

Federal Circuit Holds That Parent Company May Not Recover Lost Profits of Subsidiary in Infringement Action

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The United States Court of Appeals for the Federal Circuit recently held that a parent company may not recover the lost profits of a wholly owned subsidiary as damages in a patent infringement action, because the parent could not prove that the subsidiary's profits from the diverted sales would have "inexorably flowed" to the parent. *Mars, Inc. v. Coin Acceptors, Inc.*, Nos. 07-1409, 07-1436, 2008 WL 2229783 (Fed. Cir. June 2, 2008). Thus, when one entity in a corporate family holds the patent rights, and another entity sells the products covered by the patent, the patent-holding entity is unlikely to be able to recover the "lost profits" of the entity that sold the relevant products. The Federal Circuit noted, however, that other bases for damages *above* "reasonable royalty" damages may be appropriate. *Mars* at *5.

The *Mars* case originated in the United States District Court for the District of New Jersey. Mars alleged that Coin Acceptors, Inc. (Coinco) infringed two patents relating to technology for authenticating coins used in vending machines. After trial, the district court found Coinco infringed both patents.

During the damages proceedings, Mars sought the lost profits of its wholly owned subsidiary, Mars Electronics International (MEI). Mars had earlier granted a nonexclusive license to MEI in exchange for royalty payments based on MEI's sales of coin vending machines. Mars itself did not make or sell any vending machines covered by the patents.

The district court held that Mars was not able to recover lost profits, because Mars did not sell the relevant products and Mars only had a licensing relationship with MEI. The court did not recognize the lost licensing revenues as "lost profits" and, importantly, did not allow Mars to recover any of MEI's lost profits. MEI was maintained as a separate corporation from Mars, and profits from MEI did not inexorably flow to Mars. Therefore, Mars could not claim MEI's lost profits as its own. In so holding, the court relied on *Poly-America, L.P. v. GSE Lining Technology, Inc.*, 383 F.3d 1303 (Fed. Cir. 2004)—a case in which the Federal Circuit held a plaintiff may not recover the lost profits of a sister corporation.

A unanimous panel of the Federal Circuit affirmed this portion of the district court's order, because the court agreed that MEI's profits did not flow inexorably to Mars. The Federal Circuit acknowledged that MEI's lost sales may have caused other financial harm to Mars in addition to recoverable royalties, but

Mars only sought lost profits and reasonable royalties as damages. *Mars* at *5 (“We have previously recognized that patentees may be entitled to damages above a reasonable royalty on theories entirely distinct from lost profits.”).

The *Mars* decision shows that the allocation of intellectual property in an organization’s structure can affect the recovery of damages. The decision is also a reminder that lost profits and reasonable royalty damages are not the only available forms of damages for patent infringement. Owners of intellectual property should assess whether potential recoveries for infringement are limited by the current allocation of intellectual property.

If you have any questions about any of the issues raised in this Morgan Lewis Intellectual Property LawFlash, or about whether intellectual property is most effectively allocated in your organization, please contact either of the following Morgan Lewis attorneys:

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