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Oral Arguments in Kimble v. Marvel: *What Does Your Spidey Sense Tell You About the Court's Questioning and What It Will Mean for the Royalty Term in Your Patent License Agreement?*

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The dispute in *Kimble v. Marvel* concerns whether Marvel (the long time comic book publisher and now blockbuster movie producer) must continue paying royalties for sales of a toy no longer protected by a patent. The toy allows users to shoot silly string from their hand like Spider Man shoots a web. (Other than being *awesome*, and inspiring the title of this article, the toy, unfortunately, has nothing to do with the case.) The royalty term set forth in the relevant agreement did not set an end date, but Marvel ceased payments after the patent expired, in reliance on the Supreme Court precedent of *Brulotte v. Thys Co.*[1] In *Brulotte*, the Supreme Court created a *per se* rule against royalty payments for use of a patent after the patent term's expiration. Kimble commenced the action seeking recovery of royalty payments but lost in the District Court of Arizona and the Ninth Circuit, which both followed *Brulotte*. Thus, the question presented to the Supreme Court is whether to overrule *Brulotte's* prohibition against royalties beyond patent expiration. Oral arguments were heard on March 31, 2015.

Arguments by the Parties in the Case

Stephen Kimble (the Petitioner and inventor of the Spider Man toy), asserting that *Brulotte* should be reversed, relied on three primary arguments: (1) *Brulotte* was wrongly decided; (2) extending royalty payments does not extend patent rights because other parties can use an expired patent for free, even if licensees cannot; and (3) allowing parties to contract for longer terms is efficient economically because lower rates/costs to licensees over longer periods can increase innovation and output. According to Kimble, the Court should replace the *per se* rule of *Brulotte* with a "rule of reason" requiring the licensee to show that the patent owner has market power and is acting unreasonably or coercively to restrain competition.

Marvel (the Respondent) argued that the Court should uphold its 1964 decision in *Brulotte* under the principle of *stare decisis*. Marvel insisted that Congress, not the Court, is the appropriate branch of government to overrule the simple, clarity-providing, 50-year-old rule of *Brulotte*.

The Court's Response

During Kimble's argument, several Justices appeared to agree with Marvel's position that this is an issue for Congress, with *stare decisis* requiring a greater showing for overruling *Brulotte* than Kimble may have made here. Justice Kagan, in particular, challenged Kimble's attorney to identify concrete examples evidencing the "special justification" required for reversing *Brulotte*. According to Justice Kagan, regardless of whether or not *Brulotte* is "right," more is required for a "special justification" A petitioner seeking to have the Court reverse a Supreme Court decision must show that the decision is unworkable, "a relic of a past system that is utterly out of kilter … [*Brulotte*] may or may not be right, but there's nothing incredibly sort of weird—and anomalous about it."

Certain Justices also questioned the value or need for applying a "rule of reason" to these circumstances. Remarking on the rule of reason's attendant complexity and lack of certainty, Justice Breyer extolled the virtues of *Brulotte's* simplicity and observed that—in spite of their criticism of *Brulotte*—no economists considered the cost of judicial administration in their analyses. Similarly, Justice Sotomayor doubted the need for "importing" an antitrust principle into a specific patent royalty situation when antitrust principles would apply in problematic cases anyway. In other words, situations in which a patent owner truly has and abuses market power to misuse its patent represent antitrust violations. Thus, no special rationale for requiring application of the rule of reason exists.

During its argument, Marvel contended that reversing *Brulotte* would upset the many people who entered into license agreements over the past 50 years in reliance on *Brulotte*. None of the Justices appeared particularly concerned with this line of reasoning. Justices Scalia and Sotomayor each expressed the sentiment that the only people whose reliance interest would be upset are those who entered into contracts with license terms beyond the date of patent expiration, knowing they would stop paying the licensor earlier than they said they would in their contracts. Needless to say, the Court was not sympathetic to such parties.

Other than the questioning on the issue of reliance, however, Marvel's argument was largely a conversation with Chief Justice Roberts only. The Chief Justice appeared to express the most enthusiasm for the economic bases proffered by Kimble for overruling *Brulotte*, noting, for example, that "economists are almost unanimous that this is a very bad rule." Justice Roberts mentioned on several occasions (including during Kimble's argument) that new parties could enter the market without paying royalties after patent expiry. To that end, Justice Roberts appeared to like the idea of having some parties contractually bound to patent owners after the patent term because it would provide an incentive to new parties to enter the market. According to Justice Roberts, new market participants—unburdened by the cost of paying royalties—could enter the market at a lower price point. Marvel's counsel responded to Justice Roberts by referencing an earlier point made (during Kimble's oral argument) by Justice Breyer. Justice Breyer's point was that, practically speaking, there are no more market participants; all parties capable of using the patent in the market already started during the patent term under a license arrangement. Justice Roberts' retort, however, was that the rule of reason could be used to properly address such situations.

Roberts also appeared to buy Kimble's (and economists') argument that *Brulotte* suppresses innovation by preventing parties from amortizing the cost of development by extending royalty payments past patent expiration. Here, Marvel directed the Chief Justice back to the rationale for *stare decisis* and the ability of Congress to act. Specifically, Marvel pointed to the Hatch-Waxman Act as an example. There, in the pharmaceutical context, people were concerned that patent life was being consumed during the examination period. Congress acted by setting up a series of patent term adjustments to compensate for the problem. According to Marvel, the Hatch-Waxman Act, combined with many other instances of congressional recalibration of the patent laws over the last half century, provides strong evidence that overruling *Brulotte* is for Congress, not the Court.

What Does It All Mean for Patent License Agreements?

Having been given the run-down of the Justices lines of questioning, what does your Spidey sense tell you about how the Court will decide this case? While we do not pretend to know, we can offer some insight on what a decision either way will mean for existing licensing agreements with post patent expiration terms.

If *Brulotte* is upheld, provisions that purport to require royalty payments for *use* of the patent beyond the patent's expiration will not be enforceable. Even under *Brulotte*, though, agreements requiring payments after patent expiration are enforceable, provided the payment is for use that occurred *before* expiration. Drafting agreements along these lines should make explicitly clear that any royalty payments to be made post expiration are for pre-expiration use only. Also, when the license is for a product containing both patented and non-patented technology, royalties for the non-patented aspects may continue to be required post patent expiration. The key is discounting royalty payments after expiration, thus, clearly separating post expiration, non-patent related payments from those made for using the patent. Finally, in agreements that license a portfolio of patents, other, non-*Brulotte* precedent allows the parties to require royalty payments for sales, regardless of whether the patent is used in the products sold. In these cases, it would appear that requiring payments beyond expiration of one or more of the patents in the portfolio would be permissible.

If *Brulotte* is overruled, it is not clear what new rule the Court would offer as a replacement. Possible options include adoption of: (1) the Petitioner's proposed rule of reason approach; (2) Respondent's fallback argument that if *Brulotte* is overruled, whatever a new rule looks like, it, at a minimum, should (a) start with a presumption against validity and (b) require that allowing post-expiration royalty payments comports with the patent policy of promoting innovation; or (3) adoption of an entirely different rule altogether.

Finally, to quote the famous words of Spiderman's late Uncle Ben, "with great power, comes great responsibility." We are sure the Supreme Court will use its great power to decide this case fairly, and we look forward to their decision in this "sticky" situation.

1. Brulotte v. Thys Co., 379 U.S. 29 (1964).