

Takeaways From HTC's Fees Win, 'Pierce The Veil' Loss

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A Chicago federal judge ordered Intellect Wireless Inc. ("IW") to pay over \$4 million in legal costs and interest to HTC Corp. last month, after finding that IW and its founder Daniel Henderson sought to deceive the U.S. Patent and Trademark Office by submitting false statements during prosecution of their patents, rendering those patents unenforceable due to inequitable conduct.[1] But the case was not a complete win for HTC, which was unable to hold Henderson personally liable for the expenses associated with the suit, obtaining judgment only against IW and IW's former attorneys.

HTC had pursued individual liability from Henderson because (HTC alleged) he formed IW as a shell corporation, siphoning IW's profits into his personal bank accounts, and because IW represented to HTC that its assets would be unable to satisfy any portion of HTC's attorneys' fees and costs. These developments call into question the realizable value of the fee award for HTC.

Defendants considering potential inequitable conduct defenses to patent infringement lawsuits would do well to learn from HTC's example. This article will suggest steps to increase a prevailing patent infringement defendant's chances of realizing large fee awards where the plaintiff is suspected to have sheltered its assets by paying them out to a primary owner or executive's personal account, as IW may have done.

How Defendants Typically Obtain Fees in Patent Infringement Suits

35 U.S.C. § 285 makes the prevailing party in patent cases eligible to seek an award of attorneys' fees in "exceptional cases." Informed by the U.S. Supreme Court's decision in *Octane Fitness LLC v. ICON Health & Fitness Inc.*, district courts have discretion to determine, in light of the totality of the circumstances, whether a case is "exceptional," that is, whether it "stands out from others with respect to the substantive strength of a party's litigating position (considering both the governing law and the facts of the case) or the unreasonable manner in which the case was litigated." [2] Inequitable conduct, subjective bad faith, pursuing exceptionally meritless claims, litigation misconduct, or other case-specific circumstances can result in an award of fees under the "exceptional case" standard.



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If, as in HTC's case, inequitable conduct forms part of the basis for the fee motion, the inequitable conduct defense and counterclaim must be timely included in the defendant's answer, or leave must be sought to later amend.[3] A party wishing to seek fees under § 285 would then typically file a motion for fees in the district court setting forth all the facts and circumstances warranting a fee award. Renewed and supplemental motions may be necessary as facts and circumstances unfold (as occurred in the HTC litigation).

What Went Wrong for HTC?

HTC filed its first countercomplaint in 2009. It did not name Henderson as a counter defendant.[4] HTC's first motion for fees, filed in December 2010, described facts including Henderson's false statements, under oath, to the PTO, as well as a number of other relevant facts bearing on the request for fees. Yet that motion sought fees from only IW and IW's counsel, and again did not seek a finding that Henderson himself was personally liable.[5] When HTC renewed its motion for fees in November 2013, it again failed to seek a finding against Henderson. IW ultimately conceded liability, and in January 2015, IW's counsel was also found liable for the fees.

It was not until HTC filed an April 30, 2015, motion for judgment that HTC sought to pierce IW's corporate veil and hold Henderson personally liable for the fee award.[6] HTC alleged that Henderson formed IW as a shell corporation to enforce his fraudulently obtained patents, and siphoned 98 percent of the profits of settlements obtained from IW's lawsuits into his own personal bank accounts.[7] Yet the district court declined to consider whether Henderson should be held personally liable, because of HTC's delay in seeking judgment against him.[8]

As HTC has discovered, a party seeking to assert counterclaims against a nonparty individual owner or officer of a defendant company (a process known as "piercing the corporate veil") must show that the court has personal jurisdiction over the absent defendant under an "alter ego" theory.[9] Federal Rule of Civil Procedure 15 sets out the requirements for amended and supplemental pleadings; Rule 15(c) permits adding a defendant through amendment if certain circumstances are met. These include that the claim must have arisen out of the conduct set forth in the original pleading, the party to be joined must have received such notice that it will not be prejudiced in maintaining its defense, and that party must or should have known that, but for a mistake concerning identity, the action would have been brought against it.[10] Rule 15(c) motions can be granted post-trial.[11] However, the Supreme Court has warned that strict compliance with Rule 15(c) is necessary to protect the joined defendant's due process rights.[12]

The court declined to consider adding an additional party in response to HTC's April 2015 motion for judgment, filed nearly three years after judgment was entered dismissing the case, commenting that a post-judgment, ancillary proceeding is an inappropriate proceeding on which to base supplemental jurisdiction.[13]

Lessons Learned

Defendants in patent infringement cases, especially where the case is asserted by a patent assertion (or "nonpracticing") entity, should keep in mind the possibility that the plaintiff may have sheltered many of its assets from collection by paying the assets out to its owners' or executives' personal bank accounts. Such a corporate structure potentially decreases the realizable value of the fee award.

To mitigate this risk, as a defendant becomes aware of inequitable conduct counterclaims and of the

possibility of an “exceptional case” fee award, it should keep in mind the importance federal courts place on protecting the absent defendant’s due process rights, including through enforcing Rule 15(c)’s requirements. The HTC ruling demonstrates that due process considerations can outweigh or even preempt the court’s consideration of whether to pierce the veil and find individual liability, even where the facts seem to strongly support individual liability.

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[1] Intellect Wireless Inc. v. HTC Corp., et al., No. 1:09-cv-02945, Dkt. 374 (N.D. Ill. July 21, 2015).

[2] 134 S. Ct. 1749, 1756 (2014).

[3] See, e.g., No. 1:09-cv-02945, Dkt. 101, filed Dec. 1, 2010 (HTC first motion for fees).

[4] Dkt. 374 at 3.

[5] Dkt. 101 at 4, 6; see also Dkt. 374 at 2 (discussing renewed motion filed on Nov. 22, 2013).

[6] Dkt. 363 (Apr. 30, 2015 Motion for Judgment).

[7] Id. at 2.

[8] Dkt. 374 at 4-5.

[9] The “alter ego” theory of liability is governed by state law. It is unclear whether federal common law, rather than state law, applies to veil-piercing cases brought under federal statutes. *Bowoto v. Chevron Texaco Corp.*, 312 F. Supp. 2d 1229, 1236 (N.D. Cal. 2004) (citing *United States v. Bestfoods*, 524 U.S. 51, 63 n.9 (1998)).

[10] *Fromson v. Citiplate Inc.*, 886 F.2d 1300, 1303 (Fed. Cir. 1989). These conditions must be met within the prescribe limitations period, as well. Id.

[11] See, e.g., id. at 1303-04.

[12] *Nelson v. Adams USA Inc.*, 529 U.S. 460, 468 (2000) (approving *Fromson* but reversing a similar 15(c) amendment because the joined defendant had no opportunity to respond to the 15(c) motion).

[13] Dkt. 374 at 4-5.