

In The  
**United States Court of Appeals**  
For The Federal Circuit

**MERCEXCHANGE, L.L.C.,**

*Plaintiff-Appellant,*

v.

**eBAY, INC. and HALF.COM, INC.,**

*Defendant-Appellee,*

APPEAL FROM THE  
UNITED STATES DISTRICT COURT FOR THE  
EASTERN DISTRICT OF VIRGINIA  
IN CASE NO. 2:01-CV-736, JUDGE JEROME B. FRIEDMAN.

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**BRIEF OF APPELLANT**

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## TABLE OF ABBREVIATIONS

In this Brief, the following abbreviations and format will be observed:

MercExchange	Plaintiff-Appellant MercExchange, L.L.C.
eBay	Defendant-Appellee eBay, Inc.
Half.com	Defendant-Appellee Half.com, Inc.
defendants	Collectively, eBay and Half.com
the '265 Patent	United States Patent No. 5,845,265, issued to Thomas G. Woolston, and assigned to MercExchange
district court	United States District Court for the Eastern District of Virginia, Judge Jerome B. Friedman
App _____	Citation to Joint Appendix
Conf-App _____	Citation to the "Confidential" portions of the Joint Appendix for materials filed under seal pursuant to the protective order.
PTO	United States Patent and Trademark Office
uBid	uBid.com, Inc., licensee of the '265 Patent

## STATEMENT OF RELATED CASES

Pursuant to Federal Circuit Rule 47.5 Plaintiff-Appellant MercExchange states that: (1) MercExchange previously appealed the district court's modification of a consent judgment between MercExchange and ReturnBuy in *MercExchange, L.L.C. v. eBay, Inc. and Half.com*, Appeal No. 03-1318. This Court, Judges Rader, Schall, and Prost, dismissed the appeal on June 2, 2003 in an opinion not citable as precedent under Federal Circuit Rule 47.6. (2) Defendants-Appellees eBay and Half.com appealed and MercExchange cross-appealed a final judgment entered August 7, 2003 in *MercExchange, L.L.C. v. eBay, Inc. and Half.com, Inc.*, Appeal Nos. 03-1600, -1616. This Court, Chief Judge Michel, and Judges Clevenger and Bryson, affirmed in part, reversed in part, and vacated in part, in a published opinion dated March 16, 2005, as reported in *MercExchange, L.L.C. v. eBay, Inc.*, 401 F.3d 1323 (Fed. Cir. 2005). (3) eBay and Half.com appealed to the Supreme Court of the United States this Court's order enjoining eBay and Half.com from further acts of infringement of the '265 Patent. The Supreme Court vacated the permanent injunction and remanded the matter to the district court in a published decision dated May 15, 2006 as reported in *eBay, Inc. v. MercExchange, L.L.C.*, 126 S. Ct. 1837 (2006). (4) There is no other case known to counsel to be pending in this or in any other court that will directly affect or be directly affected by this Court's decision in the pending appeal.

## **JURISDICTIONAL STATEMENT**

MercExchange appeals from an order entered July 27, 2007, denying MercExchange's renewed motion for a permanent injunction. The district court had original jurisdiction under 28 U.S.C. §§ 1331 & 1338(a). MercExchange timely filed a notice of appeal on August 27, 2007. This Court has jurisdiction under 28 U.S.C. § 1292(a)(1).

## **STATEMENT OF THE ISSUES**

MercExchange's appeal presents the following issue:

1. Whether the district court abused its discretion in denying MercExchange a permanent injunction for defendants' continued willful infringement?

## **STATEMENT OF THE CASE**

### **Preliminary Statement.**

This is a case of deliberate willful infringement. The question in this case is whether equity favors granting injunctive relief to the patent holder, MercExchange, after a jury's finding of willful infringement against the defendants, eBay and its wholly-owned affiliate Half.com. This Court previously affirmed the jury's finding of defendants' willful infringement and defendants have exhausted all appeals. The district court failed to fully appreciate how eBay's dominance, as a market monopolist, combined with its willful infringement, impacted MercExchange's ability to exploit U.S. Patent No. 5,845,265 ("the '265

Patent”). Instead, the district court viewed MercExchange’s attempts to commercialize the ’265 Patent with skepticism, completely failing to appreciate the impact eBay’s infringing system (which remained in the market) had on MercExchange’s licensees.

The equities strongly favor injunctive relief. Not only is this a case of deliberate willful infringement, but by eBay’s own assertion, the infringement was avoidable. eBay was well aware of and tried to purchase the ’265 Patent before eBay started infringing. And eBay deliberately chose to infringe when it could have (as it contends) avoided infringement with a simple, inexpensive design-around. Under these circumstances, eBay can “make no claims whatsoever on the Chancellor’s conscience.” *Albemarle Paper Co. v. Moody*, 422 U.S. 405, 422 (1975). Further, eBay has proclaimed to the investing public that an injunction would *not* harm it.

In contrast, MercExchange continues to suffer irreparable harm absent an injunction. MercExchange, and MercExchange’s licensees are competitors of eBay. But eBay’s continued use of MercExchange’s technology irreparably harms MercExchange’s ability to market, sell, or license its technology to these existing or future competitors to eBay. If eBay, as a market monopolist, cannot be enjoined, MercExchange is effectively denied the ability to maximize the value of its patents by exclusively licensing them. The value of MercExchange’s lost

opportunities to enter into these license relationships, and to take advantage of the further business those relationships might generate, is unquantifiable.

Moreover, the harm to MercExchange has only intensified in the almost three years since the prior appeal was before this Court. eBay has solidified its market dominance, at least in part by infringing MercExchange's '265 Patent. For example, eBay, following the jury's finding of willful infringement, opened up a new channel of business entitled its "Trading Post Program," which incorporates physical consignment stores where sellers can drop off their merchandise for later sale on eBay. eBay opened this new venture despite recognizing the risk of infringing MercExchange's patents was a "10" on a scale of "1 to 10," with "10" being the highest risk. MercExchange, on the other hand, has been thwarted in its efforts to market its invention because of its inability to prevent eBay — whose dominance squeezes out potential competitors — from infringing.

The district court also erred in ignoring MercExchange's efforts to commercialize the '265 Patent prior to August 7, 2003 (the date of the district court's entry of final judgment). Apparently the district court believed it was being even-handed in refusing arguments made by both parties urging the district court to reconsider findings and holdings from its August 7, 2003 Order and Opinion. But eBay was attempting to argue that it was not a willful infringer, a finding that had been affirmed on appeal and was therefore finally established. In contrast, the

district court refused to consider arguments from MercExchange related to its pre-August 7, 2003 development efforts, despite the fact that the district court's entire analysis on the denial of injunctive relief, which included findings pertaining to MercExchange's licensing efforts, had been vacated and remanded with the mandate to analyze injunctive relief "in the first instance." Instead of approaching this analysis "in the first instance," the district court abused its discretion by relying upon its prior findings and only allowing MercExchange to present evidence of its commercialization efforts after August 7, 2003.

The public interest also favors injunctive relief. In addition to maintaining the integrity of the patent system by enforcing patent rights, enjoining eBay also serves the public interest in promoting competition. Without an injunction, eBay will further solidify its monopoly power by impairing development of potential online auction alternatives to eBay. Moreover, eBay has attempted to thwart MercExchange's effort to even interact with potential licensees and customers.<sup>1</sup>

While the factors for evaluating injunctive relief all strongly favor granting MercExchange that relief, the district court abused its discretion by refusing to enjoin eBay's future infringement.

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<sup>1</sup> eBay pressured an organization called PESA to have MercExchange's representatives removed from a public meeting that included many of eBay's "power sellers." eBay informed PESA that if MercExchange was not removed from the public meeting that PESA would no longer have "access to eBay execs."

### **Procedural History.**

MercExchange sued eBay in the district court in September 2001 for, *inter alia*, infringement of the '265 Patent. The jury found that eBay (and its wholly-owned subsidiary, Half.com) had willfully infringed the '265 Patent and awarded damages for past direct infringement of that patent in the amount of \$25 million. *MercExchange, L.L.C. v. eBay, Inc.*, 275 F. Supp. 2d 695, 698-99 (E.D. Va. 2003).<sup>2</sup> The district court upheld the jury's finding of willful infringement, *id.* at 704, and this Court unanimously affirmed the jury's verdict and the district court's judgment that the '265 Patent was valid and willfully infringed. *MercExchange, L.L.C.*, 401 F.3d at 1328-29. eBay did not seek further review on those questions, and the judgments of validity and willful infringement are now final.

With respect to MercExchange's initial request for injunctive relief, the district court denied a permanent injunction, *MercExchange*, 275 F. Supp. 2d at 715, and this Court reversed. *MercExchange*, 401 F.3d at 1339. eBay sought

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<sup>2</sup> MercExchange brought infringement claims based on three of its patents: U.S. Patent No. 6,202,051 ("the '051 patent"), U.S. Patent No. 6,085,176 ("the '176 patent"), and the '265 Patent. Before trial, the district court granted eBay summary judgment that all claims of the '051 patent were invalid for lack of a written description. *MercExchange, L.L.C. v. eBay, Inc.*, 271 F. Supp. 2d 789, 794-95 (E.D. Va. 2002). This Court vacated summary judgment and remanded for trial (which the district court has since stayed). *MercExchange, L.L.C.*, 401 F.3d at 1337. The '176 patent and '265 Patent infringement claims went to the jury; with this Court subsequently reversing the jury's verdict of willful infringement of the '176 patent after concluding that that patent was invalid. *Id.* at 1326.



certiorari on the question whether this Court had properly evaluated the propriety of a permanent injunction. Conf-App 00500163-187. The Supreme Court concluded that neither lower court properly applied the appropriate test for injunctive relief, thereby vacating this Court's decision and remanding to the district court to apply the traditional "four-factor test" for such relief in the first instance. *eBay, Inc. v. MercExchange, L.L.C.*, 126 S. Ct. 1837, 1841 (2006). The only question remanded to the district court, therefore, was whether permanent injunctive relief is proper under this four-factor test. *MercExchange, L.L.C. v. eBay, Inc.*, Nos. 03-1600, 03-1616, 2006 U.S. App. LEXIS 17505 (Fed. Cir. July 6, 2006) (remand order). The district court, in rejecting MercExchange's renewed motion for a permanent injunction, concluded that legal relief, including potentially enhanced damages, would fully compensate MercExchange for defendants' willful infringement. App 000036.

#### STATEMENT OF FACTS

In April 1995, several months before eBay was conceived, Thomas Woolston filed his first patent application involving online marketing technology. The family of patents that issued from this parent application includes the '265 Patent. App 000236.

**A. The '265 Patent.**

The '265 Patent, in general terms, describes an “electronic market” for the sale of goods. App 000236-262. In such a market, sellers can display their wares by posting pictures, descriptions, and prices of goods on a computer network, such as the Internet. A prospective buyer can electronically browse the goods on sale by connecting to the network. After selecting an item, the buyer can complete the purchase electronically, with the “electronic market” mediating the transaction, including payment, on the buyer’s behalf. The seller is then notified that the buyer has paid for the item and that the transaction is final. A central authority within the market can police the obligations and performance of sellers and buyers over time, thereby promoting trust among participants. In short, the invention provides a platform to offer goods for sale over the Internet in which the entire sales transaction, including the mediation of payment, is performed electronically. App 000236-240.<sup>3</sup>

**B. Initial Efforts to Commercialize the Invention.**

Mr. Woolston’s goal from the outset was to commercialize his patented inventions. For that purpose, he founded MercExchange (as well as an earlier

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<sup>3</sup> In affirming the district court’s claim construction for the '265 Patent, *MercExchange, L.L.C. v. eBay, Inc.*, 401 F.3d 1323, 1329 (Fed. Cir. 2005), this Court rejected eBay’s contention that the district court had “failed to perform its most critical function” of instructing the jury on claim construction issues.

iteration of that company, called Fleanet) and assigned his patent rights to it. Trial Tr. pp. 334-35; 493 (Conf-App 00500099; 00500108). He developed a business plan and sought capital investment to commercialize his patents. *Id.* pp. 315; 492-96; 513-16 (Conf-App 00500098, 107-108, 110). He also hired a computer programming staff to write software to put his inventions into practice. *Id.* pp. 1084-87 (Conf-App 00500119). In order to make the most of its limited resources, MercExchange also entered into cooperative business and license agreements with another company, Aden Enterprises, in October 1999. Conf-App 00500128-136 (agreement granting exclusive license within the online travel-sector field-of-use). At that time, Aden Enterprises was “embarking on a major industry initiative to build and deploy Internet Markets and Auctions” (Conf-App 00500128),<sup>4</sup> and MercExchange sought, through this business/license arrangement, to use its patent rights to develop its invention in ways that MercExchange could not accomplish alone. *See also* Conf-App 00500137-142 (non-exclusive license with Aden’s wholly-owned subsidiary Leftbid.com in the field of use of the “Fine Art Sector” of Internet markets); Conf-App 00500143-148 (non-exclusive license with Aden’s wholly-owned subsidiary Navlet.com that provided infrastructure (hardware and software facilities) for Internet auction systems). MercExchange hoped to leverage

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<sup>4</sup> An Internet or online auction market can allow consumers to bid their own price for various items or to buy those items at a fixed price.

the resources of these licensees to help develop and commercialize the invention. *See, e.g.*, Conf-App 00500238-239 (¶¶ 33-37) (noting these licensees were obligated to use their “best efforts” to develop the technology).

By the late 1990s, eBay was also looking for ways to offer goods for sale with the entire sales transaction, including the mediation of payment, performed electronically. Accordingly, in June 2000, eBay approached MercExchange to discuss eBay’s interest in buying MercExchange’s patent portfolio. Conf-App 00500149-150; Trial Tr. pp. 348-52; 590-92 (Conf-App 00500103-104, 115-116). eBay had been aware of MercExchange’s ’265 Patent and its technique for conducting electronic sales since the late 1990’s; in fact, eBay had filed twenty-four patent applications citing the ’265 Patent as prior art from October 1998 through February 2002. Conf-App 00500151-154. MercExchange was interested in entering into a working relationship with eBay. MercExchange relationship with Aden was ending and MercExchange hoped that by so doing business with eBay it could capitalize MercExchange to develop its new search technology. Trial Tr. pp. 348-49; 590-91 (Conf-App 00500103, 115-116). eBay, however, made clear that it was interested only in buying the patents, and all pending patents, rather than entering into any relationship that would keep MercExchange free to further develop its search technology. *Id.* pp. 348-49.

### **C. eBay's Infringement.**

When negotiations for the sale of MercExchange's patents broke down, eBay began using MercExchange's technology without authorization. By the fall of 2000 — only months after eBay had unsuccessfully tried to buy MercExchange's patents — eBay had incorporated into its website a fixed-price sales capability using the “electronic market” system of MercExchange's '265 Patent for the purchase and sale of goods and the transfer of funds in an electronic marketplace. Transcript of Whitman Deposition at 65-67 (Conf-App 00500156-157); Transcript of Krauss Deposition at 21-28 (Conf-App 00500159-162).

At the same time that eBay began using MercExchange's technology, it was becoming clear that lack of capital would prevent MercExchange from successfully commercializing its inventions directly. With no choice but to end its efforts at direct commercialization, MercExchange shifted its remaining resources to building a licensing program. Trial Tr. pp. 533; 1087 (Conf-App 00500113, 119).

While at trial eBay mocked MercExchange's business plan to commercialize its patent, eBay has since adopted that very plan, which incorporates brick and mortar consignment stores where sellers can drop their merchandise for later sale on eBay. *See* Ina Steiner, “eBay Encourages Consignment Sales Through Trading Post Program,” AuctionBytes.com (Jan. 28, 2004), *available at*

<http://www.auctionbytes.com/cab/abn /y04/m01/i28/s01> (accessed March 22, 2007) (Conf-App 00502860-862). *See also* eBay's "Trading Post FAQs," ( Conf-App 00502864-868) (defining eBay's Trading Posts as "locations that allow customers to drop items off and have them sold on eBay. Trading Posts provide the service of selling items on eBay for others for a fee."). eBay was fully aware that its new Trading Posts violate MercExchange's patent rights; eBay recognized that among the legal risks associated with this new eBay feature was the risk that it infringes the MercExchange patents "on drop off consignment model" and rated the degree of legal risk as a 10 on a scale of 1-10, where 10 was the highest risk. *See* "eBay Trading Post Franchises" (Conf-App 00502870-893).

**D. The '265 Patent reexamination process.**

After final judgment had been entered against eBay and while its appeal to the Federal Circuit was pending, eBay filed its first request for the Patent and Trademark Office ("PTO") to reexamine the '265 Patent. eBay subsequently filed a second request, which was rejected by the PTO as non-compliant for failing to specifically state the reason for a substantial new question of patentability. eBay then filed its third request for reexamination as an amended second request. Those parallel proceedings were merged and the PTO has not yet issued a final decision on the reexamination. The PTO has, however, recently issued a non-final Office *Action in which it deemed patentable and/or confirmed claims 1-25.* App 003358.

While this Office Action has preliminarily rejected claims 26-29, MercExchange will respond, believing claims 26-29 will ultimately also be deemed patentable and/or confirmed for substantially the same reasons these claims were found to be valid by the district court (and affirmed by this Court). If the PTO finally rejects claims 26-29, this decision may of course be appealed to the Board of Patent Appeals and Interferences (*see* 35 U.S.C. § 134(b)), and ultimately to this Court (*see* 35 U.S.C. § 306), which previously upheld the validity of the '265 Patent. Even if the PTO were to finally reject claims 26-29 of the '265 Patent, those claims would not be cancelled unless and until that agency action was affirmed on appeal by this Court — a process that could take years. *See* 35 U.S.C. § 307(a) (certificate canceling or confirming claims of patent on reexamination issued when appeals process has been exhausted); *In re Am. Acad. of Sci. Tech Ctr.*, 367 F.3d 1359 (Fed. Cir. 2004) (PTO's findings on reexamination not confirmed until ten years after reexamination was requested).

**E. Current Impact of eBay's Continuing Infringement.**

Although MercExchange has a final judgment that eBay willfully infringed its valid patent, not a penny of that judgment has been paid. Without an injunction ordering eBay to stop infringing the '265 Patent, the prospect that eBay will persist

in its infringement has continued to make MercExchange's efforts to commercialize its invention extremely difficult, and may completely exhaust this enterprise.

First, it is difficult for MercExchange to enter into and fully benefit from license arrangements because licensees have little incentive to make significant "up front" payments so long as eBay is infringing. Further, neither the licensee nor MercExchange come close to realizing the full benefits from those licenses due to eBay's market dominance in the market space covered by the '265 Patent. Trial Tr. pp. 1087, 1093 (Conf-App 00500119-120); *see also* Conf-App 00500255 (¶ 100). For example, in December 2002 MercExchange entered into a license agreement with AutoTrader.com, Inc. ("AutoTrader"), which competes against eBay in the field of online automobile sales. Conf-App 00500188-200. The license, which was negotiated under the cloud of eBay's infringement, permits AutoTrader to make exclusive use of the '265 Patent within the field of automobile sales — but it makes payment of royalties contingent on MercExchange's successfully stopping eBay's infringement. *Id.* In other words, royalties are payable only if eBay is prevented from continuing to practice MercExchange's patented technology. Because of eBay's continued infringement, MercExchange has been unable to realize any benefit from this license, and, for its part,



AutoTrader has been denied the rights *it* bargained for — the exclusive use of the invention for the purpose of buying and selling cars.

Second, MercExchange's post-trial experience with uBid.com, Inc. ("uBid"), one of eBay's few remaining direct competitors, well-illustrates the irreparable harm that MercExchange is suffering in the absence of an injunction. uBid and MercExchange had extensive discussions concerning merging the respective companies as evidenced by uBid wanting to take an exclusive license to the '265 Patent, in return for granting MercExchange an equity position in uBid. If eBay were enjoined, this exclusive licensing arrangement had the potential to drive up to \$12 billion in fixed-price sales from eBay's site to uBid's, with MercExchange's equity position giving it a direct and substantial stake in those market-share gains. The deal could not be consummated, however, because the absence of an injunction made its valuation too uncertain.

The history behind this lost opportunity is instructive. uBid was founded in 1997 with the express purpose of competing with eBay. Conf-App 00502760 (¶ 13). eBay launched its fixed-price sales feature in mid-2000; uBid launched its own fixed-price feature in February 2002. Conf-App 00502761 (¶ 18).

Shortly thereafter, uBid became aware that eBay's fixed-price feature (i.e., "Buy-It-Now") might infringe MercExchange's patent. After consulting with counsel, uBid voluntarily suspended its similar fixed-price feature in March 2003.

and sought a license from MercExchange. Conf-App 00502762 (¶ 19); uBid Rule 30(b)(6) Deposition Tr. at 162, 286, 306-07 (Conf-App 00502810, 818, 820). A few months later, in August 2003, the district court upheld the jury's verdict that eBay's and Half.com's fixed-price sales features willfully infringed the '265 Patent. *MercExchange, L.L.C.*, 275 F. Supp. 2d at 704; *see also* Conf-App 00502762 (¶ 20).

uBid recognized that securing a license to the '265 Patent and re-launching its fixed-price sales feature could give uBid a competitive advantage over eBay. As uBid's CEO explained in his deposition, eBay at the time was generating about \$40 billion in revenue, with about 30 percent of that revenue generated from its infringing "Buy-It-Now" sales. Conf-App 00502806 (p. 99). Because uBid believed that eBay would not be able to offer its fixed-price features without a license, uBid saw the opportunity to drive up to \$12 billion worth of sales from eBay to uBid's licensed platform. *Id.* (pp. 99-100); Conf-App 00502762 (¶ 21).

Accordingly, in May 2004 uBid entered into a license agreement with MercExchange for a non-exclusive license to the '265 Patent, and uBid re-launched its fixed-price sales feature. Conf-App 00502822-832; 00502810 (pp. 162-63). After uBid re-launched this feature under a license from MercExchange, it was the fastest growing part of uBid's business. Conf-App 00502810 (p. 163).

Based in part on the popularity of uBid's fixed-price sales feature and its future potential value, uBid sought to expand its relationship with MercExchange. Conf-App 00502763 (¶ 25); Conf-App 00502819 (p. 299). Specifically, uBid wanted to solidify its business partnership with MercExchange by converting the non-exclusive license into an exclusive one, in return for giving MercExchange an equity position in uBid. Conf-App 00502811, 00502819 (pp. 209, 299) ("What we were interested in was granting, getting a sublicense, an exclusive sublicense in return for giving up equity in the company."); *see also* Conf-App 00502763 (¶ 25).

As uBid's CEO explained, an exclusive license "could be as powerful as \$12 billion" because eBay sellers (in particular the large "power sellers") could use uBid's fixed-price feature "in lieu of eBay[']s]" (and in lieu of any of uBid's other potential competitors). Conf-App 00502812 (p. 211); *see also* App 003056 (n.8). In return for granting this exclusive license to uBid, MercExchange would get an equity stake in uBid, allowing it to compete directly with eBay and benefit directly from uBid's gains in market share. Of course, the "general premise and the power" of this proposed relationship stemming from an exclusive license-for-equity partnership was that eBay would be prevented – through an injunction – from infringing the '265 Patent. Conf-App 00502812-814, 00502819 (pp. 211, 217-18, 300).

The “premise” behind this deal was in flux, however, because the injunction issue remained unresolved. As the CEO of uBid testified, the parties “couldn’t assess the value” of an exclusive license because, in the absence of an injunction, it was unclear what value that license would give to uBid or to MercExchange over time. *Id.* at 217-18. It could be tremendously valuable, if an injunction entered to prevent the threat of future infringement, or it might not be valuable at all, if no injunction entered and there was therefore nothing to prevent eBay from continuing (or resuming) its infringement. *Id.* at 218, 299-300. Likewise, an equity position in uBid, from MercExchange’s perspective, would be worth far less if eBay was not enjoined from infringing the ’265 Patent. In the face of this uncertainty, MercExchange and uBid could not consummate their relationship and did not arrive at an agreement for exclusive license rights to the ’265 Patent in return for equity in uBid. Conf-App 00502811-812 (pp. 206-12); Conf-App 00502764 (¶ 26).

Third, eBay has also done everything within its power to interfere with MercExchange’s efforts to establish licensees and/or customers. For example, eBay used its market power to prevent MercExchange from interacting with potential licensees/customers by excluding MercExchange from public meetings of eBay “power sellers.” *See, e.g.,* Ina Steiner, “The eBay Patent Wars: PESA Summit Skirmish,” AuctionBytes.com (Oct. 29, 2005) (Conf-App 00502840). *See*