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10 SUPERIOR COURT OF THE STATE OF CALIFORNIA

11 COUNTY OF SANTA CLARA

12  
13 TREND MICRO, INCORPORATED, a  
California corporation, and TREND MICRO  
INCORPORATED, a Japanese corporation,

14 Plaintiffs,

15 v.

16  
17 FORTINET, INC., a Delaware corporation.

18 Defendant.

Case No.: 1:09-cv-149262

**FORTINET, INC.'S  
MEMORANDUM OF POINTS  
AND AUTHORITIES IN  
SUPPORT OF ITS  
OPPOSITION TO PLAINTIFFS'  
DEMURRERS TO FORTINET'S  
THIRD AFFIRMATIVE  
DEFENSE**

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26 PUBLIC VERSION  
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1 This is Fortinet, Inc.'s opposition to the plaintiffs' (collectively, Trend's) general and  
2 special demurrers to Fortinet's Third Affirmative Defense.

### 3 INTRODUCTION

4 For more than forty years, the United States Supreme Court has held that patent  
5 licensees who learn that the patents they are licensing are invalid not only *may*, but *should*,  
6 challenge the patents in court, in order to protect both themselves and the public from  
7 funneling money to a spurious monopoly. *Lear, Inc. v. Adkins*, 395 U.S. 653, 674 (1969).  
8 *Lear* recognized the "importan[ce] to the public that competition should not be repressed by  
9 worthless patents." *Lear*, 395 U.S. at 664.

10 Trend, which has a history of aggressively asserting its patents, entered into a patent  
11 license with Fortinet in 2006 under which Fortinet has paid Trend ██████ of dollars in  
12 royalties. In 2008, compelling evidence came to light that Trend's '600 patent was invalid,  
13 because it was invented earlier by someone else. A separate Trend licensee brought this  
14 evidence to the attention of the International Trade Commission. Based on the evidence, an  
15 ITC staff attorney, charged with advocating the public interest, concluded that Trend's '600  
16 patent was invalid. Trend quickly settled the ITC matter and the finding never went any  
17 further. (Trend's other patent, the closely-related '943 patent, was not at issue in the ITC  
18 proceeding but covers virtually the same technology and is also undermined by the newly-  
19 discovered evidence.)

20 Fortinet understandably does not want to pay ██████ of additional dollars in patent  
21 royalties for invalid patents. Heeding *Lear*, it brought a federal-court challenge to Trend's  
22 patents. Fortinet also stopped paying royalties, as required in a *Lear* challenge. *See*  
23 *Studiengesellschaft Kohle, M.B.H. v. Shell Oil Co.*, 112 F.3d 1561, 1568 (Fed. Cir. 1997).

24 For Trend, the patent validity question is gravely consequential. An invalidity  
25 ruling—state or federal—would preclude Trend from asserting the validity of its patents as  
26 to any other party. *See Blonder-Tongue Labs., Inc. v. Univ. of Ill. Found.*, 402 U.S. 313 (1971).  
27 With ██████ of dollars thus on the line, Trend has waged a ferocious battle to shield its  
28 patents from judicial scrutiny. It mounted a multi-pronged challenge to Fortinet's federal-

1 court *Lear* challenge, asserting, among other arguments, that res judicata barred Fortinet's  
2 validity challenge. But Judge Chesney rejected each of Trend's theories.

3 Facing the certainty that the federal court would now examine its patents, Trend  
4 developed a new tack. It covenanted never to sue Fortinet for patent infringement, then  
5 argued that its covenant deprived the district court of federal case-or-controversy  
6 jurisdiction. The district court agreed, and dismissed the case. Having thus won dismissal  
7 of Fortinet's *Lear* challenge on grounds that the *federal* courts could not hear the matter,  
8 Trend now tells *this* Court that *it* cannot hear Fortinet's case either. Worse, the *reason* Trend  
9 gives is the very res judicata theory Judge Chesney rejected in the federal court—the loss of  
10 which prompted Trend to dismiss in the first place.

11 This is not responsible conduct. This is gamesmanship. This Court should overrule  
12 Trend's demurrer, first, because it was already decided by Judge Chesney and is not open  
13 for relitigation. The Court should also overrule Trend's demurrer because it is deeply  
14 flawed on the merits.

15 Was the ITC staff attorney correct? That is the question in this case—and the one  
16 Trend is determined not to let this Court decide. But the Court *must* decide it, in order that  
17 Fortinet and the public may know whether they may cease paying ████████ of dollars to the  
18 owners of an unlawful monopoly.

## 19 BACKGROUND

### 20 A. The Original Skirmish: The 2004 Litigation.

21 In 2004, Trend sued Fortinet in federal district court in Northern California, charging  
22 infringement of its '600 patent. (*See* Trend Micro's Second Amended and Verified  
23 Complaint ("SAC") ¶ 7; Fortinet's Verified Answer to Trend Micro's Second Amended  
24 Complaint ("Answer") ¶ 7.) Simultaneously, Trend initiated an ITC proceeding against  
25 Fortinet, again asserting infringement of its '600 patent. (*See id.*) Trend did not assert its  
26 '943 patent against Fortinet in either proceeding, and to date has not done so.  
27 (*See* Declaration of Alice C. Garber in support of Fortinet's Opposition to Demurrers  
28 ("Garber Decl.") at ¶ 5.) Fortinet asserted the invalidity and unenforceability of Trend's

1 '600 patent in both proceedings. (*See* Trend Micro's Request for Judicial Notice ("TRJN")  
2 Ex. 1 ¶¶ 12-15 and Ex. 2 at 13-16.)

3 The parties settled both cases and entered into a "Settlement Agreement and Patent  
4 License Agreement" ("Agreement"). (*See* SAC ¶ 10; Answer ¶ 10.) The Agreement  
5 provided that Fortinet would pay Trend a very large up-front payment, plus royalties based  
6 on product sales. (*See* SAC, Ex. A ¶¶ 3.1, 3.2, 15-16.) It also provided that "Fortinet makes  
7 no admissions regarding the validity of the '600 Patent . . . ." (*Id.* at § 9.4.) The ITC  
8 proceeding was terminated and the district court case was dismissed with prejudice. (*See id.*  
9 at § 4.2; TRJN Ex. 3.)

10 **B. New Evidence Shows Trend's Patent Is Invalid; Trend Quickly**  
11 **Settles an ITC Action.**

12 After finishing these cases with Fortinet, Trend instituted a new ITC proceeding on  
13 its '600 patent, this time against Barracuda Networks. (*See* TRJN Ex. 4 ¶ 23.) During this  
14 proceeding, Barracuda presented newly-discovered, compelling evidence that the '600  
15 patent was invalid. (*See id.* at ¶¶ 25-26.) That evidence included a product called the "TFS  
16 Gateway," which was on the market before Trend applied for its patent, and which  
17 performed the same functions Trend's patent describes. (*See id.*)

18 Based on an independent review of the evidence, including the TFS Gateway, an ITC  
19 staff attorney concluded that each asserted claim of the '600 patent was invalid. (*See* Garber  
20 Decl. at ¶¶ 3-4.) Soon after, Trend and Barracuda settled the ITC proceeding. (*See id.*)

21 **C. Fortinet Brings a *Lear* Challenge; Trend Asserts *Res Judicata*.**

22 In light of the compelling new evidence of invalidity, as well as new Supreme Court  
23 authority casting further doubt on Trend's patents, Fortinet instituted a *Lear* challenge.  
24 (*See* TRJN Ex. 4.) In *Lear*, the U.S. Supreme Court articulated a strong federal policy  
25 encouraging licensees to challenge bad patents. *Lear*, 395 U.S. at 674. A successful patent  
26 challenger under *Lear* owes no further royalties. *Id.* In the present case, Fortinet paid Trend  
27 an up-front fee of ██████████ to license its patents, plus agreed to pay ██████████ more in  
28 running royalties as more products were sold. (Garber Decl. ¶ 2.) To date, these royalties

1 have totaled an additional [REDACTED]. (*Id.*) Not content with this [REDACTED], Trend  
2 contends a minimum of [REDACTED] of *additional* royalties are or will become due under the  
3 license. (*See id.*) Fortinet believes it unjust and (under *Lear*) *unlawful* for Trend to continue  
4 collecting [REDACTED] of dollars on invalid patents that should never have been issued.

5 Fortinet brought its *Lear* challenge in late 2008, in the Northern District of California,  
6 asserting the invalidity and unenforceability of Trend's patents. (*See* TRJN Ex. 4 ¶¶ 47-48 &  
7 52-53.) Fortinet also cited material differences in its products since the earlier litigation.  
8 (*See* Fortinet, Inc.'s Joinder and Request for Judicial Notice ("FRJN") Ex. 3 ¶ 9.) Trend  
9 moved to dismiss the 2008 lawsuit on the pleadings. (*See* FRJN Ex. 1.) It argued, among  
10 other things, that the dismissal of the 2004 litigation with prejudice barred Fortinet's  
11 validity challenges under the doctrine of res judicata. (*See id.* at 16-20.)

12 **D. Trend Loses Its Res Judicata Challenge; Trend Procures Dismissal of**  
13 **the Federal Litigation.**

14 Judge Chesney denied Trend's motion, ruling that res judicata could not be decided  
15 on the pleadings. (*See* TRJN Ex. 5 at 3-4.) Specifically, Judge Chesney held that the 2004  
16 litigation would not bar Fortinet's patent challenges as long as the products at issue in the  
17 2004 litigation differed materially from those sold by Fortinet today. (*Id.*)

18 Trend responded to this ruling by issuing a covenant not to sue Fortinet for  
19 infringement of the the licensed patents. (*See* SAC ¶ 23.) Based on this covenant, Trend  
20 renewed its motion to dismiss. (*Id.*) It now argued that with patent-infringement claims off  
21 the table, the court lacked federal "case or controversy" jurisdiction. (*See* TRJN Ex. 6 at 2.)  
22 This time Judge Chesney agreed. Noting the lack of diversity jurisdiction, she dismissed the  
23 case without prejudice to its being refiled in state court. (*See id.* at 5 n.4.)

24 **E. Trend Files the Present Lawsuit.**

25 Trend then filed the present state-court action against Fortinet for failure to make  
26 royalty payments. In answering Trend's complaint, Fortinet has reasserted its *Lear*  
27 challenge in its affirmative defense of patent invalidity and/or unenforceability (referred to  
28 interchangeably here simply as "invalidity"). (Answer to SAC at 7:10-11.) Trend now

1 attacks Fortinet's *Lear* challenge under the same res judicata theory it pressed and lost  
2 before Judge Chesney. (*Compare* Trend's Demurrers ("Dem.") 6-13 with Trend's federal  
3 dismissal papers, FRJN Ex. 1 at 16-20 and FRJN Ex. 2 at 7-11 (same).)

#### 4 F. Return of the Parallel Federal Litigation.

5 Trend and Fortinet are now back before Judge Chesney in a federal declaratory-  
6 judgment case filed in January of this year. (*See* FRJN Ex. 3.) Fortinet previously appealed  
7 Judge Chesney's jurisdictional dismissal of the 2008 litigation. (*Id.* at ¶ 32.) During the  
8 briefing of that appeal, Trend cited, as support for Judge Chesney's finding of no case or  
9 controversy, the absence of any allegations or evidence that Trend ever threatened  
10 Fortinet's customers. (*Id.* at ¶ 33.) This was significant because Trend's covenant-not-to-sue  
11 relinquished claims against *Fortinet*, but was silent as to Fortinet's customers. (*See* TRJN  
12 Ex. 6 at 2 (quoting Chen letter).) Fortinet did have evidence of such threats, but these arose  
13 after the dismissal of the district court action and so were not in the record. (*See* FRJN Ex. 3  
14 ¶¶ 26 & 34; FRJN Ex. 4 at 2.) In light of this, Fortinet voluntarily dismissed its appeal and  
15 refiled its case in the district court, this time explicitly including allegations of Trend's  
16 threats to Fortinet's customers. (*See* FRJN Ex. 3 ¶¶ 26-30 & 34-35; FRJN Ex. 4 at 2.)

17 Trend has moved to dismiss this new federal case. (*See* FRJN Ex. 5.) It argues that  
18 notwithstanding the new allegations, the court still lacks a justiciable case or controversy.  
19 (*See id.* at 1-2.) That motion is currently pending before Judge Chesney and is set for  
20 hearing on May 14, 2009. (*Id.* at 4.)

21 In response to Trend's motion to dismiss, Judge Chesney issued an order asking the  
22 parties to brief whether, even if she *does* now have jurisdiction over Fortinet's declaratory-  
23 judgment case, she should exercise her *discretionary* authority to dismiss that case in favor of  
24 *this* proceeding. (*See* FRJN Ex. 5.) That is, Judge Chesney expects *this* Court to be  
25 addressing the validity of Trend's patents. (*See id.* at 2-3.) But of course, by the present  
26 motion, Trend seeks to block just that from happening. (*See* Dem. 6-13.)

27 It is unclear what Judge Chesney will do when informed Trend is seeking to undo  
28 her res judicata decision. What is clear is that there is a strong federal bias against state-

1 court relitigation of federal decisions. The “relitigation” exception to the Anti-Injunction  
2 Act authorizes federal courts to enjoin state-court reconsideration of federal-court  
3 judgments. *See Parsons Steel, Inc. v. First Alabama Bank*, 474 U.S. 518 (1986).

4 **G. Trend’s Dual Strategy.**

5 Evident from the above history is Trend’s dual strategy of extracting ██████ in  
6 royalties from its patents while insulating those patents from judicial review. Trend settled  
7 with Barracuda just after the ITC staff attorney issued his invalidity findings, leaving no  
8 binding decision. (*See Garber Decl.* at ¶ 4.) Trend asserted res judicata to try to block  
9 Fortinet’s 2008 challenge to its patents. (*See FRJN Ex. 1.*) Upon losing that motion, Trend  
10 engineered the dismissal of the 2008 case without prejudice to its being refiled in state court.  
11 (*See TRJN Ex. 6.*) Now that the case is here, Trend argues that “only a federal court can  
12 invalidate a patent.” (Document No. 53 (Trend’s Mem. in Opposition to Fortinet’s Motion  
13 to Stay) at 8:24-9:1.) And Trend renews its rejected res judicata challenge. (Dem. 6-13.)

14 These efforts, as we now show, must fail.

15 **ARGUMENT**

16 **I. TREND PRESSED AND LOST THIS PRECISE RES JUDICATA THEORY**  
17 **BEFORE JUDGE CHESNEY; IT IS BARRED FROM LITIGATING IT**  
18 **AGAIN HERE.**

19 In its motion to dismiss in state court, Trend attempts to resurrect the exact issue it  
20 raised in its motion to dismiss in federal court—whether, at the pleadings stage of a case,  
21 res judicata bars Fortinet’s challenges to the validity and enforceability of Trend’s patents.  
22 Judge Chesney rejected that precise argument in her order denying Trend’s motion to  
23 dismiss. (*See TRJN Ex. 5* at 3-4.) Judge Chesney’s ruling on this issue is final, and bars  
24 Trend from relitigating it here.

25 In contrast to the claim preclusion aspect of res judicata, which bars a second lawsuit  
26 between the same parties on the same cause of action, collateral estoppel (or “issue  
27 preclusion”) forecloses successive litigation of an issue of fact or law “actually litigated and  
28 necessarily decided by a valid and final judgment between the parties . . . .” *Segal v. AT&T*,  
606 F.2d 842, 845 (9th Cir. 1979). A party will be precluded from relitigating an issue where:

1 (1) the issue is identical to an issue that was actually litigated and necessarily decided in the  
2 former proceeding; (2) the prior proceeding ended in a “final judgment,” which “includes  
3 any prior adjudication in the former proceeding that was ‘sufficiently firm’ to be accorded  
4 conclusive effect”; and (3) the party against whom preclusion is sought is the same as, or is  
5 in privity with, the party to the former proceeding. *See Robi v. Five Platters, Inc.*, 838 F.2d  
6 318, 326-27 (9th Cir. 1988); *Border Business Park, Inc. v. City of San Diego*, 142 Cal. App. 4th  
7 1538, 1564 (2006) (noting that, unlike claim preclusion, issue preclusion does not require a  
8 “final judgment”).

9 In determining whether a prior adjudication is “sufficiently firm to be accorded  
10 conclusive effect,” courts consider (1) whether the decision was avowedly tentative;  
11 (2) whether the parties were fully heard; (3) whether the court supported its decision with a  
12 reasoned opinion; and (4) whether the decision was subject to an appeal. *See, e.g., Luben*  
13 *Industries, Inc. v. United States*, 707 F.2d 1037, 1040 (9th Cir. 1983) (citing Restatement  
14 (Second) of Judgments § 13, cmt g); *Border Business Park*, 142 Cal. App. 4th at 1565 (same).

15 Each of the requirements for collateral estoppel is satisfied here. Trend’s present  
16 issue is identical to the one it raised before Judge Chesney: whether, at the pleadings stage  
17 of a case, res judicata may be invoked to bar Fortinet’s validity challenges to Trend’s  
18 patents. (*Compare* FRJN Ex. 1 at 16-20 *with* Dem. 6–13.) That question was actually litigated  
19 and, in fact, extensively briefed by Trend in federal court. (*See* FRJN Ex. 1 at 16-20 and Ex. 2  
20 at 7-11.)

21 In rejecting Trend’s res judicata theory, Judge Chesney supported her decision with a  
22 reasoned opinion that was in no way tentative. (*See* TRJN Ex. 5 at 3-4.) She held that “[t]he  
23 Court cannot, at the pleading stage, determine Fortinet’s claims for declaratory relief [of  
24 patent invalidity and unenforceability] are barred by the doctrine of claim preclusion.” (*Id.*  
25 at 3.) The issue was also necessarily decided—the substantive rights of the parties hinged  
26 on the ruling, and Judge Chesney’s decision allowed the litigation to go forward to its  
27 ultimate judgment. Judge Chesney entered a final, appealable, judgment disposing of the  
28 case on jurisdictional grounds two months later. (*See* TRJN Ex. 6.)

1           Instead of appealing Judge Chesney’s decision, Trend now takes another swing.  
2 Although, as we show below, Trend once again fails on the merits, this Court need not  
3 revisit them. They have been litigated, and conclusively decided, in federal court.

4           **II.       UNDER THE GOVERNING FEDERAL RES JUDICATA STANDARD,**  
5           **FORTINET FACES NO BAR TO ITS VALIDITY CHALLENGE**

6           Trend’s entire res judicata theory rests on its belief that *state* law governs the  
7 preclusive effect of the 2004 litigation. Trend is wrong. While Trend’s demurrer focuses  
8 extensively, and exclusively, on California’s “primary rights” theory of res judicata, *see, e.g.,*  
9 Dem. at 6-12, controlling Supreme Court and California precedent make federal standards  
10 the exclusive measure of the finality of a prior federal-court judgment. Under the federal  
11 standard, the 2004 litigation does not bar Fortinet’s invalidity defense. Accordingly,  
12 although Judge Chesney’s ruling is final and preclusive whether it was right or wrong, in  
13 fact the ruling was 100% correct.

14           **A.       Federal Law, Not State Law, Governs the Scope of Res Judicata Here.**

15           Federal, not state, standards govern the preclusive effect of the 2004 litigation:  
16 “California follows the rule that the preclusive effect of a prior judgment of a federal court  
17 is determined by federal law, at least where the prior judgment was on the basis of federal  
18 question jurisdiction.” *Butcher v. Truck Ins. Exch.*, 77 Cal. App. 4th 1442, 1452-53 (2000); *Levy*  
19 *v. Cohen*, 19 Cal. 3d 165, 172-73 (1977); *Louie v. BFS Retail and Commercial Operations, LLC*, 178  
20 Cal. App. 4th 1544, 1553-54 (2009) (although the parties “devote much of their appellate  
21 briefs to arguing about primary right theory,” “where a prior federal judgment was based  
22 on *federal question* jurisdiction, the preclusive effect of the prior judgment of a federal court  
23 is determined by federal law.” (emphasis in original)).

24           This is not just California’s rule. The United States Supreme Court has long held that  
25 “[t]he preclusive effect of a federal-court judgment is determined by federal common law.”  
26 *Taylor v. Sturgell*, 553 U.S. 880, 128 S. Ct. 2161, 2171 (2008); *Semtek Int’l, Inc. v. Lockheed Martin*  
27 *Corp.*, 531 U.S. 497, 507-08 (2001). *Accord Aerojet-General Corp. v. Askew*, 511 F.2d 710, 715  
28 (5th Cir. 1975).

1 The mandate that federal law governs the preclusive effect of a federal court's  
2 decision stems directly from the Constitution's Full Faith & Credit Clause, and its  
3 implementing legislation. *Levy*, 19 Cal. 3d at 172-73. See U.S. Const. art. IV § 1; 28 U.S.C. §  
4 1738; see generally, Ronan E. Degnan, *Federalized Res Judicata* 85 Yale L. J. 741 (1976).

5 Additionally, here a *second* Constitutional mandate requires application of federal  
6 standards. Under the Supremacy Clause, when state courts hear questions implicating  
7 federal law (such as patent validity), and there is a need for a "uniform rule of decision,"  
8 federal courts have "paramount power to fashion such a rule." *Farmland Irrigation Co., Inc.*  
9 *v. Dopplmaier*, 48 Cal. 2d 208, 219 (1957). *Accord Sears Roebuck & Co. v. Stiffel Co.*, 376 U.S.  
10 225, 229 (1964) (citing *Sola Elec. Co. v. Jefferson Elec. Co.*, 371 U.S. 173, 176 (1942) (state law  
11 conflicting with patent policy "must yield" under Supremacy Clause)); *Rhone-Poulenc Agro,*  
12 *S.A. v. DeKalb Genetics Corp.*, 284 F.3d 1323, 1327-28 (Fed. Cir. 2002) (state law preempted  
13 when there is a need for a "uniform body of federal law" on a patent-related question). The  
14 Federal Circuit has expressly held that there *is* a "clear need for uniformity and certainty in  
15 the interpretation of *Lear*" when it comes to res judicata challenges. *Foster v. Hallco Mfg. Co.,*  
16 *Inc.*, 947 F.2d 469, 475 (Fed. Cir. 1991).

17 Despite this overwhelming authority, a line of state-court decisions has strayed from  
18 the settled rule. *Louie*, 178 Cal. App. 4th at 1553-54 & n.5 (noting the stray California  
19 decisions but holding that federal law nonetheless governs). These stray cases trace back to  
20 a decision in which the court applied state law reflexively, without noticing the choice-of-  
21 law question before it. See *Agarwal v. Johnson*, 25 Cal. 3d 932, 954 (1979), *overruled on other*  
22 *grounds by White v. Ultramar*, 21 Cal. 4th 563 (1999)). *Agarwal* did not cite the California  
23 Supreme Court's decision just two years earlier in *Levy*, which *had* considered the choice-of-  
24 law question, and which relied on the "[f]ull faith and credit" owed to federal-court  
25 judgments to conclude that such judgments "ha[ve] the same effect in the courts of this state  
26 as [they] would have in a federal court." *Levy*, 19 Cal. 3d at 172-73. A subsequent California  
27 Court of Appeal decision then followed *Agarwal* rather than *Levy*. *Gamble v. General Foods*  
28 *Corp.*, 229 Cal. App. 3d 893, 898-99 (1991). Several subsequent Court of Appeal decisions

1 then followed *Gamble*. E.g., *Acuña v. Regents of the Univ. of California*, 56 Cal. App. 4th 639,  
 2 648 (1997); *City of Simi Valley v. Superior Court*, 111 Cal. App. 4th 1077, 1082-83 (2003).

3 These are the cases Trend cites in urging application of California's "primary rights"  
 4 res judicata analysis. (Dem. at 9.) But the cases do not apply here, for at least three reasons.  
 5 First, *Gamble*, *Simi Valley*, and *Acuña* are all Court of Appeal decisions; *Levy*, a California  
 6 Supreme Court decision, is controlling. *Levy* should also be read to control *Agarwal*: *Levy*  
 7 was the first-decided case, it identified the choice-of-law question, and it recognized and  
 8 applied the Full Faith and Credit mandate. *Agarwal* never recognized the choice-of-law  
 9 question, never considered the Full Faith and Credit mandate, and never cited (much less  
 10 overruled) *Levy*.

11 Second, none of Trend's cited cases required the state court to decide a *federal issue* as  
 12 to which there was a need for *nationwide uniformity*. So none of Trend's cited cases triggered  
 13 the *separate* mandate, imposed by the Supremacy Clause, that federal standards govern and  
 14 preempt contrary state law. Cf. *Foster*, 947 F.2d at 475; *Farmland Irrigation*, 48 Cal. 2d at 219.  
 15 Third, and dispositively, none of Trend's cited authority trumps the U.S. Supreme Court.  
 16 See *Semtek*, 531 U.S. at 507-08 ("[W]e have long held that States cannot give [federal-court  
 17 judgments in federal-question cases] merely whatever effect they would give their own  
 18 judgments, but must accord them the effect that this Court prescribes.") (citing cases);  
 19 *Taylor*, 128 S. Ct. at 2171.

20 **B. Application of the Federal Res Judicata Standard Demonstrates That**  
 21 **the 2004 Litigation Does Not Bar Fortinet's Validity Challenge.**

22 **1. The Federal Claim Preclusion Standard.**

23 Under the federal doctrine of claim preclusion, a judgment on the merits will bar a  
 24 plaintiff from maintaining another action on the same claim. *Foster*, 947 F.2d at 478.  
 25 Additionally, the judgment "bars the subsequent application of all defenses that could have  
 26 been asserted in a previous action between the same parties *on the same cause of action . . .*"  
 27 *Littlejohn v. U.S.*, 321 F.3d 915, 919-920 (9th Cir. 2003) (emphasis added). Claim preclusion  
 28 thus turns on whether the current litigation involves the "same claim" (or cause of action)

1 as the prior proceeding. *Foster*, 947 F.2d at 478.

2 In determining whether a subsequent lawsuit presents the “same claim,” the Federal  
3 Circuit looks to whether the facts “giving rise to the suit” arise from the same transaction or  
4 series of connected transactions as the prior litigation. *See id.* (citing Restatement (Second)  
5 of Judgments § 24(1)). *Accord Adv. Cardiovascular Sys., Inc. v. Scimed Life Sys., Inc.*, 989 F.  
6 Supp. 1237, 1244 (N.D. Cal. 1997) (concluding Ninth Circuit test also focuses on “same  
7 transaction”).

8 **2. Under the Federal Standard, Whether Res Judicata Applies Depends**  
9 **on Whether Fortinet’s Current Products Are “Essentially the Same**  
10 **As” Those at Issue Previously, a Fact Question Incapable of**  
11 **Resolution on the Pleadings.**

12 The Federal Circuit has repeatedly held that where, as here, the parties’ prior patent  
13 infringement case has been settled and dismissed with prejudice, the availability of a  
14 subsequent *Lear* challenge depends on a key fact question, one not ascertainable in a  
15 demurrer: whether the defendant’s current products “are essentially the same” as, or  
16 instead are “materially different” from, those at issue in the prior litigation. *Foster*, 947 F.2d  
17 at 479-80 (Fed. Cir. 1991). *Accord, e.g., Hallco Mfg. Co. v. Foster*, 256 F.3d 1290, 1297 (Fed. Cir.  
18 2001). Thus, contrary to Trend’s contentions, *see* Dem. 12-13, *Foster* and *Hallco* explicitly  
19 authorize validity challenges after settlements of prior infringement actions. *Foster*, 947 F.2d  
20 at 479-80; *Hallco*, 256 F.3d at 1297-98.

21 In *Foster*, the parties settled a prior patent infringement dispute with a royalty-  
22 bearing patent license, and terminated the litigation with a consent judgment. Four years  
23 later *Foster*, the accused infringer, created new models of his products. He notified the  
24 patentholder, *Hallco*, about the new products. He said the new products were not  
25 infringing and should thus not bear royalties. *Hallco* disagreed. It demanded royalty  
26 payments. In response, *Foster* filed a declaratory judgment action, seeking, among other  
27 relief, declarations that *Hallco*’s patents were invalid and unenforceable. That is, *Foster*  
28 brought a *Lear* challenge to the validity of the *Hallco* patents. *See Foster*, 947 F.2d at 472-73.

Hallco objected. Exactly as Trend has done here, *Hallco* argued that res judicata

1 barred Foster's *Lear* challenge. *Id.* at 473. Hallco's theory, like Trend's, was that the  
2 settlement and termination of the earlier lawsuit barred Foster from a subsequent challenge  
3 to the validity of its patents. But the Federal Circuit disagreed. Noting that claim  
4 preclusion only applies when the parties seek to bring another action on the same "claim,"  
5 the court said that the question before it turned on "whether this suit presents the same  
6 claim (cause of action) as that of *Foster I* [the parties' previous litigation]." *Id.* at 478. In  
7 answering that question, the court made the key observation that "[a]n essential fact of a  
8 patent infringement claim is *the structure of the device or devices in issue.*" *Id.* at 479 (emphasis  
9 added). The court held, in other words, that a "claim" in this context is defined by a specific  
10 set of accused products. Where the *products* are different, the *claim* is different. Defenses  
11 barred by a previously settled "claim" are *not* barred for purposes of the new one. Thus the  
12 court concluded that "for claim preclusion to apply here, *the devices in the two suits must be*  
13 *essentially the same.*" *Id.* at 479-80 (emphasis added) (also noting that the party seeking  
14 preclusion has the burden of proof). *Accord Hallco*, 256 F.3d at 1297-98.

15       Precisely so here. Trend cannot succeed with its res judicata challenge if Fortinet's  
16 redesigned products are not "essentially the same as" the products Trend accused in the  
17 2004 litigation. That, of course, is a fact-intensive inquiry wholly improper for resolution by  
18 demurrer. Accordingly, Trend's res judicata challenge must fail.

19               **3. Trend's Breach-of-Contract Claim Is a Different "Claim" Than the**  
20               **Patent Infringement Cause-of-Action It Asserted in the 2004**  
21               **Litigation.**

22       Res judicata is also inapplicable to Fortinet's defenses for an additional reason. Quite  
23 apart from the difference in products at issue in this litigation, Trend's claim for breach of  
24 contract arises out of a different "nucleus of facts" than the patent infringement claim Trend  
25 pressed in the 2004 litigation. Trend's current breach-of-contract claim is not the same  
26 "claim" as the infringement claim it asserted in 2004. *Cf. Foster*, 947 F.2d at 478-479. This is  
27 necessarily so, or Trend would itself be barred by res judicata from suing for breach of the  
28 contract. Fortinet's defenses are thus not barred by res judicata.

1                   **C. Issue Preclusion Does Not Bar Fortinet’s Defenses**

2                   Nor does issue preclusion bar Fortinet’s defenses.<sup>1</sup> As discussed in Part I, issue  
3                   preclusion forecloses the relitigation of issues that were *actually litigated* and *necessarily*  
4                   *decided* in a prior proceeding. *See Foster*, 947 F.2d at 480 (citing Restatement (Second) of  
5                   Judgments § 27). Here, the parties’ 2004 litigation was settled and dismissed before actual  
6                   litigation or determination of *any* issue related to the validity or enforceability of Trend’s  
7                   patents. (*See* FRJN Ex.6.) Thus, Fortinet is not collaterally estopped from challenging the  
8                   validity of Trend’s patents.

9                   **III. EVEN UNDER TREND’S STATE-LAW STANDARD, THE RESULT IS THE**  
10                   **SAME**

11                   **A. Claim-Preclusion Law Does Not Apply to a Defense That Cannot**  
12                   **Also Be Asserted as a “Cause of Action.”**

13                   Claim preclusion does not bar Fortinet’s invalidity defense even under Trend’s  
14                   preferred state-law standard. Claim preclusion bars the splitting of a “cause of action.”  
15                   *See Mycogen Corp. v. Monsanto Co.*, 28 Cal. 4th 888, 904 (2002). A “cause of action” is the  
16                   means by which a party seeks relief for an injury. *See id.* Patent invalidity is not a “cause of  
17                   action”; rather, because it cannot be asserted for the recovery of damages or other relief, it  
18                   can only be a defense to patent infringement, or to a royalty obligation. *See Foster*, 947 F.2d  
19                   at 479; *Lear*, 395 U.S. at 675-76. Just as there is no cause of action for “waiver” or “release,”  
20                   there is no cause of action for invalidity. Nor does Fortinet’s previous assertion of invalidity  
21                   as a declaratory judgment “plaintiff” turn the defense into a cause of action. *Foster*, 947 F.2d  
22                   at 479. *Claim* preclusion simply does not apply here, and Trend’s demurrer must be

23                   <sup>1</sup> Trend does not seriously argue otherwise. Instead, in a footnote it cites a dictum  
24                   from *Alpha Mechanical*, Dem. 8 n. 5., which this Court should decline to embrace. First, as  
25                   noted above, the preclusive effect of a prior settlement on a subsequent *Lear* challenge is  
26                   governed exclusively by federal law. *See* Part II.A. And second, *Alpha Mechanical’s* dictum  
27                   is at odds with the universally-understood rule that issue preclusion, as opposed to claim  
28                   preclusion, bars only those issues actually litigated and necessarily decided. *See, e.g.,*  
*Cromwell v. Sac County*, 94 U.S. 351, 353 (1876) (“[W]here the second action between the  
same parties is upon a different claim or demand, the judgment in the prior action operates  
as an estoppel *only* as to those matters in issue or points controverted, upon the  
determination of which the finding or verdict was rendered.”) (emphasis added).  
*Accord Clark v. Leshner*, 46 Cal. 2d 874, 880 (1956).

1 overruled. See *Nakash v. Super. Ct.*, 196 Cal. App. 3d 59, 69-70 (1988).

2 Trend's cited cases, *Alpha Mechanical* and *Torrey Pines*, only reinforce this conclusion.  
3 Both cases involved parties who dismissed with prejudice prior *causes of action* and then  
4 attempted to re-assert those same causes of action as *affirmative defenses* in subsequent  
5 matters. Fortinet is and was asserting a *defense* that cannot be a cause of action.

6 *Alpha Mechanical* involved a defendant (RAS) attempting to assert as affirmative  
7 defenses several causes of action for damages that had been brought in a previously-  
8 dismissed case. RAS's previous claims were for breach of contract and negligence causing  
9 property damage, and damage to the work of other trades. RAS's "affirmative defenses  
10 likewise sought to hold Alpha responsible for wrongful and negligent contract performance  
11 resulting in those damages." *Alpha Mechanical, Heating & Air Conditioning, Inc. v. Travelers*  
12 *Casualty & Surety Co.*, 133 Cal. App. 4th 1319, 1332 (2005). The court barred RAS from  
13 recasting (i.e., "splitting") its causes of action, previously asserted as a plaintiff, into  
14 affirmative defenses as a defendant. *Id.*

15 Similarly, in *Torrey Pines* the plaintiff guarantor (White) sued the Torrey Pines Bank,  
16 asserting "causes of action for breach of fiduciary duty, breach of the covenant of good faith  
17 and fair dealing, negligent misrepresentation and negligence." *Torrey Pines Bank v. Superior*  
18 *Court*, 216 Cal App. 3d 813, 817 (1989). White dismissed that action with prejudice and  
19 asserted the "identical facts as affirmative defenses" as a defendant in a later action against  
20 the Bank. *Id.* at 821-22. The court found the prior dismissal with prejudice barred White's  
21 subsequent affirmative defenses based on the previously-dismissed causes of action. *Id.*

22 *Alpha Mechanical* and *Torrey Pines* thus illustrate that claim preclusion bars only the  
23 splitting of a cause of action. Because patent invalidity is not a cause of action, these cases  
24 do not help Trend.

25 **B. Even Applying a Primary Rights Analysis to Fortinet's Invalidity**  
26 **Defense, the Defense Is Not Barred.**

27 Even if one were to contort California's "primary right" standard to apply to  
28 Fortinet's invalidity defense, the defense would still not be barred, because separate

1 “primary rights” are at issue in the two lawsuits. Trend suggests that the primary right  
 2 Fortinet asserted in the 2004 litigation, and again here, is the right “to be free from the  
 3 statutory monopoly granted to Trend Micro in the ‘600 patent on the ground that the patent  
 4 is invalid and unenforceable.” (Dem. 10.) This characterization misses the critical link  
 5 between patent law and the “primary rights” at stake here. As noted above, the Federal  
 6 Circuit has established that each set of materially-different products defines a different  
 7 claim for purposes of res judicata. *Foster*, 947 F.2d at 480; *Hallco*, 256 F.3d at 1297. Whereas  
 8 Fortinet’s “primary right” in the 2004 litigation was the right to produce *a specific set of*  
 9 *products* free of Trend’s unlawful monopoly, Fortinet’s primary right in *this* litigation is its  
 10 right to produce a *separate, and materially different, set of products* free of Trend’s unlawful  
 11 monopoly. *See id.* Accordingly, claim preclusion would not bar Fortinet’s defense here,  
 12 even under the theory of primary rights.<sup>2</sup>

13 **CONCLUSION**

14 For all of these reasons, Fortinet respectfully requests that the Court overrule Trend’s  
 15 demurrer. To the extent the Court sustains Trend’s demurrer on grounds of lack of  
 16 specificity, Fortinet requests leave to amend.

17 Respectfully Submitted,

18 Dated: April 16, 2010

THE BERNSTEIN LAW GROUP, P.C.

19  
 20 By: \_\_\_\_\_ /s/  
 21 Marc N. Bernstein  
 22 Attorneys for Defendant  
 23 FORTINET, INC.

24  
 25 \_\_\_\_\_  
 26 <sup>2</sup> Fortinet agrees to amend its third affirmative defense to provide the specificity  
 27 Trend requests concerning the invalidity and unenforceability of its patents. *Angie M. v.*  
 28 *Superior Court*, 37 Cal. App. 4th 1217, 1227 (1995) (“Liberality in permitting amendment is  
 the rule,” and “denial of leave to amend is an abuse of discretion unless the complaint  
 shows on its face it is incapable of amendment”).