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Sandisk Corp. v. STMicroelectronics, Inc.

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Sandisk Corp. v. STMicroelectronics, Inc.

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Licensing patented technology plays a dual role in technological advancement: it enables patent owners as licensors to be compensated for their inventions, while simultaneously allowing licensees to make, use, offer to sell, sell, or import into the United States a product or process covered by a patent.¹ In fact, licensing has allowed nations to rebuild, modernize, and gain superiority in a field.² However, negotiating a successful license can be a difficult, often laborious task.³ Potential licensors, particularly small, innovative companies, experience a variety of obstacles when negotiating a license.⁴ But what would happen if almost any licensing attempt—no matter how slight—puts a willing licensor at imminent risk of a declaratory judgment action by a potential licensee? How would the balance of power shift between the willing licensor and the potential licensee?

In *SanDisk Corp. v. STMicroelectronics, Inc.*, the Federal Circuit, in a case of first impression, examined whether there was an actual controversy for the purpose of maintaining subject matter jurisdiction in a declaratory judgment action for patent invalidity and non-infringement.⁵ A recent Supreme Court decision, *MedImmune, Inc. v. Genentech, Inc.*,⁶ called into question the Federal Circuit's test for determining the existence of an actual controversy in such an instance.⁷ In response to

1. See ORG. FOR ECON. CO-OPERATION & DEV., OECD SCIENCE, TECHNOLOGY AND INDUSTRY OUTLOOK 151 (2006) [hereinafter OECD]. An entity is liable for infringement of a patent if, "without authority [it] makes, uses, offers to sell, or sells any patented invention, within the United States, or imports into the United States any patented invention during the term of the patent." 35 U.S.C. § 271(a) (2000).

2. See LICENSING BEST PRACTICES: THE LESI GUIDE TO STRATEGIC ISSUES AND CONTEMPORARY REALITIES 4 (Robert Goldscheider ed., 2002) [hereinafter LICENSING BEST PRACTICES]. Take for example, Japan:

After World War II, licensing was extensively and effectively used by Japan to rebuild its industry, and develop dominance in fields such as consumer electronics and optics. It was also used to modernize Japan's chemical, petrochemical, and pharmaceutical industries. Japan was and is still running a large deficit in technology-related balance of payment, but its strategy of extensive licensing allowed it to jump start the country rebuilding, and in the case of consumer electronics, to dominate worldwide markets with its innovations.

Id.

3. See Vernon Parker, *Negotiating Licensing Agreements*, in INTERNATIONAL BUSINESS NEGOTIATIONS 243, 250–54 (Pervez N. Ghauri & Jean-Claude Usunier eds., 2d ed. 2003) (discussing the many elements and considerations required to successfully negotiate a patent license).

4. See *id.*

5. *SanDisk Corp. v. STMicroelectronics, Inc.*, 480 F.3d 1372, 1377–78 (Fed. Cir. 2007). The court quotes the Declaratory Judgment Act, which in relevant part reads:

In a case of actual controversy within its jurisdiction . . . any court of the United States, upon the filing of an appropriate pleading, may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought.

Id. (quoting 28 U.S.C. § 2201(a) (2000)). In a typical declaratory judgment action regarding a patent dispute, the plaintiff seeks a declaration that the patent is invalid, unenforceable, and/or not infringed upon by the plaintiff's products or processes.

6. 127 S. Ct. 764 (2007) (holding that a non-repudiating patent licensee can seek a declaratory judgment action against a licensor while the license is still in force).

7. *Id.* at 774 n.11.

MedImmune, the Federal Circuit abandoned its old test and proffered a new one.⁸ This case comment contends that the *SanDisk* court's new legal test improperly applied Supreme Court precedent by placing overly strict limitations on the district court's discretionary power. The *SanDisk* test results in the impractical effect of putting any willing licensor at risk of a declaratory judgment action for taking a necessarily adverse position—no matter how slight—against a potential licensee.

Plaintiff SanDisk is a major player in the flash memory storage market.⁹ Defendant STMicroelectronics ("ST") entered into the market more recently.¹⁰ Both companies own multiple patents in the flash memory storage field.¹¹ In April 2004, ST sent a letter to SanDisk listing several ST patents that "may be of interest" to SanDisk and requested a meeting to discuss a patent cross-licensing agreement.¹² SanDisk responded that it would need several weeks to review the patents and that it would be in touch about a potential meeting in June 2004.¹³ In July 2004, with SanDisk yet to respond, ST sent a follow-up letter, which again requested a meeting to discuss cross-licensing.¹⁴ The July letter listed additional ST patents that "may also be of interest."¹⁵ SanDisk replied that it wished to continue the "friendly discussions" between the companies' business representatives about ST selling SanDisk certain flash memory products.¹⁶ Notably, the business representatives had not yet discussed any patents or a potential cross-licensing agreement.¹⁷

In August 2004, SanDisk and ST met to discuss cross-licensing.¹⁸ As part of their negotiating strategies, SanDisk and ST presented detailed infringement analyses to explain why they believed the other party was liable for infringement.¹⁹ ST also presented an economic analysis that included both companies' revenues and research and development costs, as well as the costs of SanDisk's allegedly unlicensed actions.²⁰ Upon conclusion of the meeting, ST presented SanDisk with a packet of

8. *SanDisk*, 480 F.3d at 1381.

9. *Id.* at 1374.

10. *Id.*

11. *Id.* ST's patents-at-issue include U.S. Patent Nos. 4,839,768; 5,073,816; 5,175,706; 5,455,954; 5,589,762; 5,636,115; 5,793,679; 5,831,302; 5,999,456; 6,100,581; 6,163,487; 35,121; 5,014,312; and 5,438,504. SanDisk's patent-at-issue is U.S. Patent No. 5,172,338.

12. *Id.* A cross-license is defined as "an agreement between two or more patentees to exchange licenses for their mutual benefit and mutual use of the licensed products." BLACK'S LAW DICTIONARY (8th ed. 2004).

13. *Id.*

14. *Id.*

15. *Id.* (citation omitted).

16. *Id.* (citation omitted).

17. *Id.*

18. *Id.* at 1375.

19. *See id.*

20. *Id.*

materials, including ST's infringement analysis.²¹ ST told SanDisk that it knew these materials would provide SanDisk with a basis to seek and sustain a declaratory judgment action against ST, but that ST had "absolutely no plan whatsoever to sue SanDisk."²² SanDisk replied that it also had no plans to sue ST and that another meeting might be appropriate.²³

On September 3, 2004, upon ST's request, SanDisk sent a copy of its presentation.²⁴ On September 15, 2004, SanDisk sent ST a confidential version of SanDisk's cross-licensing offer, which would expire on September 27, 2004.²⁵ ST requested a non-confidential version of the offer, but SanDisk refused.²⁶

On October 15, 2004, after a series of communications attempting to set up another meeting, SanDisk filed suit, seeking a "declaratory judgment of noninfringement and invalidity of the fourteen ST patents that had been discussed during the cross-licensing negotiations."²⁷ ST moved to dismiss based on a lack of subject matter jurisdiction, claiming that there was no actual controversy at the time of filing.²⁸ ST based this assertion on the ground that "SanDisk did not have an objectively reasonable apprehension of suit, even though it may have subjectively believed that ST would bring an infringement suit."²⁹

The District Court for the Northern District of California, relying on the Federal Circuit's then-valid "reasonable apprehension" test, dismissed the complaint finding that it lacked subject matter jurisdiction.³⁰ The "reasonable apprehension" test requires "an explicit threat or other action by the patentee which creates a reasonable apprehension on the part of the declaratory judgment plaintiff that it will face an infringement suit."³¹ The district court found that no actual controversy existed as SanDisk failed to show a "reasonable apprehension" that ST would file an infringement suit at the time SanDisk filed its complaint.³² Alternatively, the district court

21. *Id.*

22. *Id.* at 1375–76.

23. *Id.* at 1376.

24. *Id.*

25. *Id.*

26. *Id.*

27. *Id.*

28. *Id.*

29. *Id.* (citation omitted).

30. *SanDisk Corp. v. STMicroelectronics, Inc.*, No. C 04-04379 JF, 2005 U.S. Dist. LEXIS 44870, *32–33 (N.D. Cal. 2005). The "reasonable apprehension" test was utilized to determine if an actual controversy existed at the time of filing for the purposes of maintaining subject matter jurisdiction over a declaratory judgment action. *See SanDisk*, 480 F.3d at 1376.

31. *Teva Pharms. USA, Inc. v. Pfizer Inc.*, 395 F.3d 1324, 1332 (Fed. Cir. 2005) (citing *Gen-Probe Inc. v. Vysis, Inc.*, 359 F.3d 1376, 1380 (Fed. Cir. 2004); *Amana Refrigeration, Inc. v. Quadlux, Inc.*, 172 F.3d 852, 855 (Fed. Cir. 1999); *BP Chems. Ltd. v. Union Carbide Corp.*, 4 F.3d 975, 978 (Fed. Cir. 1993)).

32. *SanDisk*, 2005 U.S. Dist. LEXIS, at *32–33.

stated “that even if it had subject matter jurisdiction over the instant claims, it would exercise its discretion and decline to decide them.”³³

SanDisk appealed the district court’s decision.³⁴ In the interim, the Supreme Court decided *MedImmune* on January 9, 2007.³⁵ *MedImmune* considered the narrow issue of whether a non-repudiating patent licensee can seek a declaratory judgment action against a licensor while the license is still in force.³⁶ The Supreme Court, in a footnote, called into question the Federal Circuit’s “reasonable apprehension” test, stating that it was at odds with its precedent.³⁷

The Federal Circuit, relying on *MedImmune*, abandoned the “reasonable apprehension” test and reversed.³⁸ In place of the “reasonable apprehension” test, the Federal Circuit proffered a new legal test: “where a patentee asserts rights under a patent based on certain identified ongoing or planned activity of another party, and where the party contends that it has the right to engage in the accused activity without a license, an Article III case or controversy will arise”³⁹ In such an instance, “the party [contending that a license is unnecessary] need not risk a suit for infringement by engaging in the identified activity before seeking a declaration of its legal rights.”⁴⁰

The Federal Circuit found that ST’s ongoing assertions that SanDisk infringed certain ST patents, including presentation of a detailed infringement analysis and royalty assertions, coupled with SanDisk’s denial that it needed to take a license, established an Article III case or controversy and thus declaratory judgment jurisdiction.⁴¹ It concluded that ST’s promise not to sue did not negate the actual controversy because ST’s conduct demonstrated a “preparedness and willingness to enforce its patent rights.”⁴² The court described ST’s actions as “the kinds of ‘extra-judicial

33. *Id.* at *33 n.30.

34. *SanDisk*, 408 F.3d at 1374.

35. *See* 127 S. Ct. 764 (2007).

36. *Id.* at 767.

37. *Id.* at 774 n.11. The Supreme Court criticized the Federal Circuit’s “reasonable apprehension” test as being at odds with *Altwater v. Freeman*, 319 U.S. 359 (1943), *Maryland Casualty Co. v. Pacific Coal & Oil Co.*, 312 U.S. 270 (1941), *Aetna Life Ins. Co. v. Haworth*, 300 U.S. 227 (1937), and *Cardinal Chemical Co. v. Morton Int’l, Inc.*, 508 U.S. 83 (1993). *Id.*

38. *SanDisk*, 480 F.3d at 1383. In order to determine the existence of an actual controversy, the Federal Circuit developed a two-part inquiry. *Teva*, 395 F.3d at 1332 (citing *EMC Corp. v. Norand Corp.*, 89 F.3d 807 (Fed. Cir. 1996)). The first part is the “reasonable apprehension” test. *Id.* at 1332. The second part requires “present activity by the declaratory judgment plaintiff which could constitute infringement, or concrete steps taken with the intent to conduct such activity.” *Id.* at 1332 (citing *Gen-Probe*, 359 F.3d at 1380; *Amana Refrigeration*, 172 F.3d at 855; *BP Chems.*, 4 F.3d at 978). The court in *SanDisk* left “to another day” the effect that *MedImmune* had, if any, on the second part. 480 F.3d at 1380.

39. *SanDisk*, 480 F.3d at 1381.

40. *Id.* (citation omitted).

41. *See id.* at 1382.

42. *Id.* at 1382–83.

patent enforcement with scare-the-customer-and-run tactics' that the Declaratory Judgment Act was intended to obviate."⁴³

Judge Bryson concurred in the result, but called into question the court's new legal test, particularly with respect to its practical application.⁴⁴ Indeed, according to Judge Bryson:

it would appear that under the court's standard virtually any invitation to take a paid license relating to the prospective licensee's activities would give rise to an Article III case or controversy if the prospective licensee elects to assert that its conduct does not fall within the scope of the patent.⁴⁵

He continued, "as the court makes clear, even a representation by the patentee that it does not propose to file suit against the prospective licensee will not suffice to avoid the risk that the patentee will face a declaratory judgment action."⁴⁶ Furthermore, Judge Bryson questioned the Federal Circuit limiting the district court on remand to consider only "additional facts' not previously before the district court."⁴⁷

The Federal Circuit's legal test proffered in *SanDisk* improperly applied the *MedImmune* decision and may have a far-reaching impact on licensing negotiations. Under the court's test, all that is necessary to satisfy the Article III case or controversy threshold is a patent owner's contact with a potential licensee and an offer of a license, and the potential licensee's assertion that it does not need a license.⁴⁸ In practice, this means that essentially any contact with a potential licensee will give rise to an actual controversy: the potential licensee will be able to seek a declaratory judgment action for patent invalidity, unenforceability, and/or non-infringement.⁴⁹

Given the Supreme Court's criticism, the Federal Circuit correctly abandoned its "reasonable apprehension" test.⁵⁰ However, the new test advanced by the Federal Circuit inappropriately results in a potential licensee being able to seek declaratory judgment relief for any necessarily adverse position taken by the patent owner, no matter how slight.⁵¹ Notably, the Supreme Court left "the equitable, prudential, and policy arguments in favor of such a discretionary dismissal for the [district] courts' consideration."⁵² The practical effect of the new test proffered by the Federal Circuit

43. *SanDisk*, 480 F.3d at 1383 (quoting *Arrow Indus. Water, Inc. v. Ecolochem, Inc.* 846 F.2d 731, 735 (Fed. Cir. 1988)).

44. *Id.* at 1384 (Bryson, J., concurring).

45. *Id.*

46. *Id.*

47. *Id.* at 1385.

48. *See id.* at 1381 (majority opinion).

49. *See id.*

50. *See id.* at 1380 (noting that "[t]he Supreme Court's opinion in *MedImmune* represents a rejection of [the Federal Circuit's] reasonable apprehension of suit test").

51. *See id.* at 1380–81.

52. *MedImmune*, 127 S. Ct. at 777.

in *SanDisk* is that it, *inter alia*, severely limits such discretionary dismissal.⁵³ This is contrary to *MedImmune*, which stated that the district court should be given liberal discretion to consider various arguments favoring dismissal.⁵⁴

If the district court finds that a patent owner alleged another party infringed a patent, the patent owner offered a license to cure the infringement, and the party denied that it needed a license, then an actual controversy exists for the purposes of declaratory action jurisdiction.⁵⁵ Furthermore, it appears that very little will negate such a finding. Take, for example, an agreement not to sue—such as the one between *SanDisk* and *ST*. This agreement not to sue, according to the court, does not negate the ability to seek relief pursuant to a declaratory judgment action.⁵⁶

Moreover, a district court can arguably no longer use its discretion to consider whether such an agreement eliminates an actual controversy giving rise to subject matter jurisdiction for the purpose of maintaining a declaratory judgment action.⁵⁷ The district court can only consider whether the patent owner engaged in conduct that showed a willingness to enforce its patents, regardless of whether there was an affirmative promise, mutually agreed upon by the parties, not to sue.⁵⁸ This is inconsistent with *MedImmune*, which continues to mandate liberal discretion to consider “any merit-based arguments for denial of declaratory relief.”⁵⁹ Certainly, a promise not to sue falls into such a category and the district court, under its discretion, should be allowed to consider such a promise, together with all the surrounding circumstances.⁶⁰ After all, an Article III case or controversy arises when, “under *all the circumstances* . . . there is a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment.”⁶¹

In the matter at hand, the *SanDisk* court summarily limited the district court’s discretion on remand to consider all the circumstances.⁶² It is irrelevant that the district court’s decision was prior to *MedImmune*. Rather, the only relevant factor is that by limiting the district court on remand to consider only the additional facts, the

53. See *SanDisk*, 480 F.3d at 1383.

54. See *MedImmune*, 127 S. Ct. at 776. The Declaratory Judgment Act “confer[s] on federal courts unique and substantial discretion in deciding whether to declare the rights of litigants.” *Id.* (quoting *Wilton v. Seven Falls Co.*, 515 U.S. 277, 286 (1995)).

55. See *SanDisk*, 480 F.3d at 1381, 1383.

56. See *id.* at 1382–83.

57. *Id.* at 1383.

58. *Id.*

59. *MedImmune*, 127 S.Ct. at 777 (emphasis added).

60. See *id.* at 776–77.

61. *Id.* at 771 (citing *Maryland Casualty Co.*, 312 U.S. at 273) (emphasis added).

62. See *SanDisk*, 480 F.3d at 1383 (limiting the district court on remand to consider only “additional facts” not initially considered).

Federal Circuit improperly applied the Supreme Court's precedent articulated in, for example, *Maryland Casualty Co. v. Pacific Coal & Oil Co.*⁶³

In *Maryland Casualty*, the plaintiff, an insurance company, sought a declaratory judgment that it was not obligated to indemnify the insured or defend an action brought against the insured stemming from an automobile collision.⁶⁴ The Supreme Court found that an actual controversy existed and stated that “[t]he difference between an abstract question and a ‘controversy’ contemplated by the Declaratory Judgment Act is necessarily one of degree, and it would be difficult, if it would be possible, to fashion a precise test for determining in every case whether there is such a controversy.”⁶⁵ The Federal Circuit in *SanDisk* did exactly what the Supreme Court warned against: it proffered a precise, legal test whereby an adverse position—no matter how slight or “abstract”—gives rise to an actual controversy.⁶⁶

Essentially, the only way for a patent owner to avoid the risk of a declaratory judgment action is to enter into an appropriate confidentiality agreement.⁶⁷ However, as Judge Bryson articulated in his concurrence, confidentiality agreements are impractical; only a party not interested in seeking a declaratory judgment in the first place would enter into such an agreement.⁶⁸ It is further impractical, in no small part, because it impedes the primary purpose of the negotiations—to enter into a mutually beneficial patent licensing agreement—by adding another agreement to be discussed, disputed, and potentially agreed upon.⁶⁹ Such an additional agreement may hinder or altogether halt negotiations.

Although the court had subject matter jurisdiction, the Federal Circuit's test places almost no outer bound on the necessary threshold to maintain a declaratory judgment action.⁷⁰ Without an appropriate outer bound, the district court will not be able to consider important factors, including equitable, prudential, and policy arguments. No longer can a patent owner enter into a negotiation without risking potentially costly litigation, regardless of whether the owner has an actual intent to enforce its patents through litigation.⁷¹ If a patent owner approaches a potential licensee, it risks a declaratory judgment action.⁷² This appears to be true regardless of

63. See *Maryland Casualty*, 312 U.S. 270.

64. *Id.* at 271.

65. *Id.* at 273.

66. See *SanDisk*, 480 F.3d at 1381.

67. See *id.* at 1375.

68. See *id.* at 1385 (Bryson, J., concurring).

69. See Parker, *supra* note 3, at 243, 250–54 (discussing the many elements and considerations required to successfully negotiate a patent license before the *SanDisk* decision).

70. See *SanDisk*, 480 F.3d at 1384 (Bryson, J., concurring).

71. See *id.* at 1381 (majority opinion) (noting that licensing negotiations will not be able to occur without risking litigation); see also *id.* at 1383 (noting that the lack of intent to litigate is irrelevant to the issue of Article III cases and controversies); LICENSING BEST PRACTICES, *supra* note 2, at 314 (discussing the high cost of litigation).

72. See *SanDisk*, 480 F.3d at 1381.

whether or not it has conducted the proper due diligence necessary to adequately sustain and answer questions from the potential licensee about infringement, validity, and royalties due (i.e., answers necessary for a typical potential licensee to entertain a license).⁷³ Conversely, if the patent owner chooses not to approach the licensee, its only hope of being compensated for its invention is to sue for infringement.

This in turn will impact patent owners, particularly start-ups and small research-oriented technology companies, by limiting their ability to reap the rewards for their inventions in a cost effective way.⁷⁴ Licensing patents can be an effective means for transferring and pooling technology, thereby enabling companies to more successfully innovate. Such patents further ensure that companies are adequately compensated for their innovations.⁷⁵ In contrast, large, well-funded companies will be incentivized to seek a declaratory judgment action against patent owners in order to gain a competitive advantage in licensing negotiations.⁷⁶

Moreover, the new test may encourage patent owners to sue first and ask questions later. The new test discourages patent owners from entering into licensing negotiations in the first place and instead, will increase a potential licensee's ability to seek relief from the court regardless of whether the patent owner has an intention to sue.⁷⁷ From a patent owner's perspective, there is an increased fear of creating an actual controversy under the court's new standard.⁷⁸ The new test places extreme restrictions on a patent owner's ability to approach a potential licensee outside a court setting.⁷⁹ From a potential licensee's perspective, there is a reduced incentive to negotiate—it gives a potential licensee an incentive to file a declaratory judgment action to better position itself in a licensing negotiation.⁸⁰ With the increased potential and new advantages of entering into litigation—either by the patent owner filing an infringement suit or the potential licensee filing a declaratory judgment action—an

73. *See id.* at 1385 (Bryson, J., concurring).

74. *See* OECD, *supra* note 1, at 154–56.

75. *See id.* at 154–55 (discussing the ability of licensing to positively impact innovation networks and economic value chains).

76. Notably, the new test is skewed toward potential licensees. Often, innovation-based companies—such as start-ups—place a considerable amount of significance on patents and the ability to effectively reap the benefits from their inventions. *See* JOHN T. PIENKOS, *THE PATENT GUIDEBOOK* 26 (2005). By increasing the ability for a potential licensee to seek a declaratory judgment action, it makes licensing more difficult for these innovation-based companies. *See, e.g.,* Parker, *supra* note 3, at 250–54.

77. *See SanDisk*, 480 F.3d at 1381–83.

78. *See id.*

79. *See id.*

80. *See* Leonard T. Nuara, *Software Litigation & Software Licensing: Draw or Draft?*, in *PATENTS, COPYRIGHTS, TRADEMARKS, AND LITERARY PROPERTY COURSE HANDBOOK SERIES* 811, 811–30 (Practising Law Institute 2004) (discussing rationale for licensing and litigating).

SANDISK CORP. V. STMICROELECTRONICS, INC.

already over-burdened court system will find itself with additional, yet potentially unnecessary, lawsuits.⁸¹

The *SanDisk* court's new test for determining the existence of an Article III case or controversy is an overly broad application of *MedImmune*. The new test is impractical and could make licensing negotiations a thing of the past. The patent system is in place to advance, not hinder, technological innovation. Licensing plays an essential role in this system. A narrower test—one that appropriately articulates *MedImmune* and leaves the district court with the requisite amount of discretion to consider all the circumstances—should be employed.

81. See LICENSING BEST PRACTICES, *supra* note 2, at 314 (discussing the expenses of litigating and the inefficiency of and burden on the court system); Nuara, *supra* note 80, at 823–24, 829 (discussing litigation costs). The time to trial in patent cases typically takes several years. For example, the average time to trial in patent cases in the Southern District of New York is 44.4 months. *Choosing a Patent Litigation Venue*, 3rd PATENT STRATEGIES CONFERENCE (Affinia Manhattan Hotel, New York, N.Y.) Mar. 30, 2007, at 4. This does not take into account potential appeals. While the litigation is pending, there is an uncertainty as to the outcome, which could also have adverse effects on a company. See Nuara, *supra* note 80, at 822–24.