

MAYER • BROWN

Intellectual Property Traps in Business Transactions: What Life Sciences Companies Need to Know

January 17, 2013

Deborah Schavey Ruff
druff@mayerbrown.com

Vera A. Nackovic
vnackovic@mayerbrown.com

Melissa A. Anyetei
manyetei@mayerbrown.com

Mayer Brown is a global legal services organization comprising legal practices that are separate entities ("Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP, a limited liability partnership established in the United States; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales; Mayer Brown JSM, a Hong Kong partnership, and its associated entities in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. "Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.

Speakers



Deborah Schavey Ruff
Chicago
+1 312 701 8601
druff@mayerbrown.com



Vera A. Nackovic
Chicago
+1 312 701 8115
vnackovic@mayerbrown.com



Melissa A. Anyetei
Chicago
+1 312 701 7103
manyetei@mayerbrown.com

The Traps

1. All Sales are Final

- Can a licensee receive a refund of royalties paid for intellectual property that is later invalidated?

2. Yours, Mine & Ours

- So what's the problem with jointly owned patents?

3. Is That IP Automatically Included?

- Is after-acquired IP included under a license?

4. Don't Rely on Future Promises

- Is a promise to assign an invention sufficient to obtain legal title to that invention?

The Traps (cont.)

5. Sadly, Time Machines Are Only Fiction

- Is it really a big deal when there is a significant difference between the effective date and the execution date of a license agreement?

6. The Right to Sue

- Can a patent licensee enforce the licensed patents?

Trap #1: All Sales Are Final

- **Question**: Can a licensee receive a refund of royalties paid for intellectual property that is later invalidated?
- **Answer**: If a licensed patent is declared invalid or unenforceable, licensee cannot obtain a refund for previously paid royalties.

Trap #1: All Sales Are Final (cont.)

- General rule – if a license is silent regarding a finding of invalidity or unenforceability of the underlying patent, a patent licensee may not recover royalties previously paid to a licensor *even if* the patent is subsequently declared invalid. *Geffner v. Linear Rotary Bearings, Inc.*, 124 F.3d 229 (Fed. Cir. 1997).
- However, patent licensee is not obligated to make ongoing royalty payments after a finding of invalidity or unenforceability. *Lear v. Adkins*, 395 U.S. 653 (1969); *see also Studiengesellschaft Kohle M.B.H. v. Shell Oil Co.*, 112 F.3d 1561 (Fed. Cir. 1997).

Trap #1: All Sales Are Final (cont.)

- The Ninth Circuit provided one of the best, and most concise, rationales for the general rule:

The possibility of obtaining a refund of all royalties paid might induce a manufacturer to accept a license based on a patent of doubtful validity, derive the benefits of suppressed competition which the patent affords, and challenge validity only after the patent's expiration. The licensee would have a chance to regain all the royalties paid while having enjoyed the fruits of the license agreement.

Bristol Locknut Co. v. SPS Technologies, Inc., 677 F.2d 1277, 1282 (9th Cir. 1982).

Trap #1: All Sales Are Final (cont.)

- However, a refund of royalty payments may be available if the licensor has induced the licensee to enter into the agreement through fraud.
- In that case, the licensee must show:
 - (1) Licensor knew or believed its patent was invalid when it negotiated the agreement;
 - (2) Licensor deliberately concealed this, intending to mislead the licensee; and
 - (3) Licensee relied upon licensor's misrepresentations.

Ardente, Inc. v. Shanley, 2010 WL 546485 (N.D. Cal. 2010).

- Mere fraud on the patent office (*i.e.*, “inequitable conduct”), while likely probative, is not sufficient. *Transitron Elec. Corp. v. Hughes Aircraft Co.*, 649 F.2d 871, 876 (1st Cir. 1981).

Trap #1: All Sales Are Final (cont.)

- Since absent fraud, “all sales are final,” licensees should consider having the license’s consideration take the following form(s):
 - Ongoing royalties, with payments made on either a monthly or quarterly basis;
 - A research and development payment; and
 - Consider this option if the patents are directed to a new technology, small molecule, biomarker, antibody, etc., as this may allow the licensee to argue that it should be reimbursed for at least part of this payment if the development is ultimately stopped due to loss of patent protection.
 - Milestones directed to events that are farther out in time from entry into the license (e.g., regulatory approval for a new indication, sales targets, etc.).

Trap #1: All Sales Are Final (cont.)

- In contrast, licensors should consider having all or part of the license's consideration take the following form(s):
 - A one-time licensing payment;
 - Significant upfront payments; and/or
 - Milestones directed to events that will occur soon after entry into the license (e.g., positive *in vitro* testing, filing of an IND, initiation of Phase I clinical trials, etc.).
- Licensor should also consider whether it can couple the licensed patents' rights with any know-how or trade secrets to have a basis to collect future royalties *even if* the licensed patents are later invalidated.

Trap #2: Yours, Mine & Ours

- **Question**: So what's the problem with jointly owned patents?
- **Answer**: Jointly owned patents can present logistical problems and challenges.

Trap #2: Yours, Mine & Ours (cont.)

- General rule for patents
 - In the absence of any agreement to the contrary, each of the joint owners of a patent may make, use, offer to sell or sell the patented invention within the United States, or import the patented invention into the United States, *without the consent of and without accounting to* the other owners. 35 U.S.C. § 262 (2012).

Trap #2: Yours, Mine & Ours (cont.)

- **Joint ownership is best avoided because of the logistical problems and challenges it may create:**
 - Ability of each owner to separately transfer or license the patents dilutes the value for all owners;
 - All co-owners must sue an infringer;
 - Warranties typically require full ownership;
 - Challenge for a company's tax advisors to value jointly owned patents;
 - Different rules for jointly owned patents across the globe; and
 - Added legal and administrative costs since all ability to exploit and enforce the jointly owned patents otherwise has to be handled contractually.

Trap #2: Yours, Mine & Ours (cont.)

- **Alternatives to jointly owned patents**

- One party may own all of the patents generated by the collaborative innovation and license it to the other party.
- Differing business needs of the parties may create different patent coverage needs. Consider dividing the patent portfolio out between the parties, based on business objectives. Cross-licenses could be added.
- Patent portfolio may be divided up between parties in order to distribute costs, with cross-licenses providing necessary coverage to fulfill business needs.
- Consider an SPV to own the jointly owned patent portfolio.

Trap #3: Is That IP Automatically Included?

- **Question**: Is after-acquired IP included under a license?
- **Answer**: Potentially, so be aware that after-acquired patents may be included in the scope of licensed rights.

Trap #3: Is That IP Automatically Included? (cont.)

- General rule – a licensor may not assert after-acquired patents against a licensee to prevent licensee from practicing the licensed invention or to seek greater royalties.
- Courts will imply a license to the after-acquired patent. *General Protecht Grp., Inc. v. Leviton Mfg. Co., Inc.*, 651 F.3d 1355 (Fed. Cir. 2011).

Trap #3: Is That IP Automatically Included? (cont.)

- **The policy behind the general rule is to protect the expectations of the parties.**
 - Had the parties known of an existing or impending after-acquired patent, they would not have agreed that it could be used to halt business or re-negotiate the agreement at a later date.
- **The rule is also based in principles of fairness and legal estoppel as it would be inequitable for a licensor of a patent to negate the licensed right by asserting against the licensee a later-acquired patent.**
 - Thus, the licensor is estopped from taking back in any extent that for which he has already received consideration.
 - *See TransCore, L.P. v. Elec. Transaction Consultants Corp.*, 563 F.3d 1271 (Fed. Cir. 2009) (“the implied license doctrine involves the fact that the licensor (or assignor) has licensed (or assigned) a definable property right for valuable consideration, and then has attempted to derogate or detract from that right. The grantor is estopped from taking back in any extent that for which he has already received consideration.”)

Trap #3: Is That IP Automatically Included? (cont.)

- Courts are more likely to find an implied license when the license agreement provides a subject matter description of the patents to be licensed, instead of a specific schedule of patents.
- However, even if an agreement includes a schedule, a license to after-acquired patents may be implied. *Minn. Mining & Mfg. Co. ["3M"] v. E.I. du Pont de Nemours & Co.*, 448 F.2d 54, 57 (7th Cir. 1971).
- Courts have even ignored boilerplate language purporting to exclude implied licenses. *Id.*

Trap #3: Is That IP Automatically Included? (cont.)

- *Exceptions*

- License will not be implied if licensee was aware of, and agreement still excluded, after-acquired patent.
- License may not be implied in a technical standard-setting process (e.g., standards for communication and interoperability of mobile telephones). *Apple Inc. v. Samsung Elecs. Co., Ltd.*, 2011 WL 4948567 (N.D. Cal. 2011); *Rambus Inc. v. F.T.C.*, 522 F.3d 456 (D.C. Cir. 2008).

Trap #3: Is That IP Automatically Included? (cont.)

- In light of the rule, when drafting agreements, licensors should take the following actions:
 - Include language in the license agreement providing that any “rights not granted are reserved”;
 - Include a “no implied license” clause; and
 - Schedule the licensed patents. Do not rely on a functional description of the patent rights granted.
 - If feasible, also include specific agreement from licensee that the license is limited to scheduled patents only.

Trap #3: Is That IP Automatically Included? (cont.)

- In light of the rule, when drafting agreements, licensees should take the following actions:
 - Include language in the agreement providing that any after-acquired patents relating to the licensed technology are included for no additional royalty.
 - If specific schedules are listed, the license should provide that continuing applications and/or applications of related subject matter are included in the licensed patent rights.

Trap #4: Don't Rely on Future Promises

- **Question**: Is a promise to assign an invention sufficient to obtain legal title to that invention?
- **Answer**: No, a promise to assign rights in the future is not an immediate transfer of those rights.

Trap #4: Don't Rely on Future Promises (cont.)

- The general rule – contractual language such as
 - “agree to assign”
 - “will assign” or “will be assigned”
 - “an agreement to assign”

reflects only a promise to assign rights in the future, and does not amount to an immediate transfer of expectant interests.

See Bd. of Tr. of Leland Stanford Univ. v. Roche Molecular Sys., 583 F.3d 832, 841 (Fed. Cir. 2009).

- In these instances, a subsequent written instrument is needed to actually complete the assignment.

Trap #4: Don't Rely on Future Promises (cont.)

- In contrast, contractual language such as
 - “do hereby assign”
 - “I assign”
 - “I will and do hereby assign”
 - “shall belong”

creates a present assignment of the inventor's existing or future inventions, and therefore is an automatic transfer of rights. *Id.*

Trap #4: Don't Rely on Future Promises (cont.)

- In a situation where you have a present assignment, “once the invention is made and an application for the patent is filed . . . legal title to the rights accruing thereunder would be in the assignee . . . and the assignor-inventor would have nothing remaining to assign.” *Id.*

Trap #4: Don't Rely on Future Promises (cont.)

- *However*, the assignee should record that assignment with the Patent Office to protect against the following:
 - Claims that someone is a *bona fide* purchaser of the patent;
 - Ownership claims that are defeated under the statute of limitations or laches; and
 - Lack of standing to bring an infringement action.
- Keep in mind that these issues can impact multiple patents in a family.

Trap #5: Sadly, Time Machines Are Only Fiction

- **Question**: Is it really a big deal when there is a significant difference between the effective date and the execution date of a license agreement?
- **Answer**: Yes, parties should proceed with caution when there is a significant difference between the effective date and the execution date of a license agreement as such action could raise several potential issues.

Trap #5: Sadly, Time Machines Are Only Fiction (cont.)

- Reasons the effective date and execution date of a license agreement may differ include:
 - Changes in corporate tax structures;
 - To establish standing for the licensee to sue independently; and
 - To memorialize what has been going on in practice.

Trap #5: Sadly, Time Machines Are Only Fiction (cont.)

- Issues that may result from differences in the effective date and execution date of a license agreement include:
 - A licensee may lack standing to initiate an infringement action; and
 - Interference with rights of sublicensees and third parties.

Trap #5: Sadly, Time Machines Are Only Fiction (cont.)

- A licensee may lack standing to initiate an infringement action.
 - A plaintiff is “required to have legal title to the patents on the day it filed the complaint,” and this requirement cannot be met retroactively. *See, e.g., Abraxis Bioscience, Inc. v. Navinta LLC*, 625 F.3d 1359, 1366 (Fed. Cir. 2010); *see also Schultz v. iGPS Co., LLC*, 2011 WL 3651267 at *3 (N.D. Ill. 2011).
 - Thus, a licensor cannot transfer rights to a licensee “after-the-fact” by backdating the effective date so as to allow the licensee to independently file an infringement complaint. If it later turns out that the licensor did not own the IP as of the effective date, the licensee may be deemed not to have standing to sue.
 - This can be particularly critical in the Hatch-Waxman context, where the patent holder only has 45 days from receipt of the Paragraph IV Notice to file suit and trigger the 30-month stay. *See* 21 U.S.C. § 355(j)(5)(B)(iii) (2012).

Trap #5: Sadly, Time Machines Are Only Fiction (cont.)

- Interference with rights of sublicensees and third parties
 - Imagine the following scenario:
 - January 1, 2011: Licensor and Licensee, a subsidiary to Licensor, enter into a license agreement. Among the rights granted to Licensee was the right to sublicense the “Licensed IP.”
 - June 6, 2011: Licensee sublicenses the Licensed IP to Sublicensee.
 - January 1, 2012: Licensor and Licensee enter into an amendment to the License, effective January 1, 2011 whereby they strike certain patents from the definition of Licensed IP.
 - The January 1, 2012 Amendment necessarily affects the rights of Sublicensee. Consequently, Licensee may be liable to Sublicensee under state law for breach of contract.
 - It is well established that mutual assent is required to effect contractual modifications. *See Metro Commc’ns Co. v. Ameritech Mobile Commc’ns, Inc.*, 984 F.2d 739 (6th Cir. 1993).

Trap #5: Sadly, Time Machines Are Only Fiction (cont.)

- Interference with rights of sublicensees and third parties
(cont.)
 - Imagine yet another scenario:
 - January 1, 2009: Licensor and Licensee, a subsidiary to Licensor, enter into a license agreement whereby Licensee obtained the right to make, use, and sell products under Patents A and B “Licensed IP” for a period of ten years.
 - June 6, 2010: Licensor acquires Patents C and D and licenses them to Third Party.
 - January 1, 2012: For tax restructuring purposes, Licensor and Licensee enter into an amendment to the License, effective January 1, 2011, whereby Patents C and D are added to the definition of Licensed IP. The parties drafting the amendment are unaware of, or do not recall, the June 6, 2010 License to Third Party.
 - Licensor may be liable to Third Party for breach of contract, and Licensee’s rights may be subject to Third Party’s rights.

Trap #5: Sadly, Time Machines Are Only Fiction (cont.)

- Thus, prior to entering into a license agreement or amendment that is retroactively effective:
 - The parties should confirm the extent of rights that the licensor had on the execution date and on the effective date; and
 - Licensors should consider the possibility of future retroactive modifications to the master agreement when entering into it with licensee.
 - Licensor may not want to grant licensee the right to sublicense without prior written consent.
 - Licensor may want a shorter term to a license agreement.

Trap #6: Right to Sue

- **Question**: Can a patent licensee enforce the licensed patents?
- **Answer**: It depends on the type of license.

Trap #6: Right to Sue (cont.)

- General rules
 - *Nonexclusive patent licensees* – do not have the right to sue for infringement regardless of the rights set forth in the license agreement.
 - *Exclusive patent licensees* – have the right to sue for infringements that occur during the effective term of the license agreement.

Trap #6: Right to Sue (cont.)

- Exclusive licenses – patents
 - An exclusive licensee generally will have the right to sue for patent infringement that occurs during the term of the license.
 - An exclusive licensee cannot sue for acts of infringement that occur before or after the licensee's period of ownership, unless the license agreement clearly sets forth this right.
 - Language in a license agreement that states “right to sue for infringement” is not sufficient. The agreement must specifically state that the right to sue is for past and/or future infringement.

Trap #6: Right to Sue (cont.)

- Exclusive licenses – patents (cont.)
 - However, the question becomes: Does the exclusive licensee have standing to sue on its own, or must the patent holder also be named in the action?
 - The exclusive licensee has standing to bring the action to sue on its own if the license agreement conveys “all substantial rights” in the patent, which is determined by the following factors:
 - ✓ Did licensor retain any right to make, use or sell?
 - ✓ Is the term of the license commensurate with the life of the patent?
 - ✓ Does the license affirmatively grant the licensee the right to sue infringers?
 - ✓ Who owns improvements?
 - ✓ Can the licensee sublicense the patent?

Trap #6: Right to Sue (cont.)

- Exclusive licenses – patents (cont.)
 - To grant a license that includes the right to sue for infringement independently, the license agreement should expressly grant “all substantial rights” in the patent so that the license is tantamount to an assignment.
 - Simply including the language – “licensor grants licensee all substantial rights in and to the patent” – will not suffice.

Questions

- Please use the Q&A panel on the right side of your screen to submit a question.

Notice

- Mayer Brown is a global legal services organization comprising legal practices that are separate entities (the "Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP, a limited liability partnership established in the United States; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales; and JSM, a Hong Kong partnership, and its associated entities in Asia. The Mayer Brown Practices are known as Mayer Brown JSM in Asia.
- The materials in this presentation are provided for informational purposes only and do not constitute legal or other professional advice. You should not and may not rely upon any information in this presentation without seeking the advice of a suitably qualified attorney who is familiar with your particular circumstances. The Mayer Brown Practices assume no responsibility for information provided in this presentation or its accuracy or completeness and disclaims all liability in respect of such information.
- The Mayer Brown Practices are, unless otherwise stated, the owner of the copyright of this presentation and its contents. No part of this presentation may be published, distributed, extracted, re-utilized or reproduced in any materials form (including photocopying or storing it in any medium by electronic means and whether or not transiently or incidentally to some other use of this publication) except if previously authorized in writing.

MAYER • BROWN

Intellectual Property Traps in Business Transactions: What Life Sciences Companies Need to Know

January 17, 2013

Deborah Schavey Ruff
druff@mayerbrown.com

Vera A. Nackovic
vnackovic@mayerbrown.com

Melissa A. Anyetei
manyetei@mayerbrown.com

Mayer Brown is a global legal services organization comprising legal practices that are separate entities ("Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP, a limited liability partnership established in the United States; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales; Mayer Brown JSM, a Hong Kong partnership, and its associated entities in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. "Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.