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SanDisk Corporation v. STMicroElectronics, Inc.: The Federal Circuit Expands the Availability of Declaratory Judgment Actions in the Patent Licensing Context

The approach to patent licensing negotiations has always been a delicate one. In the past, if a patentee sought to license its patents, it could offer a license without threatening to sue and could avoid the risk of being exposed to a declaratory judgment action by the potential licensees. The Federal Circuit's recent decision in SanDisk Corporation v. STMicroElectronics, Docket No. 05-1300 (Fed. Cir. March 26, 2007), has dramatically changed the backdrop against which patent licensing negotiations will occur by removing this safe haven for patentees.

The SanDisk case involved two companies in the flash memory storage market, SanDisk Corporation and STMicroelectronics, that engaged in discussions over several months regarding the possibility of a patent cross-licensing arrangement. ST aggressively pursued its licensing agenda but explicitly told SanDisk it had no plan to sue the company. At a licensing meeting, ST experts presented a detailed infringement analysis and gave SanDisk a voluminous packet of materials pertaining to this analysis. SanDisk, for its part, maintained that it could continue its conduct without paying royalties to ST. In an opinion by Judge Linn, concurred in by Judge Dyk, the Federal Circuit held that these facts were sufficient to create a controversy between the parties having adverse legal interests that was of sufficient immediacy and reality to create declaratory judgment jurisdiction. Slip Op. at 17. This holding sharply departs from prior case law.

Prior to the SanDisk case, the Federal Circuit in Arrowhead Indus. Water, Inc. v. Ecolochem, Inc., 846 F.2d 731, 736 (Fed. Cir. 1988), had recognized a two-part test for determining whether a patentee's licensing activities might permit a DJ action. The first step involved determining whether a patentee's actions created "a reasonable apprehension" on the part of the potential licensee that, in the absence of a license agreement, it would face an infringement suit. The second step considered whether the conduct of the potential licensee amounts to an infringing activity or whether concrete steps have been taken in preparation to pursue such activity. Before *SanDisk*, the case law was clear that an invitation to enter into licensing discussions -- without a threat to file a lawsuit -- did not suffice to create DJ jurisdiction. *See* Phillips Plastics Corp. v. Kato Hatsu-Jou Kabushiki Kaisha, 57 F.3d 1051 (Fed. Cir. 1995).

The Court's departure from the Arrowhead test follows in the wake of MedImmune, Inc. v. Genentech, Inc., 127 S. Ct. 764 (2007), in which the Supreme Court rejected the reasonable apprehension of suit test. *See* 127 S.Ct. at 774 n. 11. Slip. Op. at 14. In view of MedImmune, the Federal Circuit held that "declaratory judgment jurisdiction generally will not arise merely on the basis that a party learns of the existence of a patent owned by another or even perceives such a patent to pose a risk of infringement, without some affirmative act by the patentee." Slip. Op. at 14. DJ jurisdiction is created, however, "where the patentee takes a position that puts the declaratory judgment plaintiff in the position of either pursuing arguably illegal behavior or abandoning that which he claims a right to do." Slip Op. at 14. In other words, the Court held that "where a patentee asserts rights under a patent based on certain identified ongoing or planned activity of another party, and where that party contends that it has the right to engage in the accused activity without license, an Article III case or controversy will

arise and the party need not risk a suit for infringement by engaging in the identified activity before seeking a declaration of its legal rights." (Slip Op. at 15.)

The Court was not swayed by ST's express assertion that it did not intend to sue SanDisk. Further the Court indicated that the District Court erred in exercising its inherent discretion not to hear the declaratory judgment action, which could have resolved an actual controversy.

Notwithstanding this "sweeping" decision, there may be one remaining safe harbor -- at least for the moment. *See* Bryson J. opinion, Slip Op. at 5 (court's decision "will effect a sweeping change in our law regarding declaratory judgment jurisdiction"). In a first footnote, underscored by Judge Bryson's concurring opinion, the panel noted that ST could have avoided the risk of a DJ action by entering into a suitable confidentiality agreement with SanDisk (as opposed to pursuing the licensing negotiation under the guise of Federal Rule of Evidence 408 relating to settlement discussions). In a second footnote, the Court specifically noted that its opinion addresses only the first prong of the Arrowhead reasonable apprehension of suit test and declined to comment on the second prong of the test directed to the activities of the potential licensee.

The SanDisk case leads to a stronger negotiating position for a potential patent licensee and will require careful strategic planning on the part of the patent owner and licensor before pursuing patent licensing efforts. Such strategic planning should include a litigation strategy. A patent holder should be prepared to defend a declaratory judgment action in a forum selected by an accused infringer before inviting and undertaking licensing negotiations.

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