

REPORT

SUPREME COURT RULES IN *MICROSOFT* CASE THAT ONLY COMPONENTS SUPPLIED FROM THE UNITED STATES AND COMBINED ABROAD, AND NOT FOREIGN-MADE COPIES OF THE COMPONENTS, TRIGGER INFRINGEMENT LIABILITY UNDER 35 U.S.C. §271(f)

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On April 30, in *Microsoft Corp. v. AT&T Corp.*,¹ the United States Supreme Court construed 35 U.S.C. §271(f) to mean that only "the very components supplied from the United States, and not copies thereof, trigger §271(f) liability when combined abroad to form the patented invention at issue." Applying this new construction, the Court held that, because Microsoft did not supply from the United States the tangible software copies actually combined with foreign-made computers to make AT&T's patented invention, Microsoft did not "suppl[y] from the United States" "components" of those computers, and therefore was not liable for patent infringement under §271(f). In so holding, the Court also determined that "software in the abstract," without physical embodiment, was not amenable to "combination" and did not constitute a "component" under §271(f). Electing not to engage in "dynamic judicial interpretation of §271(f)," the Court left it to Congress to consider and close any "loophole" in §271(f) if it finds such action warranted.

By way of brief legal background, under U.S. patent law, the general rule is that no infringement occurs when a machine covered by a U.S. patent ("patented machine") is made and sold in another country. Congress enacted 35 U.S.C. §271(f) as an exception to this general rule and as a response to the Supreme Court's decision in *Deepsouth Packing Co. v. Laitram Corp.*² That case had held that nothing in the U.S. patent law stopped a U.S. manufacturer from making in the United States the parts of a patented

machine, as opposed to the machine itself, and selling those parts to foreign buyers for assembly and use abroad. To close this "loophole," Congress enacted §271(f), which provides that infringement occurs when one "suppl[ies] ... from the United States," for "combination" abroad, one or more of a patented invention's "components."

The Supreme Court's *Microsoft* decision reversed a ruling by the Court of Appeals for the Federal Circuit holding Microsoft liable for patent infringement under §271(f). The Federal Circuit found Microsoft liable for sending Windows computer software from the United States to a foreign manufacturer on a master disk, or by electronic transmission, to be copied, with the copies being installed on computers made and sold abroad.³ In reversing the Federal Circuit, the Supreme Court held that, because Microsoft does not supply from the United States "the copies of Windows actually installed on the foreign computers," Microsoft does not "suppl[y] from the United States" "components" of those computers, and therefore is not liable for patent infringement under §271(f).

This Special Report summarizes the Supreme Court's decision, including the majority opinion by Justice Ginsburg, the concurring opinion by Justice Alito (joined by Justices Thomas and Breyer), and the dissenting opinion by Justice Stevens. It also presents some conclusions and recommendations in view of the decision.

¹ 550 U.S. ___, 82 USPQ2d 1400, 2007 WL 1237838 (2007).

² 406 U.S. 518 (1972).

³ Microsoft conceded that the Windows software, when installed on a computer, enables the computer to process speech in the manner claimed by AT&T's patent.

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I. The Supreme Court Decision

A. Background and Decisions Below

AT&T has a patent claiming a computer for digitally encoding and compressing recorded speech. Microsoft's Windows operating system, when installed in a computer, enables the computer to process speech in the manner claimed by AT&T's patent. Microsoft sells Windows to foreign manufacturers for installation on computers sold abroad. Microsoft sends each manufacturer a master version of Windows, in the form of a master disk or by electronic transmission, which the manufacturer copies locally to generate individual copies. Those copies, not the master version sent by Microsoft, are physically installed on the manufacturers' computers sold abroad.

AT&T filed an infringement action against Microsoft charging Microsoft with liability for domestic U.S. installations of Windows, and under §271(f) for foreign installations of Windows. With respect to the foreign installations of Windows, Microsoft argued that a master disk that is never combined with a computer does not constitute a "component" of an invention under §271(f), and that the foreign-generated copies of Windows actually installed on computers abroad were not "supplie[d] ... from the United States."

AT&T countered that reading §271(f) narrowly to cover only those copies of software actually dispatched from the United States creates a "loophole" for software makers. The district court agreed and held that Microsoft was liable under §271(f). A divided Federal Circuit affirmed. The Federal Circuit majority found AT&T's argument compelling in view of the "remedial nature" of §271(f), stating "[w]ere we to hold that Microsoft's supply by exportation of the master versions of the Windows software -- specifically for the purpose of foreign replication -- avoids infringement, we would be ... permitting a technical avoidance of the statute by ignoring the advances in a field of technology -- and its associated industry practices -- that developed after the enactment of §271(f)."

B. The Majority Opinion

The Supreme Court reversed the Federal Circuit's decision.

The basic question presented to the Supreme Court was: "Does Microsoft's liability extend to computers made in another country when loaded with Windows software copied abroad from a master disk or electronic transmission dispatched from the United States?" In answering this question no, the Court found controlling the facts that (1) the master disk or electronic transmission Microsoft sends from the United States is never itself installed on any foreign-made computer and (2) instead, tangible copies made abroad are used for installation. The Court reasoned: "Because Microsoft does not export from the United States the copies actually installed, it does not 'supp[y] ... from the United States' 'components' of the relevant computers, and therefore is not liable under §271(f) as currently written."

The Court more specifically considered two subsidiary questions. "First, when, or in what form, does software qualify as a 'component' under §271(f)? Second, were 'components' of the foreign-made computers involved in this case 'supplie[d]' by Microsoft 'from the United States'?"

In answer to the first subsidiary question, the Court distinguished between "software in the abstract" and "a tangible 'copy' of software, the instructions encoded on a medium such as a CD-ROM." The Court found that, in order to qualify as a "component" under §271(f), software must be expressed as a "computer-readable 'copy,' e.g., on a CD-ROM," such that it is "amenable to 'combination'" or "combinable." The Court expressly rejected AT&T's argument that "software in the abstract" qualifies as a "component" under §271(f), and stated that "[a]bstract software code is an idea without physical embodiment, and as such, it does not match §271(f)'s categorization 'components' amenable to 'combination.'" Analogizing computer software to a blueprint, the Court further stated that "[a] blueprint may contain precise instructions for the construction and combination of the components of a patented device, but it is not itself a combinable component of that device." In a similar vein, the Court commented that "[a]bstracted from a usable copy, Windows code is intangible, uncombinable information, more like notes of music in the head of a composer than 'a roller that causes a player piano to produce sound,'" as argued by Justice Stevens in dissent (discussed below).

As to the second subsidiary question, the Supreme Court expressly rejected the Federal Circuit majority's analysis that "sending a single copy abroad with the intent

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that it be replicated invokes §271(f) liability for th[e] foreign-made copies." The Court agreed with Federal Circuit Judge Rader, who noted in dissent in the Federal Circuit decision under review that "copying and supplying are separate acts with different consequences -- particularly when the 'supplying' occurs in the United States and the copying occurs in Düsseldorf or Tokyo." Reasoning that "the very components supplied from the United States, and not copies thereof, trigger §271(f) liability when combined abroad to form the patented invention at issue," the Court held that "the copies of Windows actually installed on the foreign computers were not themselves supplied from the United States."⁴

The Supreme Court acknowledged at the outset that "plausible arguments can be made for and against extending §271(f) to Microsoft's conduct." However, throughout its opinion, the Court repeatedly emphasized that U.S. patent law does not generally apply to activities conducted outside the United States. In refusing to give §271(f) the expansive interpretation advocated by AT&T, the Court characterized §271(f) as an exception to the general rule that U.S. patent law does not apply extraterritorially, and expressed the view that any adjustment to its scope should be left to Congress.

C. The Concurring Opinion

Justice Alito (who was joined by Justices Thomas and Breyer) wrote a concurring opinion, which reaches the same result as the Supreme Court majority, but by different reasoning. Under the concurring opinion analysis, §271(f) "components" must be "something physical" and, in order to be capable of being "combined" with other components, they must "remain a part" of the infringing device. Based on this interpretation, the concurring Justices found controlling the fact that "[n]o physical aspect of a Windows CD-ROM -- original disk or copy -- is ever incorporated into the computer itself." According to the concurring

⁴ In view of its holding, the Court did not address Microsoft's argument that a disk shipped from the United States to a foreign manufacturer and actually used by the foreign manufacturer to install Windows on a computer would not give rise to liability under §271(f) if the disk was removed after installation. We nonetheless note that this argument does not address the fact that for some period of time the disk would be in the computer and the infringing combination arguably would have occurred.

opinion, "[b]ecause no physical object originating in the United States was combined with these computers, there was no violation of §271(f)."

The concurring opinion thus substantially differs in its reasoning from the majority opinion, which expressly declined to decide the issue (presented by Microsoft) of whether a disk shipped from the United States and used to install Windows *directly* on a foreign computer would give rise to liability under §271(f) *if* the disk were removed after installation. By contrast, under the analysis set forth in the concurring opinion, it is irrelevant (as Microsoft argued) that the Windows software was not copied *directly* from a master disk or electronic transmission that originated in the United States.

It should be noted that the majority opinion written by Justice Ginsburg, not the concurring opinion written by Justice Alito, establishes the controlling law. It should be further noted that the concurring opinion, like Microsoft's argument discussed above, does not address the fact that for some period of time the disk would be in the computer and the infringing combination arguably would have occurred.

D. The Dissenting Opinion

In dissent, Justice Stevens wrote that "if a disk with software inscribed on it is a 'component,' I find it difficult to understand why the most important ingredient of that component is not also a component." He opined that "unlike a blueprint that merely instructs a user how to do something, software actually causes infringing conduct to occur" and that "[i]t is more like a roller that causes a player piano to produce sound than sheet music that tells a pianist what to do."

In a footnote, the majority opinion rebuts Justice Stevens' dissent by pointing out that "Windows can caus[e] infringing conduct to occur ... only when expressed as a computer-readable copy." The majority opinion also addressed Justice Stevens' music analogy, as discussed above.

II. Conclusions and Recommendations

As the law now stands, "component" has a limited meaning as used in §271(f), *i.e.*, a component must be "tangible" and "combinable." Furthermore, to trigger §271(f) liability, that component must itself be supplied in

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or from the United States and actually installed in an infringing device manufactured outside the United States, *i.e.*, foreign-made copies do not trigger §271(f) liability. Although the issue in *Microsoft* concerned physical embodiments of computer software made from a master disk or electronic transmission, the decision has broader application to other fields, in which a master copy, or a template or mold, is used to make a physical embodiment that is actually installed in a product.⁵

As always, we recommend claiming patentable components themselves, and the things used to make them (such as master copies, templates and molds), as well as combinations including those components. Even though foreign-made copies will not trigger §271(f) liability, the U.S. manufacture and use of patented master copies and the like will trigger liability under §271(a). The patentee could then attempt to recover damages for a manufacturer's U.S. origin §271(a) direct infringement by taking into account the value of the foreign-made copies.

With respect to software inventions, we recommend that patent applicants attempt to obtain claims directed to the program itself, rather than merely to a computer or other device in which the program is installed. In this connection, we note that the Patent Office, under its current policy, allows claims reciting a computer-readable medium that stores the patentee's software program, but does not allow claims reciting a program in an electronic form suitable for electronic transmission.⁶ However, the Patent

Office policy in this regard (*i.e.*, relating to the patentability of electrical signals *per se*) is presently under review in *In re Petrus A.C.M. Nuijten*, pending before the Federal Circuit (Appeal No. 06-1371, argued February 5, 2007). We anticipate that we will issue a Special Report, and/or provide other guidance on this topic, when the Federal Circuit issues its decision in that case.

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⁵ We note that Congress has been actively considering various patent reforms in recent years, and it is unclear when, and whether, Congress will act in a manner that confirms whether §271(f) will stand as is, or will be amended to reach conduct like Microsoft's.

⁶ Thus, competitors may avoid literal infringement of currently issuing patents by transmitting a master copy of the patented program electronically. It is, however, beyond the scope of this report whether the electronic version of the program would be deemed an equivalent under the doctrine of equivalents.