



An Uptick in Customer-Suit Exception After TC Heartland?

By Matthew Zorn

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One speculated consequence of TC Heartland is that patentees may choose to file lawsuits against other parties in the supply chain. Since the patent laws provide a remedy against “whoever ... sells any patented invention, within the United States,” manufacturers are not the only potential target.[1] Plaintiffs may sue distributors or retailers instead. Notably, plaintiffs can sue distributors or retailers in venues in which venue against the manufacturer might be improper. Therefore, plaintiffs can outflank TC Heartland by suing a batch of big-box retailers in the desired venue and capture a slice of the royalty pie from each. To some extent, this may already be happening. For example, very recently, trampoline manufacturer JumpSport Inc. sued Lowe’s Companies Inc. in the Eastern District of Texas for sales of Skywalker branded trampolines.[2]

These “customer suits” illustrate a key issue with TC Heartland and why, for many companies, the decision may cause more problems than it solves. If plaintiffs cannot sue an electronics manufacturer in the chosen venue, they can simply sue Best Buy or Walmart instead. Can’t sue the app developer? Sue distributors or users of the application. Then use third-party discovery to prove up the case.

This approach is less than ideal for the judicial system for a number of reasons. In general, we want to have the least cost avoider as the defendant, i.e., the party in the best position to avoid the harm. Suing down the supply chain violates this principle. Even patent holders ought to want the least cost avoider as defendant because it usually offers the greatest potential damages in a single lawsuit. But in a world where venue can be king, the downsides of having to sue in the manufacturer’s home venue may be substantially outweighed by the benefits of plaintiff having its venue of choice. Moreover, TC Heartland ought to do little to disrupt revenue models that depend less on receiving a reasonable royalty and more on collecting below cost-of-litigation settlements from multiple parties. In this nuisance model of patent litigation, the approach of suing a multitude of customers instead of a single manufacturer or supplier may prove to be even more profitable than a single manufacturer suit.[3]

When customer suits happen, indemnification clauses may compel suppliers or manufacturers to intervene or otherwise become involved in the customer action. Or they may want to intervene to preserve goodwill among its customers. Particularly in patent cases, intervention may simply be prudent. Issues arising in customer litigation relating to the asserted patent may affect later litigation against the manufacturer, even if the manufacturer litigation takes place in a different forum. For example, recognizing the importance in uniformity in claim construction, district courts often give “reasoned deference” to prior claim construction orders in other jurisdictions. [4]

If (or when) customer suits increase, practitioners and in-house counsel should become familiar with the “customer-suit exception” and the body of case law surrounding it, an area

that as recently as 2013 was characterized by academics as “forgotten” and in “relative disuse.”[5] Formally, the customer-suit exception is an exception to the first-filed rule. Under the exception, litigation against or brought by the manufacturer of infringing goods takes precedence over a suit by the patent owner against customers of the manufacturer, even if the manufacturer suit is later-filed. Application of the exception depends on the determination of three factors: (1) whether the customer defendant in the earlier-filed case is merely a reseller; (2) whether the customer-defendant agrees to be bound by any decision in favor of the patent owner; and (3) whether the manufacturer is the only source of the infringing product. Therefore, one way for manufacturers to defend their customers is to respond with a declaratory judgment action in the forum of its choice. Then, either the manufacturer or its customer moves for a stay in the customer forum. The customer-suit exception solves some of the least cost avoider issues inherent with suing down the supply chain in patent cases.

Recent cases have expanded the exception beyond its formal strictures. What emerges is the general principle that infringement suits against customers should yield if the manufacturer suit has the potential to simplify or resolve the customer suits. Three relatively recent and lesser acclaimed Federal Circuit mandamus cases coming out of the Eastern District of Texas illustrate the contours of the customer-suit exception and principles of comity: In re Nintendo, In re Google and In re Dell.

In Nintendo, the Federal Circuit concluded that customer suit exception principles can cover a case in which a manufacturer is sued along with customers in the same forum. In the case, Nintendo moved to sever and transfer the claims against it to the Western District of Washington, which it argued was a more convenient forum. Nintendo also requested a stay and pointed out that the retailers had stipulated that they would be bound by a judgment rendered by the Western District of Washington. The Eastern District of Texas court denied the motion. Having decided against severance, the district court concluded that the request for transfer must also be denied. Nintendo sought a writ of mandamus, and the Federal Circuit issued the writ. While the Federal Circuit acknowledged that the circumstances of the case differed from the formal customer-suit exception, it held that the same general principles applied nonetheless. It concluded that to facilitate a just, convenient, efficient, and less expensive determination, the district court should have granted Nintendo’s motion and stayed the remaining customer cases in the Eastern District of Texas.[6]

The Google case illustrates a different fact pattern where the patent holder omits the manufacturer from suit. The Rockstar Consortium sued various handset manufacturers in the Eastern District of Texas for patent infringement, but did not sue the manufacturer of the allegedly infringing Android operating system, Google Inc. Google then filed a declaratory judgment action in the Northern District of California for a judgment that its Android operating system did not infringe. In response, Rockstar amended its Texas complaint to include Google as a defendant and moved in the California case for transfer or dismissal. The California court denied the motions. Then, Google moved in Texas for transfer or dismissal, which was denied also. Google petitioned the Federal Circuit for a writ of mandamus in the Texas Court, and the Federal Circuit granted the writ. Similar to Nintendo, the Court found that under principles of comity, “there was no need to proceed with the five Texas actions because the one California action may suffice.”

However, if the customer and manufacturer or supplier are properly joined in the same suit

and in the right venue, the customer-suit exception and principles of comity may not prevail. This is what happened in the Dell case. In Dell, the plaintiff sued manufacturer-customers such as Dell in the Eastern District of Texas, along with the supplier of the allegedly infringing operating system, Microsoft Corp. The manufacturer-customers and supplier Microsoft moved to transfer the case to the Western District of Washington. The district court denied the motion and further denied a motion to stay. Then, the Federal Circuit denied the writ of mandamus that followed. The Federal Circuit concluded that the district court did not err in denying the transfer, noting that numerous judicial economy issues favored maintaining venue in the Eastern District of Texas. Then, the court rejected the notion that a district court must stay proceedings against a customer in the same litigation that will, regardless of the requested stay, go forward against the supplier. It clarified that Nintendo and Google stand for the proposition that customer suits should be stayed when the litigation is separate or should be separated to prevent parallel duplicative or inefficient litigation.[7]

As powerful as customer-suit principles are, they are no panacea to manufacturers or suppliers. First, while cases like Dell may fall outside of the customer-suit exception, after TC Heartland, those cases might become rare. Since venue must be proper as to each defendant, it may be impossible for the plaintiff to properly join the customer and supplier in the same court as was the case in Dell. Second, a key limitation to a defensive declaratory judgment action remains: personal jurisdiction. Declaratory judgments require personal jurisdiction over the declaratory judgment defendant, and declaratory judgment actions for noninfringement or invalidity are no exception.[8] Under Daimler, general contacts with a state are not sufficient to establish general jurisdiction.[9] In addition, sending enforcement letters, without more, is generally not sufficient to satisfy specific jurisdiction.[10] By contrast, sending enforcement letters into a jurisdiction and then visiting the jurisdiction to enforce or defend the patent might be sufficient.[11] So while personal jurisdiction over a practicing entity that distributes products into the forum might be easy enough to obtain, personal jurisdiction over nonpracticing entities is an entirely different matter. And when it comes to the archetypal pop-up patent assertion entity, personal jurisdiction may be near impossible to establish anywhere but the PAE's home state.

In these more difficult cases, lawyers may need to be creative. Suppliers or manufacturers should examine the corporate structure of plaintiff to see if a basis to assert personal jurisdiction outside the customer-suit venue exists. For example, the facts may allow an argument that the parent's contacts should be imputed to its subsidiary under a reverse "alter ego" doctrine. By the same token, patent holders intent on maintaining their choice of forum ought to plan ahead and minimize contacts with forums it perceives to be hostile to its patent rights. In any case, on both fronts, a little foresight can go a long way in saving litigation expense for the client and holding onto a forum of choice.

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[1] 35 U.S.C. § 271.

[2] See *Jumpsport, Inc. v. Lowe's et al.*, 6:17-cv-0606 (E.D. Tex.).

[3] See Brian J. Love & James C. Yoon, *Expanding Patent Law's Customer Suit Exception*, 93 B.U. L. Rev. 1605, 1609–1613 (2013).

[4] See, e.g., *Finjan, Inc. v. Symantec Corp.*, 2017 WL 550453, at *3 (N.D. Cal. Feb. 10, 2017); *Visto Corp. v. Sproqit Techs., Inc.*, 445 F. Supp. 2d 1104, 1108 (N.D. Cal. 2006).

[5] See Love at 1605, 1614.

[6] *In re Nintendo of America, Inc.*, 756 F.3d 1363 (Fed. Cir. 2014).

[7] *In re Dell*, 600 Fed. App'x 728 (Fed. Cir. 2015).

[8] See, e.g., *Autogenomics, Inc. v. Oxford Gene Tech. Ltd.*, 566 F.3d 1012 (Fed. Cir. 2009)

[9] See *Daimler AG v. Bauman*, 134 S. Ct. 746 (2014).

[10] *Genetic Implant Sys., Inc. v. Core-Vent Corp.*, 123 F.3d 1455, 1458 (Fed. Cir. 1997); *Red Wing Shoe Co. v. Hockerson-Halberstadt, Inc.*, 148 F.3d 1355, 1360 (Fed. Cir. 1998)

[11] *Xilinx, Inc. v. Papst Licensing GmbH & Co. KG*, 848 F.3d 1346, 1354 (Fed. Cir. 2017)