

April 25, 2018

Oil States, SAS Institute, and New Approaches at the U.S. Patent Office

Supreme Court Holds that Challenges to Patent Validity Need Not Proceed Before an Article III Court and Sends More Claims Into Review, While Incoming PTO Director Signals Greater Deference to Existing Patent Rights

SUMMARY

Yesterday the Supreme Court issued two decisions addressing the U.S. Patent and Trademark Office's ("PTO") *inter partes* review ("IPR") proceedings, in which challenged patents can be invalidated through a condensed hearing before an administrative board empaneled by the PTO. The Court's decisions will broaden the mandate of the PTO's Patent Trial and Appeals Board ("PTAB") to review patent validity—a mandate that has already proven controversial since those procedures were created by statute six years ago.

In the long-awaited decision in *Oil States Energy Services, LLC v. Greene's Energy Group, LLC*, 584 U.S. ____ (2018) ("*Oil States*"), the Supreme Court ruled that the Constitution does not require that challenges to patent validity be heard before an Article III court and a jury, and thus upheld the PTAB's power to decide validity challenges in IPR (subject to Federal Circuit review on appeal). In *SAS Institute Inc. v. Iancu*, 584 U.S. ____ (2018) ("*SAS Institute*"), the Court addressed the PTAB's process of instituting IPR on some but not all challenged patent claims, and held that the PTAB's final decision must adjudicate the patentability of *every* patent claim that was challenged in the petition.

In combination, these cases mean that IPR proceedings will continue and may become more extensive. Significantly, the *Oil States* opinion specifically left open the possibility of constitutional challenges to IPR on grounds other than Article III and the Seventh Amendment, and both decisions have implications for several strategic decisions made by parties to IPR proceedings (discussed below).

SULLIVAN & CROMWELL LLP

While these decisions by the Supreme Court affirmed the constitutionality of IPR and arguably expanded the PTAB's mandate, the newly appointed Director of the PTO, Andrei Iancu, recently indicated that the PTO may undertake rulemaking to reduce the frequency with which issued patents are held invalid and otherwise address issues raised by patentees about the IPR process.

DISCUSSION

In *Oil States*, Justice Thomas began the analysis for the seven-Justice majority by noting that the constitutional separation of powers requires Article III courts to adjudicate “private” rights but not necessarily “public” rights. The Court noted earlier decisions confirming that Congress had considerable latitude to assign adjudication of “public rights” to non-Article III courts.¹ Justice Thomas next observed that the parties did not dispute that the original *grant* of a patent was “the grant of a public franchise” and that “reconsideration of the Government’s decision to grant a public franchise” thus “falls squarely within the public rights doctrine” and can be assigned to a non-Article III court without violating the separation of powers.² For the same reason, the Court held that the Seventh Amendment’s guarantee of trial by jury did not apply to an adjudication that was properly “assign[ed]” to a non-Article III tribunal.³

Significantly, the majority opinion went out of its way to “emphasize the narrowness of [its] holding.” The Court noted that its opinion was limited to validity challenges, and not whether infringement questions also “can be heard in a non-Article III forum” (such as another executive agency, the International Trade Commission, that adjudicates infringement).⁴ The Court also noted that it had addressed only the Article III and Seventh Amendment issues—not challenges to IPR on any other constitutional grounds, such as whether the patent property right is subject to due process guarantees or the Takings Clause, whether IPR procedures comported with due process, or whether retroactive application of IPR to patents issued before that procedure’s enactment was permissible.⁵

In the other opinion issued the same day, *SAS Institute*, the Court explained that the IPR process proceeds in two phases: a petition to “institute” an IPR proceeding, which is followed (if granted) by a trial on the merits that includes “many of the usual trappings of litigation.”⁶ To clear the first hurdle, a party must establish in a petition to the PTO a “reasonable likelihood” that at least one claim of an issued patent is invalid because another person had previously disclosed either the same invention or enough of the invention to render it obvious.⁷

SAS Institute filed a petition to institute IPR, challenging all 16 claims of a software patent held by ComplementSoft. The PTO found a reasonable likelihood that SAS would prevail as to nine of the 16 challenged claims, and declined to review the remaining seven. The PTAB then proceeded with the second phase of review—a mini-trial on the merits of the nine “instituted” claims—and, in its final decision, held nearly all of the nine reviewed claims unpatentable. SAS appealed to the Federal Circuit, arguing that once SAS had cleared the first hurdle as to any claim, then at the second phase, the plain statutory language of 35 U.S.C. § 318(a) required the Board to decide the patentability of every claim SAS had

SULLIVAN & CROMWELL LLP

challenged in its original petition. The Federal Circuit sided with the PTAB, and held that limited review was permissible under the statute.⁸

In a five-to-four decision written by Justice Gorsuch, the Court reversed. Focusing on the plain language of § 318(a), the Court wrote that “when [the statute] says the Board’s final written decision ‘shall’ resolve the patentability of ‘any patent claim challenged by the petitioner,’ it means the Board *must* address *every* claim the petitioner has challenged.”⁹ Because the majority found the statute unambiguous, it did not give the PTO’s statutory interpretation any administrative-agency deference under the *Chevron* doctrine.¹⁰ Likewise, the Court rejected the PTO’s policy arguments favoring a more limited scope of IPR trials, writing that “[p]olicy arguments are properly addressed to Congress, not this Court.”¹¹

THE PTO’S APPROACH TO INTELLECTUAL PROPERTY PROTECTION

Director Iancu’s Recent Statements

To fully understand the current IPR environment, the Court’s two decisions should be considered together with recent comments about IPR by the newly appointed Director of the PTO, Andrei Iancu. He has forcefully and publicly indicated, including before Congress, that he intends to re-order the agency’s priorities and to take a hard look at whether the IPR process is currently fair to patentees. For example, in remarks at the U.S. Chamber of Commerce Patent Policy Conference on April 11, 2018, Iancu singled out “patent opposition procedures” such as IPR proceedings as a key reason “why our patent system has dropped” compared to other systems worldwide.¹² Iancu similarly recognized that “the patent grant is less reliable today than it should be,” noting that IPRs “can come years after issuance, when the patent owners and the public may both have relied on those rights and made investments accordingly.”¹³ Thus, he emphasized a “need to carefully balance rights-holder’s and rights challenger’s interests,” and not “to throw out the baby with the bathwater.”¹⁴

Commentators have been predicting a more pro-patent approach from Iancu, and his recent testimony before the Senate Judiciary Committee elaborated on how he might deliver: “Some of the issues we are currently studying include the institution decision, claim construction, the amendment process, and the conduct of hearings.”¹⁵ He also testified that the PTAB was also reviewing several operating procedures, including “the paneling of judges to cases, expansion of panels, preparation of decisions, amicus briefing, joinder, and rehearing requests.”¹⁶

In particular, one possible rule change the PTO is likely considering is whether to stop using the “broadest reasonable interpretation” (“BRI”) claim construction standard to adjudicate whether claims are invalid. Use of the BRI standard, which the Supreme Court upheld in *Cuozzo Speed Technologies, LLC v. Lee*, 579 U.S. ___, 136 S. Ct. 2131 (2016), is widely seen to favor patent challengers because the BRI standard is broader than the construction standard employed by the district courts, thereby making relevant a broader array of prior art that can be used to invalidate claims. A change in the claim

construction standard and other procedures apparently under review by the PTO may profoundly change the way IPR proceedings fit into a patent litigation strategy.

IMPLICATIONS

The Supreme Court's decisions in *Oil States* ensures that IPR proceedings will continue, while the Court's decision in *SAS Institute* means the scope of PTAB decisions will actually broaden. For those involved in IPR, the decisions have several implications.

First, patentees should continue to preserve objections to the constitutionality of the IPR process on multiple grounds other than a claim that the process violates Article III's separation of powers.

Second, the determination in *Oil States* that patent rights are public rights may also lend credence to public policy arguments in patent litigation—not only before the PTAB, but also before the federal district courts. For example, whether a court should enter an injunction on an infringed patent that is essential to an industry standard has received considerable attention in the courts, by commentators, and by government agencies worldwide. It may very well be that policy considerations will play a more prominent role in that and other patent-related determinations in light of the Court's *Oil States* decision.

As for *SAS Institute*—which one study indicated would only implicate approximately 15% of cases before the PTAB—one likely result is that IPR challenges will become more costly and time-consuming for the parties as well as the Board. The requirement to address all challenged claims in the second trial phase may also lead more district courts to stay infringement cases pending IPR. The stay standard relies largely on whether the IPR will simplify the court proceeding, and an IPR that must adjudicate the validity of all challenged claims may very well be deemed more likely to simplify the federal court case. Similarly, the Court's decision is likely to reduce piecemeal litigation. While an IPR petitioner in the past may have sought to raise some claim challenges in IPR and others in district court, that strategy will be far less attractive.

SAS Institute also has significant strategic implications for patentees that previously hoped to avoid institution of IPR of a patent's dependent claims on grounds that did not apply equally to the independent claims. This strategy will no longer make sense, and oppositions to IPR institution will focus on grounds common to all challenged claims.

SAS Institute also has implications for estoppel. If a petitioner in an IPR “that results in a final written decision” is also accused of infringement in district court, that petitioner is estopped in the district court from asserting prior art that the petitioner “raised or reasonably could have raised during that inter partes review.”¹⁷ That estoppel typically did not apply to challenged claims for which the PTAB had declined to institute IPR in the first phase of its review. But now that the PTAB cannot limit IPR to only a subset of the challenged claims, every instituted IPR proceeding will result in a “final written decision” on every challenged claim, and consequently petitioners may face broader estoppel. In other words, petitioners in

SULLIVAN & CROMWELL LLP

IPR now face greater risk when combining challenges that may be less likely to succeed with others that are more likely to proceed to the trial phase. While previously, challenges that failed at the first phase of IPR would not cause estoppel, after *SAS Institute*, such challenges will still reach the second phase and will likely lead to statutory estoppel in the district court. Petitioners should therefore be well aware of the greater risk they take to challenge claims on grounds the PTAB might previously have found simply unworthy of review.

In the more than five years since its enactment, IPR has invalidated tens of thousands of claims, created additional litigation, and caused many to debate whether IPR has a positive or negative impact on our patent system. Recent developments suggest that IPR will continue to be a focus of challenges to patent validity, and that the process is very likely to undergo significant revisions.

* * *

ENDNOTES

- 1 *Oil States*, slip op. at 6.
- 2 *Id.* at 6-7.
- 3 *Id.* at 17.
- 4 *Id.* at 16-17.
- 5 *Id.* at 16-17.
- 6 *SAS Institute*, slip op. at 3.
- 7 *Id.*
- 8 *See id.* at 4.
- 9 *Id.* at 5 (emphases in original).
- 10 *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U. S. 837 (1984).
- 11 *SAS Institute*, slip op. at 10.
- 12 Director of the U.S. PTO Andre Iancu, Keynote Address, ““Role of U.S. Patent Policy in Domestic Innovation and Potential Impacts on Investment,” April 11, 2018, *available at* <https://www.uspto.gov/about-us/news-updates/remarks-director-andrei-iancu-us-chamber-commerce-patent-policy-conference>.
- 13 *Id.*
- 14 *Id.*
- 15 Stmt. of Andrei Iancu, Under Secretary of Commerce for Intellectual Property and Director of the United States Patent and Trademark Office, Senate Judiciary Committee (Apr. 18, 2018), at 5, *available at* <https://www.judiciary.senate.gov/imo/media/doc/04-18-18%20Iancu%20Testimony.pdf>.
- 16 *Id.*
- 17 35 U.S.C. § 315(e)(2).

SULLIVAN & CROMWELL LLP

ABOUT SULLIVAN & CROMWELL LLP

Sullivan & Cromwell LLP is a global law firm that advises on major domestic and cross-border M&A, finance, corporate and real estate transactions, significant litigation and corporate investigations, and complex restructuring, regulatory, tax and estate planning matters. Founded in 1879, Sullivan & Cromwell LLP has more than 875 lawyers on four continents, with four offices in the United States, including its headquarters in New York, four offices in Europe, two in Australia and three in Asia.

CONTACTING SULLIVAN & CROMWELL LLP

This publication is provided by Sullivan & Cromwell LLP as a service to clients and colleagues. The information contained in this publication should not be construed as legal advice. Questions regarding the matters discussed in this publication may be directed to any of our lawyers listed below, or to any other Sullivan & Cromwell LLP lawyer with whom you have consulted in the past on similar matters. If you have not received this publication directly from us, you may obtain a copy of any past or future publications by sending an e-mail to SCPublications@sullcrom.com.

CONTACTS

New York

Mehdi Ansari	+1-212-558-4314	ansarim@sullcrom.com
Garrard R. Beeney	+1-212-558-3737	beeneyg@sullcrom.com
John Evangelakos	+1-212-558-4260	evangelakosj@sullcrom.com
Marc De Leeuw	+1-212-558-4219	deleeuwm@sullcrom.com
Adam R. Brebner	+1-212-558-3011	brebnera@sullcrom.com
Stephen J. Elliott	+1-212-558-7446	elliotts@sullcrom.com
Rudy Kleysteuber	+1-212-558-7226	kleysteuberr@sullcrom.com
James T. Williams	+1-212-558-3130	williamsj@sullcrom.com

Washington, D.C.

Renata B. Hesse	+1-202-956-7575	hesser@sullcrom.com
-----------------	-----------------	--

Palo Alto

Nader A. Mousavi	+1-650-461-5660	mousavin@sullcrom.com
Laura Kabler Oswell	+1-650-461-5679	oswell@sullcrom.com
