Published on *The National Law Review* https://natlawreview.com

Walking the Jurisdictional Line: Cashing in on Federal Jurisdiction in Patent Licensing Disputes

Article By:

Jeffrey S. Whittle

Johnny Cash's famous "I Walk the Line" song draws a line emphasizing how difficult it can be to stay faithful with temptations "on the road" as the singer travels on tour. Similarly, patent license drafters and litigators can find it difficult to walk the line between federal and state jurisdiction when drafting license agreements and framing disputes for court.

Similar to Johnny Cash's meandering line he attempted to walk, the recent Federal Circuit case of *Inspired Development Group, LLC vs. Inspired Products Group, LLC d/b/a KidsEmbrace, LLC* illustrates that this jurisdictional line may not always be straight as well. Inspired Development holds patents for a series of child car seat designs shaped like cartoon and comic book characters. The company entered an exclusive licensing agreement with KidsEmbrace in 2007 to commercialize the car seats in exchange for royalty payments. After a change in company leadership, KidsEmbrace terminated the licensing agreement with Inspired Development, which believed it was due additional payments per terms of the deal. In 2016, Inspired Development filed a breach of contract and unjust enrichment suit against KidsEmbrace in federal court on the basis of diversity jurisdiction. [1]

After losing on several counts, Inspired Development appealed to the Eleventh Circuit Court of Appeals. The appeals court, however, noted that the parties had not alleged sufficient facts to support diversity jurisdiction, and after an investigation, the parties were forced to concede that diversity jurisdiction did not exist. [2] Thus, the parties found themselves on the wrong side of the federal jurisdiction line, and the case appeared to be headed for dismissal. At that point, KidsEmbrace sought to preserve federal court jurisdiction by arguing that the state law breach of contract and unjust enrichment claims in the complaint actually arose under federal patent law. [3] Focusing primarily on a claim for unjust enrichment, KidsEmbrace argued that for Inspired Development to show that it conferred a benefit on KidsEmbrace (an element of proving unjust enrichment) Inspired Development would have to prove that KidsEmbrace infringed its patents.

The US District Court for the Southern District of Florida initially agreed with KidsEmbrace and ruled that it retained jurisdiction. The case then returned to the Eleventh Circuit Court of Appeals, which transferred the appeal to the Federal Circuit to decide if the claims invoked federal patent law and, therefore, should be litigated in federal courts.

The Federal Circuit disagreed with the lower court, ruling that the asserted claims did not arise under federal patent law. In reaching that holding, the court applied the *Gunn v. Minton* test . While explicit federal jurisdiction exists over matters created by the federal patent statutes (such as a claim for patent infringement), the Supreme Court also has found federal jurisdiction to exist over a "special and small category" of state law claims which require the resolution of a substantial question of federal patent law. [4] The 2013 Supreme Court decision in *Gunn v. Minton* laid out a four part test to determine whether such a question exists, noting that "federal jurisdiction over a state law claim will lie if 'a federal issue' is: (1) 'necessarily raised,' (2) 'actually disputed,' (3) 'substantial,' and (4) 'capable of resolution in federal court without disrupting the federal-state balance approved by Congress.'" [5] The Federal Circuit expanded on the test in its 2015 *NeuroRepair* opinion, explaining that the question of whether the federal issue was "substantial" was determined by whether (1) its resolution is dispositive of the current case, (2) its resolution will control "numerous other cases," and (3) the Government "has a direct interest in the availability of a federal forum to vindicate its own administrative action." [6]

Applying the *Gunn* test in light of the *NeuroRepair* factors, the Federal Circuit agreed that one way Inspired Development could prove its unjust enrichment claim "was to show that KidsEmbrace [benefited by using] one or more of Inspired Development's 'utility and design Patents' in the car seats it manufactured and sold. Thus, Inspired Development's unjust enrichment claim potentially raises a question of patent law regarding infringement." [7] The Federal Circuit, however, also noted there were other ways KidsEmbrace could have benefited from the agreement even without infringing the patents, such as "avoid[ing] uncertainty and litigation" and "ensuring that no other entity has the ability to create competing products." [8] Because the dispute could potentially be resolved without reaching the question of patent law, the case could not pass the "necessarily raised" part of the *Gunn* test, nor could it pass the "substantial" part of the *Gunn* test because its resolution would not be dispositive of the case.

With that, the Federal Circuit reversed the District Court's decision and found that the dispute did not belong in federal court. The District Court judgment was vacated and the case was remanded for dismissal.

One of the key takeaways from *Inspired Development* is how critical it is for the patent question asserted to be a necessary element of the case in order to stay on the federal jurisdiction side of the line. While an action for breach of a patent license can arise under federal patent law, the *Inspired Development* holding shows that any alternative basis for proving an element of a claim can potentially destroy federal jurisdiction. Parties wanting to walk the line of preserving the availability of federal jurisdiction should keep a close watch when drafting the agreement (to ensure that litigating compliance with the agreement will require analysis of an issue of patent law) and keep their eyes wide open for alternate claims to assert. For example, a state law disparagement claim based on statements that a competing product infringes a patent can potentially support federal patent jurisdiction when resolving the disparagement claim necessarily requires determining whether infringement occurred. [9]

As *Inspired Development* shows, parties might not find it easy to be true when judging on which side of the jurisdictional line a dispute will fall. It can be difficult to even try to turn the tide if the patent question is not an essential part of the dispute. Nonetheless, parties have a way to keep jurisdiction on their side if they draft agreements with an eye towards litigation and carefully select claims to assert. Parties may not have the same swagger as Johnny Cash, but with these goals in mind, they too can walk the line.

[1] Federal courts have jurisdiction over suits when each defendant is a citizen of a different state from each plaintiff, and the amount in controversy is greater than $75,000. 28 U.S.C. § 1332. This is commonly referred to as “diversity jurisdiction.”

[2] Inspired Development is a Florida Limited Liability Corporation (LLC) and KidsEmbrace is a California LLC. However, the citizenship of an LLC is determined by the citizenship of its members for purposes of evaluating whether diversity jurisdiction exists. *See, e.g., Mallory & Evans Contractors & Engineers, LLC v. Tuskegee Univ.* , 663 F.3d 1304, 1305 (11th Cir. 2011). Because Inspired Development and KidsEmbrace had two members in common, diversity jurisdiction was impossible.

[3] Federal courts have jurisdiction over suits “arising under” federal patent law. 28 U.S.C. § 1338(a).

[4] *Gunn v. Minton* , 568 U.S. 251, 258 (2013).

[5] *Id.*

[6] *NeuroRepair, Inc. v. The Nath Law Group* , 781 F.3d 1340, 1345 (Fed. Cir. 2015).

[7] *Inspired Development* , slip op. at 11-12.

[8] *Id.*

[9] *See Additive Controls & Measurement Sys., Inc. v. Flowdata, Inc.* , 986 F.2d 476 (Fed. Cir. 1993); *Hunter Douglas, Inc. v. Harmonic Design, Inc.,* 153 F.3d 1318 (Fed. Cir. 1998), overruled on other grounds by *Midwest Indus., Inc. v. Karavan Trailers, Inc.*, 175 F.3d 1356 (Fed. Cir. 1999).

National Law Review, Volume IX, Number 301