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SCOTUS Rules That Fee-Shifting Is Patently Unfair When Patent (and Trademark?) Applicants Head To Federal District Court

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The United States Supreme Court handed down a unanimous decision on Dec. 11, 2019, protecting the American Rule, which provides the "bedrock principle" that "[e]ach litigant pays his [her, or its] own attorney's fees, win or lose, unless a statute or contract provides otherwise." *Peter v. NantKwest, Inc.*, No. 18-801, ___ U.S. ___ (2019) (citations omitted). The Supreme Court's decision was in the context of 35 U.S.C. § 145 civil actions brought in federal district courts against the United States Patent and Trademark Office (PTO) challenging PTO refusals to register patent applications and other adverse decisions. Because the Lanham Act (for trademarks) has an identical provision, 15 U.S.C. § 1071(b)(3), this decision almost certainly also will govern district court civil actions brought against the PTO, pursuant to 15 U.S.C. § 1071(b)(1), for refusals to register trademark applications.

Background

Section 145 of the Patent Act affords dissatisfied applicants the right to file a civil action in the United States District Court for the Eastern District of Virginia. One of the advantages of §145 is that it permits the applicant to present new evidence not previously presented to the PTO. In a §145 action, the district court acts as a factfinder when new evidence is introduced and makes *de novo* determinations. Section 145 also specifies, "[a]ll the **expenses** of the proceedings shall be paid by applicant."

Prior to the Supreme Court's decision, applicants recently faced the obstacle of paying for the fees of the PTO's attorneys and paralegals if the applicant desired to proceed under §145 – rather than appeal directly to the Federal Circuit under §141 – *even if the applicant ultimately won*. Accordingly, the PTO's recent application of §145 to attorney's fees acted as a deterrent for applicants asking for a *de novo* review of an unfavorable PTO decision. While the Supreme Court's decision in *Nantkwest* removed this obstacle, and restored the American Rule that both parties pay their own attorney's fees in the context of §145, applicants are still liable for the PTO's other "expenses of the proceedings," regardless of whether they win or lose.

Procedural History

After the PTO denied NantKwest's patent application, NantKwest filed a complaint under §145 against the PTO in the Eastern District of Virginia. After the District Court granted summary judgment to the PTO on the merits, and the United States Court of Appeals for the Federal Circuit affirmed, the PTO subsequently moved for reimbursement of expenses that included the *pro rata* salaries of PTO attorneys and a paralegal who worked on the case. The District Court denied the PTO's motion to recover its *pro rata* legal fees as "expenses" of the §145 proceeding. A divided Federal Circuit panel reversed, stating that the American Rule likely did not apply, but even if it did, the statute explicitly allowed the recovery of the fees. The Federal Circuit voted *sua sponte* – without prompting by either party – to rehear the case *en banc* and reversed the panel. The majority *en banc* opinion held that the American Rule's presumption against fee shifting applied to §145 because it is "the starting point whenever a party seeks to shift fees from one side to the other in adversarial litigation." The Supreme Court granted *certiorari* and affirmed.

Supreme Court's *Nantkwest* Decision

Justice Sotomayor delivered the unanimous opinion of the Court in *Nantkwest* that "expenses" do not include the salaries of attorneys and paralegals employed by the PTO.

The Court quickly dispensed with the Government's argument that the American Rule did not apply to non-prevailing party statutes. Indeed, the Supreme Court held that no statute is exempt from the presumption against fee-shifting. The Court explained that "the presumption against fee shifting not only applies, but is particularly important because §145 permits an unsuccessful government agency to recover its expenses from a prevailing party." The Court continued, "Reading §145 to award attorney's fees in that circumstance 'would be a radical departure from longstanding fee-shifting principles adhered to in a wide range of contexts.'"

After concluding that the presumption applied, the Court then focused on the language "expenses of the proceeding" in the statute. The Court explained that Congress must be "specific and explicit" to overcome the presumption against fee-shifting. The term "expenses of the proceeding" is like "expenses of the litigation," which has long been recognized in other statutes not to include attorney's fees. Analyzing other statutes, the Court concluded that Congress understands the two terms "expenses" and "attorney's fees" to be distinct and not inclusive of each other. Put differently, if Congress had intended the PTO to recover its attorney's fees for any case filed by a dissatisfied applicant, it would have said so by including both terms.

The Court also discussed how the Patent Act's history reinforces that Congress did not intend to shift fees in §145 actions. Historically, the Court explained, there is no evidence that the PTO's predecessor, the Patent Office, originally paid its personnel from sums collected from adverse parties in litigation. That salaries of PTO employees might have qualified as an "expense" of the agency does not automatically render them an "expense" of a §145 proceeding. Importantly, the Court noted that "[n]either has the PTO, until this litigation, sought its attorney's fees under §145." Indeed, the Court concluded, "[t]hat the agency has managed to pay its attorneys consistently suggests that financial necessity does not require reading §145 to shift fees, either."

Accordingly, the Court held the plain text of §145 does not overcome the American Rule's presumption that each side pays its own attorney's fees.

Application of *Nantkwest* in Trademark Context

Practitioners should take note of the applicability of this decision in trademark civil actions brought against the PTO in the district court, pursuant to 15 U.S.C. § 1071(b)(1). The Lanham Act contains an analogous provision to §145, 15 U.S.C. § 1071(b)(3), for reimbursement of expenses, and using the same reasoning, the PTO also has asked for attorney's fees in *ex parte*, *de novo* trademark appeals, whether it wins or loses.

Reviewing §1071(b)(3), in *Shammas v. Focarino*, the United States Court of Appeals for the Fourth Circuit held that "the imposition of all expenses on an applicant in an *ex parte* proceeding, *regardless of whether he wins or loses*, does not constitute fee-shifting that implicates the American Rule but rather an unconditional compensatory charge imposed on a dissatisfied applicant who elects to engage the PTO in a district court proceeding." 784 F. 3d 219, 221 (4th Cir. 2015). "And we conclude that this compensatory charge encompasses the PTO's salary expenses for the attorneys and paralegals who represent the Director." *Id*.

Although the Supreme Court denied *certiorari* to the Fourth Circuit's *Shammas* decision, last month the Supreme Court granted *certiorari* to review another Fourth Circuit decision in which it will primarily be reviewing whether the addition of .COM to a generic term creates a registrable trademark. But because the Fourth Circuit affirmed the District Court's award of over $50,000 in attorney's fees to the PTO, stating "*Shammas* remains the law in this circuit, and as long as we continue to be bound by that precedent we must affirm the district court's grant of attorneys fees," the Supreme Court will also have the opportunity to clarify that its ruling in *Nantkewst* applies to the Lanham Act's parallel provision.

In the meantime, it remains to be seen if the PTO voluntarily will cease making attorney's fees demands in the trademark context, given the Supreme Court ruling in *Nantkwest*, and the clear parallels between §145 and §1071(b)(3). It should do so, as it appears the Fourth Circuit's *Shammas* decision effectively has been overruled by *Nantkwest* to the extent it sought to shift expenses categorized as attorney's fees.

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