commission strictly construed Section 337 to require actual manufacturing-related activities in the United States, such as “significant investment in plant and equipment” or “significant employment of labor or capital,” to establish the economic prong of domestic industry standing requirement.⁵ However, with the shift of the economic pendulum that began in the mid-1980s, transforming the U.S. economy from one that was predominately based on tangible assets to one predominately based on intangible assets, legislators passed amendments to Section 337 contained in the Omnibus Trade and Competitiveness Act of 1988 to reflect this major reallocation of domestic resources. These amendments, which expressly acknowledged the exponential growth of non-practicing activities in the United States, made clear the legislative intent that the economic prong of the domestic industry requirement could be satisfied not only through actual production-related activities in the United States, but also through “substantial investment in [the] exploitation [of intellectual property rights], including engineering, research and development, or licensing” activities, in the United States.⁶

These amendments, which addressed congressional concern at that time that the Commission was interpreting the domestic industry requirement in an unduly restrictive manner,⁷ opened the door of the Commission to non-practicing entities.

A Clear Trend Toward Reducing the Amount of Domestic Activity Necessary for Non-practicing Entities to Satisfy the Domestic Industry Requirement

The amendments to Section 337 contained in the Omnibus Trade and Competitiveness Act of 1988 arose principally from a 1986 decision of the Commission, overturning the presiding Administrative Law Judge’s finding of a domestic industry based on the patent owner’s licensing program.⁸ Specifically, the Commission, citing the legislative history to the Trade Act of 1974,⁹ found the term “exploitation” of an intellectual property right to mean “exploitation of the right by production in the United States.”¹⁰ The Commission reasoned that “[p]roduction-related activities distinguish a domestic industry from an importer or inventor” – the latter two of which the legislative history suggests are not, on their own, protected by Section 337.¹¹ With the passage of the Omnibus Trade and Competitiveness Act of 1988, however, the term “exploitation” was clarified to include “engineering, research and development, or licensing” activities.¹²

Almost immediately upon its enactment, patent owners began testing the scope of the engineering, research and development, or licensing provision of Section 337 to establish the economic prong of the domestic industry requirement. Due to uncertainty with respect to a domestic industry finding based exclusively on this provision, patent owners initially coupled their engineering, research and development, or licensing activities with traditional production-related activities (in some instances relying, in part, on the production-related activities of their licensees) to establish the economic prong of the domestic industry requirement.¹³

These early efforts to define the scope of the engineering, research and development, or licensing provision were largely successful and resulted in a number of favorable domestic industry determinations based, in part, on the newly-enacted provision. However, important precedent regarding the scope of the engineering, research and development, or licensing provision also resulted from a few such investigations in which the patent owners did not fair so well. Most significant in this regard was an investigation in which the patent owner unsuccessfully sought to establish a domestic industry based primarily on its substantial investment in engineering and research and development activities.¹⁴ Therein, the patent owner claimed that certain engineering and research and development activities, which generally related to the subject area of the patent at issue, were sufficient to meet the requisite standard. Notably, the patent owner had not engaged in any licensing activities related to the patent at issue.¹⁵ Finding that the patent owner failed to make a sufficient domestic industry showing, the presiding Administrative Law Judge opined that relief under Section 337 is contingent upon the existence of a domestic industry “relating to the articles protected by the patent” or “exploiting or practicing the patent in controversy,” not merely devoted to the patent’s general field of technology.¹⁶

Building on the precedent established in these early investigations, including determinations indicating that Congress intended a liberal and flexible interpretation of the domestic industry requirement, in the late 1990s patent owners began to focus on domestic industry claims based primarily on licensing activities. In one of the first of these investigations, the presiding Administrative Law Judge unambiguously stated that a patent owner can establish a domestic industry under Section 337 based solely on licensing activities, and that such a showing does not require the patent owner or its licensees to manufacture a product covered by the patents at issue.¹⁷ These statements signaled a major initial victory for non-practicing entities before the Commission. Unfortunately, because the claims of the patent at issue were found by the Administrative Law Judge to be invalid and not infringed, the Commission affirmed on those bases and took no position on the domestic industry issue. However, patent owners nevertheless seized on the Administrative Law Judge’s opinion and soon thereafter established more meaningful precedent on licensing-based domestic industries.¹⁸

Since that time, the issues regarding domestic industries based solely on licensing activities have focused primarily on the types of licensing investments that the Commission will consider, defining the threshold for meeting the statutory “substantial” requirement, and the showing necessary to establish a domestic licensing industry “in the process of being established.”

With respect to the former, to prove substantial domestic licensing activities the Commission has looked to a number of factors, including investments in licensing efforts (such as employees, facilities and outside counsel legal fees to license and/or enforce the patent), continuing efforts of the patent owner to license the patent, as well as the number of companies licensed under the patent.¹⁹ However, to date, these factors have not been controlling as the Commission has never found a domestic industry to exist based solely on licensing activities in the absence of the receipt of revenues (*i.e.*, royalties) by the patent owner from its licensing activities.²⁰ Accordingly, to establish the existence of a domestic industry (as opposed to a domestic industry in the process of being established) based solely on licensing activities it appears that those efforts must result in a consummated license agreement, pursuant to which the patent owner has received revenues.

As to the showing required to establish the statutory “substantial” threshold, the major obstacle confronted by most non-practicing entities is demonstrating a sufficient nexus between the investment and the patents-in-suit. In this regard, the Commission has “emphasize[d] that there is no minimum monetary expenditure that a complainant must demonstrate to qualify as a domestic industry under the “substantial investment” requirement [T]he requirement for showing the existence of a

domestic industry will depend on the industry in question, and the complainant's relative size . . . , [but] there is no need to define or quantify the industry itself in absolute mathematical terms."²¹

Moreover, even if a non-practicing entity is unable to demonstrate standing by reason of a current domestic industry based on licensing activities, as discussed above, standing may nevertheless be established under the more relaxed nascent domestic industry standard. "An industry is 'in the process of being established' if the [non-practicing entity] 'can demonstrate that it is taking the necessary tangible steps to establish such an industry in the United States,' S. Rep. 100-71 at 130, and there is a 'significant likelihood that the industry requirement will be satisfied in the future.'" H. Rep. 100-40 at 157."²² While, to date, there is little Commission precedent on nascent domestic industries based solely on licensing activities, recent complaints filed before the Commission seek to fill that void.

In light of the foregoing, there is an unmistakable trend by the Commission toward reducing the amount of domestic activity necessary for non-practicing entities to satisfy the domestic industry standing requirement.

The Heightened Bar Post eBay for Non-practicing Entities in Federal District Court

While the bar for non-practicing entities to avail themselves to relief before the Commission under Section 337 has progressively lowered, at the same time, it has become increasingly harder for non-practicing entities to avail themselves to comparable relief before federal district courts.

In *eBay, Inc. v. MercExchange*, the Supreme Court invalidated the Federal Circuit's "general rule" that "a permanent injunction will issue once infringement and validity have been adjudged."²³ Specifically, the Supreme Court, in rejecting the Federal Circuit's general rule "that injunctions should be denied only in the 'unusual' case, under 'exceptional circumstances' and 'in rare instances . . . to protect the public interest,'"²⁴ found that well-established equitable principles require that a patent owner, seeking a permanent injunction in an action under the Patent Act, satisfy the traditional four-factor permanent injunction test applicable to other causes of action. As such, following the Supreme Court's decision in *eBay*, a permanent injunction in a federal district court patent case will issue only if a patent owner demonstrates: "(1) that it has suffered an irreparable injury; (2) that remedies available at law, such as monetary damages, are

inadequate to compensate for that injury; (3) that, considering the balance of hardships between the patent owner and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction."²⁵

In contrast to the permanent injunction test now applicable to patent infringement cases brought before federal district courts, proof of injury in statutory-based Section 337 cases is not a prerequisite to remedial relief. Indeed, in amending Section 337 in the Omnibus Trade and Competitiveness Act of 1988, Congress expressly removed the injury requirement from statutory-based Section 337 cases. Committee reports explain:

The owner of intellectual property has been granted a temporary statutory right to exclude others from making, using, or selling the protected property In return for temporary protection, the owner agrees to make public the intellectual property in question. It is this trade off which creates a public interest in the enforcement of protected intellectual property rights. Any sale in the United States of an infringing product is a sale that rightfully belongs only to the holder or licensee of that property. The importation of any infringing merchandise derogates from the statutory right, diminishes the value of the intellectual property, and thus indirectly harms the public interest. Under such circumstances, the Committee believes that requiring proof of injury, beyond that shown by proof of the infringement of a valid intellectual property right, should not be necessary.²⁶

Accordingly, the first prong of the permanent injunction test is wholly inapplicable to statutory-based Section 337 cases.²⁷ Similarly, because the only remedies statutorily available to the Commission are essentially ones in equity, the second and third prongs of the traditional four-factor permanent injunction test are also not applicable to Section 337 cases.²⁸ The fourth prong of the traditional four-factor test is, however, required by Section 337.

The aforementioned distinction between the federal district court and Commission forums is of particular importance to non-practicing entities which are likely to have difficulty establishing irreparable injury due to the purely economic nature of their business, and thus difficulty in establishing that the remedies available at law are inadequate and that the balance of hardships weighs in favor of a remedy in equity. For these reasons, non-practicing entities can significantly benefit from selecting the Commission forum rather than traditional federal district court litigation where imports are involved. Under Section 337, a non-practicing entity need only establish infringement and that a domestic industry exists relating to the patent at issue to avail itself of relief in the form of an exclusion order and cease-and-desist order. Accordingly, while eBay the entity is probably best known for opening the door to the largest and most diverse store via its online auction site, eBay the case has emerged as a major factor encouraging non-practicing entities to enter the doors of the Commission to resolve patent infringement disputes.

Recent complaints filed under Section 337, most notably *Electronic Devices, Including Handheld Wireless Communications*, filed by Saxon Innovations, LLC, and *Short-Wavelength Light Emitting Diodes, Laser Diodes and Products Containing Same*, filed by Gertrude Neumark Rothschild, reflect a growing preference by non-practicing entities for the Commission forum. This trend is no doubt the result of the legislative and judicial events discussed above. The gain in popularity of the Commission among non-practicing entities shows no signs of weakening and is only likely to increase further as the Commission hands down additional precedent favorable to non-operating entities.

¹ Charles F. Schill is a partner at the law firm of Steptoe & Johnson LLP. Jamie B. Beaber is an associate at the law firm of Steptoe & Johnson LLP. Collectively, Messrs. Schill and Beaber have over 35 years of experience in unfair trade practice litigation, encompassing approximately 100 Section 337 investigations.

² 126 S. Ct. 1837 (2006).

³ 19 U.S.C. § 1337(a)(2).

⁴ *Video Graphics Display Controllers and Products Containing Same*, Inv. No. 337-TA-412, Initial Det. (May 17, 1999).

⁵ See H.R. Rep. No. 93-571, 93rd Cong., 1st Sess., at 78 (1973) (“In cases involving the claims of U.S. patents, the patent must be exploited by production in the United States”); see also S. Rep. No. 100-71, 100th Cong., 1st Sess., at 129 (1987) (“The first two factors in this definition have been relied on in prior Commission decisions finding that an industry exists in the United States.”); H.R. Rep. No. 100-40, 100th Cong., 1st Sess., at 157-58 (1987) (same); 19 U.S.C. § 1337(a)(3)(A)-(B).

⁶ See 19 U.S.C. § 1337(a)(3)(C); see also S. Rep. No. 100-71, 100th Cong., 1st Sess., at 129 (1987) (“The third factor, however, goes beyond the ITC’s recent decisions in this area.”); H.R. Rep. No. 100-40, 100th Cong., 1st Sess., at 157-58 (1987) (same).

⁷ See *Certain Miniature, Battery-Operated, All-Terrain, Wheeled Vehicles*, Inv. No. 337-TA-122, USITC Pub. No. 1300 (1982), *aff’d*, *Schaper Manuf. Co. v. U.S. Int’l Trade Comm’n*, 717 F.2d 1368, 1371-73 (Fed. Cir. 1983); see also *Certain Products with Gremlins Character Depictions*, Inv. No. 337-TA-201, USITC Pub. No. 1815 (1986).

⁸ See *Certain Products with Gremlins Character Depictions*, Inv. No. 337-TA-201, USITC Pub. No. 1815 (1986).

⁹ See H.R. Rep. No. 93-571, 93rd Cong., 1st Sess., at 78 (1973) (“In cases involving the claims of U.S. patents, the patent must be exploited by production in the United States”).

¹⁰ See *id.*; see also *Certain Miniature, Battery-Operated, All-Terrain, Wheeled Vehicles*, Inv. No. 337-TA-122, USITC Pub. No. 1300 (1982), *aff'd*, *Schaper Manuf. Co. v. U.S. Int'l Trade Comm'n*, 717 F.2d 1368, 1371-73 (Fed. Cir. 1983).

¹¹ *Certain Products with Gremlins Character Depictions*, Inv. No. 337-TA-201, USITC Pub. No. 1815 (1986).

¹² See 19 U.S.C. § 1337(a)(3)(C).

¹³ See *Certain Single In-Line Memory Modules and Productions Containing Same*, Inv. No. 337-TA-336, Order No. 8 (Mar. 19, 1992); see also *Certain Integrated Circuit Telecommunication Chips and Products Containing Same Including Dialing Apparatus*, Inv. No. 337-TA-337, Initial Det., USITC Pub. No. 2607 (Mar. 3, 1993).

¹⁴ *Certain Dynamic Sequential Gradient Compression Devices and Component Parts Thereof*, Inv. No. 337-TA-335, USITC Pub. No. 2575 (Comm. Op. on Temp. Relief Nov. 1992).

¹⁵ *Certain Dynamic Sequential Gradient Compression Devices and Component Parts Thereof*, Inv. No. 337-TA-335, USITC Pub. No. 2575 (Comm. Op. on Temp. Relief Nov. 1992).

¹⁶ *Certain Dynamic Sequential Gradient Compression Devices and Component Parts Thereof*, Inv. No. 337-TA-335, USITC Pub. No. 2575 (Comm. Op. on Temp. Relief Nov. 1992). Subsequent precedent has explicitly found that, in relying on licensing activities to establish a domestic industry, the complainant need not show that it or one of its licensees practice the patent-in-suit, but there must be a “nexus” between the activities upon which it relies and the asserted patent. See *Certain Digital Processors and Digital Processing Systems, Components Thereof and Products Containing Same*, Inv. No. 337-TA-559, Initial Det. (May 11, 2007); see also *Certain Semiconductor Chips with Minimized Chip Package Size and Products Containing Same*, Inv. No. 337-TA-630, Order No. 31 (Sept. 16, 2008).

¹⁷ *Digital Satellite System (DSS) Receivers and Components Thereof*, Inv. No. 337-TA-392, Initial Det. (Oct. 20, 1997).

¹⁸ *Certain Semiconductor Chips with Minimized Chip Package Size and Products Containing Same*, Inv. No. 337-TA-432, Order No. 13 (Jan. 24, 2001); *Certain Integrated Circuits, Processes for Making Same, and Products Containing Same*, Inv.

No. 337-TA-450, Initial Det. (May 6, 2002) (“it is not always necessary to show that the products of the complainant or its licensees are covered by the patent. For example, when a domestic industry exists under subsection 337(a)(3)(C) due to a substantial investment made in the licensing of a patent, it is not necessary to prove that a patent holder or licensee is involved in actual domestic product.”).

¹⁹ *Certain Semiconductor Chips with Minimized Chip Package Size and Products Containing Same*, Inv. No. 337-TA-432, Order No. 13 (June 6, 2002); *Certain Digital Satellite System (DSS) Receivers and Components Thereof*, Inv. No. 337-TA-392, Comm. Op., USITC Pub. 3418 (Apr. 2001).

²⁰ *Certain Digital Processors and Digital Processing Systems, Components Thereof and Products Containing Same*, Inv. No. 337-TA-559, Initial Det. (May 11, 2007) (“Commission decisions [] reflect the fact that a complainant’s receipt of royalties is an important factor in determining whether the domestic industry requirement is satisfied There is no Commission precedent for the establishment of a domestic industry based on licensing in which a complainant did not receive any revenue from alleged licensing activities. In fact, in previous investigations in which a complaint successfully relied solely on licensing activities to satisfy section 337(a)(3), the complainant had licenses yielding royalty payments.”); *Certain Semiconductor Chips with Minimized Chip Package Size and Products Containing Same*, Inv. No. 337-TA-630, Order No. 31 (Sept. 16, 2008) (same); *Certain Video Graphics Display Controllers and Products Containing Same*, Inv. No. 337-TA-412, Initial Det., USITC Pub. 3224 (July 19, 1999) (finding a domestic industry where “in exchange for significant monetary

payment, [a company] has licensed [its patent] to at least one third party”); *Certain Zero-Mercury-Added Alkaline Batteries, Parts Thereof and Products Containing Same*, Inv. No. 337-TA-493, Initial Det. (June 2, 2004); *Certain Digital Satellite System (DSS) Receivers and Components Thereof*, Inv. No. 337-TA-392, Comm. Op., USITC Pub. 3418 (Apr. 2001); *compare with Certain Male Prophylactic Devices*, Inv. No. 337-TA-546, Order No. 22 (Mar. 15, 2006) (“It is inconsistent with the purpose of Section 337 to allow legal fees, standing alone, to establish the economic prong of the domestic industry requirement.” “Litigation filed against an accused infringer may be a powerful tool for a patentee’s licensing efforts. Unless those efforts result in a license, however, there is no support for finding that litigation expenses are an investment in licensing.”); *NAND Flash Memory Devices*, Inv. No. 337-TA-553, Initial Det. (2008) (finding that a domestic industry did not exist under Section 337(a)(3)(C) based on the complainant’s investments in legal fees, including litigation fees and license negotiation costs, for services performed on its behalf by outside patent counsel in the United States to cross-license complainant’s patent portfolio to at least ten other semiconductor companies. The exploitation efforts therein had resulted in four signed license agreements and one other completed, although unsigned agreement, yet there was no evidence that any of the licenses resulted in any meaningful or reliable value or consideration to complainant.); *Certain Stringed Musical Instruments and Components Thereof*, Inv. No. 337-TA-586, Comm. Op. (May 16, 2008).

²¹ *Certain Stringed Musical Instruments and Components Thereof*, Inv. No. 337-TA-586, Comm. Op. (May 16, 2008).

²² *Certain Stringed Musical Instruments and Components Thereof*, Inv. No. 337-TA-586, Comm. Op. (May 16, 2008).

²³ 126 S. Ct. 1837, 1841 (2006) (quoting *eBay, Inc. v. MercExchange, LLC*, 401 F.3d 1323, 1338 (Fed. Cir. 2005)).

²⁴ *Id.* at 1841 (quoting *eBay*, 401 F.3d at 1338–39).

²⁵ *Id.*

²⁶ H.R. REP. NO. 100-40, 100th Cong., at 156 (1987).

²⁷ *Certain Baseband Processor Chips and Chipsets, Transmitter and Receiver (Radio) Chips, Power Control Chips,*

and Products Containing Same, Including Cellular Telephone Handsets, Inv. No. 337-TA-543, Comm. Op. (June 19, 2007), providing:

The Commission, in interpreting its organic statute, takes the position that the Tariff Act of 1930, as amended, represents a legislative modification of the traditional test in equity for the following reasons. The Tariff Act of 1930 replaced the monetary remedy of § 316 of the Tariff Act of 1922 with the remedy of exclusion. 19 U.S.C. § 1337(d), (e), (f). This represents a legislative determination that there is an inadequate remedy at law for infringement by importation. Second, the Tariff Act of 1930 was amended in 1988 to remove the requirement of proof of harm to a domestic industry. This represents a legislative determination that it is unnecessary to show irreparable harm to the patentee in the case of infringement by importation . . . The difference between exclusion orders granted under the Tariff Act of 1930, as amended, and injunctions granted under the Patent Act, 35 U.S.C. § 283, is reasonable in light of the long-standing principle that importation is treated differently than domestic activity. See, e.g., *United States v. 12-200-Ft. Reels of Super 8 MM. Film* (Paladini, Claimant), 413 U.S. 123, 125 (1973) (“Import restrictions and searches of persons or packages at the national borders rest on different considerations and different rules of constitutional law from domestic regulations.”) (rejecting facial challenge to § 305(a) of the Tariff Act of 1930, as amended).

²⁸ *Id.*