SCC provides clarity on accounting of profits remedy in patent infringement

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On November 18, 2022, the Supreme Court of Canada (SCC) released its much-awaited decision in the case of *Nova Chemicals Corporation v. Dow Chemical Co*.

What you need to know

- The SCC dismissed the appeal by Nova Chemicals Corp. (Nova) in an 8-1 decision.
- This case considered accounting of profits as a remedy for patent infringement and provided some much-needed guidance on how to determine if a non-infringing option exists, and whether to use it in the calculation of the profits to be disgorged by the infringer.
- The SCC upheld the award of springboard profits to Dow Chemical Co. (Dow) for Nova's infringement.

Background

In 2014, a patent owned by Dow, entitled "Fabricated Products Made From Ethylene Polymer Blends", was found by the Federal Court (the Court) to be valid and infringed by Nova. These findings were upheld by the Federal Court of Appeal (the Court of Appeal) in 2016. A reference to determine the quantum of the award, either through an accounting of Nova's profits or damages sustained by Nova's infringement, was commenced. Dow elected to recover Nova's profits, and the Court rendered its decision on these issues in 2017, which was upheld by the Court of Appeal in 2020.

At the trial level, a number of issues were considered, such as the calculation of a reasonable royalty for the period after which the patent was published but before it issued. Of particular interest was the Court's determination of the quantum of profits to be disgorged. This decision was also the first award of springboard profits in a patent infringement case in Canada. Springboard profits or damages are causally attributable to the infringement that occurred during the patent term, but that arise following expiry of the patent.

The Court of Appeal ultimately upheld the Court's determination but took the opportunity to set out the principles governing an accounting of profits as a remedy for patent infringement. In particular, the Court of Appeal noted that the purpose behind an accounting of profits is to disgorge the profits made by the infringer as a result of the infringement. The Court of Appeal also noted that reducing the quantum of recovery determined in accordance with the proper principles on the basis that it is "enormous" is not a judicial response. Ultimately, the Court of Appeal found that the Court selected the "full costs" or "absorption" method on an incorrect basis, but reached the correct outcome in deducting costs and upheld the Court's decision.

SCC decision

The SCC started from the principle that "an accounting of profits requires that a party who infringes a patent (the infringer) disgorge all the profits they gained that are causally attributable to the invention." (para 1)

The SCC briefly summarized the monetary remedies available in patent law: reasonable royalty, damages, and an accounting of profits. The Court then briefly summarized the potential methods that can be used to calculate profits: differential costs, full costs, and differential profits.

Accounting of profits

The SCC set out a three-step test to conceptualize an accounting of profits:

> "Step 1: Calculate the actual profits earned by selling the infringing product — *i.e.*, revenue minus (full or differential) costs.
>
> Step 2: Determine whether there is a non-infringing option that can help isolate the profits causally attributable to the invention from the portion of the infringer's profits not causally attributable to the invention — *i.e.*, differential profits. It is at this step that judges should apply the principles of causation. Causation "need not be determined by scientific precision: it is 'essentially a practical question of fact which can best be answered by ordinary common sense'" [citations omitted].
>
> Step 3: If there is a non-infringing option, subtract the profits the infringer could have made had it used the non-infringing option from its actual profits, to determine the amount to be disgorged." (para 15)

The principal issue on the appeal was the clarification of what would constitute a non-infringing option. The SCC did not address whether the full or differential costs method should be used in Step 1. The overarching theme of the SCC's decision is that a court must determine profits causally attributable to the invention.

However, the SCC did confirm that in Step 1, the patentee takes the infringer as they find them. Only **actual** revenues and costs are to be considered. This may mean that the infringer earned more or less profit by infringing than the patentee would have or could have but it is what was actually earned that is to be considered at this step.

Non-infringing option

The SCC refused to deduct theoretical profits that could have been earned on a non-infringing option, stating that a "non-infringing option helps courts isolate the profits causally attributable to the invention from profits that arose at the same time the infringing product was used or sold, but which are not causally attributable to the invention." (para 3)

Nova argued that the SCC in *Schmeiser* held that the profits from the 'best non-infringing option' should be deducted from the infringing profits. Nova further argued that the 'best non-infringing option' is synonymous with the 'most profitable' alternative option; arguing that, had it not used its ethylene in the infringing plastic product, it would have used it to make polyethylene plastics that it could have sold for profit. Thus, Nova argued those theoretical profits should be deducted. Justice Côté in dissent agreed with this principal. However, the majority of the SCC disagreed.

The SCC held that an accounting of profits is a remedial tool designed to protect the patent bargain. It ensures that infringers are deterred - but not punished - for infringement. The profits earned by using the patentee's property rightly belong to the patentee, and thus should be disgorged.

The SCC reiterated that non-infringing options are often used where the infringement provides a more profitable manner in which to commercialize the good than without infringement.

However, a non-infringing option is not the "infringer's "most profitable" alternative sales product that it "would have" and "could have" sold had it not infringed." (para 58). The idea that an accounting of profits is designed to ensure the infringer ends up no worse off than had they not infringed is incorrect. Furthermore, such an approach would undermine the patent bargain. It would create a form of business insurance for infringers, which is not the purpose of an accounting of profits. It would also provide no incentive not to infringe. In addition, it would advantage bigger infringers with diverse product lines and disproportionately disadvantage smaller businesses, which does not accord with the principles of equity.

The establishment of a non-infringing option is a question of fact with no strict rules. It need not be a strict market substituted. The onus, however, is on the infringer "to adduce sufficient evidence to satisfy the court that the profits from its infringing product arose by virtue of features other than the patentee's invention and that there is a non-infringing option that can help the courts isolate this value". (para 67)

Springboard profits

The SCC also upheld the award of springboard profits, holding that they are an extension of the principle that profits causally attributable to the infringement.

The SCC confirmed springboard profits are legally permissible. Similar to springboard damages, "an infringer that begins selling the invention before the patent expires interferes with the patentee's right to build sales capacity and market share in the absence of competition. This can reduce the patentee's post-patent-expiry profits." (para 80) As a result of pre-expiry infringement, the infringer uses its sales capacity and market share to earn profits it would not otherwise have earned. This is unfair to third parties who wait until the patent expires to compete with the patentee.

The SCC held that the need to disgorge springboard profits is a factual question: “are there any profits earned post-patent-expiry that are causally attributable to infringement of the invention, during the period of patent protection?” (para 84)

Conclusion

The SCC dismissed the appeal and held that Dow was entitled to its costs throughout. Now that the SCC has provided its guidance as to the proper approach to a determination of an accounting of profits, it will fall to the courts to apply these principles to the facts before them in future cases.

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