Keywords: **sale or offer for sale, § 271(a), willfulness**

General: **Mere negotiation and contracting for an eventual sale of a product outside the U.S. does not give rise to infringement under § 271(a). Post-suit developed defenses, when found to raise a substantial question of the validity of a patent, may operate to preclude a finding of willful infringement.**

Halo Electronics, Inc. v. Pulse Electronics, Inc. and Pulse Electronics, Corp.
(Fed. Cir. 2014)
Decided October 22, 2014

I. Facts

Halo Electronics, Inc. ("Halo") is a supplier of electronic components and owns U.S. Patents 5,656,985, 6,297,720, and 6,344,785 (collectively "the Halo patents") directed to surface mount electronic packages containing transformers for mounting on a printed circuit board inside electronic devices such as computers and internet routers. Pulse Electronics, Inc. and Pulse Electronics Corp. (collectively "Pulse"), another supplier of electronic components, designs and sells surface mount electronic packages and manufactures those products in Asia. Some of Pulse's products were delivered by Pulse to customers in the United States, but the majority of them were delivered outside the United States, for example, to contract manufacturers for companies such as Cisco. Those contract manufacturers incorporated the electronic packages supplied by Pulse into end products overseas, including internet routers manufactured for Cisco, which were then sold and shipped to consumers around the world.

For those products that Pulse delivered abroad, all purchase orders were received at Pulse's foreign sales offices. However, Pulse engaged in pricing negotiations in the U.S. with companies such as Cisco, and Pulse's employees in the U.S. approved prices that its agents quoted to foreign customers. Pulse also engaged in other activities in the U.S., including meeting regularly with Cisco design engineers, sending product samples to Cisco for pre-approval, attending sales meetings with its customers, and providing post-sale support for its products. Although Cisco outsourced its manufacturing activities to foreign contract manufacturers, Cisco negotiated with its component suppliers the prices that its contract manufacturers would pay when purchasing component parts. As one of Cisco's component suppliers, Pulse executed a general agreement with Cisco that set forth manufacturing capacity, low price warranty, and lead time terms. However, the general agreement did not refer to any specific Pulse products or prices.

Pulse allegedly knew of the Halo patents as early as 1998. In 2002, Halo sent Pulse two letters offering licenses to the Halo patents, but did not accuse Pulse of infringement in those letters. An engineer at Pulse reviewed the Halo patents and concluded that they were invalid in view of prior Pulse products, but no opinion of counsel was sought.

In 2007, Halo sued Pulse for patent infringement. Pulse denied infringement and challenged the validity of the Halo patents based on obviousness and other grounds. During the suit, Pulse moved for summary judgment and argued that it did not directly infringe the Halo patents by selling or offering to sell products that Pulse manufactured, shipped, and delivered outside of the U.S. The district court granted the motion, holding that those products were sold and offered for sale outside of the U.S. and, thus, were beyond the scope of 35 U.S.C. § 271(a).

The parties proceeded to trial on claims of direct infringement by products that Pulse shipped into the U.S. and inducement of infringement by products shipped by Pulse that were incorporated into end products that were imported into the U.S. The jury found both direct and induced infringement by Pulse and noted that it was highly probable that Pulse's infringement was willful. In response to a post-trial motion, the district court concluded that the objective component of willfulness was not satisfied because Pulse "reasonably relied on at least its obviousness defense" and the defense was not "objectively baseless." Halo appealed.

II. Issues

A. Did the district court err in granting summary judgment of no direct infringement with respect to products that Pulse delivered abroad?

B. Did the district court err in concluding that the objective component of willfulness was not satisfied because Pulse "reasonably relied on at least its obviousness defense" and the defense was not "objectively baseless?"

III. Discussion

A. No. Halo argued that the Pulse products delivered abroad were sold or offered for sale within the U.S. because negotiations and contracting activities occurred within the U.S., which resulted in binding contracts that set specific terms for price and quantity. Halo also argued that the location of the sale or offer for sale should not be limited to the location of delivery. Pulse countered that the products at issue were sold or offered for sale outside of the U.S. because the products were manufactured, ordered, invoiced, shipped, and delivered abroad. Pulse further argued that the discussions in the U.S. with Cisco were not a guarantee that they would receive any actual orders from the contract manufacturers. Finally, Pulse contended that Halo was attempting to improperly expand the geographic scope of § 271(a) to reach activities outside of the U.S.

35 U.S.C. § 271(a) states "whoever without authority makes, uses, offers to sell, or sells any patented invention, within the United States...infringes the patent." The court noted the existence of a strong policy against extraterritorial liability in patent law. The court also noted that while a place of contracting may be one of several possible locations for a sale to confer personal jurisdiction, negotiation and contracting activities alone have not been found to rise to the level of a sale when the vast majority of activities underlying the sales transaction occur wholly outside of the U.S. The term "sale" for purposes of §

271(a) is not defined in the patent statute and the court noted that a sale generally includes the concept of a transfer of title or property, but can also include an agreement by which such a transfer takes place. However, the court concluded that when substantial activities of a sales transaction, including the final formation of a contract for sale encompassing all essential terms as well as the delivery and performance under that sales contract, occur outside of the U.S., pricing and contract negotiations alone do not constitute or transform the extraterritorial activities into a sale within the U.S. for purposes of § 271(a).

Here, the products were manufactured, shipped, and delivered abroad, the purchase orders were received abroad from foreign contract manufacturers, and Pulse was paid by the contract manufacturers. Thus, the substantial activities of the sales transaction were found to be performed outside of the U.S. and, accordingly, the contracting and negotiating by Pulse in the U.S. did not constitute a sale under § 271(a).

The court next turned to the alleged offer for sale by Pulse of the products that were manufactured, shipped, and delivered abroad. The court noted that an offer to sell generally communicates a willingness to enter into a bargain that can be accepted by another to finalize the bargain. The court noted that Federal Circuit precedent (*Transocean v. Maersk*) established that for an offer to sell to constitute infringement, the offer must be to sell a particular patented invention within the U.S. Thus, contract negotiations outside the U.S. covering delivery and performance in the U.S. constituted infringement. The court noted that the present case involves the opposite situation (a negotiation in the U.S. for a sale outside of the U.S.). The court adopted the reasoning of *Transocean* and found that an offer for sale, in order to constitute infringement, must be an offer contemplating sale in the in the U.S. As the Pulse products manufactured, shipped, and delivered abroad were not found to be sold in the U.S., no offer for sale of the products under § 271(a) had occurred. As such, the court found that the district court was correct in granting summary judgment of no infringement with respect to the products that Pulse manufactured, shipped, and delivered abroad because the products were not sold or offered for sale by Pulse within the U.S.

B. No. 35 U.S.C. § 284 states "[w]hen the damages are not found by a jury, the court shall assess them. In either event the court may increase the damages up to three times the amount found or assessed." Supreme Court precedent requires either willful or bad-faith infringement for enhancement of damages under this provision.

Establishing willful infringement of a valid patent requires a two-prong analysis entailing an objective and a subjective inquiry. As set forth in the Federal Circuit *en banc* decision in *Seagate*, a patentee must show by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent. The state of mind of the accused infringer is not relevant to this objective inquiry. Second, if the threshold objective standard is satisfied, the patentee must also demonstrate that this objectively-defined risk (determined by the record developed in the infringement proceeding) was either known or so obvious that it should have been known to the accused infringer. The district court found that the objective prong was not met in the present case because the obviousness defense presented at trial by Pulse was not objectively baseless. Halo argued that Pulse did not rely on any invalidity defense pre-suit and only developed the defense after the suit was filed. Halo also argued that Pulse did not rely on the cursory analysis of the Halo patents by its engineer in 2002 to assess whether it was infringing valid patents. Pulse argued that there was no accusation of infringement in the 2002 letters, the engineering review was sufficient to conclude that the patents were invalid, and the defense presented at trial raised a substantial question of invalidity and, thus, their actions were objectively reasonable.

The court agreed with Pulse that the district court did not err in holding that the objective prong of the willfulness inquiry was not satisfied. The court found that the district court had reviewed the totality of the record evidence, including the obviousness defense developed during litigation, to determine whether there was an objectively-defined risk of infringement of a valid patent. Because a substantial question as to the obviousness of the Halo patents was raised at trial, the court affirmed district court's finding of non-willful infringement.

IV. Conclusion

Negotiation and contracting for an eventual sale of a product outside the U.S. does not give rise to infringement under § 271(a). Additionally, post-suit developed defenses, when found to raise a substantial question of the validity of a patent, may operate to preclude a finding of willful infringement.