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## Recent Bankruptcy Court Ruling Denies Stay Relief For Apple to Litigate Patent Infringement Claims With Eastman Kodak<sup>1</sup>

A recent Southern District of New York bankruptcy court ruling denied two motions filed by Apple Inc. (“Apple”) seeking relief from the automatic stay to continue patent infringement litigation with, and to commence new patent litigation against, Eastman Kodak Company and its affiliated debtors (“Kodak”). In the first motion, the court denied Apple’s request to continue litigation related to the ownership of certain patents, including patents that comprise a significant portion of the multi-billion dollar patent portfolio that Kodak will seek to divest as part of an anticipated sale under section 363 of the Bankruptcy Code later this year. While the court recognized the significance of resolving ownership disputes before a sale occurs, the court rejected Apple’s proposal because it did not propose a process that would resolve promptly the ownership dispute. In the second motion, the court denied Apple’s request to commence new patent infringement litigation related to alleged post-petition conduct because Apple failed to make a sufficient showing regarding the relief sought or its entitlement to such relief.

The court's ruling highlights an interesting tension between a debtor's interest in protecting and maximizing the value of its assets against the concern that third parties' rights and interests in such assets are adequately protected in the bankruptcy process. The ruling also highlights the tension between the need to adjudicate that ownership interest early in a chapter 11 case, and the need to provide debtors with appropriate breathing room under the automatic stay.

### Background

Apple and Kodak have been involved in litigation related to Kodak’s patents for some time. In early 2010, Kodak requested that the International Trade Commission (the “ITC”) investigate whether Apple’s products infringe on Kodak’s patents. Around the same time, Kodak filed a federal civil complaint against Apple in Rochester, N.Y. that alleged patent infringement. Later in 2010, Apple filed its own lawsuit against Kodak, alleging that

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<sup>1</sup> The court’s ruling was issued on the record at a hearing on March 8, 2012 and the court entered orders denying the relief on March 12, 2012. The ruling did not contain findings of fact. All facts contained in this Alert Memo are based on the parties’ pleadings or the hearing transcript.

Kodak was not the proper owner of certain Apple technology, including ownership to U.S. Patent No. 6,292,218 (the “‘218 Patent’).<sup>2</sup> Apple asserts that contracts made between Apple and Kodak dating back to the early 1990s (when the parties worked together to develop intellectual property and digital cameras) evidence Apple’s ownership of certain Kodak technology. All of these claims are now part of the same lawsuit (the “Existing Patent Litigation”), which has been stayed by the federal court in Rochester, N.Y. until a determination from the ITC is made. Kodak also has commenced several patent infringement lawsuits against other third parties.

In early 2012, Kodak filed for bankruptcy in the United States Bankruptcy Court for the Southern District of New York. Kodak obtained debtor-in-possession financing that requires it to divest certain patent assets through a sale under section 363 later this year.

Shortly after the bankruptcy petition was filed, Apple filed the two instant motions for relief from the automatic stay provided under section 362 of the Bankruptcy Code. Apple’s first motion sought stay relief so Apple and Kodak could continue the Existing Patent Litigation relating to inter alia the ownership of the ‘218 Patent (the “‘218 Stay Motion’”). Apple’s second motion sought stay relief so Apple could file a new complaint with the ITC (the “ITC Complaint”) and a companion civil complaint in federal district court (the “Companion Civil Complaint,” and with the “ITC Complaint,” the “New Infringement Complaints”) related to Kodak’s alleged post-petition patent infringement of Apple’s patents (the “ITC Stay Motion,” and with the ‘218 Stay Motion, the “Stay Motions”).

The court denied each Stay Motion independently, and our analysis is separated into a discussion of (1) the ‘218 Stay Motion and (2) the ITC Stay Motion.

### The Bankruptcy Court’s Ruling

#### 1. The ‘218 Stay Motion

In support of the ‘218 Stay Motion, Apple offered a process for resolving promptly the Existing Patent Litigation by seeking a venue transfer to the United States District Court for the Southern District of New York. Apple argued inter alia that “cause” exists to lift the stay and seek a transfer because (1) the Southern District has expertise in patent law issues and can conduct a jury trial, (2) obtaining full resolution of the Existing Patent Litigation is critical to Kodak, in part because it will impact the section 363 sale (the ‘218 Patent would likely be included in the section 363 sale), and (3) continuing the Existing Patent Litigation in the Southern District will not interfere with the administration of the chapter 11 cases.

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<sup>2</sup> The ‘218 Patent generally claims a digital camera capable of capturing an image while previewing the scene to be captured on an LCD screen.

In response, Kodak agreed that resolution of Apple's ownership claims must be resolved promptly, but argued that the bankruptcy court – and the bankruptcy court alone – should resolve the dispute. Apple also argued that “cause” did not exist to lift the stay because Apple failed to show prejudice from a bankruptcy court resolution, and because inter alia (1) Apple has always contended that the ownership dispute is not a question of federal patent law, (2) multiple civil actions are distracting for Kodak in the early stages of the case, and (3) the Existing Patent Litigation has been stayed, which undercuts any judicial economy concern.

Against this backdrop, the court denied the ‘218 Stay Motion, noting that:

- Although it is unclear if the ‘218 Stay Motion seeks relief to resolve all matters in the Existing Patent Litigation, the court assumes the dispute centers on the ownership of the ‘218 Patent.
- The ownership dispute is an important matter in Kodak's bankruptcy case.
- Apple's proposed relief would not result in prompt resolution because it is dependent on many factors, including a timely motion to unfreeze the Existing Patent Litigation, a further motion to transfer venue to the District Court in the Southern District, and other uncertainties such as future amendments to the pleadings.
- It is not certain, at least at this stage in the case, what determination must be made before the patents can be sold as part of the section 363 sale.
- The court has not considered alternative resolutions, but if this matter requires quick resolution, the parties should develop procedures to resolve critical ownership issues.
- The resolution of these disputes could be accomplished without a waiver (1) of any jury trial right or (2) a claim that a district court could withdraw the bankruptcy reference as to the ownership dispute.

In denying the ‘218 Stay Motion, the court makes clear that Apple's strategy of seeking to transfer the Existing Patent Litigation to the District Court in the Southern District was not adopted because it would not result in prompt resolution of the dispute. For now, the court left it to the parties to agree on procedures for a quick resolution of the critical issues.

## 2. The ITC Stay Motion

With the ITC Stay Motion, Apple sought authority (1) to file the ITC Complaint, which is a requirement for the ITC to initiate an investigation into the alleged infringing

activity, and which could ultimately result in importation and customs restrictions for infringing products, and (2) to file the Companion Civil Complaint, which would seek injunctive relief against ongoing post-petition infringement. Apple alleged that it owns a number of valuable patents relating to various aspects of hardware and software used to implement photo and device management, and that Kodak continues to infringe on those patents in the course of its post-petition operations.

Apple made three principal arguments in support of the ITC Stay Motion. First, Apple argued that ITC investigations are excepted from the automatic stay because the ITC exercises a “police and regulatory power” as understood under section 362(b)(4) of the Bankruptcy Code.<sup>3</sup> Specifically, Apple relied on United States Int’l Trade Comm. v. Jaffe, 433 B.R. 538 (E.D. Va. 2010), for the proposition that ITC proceedings fall within the “police and regulatory power” exception because the ITC is not acting for its own pecuniary interest. Second, Apple argued that the automatic stay does not apply because the infringing activity occurred post-petition. Third, Apple argued that, should the automatic stay apply, “cause” exists to lift the stay because inter alia (1) the ITC is a specialized tribunal, (2) the proposed ITC investigation would not prejudice Kodak’s creditors, and (3) the ITC investigation will facilitate the resolution of issues critical to both Apple and Kodak.

In response, Kodak argued that (1) Apple failed to satisfy its burden of proof by failing to provide the court with sufficient detail as to what patents Kodak allegedly infringed, (2) ITC proceedings commenced post-petition by private parties do not fall within the “police and regulatory power” exception because the ITC would not investigate the conduct but for the post-petition filing of the ITC Complaint, and (3) in the event the automatic stay does not apply, the court should extend the automatic stay to cover the New Infringement Complaints.

The court denied the ITC Stay Motion, noting that:

- The New Infringement Complaints could have been commenced prior to the bankruptcy petition, which is a requirement for the automatic stay to apply under section 362(a)(1) of the Bankruptcy Code.
- The filing of the Companion Civil Complaint is subject to the automatic stay.
- Apple may file a separate motion for stay relief related to post-petition conduct, but if it does, it is admonished to make clear exactly what it proposes to do with the ITC complaints and what the specific allegations are.

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<sup>3</sup> In relevant part, section 362(b)(4) of the Bankruptcy Codes excepts from the automatic stay “the commencement or continuation of an action or proceeding by a governmental unit . . . to enforce such governmental unit’s . . . police and regulatory power. . . .”

- Apple must identify what patents or other intellectual property rights are at issue and what litigation it wants to commence (or to have the ITC commence) as part of any subsequent stay relief motion (including what conduct Apple wants Kodak to stop).
- The court declined to decide whether filing the ITC Complaint is subject to the automatic stay.

In denying the ITC Stay Motion, the court concluded that companion civil complaints accompanying ITC complaints are subject to the automatic stay if the complaint could have been filed with the ITC before the bankruptcy filing where, as here, the alleged post-petition infringement was effectively a continuation of pre-bankruptcy conduct. Notably, the court did not clarify whether plaintiffs can file complaints with the ITC post-petition, although the court seemed skeptical that such complaints fall within the “police and regulatory power” exception, noting that Apple provided no authority for that proposition. Finally, the court’s ruling makes clear that plaintiffs seeking stay relief for patent infringement claims must provide the court with sufficient factual detail to evaluate the propriety of lifting the stay, including, at a minimum, more precise allegations regarding the intellectual property being infringed.

Given Kodak’s plans to divest its patent assets in the upcoming months and Apple’s continued efforts to protect its alleged interest in certain of those patents, it is likely that these issues will be revisited further by the bankruptcy court in the near future.

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If you have any questions, please feel free to contact any of your regular contacts at the firm or any of our partners and counsel listed under “Bankruptcy and Restructuring” in the “Practices” section of our website ([www.clearygottlieb.com](http://www.clearygottlieb.com)).

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