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SUING AN INFRINGING COMPETITOR'S CUSTOMERS: OR, LIFE UNDER THE SINGLE RECOVERY RULE

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This article considers a patentee's rights against an infringing competitor's customers.¹ First, the various types of infringement under 35 U.S.C. § 271 are set forth. As a product moves along the distribution chain, each actor along that chain may be liable for infringement. As a result, the issue of monetary recovery against these actors may become important.

Suit normally can be filed against infringers wherever they may be along a product distribution chain. In the ordinary course of events, however, there is likely to be only a single recovery of damages. Still, there are several opportunities for creative lawyering around the ordinary situation. These opportunities are discussed below.

I. THE VARIOUS TYPES OF INFRINGEMENT

Section 271 of Title 35 defines several forms of infringement. Section 271(a) defines a direct infringer as anyone who, *inter alia*, "makes, uses, offers to sell [or] sells any patented invention, within the United States"² A manufacturer who makes and sells an infringing product is a direct infringer under each of the making

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1. This article does not address the business or political questions that arise when a patentee and an infringing competitor share customers. Business executives who favor expediency over technical legal niceties most often answer this fairly common question. Instead, the focus here is on what legal options a patentee may pursue.

2. 35 U.S.C. § 271(a) (1994). Section 271(a) states, "Except as otherwise provided in this title, whoever without authority makes, uses, offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent therefor, infringes the patent." *Id.*

and selling clauses.³ A customer of the manufacturing infringer who uses the infringing product also directly infringes under the using clause.⁴ Under the selling clause, a customer who resells the infringing product is also a direct infringer.⁵ Furthermore, a patent that includes component and system claims or combination and subcombination claims can be directly infringed by both the competitor who sells the component and its customer who assembles and sells the component in a system.⁶

Section 271(b) makes the act of active inducement of infringement an infringement itself.⁷ Inducement of infringement of a patent occurs when one knowingly causes, urges, encourages or aids another in infringement, even though the inducer has not itself directly infringed any claim of the patent by making, using or selling the patented invention.⁸ There are a number of recognized indicia of inducement.⁹ However, direct infringement must exist

3. See *Caterpillar Tractor Co. v. International Harvester Co.*, 106 F.2d 769, 774 (9th Cir. 1939) (finding that the manufacture of a patented tractor is considered an infringement regardless of whether the tractor was actually used). See also *Westinghouse Elec. & Mfg. Co. v. Precise Mfg. Corp.*, 11 F.2d 209, 212 (2d Cir. 1926) (concluding that the sale of a non-infringing device is still an infringement of the patent if the device is capable of an infringing use and is sold with the intent that it be used in such a manner); *Bassick Mfg. Co. v. Auto Equip. Co.*, 13 F.2d 463, 464 (7th Cir. 1926) (holding that parts manufactured for use, even if not used, constitute infringement).

4. See *Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., Inc.*, 377 U.S. 476, 484 (1964) (stating, "it has often and clearly been held that unauthorized use, without more, constitutes infringement").

5. *Triangle Conduit & Cable Co., Inc. v. National Elec. Prods. Corp.*, 138 F.2d 46, 48 (3rd Cir. 1943). See also *Green v. Electric Vacuum Cleaner Co., Inc.*, 132 F.2d 312, 314 (6th Cir. 1942) (finding that it was infringement for defendant to buy patented parts of vacuums from junkman and resell them in reconditioned vacuums because the license implied from sales in usual channels of trade does not apply to an article to be scrapped).

6. See *Warner & Swasey Co. v. Held*, 256 F. Supp. 303, 311 (E.D. Wis. 1966) ("supply[ing] patented parts of a patented combination without authority from the patentee to purchasers of the combination is a direct infringement of the claims of the patent on the part and a contributory infringement of claims of the patent on the combination . . .").

7. 35 U.S.C. § 271(b) (1994). The statute provides that "Whoever actively induces infringement of a patent shall be liable as an infringer." *Id.*

8. See *Manville Sales Corp. v. Paramount Sys., Inc.*, 917 F.2d 544, 553 (Fed. Cir. 1990) (stating that specific intent to encourage infringement is an element). *E.g.*, *Fromberg, Inc. v. Thornhill*, 315 F.2d 407, 411 (5th Cir. 1963); *Nationwide Chem. Corp. v. Wright*, 458 F. Supp. 828, 839-40 (M.D. Fla. 1976); *Zenith Labs. Inc. v. Bristol-Myers Squibb Co.*, 19 F.3d 1418, 1423 n.5 (Fed. Cir. 1994).

9. For example, instruction and advertising activities on the part of the seller of a product or providing instructions or directions as to infringing use, can constitute active inducement. *Taylor Engines, Inc. v. All Steel Engines, Inc.*, 192 F.2d 171, 174 (9th Cir. 1951). Design of an infringing item for another also may constitute active inducement. *Id.* Licensing others similarly may constitute active inducement if the licensor provides instructions or plans

before inducing liability can arise.¹⁰

Section 271(c) defines the tort of contributory infringement.¹¹ Contributory infringement requires the sale of a component of a patented machine, combination or composition, or a material or apparatus for use in practicing a patented process, which constitutes a material part of the invention.¹² However, for this activity to constitute contributory infringement, the contributory infringer must know that the component, material or apparatus is specially made or adapted for use in a patent-infringing device.¹³ Furthermore, the material, component or apparatus must not be a staple article or commodity of commerce suitable for substantial non-infringing use.¹⁴ Contributory infringement can only occur if there is direct infringement.¹⁵ The contributory infringer must have known that the combination for which his component was designed had been patented and that its customer was not entitled to practice the patent in issue.¹⁶ However, this knowledge requirement can be satisfied in many ways.¹⁷

II. THE BENEFITS AND PITFALLS OF PURSUING PARALLEL LITIGATION

Part II discusses how courts deal with those situations where more than one patent lawsuit is ongoing among a patentee, its competitor and the competitor's customers.

A. *The "Customer Suit" Exception to the First-Filed Rule*

Absent special circumstances, the first filed suit has priority over a second filed suit in federal court.¹⁸ Typically, later-filed

enabling the licensee to practice the potential product or process, and if there is some connection between the licensee and the act of infringement. *Id.*

10. *Met-Coil Sys. Corp. v. Korners Unlimited, Inc.*, 803 F.2d 684, 687 (Fed. Cir. 1986).

11. 35 U.S.C. § 271(c) (1994). The statute provides:

Whoever offers to sell or sells a component of a patented machine, manufacture, combination or composition, or a material or apparatus for use in practicing a patented process, constituting a material part of the invention, knowing the same to be especially made or especially adapted for use in an infringement of such patent and not a staple article or commodity of commerce suitable for substantial noninfringing use, shall be liable as a contributory infringer.

Id.

12. *Id.*

13. *Id.*

14. *Id.*

15. *Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., Inc.*, 377 U.S. 476, 498-99 (1964).

16. *Id.* at 488.

17. *Id.* at 488-90. For example, it can be satisfied by a notice of infringement.

18. *William Gluckin & Co. v. International Playtex Corp.*, 407 F.2d 177, 178 (2d Cir. 1969).

lawsuits are stayed pending the outcome of the first action. However, one situation commonly justifies a departure from the first-filed rule of priority - the "customer suit" exception. The customer suit exception is applied when "the first suit is filed against a customer who is simply a reseller of the accused goods, while the second suit is a declaratory action brought by the manufacturer" of the goods against the patentee.¹⁹ In this situation, the first-filed suit against the reseller is likely to be stayed, while the manufacturer pursues the litigation against the patentee.

For example, in *William Gluckin & Co. v. International Playtex Corp.*, Playtex brought a patent infringement case against Woolworth's in a Georgia federal district court alleging Woolworth's was selling a patented brassiere in its Gainesville, Georgia store.²⁰ The manufacturer of the alleged infringing brassiere, Gluckin, brought a declaratory judgment suit in New York, its principal place of business, against Playtex for non-infringement and patent invalidity.²¹ The district court stayed the first-filed suit in Georgia under the customer suit exception.²² At the appellate level, Playtex argued that there was no reason to stay the first suit simply because the defendant is a customer of the manufacturing infringer.²³ Playtex argued that 35 U.S.C. § 271 identifies selling as an act of infringement such that Woolworth's was an infringer of the patent every bit as much as Gluckin, the manufacturer.²⁴ Playtex asserted that there must be a finding of harassment or forum shopping before the first filed suit could be enjoined.²⁵ Nevertheless, the appellate court determined that the issuance of an injunction by the district court against continued prosecution of the

19. *Kahn v. General Motors Corp.*, 889 F.2d 1078, 1081 (Fed. Cir. 1989). The federal district courts, of course, have general authority to transfer actions, consolidate discovery and otherwise simplify logistics, with various qualifications and limitations. 28 U.S.C. §§ 1404, 1407 (1994); FED. R. CIV. P. 42. A patentee who institutes contemporaneous lawsuits both against a competitor and against its customer (not merely a reseller) can expect a motion to stay or transfer one of the cases to the same district in which the other case is pending, with the ultimate goal of case consolidation. See 28 U.S.C. § 1404(a) (permitting transfer to a different forum "for the convenience of parties and witnesses, in the interest of justice . . ."). Section 1404(a) is somewhat limited in that transfer is authorized only to any district or division where the suit "might have been brought." *Id.*; *Hoffman v. Blaski*, 363 U.S. 335, 344 (1960). A decision by a trial court on whether to stay or transfer a matter is committed to the court's sound discretion and tends to be very fact-specific. See generally E. HORWITZ AND L. HORWITZ, PATENT LITIGATION, PROCEDURE & TACTICS § 4.02[2], at 4-10.2, et. seq. (1995).

20. 407 F.2d 177 (2d Cir. 1969).

21. *Id.* at 178.

22. *Id.*

23. *Id.*

24. *Id.*

25. *Id.* at 179.

first suit was not an abuse of discretion.²⁶ The appellate court stressed that trial courts have broad discretion in implementing rules of judicial administration like the first-filed rule and the "customer suit" exception.²⁷

In *Kahn v. General Motors Corp.*,²⁸ the Federal Circuit Court of Appeals considered when to apply the customer suit exception.²⁹ Kahn filed suit against General Motors (GM) based on its manufacture and sale of stereo receivers.³⁰ Motorola then filed suit against Kahn arguing that certain integrated circuits Motorola used in its stereo receivers did not infringe Kahn's patent as asserted in the first action.³¹ Motorola was labeled by the district court as the manufacturer and GM was deemed a simple customer.³² The district court stayed the first action and an appeal followed.³³ According to the appellate court, however, the Motorola component did not infringe the patent-in-suit under § 271 (a), (b) or (c).³⁴ Infringement occurred only when GM incorporated the circuits into receivers.³⁵ The appellate court explained that "the customer suit exception is based on the manufacturer's presumed greater interest in defending its actions against charges of patent infringement; and to guard against the possibility of abuse."³⁶ Consequently, GM was not a mere reselling customer so the customer suit exception did not apply.³⁷ The appellate court then applied the first-filed rule³⁸ and vacated the stay of the first-filed suit.³⁹

26. *Gluckin*, 407 F.2d at 179.

27. *Id.*

28. 889 F.2d 1078 (Fed. Cir. 1989).

29. *Id.* at 1081-82.

30. *Id.* at 1078.

31. *Id.*

32. *Id.* at 1081.

33. *Id.* at 1078.

34. *Kahn*, 889 F.2d at 1081.

35. *Id.*

36. *Id.* at 1081.

37. *Id.* "Cases in which a customer suit exception has been held to favor the forum of the second-filed action [were situations in which] the second action would resolve all charges against the customers in the stayed suit, including liability for damages." *Id.* By contrast, this judicial economy would not obtain in the case under appeal. *Id.* at 1081-82. Also, the Federal Circuit noted that decisions staying a customer action in favor of a subsequent suit typically involved resellers or retailers where identical issues were presented, or where the different customer defendants agreed to be bound by any injunction issued in the manufacturer case. *Id.* at 1082. GM had not agreed to be so bound. *Id.*

38. *Id.* at 1082.

39. *Id.* at 1083.

B. Preclusion of Suit Against Customers of an Already-Sued Manufacturer

Over the years, courts have debated the circumstances under which a lawsuit may be filed against a customer of an already-sued manufacturer. *Bechik Products, Inc. v. Flexible Products, Inc.*⁴⁰ was an appeal by a patentee from a preliminary injunction that prohibited the patentee from suing any of the customers of the defendant manufacturer.⁴¹ Bechik, the patentee, accused Flexible of making and selling Bechik's patented mattress handles.⁴² Bechik accused another defendant, Crown, of contributory infringement for using the handles in mattresses of its manufacture.⁴³ The manufacturer admitted financial responsibility for all possible damage.⁴⁴

The patentee sent a notice threatening suit to at least one Crown customer.⁴⁵ The trial court found that such notice was not sent in bad faith and that there was nothing unfair about the notice.⁴⁶ The appellate court characterized the letter as nothing more than a fair warning to the customer of the potential financial liability it faced in the event that the accused infringing manufacturer was not financially able to satisfy a damage award.⁴⁷

The reviewing court explained that the "owner of a patent has a right to threaten suits for infringement, provided he does so in good faith."⁴⁸ Moreover, "[t]his is not a case in which effort was made to harass or ruin a competitor's business on the basis of claimed patent rights known to be groundless."⁴⁹ Nevertheless, the Second Circuit Court of Appeals conceded that the grant of an injunction during the pendency of litigation involved several considerations.⁵⁰ Significantly, while the patentee has a statutory right to protect its intellectual property by prosecuting suits against infringers, the injunction could be sustained if it did not substantially impair the patentee's rights under patent law and it operates to prevent needless litigation.⁵¹ This, the court explained, "has been an historic and traditional objective of equity."⁵²

The appellate court then distinguished between the stay of actions already brought and the preclusion of institution of new

40. 225 F.2d 603 (2d Cir. 1955).

41. *Id.* at 605.

42. *Id.*

43. *Id.*

44. *Id.*

45. *Id.*

46. *Bechik*, 225 F.2d at 605.

47. *Id.*

48. *Id.* at 606.

49. *Id.*

50. *Id.*

51. *Id.*

52. *Bechik*, 225 F.2d at 606.

actions.⁵³ The former seemingly involved less risk of impairment to the rights of the patentee. For instance, an injunction against new suits would create a change in the initial date for which damages could be recovered.⁵⁴ However, the appellate court considered this a remote risk because it believed the patentee could recover sufficient damages from the manufacturing defendant to include damages otherwise recoverable from the manufacturer's customers.⁵⁵ The appellate court therefore held that the injunction might issue, but only on condition that the accused manufacturer furnish a bond sufficient to cover damages resulting from its direct infringement and its customer's contributory infringement.⁵⁶

On the other hand, *American Chemical Paint Co. v. Thompson Chemical Corp.*⁵⁷ was a case in which a preliminary injunction precluding a patentee from commencing suit against customers of the accused manufacturer, pending determination of the action against the manufacturer, was reversed on appeal.⁵⁸ Here, the alleged infringement consisted of the manufacture and sale of materials embodying the patented invention.⁵⁹ During the course of discovery, the patentee learned that the accused manufacturer had sold the materials to various dealers.⁶⁰ The patentee then filed suit against two dealer customers of the manufacturing defendant.⁶¹ The manufacturer intervened in the two lawsuits, seeking to stay those proceedings pending disposition of the first action.⁶² It also moved in the original action to enjoin the patentee from bringing any further actions pending resolution of the case on the merits.⁶³ In one of the subsequent customer suits, a stay was granted.⁶⁴ In the other, however, it was denied.⁶⁵ The trial court in

53. *Id.* at 606-07.

54. *Id.* at 607; 35 U.S.C. § 286 (1994). Postponement of suit would theoretically allow some infringing acts to become stale, *i.e.*, to have occurred more than six years before suit was filed.

55. *Bechik*, 225 F.2d at 607.

56. *Id.* In *Signode Corp. v. Weld-Loc Sys., Inc.*, 700 F.2d 1108 (7th Cir. 1983), the court adopted a comparable rationale in a somewhat different context. Here, the patentee appealed the denial of a preliminary injunction against further sales of the accused product. *Id.* at 1110. One of its arguments was that it would ultimately be entitled to injunctive relief against all users of the infringing product. *Id.* at 1115. Ever increasing sales of the infringing tools, the patentee contended, would increase its litigation burden to the point of irreparable harm. *Id.* The Seventh Circuit rejected this argument because, if the patentee prevailed on the merits, the manufacturing infringers "will be obliged to pay any lost profits due on these sales . . ." *Id.*

57. 244 F.2d 64 (9th Cir. 1957).

58. *Id.* at 65, 67.

59. *Id.* at 65.

60. *Id.*

61. *Id.* at 65-66.

62. *Id.* at 66.

63. *American Chem. Paint Co.*, 244 F.2d at 66.

64. *Id.*

the original action then issued an injunction against the commencement of new actions and the prosecution of the two customer suits.⁶⁶

At the outset, the appellate court considered the propriety of the trial court granting an injunction on the same issue that already had been ruled upon by a court of "co-ordinate jurisdiction."⁶⁷ It determined that there are cases in which overruling an injunction is necessary to protect the initial court's power to act, but that the instant case did not fit in this category.⁶⁸

Then the appellate court considered that part of the order that enjoined the commencement of new infringement suits against the manufacturer's customers.⁶⁹ It stated that "a patent owner has a cause of action, separate and independent from that against an infringing manufacturer, to recover profits and damages and to restrain one who resells a product, which he purchased from an infringing manufacturer."⁷⁰ The reviewing court emphasized that the right to bring such an action is sanctioned by statute and should not be interfered with absent compelling reasons.⁷¹ It recognized that an injunction precluding a patentee from commencing infringement suits against customers of the manufacturer pending disposition of the initial litigation could operate to prevent needless litigation without substantial impairment to the patentee's rights.⁷² However, unless the manufacturer was financially able to respond in damages for any infringement for which it or its customers might be held accountable, an injunction against customer suits could substantially impair the patentee's rights.⁷³ The district court in *American Chemical Paint Co.* had given the patentee the right, under the preliminary injunction, to show that the manufacturer was financially unable to respond in damages.⁷⁴ The Court of Appeals for the Ninth Circuit did not consider this to be an acceptable substitute for a finding of financial ability because it was not a present determination of financial responsibility, and it placed the burden of proof on the wrong party, the patentee.⁷⁵ The injunction against filing additional suits against customers was reversed.⁷⁶

65. *Id.*

66. *Id.*

67. *Id.*

68. *Id.* at 66-67.

69. *American Chem. Paint Co.*, 244 F.2d at 67.

70. *Id.*

71. *Id.*

72. *Id.* (citing *Bechik Products Inc. v. Flexible Products, Inc.*, 225 F.2d 603, 606 (2d Cir. 1955)).

73. *American Chem. Paint Co.*, 244 F.2d at 67.

74. *Id.*

75. *Id.*

76. *Id.*

The Seventh Circuit in *Sunstrand Corp. v. American Brake Shoe Co.* also considered, *inter alia*, the propriety of an injunction against future suits or charges of infringement by a patentee against customers and users of products of the accused manufacturer.⁷⁷ The Seventh Circuit Court of Appeals turned to *Kerotest Manufacturing Co. v. C-O-Two Fire Equipment Co.*⁷⁸ for guidance.⁷⁹ The court interpreted *Kerotest* to mean that trial courts have the discretion to protect manufacturers from harassment of their customers.⁸⁰ At a minimum, the court determined harassment or probable harassment must be demonstrated by the manufacturer before the patentee's right to sue customers and users should be curtailed.⁸¹ The appellate court did not address the issue of whether the manufacturer was capable of responding in damages. In the absence of any showing that suit brought against customers was in anything but good faith and for a legitimate purpose, the injunction against future suits was reversed.⁸²

Several conclusions can be drawn as to a patentee's right to pursue parallel litigation against an infringing manufacturer and the infringing manufacturer's customers. Consistent with the general rule, a first-filed suit will have priority except where it is against a customer who is simply a reseller of the accused goods, if the manufacturer brings a second, declaratory judgment action.

The issue of whether an accused manufacturer's financial ability to compensate the patentee for all damages sustained by the manufacturer and its customers is a basis on which to enjoin subsequent suits against the customer has not been addressed by the Federal Circuit Court of Appeals. In the absence of a preliminary injunction issue, this would seem to be a reasonable accommodation of competing interests.

However, a different result may be appropriate when a patentee obtains or is seeking interim injunctive relief. The balance of interests should shift from the above-described situations when monetary damages are sought. An infringing manufacturer's customers should not have the right to continue business as usual if interim injunctive relief is appropriate and if the patentee can post the appropriate bond.

C. Estoppel to Relitigate

There is also a judicial limitation on the ability of a patentee to sue for patent infringement once a federal court declares the patent invalid. In *Blonder-Tongue Laboratories Inc. v. University of*

77. 315 F.2d 273, 276 (7th Cir. 1963).

78. 342 U.S. 180 (1952).

79. *Sunstrand*, 315 F.2d at 274.

80. *Id.* at 276.

81. *Id.*

82. *Id.* at 276-77.

Illinois Foundation,⁸³ the United States Supreme Court determined that a patent holder should not be able to sue on its patent after the patent has been invalidated, with one exception.⁸⁴ The patentee must be permitted to demonstrate, if it can, that it "did not have a fair opportunity procedurally, substantively and evidentially to pursue this claim the first time."⁸⁵ Not surprisingly, very few lower court decisions after *Blonder-Tongue* have agreed that a patentee did not receive a full and fair opportunity to litigate.⁸⁶

This is a generalization of the hoary rule that a patent infringement action against a customer is barred if the vendor previously prevailed against the patentee because of invalidity or non-infringement of the patent.⁸⁷

Collateral estoppel on patent validity is, however, a one-way street. A judgment of patent invalidity binds a patent owner, but a judgment of validity does not bind persons who were neither parties nor in privity with parties to the suit.⁸⁸ Thus, a patentee who prevails against a competitor infringer does not automatically prevail against the competitor's customer. Nevertheless, there is some benefit to prior success. Courts will at least consider a prior holding of validity or infringement as evidence.⁸⁹

III. THE HISTORICAL EVOLUTION OF PATENT DAMAGES

A patentee can in theory obtain multiple judgments against its competitor and the competitor's customers. The patentee's right to enforce each judgment, however, is limited by a doctrine

83. 402 U.S. 313 (1971).

84. *Id.* at 348-50.

85. *Id.* at 333 (citing *Eisel v. Columbia Packing Co.*, 181 F. Supp. 298, 301 (D. Mass. (1960))).

86. See generally *Stevenson v. Sears, Roebuck & Co.*, 713 F.2d 705, 712 (Fed. Cir. 1983) (rejecting patentee's argument that the prior determination of invalidity by summary judgment was denial of full and fair opportunity to litigate); *Westwood Chem., Inc. v. Molded Fiber Glass Body Co.*, 498 F.2d 1115, 1119-20 (6th Cir. 1974) (rejecting assertion that "false testimony" by accused infringer amounted to a denial of full and fair opportunity to litigate). One of the rare occasions in which *Blonder-Tongue* estoppel was not applied occurred in *Loctite Corp. v. Ultraseal Ltd.*, 209 U.S.P.Q. 1030 (E.D. Wis. 1980). In that case, a proceeding before the International Trade Commission was dismissed based on the patent owner's express doubts as to validity. *Id.* at 1032. The district court, in subsequent litigation between the parties, concluded that in the absence of a contested hearing, the validity issue had not been fully and fairly litigated at the administrative level. *Id.* at 1031.

87. *Kessler v. Eldred*, 206 U.S. 285 (1907); *MGA, Inc. v. General Motors Corp.*, 827 F.2d 729, 734 (Fed. Cir. 1987).

88. *Stevenson*, 713 F.2d 705. See also *Boutell v. Volk*, 449 F.2d 673, 678 (10th Cir. 1971) (finding that it was "grossly inequitable to bind a party to a judgment of validity rendered in an action against some other party.")

89. See generally 5 DONALD S. CHISUM, PATENTS § 19.02[2] (1995).

known as the single recovery, or full compensation, rule.⁹⁰ The rule as applied to patent litigation is simple: a patentee is entitled to full compensation for related acts of infringement, but the patentee, like any tort victim, is not entitled to multiple recoveries for the same injury. Courts in the United States have grappled with implementation of the single recovery rule, and what constitutes full compensation, for many years.

In order to appreciate the nuances and complexities involved in such a determination, it is important to understand the basic principles behind patent damages law. 35 U.S.C. § 284 provides:

Upon finding for the claimant the court shall award the claimant damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court . . . [T]he court may increase the damages up to three times the amount found or assessed.⁹¹

This statute, enacted as part of the 1952 Patent Act, was intended to codify existing law.⁹² Therefore, a brief review of the evolution of patent damage laws is useful to its interpretation.

Section 4 of the Patent Act of 1790 allowed patentees to recover damages from infringers.⁹³ The Patent Act of 1793 changed the patentee's recovery in that it specified "a sum, that shall be at least equal to three times the price, for which the patentee has usually sold or licensed to other persons, the use of the said invention."⁹⁴ Thus, the price of a license became the measure of single damages, and an infringer was required to "forfeit and pay to the patentee" an amount which was three times that sum.⁹⁵ The form

90. The single recovery rule requires a party to include all past, present and future claims against an adversary in one cause of action. Amy B. Blumenberg, *Medical Monitoring Funds: The Periodic Payment of Future Medical Surveillance Expenses in Toxic Exposure Litigation*, 43 HASTINGS L.J. 661, 661 (1992).

91. 35 U.S.C. § 284 (1994).

92. *Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., Inc.*, 377 U.S. 476, 505 n.20 (1964) (quoting H.R. Rep. 1923, 82nd Cong., 2d Sess. 10, 29 (1952)). See Donner, *BIC Leisure v. Windsurfing: The Federal Circuit Catches the "Big One" and Leaves the Supreme Court on Shore to Dry*, 4 FED. CIR. BAR. J. 167 (1994), for a comprehensive discussion of the evolution of § 284.

93. Patent Act of 1790, ch. 7, § 4, 1 STAT. 111 (1790). "[E]very person so offending, shall forfeit and pay to the said patentee . . . such damages as shall be assessed by a jury, and moreover shall forfeit to the person aggrieved, the thing or things so devised, made, constructed, used, employed, or vended . . ."

Id.

94. Patent Act of 1793, ch. 11, § 5, 1 STAT. 318 (Feb. 21, 1793).

95. *Seymour v. McCormick*, 57 U.S. (16 How.) 480, 488 (1853). The Court noted, however, that experience has shown that "some inventions or discoveries had their chief value in a monopoly of use by the inventor, and not in a sale of licenses, [thus,] the value of a license could not be made a universal rule, as a measure of damages." *Id.*

of damages was again changed in the Patent Act of 1800.⁹⁶ It authorized a patentee to recover "a sum equal to three times the actual damages sustained by such patentee . . . from or by reason of such offence, which sum shall and may be recovered, by action of the case."⁹⁷

The Patent Act of 1819 ushered in federal equity's involvement in patent litigation.⁹⁸ Until then, a patentee only had the legal remedy of an action on the case, with the relief limited to an award of damages.⁹⁹ The Act of 1819 expanded a patentee's remedy to include a suit in equity for injunctive relief.¹⁰⁰ Under the Act, courts of equity could order equitable accountings of the infringer's profits but not the recovery of the patentee's lost profits or royalty.¹⁰¹

Congress' next change to damages was in the Patent Act of 1836.¹⁰² By that Act, the jury in a court of law was to assess "actual damages" for patent infringement.¹⁰³ However, mandatory trebling, which had continued in effect from the Patent Act of 1800, was repealed.¹⁰⁴ Instead, courts were vested with the power to award up to treble the amount of the actual damages, in their discretion, as punitive damages.¹⁰⁵ Federal equity jurisdiction was also continued into the Patent Act of 1836.¹⁰⁶

In 1870, Congress expanded the power of federal equity to include where appropriate the award of the patentee's damages as well as the infringer's profit. Section 59 of the 1870 Act retained "actual damages" as the standard that a jury could award in an action at law.¹⁰⁷ However, an infringer's profits still remained the

96. Patent Act of 1800, ch. 25, § 3, 2 STAT. 37 (1800).

97. *Id.* In *Whittemore v. Cutter*, Justice Story interpreted the "actual damages" provision of the Patent Act of 1800 to mean "such damages as the plaintiffs can actually prove and have in fact sustained, as contradistinguished to mere imaginary or exemplary damages, which in personal torts are sometimes given . . ." 29 F. Cas. 1123, 1125 (D. Mass. 1813).

98. Patent Act of 1819, ch. 19, § 1, 3 STAT. 481-82 (1819).

99. CHISUM, *supra* note 89, at § 20.02[1][a]. Injunctive relief was only available in state courts and when a federal court sat based on diversity of citizenship. *Id.* at § 20.02[1][b].

100. Patent Act of 1819, ch. 19, § 1, 3 STAT. 481-82.

101. *Id.* See also *Root v. Railway*, 105 U.S. 189 (1882) (quoting the language of the Patent Act of 1819 regarding equitable relief).

102. Patent Act of 1836, ch. 357, § 17, 5 STAT. 117 (1836).

103. *Id.*

104. *Id.*

105. *Id.* at § 14. See also *Seymour v. McCormick*, 57 U.S. 480, 489 (1853) (stating that the court's discretionary power to inflict punitive damages is limited within the trebling of actual damages).

106. Patent Act of 1836, ch. 357, § 17, 5 STAT. 117.

107. Patent Act of 1870, ch. 230, § 59, 15 STAT. 198 (1870).

[T]he court shall have power, upon bill in equity filed by any party aggrieved, to grant injunctions according to the course and principles of courts of equity, to prevent the violation of any right secured by patent,

primary award for relief in a suit at equity while a patentee's damages was the primary award in a suit in a court of law.¹⁰⁸

One case that lent its imprimatur to our current scheme of patent damages is *Dowagiac Manufacturing Co. v. Minnesota Moline Plow Co.*¹⁰⁹ It articulated a "reasonable royalty" damages option. The Court stated:

The plaintiff was clearly entitled to damages for the infringement. If there had been an established royalty, the jury could have taken that sum as a measure of damages. In the absence of such royalty, and in the absence of proof of lost sales or injury by competition, the only measure of damages was such sum as, under all the circumstances, would have been a reasonable royalty for the defendant to have paid. This amount was the province of the jury to determine. In so doing, they did not make a contract for the parties, but found a measure of damages.¹¹⁰

In 1946, Congress substantially altered the equitable relief provisions of the patent statute.¹¹¹ Significantly, Congress eliminated the right to an accounting for an infringer's profits in courts of equity and changed the equitable damages remedy to "general damages which shall be due compensation for making, using or selling the invention, not less than a reasonable royalty therefor"¹¹² The legislative history of the 1946 Act manifested Congress' concern with the difficulties that had plagued the courts in apportioning from the infringer's profits, for recovery by the patentee, that portion attributable to the claimed invention. The accounting had become protracted, expensive and unworkable.¹¹³ At

on such terms as the court may deem reasonable; and upon a decree being rendered in any such case for an infringement, the complainant shall be entitled to recover, in addition to the profits to be accounted for by the defendant, the damages the complainant has sustained thereby . . . and the court shall have the same powers to increase the same in its discretion that are given by this act to increase the damages found by verdicts in actions upon the case

Id. at § 55. See also *Marsh v. Seymour*, 97 U.S. 348, 360 (1878) (holding that "[d]amages of a compensatory character may be allowed to a complainant in an equity suit, where it appears that the business of the infringer was so improvidently conducted that it did not yield any substantial profits, as in the case before the court"); *Root v. Railway*, 105 U.S. 189 (1882) (quoting the language of the Patent Act of 1870).

108. *Burdell v. Denig*, 92 U.S. 716, 719-20 (1876).

109. 235 U.S. 641 (1915).

110. *Id.* at 649 (citing *Hunt Bros. Fruit-Packing Co. v. Cassiday*, 64 F. 585, 587 (9th Cir. 1894)).

111. 35 U.S.C. § 70 (1994).

112. *Id.* See also *Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., Inc.*, 377 U.S. 476, 505-06 (1964).

113. "[I]t is absolutely impossible to apportion the profits due to the invention, those being the only profits to which the patentee is entitled The only sound principle is to have the plaintiff recover the damages he can prove." H.R. Rep., No. 1587, 79th Cong., 1, at 3 (1946). See also, S.Rep., No.

the same time, Congress tried to make sure that patent owners would be completely compensated.¹¹⁴ In enacting § 284 in its present form in 1952, Congress reportedly consolidated § 67 and § 70 of the 1946 code, with changes to the language.¹¹⁵

IV. DAMAGES FOR PATENT INFRINGEMENT

Under the Patent Act of 1952, recoverable damages in patent infringement litigation have currently evolved into two general species: the patentee's lost profits and royalty-based damages.¹¹⁶ Both types of damages are discussed below.

A. Lost Profits

A court will infer that the patentee's lost sales are equal in quantity to the infringing sales if the patentee proves: (1) demand for the patented product; (2) absence of acceptable non-infringing substitutes; and (3) manufacturing and marketing capability to exploit the demand.¹¹⁷ The patentee also needs to prove the amount of his lost profit.¹¹⁸ Many decisions of the Federal Circuit apply this methodology.¹¹⁹

1503, 79th Cong., 2 (1946).

114. *General Motors Corp. v. Devex Corp.*, 461 U.S. 648, 655 (1983).

115. *Aro*, 377 U.S. at 505 n.20.

116. *Hartness Int'l, Inc. v. Simplicmatic Eng'g Co.*, 819 F.2d 1100, 1112 (Fed. Cir. 1987).

117. *Panduit Corp. v. Stahlin Bros. Fibre Works, Inc.*, 575 F.2d 1152, 1156 (6th Cir. 1978).

118. *See BIC Leisure Prods., Inc. v. Windsurfing Int'l, Inc.*, 1 F.3d 1214 (Fed. Cir. 1993) (explaining that in order to recover lost profits, a patent owner must prove a causal relation between the infringement and lost profits); *Bio-Rad Labs., Inc. v. Nicolet Instrument Corp.*, 739 F.2d 604, 616 (Fed. Cir. 1984) (stating that a patent owner must show that it would have made sales but for the infringing activity).

119. *See, e.g., King Instrument Corp. v. Otari Corp.*, 767 F.2d 853, 864 (Fed. Cir. 1985) (stating that evidence showing a reasonable probability that the patent owner would have made sales is sufficient to prove lost profits); *Standard Havens Prods., Inc. v. Gencor Indus., Inc.*, 953 F.2d 1360 (Fed. Cir. 1991) (stating that lost profit awards require a showing that the patent owner would have made the sales but for the infringement). In *Bio-Rad Laboratories*, the Federal Circuit indicated that while *Panduit* articulates a permissible way to establish lost profits, it does not establish the only way to determine entitlement to lost profits. 739 F.2d at 616. The presence or absence of acceptable non-infringing substitutes can be shown in a variety of ways. *E.g., Lam, Inc. v. Johns-Manville Corp.*, 718 F.2d 1056 (Fed. Cir. 1983); *Marsh-McBirney, Inc. v. Montedoro-Whitney Corp.*, 882 F.2d 498 (Fed. Cir. 1989). The simplest case arises when the patent owner and the infringer are the only suppliers to the relevant market. *E.g., Lam*, 718 F.2d 1056; *Marsh-McBirney*, 882 F.2d 498. When the relevant market holds but those two competitors, the patentee most likely would have made the sales "but for" the infringing product. *Lam*, 718 F.2d at 1065; *Marsh-McBirney*, 882 F.2d at 505. The patentee has more difficulty showing causation when the relevant market holds more than two competitors. The Federal Circuit has also reviewed the following types of evi-

When the patentee and infringer are not sole competitors in a relevant market, proof of a sale by the patentee "but for" the infringing product can be difficult. In these circumstances, the Federal Circuit has awarded pro rata lost profits damages based on a "market share" theory. *State Industries, Inc. v. Mor-Flo Industries, Inc.* is the seminal case on market share lost profits damages.¹²⁰ Mor-Flo infringed a patented method of insulating water heaters with foam.¹²¹ State Industries held approximately 40% of the relevant nationwide market.¹²² The district court awarded State lost profits on 40% of the infringing sales by Mor-Flo and a reasonable royalty of 3% on the other 60% of the infringer's sales.¹²³ The court of appeals affirmed the decision on appeal.¹²⁴ The federal court stated that since State had sufficient marketing and manufacturing capabilities to meet its market share of the demand, "it is eminently reasonable for the district court to infer that State could have sold its market share of Mor-Flo's infringing sales wherever the opportunity occurred."¹²⁵

The recent Federal Circuit opinion in *BIC Leisure Products, Inc. v. Windsurfing International, Inc.* qualified the market share theory of lost profits.¹²⁶ The appellate court first reiterated that "[t]o recover lost profits as opposed to royalties, a patent owner must prove a causal relation between the infringement and its loss of profits."¹²⁷ The patent owner must prove that "but for" the infringement, it would have made the infringer's sales.¹²⁸ The evi-

dence when determining what constitutes acceptable substitutes: (1) whether the patent owner lost sales to an infringer under a bidding system; (2) whether the patent owner's sales or prices fell and rose contemporaneously with the infringer's entry and departure from the market; and (3) whether the infringer was either a former customer of the patent owner or a supplier to such former customer. *CHISUM, supra* note 89, at §§ 20.03[1][a][iv][B]-[D].

120. 883 F.2d 1573 (Fed. Cir. 1989).

121. *Id.* at 1575.

122. *Id.* at 1576.

123. *Id.* at 1575.

124. *Id.* at 1582.

125. *Id.* at 1579. The same "market share" approach is seen in *King Instrument Corp. v. Perego*, 737 F. Supp. 1227, 1241-42 (D. Mass. 1990). The appellate court qualified the *State Industries* holding in *Slimfold Manufacturing Co., Inc. v. Kinhead Industries, Inc.*, 932 F.2d 1453 (Fed. Cir. 1991). The patentee asserted that the trial court had abused its discretion in failing to award lost profits based on market share. The appellate court explained that there was a "critical difference" between *State Industries* and the present case in that *State Industries* held the grant of lost profits based on market share was not an abuse of discretion. The court then announced, "[h]owever, that holding does not mean that the contrary is true, i.e. that the failure to award lost profits based on market share would constitute an abuse of discretion. We hold that such a failure to award lost profits in the present case was not an abuse of discretion." *Id.* at 1458.

126. 1 F.3d 1214, 1218 (Fed. Cir. 1993).

127. *Id.*

128. *Id.*

dence at trial revealed that demand for sailboards (to which the patent related) was relatively elastic.¹²⁹ The record further showed that the sailboard market's entry level, where the accused infringer competed, was particularly sensitive to price disparities.¹³⁰ The infringer's sailboards cost \$350 while the patentee's boards were priced around \$600.¹³¹ The court explained that without the infringer in the market, its customers would likely have bought boards in the same price range.¹³² The patentee failed to show that the infringer's customers would have purchased from the patentee in proportion with the patentee's market share.¹³³ The court refused to infer this fact in light of what occurred in *State Industries*.

BIC Leisure distinguished its holding from the holding in *State Industries*. The court opined that the *Panduit* test¹³⁴ for lost profits operates under an inherent assumption that the patent owner and the infringer sell products sufficiently similar to compete against each other in the same market segment.¹³⁵ If the products of the patentee and the infringer are not substitutes in a competitive market, then the first two factors of the *Panduit* test are not met, and lost profits are not recoverable.¹³⁶ The opinion emphasized that a patent owner may substitute proof of its market share for proof of the absence of acceptable substitutes, but only when the patent owner and the infringer compete in the same market.¹³⁷

When the patent in question covers only a part of the commercial device sold or used by the patent owner or infringer, the fact finder must determine whether lost profits should be based only on the patented component or on the system as a whole. This issue has long been one of the most complex areas of patent damages law.¹³⁸

In *Paper Converting Machine Co. v. Magna-Graphics Corp.*, the patented invention was an automatic rewinder to roll consumer goods from a paper web under high tension.¹³⁹ The mechanism for the high-speed manufacture of paper rolls included several components, only one of which - the rewinder - incorporated the claimed invention.¹⁴⁰ Peripheral equipment included a stand to

129. *Id.*

130. *Id.*

131. *Id.*

132. *BIC Leisure*, 1 F.3d at 1218.

133. *Id.*

134. *Panduit Corp. v. Stahlin Bros. Fibre Works*, 575 F.2d 1152, 1156 (6th Cir. 1978).

135. *BIC Leisure*, 1 F.3d at 1218.

136. *Id.*

137. *Id.* at 1219.

138. 7 DONALD S. CHISUM, CHISUM ON PATENTS § 20.02[3] (1997).

139. 745 F.2d 11, 23 (Fed. Cir. 1984).

140. *Id.* at 13-14.

support a large roll of paper, a core loader to supply pasteboard cores to the patented rewinder, an embosser to provide a special textured surface on the paper and a tail seeker to seal the paper's trailing end to the consumer-sized roll.¹⁴¹ None of the auxiliary units were integral parts of the rewinder.¹⁴² Nevertheless, the Federal Circuit explained that the deciding factor is whether "normally the patentee (or its licensee) can anticipate sale of such unpatented components as well as of the patented" ones.¹⁴³ If in all reasonable probability the patent owner would have made the sales which the infringer has made, what the patent owner, in reasonable probability, would have netted from the sales denied to him is the measure of his loss, and the infringer is liable for that amount.¹⁴⁴ Whether a patentee could anticipate additional income from the auxiliary parts was a question of fact, which the reviewing court would not disturb because the lower court's finding was not clearly erroneous.¹⁴⁵

In *Del Mar Avionics, Inc. v. Quinton Instrument Co.*,¹⁴⁶ the court noted:

[I]n appropriate circumstances, the patentee may prove the extent of its lost profits by the "entire market value rule" . . . based on a showing that the patentee could reasonably anticipate the sale of the unpatented components together with the patented components Other factors, such as development costs and business risks, may be taken into account if the circumstances warrant.¹⁴⁷

In *State Industries, Inc. v. Mor-Flo Industries, Inc.*, the appellate court affirmed an award by the district court of lost profits based on the patentee's profit margin on the sale of water heaters, although the patent was on a method of adding foam insulation to water heaters.¹⁴⁸ The court explained that the "entire market value rule . . . permits recovery of damages based on the value of the entire apparatus containing several features, where the patent-related feature is the basis for customer demand."¹⁴⁹

Rite-Hite Corp. v. Kelley Company, Inc. is the most recent damages pronouncement from the Federal Circuit Court of Appeals.¹⁵⁰ Rite-Hite sued the Kelley Company for infringement of a patented mechanism that secured trucks to loading docks during

141. *Id.* at 23.

142. *Id.*

143. *Id.*

144. *Id.*

145. *Paper Converting Machine*, 745 F.2d at 23.

146. 836 F.2d 1320 (Fed. Cir. 1987).

147. *Id.* at 1327 (citations omitted). The case was remanded for the trial court to consider all relevant evidence. *Id.* at 1329.

148. 883 F.2d 1573 (Fed. Cir. 1989).

149. *Id.* at 1580.

150. 56 F.3d 1538 (Fed. Cir. 1995).

the loading or unloading process.¹⁵¹ The district court found infringement and awarded Rite-Hite the wholesale profits that the manufacturer patentee would have made on lost sales of its competing product.¹⁵² The competing product, though, did not practice the patent-in-suit. The Federal Circuit, in an en banc decision, agreed that Rite-Hite was entitled to lost profits in connection with lost sales of its competing, unpatented product.¹⁵³ The appellate court stated that a patentee must prove "but for" causation for lost profits and also that the lost sales were "foreseeable" or proximately caused by the infringement, as those terms are traditionally defined.¹⁵⁴ The majority concluded that the lost sales of the unpatented product were foreseeable because Rite-Hite's unpatented product was in direct competition with the infringer's product.¹⁵⁵

In *Rite-Hite*, the Federal Circuit affirmed the use of the entire market rule to determine whether unpatented components sold with a patented apparatus should be included in the damages calculation of lost profits. The court, though, restricted application of the rule to situations in which the patented and unpatented components were analogous to a single functioning unit. This holding adds an additional element to *Paper Converting Machine's* main query of whether a patentee can reasonably anticipate sale of the unpatented components as well as the patented components.¹⁵⁶ Thus, under *Rite-Hite* one must first decide the single functioning unit rule is applicable before even applying the underlying question of reasonable anticipation.

151. *Id.* at 1542.

152. *Id.* at 1543.

153. *Id.*

154. *Id.* at 1558, 1569.

155. *Id.* at 1555. A dissenting opinion by Judge Nies disagreed with this proposition. *Id.* at 1556. The dissent rejected the foreseeability test and stated that the property rights of a patentee do not extend to its market in goods unprotected by the litigated patent. *Id.* at 1569. Thus, the dissent argued, diversion of sales of an unpatented product is not an injury to the patentee's property rights and cannot constitute legal injury for which lost profits may be awarded. *Id.* at 1569-70. See also *King Instruments Corp. v. Perego*, 65 F.3d 941 (Fed. Cir. 1995) (affirming the district court award of lost profits from sales of unpatented competing product).

156. The Federal Circuit in *Rite-Hite* tried to reconcile its holding to *Paper Converting* by stating:

[W]e may have appeared to expand the rule when we emphasized the financial and marketing dependence of the unpatented component on the patented component. In *Paper Converting*, however, the rule was applied to allow recovery of profits on the unpatented components only because all the components together were considered to be parts of a single assembly. The references to "financial and marketing dependence" and "reasonable probability" were made in the context of the facts of the case and did not separate the rule from its traditional moorings.

56 F.3d at 1550.

B. Damages Based on Royalties

A patent owner may either recover damages based on an established royalty rate or if there is no established rate, on a "reasonable" royalty rate. An established rate is based on prior actual licenses for acts comparable to those engaged in by the infringer without authority. The Supreme Court stated the factors for proving an established royalty rate over a century ago:

It is undoubtedly true that where there has been such a number of sales by a patentee of licenses to make, use, and sell his patents as to establish a regular price for a license, that price may be taken as a measure of damages against infringers . . . In order that a royalty may be accepted as a measure of damages against an infringer, who is a stranger to the license establishing it, it must be paid or secured before the infringement complained of; it must be paid by such a number of persons as to indicate a general acquiescence in its reasonableness by those who have occasion to use the invention; and it must be uniform at the places where licenses are issued.¹⁵⁷

A "reasonable" royalty is one which a willing licensor and willing licensee would arrive at in a hypothetical negotiation at the time infringement starts, assuming the patent to be valid and having available all information relevant to the determination of a fair royalty. *Georgia-Pacific Corp. v. United States Plywood Corp.* lists fifteen factors to consider in determining the reasonable royalty.¹⁵⁸ The Federal Circuit has cited *Georgia-Pacific* with ap-

157. *Rude v. Westcott*, 130 U.S. 152, 165 (1889).

158. 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970). The factors are as follows:

(1) The royalties received by the patentee for the licensing of the patent-in-suit, proving or tending to prove an established royalty; (2) the rates paid by the licensee for the use of other patents comparable to the patent-in-suit; (3) the nature and scope of the license, as exclusive or non-exclusive, or as restricted or non-restricted in terms of territory or with respect to whom the manufactured product may be sold; (4) the licensor's established policy and marketing program to maintain his patent monopoly by not licensing others to use the invention or by granting licenses under special conditions designed to preserve that monopoly; (5) the commercial relationship between the licensor and the licensee, such as, whether they are competitors in the same territory in the same line of business; or whether they are inventor and promoter; (6) the effect of selling the patented specialty in promoting sales of other products of the licensee, the existing value of the invention to the licensor as a generator of sales of his non-patented items, and the extent of such derivative or convoyed sales; (7) the duration of the patent and the term of the license; (8) the established profitability of the product made under the patent, its commercial success and its current popularity; (9) the utility and advantages of the patent property over the old modes or devices, if any, that had been used for working out similar results; (10) the nature of the patented invention, the character of the commercial embodiment of it as owned and produced by the licensor, and the benefits to those who have used the invention; (11) the extent to which the infringer has made use of the invention, and any evidence probative of the value of

proval.¹⁵⁹ These factors generally fall into two groups. The first group relates to the specific and general market conditions in the pertinent industry. The second group relates to the anticipated profitability of the product made, used or sold by the infringer and covered by the patent.

In *Rite-Hite*, the Federal Circuit affirmed the district court's award to Rite-Hite of reasonable royalties based on the patentee's profits rather than on the infringer's profits.¹⁶⁰ The district court reasoned that Rite-Hite owned a pioneer patent and had consistently followed a practice of exploiting its own patents, rather than licensing them.¹⁶¹ The Federal Circuit stated that the royalty may be based on an established royalty or on the results of hypothetical negotiations between the plaintiff and defendant.¹⁶² The appellate court agreed that it was not unreasonable for the trial court to find that an unwilling patentee would only license for one-half its expected lost profits and that such an amount was a reasonable royalty.¹⁶³ The fact that the award was not based on the infringer's profits did not make it an unreasonable award.¹⁶⁴

V. THE EBB AND FLOW OF "FULL COMPENSATION"

A. *Evolution of the Single Recovery Rule*

To some extent, the courts have explored the ramifications of full compensation on subsequent suits by a patentee. Several cases from the first century of American patent jurisprudence sup-

that use; (12) the portion of the profit or the selling price that may be customary in the particular business or in comparable businesses to allow for the use of the invention or analogous inventions; (13) the portion of the realizable profit that should be credited to the invention as distinguished from non-patented elements, the manufacturing process, business risks, or significant features or improvements added by the infringer; (14) the opinion testimony of qualified experts; and (15) the royalty that a licensor (such as the patentee) and a licensee (such as the infringer) would have agreed upon at the time the infringement began, if both had reasonably and voluntarily been trying to reach an agreement.

Id.

159. See, e.g., *Smithkline Diagnostics, Inc. v. Helena Labs. Corp.*, 926 F.2d 1161 (Fed. Cir. 1991) (citing *Georgia-Pacific* with approval); *Railroad Dynamics, Inc. v. A. Stucki Co.*, 727 F.2d 1506 (Fed. Cir. 1984) (citing the fifteen factors set forth in *Georgia-Pacific*).

160. *Rite-Hite*, 56 F.3d at 1555.

161. *Id.* at 1552-53.

162. *Id.* at 1554.

163. *Id.* at 1555.

164. *Id.* at 1576-77. Judge Nies, again in the dissent, states that "a reasonable royalty requires a balancing of the interests of the parties" and that "it is simply beyond reality to infer that the management for the five hundred employee-owners of Kelley would have negotiated a royalty which, it was evident at the time, would destroy their business and jobs." *Id.* at 1576-77.

ported the rule that:

[after a] patentee has already received full compensation [from a competitor] in the same manner and to the same extent as if he had sold the patented articles himself . . . the infringing articles so sold may be used by the vendees thereof free from any further claim of the patentee, or, in other words, that the vendees under such circumstances acquire an implied license to use them.¹⁶⁵

This rule changed in 1884 after the Supreme Court decided *Birdsell v. Shaliol*.¹⁶⁶ The facts from *Birdsell* are instructive. Birdsell was the inventor and the patentee of an improvement in machines for threshing and hulling clover-seed.¹⁶⁷ He had granted to the Birdsell Manufacturing Company an exclusive oral license to make, vend and use his invention.¹⁶⁸ Birdsell had brought a prior suit against the Ashland Machine Company.¹⁶⁹ Birdsell Manufacturing Company was not a party in that prior suit, but helped fund it.¹⁷⁰ The court determined that Ashland had infringed. The court in the prior suit issued a permanent injunction and referred the case to a master for damages.¹⁷¹ The master concluded that Ashland had made no profits for which it should account and that, if any damages had been sustained, they had been sustained by non-party Birdsell Manufacturing Company.¹⁷² Accordingly, Birdsell (the plaintiff) was entitled to recover only \$1.00, as nominal damages.¹⁷³

Birdsell and Birdsell Manufacturing Company then sued Ashland's customers Shaliol and Feikert for their use of one of the machines manufactured by the Ashland Machine Company.¹⁷⁴ Shaliol analogized his situation to the "first sale" doctrine.¹⁷⁵ Under that doctrine, once a patentee sells a patented item, the purchaser has the right to make, use and resell that item without further obligation to the patentee.¹⁷⁶ Similarly, under that doctrine the patentee of the patented machine is deemed to treat machines sold by the licensee under authority of his license in comparable

165. *De Laski & Thropp Circular Woven Tire Co. v. Empire Rubber & Tire Co.*, 239 F. 139, 143 (D.N.J. 1916) (citations omitted).

166. 112 U.S. 485, 487 (1884). See also *United States Printing Co. v. American Playing-Card Co.*, 70 F. 50, 51 (C.C.W.D. Mich. 1895) (explaining that cases to the contrary "are virtually overruled by" *Birdsell*.)

167. *Id.*

168. *Id.*

169. *Id.*

170. *Id.*

171. *Id.*

172. Prior to 1946, a patentee could recover an infringer's lost profits and any damages suffered by the patentee. See *supra* Part IV.

173. *Birdsell*, 112 U.S. at 485-86.

174. *Id.* at 486.

175. *Id.* at 487.

176. *Id.*

fashion to a sale.¹⁷⁷ In both instances, all claims of the patentee for the use of such machines are exhausted. The lower court held that because of the final decree in the suit against manufacturer Ashland, and the recovery in payment of even \$1.00 in nominal damages, both Birdsell and Birdsell Manufacturing Company were estopped to maintain the customer suit.¹⁷⁸

In contrast, the Supreme Court did not find this analogy dispositive. It explained that an infringer does not, by paying damages for making and using a machine in infringement of a patent, acquire any right itself to the future use of the machine.¹⁷⁹ The Court observed that in addition to the payment of damages for past infringement, an infringer may be restrained by injunction from further use.¹⁸⁰ Similarly, one who pays damages for selling a machine in infringement of a patent does not acquire for itself or its vendee any right to use that machine.¹⁸¹

The Supreme Court referred to an analogous English lawsuit brought by a patentee against both the manufacturer and the user.¹⁸² The English patentee asked for an injunction against each, an accounting for profits against the manufacturer and for damages against the user.¹⁸³ The English customer asserted that the patentee was not entitled to both damages against it and an accounting against the manufacturer.¹⁸⁴ Furthermore, the user argued that the patentee could not have an accounting against the manufacturer without in effect ratifying the sale to the user.¹⁸⁵ Accordingly, it was urged, if the patentee adopted the sale by obtaining the manufacturer's profits, the patentee had no right to any additional recovery from the purchaser.¹⁸⁶ The English Vice Chancellor rejected this argument while observing that, "it has never, I think, been held in this court that an account[ing], directed against a manufacturer of a patented article, licenses the use of that article in the hands of all the purchasers."¹⁸⁷ So long as the article is used, the Vice Chancellor opined, there is continuing damage.¹⁸⁸

The Supreme Court then conceptualized its view about recovery in sequential vendor-vendee patent cases as follows:

If one person is . . . exempt from being sued for damages for using

177. *Id.* at 488.

178. *Id.* at 486.

179. *Birdsell*, 112 U.S. at 487.

180. *Id.*

181. *Id.* at 488.

182. *Id.*

183. *Id.*

184. *Id.*

185. *Birdsell*, 112 U.S. at 488.

186. *Id.*

187. *Id.* (citing *Penn v. Bibby*, L.R. 3 Eq. 308; S.C. 15 Weekly Report 192).

188. *Id.*

the same machine for the making and selling of which damages have been recovered against and paid by another person, it can only be when actual damages have been paid, and upon the theory that the plaintiff has been deprived of the same property by the acts of two wrong-doers, and has received full compensation from one of them.¹⁸⁹

Under United States law, the Supreme Court observed, judgment against one joint trespasser, without full satisfaction, is no bar to a suit against another for the same trespass.¹⁹⁰ Ultimately, the Supreme Court held that a judgment for nominal damages against one wrongdoer does not bar a suit against another for a continuance of the wrong.¹⁹¹

Tuttle v. Matthews was one of the first cases decided after *Birdsell* that presents the issue of making the patentee whole, while providing only a single recovery for the injury.¹⁹² In this case, the court first entered a decree that the patents in issue were valid and infringed by harrows made and sold by the defendant.¹⁹³ Then the matter proceeded to an accounting.¹⁹⁴ While that hearing was pending, the infringer learned that the patentee was collecting money from the users of the infringing harrows for which an accounting was in process.¹⁹⁵ The infringing manufacturer sought an injunction restraining the patentee from interfering with the infringer's customers.¹⁹⁶ This, the court declined to do.¹⁹⁷ At the outset, the court explained that the chief value of many patented machines is in their use.¹⁹⁸ It observed that the right to make, use

189. *Id.* at 488-89.

190. *Id.* at 489.

191. *Birdsell*, 112 U.S. at 489. In *Stutz v. Armstrong*, 25 F. 147 (C.C.W.P.A. 1885), the court considered an appeal from a master's report on damages. The accused infringer argued that damages based on a fixed license fee should be apportioned because the enforced payment would not confer upon it the right to further use the infringing machine. *Id.* at 148. The court rejected this argument stating:

But such is not my understanding of the law. I think the true doctrine, and one reconciling any seeming inconsistencies in the decisions, is this: That while the patentee may, if he choose, confine himself to a recovery for past infringement, and insist that the further use of the infringing machine be enjoined, yet if he elect as his measure of damages the full license fee established by himself, the payment thereof operates to vest in the defendant the right to use the machine during the term of the patent, or until that particular machine is worn out.

Id.

192. 28 F. 98 (C.C.N.D.N.Y. 1886).

193. *Id.*

194. *Id.*

195. *Id.*

196. *Id.*

197. *Id.* at 99.

198. *Tuttle*, 28 F. at 98.

and sell were independent rights.¹⁹⁹ Recovery by the patentee for one or more of those rights should not necessarily dedicate the machine to the public for unfettered use "with impunity."²⁰⁰

Another relevant case from the *Birdsell* era is *United States Printing Co. v. American Playing Card Co.*²⁰¹ Here, the patentee sued a printing company which was using a machine accused of infringement for printing playing cards.²⁰² The patentee had previously sued the manufacturer of the machine and settled.²⁰³ The manufacturer asserted the settlement as a defense, albeit unsuccessfully.²⁰⁴ The court noted a distinction between settlement and a judgment for damages for past infringement on the one hand, and an award of profits on the other hand stating:

Where a patentee takes a decree for profits against a manufacturing infringer, he thereby sets the manufactured machine free In such cases, the profits of the infringer are full compensation to the complainant for the wrong done him by the unauthorized manufacture and sale of the infringing machine; but, where there is merely a settlement of judgment for damages, it is only for damages in the past, and has no relation to the future.²⁰⁵

A similar issue was considered in *De Laski & Thropp Circular Woven Tire Co. v. Empire Rubber & Tire Co.*²⁰⁶ Again, the patentee first sued a manufacturer for infringement.²⁰⁷ That case was settled and the patentee decided to sue one of the manufacturer's customers for infringement by use.²⁰⁸ That prior settlement was asserted as a defense.²⁰⁹ The district court observed that the question of whether the stipulation released not only the manufacturer, but also its customer needed to be answered by the terms of the stipulation itself.²¹⁰ The trial court concluded that the stipulation was only intended to cover claims asserted against the manufacturer, for infringements in making and selling the machine.²¹¹ Hence, the money paid under the stipulation was not in satisfaction of the injury subsequently complained of use.²¹² The trial court observed that even if the patentee had received full compensation for the

199. *Id.*

200. *Id.*

201. 70 F. 50 (C.C.W.D. Mich. 1895).

202. *Id.* at 51.

203. *Id.* at 52.

204. *Id.*

205. *Id.* at 53. Recall that recovery of an infringer's profits was eliminated as a remedy in 1946. See *supra* Part IV.

206. 239 F. 139 (D.C.D.N.J. 1916).

207. *Id.*

208. *Id.* at 141.

209. *Id.*

210. *Id.*

211. *Id.* at 142.

212. *De Laski*, 239 F. at 142.

damages it sustained to the same extent as if it had manufactured and supplied the customer being sued, this was not a bar to relief.²¹³

Nevertheless, the court was sensitive about awarding a double recovery. The district court explained that the patentee could not be held to have received full compensation in the first suit, unless it would have been entitled to recover from the manufacturer infringer "all that it could presumably recover by way of damages from the" customer in the second suit.²¹⁴ The evidence showed that the infringer's customer would not have used the patented machines even if it had not acquired the infringing machines.²¹⁵ Accordingly, the district court concluded that the recovery in the first case could not have included compensation for use by the infringer's customer.²¹⁶ The court also concluded that the patentee, if it so elected, was entitled to recover profits from the customer, irrespective of the recovery of damages from the manufacturer, and to an injunction against the further use of the infringing machines.²¹⁷

Dowagiac Manufacturing Co. v. Deere & Webber Co. was another customer suit in which was interposed the defense of recovery by the patentee in satisfaction of a judgment against the manufacturer of the infringing drills.²¹⁸ The court considered *Birdsell* and its progeny and rejected the defense.²¹⁹ "The fact that there was a recovery against the manufacturer for profits in making the article complained of as an infringement does not prevent the patentee from proceeding against the manufacturer's vendee for an accounting, if he had made a profit, or for damages, or for an injunction."²²⁰

The United States Supreme Court returned to this area of law in *Union Tool Co. v. Wilson*.²²¹ Wilson successfully sued the Union Tool Company for infringement of a patent for underreamers.²²² He obtained a permanent injunction and the right to an accounting.²²³ The writ of injunction forbade the manufacture and sale, not only of infringing machines, but also of parts or elements that might be used in combination to effect infringement.²²⁴ The pat-

213. *Id.* at 143.

214. *Id.* at 144-45.

215. *Id.* at 146.

216. *Id.*

217. *Id.*

218. 284 F. 331 (8th Cir. 1922).

219. *Id.* at 334-50.

220. *Id.* at 335. The court then considered the distinction between recovery for profits and for damages, a range of remedies which no longer exists. *Id.*

221. 259 U.S. 107 (1922).

222. *Id.* at 108.

223. *Id.*

224. *Id.*

entee later sought to have the Union Tool Company held in contempt for violating the permanent injunction.²²⁵ The district court found that after the injunction, the Union Tool Company sold spare parts to be used with the machines sold by the company prior to the injunction.²²⁶ The Supreme Court explained the issue as follows:

The interlocutory decree awards to Wilson, among other things, compensation by way of damages and profits, for employing the invention in any machine sold prior to the service of the injunction. A patentee, in demanding and receiving full compensation for the wrongful use of his invention in devices made and sold by a manufacturer adopts the sales as though made by himself, and therefore necessarily licenses the use of the devices, and frees them from the monopoly of the patent. The license continues during the life of the machine; it does not end when repairs become necessary.²²⁷

Therefore, Union Tool Company argued that the sale of parts was licensed and not a violation of the injunction.²²⁸ This argument, in fact, prevailed in the district court.²²⁹ It did not succeed at the Supreme Court.²³⁰ Wilson had not yet received any compensation for the infringement.²³¹ Accordingly, implied license to use the spare parts in these machines existed.²³² Since such use constituted an infringement, the sale of the spare parts also violated the injunction.²³³ A finding of contempt by the court of appeals was affirmed.²³⁴

Directoplate Corp. v. Huebner-Bleistein Patents Co. was an appeal from an order of the trial court denying an infringing competitor's request that the patentee be enjoined from prosecuting suits against the infringer's customers.²³⁵ There had been a first suit, in which the patentee prevailed against the manufacturer on several, if not all, of the asserted patents.²³⁶ Then the patentee filed three separate suits against customers of the manufacturing infringer, charging infringement by use.²³⁷ On appeal, the court considered whether the patentee could maintain a suit against the infringer's customers and recover for infringement because of the use of the same devices for which the patentee already recovered

225. *Id.* at 109.

226. *Id.*

227. *Union Tool*, 259 U.S. at 113.

228. *Id.*

229. *Id.*

230. *Id.*

231. *Id.* at 114.

232. *Id.*

233. *Union Tool*, 259 U.S. at 114.

234. *Id.*

235. 44 F.2d 783 (7th Cir. 1930).

236. *Id.*

237. *Id.*

from the manufacturer.²³⁸ Both parties cited the *Birdsell* opinion. Without mentioning *Wilson*, the appellate court concluded that *Birdsell* was authority for the proposition that suits may be maintained against users despite prior recovery.²³⁹

*Egry Register Co. v. Standard Register Co.*²⁴⁰ involved a manufacturer who directly infringed by making and selling infringing machines and was also found to contributorily infringe by selling special supplies for the machines.²⁴¹ The appellate court first concluded that the plaintiff was not entitled to profits, but only to a reasonable royalty as the measure of damages.²⁴² The court explained that the reasonable royalty measure of recovery adopted the fiction that a license is granted when infringement begins.²⁴³ In effect, it explained, the judgment "creates and applies retrospectively a compulsory license."²⁴⁴ Finally, the reviewing court held that after adoption of the reasonable royalty basis of recovery, "the whole structure of subsequent contributory infringement falls, because the theory that the users of the devices were infringing the patent has been rejected and the theory of a lawful and noninfringing use flowing from a license has been substituted."²⁴⁵

*Goodyear Tire & Rubber Co. v. Overman Cushion Tire Co.*²⁴⁶ involved a variation of the typical customer suit situation. The patentee filed a first suit against the competitor's New York sales subsidiary.²⁴⁷ Validity and infringement were established. Then, in the accounting phase, the patentee unsuccessfully sought to add the manufacturing competitor as a co-defendant, after which it brought a second suit against the manufacturer.²⁴⁸ The first suit proceeded to a final decree on the accounting.²⁴⁹ The court awarded the patentee a reasonable royalty on the tires sold by the subsidiary.²⁵⁰

In the second case, the patentee sought to recover the manufacturer's profits on tires sold to its New York subsidiary, even though a reasonable royalty damage had been awarded and paid in the prior action.²⁵¹ The appellate court noted that the amount awarded in the prior case actually exceeded what the patentee

238. *Id.*

239. *Id.*

240. 23 F.2d 438 (6th Cir. 1928).

241. *Id.* at 439.

242. *Id.* at 442.

243. *Id.*

244. *Id.* at 443.

245. *Id.*

246. 95 F.2d 978 (6th Cir. 1937).

247. *Id.* at 980.

248. *Id.*

249. *Id.*

250. *Id.*

251. *Id.*

would have recovered if it had been successful in joining the parent company as a party for purposes of accounting for profit.²⁵² The court believed that in the prior case the reasonable royalty had been based upon the entire channel of production from wrongful manufacture and sale to the subsidiary to sale by the subsidiary to the public.²⁵³ The subsidiary purchaser was sued first and it paid a reasonable royalty for the manufacture and all sales. As a result, the court deemed the competitor's manufacture and sale to its subsidiary to have been licensed from the beginning.²⁵⁴

Wagner Sign Service, Inc. v. Midwest News Reel Theatres, Inc. presented another factual variation on the application of the single recovery rule.²⁵⁵ Here, the issue concerned the rights of the patentee after judgment but before payment.²⁵⁶ The *Wagner* appellate decision had been preceded by a case that found Adler had infringed the *Wagner* patent by the manufacture and sale of certain letter sign equipment.²⁵⁷ Adler appealed this finding of liability and the court granted a supersedeas upon the posting of a bond, which Adler furnished.²⁵⁸ While the appeal was pending on liability, the first case continued before a special master to report an account of damages and lost profits.²⁵⁹ As of the time of the appeal in the second action, the accounting had not yet been completed.²⁶⁰ The second suit was filed against one of Adler's customers.²⁶¹ The defendant in the second suit had no connection with, or interest in, the equipment in controversy, other than that of a user.²⁶² The district court entered a preliminary injunction against the user.²⁶³

The defendant customer argued on appeal that there was no valid basis for the injunction because it had purchased the equipment from Adler who was required to account to *Wagner* for all profits and damages and had furnished an appropriate bond.²⁶⁴ *Wagner* did not exact a royalty from its customers; the company derived all profits from manufacture and sale.²⁶⁵ The patentee ar-

252. *Goodyear*, 95 F.2d at 983.

253. *Id.* at 984. The court discussed the alternative, noting that if that had been the case, "[p]rofits earned by the parent company's sales to its subsidiary or even damages, if any, suffered by plaintiff by reason of manufacture and such sales, might then have been recoverable . . . The subsidiary's wrongdoing would be separate and distinct from that of the parent company." *Id.*

254. *Id.*

255. 119 F.2d 929 (7th Cir. 1941).

256. *Id.* at 930.

257. *Id.* at 929.

258. *Id.*

259. *Id.*

260. *Id.*

261. *Wagner*, 119 F.2d at 929.

262. *Id.*

263. *Id.*

264. *Id.* at 930.

265. *Id.*

gued that it had not yet been compensated by recovery and, therefore, was entitled to proceed by injunction against the defendant, as purchaser from Adler and user.²⁶⁶ The court started with "the generally accepted doctrine that where a patentee has been fully compensated by an infringing manufacturer for the manufacture and sale of the infringing device, the patentee has no recourse against a customer of such infringing manufacturer who is solely a user of such device."²⁶⁷ According to the appellate court, the real question was whether the protection afforded to the patentee by the supersedeas bond should be treated in lieu of actual compensation paid by Adler.²⁶⁸ If so, the patentee should not be permitted to maintain the second customer action. According to the appellate court, a supersedeas bond that such profits and damages would be paid when ascertained had assured the patentee.²⁶⁹ The patentee, having elected to obtain a judgment for all profits and damages that it could prove against the manufacturer and having assurance in the form of a bond that such judgment would be satisfied, "is in no position to complain of the mere use of the device by the defendant."²⁷⁰ The preliminary injunction was reversed.²⁷¹

B. Application of Single Recovery Rule Under Patent Act of 1952

After the passage of the Patent Act of 1952, the Supreme Court of the United States addressed the single compensation issue in *Aro Manufacturing Co., Inc. v. Convertible Top Replacement Co., Inc.*²⁷² There, the Supreme Court considered whether a contributory infringer could avoid damages because of payment by a direct infringer.²⁷³ Although *Aro* did not involve a supplier-customer relationship, the case is relevant for its reasoning.

Ford Motor Company was found to infringe a patent on a combination convertible top structure by including the combination in several model years without authority.²⁷⁴ Ford and the patentee entered into a settlement agreement by which Ford, its dealers, customers and users of its product were released from liability for infringement arising out of manufacture, use, or sale of cars made prior to the year in which settlement was effectuated.²⁷⁵ The

266. *Id.*

267. *Wagner*, 119 F.2d at 930.

268. *Id.*

269. *Id.*

270. *Id.* at 932. By contrast, in *TWM Manufacturing Co. v. Dura Corp.*, 722 F.2d 1261, 1270 (6th Cir. 1983), the appellate court distinguished *Wagner* on the grounds that bond posted by TWM of \$5000 was insufficient to cover the expected award from the accounting.

271. *Wagner*, 119 F.2d at 932.

272. 377 U.S. 476 (1964).

273. *Id.* at 481.

274. *Id.* at 478-79.

275. *Id.* at 482 n.4.

release expressly excluded "replacement top fabrics," as to which Ford was granted a license to make and sell for a specified royalty.²⁷⁶

The patentee then sued Aro Manufacturing Company for contributory infringement because it made and sold replacement tops especially designed for use in Ford automobiles.²⁷⁷ Aro asserted the release as a defense.²⁷⁸ The patentee relied on *Birdsell* and *Union Tool*. The Supreme Court disagreed with the patentee, stating that:

Birdsell allowed the patentee to hold one infringer liable for use of the patented machines after obtaining a judgment against another infringer for the manufacture and sale of the same machines; *Union Tool* held infringement to exist where the defendant, after being held liable for the manufacture and sale of certain infringing machines, sold spare parts for use in the same machines. Both cases turned upon the fact that the patentee had not collected on the prior judgment and thus had not received any compensation for the infringing use—or, indeed, any compensation at all. Here, in contrast, the amount paid by Ford under the agreement was expressly stated to include compensation for the use of the patented structures by Ford's purchasers; moreover, the agreement covered future use and in this respect operated precisely like a license, with the result that after the agreement date, there was simply no infringing use for which the patentee was entitled to compensation . . .²⁷⁹

Because the release expressly licensed continued use of the patented combination in Ford cars, the sale of replacement tops did not constitute contributory infringement.²⁸⁰

In contrast, the release preserved the patentee's rights against pre-release contributory infringers.²⁸¹ The Court agreed that "under the old common law rule, a release given to one joint-tortfeasor necessarily released another, even though it expressly stated that it would have no such effect."²⁸² However, the Court also noted that *Birdsell* rejected the common law rule.²⁸³ "By our law, judgment against one joint trespasser, without full satisfaction, is no bar to a suit against another for the same trespass.' What is true of a judgment is true of a release."²⁸⁴ The exclusionary clause in the release was effective.²⁸⁵

276. *Id.* at 494.

277. *Id.* at 479.

278. *Aro*, 377 U.S. at 493.

279. *Id.* at 499.

280. *Id.* at 500.

281. *Id.*

282. *Id.* at 501.

283. *Id.*

284. *Aro*, 377 U.S. at 501 (quoting *Birdsell v. Shaliol*, 112 U.S. 485, 489 (1884)).

285. *Id.* at 502.

Then, the Supreme Court considered what measure of damages could be recovered by the patentee against the contributory infringer for its pre-release sales of replacement tops.²⁸⁶ The Supreme Court started from the premise that if "full compensation" paid by a maker and seller can have the effect of releasing a user, such a result should follow in the case of a contributory infringer.²⁸⁷ In such a case, full payment by or on behalf of the direct infringer leaves nothing to be collected from the contributory infringer.²⁸⁸ The issue then became whether Ford's payment under the release constituted full payment for the infringing use committed directly by Ford's purchasers and contributorily by Aro.²⁸⁹ The Court remanded the case for a determination of whether the amount paid by Ford under the settlement was in fact adequate compensation that placed the plaintiff in as good a position as it would have occupied had there been no infringement.²⁹⁰

Maloney-Crawford Tank Corp. v. Sauder Tank Co., Inc. demonstrates the impact of Aro on customer suits.²⁹¹ This was a sister case to a patent action previously decided. In the first case, three patents were found to be valid and infringed.²⁹² The trial court assessed damages in the form of a reasonable royalty for the infringement of all three patents and stipulated that the royalty represented full and complete satisfaction for any form of infringement by the manufacturer or any of its purchasers.²⁹³

On appeal, the patentee argued that the trial court erred in precluding subsequent actions against the manufacturer's customers.²⁹⁴ The patentee contended that the manufacturer had infringed only one of the patents by making and selling the infringing units, whereas its customers, by using the units, infringed the two companion process patents.²⁹⁵ The trial court rejected this argument because it concluded the infringing units were designed to accomplish all of the contested claims of all three patents, and the patentee had stipulated that the only compensation it received for sale of products manufactured under the patents in suit is the initial purchase price.²⁹⁶ The Tenth Circuit Court of Appeals determined that the trial court's findings were not clearly erroneous and affirmed the preclusion of customer litigation.²⁹⁷

286. *Id.*

287. *Id.*

288. *Id.* at 503.

289. *Id.*

290. *Aro*, 377 U.S. at 513.

291. 511 F.2d 10 (10th Cir. 1975).

292. *Id.* at 11.

293. *Id.* at 12.

294. *Id.*

295. *Id.*

296. *Id.* at 12-13.

297. The Federal Circuit put an early gloss on the full compensation rule in

The Federal Circuit had occasion to construe the *Aro* and *Wilson* Supreme Court opinions in *King Instrument Corp. v. Otari Corp.*²⁹⁸ In this case, the patentee prevailed and was awarded damages as to machine sales and the sales of spare parts.²⁹⁹ In a first appeal, the Federal Circuit affirmed the award of damages on machine sales, but remanded the award on spare parts.³⁰⁰ The district court entered a permanent injunction against machine sales, and subsequently modified the injunction to include spare parts as well.³⁰¹ The infringer challenged the modified injunction to the extent it prohibited the sale of spare parts.³⁰² The reviewing court, citing *Wilson*, noted that the infringer had paid damages as to the past infringing machine sales in full "and hence has received an implied license on those sales."³⁰³ Since the manufacturer was an implied licensee, its sale of unpatented repair parts to its customers did not constitute direct infringement.³⁰⁴

The Federal Circuit Court of Appeals distinguished those facts in *Carborundum Co. v. Molten Metal Equipment Innovations, Inc.* to reach an opposite result.³⁰⁵ Metaullics manufactured an unpatented pump designed especially for use in its patented system for gas injection into molten metal.³⁰⁶ Metaullics also sold replacement parts for its pumps and, in fact, estimated that replacement parts cost about \$35,000 a year while the pumps cost between \$8,000 and \$20,000.³⁰⁷ Customers were free to buy spare parts for Metaullics' pumps from other sources.³⁰⁸ Metaullics successfully sued a competitor, MMEI, for contributory patent infringement resulting from MMEI's sale of its own pumps for use in

Stickle v. Heublein, Inc., 716 F.2d 1550 (Fed. Cir. 1983). The appellate court opined that:

[I]n appropriate circumstances, a patent owner may be able to recover the patent owner's lost profits attributable to each of a series of infringers. In contrast, when damages must be based on a reasonable royalty . . . [Aro] instructs us that a reasonable royalty is not to be separately calculated against each successive infringer. Once full recovery is obtained from one infringer with respect to a particular infringing device, at most nominal additional damages may be awarded against another with respect to the same device . . .

Id. at 1561.

298. 814 F.2d 1560 (Fed. Cir. 1987).

299. *Id.* at 1564.

300. *Id.* at 1561.

301. *Id.*

302. *Id.*

303. *Id.* at 1564.

304. *King Instrument*, 814 F.2d at 1564. The court also recognized that the sale of spare parts may or may not be an infringement. *Id.* It concluded that the infringer could properly supply its customers with spare parts attributable to repair. *Id.*

305. 72 F.3d 872 (Fed. Cir. 1995).

306. *Id.* at 875.

307. *Id.* at 876.

308. *Id.*

the patented system.³⁰⁹ The court awarded Metaullics lost profits and issued an injunction against future sales of pumps or from future sales of repair spare parts for its pumps.³¹⁰ MMEI challenged the scope of the injunction arguing that since it compensated Metaullics for its infringement of sales of its pumps with lost profit damages, it obtained an implied license for its customers to repair its pumps.³¹¹ Thus, MMEI argued, it was entitled to sell spare parts for its pumps to its customers in the future.³¹²

Because the injunction had been granted, Metaullics argued that it did not seek or receive compensation for future sales of spare parts.³¹³ If the injunction had not issued, Metaullics believed that it would have been entitled to lost profits on any future sales of spare parts as well.³¹⁴ The Federal Circuit Court of Appeals agreed that Metaullics had not received compensation for future sales of spare parts and affirmed the injunction.³¹⁵ The court went on to distinguish this case from *King Instruments*, stating that King Instruments had failed to prove entitlement to lost profits on sales of repair parts under the entire market value rule.³¹⁶

Finally, *Amstar Corp. v. Envirotech Corp.*³¹⁷ considered several aspects of the full compensation rule. Here, the patentee sought an injunction against the manufacturer's customers to preclude continued use.³¹⁸ The patentee had been awarded its lost profits for the infringer's sale of the devices in question.³¹⁹ The patentee argued that it was entitled to an injunction because it had not been paid yet.³²⁰ The infringer's parent company had filed a corporate guaranty that promised to pay the judgment by certified check within thirty days of the appellate court's mandate.³²¹ The patentee intimated that the parent company might not pay the judgment, but the reviewing court characterized such intimations as "unsupported."³²² The Federal Circuit concluded that the filing of a corporate guaranty was "sufficiently equivalent to compensation" to warrant denial of an injunction against the infringer's customers.³²³

309. *Id.*

310. *Id.*

311. *Carborundum*, 72 F.3d at 887.

312. *Id.*

313. *Id.*

314. *Id.*

315. *Id.* at 881-82.

316. *Id.* at 882.

317. 823 F.2d 1538 (Fed. Cir. 1987).

318. *Id.* at 1541.

319. *Id.*

320. *Id.*

321. *Id.*

322. *Id.* at 1549.

323. *Amstar*, 823 F.2d at 1549.

VI. THE FUTURE OF SEQUENTIAL LITIGATION UNDER THE SINGLE RECOVERY RULE

As is the case in many areas of patent law, the nature of damages recoverable from an infringer's customers has shifted substantially over the years. To some extent, the shift from *Birdsell* to *Aro* has been aided by the elimination of the right to recover an infringer's profits in the Patent Act of 1946.³²⁴ Stated differently, a patentee who suffers lost profits or loss of royalty income ordinarily can be compensated and made whole by the manufacturing infringer. In the usual course of events, the length of the accused manufacturer's distribution chain should have no impact on the patentee's ability to be made whole by the manufacturer. By contrast, if an infringer's profits were also recoverable, as was the case between 1819 and 1946, making the patentee whole would be a far more complicated matter.

Consequently, with the simplification of the damages recovery model under the Patent Act of 1946, a patentee is much more likely to receive full compensation from the first defendant, which typically is the manufacturing infringer. Whether a court in a subsequent suit decides a patentee has received full compensation depends on the scope of the judgment, the construction of any settlement agreements and whether the damages previously recovered were compensation for the infringement along the entire channel of trade. In any event, full satisfaction of those damages along the channels of trade would seemingly permit an infringer's customers to continue use of an infringing product. In view of the modern theory of damages, it appears that efforts to procure recovery from different levels in the distribution (or user) chain will be difficult to accomplish, so long as the manufacturer is solvent.

Nevertheless, the application of the single recovery rule leaves several open questions. First, can a patentee preserve its right to pursue an infringing competitor's customers? In theory, a patentee could assert a claim against its competitors only for "making" and later suing the customer for "using."³²⁵ This approach might apply when a patentee occupies two levels in the distribution chain and its patent covers both levels (*i.e.*, an integrated company that manufactures a patented component that is incorporated into a patented system). In this type of situation, an infringing manufacturer and its infringing customer might each be liable for respective levels of damage to the patentee. However, even if the exclusionary rights remain separate and independent, the is-

324. See *Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., Inc.*, 377 U.S. 476, 505 n.20 (1964); 35 U.S.C. § 70 (1994).

325. A claim for "making" and "selling" after a first recovery might give rise to an implied license defense (or an exhaustion defense) by the infringing competitor's customer. *E.g.*, *King Instrument Corp. v. Otari Corp.*, 814 F.2d 1560 (Fed. Cir. 1987); *United States v. Univis Lens Co.*, 316 U.S. 241 (1942).

sue of whether compensation for "making" is sufficient to preclude recovery for "using" lingers. Presumably, it is possible to create a damage model limited to the "making" of a product that is intended to be resold, such as where the infringing product is used as a loss leader for other products or services.³²⁶ Whether this approach would be effective against an infringing competitor and its customers in an "ordinary" marketing situation is even more problematic, but the creativity of damage experts faced with a proximate causation standard should not be underestimated.

Second, can a patentee that seeks only injunctive relief against an infringing manufacturer obtain an injunction and damages against the manufacturer's customers? This would seem to be an appropriate election of remedies by a patentee and a result consistent with existing case law. On the other hand, a manufacturing defendant accused of infringement might assert a declaratory counterclaim in an effort to foreclose or preempt suit against the manufacturer's customers. While it is beyond the scope of this article to wade through the nuances of a declaratory judgment counterclaims for a determination of damages, it does appear such a claim would be ripe, if only because of a manufacturer's traditional indemnification obligations.³²⁷

Third, what is the impact of an agreed or consent judgment, which is often involved in patent cases? Such a judgment has the same effect as a trial on the merits. Unless the judgment reserves issues within its four corners, a subsequent suit on the same claim or cause of action generally is barred.³²⁸ To the extent the judgment grants or denies relief, such as money damages, additional or different relief cannot be obtained in a new lawsuit.³²⁹ Thus, a patentee needs to be careful in crafting a consent judgment if the patentee plans to seek additional compensation downstream.

CONCLUSION

The evolution of patent damage law appears to have greatly simplified full compensation for the patentee. In many cases, patent damage law allows continued use by an infringer's customers. However, there appear to be at least some circumstances in which

326. See, e.g., *Rite-Hite Corp. v. Kelley Co.*, 56 F.3d 1538 (Fed. Cir. 1995) (holding that the infringer's liability to compensate for injury is limited only by proximate causation).

327. See, e.g., TEX. BUS. & COM. CODE ANN. § 2.312(c) (West 1994) (stating that "[u]nless otherwise agreed, a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third party by way of infringement.").

328. *Epic Metal Corp. v. H.H. Robertson Co.*, 870 F.2d 1574 (Fed. Cir. 1989); *Kurzweg v. Marple*, 841 F.2d 635 (5th Cir. 1988).

329. E.g., *Eichman v. Fotomat Corp.*, 871 F.2d 784 (9th Cir. 1989); *Lubrizol Corp. v. Exxon Corp.*, 871 F.2d 1279 (5th Cir. 1989).

relief may be available against both the infringing manufacturer and its customers.