



IDEAS ON INTELLECTUAL PROPERTY LAW

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Manufacturer vs. distributor

Who owns that unregistered trademark?

Manufacturers that let their distributors use their unregistered trademarks may later find themselves in a fight over the marks' ownership. This article highlights how one federal court of appeals recently addressed such ownership disputes and adopted a different test for determining ownership of common law trademarks where there is no agreement addressing the issue.

COMPANIES CLASH OVER MARKS

Coverttech Fabricating, Inc., manufactures protective packaging and reflective insulation. It sells numerous products under the umbrella of its lucrative rFOIL brand. In 1998, Coverttech entered into a verbal agreement with TVM Building Products, Inc., that designated TVM as the exclusive marketer and distributor of rFOIL products in the United States. TVM agreed to refrain from selling competitors' products.

Coverttech terminated the agreement in October 2007, partly because it had discovered that TVM had been purchasing comparable product from another manufacturer and passing it off as Coverttech's. TVM assured Coverttech that its labeling indiscretions were isolated incidents caused by errors in filling its orders, and the companies entered a new agreement not long after. That agreement was subsequently terminated, too.

Nonetheless, TVM continued to market products using the rFOIL brand names. Coverttech ultimately sued TVM.

The trial court ruled for Coverttech on its trademark claims, and TVM appealed.

COURT ADOPTS NEW OWNERSHIP TEST

The rFOIL brand comprises several products, including products under the ULTRA NT RADIANT BARRIER, which isn't registered. On appeal, TVM argued that it, not Coverttech, owned the ULTRA mark. In assessing ownership of the mark the trial court relied on the "first use test," which determines ownership by asking which party was the first to use an unregistered trademark in commerce.

The McCarthy test allows courts to conduct a thorough, individualized analysis of each case that accounts for the unique attributes of the manufacturer-distributor relationship.

The Third Circuit Court of Appeals acknowledged that the first use test is generally appropriate for unregistered trademarks but found an "imperfect fit" when it comes to the "often exclusive and noncompetitive manufacturer-distributor relationship." In that circumstance, ownership rights would go to the distributor in many cases simply because the distributor made the initial sale of goods bearing the mark to the public. Thus, the court said, a different test is necessary when ownership isn't decided in advance.



COURT REJECTS INFRINGER'S "ACQUIESCENCE" DEFENSE

The defendant in *Coverttech Fabricating, Inc. v. TVM Building Products, Inc.*, also argued that Coverttech's claims should have been barred due to acquiescence. An alleged infringer can assert the defense when the trademark owner conveys implied consent to the defendant's use of a mark.

In this type of defense, the court considers whether:

- The owner actively indicated that it wouldn't assert a right,
- The owner's delay between the indication and its assertion of the right was excusable, and
- The delay caused the defendant undue prejudice (meaning the loss of legal rights).

Once the use becomes infringing, the relevant date as far as the delay is when the owner either knew — or should have known — of the existence of a provable infringement claim.

These considerations led the appellate court to conclude that Coverttech didn't acquiesce to TVM's infringement. Coverttech never expressly or impliedly authorized the infringement, and TVM didn't show that the delay in filing the lawsuit was inexcusable or unduly prejudicial. The court upheld the trial court's ruling that Coverttech's delay in initiating its lawsuit didn't demonstrate implied consent.

On appeal, the Third Circuit held that the proper test in such circumstances is the "McCarthy test" (named after the legal treatise where it was first laid out). Under that test, the manufacturer is the presumptive trademark owner. The distributor can rebut that presumption using a balancing test that considers the following six factors:

1. Which party invented or created the mark,
2. Which party first affixed the mark to goods sold,
3. Which party's name appeared on packaging and promotional materials in conjunction with the mark,
4. Which party exercised control over the nature and quality of goods on which the mark appeared,
5. Which party customers looked to as standing behind the goods (for example, the party that received complaints about defects and made appropriate replacements or refunds), and
6. Which party paid for advertising and promotion of the trademarked product.

According to the Third Circuit, this approach allows courts to conduct a thorough, individualized analysis of each case that accounts for the unique attributes of the manufacturer-distributor relationship.

Applying the test to the Coverttech-TVM relationship, the court found that the first, second, fourth and fifth factors favored Coverttech. The third factor was neutral, and the last factor favored TVM. The court therefore held that the six factors in the McCarthy test weighed in favor of Coverttech. The trial court's conclusion that Coverttech owned the mark, while based on the incorrect test, was upheld.

BETTER PROTECTION FOR MANUFACTURERS

The court's adoption of the McCarthy test is welcome news for manufacturers with common law trademarks. However, manufacturers would be wise to expressly address mark ownership in their agreements with distributors. ■



A uniform standard for copyright for industrial designs

Fashion and apparel have long existed in a cloud of copyright confusion. Clothing often incorporates design elements, which may be protectable, and functional elements, which aren't. The U.S. Supreme Court has now established a two-part test intended to resolve "widespread disagreement" regarding copyright protection for such "industrial designs."

OUTFIT SELLERS SQUARE OFF

Varsity Brands, Inc., designs, makes and sells cheerleading uniforms. It owns more than 200 U.S. copyright registrations for two-dimensional designs that appear on the surface of its uniforms, primarily "combinations, positionings, and arrangements of elements," including chevrons, lines, curves, stripes, coloring and shapes. Star Athletica, LLC, also markets and sells cheerleading uniforms. Varsity sued Star Athletica for infringing its copyrights in five designs.

The Copyright Act of 1976 makes "pictorial, graphic, or sculptural features" of the "design of a useful article" eligible for copyright protection as artistic works if the features can be identified separately from — and are capable of existing independently of — the articles' utilitarian (or useful) aspects. A useful article is one with an intrinsic utilitarian function more than merely portraying the appearance of the article or conveying information (for example, a piece of clothing). Useful articles themselves aren't protectable by copyright.

The trial court dismissed Varsity's case before trial. It held that Varsity's designs weren't protectable pictorial, graphic or sculptural works because they served the useful function of identifying the garments as cheerleading uniforms. Therefore, the court said, the designs couldn't be physically or conceptually separated from the utilitarian function of the uniform. The Sixth Circuit Court of Appeals disagreed and reversed.



COURT FASHIONS A TEST

On appeal, the Supreme Court set out to determine whether Varsity's arrangements of lines, chevrons and colorful shapes on the surface of their uniforms were eligible for copyright protection as separate features of the uniforms' designs. To do so, it established a two-part test. Under the test, a feature incorporated into the design of a useful article is eligible for copyright protection only if it:

1. Can be perceived as a nonuseful two- or three-dimensional work of art separate from the useful article, and
2. Would qualify as a protectable pictorial, graphic or sculptural work — either on its own or embodied in an object from which the work can be perceived, reproduced or otherwise communicated — if it were imagined separately from the useful article.

According to the Court, copyright protection extends to pictorial, graphic and sculptural works regardless of whether they were created as freestanding art or as features of useful articles.

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Applying the test to the uniform decorations, the Supreme Court found they were separable and therefore eligible for copyright protection. The decorations could be identified as features with pictorial, graphic or sculptural qualities. And, if they were separated from the uniforms and applied in another medium, they would qualify as two-dimensional works of art under the Copyright Act. Imaginatively removing the decorations

from the uniforms and applying them in another medium also wouldn't replicate the uniform itself.

The Court cautioned, though, that the two-dimensional applied art on the surface of the uniforms were the only feature eligible for a copyright. Varsity has no right to prevent anyone from manufacturing a cheerleading uniform that's identical in shape, cut or dimensions to the uniforms at issue.

The focus should be on the extracted design features, the Court emphasized, not on any aspects of the useful article remaining after the imaginary extraction. The law doesn't require the imagined remainder to be a fully functional useful article.

SOMETHING TO CHEER ABOUT

The high court's ruling provides clothes designers and manufacturers with some certainty regarding the test that courts will apply when determining whether copyright protection is available. They should bear in mind, though, that a garment's shape, cut and dimensions remain unprotected. ▣

Supreme Court limits venue for patent lawsuits

In a landmark decision, the U.S. Supreme Court has dramatically tightened the restrictions on where patent owners can file infringement lawsuits. The court's unanimous ruling is expected to rein in the "forum shopping" that so often occurs in patent infringement cases, where patentees try to file in judicial districts considered to be more plaintiff-friendly, such as the defendant-dreaded Eastern District of Texas.

TRADING PLACES

The case involved a lawsuit between two companies and the states where they do business. TC Heartland LLC is organized and headquartered in Indiana.

Kraft Foods Group Brands LLC is organized under Delaware law, with its principal place of business in Illinois. Kraft sued TC Heartland for patent infringement in the federal district court in Delaware. TC Heartland isn't registered to conduct business in Delaware and has no meaningful presence there, but it does ship the allegedly infringing products into the state.

TC Heartland asked to have the case transferred to a district court in Indiana. The trial court in Delaware rejected the request, and the Federal Circuit Court of Appeals agreed. TC Heartland then turned to the Supreme Court.



HOME, SWEET, HOME

The patent venue law, also known as Section 1400(b), provides that infringement actions should be filed in the judicial district where 1) the defendant resides or 2) has committed infringement and has a regular and established place of business. According to the Federal Circuit, the general venue law, Sec. 1391(c), defines “residence” for corporate defendants.

Section 1400 is the sole and exclusive law controlling patent infringement venue and isn't to be supplemented by Sec. 1391.

Sec. 1391 currently provides that “[e]xcept as otherwise provided by law” and “[f]or all venue purposes,” a corporate defendant resides in any judicial district where it’s subject to personal jurisdiction for the lawsuit in question. Because the Delaware court could exercise personal jurisdiction over TC Heartland, the Court of Appeals reasoned, the company resided in Delaware under Sec. 1391 and, therefore, under Sec. 1400(b).

The Supreme Court disagreed. It pointed to its 1957 decision in *Fourco Glass Co. v. Transmirra Products Corp.*, where it found that Congress enacted Sec. 1400(b) as a standalone venue statute and that “resides” for purposes of the provision meant the state of incorporation. Sec. 1400, the Court said, is the sole and exclusive law

controlling patent infringement venue and isn’t to be supplemented by Sec. 1391.

According to the Court, the only question here was whether Congress changed Sec. 1400(b)’s meaning when it amended Sec. 1391 in 1988 to state that it applied “for purposes of venue under this chapter” of laws or when it adopted the current version in 2011. When Congress intends to make such a change, the Court found, it ordinarily provides a relatively clear indication of its intent in the amended provision’s text.

No such indication appears in the current version of Sec. 1391, the high court said. In fact, the current version includes a savings clause that expressly states that it doesn’t apply “when otherwise provided by law,” making clear that Sec. 1400(b) is a standalone statute.

MAPPING THE FUTURE

The Court concluded that, as applied to domestic corporations, the term “resides” in Sec. 1400(b) refers only to the state of incorporation. This interpretation significantly narrows patent owners’ options when deciding where to file infringement actions.

Defendants may enjoy a home-court advantage more often now, instead of ending up in courts that might have rules and procedures different from their own. They could, however, face extended delays due to protracted pretrial litigation over whether they have a “regular and established place of business” in a district sufficient to justify finding venue there. □

Coding error: Court rejects software patent

Oops — they did it again. The Federal Circuit Court of Appeals has rejected yet another software patent. The court, which hears all appeals involving patents, found that the patent was for a patent-ineligible invention.

SNAPSHOT OF THE CASE

RecogniCorp, LLC, owns a patent for a method and apparatus for building a composite facial image using “constituent parts.” Previously, composite facial images typically were stored in file formats that required significant memory, and compressing the images often reduced image quality. Digital transmission could be difficult. The patent encodes images at one end using a mathematical formula in a way that requires less memory and bandwidth and decodes the images at the other end of transmission.

The company sued Nintendo Co., Ltd., for infringement. The trial court dismissed its lawsuit before trial, ruling that the invention wasn’t patent-eligible, and RecogniCorp appealed.

THE COURT’S FOCUS

On review, the appellate court applied the so-called *Alice* test for identifying patents that cover nothing more than abstract ideas. First, the court determines whether the claimed invention is a patent-ineligible abstract idea. If so, it determines whether the invention includes an “inventive concept” that transforms it into a patent-eligible application of the abstract idea.

When dealing with software patents, the first inquiry is often whether the invention is a specific means or method for improving technology or just an abstract end-result. The court found that the patent claim here covered the abstract idea of encoding and decoding. According to the court, adding one abstract idea (math) to another abstract idea (encoding

and decoding) doesn’t make a claimed invention nonabstract.

Proceeding to the second step, the court considered RecogniCorp’s contention that its encoding process, using its specific algorithm, transformed the abstract idea into a patent-eligible invention. It rejected the argument, finding that the addition of a mathematical equation that simply changes the data into other forms of data couldn’t save the patent.

The court noted that RecogniCorp didn’t allege a particularized application of the abstract idea. The Federal Circuit acknowledged that the patent claimed the use of a computer, but found that it also did exactly what the court has previously warned a software patent may not do — tell a user to take an abstract idea and apply it with a computer.

THE BIG PICTURE

Some observers point to the court’s ruling as another nail in the coffin for software patents, but that’s probably an overstatement. The court’s various rulings applying the *Alice* test have largely been fact-specific, indicating the need to take the test into account in the patent drafting stage. ■



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TC Heartland and Improper Venue Waiver in Patent Infringement Lawsuits: The District of Minnesota Perspective

By Adam E. Szymanski

The dust has settled on the Supreme Court's May 2017 *TC Heartland* decision that a domestic corporation "resides" only in the state of incorporation under the patent venue statute—28 U.S.C. § 1400(b). Abrogating the Federal Circuit's intervening decision in *VE Holding Corp. v. Johnson Gas Appliance Co.*, the Court confirmed that the decision in *Fourco Glass Co. v. Transmirra Prod. Corp.* unambiguously defined the term sixty years earlier and that Congress's subsequent amendments to the general venue statute, 28 U.S.C. § 1391, did not alter that meaning or ratify the Federal Circuit's interpretation.

Yet despite this clarity, a new issue has emerged: If a defendant failed to raise the defense of improper venue in district court because it was not available before *TC Heartland*, did they inadvertently waive it? Under Federal Rules of Civil Procedure 12(h)(1) and (g)(2), a party waives a defense that it failed to timely raise unless that defense was not previously "available" to that party. Because understandings of "available" differ, a defendant may find itself in the curious position of having unknowingly waived a venue defense.

A number of district courts have addressed this issue and arrived at opposite outcomes. Some have deemed such a failure to result in waiver—finding that the Supreme Court never overruled the *Fourco* decision. For these courts, *TC Heartland* did not amount to an intervening change in the law, and the defendants waived the improper venue defense by not raising it. Other courts have acknowledged that, for nearly three decades, practice conformed to the Federal Circuit's broader interpretation in *VE Holding*, such that "resides" was defined by the general venue statute and was proper where there was personal jurisdiction. For these courts, *TC Heartland* was an intervening change in the law and the defense to improper venue was not available until *TC Heartland*.

Until recently, the U.S. District Court for the District of Minnesota had yet to pick a side. On August 4, 2017, the district court of Minnesota opted for the latter understanding—that *TC Heartland* was indeed an intervening change in the law—in its *Cutsforth* and *Valspar* decisions. *Cutsforth, Inc. v. LEMM Liquidating Co., LLC*, No. 12-CV-1200 (SRN/LIB), 2017 WL 3381816 (D. Minn. Aug. 4, 2017); *Valspar Corp. v. PPG Indus., Inc.*, No. 16-CV-1429 (SRN/SER), 2017 WL 3382063 (D. Minn. Aug. 4, 2017). In both cases, the district court noted that, if defendants had attempted to raise the defense of improper venue before *TC Heartland* and argued that *VE Holding* was not binding, they would not have been successful. The court said: "It is illogical and unfair to argue that [defendant] erred by not making an argument that both this Court and the parties knew would have been rejected—just as it had consistently been rejected around the country for a quarter of a century." At least in the district court for the district of Minnesota, defendants under similar circumstances have two cases standing against waiver of the improper venue defense. Whether a change of venue will be granted on that basis, however, is still within the discretion of the district court.