LEGAL UPDATE

FULFILLING THE “DUE CARE” REQUIREMENT AFTER

KNORR-BREMSE

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I. INTRODUCTION

Since September 2003, the legal community and the manufacturing and technical communities have anxiously awaited the Federal Circuit’s ruling in a case concerning infringement of a patent for air disc brakes.1 The court agreed sua sponte at that time to visit the issues of willful patent infringement and waiver of the attorney-client privilege en banc.2

The issue of willful patent infringement hangs over the manufacturing industry like a dark cloud. Even if a manufacturer does not copy a patented invention, it may still be liable for patent infringement involving its independently-produced similar item.3 Patent infringement litigation is lengthy and time consuming and can have dire consequences. If a court finds the manufacturer liable for patent infringement, the court can award the patent owner a sizeable judgment4, it can bar the manufacturer from selling key products, or both. A finding of willful infringement can then triple the damages and force the infringer to pay the patent owner’s legal fees in addition


2 Id. It was especially significant that the court decided to hear this argument en banc, since only en banc decisions by the Federal Circuit are binding on future panels. Nystrom v. Trex Co., 374 F.3d 1105, 1112 n.2 (Fed. Cir. 2004) (citing Newell Cos. v. Kenney Mfg. Co., 864 F.2d 757, 765 (Fed. Cir. 1988)).

3 Inadvertent infringement occurs when the infringer has not copied the patent, but its product is similar to the patented product.

4 The damages for patent infringement are a “reasonable royalty” plus the patent owner’s lost profits, if any. 7 DONALD S. CHISUM, CHISUM ON PATENTS § 20.03 (2002).
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to the infringer’s own.5 On the other hand, it is not clear to the legal community, much less to technologists, as potential infringers, how best to avoid a finding of willful infringement.6

Both manufacturers and the patent bar hoped that the court’s en banc decision in Knorr-Bremse Systeme Fuer Nutzfahrzeuge GmbH v. Dana Corp.7 would clarify this situation. Although the decision upheld the sanctity of the attorney-client privilege, it did not go nearly far enough in informing potential litigants how to shape their behavior.8 Since a practical goal of a binding en banc decision is to guide the public’s actions, the Federal Circuit has fallen short, at least in this respect.

II. THE BEGINNING OF WILLFUL PATENT INFRINGEMENT

The Federal Circuit was formed in part with the intention of strengthening patent rights to encourage innovation.9 It made this clear in one of its early cases, Underwater Devices, Inc. v. Morrison-Knudsen Co.10 Morrison-Knudsen (“MK”) was hired to install underwater pipe in Hawaii.11 Underwater Devices (“UDI”) held patents covering underwater pipes and a method for laying them.12 UDI routinely licensed its patented technology to contractors laying underwater piping.13 After MK bid on the Hawaii project, UDI sent MK a letter informing MK of UDI’s patent and offering a license before MK began work.14 MK’s in-house counsel advised the regional manager that he should go ahead without a license for a number of reasons.15

Although the letter did indicate some belief that the patents could be invalid because of the existence of prior art, the most compelling reason to forego a license was probably the one that irritated the court so much.16 The counsel stated that, “Courts, in recent years, have – in patent infringement cases – found the patents claimed to be infringed upon invalid in approximately 80%

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5 Id.
6 The problem is most pronounced for inadvertent infringers, those that are not aware that their products are covered by another’s patents, until the patent owner tells them.
7 383 F.3d 1337 (Fed. Cir. 2004).
8 See generally id.
9 Knorr-Bremse, 383 F.3d at 1343 (citing Advisory Committee on Industrial Innovation Final Report, Dept. of Commerce (Sept. 1979)).
10 717 F.2d 1380 (Fed. Cir. 1983).
11 Id. at 1384.
12 Id. at 1382.
13 Id. at 1384.
14 Id. at 1384-85.
15 Underwater Devices, 717 F.2d at 1385.
16 Id.
of the cases.”\textsuperscript{17} He believed that UDI would not sue, because they were currently receiving some royalties from licensees and if they sued, the patent would likely be invalidated and then UDI would receive nothing.\textsuperscript{18}

UDI did sue MK.\textsuperscript{19} The district court found validity, infringement and willful infringement.\textsuperscript{20} The court trebled the damages in response to the finding of willfulness.\textsuperscript{21} The Federal Circuit affirmed on all counts.\textsuperscript{22} The court stated that MK did not act in good faith based on the “totality of the circumstances.”\textsuperscript{23} Among the reasons the court gave were: 1) getting the ‘freedom to operate’ opinion from in-house counsel rather than an outside patent attorney, 2) not looking at the prosecution histories of the patents involved, and 3) the opinion from in-house counsel was inadequate since it did not contain a complete and exhaustive validity and infringement analysis.\textsuperscript{24}

A. Patent Opinion Letters

\textit{Underwater Devices} stressed the de facto requirement of obtaining an opinion from a qualified outside patent attorney concerning the validity and possible infringement of any patent by any product.\textsuperscript{25} The court emphasized that the manufacturer must obtain this opinion before it begins any potentially infringing activity.\textsuperscript{26} Determination of the validity of a patent depends on a thorough search of the prior art to look for references which render the patent either anticipated or obvious.\textsuperscript{27} Along with willfulness, the obviousness standard has changed over time and may even vary by industry.\textsuperscript{28} It is therefore very difficult to predict if the court might find a patent valid.

Even more difficult is the question of infringement. Since the Federal Circuit’s decision in \textit{Markman v. Westview Instruments}, determination of infringement consists of a two-step analysis.\textsuperscript{29} First the claims are construed to

\textsuperscript{17} Id.
\textsuperscript{18} \textit{Underwater Devices}, 717 F.2d at 1385 (“Underwater Devices must recognize that if they sue us, they might kill the goose that lays the golden eggs.”).
\textsuperscript{19} Id.
\textsuperscript{20} Id. at 1386.
\textsuperscript{21} Id.
\textsuperscript{22} Id. at 1390-91.
\textsuperscript{23} \textit{Underwater Devices}, 717 F.2d at 1390.
\textsuperscript{24} Id.
\textsuperscript{25} Id.
\textsuperscript{26} Id.
\textsuperscript{27} Id.
\textsuperscript{29} Vitronics Corp. v. Conceptronic, Inc., 90 F.3d 1576, 1581-82 (Fed. Cir. 1996) (citing \textit{Markman v. Westview Instruments}, Inc., 52 F.3d 967, 976 (Fed. Cir. 1995)).
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determine their plain meaning to a person having ordinary skill in the art (“PHOSITA”). Then the product is compared to those claims. Only where every limitation in a given claim or its equivalent is found in the product does the product infringe that claim. This analysis is lengthy and painstaking. A slight difference in the presumed meaning of any claim term could change the entire result, as is often seen when infringement cases are appealed.

In order to avoid a finding of willfulness, the Federal Circuit has held that when “a potential infringer has actual notice of another’s patent rights, he has an affirmative duty to exercise due care to determine whether or not he is infringing.” This exercise of due care includes getting a patent opinion letter from outside counsel. For a manufacturer, freedom to operate thus entails multiplying the time, effort, and cost required in getting a complete validity and infringement opinion by the number of patents (and products) that a manufacturer is aware of, and factoring that into his development costs. Also, as the patent law develops and new patents are granted, opinions need to be updated in order to be fully valid.

B. WILLFULNESS DETERMINATION AND ITS RAMIFICATIONS

In Underwater Devices, the court stated that it would determine willfulness based on the “totality of the circumstances.” Nine years later, in Read Corp. v. Portec, Inc., the court listed the factors it would consider in determining if damages should be increased. These factors are: 1) intentional copying by infringer; 2) good faith belief that any patents infringer knew of were invalid or not infringed (based on patent opinion by qualified outside counsel), 3) infringer’s behavior in litigation, 4) infringer’s size and financial condition, 5) closeness of the case, 6) duration of infringing behavior, 7) infringer’s remedial actions to stop infringing, 8) infringer’s motivation to harm patent owner, and 9) infringer’s attempts to hide infringing activity. The court refers to these factors as punitive damage considerations, thereby equating willfulness with behavior worthy of “punishment.”

Consistent with the view that a willful patent infringer deserves punitive damages is the assessment of attorney’s fees. By statute, the court may award

31 Vitronics, 90 F.3d at 1581-82.
33 Vitronics, 90 F.3d at 1586.
34 Underwater Devices, 717 F.2d at 1389.
35 Id. at 1390.
36 Id. at 1390.
38 Read, 970 F.2d at 827.
39 Id.
attorney’s fees to the winning party in “exceptional” cases.40 “Exceptional” is not defined anywhere, but the Federal Circuit has practically equated a finding of willfulness with a finding that a case is exceptional.41 Depending on how the considerations turn in a particular case, even an unintentional infringer may find himself exposed to a greatly magnified damage award. The size of the award may be solely based on the infringer either not obtaining or not divulging an attorney’s patent opinion letter.42

III. PROBLEMS WITH THE WILLFULNESS DOCTRINE

A. Rational Ignorance

An obvious solution to the problem of the costs and difficulties in obtaining patent opinions by outside counsel is deliberate ignorance. If a company advises its employees to actively avoid reading any patents, the company can avoid the “actual notice” which triggers the “duty to exercise due care.”43 Is it possible that rational ignorance is the solution? The purpose of the patent system is “[t]o promote the Progress of Science and Useful Arts.”44 The progress of science is served much better by having inventors build on others’ work.45 The Federal Circuit has repeatedly held that the purpose of the patent disclosure is to enable the PHOSITA to reproduce, build upon, or design around the patented invention.46 The PHOSITA cannot do this if he cannot look at a patent, lest he risk triple damages in a later infringement suit. This also does nothing to address the “widespread disregard of patent rights [that] was undermining the national innovation incentive” when Congress created the Federal Circuit.47

Several of the amicus briefs in the Knorr-Bremse case pointed out that the court’s willfulness doctrine has done little to help patent owners, but has had

41 S.C. Johnson & Son, Inc. v. Carter-Wallace, Inc., 781 F.2d 198, 201 (Fed. Cir. 1986). While the trial court must explain its basis for finding a case is exceptional, where there is willfulness, the trial court must explain why it did not find the case exceptional. Id.
42 See infra Section III.B.
43 Knorr-Bremse, 383 F.3d at 1351 (Dyk, J., dissenting).
44 U.S. CONST. art. I, § 8, cl. 8.
47 Knorr-Bremse, 383 F.3d at 1343 (citing Advisory Committee On Industrial Innovation Final Report, Dept. of Commerce (Sept. 1979)).
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several detrimental affects on industry.48 In addition to rational ignorance of all patents, there are “window-dressing” legal opinions49, and the ability of questionable patents to force competitors to either pay licensing fees or leave the business.50 Finally, the Federal Trade Commission has recommended that Congress limit willfulness to cases of truly culpable behavior.51

B. Attorney-Client Privilege Waiver: Adverse Inference

Shortly after its Underwater Devices decision, the Federal Circuit clarified its view on patent opinion letters.52 In Kloster Speedsteel AB v. Crucible Inc., the court held that the infringer’s

“[S]ilence on the subject [of advice of counsel], in alleged reliance on the attorney-client privilege, would warrant the conclusion that it either obtained no advice of counsel or did so and was advised that its importation and sale of the accused products would be an infringement of valid U.S. patents.”53

The court would assume that the infringer had not exercised due care, or worse yet, assume that the infringer was flagrantly going against advice of counsel, based on the infringer’s unwillingness to waive his attorney-client privilege. The court recognized the dilemma created for the infringer: either assert attorney-client privilege and risk a finding of willfulness, or waive it and open himself up to potential prejudice in the liability phase.54

48 Id. at 1351.

49 These are opinions written to justify the manufacturer’s infringing behavior, rather than to honestly assess infringement. Id.

50 Id. Law firms and investors can buy patents at bankruptcy auctions and then assert them against a manufacturer. The ‘patent troll’ has nothing to lose, but the manufacturer has significant exposure. The manufacturer cannot ignore the troll, because that could lead to a finding of willfulness. Often the manufacturer will settle with the troll, rather than engage in expensive, risky litigation. This, unfortunately, only encourages the troll and gives him more ammunition to use against his next victim. Patent Quality Improvement: Hearing Before the Subcommittee on Courts, the Internet and Intellectual Property of the Committee on the Judiciary, House of Representatives, 108th Congress, 3-5 (July 24, 2003) (statement of David M. Simon, Chief Patent Counsel, Intel Corporation), available at http://www.house.gov/judiciary/simon072403.pdf.


53 Id. at 1580.

54 Quantum Corp. v. Tandon Corp., 940 F.2d 642, 643-44 (Fed. Cir. 1991). A completely one-sided opinion may indicate a lack of objectivity and therefore a lack of accuracy. Id. The court views any doubts expressed in the opinion as signs of genuineness, but that evidence could be damaging in the liability phase. Id.
Requiring a party accused of patent infringement to waive his attorney-client privilege represents a substantial burden to that party. As the court notes in *Knorr-Bremse*, "the Supreme Court describes the attorney-client privilege as 'the oldest of the privileges for confidential communications known to common law.'" Based on that fact alone, the court should respect the attorney-client privilege and find no adverse inference in a party’s decision not to waive it. In practice, there are additional reasons to find no adverse inference. Once the infringer waives his attorney-client privilege, it is entirely waived. Any and all communications between the infringer and his attorney on that matter are available to the court.

Waiver of the attorney-client privilege for patent opinions has led to convoluted practice in patent litigation. To limit the scope of the waiver, often a manufacturer will hire an attorney separate from his normal litigation or patent attorney. This increases the client’s costs, since this attorney is not familiar with the patents or the manufacturer’s products. It also puts the manufacturer in a difficult situation of having to choose a new attorney. The attorney writing the patent opinion is also in a difficult situation. He knows he must be diligent and give an honest opinion, but he knows that even a tentative opinion may reflect badly on his client. In some cases, attorneys were forced to testify during their client’s infringement trials, in other cases, litigation expanded as the scope of the privilege waiver was debated.

The other problem associated with the practice of waiving the attorney-client privilege and producing patent opinion letters relates to prejudice during the liability phase of an infringement trial. The patent opinion will likely detail all the possible ways infringement might be found, even as the attorney rebuts them. This letter might lay out the patent owner’s entire case, or at least divulge the infringer’s entire defense. Some courts choose to bifurcate the trials of liability and damages, even using different juries, to solve this problem. This, combined with a stay on discovery of the patent opinion until after the liability phase, removed the prejudice from the liability phase, but made litigation lengthy and complicated.

Even without these problems, the patent opinion is vulnerable on many

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55 *Knorr-Bremse*, 383 F.3d at 1344 (citing Upjohn Co. v. U.S., 449 U.S. 383, 389 (1981)).
58 *Id*. Rough drafts of patent opinions as well as any notes by the attorney are admissible once the privilege is waived.
59 *Id*.
60 Thomas Presson, Knorr-Bremse and Questions about Production of an Exculpatory Legal Opinion and the Adverse Inference, 44 IDEA 409, 422-23 (2004).
61 *Id*.
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fronts during a jury trial. The patent owner can attempt to impeach the qualifications of the attorney who wrote the opinion, on either a technical or a legal basis.62 If the infringer paid ‘too little’ for the opinion, it must not be very good; if the infringer paid ‘too much’, he may have ‘bought’ just the opinion he wanted, rather than the truth.63 If a manufacturer obtains complete patent opinions as soon as he becomes aware of any relevant patent and then updates them regularly with any change in the law, his products, or the patents, he will be spending a lot of money on patent opinions.64 If the manufacturer waits until the patent owner sues him, the jury could find that is too late to show ‘due care’.65 Once the jury finds liability for patent infringement, a finding of willfulness is all too easy.

IV. THE KNORR-BREMSE EN BANC DECISION

Knorr-Bremse is a German manufacturer of air disc brakes for trucks, and owns patents to cover those brakes in Europe and the United States.66 Haldex Brake Products Corp., (“Haldex”), a co-defendant, is a Swedish brake manufacturer, which sells through Dana Corp. (“Dana”), an American corporation.67 Knorr-Bremse gave both Haldex and Dana notice of possibly infringing activity before bringing suit for infringement.68 At the trial, Haldex told the court it had consulted American and European lawyers for advice on possible infringement, but refused to waive its attorney-client privilege and disclose that advice.69 Dana stated that it relied on Haldex’s legal advice and did not seek its own.70 The district court concluded that Haldex’s opinions were unfavorable.71 The court went on to find that Dana and Haldex had willfully infringed Knorr-Bremse’s patents and awarded Knorr-Bremse enhanced damages and attorney fees.72

It was this issue of an adverse inference whenever an infringer refused to waive his attorney-client privilege and produce a patent opinion letter that the court considered en banc.73 The court received twenty four amicus curiae

63 Id.
64 Id.
65 Id.
66 Knorr-Bremse, 383 F.3d at 1341.
67 Id.
68 Id.
69 Id. at 1342.
70 Id.
71 Knorr-Bremse, 383 F.3d at 1342.
72 Id.
73 Id. at 1344.
briefs in this case, from both bar associations and manufacturers. The amici were unanimous in recommending that the court remove the adverse inference and that a substantial defense to infringement should defeat willfulness even without a patent opinion letter. The court removed the adverse inference from both the failure to waive the attorney-client privilege and the failure to seek timely, competent legal advice at all. The court declined, though, to allow a substantial defense to infringement to defeat a finding of willfulness. Furthermore, the court stressed that an infringer may still waive privilege and introduce a patent opinion. Also, the court declined to rule on whether or not the finder of fact may consider 1) whether the infringer obtained an opinion and 2) whether or not the infringer admitted the opinion, in the ‘totality of the circumstances’ for willfulness.

Removing the adverse inference was a step in the right direction, but it was not nearly enough. Manufacturers and technologists are left with no clear guidance on the necessity of obtaining a patent opinion every time a patent owner makes them aware of a patent they may infringe. Arguably, telling a jury that an infringer did not bother to obtain a patent opinion when he could and should have is very similar to an adverse inference. Likewise, telling a jury that an infringer obtained a patent opinion and is choosing not to disclose it will likely create an adverse inference in their minds.

The dissent in Knorr-Bremse recognized that the majority opinion was very limited. Judge Dyk stated that the duty to obtain the patent opinion should have been removed, rather than just the adverse inference. The dissent first points out that enhanced damages for willfulness are a form of punitive damages, just as the court found in the Underwater Devices case. He then acknowledged that a finding of willfulness would be appropriate in some cases, as when there is deliberate copying, hiding infringing activity, or cases where the infringer has only frivolous defenses or was deliberately out to harm the patent owner. These behaviors rise to a level that is commensurate with the awarding of punitive damages in other tort cases.

After analyzing the history of the patent damages statute the dissent

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75 Id.
76 Knorr-Bremse, 383 F.3d at 1344-45.
77 Id. at 1347.
78 Id. at 1345.
79 Id. at 1346-47.
80 Id. at 1348 (Dyk, J., dissenting).
81 Knorr-Bremse, 383 F.3d at 1348 (Dyk, J., dissenting).
82 Id. at 1348-49 (Dyk, J., dissenting).
83 Id. at 1349 (Dyk, J., dissenting).
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concludes that the Supreme Court and Congress never read a duty of care into patent infringement damages. Further, the Supreme Court has held that punitive damage awards should be confined to cases where the conduct is truly reprehensible. Awarding punitive damages for less culpable behavior may violate the due process clause.

Finally, the dissent recognizes that the due care requirement has not helped the patent system. The complexity of patent law renders patent opinions difficult and expensive. The detrimental side effects like rational ignorance and deterring validity challenges outweigh any benefits. The dissent concludes that the court should eliminate the entire due care requirement, not just the adverse inference.

V. PROPOSED SOLUTIONS

The Federal Circuit has spoken en banc and still supports the due care requirement, with the exception of one dissenter. If the parties in the Knorr-Bremse case appeal to the Supreme Court, the Court could take that opportunity to ensure that all awards of punitive damages are in line with the due process clause and limit willfulness to a higher level of culpability. Conversely, the Federal Circuit could wait for the next case, where willfulness was based on the totality of the evidence that a manufacturer failed to disclose a patent opinion (with no adverse inference). The court could then remove the due care requirement from the considerations for willfulness. Finally, Congress could act to remove the due care requirement in one of two ways. First, it could amend the patent damages statute to identify and limit the considerations for a finding of enhanced damages to instances of reprehensible conduct. Second, Congress could add a federal rule of evidence restricting admissibility of patent opinions in the same way that evidence of subsequent remedial measures is restricted.

VI. CONCLUSION

The Federal Circuit en banc Knorr-Bremse decision eliminated the adverse inference associated with the failure of an infringer to obtain and/or divulge an

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84 Id. at 1349-50 (Dyk, J., dissenting).
85 Id. at 1350 (Dyk, J., dissenting).
86 Knorr-Bremse, 383 F.3d at 1350 (Dyk, J., dissenting).
87 Id. at 1351 (Dyk, J., dissenting).
88 Id. (Dyk, J., dissenting).
89 Id. at 1352 (Dyk, J., dissenting).
90 FED. R. EVID. 407. The notes accompanying the rule state that the evidence is excluded for two reasons: 1) because the behavior is not necessarily consistent with liability and 2) the social policy of not discouraging people from taking remedial measures. Id. advisory committee’s note.
outside counsel patent opinion. Unfortunately, the decision did little else. By retaining the standard of due care and the totality of the circumstances considerations for a finding of willfulness, it is likely that the patent opinion will continue to play a dominant role. If anything, this decision leaves parties less certain about whether to obtain independent patent opinions, or what to do with them if they do. As this is an important area of patent law, either Congress or the courts should act to remove the de facto requirement of patent opinions.