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Introduction

Courts have uniformly barred patent holders producing goods through subsidiaries from claiming their full amount of lost profits due to patent infringement. The court in *St. Jude Medical, Inc. v. Access Closure, Inc.* was the first—and currently the only—court to allow a parent corporation to seek damages based on its subsidiaries' lost profits.[1]

Though the patent statute entitles patentees to adequate compensation for infringement,[2] courts usually limit parent corporations' damages to a reasonable royalty rate, not compensation based on their real injuries.[3] This limitation is due to the patent holder's corporate structure.[4] Corporations often produce goods through subsidiaries that they wholly own—usually for efficiency and tax benefits.[5] This remedy issue arises when someone infringes on a patent that is held by a parent corporation, but its subsidiaries, not the parent corporation, lose sales due to infringement. In this situation, subsidiary companies are normally unable to claim any damages; because they do not have substantial rights to the patents, the subsidiaries lack standing to join the infringement suit.[6] Further the parent corporation, by selling through its subsidiaries, is not itself selling a product, so "by definition there can be no lost profits."[7] As a result, patent-holding parent corporations also cannot normally claim any damages related to their subsidiaries' lost sales.[8]

Recently, however, courts have acknowledged the close relationship between parent corporations and their subsidiaries, but have struggled to find a

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1. No. 08-CV-4101, 2010 WL 4968147, at *6 (W.D. Ark. Dec. 1, 2010) (mem. op.).

2. 35 U.S.C. § 284 (2012).

3. Robert A. Matthews, Jr., *Legal Nuances When a Patent-Holding Company Seeks to Enforce a U.S. Patent*, 49 IDEA 549, 552–57 (2009); Bryce Young, Note, *Recovering Lost Profits: The Resurrection of Subsidiaries (Is There Life on Mars?)*, 8 U. St. Thomas L.J. 275, 277-78 (2011).

4. Young, *supra* note 3, at 281.

5. *Id.* at 277–78.

6. Morrow v. Microsoft Corp., 499 F.3d 1332, 1338–40 (Fed. Cir. 2007).

7. Rite-Hite Corp. v. Kelley Co., 56 F.3d 1538, 1548 (Fed. Cir. 1995).

8. Poly-America, L.P. v. GSE Lining Tech., Inc., 383 F.3d 1303, 1311 (Fed. Cir. 2004) ("[T]he patentee needs to have been selling some item, the profits of which have been lost due to infringing sales, in order to claim damages consisting of lost profits.").

way to take this into account.[9] *St. Jude Medical* advances these judicial sympathies by proposing a new remedy outside of the two traditional categories of compensation: reasonable royalty rate or pure lost profits.[10] There, St. Jude claimed that "the decrease in its own market value [was] due to the lost sales of its wholly-owned subsidiaries."[11] These damages step away from recovery based solely on the patent's license agreements, and they instead reflect corporate structure agreements. Thus, by taking a fresh look at remedy considerations, *St. Jude Medical* allows corporate patent holders to seek more realistic compensation for their actual, total injuries.

St. Jude Medical is a victory for corporate patentees. It proposes unique damages that may allow more realistic compensation. More importantly, however, *St. Jude Medical* exemplifies the new judicial trend acknowledging parent-subsidiary corporate structures and begins a dialogue of corporate remedy.

Factual Background

Plaintiff St. Jude Medical, Inc. (St. Jude), a provider of medical technology, developed the vascular closure devices at issue in this case.[12] Defendant Access Closure, Inc. (Access Closure), also manufactures vascular closure devices, including the allegedly infringing Mynx Vascular Closure Device (the Mynx).[13] These products involve technology "used to close blood vessels following catheterization procedures."[14]

Catheterization is a process of inserting a device into a blood vessel.[15] The example given by the court was an angioplasty, a procedure in which a blocked artery is treated by inserting a balloon-like device into the femoral artery and expanding it near the clogged artery.[16] Removing the catheterization device leaves a hole in the blood vessel, which was previously treated by applying physical pressure on the skin over the opening in the artery to prevent bleeding.[17] Because this practice is slow and uncomfortable, "[t]he pat-

9. *See* Union Carbide Chems. & Plastics Tech. Corp. v. Shell Oil Co., 425 F.3d 1366, 1378 (Fed. Cir. 2005) (allowing the jury to consider the patent holder's subsidiary when determining a reasonable royalty rate).

10. *St. Jude Med.*, 2010 WL 4968147, at *6.

11. *Id.*

12. *Id.* at *1.

13. *Id.*

14. *Id.*

15. *Id.*

16. *St. Jude Med.*, 2010 WL 4968147, at *6.

17. *Id.* at *1.

ents at issue in this case describe devices and methods intended to" seal the hole in the blood vessel more quickly and comfortably.[18]

St. Jude held two patent families relevant to the case: the '616 patent, the '602 patent, and the '375 patent (referred to as the "Fowler patents"); and the '498 patent and the '439 patent (together called the "Janzen patents").[19] The Fowler patents, named after their inventor Bradford Fowler, pertain to the method and assembly of inserting the device into the patient's body.[20] The Janzen patents, on the other hand, were invented by Ernst Janzen and describe the device and method of sealing puncture wounds.[21]

The court in this case did not examine St. Jude's damage claims based on the Fowler patents, so their disposal was irrelevant to the issue of lost profits.[22] Additionally, all claims regarding the '498 patent were dropped.[23] Thus, only the '439 patent was relevant.[24]

St. Jude was the patent-holding parent company of the '439 patent, but it "d[oes] not manufacture or sell any products with which the allegedly infringing products compete."[25] Instead, St. Jude wholly owned three manufacturing subsidiaries that had potentially lost sales due to infringement of the '439 patent.[26]

Procedural and Substantive History

St. Jude filed suit against Access Closure in October 2008, alleging that Access Closure's involvement with the Mynx "has and is infringing, contributorily infringing, and inducing the infringement" of St. Jude's patents.[27] Access Closure responded by "denying the allegations, raising twelve affirmative defenses, and asserting eleven counterclaims" against St. Jude.[28] This opinion was issued in response to the subsequent motions for summary judgment filed by both parties.[29] Though a jury verdict later was in favor of

18. *Id.*

19. *Id.* at *1–2.

20. *Id.* at *1.

21. *Id.* at *2.

22. *St. Jude Med.*, 2010 WL 4968147, at *5–6.

23. *Id.* at *2 n.3.

24. *Id.* at *5–6.

25. *Id.* at *5.

26. *Id.*

27. *Id.* at *2.

28. *St. Jude Med.*, 2010 WL 4968147, at *2.

29. *Id.*

St. Jude, the court has stayed determining damages related to the '439 patent until Access Closure's appeal is resolved.[30]

Description of the Claim

Access Closure argued in its motion for summary judgment that "St. Jude cannot collect lost profit damages because the owner of the '439 patent (St. Jude Medical, Inc.) does not manufacture or sell any products with which the allegedly infringing products compete."[31]

In response to Access Closure's assertion, St. Jude stated "that it [wa]s not seeking to recover lost profit damages, but rather the decrease in its own market value due to the lost sales of its wholly-owned subsidiaries."[32] Thus, St. Jude claimed that Access Closure's argument was moot because no lost profits were sought: St. Jude was only attempting to recover the lost "value of its ownership interest in its subsidiaries."[33] Access Closure responded, stating: "St. Jude's proposed theory is nothing more than a relabeling of the unavailable lost profits damages," because "the mechanics of the 'lost profits' calculation are essentially identical to the 'reduction in income' calculations."[34] Unfortunately, the exact calculations claimed by St. Jude are unknown because all motions related to this opinion are sealed and the court's determination of damages is stayed pending Access Closure's appeal.[35]

District Court's Holding and Overview of Rationale

The United States District Court for the Western District of Arkansas held that St. Jude could potentially recover on its reduction in income theory.[36] The court noted that, although "St. Jude [could not] recover damages

30. Judgment at 1–2, *St. Jude Med.*, No. 08-4101, 2010 WL 4968147 (W.D. Ark. Jan. 23, 2012), ECF No. 308.

31. *St. Jude Med.*, 2010 WL 4968147, at *5.

32. *Id.* at *6.

33. *Id.*

34. *Id.*

35. Judgment, *supra* note 33, at 2-3; *see* Pls.' Reply to Resp. to Mot., *St. Jude Med.*, No. 08-4101, 2010 WL 4968147 (W.D. Ark. Nov. 19, 2010), ECF No. 179; Pls.' Resp. in Opp'n to Mot., *St. Jude Med.*, No. 08-4101, 2010 WL 4968147 (W.D. Ark. Nov. 12, 2010), ECF No. 169; Pls.' Mot. for Summ. J., *St. Jude Med.*, No. 08-4101, 2010 WL 4968147 (W.D. Ark. Oct. 22, 2010), ECF No. 145; Defendant's Reply to Resp. to Mot., *St. Jude Med.*, No. 08-4101, 2010 WL 4968147 (W.D. Ark. Nov. 19, 2010), ECF No. 181; Def.'s Response in Opposition to Motion, *St. Jude Med.*, No. 08-4101, 2010 WL 4698147 (W.D. Ark. Nov. 12, 2010), ECF No. 167; Def.'s Mot. for Summ. J., *St. Jude Med.*, No. 08-4101, 2010 WL 4698147 (W.D. Ark. Oct. 22, 2010), ECF No. 146; (all filed under seal).

36. *St. Jude Med.*, 2010 WL 4698147, at *6.

for the '439 patent on a lost profits theory," the damages sought by St. Jude were not based on a lost profits theory.[37] Furthermore, the court viewed 35 U.S.C. § 284 as taking a flexible approach to damages.[38] Accordingly, the court allowed St. Jude to recover damages flowing from its subsidiaries' lost profits on a reduction of income theory, so long as St. Jude could "show what damages *it* sustained from [Access Closure]'s actions."[39]

Court's Rationale

While not expressed in this court's opinion, it is important to note that "'[w]hether lost profits are legally compensable in a particular situation is a question of law.'"[40] Under the patent statute, a successful patent infringement claimant is entitled to "damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer."[41] In practice, courts usually acknowledge only "'[t]wo alternative categories of infringement compensation . . .[:] the patentee's lost profits and the reasonable royalty he would have received through arms-length bargaining.'"[42] Still, the statute has been used to support a flexible approach to the damages that can be claimed by patent holders, and it sets the minimum award to a reasonable royalty rate for the use made by the infringer.[43]

In this case, the court began by recounting the ruling under *Mars* that, "a patent holder cannot collect the lost profits of a wholly-owned subsidiary without showing that profits flow inexorably from subsidiary to parent."[44] Based on this, the court ruled that St. Jude could not recover "on a lost profits theory."[45]

Fortunately for St. Jude, the court held that lost profits were not being sought.[46] Although Access Closure argued that St. Jude's reduction in income theory was but a thinly veiled attempt to recover its subsidiaries' lost

37. *Id.*

38. *Id.*

39. *Id.*

40. Mars, Inc. v. Coin Acceptors, Inc., 527 F.3d 1359, 1365 (Fed. Cir. 2008), *rev'd on other grounds*, 557 F.3d 1337 (2009) (quoting *Poly-America*, 383 F.3d at 1311).

41. 35 U.S.C. § 284.

42. Whitserve, LLC v. Computer Packages, Inc., 694 F.3d 10, 26 (Fed. Cir. 2012) (quoting Lucent Tech., Inc. v. Gateway, Inc., 580 F.3d 1301, 1324 (Fed. Cir. 2009)).

43. *St. Jude Med.*, 2010 WL 4968147, at *6.

44. *Id.* at *5 (citing 527 F.3d at 1367).

45. *Id.* at *6.

46. *Id.*

profits, the court was willing to accept this veil, stating, "Because St. Jude [had] disclaim[ed] any potential recovery under a lost profits theory, [and that Access Closure]'s arguments regarding the unavailability of lost profits damages are moot."[47]

Once the lost profit arguments were disposed, the court examined St. Jude's reduction in income theory on its own as an alternative damage claim.[48] Access Closure argued that the reduction in income theory had a "dearth of precedent" to support it.[49] In fact, no court had allowed these damages to be sought since the Federal Circuit's holding in *Mars*.[50] However, the court relied on *Rite-Hite*, *SEB, S.A. v. Montgomery Ward & Co.* (*Montgomery Ward I*), and *Mars* to support its holding that 35 U.S.C. § 284 "envisions a flexible approach to patent damages,"[51] noting:

> We have previously recognized that patentees may be entitled to damages above a reasonable royalty on theories entirely distinct from lost profits . . . [but because Mars seeks only lost profits and reasonable royalties] . . . we need not determine whether Mars would have been entitled to recover under any other damages theory for the economic injury that it suffered as a result of [its subsidiary's] lost sales.[52]

Accordingly, the court concluded that St. Jude could, as a matter of law, present its claim for damages based on reduction in income theory to the jury.[53]

Critique of Court's Approach

The court's decision is a positive step towards recovering damages for intellectual property right infringement because it creates a potential way for patentees to recover some of the damages incurred when their subsidiaries lose profits.[54] It offers a novel answer to the question raised in *Mars* about what profits "flow inexorably" from subsidiaries to their parent corpora-

47. *Id.*

48. *Id.*

49. *St. Jude Med.*, 2010 WL 4968147, at *6.

50. *See* Robert A. Matthews, *Wholly Owned Subsidiary Manufacturer*, 4 ANNOTATED PAT. DIG. § 30:70 (2013).

51. *St. Jude Med.*, 2010 WL 4968147, at *6 (referencing Rite-Hite Corp. v. Kelley Co., 56 F.3d 1538 (Fed. Cir. 1995)); SEB, S.A. v. Montgomery Ward & Co., Inc., 412 F. Supp. 2d 336 (S.D.N.Y. 2006); *Mars*, 527 F.3d at 1365.

52. *St. Jude Med.*, 2010 WL 4968147, at *6 (quoting *Mars*, 427 F.3d at 1366) (alteration in original).

53. *Id.*

54. *See id.* at *5 (citing *Mars*, 527 F.3d at 1367).

tions.[55] While the traditionally rigid case law will most likely limit the effect of this holding, this case, at the very least, reflects the judicial trend of more realistically compensating the corporate victims of patent infringement.

Courts have historically been reluctant to allow corporations to seek lost profits for products they did not make or sell, even if the patent holder wholly owns and controls the company that does make and sell those products.[56] In fact, in 2004, the Federal Circuit expressly stated that the parent-subsidiary corporate structure was limited in that the patent holder could not claim the lost profits of its subsidiary if it did not have an exclusive license.[57]

Only four years later, however, the Federal Circuit in *Mars* took a step back from its bright-line rule by stating that a patent holder may have grounds to recover based on its subsidiaries' lost profits if those profits "flow inexorably" to the parent corporation.[58] Admittedly, the *Mars* Court was reluctant to let patent holders recover lost profit damages based on a non-exclusive licensee's sales, even where the licensee is a subsidiary of the patent holder.[59] That court even held that the patent holder in the case could not recover for the lost profits of its wholly-owned subsidiaries.[60] Still, the Federal Circuit limited its holding to the "conclu[sion] that [the subsidiary]'s profits did not–as Mars argued–flow inexorably to Mars."[61] Thus, the court left open the question of whether lost profits that "actually *do* flow inexorably" from the subsidiary to its patent-holding parent corporation may be recovered by that parent corporation.[62]

Since *Mars*, district courts have considered the "flow inexorably" theory, but no court—until *St. Jude Medical*—has allowed any parent corporation to seek damages on that theory, or any other similar theory.[63] For example, the court in *Kowalski* precluded the sole, individual owner of a corporation from seeking his own corporation's lost profits because the owner never personally sold any products and, though "he had complete con-

55. *Id.*

56. Matthews, *supra* note 3, at 551.

57. *Poly-America*, 383 F.3d at 1311 ("Poly-America and Poly-Flex may not enjoy the advantages of their separate corporate structure and, at the same time, avoid the consequential limitations of that structure-in this case, the inability of the patent holder to claim the lost profits of its non-exclusive licensee.").

58. 527 F.3d at 1367.

59. *Id.* at 1366–67; "Mere ownership and control is sufficient to prove that profits flowed inexorably from a subsidiary to a parent." Kowalski v. Mommy Gina Tuna Res., 574 F. Supp. 2d 1160, 1163 (D. Haw. 2008).

60. *Mars*, 527 F.3d at 1366.

61. *Id.* at 1367.

62. *Id.*

63. *See* Matthews, *supra* note 3, at 566 (noting that district courts have considered whether profits flow inexorably, but have not concluded in the affirmative).

trol of any profits reaped by his corporation," his corporation's profits did not automatically go to him—he could have left them in the corporation.[64] The Southern District of New York in *Montgomery Ward I*—cited in *St. Jude Medical*—allowed a patent-holding-company's lost profits claim to survive summary judgment on the condition that the patent holder show that *its* damages were a foreseeable consequence of infringement.[65] The district court, however, ultimately refused to allow the patent holding company to seek lost profit damages because the company had failed to show the damages caused with sufficient precision.[66]

St. Jude Medical offers a solution to the *Mars* question by only seeking those damages that directly and "inextricably" flow to the patent holder.[67] Though St. Jude's exact damages calculations are unknown, the reduction in income theory could be calculated in two ways. First, the patent holder could show, based on its subsidiary agreements, how much of the subsidiary's profits are guaranteed to go to the patent holder and then compare that to the subsidiary's lost profits. Notably, this calculation varies heavily based on the patent holder's subsidiary agreements and could result in damages very similar to lost profits depending on the corporate structure. The second calculation alternative requires establishing the subsidiary's lost profits, determining how much these lost profits affect the fair market value of the subsidiary, and comparing that amount to the patent holder's ownership interest in the subsidiary. While this damages calculation may first appear to be the same as lost profits if the subsidiary is wholly-owned, the subsidiary's lost profits are not likely to be fully represented in its total value; lost profits are most likely diluted when considering the subsidiary's market value. Admittedly, these calculations are more complicated than the normal lost profits damages calculation, but they have the potential to increase the patent holder's damage award and more accurately reflect the real harm caused by infringement. Additionally, in line with case law, these calculations reflect only damage inflicted directly on the patent holder, not damage to the subsidiary.

An interesting quality of this damage theory is that it is independent of the patent license agreement between the patent holder and its subsidiary. Courts generally focus on patent licenses to determine the basis for damages.[68] The traditional way to reclaim any damages related to the patent

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64. 574 F. Supp. 2d at 1163.

65. *Montgomery Ward I*, 412 F. Supp. 2d at 347–48.

66. SEB, S.A. v. Montgomery Ward & Co. (*Montgomery Ward II*), No. 99-Civ.-9284-SCR, 2008 WL 4540416, at *3–4 (S.D.N.Y. Oct. 1, 2008); SEB, S.A. v. Montgomery Ward & Co., Inc. (*Montgomery Ward III*), 594 F.3d 1360, 1380 (Fed. Cir. 2010) (Federal Circuit proceeding noted the district court ruled that lost profits were not available).

67. *St. Jude Med.*, 2010 WL 4968147, at *5–6.

68. *See* Aspex Eyewear, Inc. v. Altair Eyewear, Inc., 288 Fed. App'x 697, 706 (Fed. Cir. 2008).

holder's subsidiary requires that the subsidiary have an exclusive license to the patent, and thus standing to join the suit.[69] Despite this, courts have recently begun acknowledging the potential for recovery if the relationship between parent corporations and their subsidiaries "goes far beyond a licensor/ licensee arrangement."[70] In an attempt to reconcile these ideas, courts have allowed subsidiaries to claim an implied exclusive license and join the infringement suit.[71] Establishing an implied exclusive license, however, is extremely difficult.[72] In *Spine Solutions*, for example, the Federal Circuit overruled an implied exclusive license granted by the district court.[73] Though the patentee only practiced the patent through its subsidiary, did not allow anyone else to practice it, and showed no intention of allowing others to practice it, the subsidiary needed more specific evidence of its own right to exclude others from using the patent for an exclusive license to be implied.[74]

The damages claimed under *St. Jude Medical* do not require proving an implied exclusive license or any license at all.[75] Under *Rite-Hite*, the lost sales used to determine lost profits do not need to "be of products covered by the infringed patent."[76] Instead, the patentee only needs to "prove[ ] that the infringement in fact caused the loss."[77] As a result of these two cases, so long as the parent corporation can prove that its subsidiary lost sales due to the infringement of the parent corporation's patent, the parent corporation would be able to reclaim its damages from the subsidiary's lost profits, regardless of whether the subsidiary practiced the patent at all.[78] In fact, the reduction in income theory seems to allow the patentee to recover based on anyone's lost profits, so long as the patentee has some ownership interest in the entity losing sales due to infringement. While this appears broad, the patent holder would only be able to reclaim damages proportionate to its ownership interest in the entity. Thus, though the patent holder would be able to claim damages based on multiple entities' lost profits, this theory continues to limit the patent holder's damages to its own actual injury.

Though the reduction in income theory is unique, fitting, and unprecedented, this case will most likely not cause a revolution. At minimum, the

69. *See Rite-Hite*, 56 F.3d at 1552.

70. *Union Carbide*, 425 F.3d at 1378.

71. *Aspex Eyewear*, 288 Fed. App'x at 706 (citing Weinar v. Rollform, Inc., 744 F.2d 797, 806–07 (Fed. Cir. 1984)).

72. *See* Spine Solutions, Inc. v. Medtronic Sofamor Danek USA, Inc., 620 F.3d 1305, 1318 (Fed. Cir. 2010).

73. *Id.*

74. *Id.*

75. *See St. Jude Med.*, 2010 WL 4968147, at *6; *Rite-Hite*, 56 F.3d at 1548.

76. *Rite-Hite*, 56 F.3d at 1548.

77. *Id.*

78. *See St. Jude Med.*, 2010 WL 4968147, at *6; *Rite-Hite*, 56 F.3d at 1548.

patent holders are already guaranteed to recover a reasonable royalty rate.[79] Because this court has stayed its damages calculations[80] and no other case has used this reduction in income theory, it is difficult to ascertain whether it will result in greater damage awards than reasonable royalty rates. Still, this case reflects the judicial trend recognizing the close relationship between a parent corporation and its subsidiaries in the patent infringement context. In the end, this case shows a willingness to let patent holders seek alternative damage theories because rigid restriction of damages to lost profits or a reasonable royalty rate often bars corporate patent holders from reclaiming their actual damages.

Conclusion

Modern corporate structures demand a reimagining of patent infringement remedies. Recognizing this, the court in *St. Jude Medical* steps beyond the tradition and expands the idea of profit flow. Profit flows in modern corporate structures are no longer as linear as the law assumes, and can no longer be realistically qualified through traditional lost profit calculations or reasonable royalty rates. As a result, taking advantage of these corporate structures and nonlinear profit flows has historically precluded those corporations from reclaiming all of their damages due to infringement; specifically, they forfeit the lost profits of their subsidiaries. The holding in *St. Jude Medical*, however, allows those companies to seek their previously inaccessible damages suffered due to patent infringement. Overcoming the "dearth of precedent,"[81] this case takes a positive step towards more effectively and realistically defending patent holders.

Admittedly, calculations for the reduction in income theory need to be further developed before their widespread utility can be determined. With this case still pending appeal, however, the Federal Circuit may shed some light on how corporate patentees may calculate their recovery.

Regardless of whether the damage claims in *St. Jude Medical* take root, the case marks a judicial trend towards acknowledging the practical damages that the patentees suffer when their patents are infringed. In sum, this case shows that at least one court is willing to look at the impact of subsidiary lost profits on patent holders with fresh eyes; hopefully others will follow its lead.

79. 35 U.S.C. § 284.

80. Judgment, *supra* note 33, at 2–3.

81. *St. Jude Med.*, 2010 WL 4968147, at *6.