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Nike Case Could Spark More IP Validity Challenges

By **Ryan Davis**

Law360, New York (October 31, 2012, 8:53 PM ET) -- A U.S. Supreme Court case set for oral argument next week involving Nike Inc. could require intellectual property plaintiffs to defend the validity of their intellectual property even after agreeing not to sue an accused infringer, eliminating a way to escape validity challenges and forcing IP owners to rethink their litigation strategy, attorneys said.

In the case, slated for argument on Wednesday, Nike sued rival shoemaker Yums LLC over a sneaker trademark, leading Yums to counterclaim that the trademark was invalid. Nike then executed a covenant not to sue Yums that the lower courts ruled deprived them of jurisdiction to hear the validity challenge by resolving the controversy between the parties.

Although this is a trademark case, the high court's ruling would apply equally to patent law, where covenants not to sue aimed at foreclosing validity challenges are more common, said Jedediah Wakefield of Fenwick & West LLP. If the court sides with Yums and holds that accused infringers can challenge validity even after a covenant not to sue, plaintiffs would be faced with the prospect of having to defend the validity of their IP any time they file an infringement action, he said.

"The implication would be that intellectual property plaintiffs would always need to think carefully before filing suit, because the decision to end the litigation may not be theirs in the end," he said. "They couldn't pull the plug if it's not in their interest anymore."

Trademark owners often file suit to police their brand and get the defendant to stop infringing, without any intention of litigating the case to a conclusion, Wakefield noted. An increased risk that suing could lead to the mark being invalidated could make plaintiffs more cautious about filing such suits, he said.

The use of covenants not to sue to shut down invalidity counterclaims is more widespread among patent owners, and that may be the reason the high court took the case, even though it deals with trademarks, according to Uli Widmaier of Pattishall McAuliffe Newbury Hilliard & Geraldson LLP.

"This doesn't happen that often in trademark law," he said. "This is not a normal case, so it's not a huge problem in trademark law that screams out for a solution. It happens much more frequently in patent law."

Companies will often file suit for patent infringement expecting the defendant to roll over and settle, Widmaier said. The Supreme Court may be uncomfortable with the idea that plaintiffs can do that secure in the knowledge that if the defendant fights back and argues that the patent is invalid, the plaintiff can get out of the bind by simply executing a covenant not to sue, he said.

"That may strike some of the justices as overreaching by the plaintiff," he said.

Allowing validity challenges to persist after a covenant not to sue would change the calculus for both plaintiffs and defendants in IP cases, said Donald Falk of Mayer Brown LLP. For plaintiffs, it would discourage settlement, since one of the motivations for rights holders to settle and execute a covenant not to sue is curtail the risk that their rights might be invalidated, he said.

It would also grant defendants the right, once they've been sued for infringement, to have the validity of a patent or trademark determined even if there were no longer an impending suit, Falk noted.

"That would have a fairly significant effect on the balance of power and the balance of incentives between rights holders and potential infringers," he said.

Yums told the Supreme Court that the lower court's ruling that a covenant not to sue deprives the federal courts of jurisdiction over invalidity counterclaims allows trademark owners to effectively obtain "perpetual trademark protection."

Owners of a potentially invalid trademark sue competitors "and then, if unexpected resistance is encountered, deliver a 'covenant not to sue' and evade any prompt or cost-effective test of the validity of the asserted registration," Yums said.

Nike told the court that the ruling "does not mean, as petitioner contends, that trademark holders have a free hand to manipulate the judicial system to prevent cancellation of unlawful registrations," since Yums is free to challenge the validity of Nike's mark by pursuing a cancellation proceeding at the U.S. Patent and Trademark Office.

The question presented in the case is whether there is a "case or controversy" between the parties over the validity of Nike's mark that gives the federal courts jurisdiction to hear it under Article III of the U.S. Constitution.

Nike says the covenant not to sue eliminated any possible controversy, while Yums claims that its interest in keeping Nike's allegedly invalid mark from being used to threaten future litigation is an ongoing controversy that gives the courts jurisdiction.

U.S. Solicitor General Donald Verrilli, who filed an amicus brief in the case representing the government, took a middle position, arguing that the lower court failed to require Nike to prove that its covenant not to sue actually meant that Yums can never be sued over the trademark at issue. He said the Supreme Court should remand the case for further proceedings on whether a controversy still exists and the courts have jurisdiction.

In ruling that Nike's covenant not to sue deprived the courts of jurisdiction over Yums' invalidity claims, the Second Circuit relied on the Supreme Court's 2007 *MedImmune v. Genentech* decision, which held that declaratory judgment plaintiffs must demonstrate a substantial controversy of sufficient immediacy and reality for jurisdiction to exist.

In the Nike case, the court will consider whether it makes sense to use that standard when an accused infringer files a counterclaim seeking declaratory judgment of invalidity, Wakefield said.

"The question is whether the court should craft a different standard for declaratory judgment in that context," he said.

If the court decides that the *MedImmune* standard makes it too easy for plaintiffs to avoid invalidity challenges after a covenant not to sue, it could hold that the standard in that situation should be akin to the rule for showing that a case is moot, Wakefield said.

Under that standard, jurisdiction would exist unless it was "absolutely clear" that the threat posed to the defendant by the plaintiff's trademark or patent could not recur, which would be harder for the plaintiff to meet, he said.

However the court rules, the outcome will be closely watched by trademark and patent owners, Wakefield said.

"I expect the justices to be keenly aware that the outcome here has broad ramifications," he said.

Yums is represented by James Dabney, John Duffy, Victoria J.B. Doyle and Randy Eisensmith of Fried Frank Harris Shriver & Jacobson LLP.

Nike is represented by Thomas C. Goldstein and Kevin K. Russell of Goldstein & Russell PC and Christopher J. Renk, Erik S. Maurer and Audra C. Eidem Heinze of Banner & Witcoff Ltd.

The case is Already LLC, doing business as Yums v. Nike Inc., case number 11-982, in the U.S. Supreme Court.

--Editing by John Quinn.

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