Licensee Beware: The Seventh Circuit Holds That a Patent License by Any Other Name Is Not the Same

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LICENSEE BEWARE: THE SEVENTH CIRCUIT HOLDS THAT A PATENT LICENSE BY ANY OTHER NAME IS NOT THE SAME

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INTRODUCTION

Intellectual property licensing has grown significantly over the years with a global market estimated at more than $100 billion.1 In fact, “intellectual property assets account for 40% of the net value of all corporations in America.”2 Notwithstanding the likelihood of more and more licensing transactions, a complex area of the law, patent licensing has not received much attention in legal journals and scholarly publications.3 As companies increasingly license and cross-

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2 Id.

license technologies, issues arising about the nature and meaning of license agreements will likely be litigated, particularly because licensing agreements combine matters governed by state contract law and federal patent law.

One area of patent licensing not discussed in depth is if a settlement for patent infringement may ever be considered a patent license agreement. The legal designation of a patent settlement as a patent license agreement will have implications for licensees with a “most favored licensee” status, a legal clause granting deferential treatment to a licensee in order to prevent a “competitive disadvantage resulting from more-favorable terms granted to another licensee.”

Although some courts have decided this issue, they have decided differently what effect, if any, a patent settlement agreement has on an existing third party licensee with a “most favored licensee” clause in the license agreement.

In *Waterloo Furniture Components Ltd. v. Haworth, Inc.*, a case of first impression, the Seventh Circuit recently held that “[a] settlement for past infringement entered into after [a patent expires is not] a license.” Additionally, the Seventh Circuit acknowledged that federal appellate courts are divided on whether a settlement agreement

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6 Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corp., 103 F.3d 9, 13 (2d Cir. 1997).
7 See Ransburg Electro-Coating Corp. v. Spiller & Spiller, 489 F.2d 974 (7th Cir. 1973) and Studiengesellschaft Kohle v. Novamont Corp., 704 F.2d 48, (2d. Cir. 1983) (each case finding that a patent settlement agreement may not be construed as a license); Shatterproof Glass Corp. v. Libbey-Owens-Ford Co., 482 F.2d 317 (6th Cir. 1973) and Studiengesellschaft Kohle v. Hercules, 105 F.3d 629 (Fed. Cir. 1997) (each ruling that a patent settlement agreement may be considered a license).
8 Waterloo Furniture Components Ltd. v. Haworth, Inc. (“*Waterloo II*”), 467 F. 3d 641 (7th Cir. 2006).
9 For the first time, a court explicitly held that a settlement agreement is not a license in the context of an expired patent. Other courts, including the Seventh Circuit, have resolved the issue (albeit differently) in the context of an unexpired patent, see supra note 7.
10 *Waterloo II*, 467 F.3d at 647 (emphasis added).
entered into before a patent expires constitutes a license. The linchpin in any of the regional appellate court’s reasoning on the issue boils down its their correct or incorrect understanding of what essentially a patent license constitutes. For example, what ultimate effect does a patent license serve and is a license solely prospective in nature with no retroactive qualities?

Part I of this Note describes the relevant background of patent law, patent infringement, and patent licenses. Part II explains the circuit split among the Federal Regional Courts of Appeal, including the Waterloo decision. Part III of this Note contends that patent licenses have a unique nature given their purpose, including retroactive qualities, and that a settlement for past patent infringement, regardless of whether the patent has expired or not, may constitute a license, especially when the settlement implicates a “most favored licensee” clause. Part IV of this Note explains the implications of the Seventh Circuit’s Waterloo decision, especially because of the increasing importance of patent law and licensing agreements.

I. BACKGROUND

A. Patent Law

A patent grants the patentee a right to exclude others from making, using, selling, or offering to sell the patented invention within the United States, or importing the invention to the United States. Frequently the right to exclude is commonly misunderstood. Many

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11 Id. at 647 n.1.
12 Although sometimes referred to as a “most favored nation” clause, see, e.g., id. at 643-48, to be more accurate, this Note uses only the phrase “most favored licensee”.
13 The word patentee as used in this Note has the same meaning as its statutory definition in 35 U.S.C. § 100 (d) (2000) (“The word ‘patentee’ includes not only the patentee to whom the patent was issued but also the successors in title to the patentee”).
people, including those in the legal profession,\textsuperscript{15} experts on patent law,\textsuperscript{16} and even judges,\textsuperscript{17} conflate the statutory right to exclude with a permissive and exclusive right of the patentee to actually make, use, or sell the patented invention. The resulting confusion is understandable, however. Over the years, Congress has changed the language of the statute specifying the rights granted a patentee,\textsuperscript{18} and it is common for people to assume that intellectual property ownership, like other types of property ownership, carries with it the three basic property rights: the right to use, the right to exclude, and the right to transfer.\textsuperscript{19}

Patent laws have existed since 1790, but Congress enacted the current patent statute in 1952 under Title 35 of the United States Code.\textsuperscript{20} Because a patent grants an exclusive right to the mental concept of the invention, “a patent protects no single physical embodiment of an invention as such; rather it controls the abstract information in the invention, as expressed in the patent’s claims.”\textsuperscript{21} In

\textsuperscript{15} For instance, the well-known and generally respected Black’s Law Dictionary defined the rights a patent grants as “the exclusive right to make, use or sell an invention for a specified period” in the 7th edition. BLACK’S LAW DICTIONARY 1147 (7th ed. 1999). However, the 8th edition defines the rights a patent grants as the “right to exclude.” BLACK’S LAW DICTIONARY 1156 (8th ed. 2004).

\textsuperscript{16} See, e.g., Arthur R. Miller & Michael H. Davis, INTELLECTUAL PROPERTY: PATENTS, TRADEMARKS AND COPYRIGHT IN A NUTSHELL 11 (1983) (describing the right a patent grants as “giving the patentee the exclusive right to make, use, or sell the invention”).

\textsuperscript{17} United States v. Univis Lens Co., 316 U.S. 241, 250 (1942) (“The full extent of the monopoly is the patentee’s “exclusive right to make, use, and vend the invention or discovery”).

\textsuperscript{18} See Part IIIA1, infra.

\textsuperscript{19} See Kenneth L. Port, Jay Dratler, Jr., Faye M. Hammersley, Terence P. McElwee, Charles R. McManis & Barbara A. Wrigley, LICENSING INTELLECTUAL PROPERTY IN THE INFORMATION AGE 5-6 (2d ed. 2005).


exchange for disclosing the patented invention in sufficient detail within the patent application, the Government grants the patentee a twenty-year monopoly from the filing date of the patent to exercise any of the exclusionary rights.\textsuperscript{22}

The monopolistic rights give the patentee the ability to gain financially from the patent in various ways.\textsuperscript{23} The patentee may sell the invention or rights to the invention at monopolistic prices to recoup any investment costs into research of the patented technology, or simply to realize a profit.\textsuperscript{24} The patentee may assign or license all or some of the patent rights to another in exchange for any price or even no price at all.\textsuperscript{25} A patentee may license use of the patented technology to another in exchange for royalties, rights to use another patented technology (cross-licensing agreements), or for just about anything that the parties agree upon.\textsuperscript{26} In short, a patent grants rights similar in function to holders of tangible property\textsuperscript{27}—except the right to use.\textsuperscript{28}

\begin{itemize}
\item were to be limited to devices operated precisely as a specification-described embodiment is operated, there would be no need for claims\textquotedblright).\textsuperscript{22}
\item James Bessen & Michael J. Meurer, \textit{Lessons For Patent Policy From Empirical Research on Patent Litigation}, 9 LEWIS & CLARK L. REV. 1, 9-10 (2005) (discussing three main sources of profits derived from patents: (1) excluding competitors, (2) forcing competitors to accept licenses, (3) strategically using patents to avoid litigation such as using patents to facilitate cross-licensing and opportunistic and anticompetitive patent suits based on weak or invalid patents).
\item See, e.g., Crown Die & Tool Co. v. Nye Tool & Mach. Works, 261 U.S. 24, 36-37 (1923) (\textquotedblleft[T]he government is not granting the common-law right to make, use and vend, but it is granting the incident of exclusive ownership of that common-law right, which [cannot] be enjoyed save with the common-law right\textquotedblright and that \textquotedblleft a patent confers a monopoly\textquotedblright); W.L. Gore & Assocs., Inc. v. Carlisle Corp., 529 F.2d 614 (3d Cir. 1976) (noting that a patent holder does not misuse a patent when the patentee demands an exorbitant royalty rate, essentially refusing to do business with the willful infringer).
\item See Bessen & Meurer, \textit{supra} note 23, at 9-10.
\item See 35 U.S.C. § 154(a) (2000); see also Part IIIA1, \textit{infra}.
\end{itemize}
B. Patent Infringement

Patent infringement occurs when “[anyone] without authority makes, uses or sells any patented invention, within the United States during the term of the patent thereof.” 29 A patent term begins the day the patent issues and ends twenty years from the filing date of the patent application. 30 An entity may infringe a patent in three ways: direct infringement, contributory infringement, and induced infringement. 31

The remedy for patent infringement may include injunctions, 32 monetary damages (including treble damages), 33 and even attorney’s fees 34 in warranted cases. By statute, the court awards monetary damages adequate to compensate for infringing the patented invention. 35 A court may calculate adequate compensation based on the patentee’s lost profits due to the infringing activities of the infringer. 36

Furthermore, statutory law mandates a minimum amount of damages awarded to the patentee. 37 A court calculates the “floor” award for patent infringement damage based on “a reasonable royalty for the use made of the invention by the infringer.” 38 However, statutory law also places temporal limits on the amount of damages sought by the patentee. 39 35 U.S.C. § 286 confines collecting damages to six years “prior to the filing” of an infringement claim. 40

38 Id.
40 Id.
Lastly, the Court of Appeals for the Federal Circuit has exclusive appellate jurisdiction in cases involving issues of patent law. The Federal Circuit is a court of Federal Appeals especially created to hear, among other things, patent cases appealed from Federal District Courts and, as such, has no geographic limitations within the United States and its territories. Thus, substantive patent law comes substantially from the Federal Circuit or the Supreme Court. Although after Holmes Group Inc. v. Vornado Air Circulation Systems, other federal appellate courts may decide substantive patent law issues when a compulsory counterclaim pleads substantive patent law issues, even though the complaint does not assert any claim arising under the patent laws of the United States.

C. Licensing

The owner of a patent may grant licenses to others. Since the patentee has the right to exclude others from making, using, offering for sale or selling, or importing the invention, no one else may engage in any of these acts without the patentee’s permission without risking liability for infringement. While federal statutory and case law governs substantive patent law, state laws govern interpretation of license agreements due to their contractual nature. However, where

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state contract law yields inconsistent results with federal patent policy, federal patent law governs.\textsuperscript{50}

Patent license agreements may be exclusive, partially exclusive, or nonexclusive.\textsuperscript{51} A license “[i]n its simplest form . . . means only leave to do a thing which the licensor otherwise would have a right to prevent.”\textsuperscript{52} Thus, a patent license agreement is in essence nothing more than a promise by the licensor not to sue the licensee,\textsuperscript{53} though an exclusive license agreement may also grant the licensee the right to sue other infringers.\textsuperscript{54}

A patentee may limit the license agreement by geography, by duration, or by invention scope.\textsuperscript{55} A license may grant unrestricted or limited use in a particular field.\textsuperscript{56} For example, a patentee may limit a license agreement for a patented veterinary drug to only dogs in California for two years but not other animals in other states. Generally, the license agreement may include whatever provisions the

\textsuperscript{50} In re CFLC, Inc., 89 F.3d 673, 677 (9th Cir. 1996) (quoting Lear v. Adkins, 395 U.S. 653, 673 (1969)) (“The construction of a patent license is generally a matter of state contract law, except where state law ‘would be inconsistent with the aims of federal patent policy’”).

\textsuperscript{51} Drackett Chem. Co. v. Chamberlain Co., 63 F.2d 853, 855 (6th Cir. 1933).

\textsuperscript{52} W. Elec. Co., Inc. v. Pacent Reproducer Corp. 42 F.2d 116, 118 (2d Cir. 1930).

\textsuperscript{53} Jim Arnold Corp. v. Hydrotech Sys., 109 F.3d 1567, 1577 (Fed. Cir. 1997).

\textsuperscript{54} See Group One, Ltd. v. Hallmark Cards, Inc., 254 F.3d 1041, 1053 (Fed. Cir. 2001) (Lourie, J. additional remarks) (“A patent license, if it is non-exclusive, is an agreement to forbear from suit. If the license is exclusive, it may be tantamount to an assignment of the patent”); see also Intellectual Prop. Dev., Inc. v. TCI Cablevision of Cal., Inc., 248 F.3d 1333, 1345 (Fed. Cir. 2001) (“An exclusive licensee receives more substantial rights in a patent than a nonexclusive licensee, but receives fewer rights than an assignee of all substantial patent rights”).

\textsuperscript{55} See Spindelfabrik Suessen-Schurr Stahlecker & Grill GmbH v. Schubert & Salzer Maschinenfabrik Aktiengesellschaft, 829 F.2d 1075, 1081 (Fed. Cir. 1987) (“In any event, patent license agreements can be written to convey different scopes of promises not to sue, e.g., a promise not to sue under a specific patent or, more broadly, a promise not to sue under any patent the licensor now has or may acquire in the future”); see also Intellectual Prop. Dev., 248 F.3d at 1345 (“[A]n exclusive licensee could receive the exclusive right to practice an invention within a given limited territory”).

parties agree upon, such as the payment of royalties, duration of the agreement, exclusive or non-exclusive terms, and permitted uses—for example, selling but not making.\textsuperscript{57}

A license is a contract,\textsuperscript{58} and may be written or oral,\textsuperscript{59} express\textsuperscript{60} or implied.\textsuperscript{61} The terms and conditions of the license must be consistent with the scope of the patent.\textsuperscript{62} No particular form of license is required.\textsuperscript{63} A license may also explicitly include a release from past infringement,\textsuperscript{64} though the agreement itself releases the infringer from any rights of the patentee to exclude the infringer from using the patented invention.\textsuperscript{65}

License agreements may also include a “Most Favored Licensee” (MFL) or “Most Favored Nation” clause. A MFL clause protects the licensee from “a competitive disadvantage resulting from more-favorable terms granted to another licensee.”\textsuperscript{66} MFL status assures the licensee that it will not pay more in royalties than another licensee, and usually that the licensor will inform the licensee of any other

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\item \textsuperscript{57} Id. at 127 (quoting United States v. Gen. Elec. Co., 272 U.S. 476, 489 (1926)) (“[T]he patentee may grant a license ‘upon any condition the performance of which is reasonably within the reward which the patentee by the grant of the patent is entitled to secure’”).
\item \textsuperscript{58} Metabolite Labs., Inc. v. Lab. Corp. of Am. Holdings, 370 F.3d 1354, 1369-70 (Fed. Cir. 2004).
\item \textsuperscript{59} De Forest Radio Tel. Co. v. United States, 273 U.S. 236, 241 (1927).
\item \textsuperscript{60} Michael J. Swope, Comment, \textit{Recent Developments in Patent Law: Implied License – An Emerging Threat to Contributory Infringement Protection}, 68 \textit{TEMP. L. REV.} 281 (1995) (“An express license operates by written or oral contract between the patent owner and the purchaser of the product”).
\item \textsuperscript{61} Hughey, \textit{supra} note 3, at 55-56.
\item \textsuperscript{62} Id.
\item \textsuperscript{63} Id.
\item \textsuperscript{64} United States v. Line Material Co., 333 U.S. 287, 297 (1948) (“By accepting [the license agreements,] they secured release from claims for past infringement through a provision to that effect in the license”).
\item \textsuperscript{65} Id. at 343 (“[The] nonexclusive license agreement . . . served only to release the licensee from the right of the patent holder to exclude him from making, using or selling a patented article”); \textit{see} Standard Oil Co. v. United States, 283 U.S. 163, 168 (1931).
\item \textsuperscript{66} Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corp., 103 F.3d 9, 13 (2d Cir. 1997).
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licensees and the terms of their agreements. Essentially, MFL clauses suggest that licensed competitors should be treated equally, so long as they bear equivalent obligations to the licensor/patentee.

II. THE CIRCUIT SPLIT AND WATERLOO

Four federal courts of appeal have decided the issue of whether a settlement agreement for patent infringement may constitute a license for an unexpired patent: the Second, Sixth, Seventh, and Federal Circuits. The Second and Seventh circuits decided the issue differently than the Sixth and Federal circuits, and thus their decisions differ in the effect a patent settlement agreement has on an existing third party licensee with a “most favored licensee” clause in the license agreement.

The Seventh Circuit in the Waterloo decision, however, is the only appellate court to decide the issue in the context of an expired patent. A review of the reasoning justifying the holdings of the other federal regional appellate courts in the context of an unexpired patent will help define the split among the circuits and illuminate how that split influenced the Seventh Circuit’s Waterloo decision. First, this Note will explain the circuit split, beginning with the Second and Seventh circuits, followed by the Sixth and Federal Circuits. Finally, this Note will explain the relevant details and reasoning of the Seventh Circuit’s Waterloo decision.

See, e.g., Studiengesellschaft Kohle, m.b.H. v. Hercules, Inc., 105 F.3d 629, 633 (Fed. Cir. 1997) (noting that the licensor's obligation was to notify the licensee of the terms and conditions of any other license agreements, not simply "more favorable” license agreements in the licensors opinion).


See Ransburg, 489 F.2d 974 and Novamont, 704 F.2d 48 (each case finding that a patent settlement agreement may not be construed as a license); Shatterproof Glass, 482 F.2d 317 and Hercules, 105 F.3d 629 (each ruling that a patent settlement agreement may be considered a license).
A. Other Federal Courts of Appeal Decisions

1. According to the Second and Seventh Circuits, a settlement agreement is not a license before a patent expires.

Two federal appellate circuits have held that a settlement agreement entered into before a patent expires is not a license agreement: the Second Circuit in Studiengesellschaft Kohle v. Novamont Corp. and the Seventh Circuit in Ransburg Electro-Coating Corp. v. Spiller & Spiller. Because this Note focuses on the Waterloo decision, only a cursory overview of the reasoning and any pertinent facts in the cases will be given, beginning with the Second Circuit decision in Novamont Corp.

In Novamont Corp., the court held that a settlement agreement for past infringement did not implicate the MFL status of a licensee. The court considered the “treatment of an earlier licensee, who was entitled to a MFL clause and a competitor who took a license later, after a period of infringing activity.” The licensor granted a license to Novamont in 1967 to produce certain polymers of propylene. The license included a “Most Favored Licensee” (MFL) clause requiring the licensor to “promptly furnish Novamont with the full text of any licenses granted under the [patent], if . . . considered in their entirety, the licenses were more favorable than those in the licensee agreement [with Novamont].”

Later, the licensor granted a third-party competitor a license but did not promptly inform Novamont about the new agreement. When the licensor finally did inform Novamont of the agreement, the licensor did not include in the notification a particular clause within

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70 704 F.2d 48 (2d Cir. 1983).
71 489 F.2d 974 (7th Cir. 1973).
72 Novamont, 704 F.2d at 52.
73 Id.
74 Id. at 50.
75 Id.
76 Id. at 51-52
the agreement.\textsuperscript{77} The clause in the agreement released the third-party competitor from past infringement pending the outcome of another infringement case and permitted the third-party competitor to credit any money the licensor recovered from the third-party competitor for past infringement against royalties the third-party competitor owed the licensor.\textsuperscript{78}

In other words, the third-party competitor would pay the licensor royalties for past infringement that would count towards the future royalties the third-party competitor owed the licensor under the license agreement, a two-birds-for-one-stone-type agreement. After Novamont learned of the undisclosed clause, they requested the same treatment, believing that the clause permitted the third-party competitor to pay a reduced royalty because the royalty covered both past and future infringing use of the patented technology.\textsuperscript{79}

The Second Circuit disagreed that the clause settling past infringement implicated Novamont’s MFL status for two reasons.\textsuperscript{80} First, Novamont could not have benefited from the second license agreement because Novamont had not been an infringer at the time the third-party competitor and the licensor reached the second agreement.\textsuperscript{81}

Second, granting Novamont the benefit of the second license agreement terms would require the licensor to insist upon a payment for past infringement from the third-party competitor equal to the “royalty terms governing [Novamont] during the same period, or [the licensor] must make a refund to [Novamont].”\textsuperscript{82} Ultimately, the court decided that MFL clauses do not require such a high “degree of equivalency” and courts “have declined to interpret the clauses with that breadth.”\textsuperscript{83} The court declined to discuss in any detail the prospective or retroactive qualities of a patent license agreement,
briefly acknowledging that the Sixth Circuit’s earlier reasoning in *Shatterproof Glass* did not persuade them.84

Next, this Note will review the Seventh Circuit’s *Ransburg* decision, holding that a patent license agreement is prospective in nature and not equivalent to a release for past infringement.85 In *Ransburg*, an accused infringer settled a patent infringement suit by making monthly installments to compensate the patentee.86 Later, in a separate infringement action, a court held the patent invalid.87 The infringer subsequently ceased making payments under the terms of the settlement agreement.88 The patentee sued the accused infringer to recover the remaining amount owed under the settlement agreement.89

The Seventh Circuit rejected the infringer’s arguments that the settlement agreement was a retroactive licensing agreement and that because the patent was now invalid, the infringer no longer had to pay the patentee as obligated by the earlier settlement agreement.90

To require the infringer to continue payment of the settlement agreement would be contrary to the Supreme Court’s policy of “ridding the public of invalid patents thereby dedicating ideas to the common good,” or so the infringer argued.91 The court disagreed with the infringer, reasoning that a patent license has only a prospective quality, negating any possible retroactive effects of a patent license.92 Thus, a patent license is not equivalent to a release for past wrongdoing (a settlement agreement).93 Moreover, the court listed the public policy reasons for continuing to enforce a settlement agreement

84 Id. at 52 n.5.
85 Ransburg Electro-Coating Corp. v. Spiller & Spiller, 489 F.2d 974, 977-78 (7th Cir. 1973).
86 Id. at 976.
87 Id.
88 Id.
89 Id.
90 Id. at 977.
91 Id.
92 Id. at 977-78.
93 Id.
for infringement of a patent, even though the patent was subsequently found invalid.94

2. According to the Sixth and Federal Circuits, a settlement agreement may be a license before a patent expires.

In contrast to Novamont and Ransburg, two other federal appellate circuits have held that a settlement agreement entered into before a patent expires is a license agreement: the Sixth Circuit in Shatterproof Glass Corp. v. Libbey-Owens-Ford Co.95 and the Federal Circuit in Studiengesellschaft Kohle v. Hercules.96 Again, only a cursory overview of the reasoning and any pertinent facts in the cases will be given, beginning with the Sixth Circuit decision in Shatterproof Glass.

The Shatterproof Glass case, in which the Sixth circuit held that a patent settlement agreement may constitute a license for purposes of a MFL clause,97 entails a few unique facts. Shatterproof Glass, a second licensee, entered into a licensing agreement with a licensor in 1955.98 The licensing agreement included a MFL clause that covered not only future licenses but also already existing licenses with other third parties.99

The first licensee had originally entered a licensing agreement in 1931.100 Later, the first licensee entered into another agreement in 1961 for a release of infringement prior to 1961 of certain patents and a paid-up license under another patent in exchange for lump sum payments.101 The license agreement also included a royalty rate for future use of other patents.102

The licensor failed to notify Shatterproof Glass of the more favorable terms found in the 1931 and 1961 agreements, in violation

94 Id. at 977-78.
95 482 F.2d 317 (6th 1973).
96 105 F.3d 629 (Fed. Cir. 1997).
97 Shatterproof Glass, 482 F.2d at 321.
98 Id. at 318.
99 Id. at 318 n.1.
100 Id. at 319.
101 Id.
102 Id.
of the MFL clause. Shatterproof Glass sought to recover royalties already paid in excess of the more favorable rates the first licensee had paid.

Shatterproof Glass argued that the “nature of the [agreements]” and not their label is controlling, and “that properly construed, the document is a retroactive license.” The Sixth Circuit agreed, reasoning that “a release can, in certain circumstances, have the effect of and be construed as a license.” Additionally the court recognized that a patent license is “a mere waiver of the right to sue by the patentee.” Moreover, the agreement that released the first licensee from any claims of infringement “was in effect a settlement by payment of just compensation for previous use of the patent . . . [otherwise] evasion of a ‘favored [licensee]’ clause [would be] possible.”

Turning now to the Studiengesellschaft Kohle, m.b.H., v. Hercules, Inc. case, the Federal Circuit held that a MFL licensee was entitled to the same terms as a settlement for past infringement by a third-party competitor. In Hercules, a licensor, failed to notify a MFL licensee, Hercules, of another license agreement with a third-party competitor, in violation of the MFL clause. Meanwhile, Hercules had stopped paying royalties during a six-year period, triggering the licensor to commence a patent infringement lawsuit against Hercules.

After Hercules discovered the third-party competitor license agreement with more favorable royalty rates and a release for past infringement, Hercules requested a retroactive license with royalty rates similar to the third-party competitor license agreement, reaching

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103 Id. at 319-20.
104 Id.
105 Id. at 320.
106 Id. at 321.
107 Shatterproof Glass, 482 F.2d at 320.
108 Id. at 321.
109 105 F.3d 629 (Fed. Cir. 1997).
110 Id. at 634.
111 Id. at 631-32.
112 Id. at 632.
back to the date any allegedly infringing activities began, “thereby insulating itself from any infringement claim.”

The Federal Circuit observed that “absolving six years of infringement via a retroactive license [was] troubling” because it was uncertain if Hercules would have accepted a similar agreement had the licensor offered Hercules the same terms as the third-party competitor license agreement within the timeframe required by the MFL clause. Nevertheless, because the licensor breached the MFL clause by not notifying Hercules of the third-party competitor license agreement within the required timeframe, the uncertainty was the licensor’s to bear.

The Federal Circuit ruled that “Hercules [was] entitled to the terms of the [third-party competitor] license effective May 1980, when the [third-party competitor] license became effective.” Notably, the Federal Circuit did not dwell on the prospective-retroactive potential dualism of a patent license as did the Seventh and Sixth circuits. Instead, the court apparently accepted the possibility of a retroactive license as a concept requiring little to no justification, almost as if the concept itself was self-evident. The uncertain actions of the parties caused the Federal Circuit some hesitancy with its decision but not the concept of a retroactive license itself.

The Sixth and Seventh Circuit courts extensively discussed their rationale for why they decided a settlement agreement or release from past infringement may or may not be considered a patent license, emphasizing the retroactive, or alternatively, the sole prospective

113 Id. at 634.
114 Id.
115 Id.
116 Id.
119 See id.
120 See id.
quality of patent licenses. The Seventh Circuit in *Waterloo* was no different.

**B. The Waterloo Case**

The Seventh Circuit is the only court to address whether settlement agreements for past infringement may constitute a patent license even though the patent has expired. In *Waterloo*, the Seventh Circuit held that “[a] settlement for past infringement entered into after [a patent expires is not] a license.” Additionally, the Seventh Circuit acknowledged that federal appellate courts are divided on whether a settlement agreement entered into before a patent expires constitutes a license. As will be discussed in greater detail below, the linchpin in Seventh Circuit’s reasoning boils down to their correct or incorrect understanding of what essentially a patent license constitutes.

*Waterloo* manufactures keyboard support devices. Haworth owned Patent No. 4,616,798 (the ‘798 patent) for a computer keyboard adjustable support, which attaches to the underside of a desk. In December 1992, *Waterloo* and Haworth entered into a licensing agreement to resolve an infringement claim Haworth brought against *Waterloo*. Although the parties executed the agreement in December 1992, it retroactively covered *Waterloo*’s past infringement that occurred before December 1992.

The agreement included a MFL clause wherein Haworth promised to automatically offer *Waterloo* a more favorable royalty rate if

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122 *Waterloo Furniture Components Ltd. v. Haworth, Inc.* ("*Waterloo II*"), 467 F. 3d 641, 647 (7th Cir. 2006) (emphasis added).
123 Id. at 647 n.1.
124 See Part III, infra.
125 Id. at 643.
126 Id. at 644.
127 Id.
Haworth licensed the ‘798 patent to a third party at a more favorable rate. The license agreement also included the express intention of the parties, namely that “Waterloo is treated no less favorably than direct competitors of Waterloo in regard to licensing of the ‘798 patent.” Moreover, Haworth promised to provide written notice to Waterloo of any subsequent third party license agreement and its terms within thirty days following the license agreement’s execution. Michigan law governed the agreement.

In 1997, a third party, SoftView, filed a declaratory judgment action against Haworth, arguing that SoftView was not infringing the ‘798 patent. Haworth filed a counterclaim in June 1998 that SoftView had infringed the ‘798 patent. On December 9, 2003, after five and half years of litigation, the parties reached an agreement in principle to settle the case. A formal settlement was executed on March 24, 2004. Meanwhile, the ‘798 patent expired on October 14, 2003.

Waterloo learned about the settlement agreement and requested a copy from Haworth. Haworth responded that its agreement with SoftView was confidential. Waterloo filed a breach of contract claim in the Northern District of Illinois because it suspected that its licensor, Haworth, had entered into a settlement agreement that offered an infringing competitor more favorable royalty terms than the terms of Waterloo’s own license.

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129 *Waterloo II*, 467 F.3d at 644.
130 *Id.*
131 *Id.*
132 *Id.*
133 *Id.*
134 *Id.*
135 *Id.*
136 *Id.* at 643.
137 *Id.* at 644.
138 *Id.*
Haworth moved for summary judgment, and Waterloo served discovery requests, including a request to see the SoftView/Haworth settlement agreement. The district court halted discovery *sua sponte* and granted Haworth’s summary judgment motion after allowing the parties to submit briefs on the summary judgment motion.

The Seventh Circuit affirmed the district court’s judgment, holding that “a settlement for past infringement entered into after [a] patent’s expiration [does not] constitute a license.” The court reasoned that a license is only prospective in nature because a patent license grants a licensee a future right to make or use the patented invention.

In affirming the district court’s judgment, the Seventh Circuit went beyond what was necessary to adjudicate the case. The district court merely found that the license agreement between Waterloo and Haworth expired, and as a result, neither party had any obligations to each other at the time Haworth and SoftView entered into a settlement agreement.

The Seventh Circuit agreed with the district court’s interpretation of the Haworth/Waterloo agreement, at which point the adjudication could have ended. But then the court went on to hold that a settlement agreement may not be considered a license agreement after the patent expired (even if the Haworth/Waterloo agreement was still in force at the time Haworth and SoftView executed their settlement agreement) thus still negating Waterloo’s breach of contract claims.

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141 *Waterloo II*, 467 F.3d at 644.
142 *Waterloo I*, 402 F. Supp. 2d at 953. Although the district court held that the licensing agreement terminated with the patent’s expiration, *Waterloo I*, 402 F. Supp. 2d at 953, to which the Seventh Circuit agreed, *Waterloo II*, 467 F.3d at 645-46, whether the contract’s terms were correctly interpreted by the Federal Courts is beyond the scope of this Note.
143 *Waterloo II*, 467 F.3d at 647.
144 *Id.*
146 *Waterloo II*, 467 F.3d at 645-47.
147 *Id.*
III. THE SEVENTH CIRCUIT’S MISSTEPS

The Seventh Circuit made several missteps in the *Waterloo* case. First, it made incorrect assumptions about the nature of a patent license. The Seventh Circuit incorrectly defined what constitutes a patent law license, oddly relying in part on a 1951 edition of Black’s Law Dictionary. Moreover, because the court began with the wrong definition of a patent license, the court then incorrectly deemed that licenses may only be prospective in nature. The court then bolstered these assumptions by implying that an expired patent retains no value to the patentee, and thus a patent license may only be prospective in nature. In reality, the first misstep combines a series of flawed missteps.

Second, the court arguably ignored the Supreme Court’s analysis of the legal effects of a patent license and should have been more deferential to the Federal Circuit, the court Congress especially created to determine patent issues and bring uniformity to patent laws.

Third and finally, not only did the Seventh Circuit make wrong assumptions in its reasoning, but also it ignored the actual negotiation process and result of both a licensing agreement and a settlement agreement for patent infringement. Instead, the Seventh Circuit focused on the labels given to a document ending disputes negotiated under threat of litigation or actual litigation and not its substance.

A. Incorrect Assumptions Made About the Nature of Licenses

The first misstep actually involves a series of flawed missteps. The Seventh Circuit made three incorrect primary assumptions about

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148 Id. 
149 Id. 
150 Id. at 641. 
151 See Part IIIB, infra. 
the nature of a patent license and patents in general. The court began with a wrong definition of a patent license, and then the court relied on that definition in deciding that patent licenses have only prospective qualities. Finally, the court bolstered the prospective quality of a patent license with the mistaken implication that an expired patent no longer has value. Before we detail the series of missteps and why they are flawed, however, this Note will detail the Seventh Circuit’s reasoning in *Waterloo*.

Broken down, the Seventh Circuit’s reasoning in *Waterloo* follows these steps. First, a patent license grants a licensee a permissive right to use the patented invention. Because a patent license grants the licensee a permissive, future right to use the patented invention, a patent license can only be prospective in nature. Furthermore, because a patent license is prospective in nature, a patentee may not license a patent after its expiration; indeed “there is nothing left for the patent holder to license.” Thus, a settlement entered into after a patent’s expiration is not a license.

Implicit in this reasoning is that a settlement may be both prospective and retrospective in nature, i.e. a settlement agreement may release the infringer from past tortious acts in addition to any future ones that may occur. The Seventh Circuit also reinforced its decision by implying that an expired patent no longer has value or may be sued upon.

The mistakes made in the Seventh Circuit’s reasoning flow from their beginning assumptions, namely that a license grants permissive rights and is only prospective in nature. By starting on the wrong foot, the Seventh Circuit ended up in the wrong place.

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153 *Waterloo II*, 467 F.3d at 647.
154 *Id.*
155 *Id.* at 647-48.
156 *Id.* at 647.
157 *Id.*
158 *Id.* at 647-48.
159 *Id.* at 647.
160 *Id.*
161 *Id.*
1. A patent license is in essence a promise not to sue the licensee, not a grant to the licensee of rights to use the patented invention.

The Seventh Circuit started off on the wrong foot. First, the Seventh Circuit mistakenly understood a license as a “written authority granted by the owner of a patent to another person empowering the latter to make or use the patented article for a limited period or in a limited territory.” Surprisingly, and somewhat oddly, the Seventh Circuit relied on the fourth edition of Black’s Law Dictionary, published in 1951, as its quoted authority on what a patent license constitutes.

Why seek a definition of a patent license from an out-of-date, albeit generally respected, legal dictionary instead of precedent from the Federal Circuit? Even better, why not consult Supreme Court precedent on the meaning of a license in the context of patent law? As will be shown, both types of precedential and persuasive authority were amply available for the Seventh Circuit’s choosing.

Before reviewing various Federal Circuit definitions of a patent license, a short review of the rights conferred by a patent is in order. Only after a correct understanding of the property rights a patent grants a patentee can a proper understanding of the rights a patent license grants a licensee be reached.

By statute, a patent grants the patentee “the right to exclude others from making, using, selling, or offering to sell” the patented invention within the United States. However, the exact contours of this right were not always unmistakably comprehended because of ambiguities in the statute language prior to 1952. In the 1946 Patent Act for example, Congress established that a patent granted the patentee

162 Id.
163 Id.
164 See Part IIIB, infra.
“the exclusive right to make, use, and vend the invention . . . throughout the United States.” This older version of the Patent Act may help explain the erroneous definition of a patent law license found in the 1951 fourth edition of Black’s Law Dictionary and subsequently relied upon by the Seventh Circuit. As will be discussed in greater detail below, the phrase “exclusive right to [use]” created an ambiguity in the understanding of the rights conferred by a patent.

After 1951, Congress enacted the current Patent Act in 1952, revising the statutory language describing the rights a patent confers. The current statute utilizes the same relevant language from the 1952 Patent Act with some minor additions. At present, a patent grants the patentee “the right to exclude others from making, using, offering for sale, or selling the invention.” In relevant part, Congress omitted the word “exclusive” from the 1942 Patent Act and added the words “exclude others from” in the 1952 Patent Act, clarifying the tenor of rights a patent grants a patentee to conform with existing law as interpreted by the Supreme Court.

Although the 1952 Patent Act revised the language describing the rights conferred by a patent to render the meaning clearer, the Supreme Court has concluded on numerous occasions that a patent

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170 Waterloo Furniture Components Ltd. v. Haworth, Inc. ("Waterloo II"), 467 F. 3d 641, 647 (7th Cir. 2006).
171 35 U.S.C. § 154 (1952) (“Every patent shall . . . grant to the patentee . . . the right to exclude others from making, using, or selling the invention throughout the United States”).
174 Id. Congress also added the phrase “offering for sale” sometime after the 1952 Patent Act.
175 S. REP. NO. 82-1979 (1952), as reprinted in 1952 U.S.C.C.A.N. 2394, 2417 (“The wording of the granting clause is changed to ‘the right to exclude others from making, using, or selling’, following language used by the Supreme Court, to render the meaning clearer”) (emphasis added).
confers the right to exclude others from using\textsuperscript{176} the invention.\textsuperscript{177} At other times, the Court has declared that a patent grants the patentee the right to use the invention.\textsuperscript{178} The perhaps seemingly inconsistent views of the Court are explained below.

In \textit{Continental Paper Bag Co. v. Eastern Paper Bag Co.},\textsuperscript{179} the Court extensively discussed the rights granted a patentee and the theories supporting those rights.\textsuperscript{180} The Court endorsed the view that a common law understanding of property already granted the patentee a right to use his invention,\textsuperscript{181} and that the only right Congress granted

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{176} For the reader’s sake, the terms “use” or “using,” in the context of rights granted a patentee here and throughout this Note, include the statutory rights of making, using, selling and offering to sell when not explicitly listed.
\item \textsuperscript{177} Bloomer v. McQuewan, 55 U.S. 539, 549 (1853) (“The franchise which the patent grants, consists altogether in the right to exclude every one from making, using, or vending the thing patented, without the permission of the patentee. This is all [the patentee] obtains by the patent”); United Shoe Mach. Corp. v. United States, 258 U.S. 451, 463 (1922) (citing \textit{Bloomer}, 55 U.S. 539) (“From an early day it has been held by this court that the franchise secured by a patent consists only in the right to exclude others from making, using, or vending the thing patented without the permission of the patentee”); \textit{see also} United States v. Line Material Co., 333 U.S. 287, 316 (1948) (Douglas, J. concurring) (quoting U.S. CONSTAT. art. I, § 8, Cl. 8) (“It is to be noted first that all that is secured to inventors is ‘the exclusive right’ to their inventions”); Kewanee Oil Co. v. Bicron Corp. et al., 416 U.S. 470, 480 (1974) (Patent laws promote progress of science and useful arts “by offering a right of exclusion for a limited period as an incentive to inventors”).
\item \textsuperscript{178} United States v. Univis Lens Co., 316 U.S. 241, 250 (1942) (“The full extent of the monopoly is the patentee's ‘exclusive right to make, use, and vend the invention or discovery’”).
\item \textsuperscript{179} 210 U.S. 405 (1908).
\item \textsuperscript{180} \textit{Id.} at 423-25.
\item \textsuperscript{181} \textit{Id.} at 424-25 (“[The patentee] receives nothing from the law that he did not have before”); \textit{accord} Bauer & Cie v. O’Donnell, 229 U.S. 1, 10 (1913) (“The right to make, use and sell an invented article is not derived from the patent law. This right existed before and without the passage of the law and was always the right of an inventor”); Crown Die & Tool Co. v. Nye Tool & Mach. Works, 261 U.S. 24, 34-35 (1923) (“[This] Court held that the Government did not confer on the patentee the right himself to make, use or vend his own invention, that such right was a right under the common law not arising under the federal patent laws and not within the grant of power to Congress to enact such laws”).
\end{itemize}
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by statute was the *exclusive right* to use the invention,\(^\text{182}\) which the
Court interpreted as the *right to exclude* others from using the
invention.\(^\text{183}\)

In summary, Congress never conferred by patent the statutory
right to use the invention although the language used to describe the
rights conferred by patent may have been misunderstood as conferring
a “right to use” in the 1942 Patent Act and all previous versions of the
Patent Act.\(^\text{184}\) Rather, Congress only intended the statutory language to
\(^\text{182}\) *Cont’l Paper Bag Co.*, 210 U.S. at 423-25 ("Congress has . . . guaranteed
the patentee an exclusive right to [his invention] for a limited time"); *accord Bauer*, 229 U.S. at 10 ("The [Patent Act] secured to the inventor the exclusive right
to make, use and vend the thing patented"); *see Crown Die*, 261 U.S. at 34-35.

\(^\text{183}\) *Cont’l Paper Bag Co.*, 210 U.S. at 423-25 ("[T]he only effect of the patent
is to restrain others from manufacturing and using that which he has invented"); *accord Bauer*, 229 U.S. at 10 (The Patent Act consequently, “secured to the inventor
the exclusive right . . . to prevent others from [using the patented invention] without
the consent of the patentee"); *Crown Die*, 261 U.S. at 34-35 ("[This] Court further
held that in its essence all that the Government conferred by the patent was the right
to exclude others from making, using or vending his invention").

\(^\text{184}\) The previous Patent Acts used some form of the phrase “right to use the
invention,” albeit with different wording over the years. The Supreme Court
summarized the historical changes in the language used to describe the rights
conferred by patent in the relevant statutes for the Patent Acts of 1790, 1793, 1736,
and 1870 as follows:

The protection given to inventors and authors in the United States
originated in the Constitution, § 8 of Art. I of which authorizes the
Congress “to promote the progress of science and useful arts, by
securing for limited times to authors and inventors the exclusive
right to their respective writings and discoveries.” This protection,
so far as inventors are concerned, has been conferred by an act of
Congress passed April 10, 1790, and subsequent acts and
amendments. The act of 1790, 1 Stat. 109, c. 7, granted “the sole
and exclusive right and liberty of making, constructing, using and
vending to others to be used, the said invention or discovery.” In
1793 (Feb. 21, 1793, 1 Stat. 318, c. 11) the word “full” was
substituted for the word “sole,” and in 1836 (July 4, 1836, 5 Stat.
117, § 5, c. 357) the word “constructing” was omitted. This
legislation culminated in § 4884 of the Revised Statutes, the part
with which we are dealing being practically identical with the act
of July 8, 1870, 16 Stat. 198, § 22, c. 230. It provides that every
patent shall contain “a grant to the patentee, his heirs and assigns,
grant the property right to exclude others from using the invention.\textsuperscript{185} In other words, even though the statutory language in the Patent Acts before 1952 used the phrase “exclusive right to use” in describing the rights conferred by patent, Supreme Court cases interpreted that phrase to mean that a patent only grants the patentee the right to exclude others from using the patented invention.\textsuperscript{186} To be sure, all forms of intellectual property share the essential right to exclude others from using, without permission, the copyright, patent, trademark, or trade secret.\textsuperscript{187}

Despite the statutory definition of what rights a patent grants a patentee, it is still common to perceive a patent’s grant as a de facto monopoly for the patentee to make, use, and sell the invention, and with it the ability to license those same rights to a licensee.\textsuperscript{188} Common experience with tangible personal or real property may make it difficult for many people to conceive of a right to exclude without simultaneously having the right to use tangible property.\textsuperscript{189} However, because intellectual property is intangible, the concept of having only the right to exclude and not the right to use becomes troublesome for

\textit{for the term of seventeen years, of the exclusive right to make, use, and vend the invention or discovery.}

\textit{Bauer}, 229 U.S. at 9-10.

\textsuperscript{185} \textit{See} Richardson v. Suzuki, 868 F2d. 1226, 1247 (Fed. Cir. 1989) (“The right to exclude recognized in a patent is but the essence of the concept of property”).

\textsuperscript{186} \textit{See}, e.g., Special Equip. Co. v. Coe, 324 U.S. 370, 378 (1945) (“The patent grant is not of a right to the patentee to use the invention, for that he already possesses. It is a grant of the right to exclude others from using it. As the statute, R. S. § 4884, provides, the grant is of the “exclusive right to make, use, and vend” the invention”).

\textsuperscript{187} Kenneth L. Port, Jay Dratler, Jr., Faye M. Hammersley, Terence P. McElwee, Charles R. McManis & Barbara A. Wrigley, L\textsc{i}censing \textsc{i}ntel\textsc{l}lectual \textsc{p}roperty in the Information Age 6 (2d ed. 2005) (“The direct impact of intellectual property is entirely negative: it prevents those who do not own it from doing things they otherwise might lawfully and productively do, normally without invading any one’s tangible property”).

\textsuperscript{188} \textit{See} Part IA, \textit{supra}.

\textsuperscript{189} Kenneth L. Port, Jay Dratler, Jr., Faye M. Hammersley, Terence P. McElwee, Charles R. McManis & Barbara A. Wrigley, Licensing Intellectual Property in the Information Age 5-6 (2d ed. 2005).
many. An example of why this distinction is important will help illuminate the concept, and explain how the distinction affects licensing agreements.

Suppose inventor Jon holds a patent for a widget with elements A+B+C and inventor Kate holds a patent for a widget with elements A+B. Despite Jon’s patent, Kate may still exclude Jon from making, using, or selling his widget with elements A+B+C, because it would infringe Kate’s patent for a widget with elements A+B. Kate’s patent claim would read on Jon’s widget.190 Inventor Kate owns a “dominating” patent.191

The following drawing helps to visualize this situation where Jon’s patent for a widget with elements A+B+C is the inner circle, and Kate’s patent for a widget with elements A+B is the outer circle encompassing Jon’s inner circle. The drawing represents how Kate’s “dominate” patent prevents Jon from freely using his invention; Kate has the right to exclude Jon from using any widget that includes elements A+B. Even though the law grants Jon the right to exclude others from using his invention, he himself does not have the right to use his invention without Kate’s consent.

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190 “Read on” is a term of art in patent litigation. *See* 8 Donald S. Chisum, *CHISUM ON PATENTS* Glossary (2001) (Explaining meaning of the term “reads on” as “a claim ‘reads on’ or covers products or processes that contain all of the elements and limitations of the claim”).

191 *See* BLACK’S LAW DICTIONARY 1156 (8th ed. 2004) on blocking patent, dominating patent, and fencing patent.
A similar situation, often referred to as a “blocking patent,” would arise if Jon instead held a patent for a widget with elements A+C, yet Jon makes, uses, and sells a widget with elements A+B+C. In that case, both Jon and Kate could prevent each other from making, using, or selling a widget with elements A+B+C. This is because Jon’s patent claim including elements A+B and Kate’s patent claim including elements A+C would read on the widget with elements A+B+C, each patent “blocking” the other’s use of the widget.

The following drawing helps to visualize this situation, where Jon’s patent for a widget with elements A+C is the right circle, and Kate’s patent for a widget with elements A+B is the left circle. The overlapping area of the two circles represents the overlapping patent rights that Kate and Jon share. The drawing represents how Kate and Jon’s patents “block” each other from freely using their inventions without the other’s consent.

Kate has the right to exclude Jon from using any widget that includes elements A+B and Jon has the right to exclude Kate from using any widget that includes elements A+C. Even though the law grants Jon and Kate the right to exclude others from using their respective inventions, neither Jon nor Kate has the right to use their invention without the other’s consent. Cross-licensing the patents would permit both Jon and Kate to make, use, and sell the widget A+B+C.

192 Id.
193 Id.
194 Id.
The previous hypotheticals are not mere mental gymnastics to illuminate theories of patent law, but they occur in actual court cases, and affect their outcomes. Why is the distinction between the right to use and the right to exclude important? It is important because understanding what rights a patent grants a patentee shapes what rights a licensee receives from the patentee, and thus what a patent license constitutes.

Notwithstanding the actual language of a license agreement, a patent license is not a grant of rights to the licensee to use the invention; rather, a patent license is an agreement that the licensor will not sue the licensee, so long as neither party breaches the agreement. According to the Supreme Court, a patent license “amounts to no more than ‘a mere waiver of the right to sue.’” The federal courts of appeal have also declared that a patent license is nothing more than a promise not to sue. In fact, a patentee has no other obligations to the licensee, even to the point that a patentee does not have to sue other infringers of the licensed patent. Neither

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196 U.S. Philips Corp. v. ITC, 424 F.3d 1179, 1189 (Fed. Cir. 2005).

197 Gen. Talking Pictures v. W. Elec. Co., 304 U.S. 175, 181 (1938) (quoting De Forest Radio Tel. Co. v. United States, 273 U.S. 236, 242 (1927)). It should be noted that an exclusive licensee receives more in addition to the promise not to sue, namely the ability to sue others for infringement in some circumstances. See Part IC, supra.

198 See W. Elec. Co. v. Pacent Reproducer Corp., 42 F.2d 116, 118 (2d Cir. 1930) (noting that “a license grants to the licensee merely a privilege that protects him from a claim of infringement by the owner of the patent”); Rite-Hite Corp. v. Kelley Co., 56 F.3d 1538, 1552 (Fed. Cir. 1995) (en banc) (noting that a licensee with a bare license “has received only the patentee’s promise that [the licensee] will not be sued for infringement”); U.S. Philips Corp., 424 F.3d at 1189 (noting that “a nonexclusive patent license is simply a promise not to sue for infringement”).

199 Again, this is for a “bare licensee”, which is a minimum received by all licensees, though exclusive licensees receive more rights. See Part IC, supra.

200 W. Elec. Co., 42 F.2d at 118 (noting that a patentee may freely enter licensing agreements with others or even tolerate infringers, and in neither case violate the rights of the patent licensee, though such actions may cause the licensee
does the licensee have any other obligations to the patentee outside the terms of the agreement.\textsuperscript{201}

Why have courts declared that a patent license is nothing more than a promise not to sue or a mere waiver of a right to sue? Recall that the patentee does not have the right to use the patented invention; rather the patentee has the right to \textit{exclude others} from making, using, selling, or offering to sell the invention.\textsuperscript{202} Therefore, if the patentee does not have the right to use the invention, then how can the patentee grant the licensee a right to use the invention when the patentee does not have that right themselves?

The Federal Circuit acknowledged this absurdity. Based on the exclusionary rights granted a patentee, the Federal Circuit reasoned as follows about the actual nature of a patent license:

\begin{quote}
Even if \textquote{[a patent license is]} couched in terms of \textquote{"licensee is given the right to make, use, or sell X,"} the agreement cannot convey that absolute right because not even the patentee of X is given that right. His right is merely one to exclude others from making, using or selling X, 35 U.S.C. § 154. Indeed, the patentee of X and his licensee, when making, using, or selling X, can be subject to suit under other patents.\textsuperscript{203}
\end{quote}

Because a patentee cannot grant a right to that which it does not have, the Federal Circuit held that \textquote{[a]s a threshold matter, a patent license

\textsuperscript{201} \textit{U.S. Philips Corp.}, 424 F.3d at 1189 (noting that granting a license \textquote{does not obligate the licensee to do anything; it simply provides the licensee with a guarantee that it will not be sued for engaging in conduct that would infringe the patent in question}).


\textsuperscript{203} Spindelfabrik Suessen-Schurr Stahlecker & Grill GmbH v. Schubert & Salzer Maschinenfabrik Aktiengesellschaft, 829 F.2d 1075, 1081 (Fed. Cir. 1987).
agreement is in essence nothing more than a promise by the licensor
not to sue the licensee” for patent infringement.204

With this understanding, the Federal Circuit recently declared that
a license is equivalent to a covenant not to sue.205 Even some
commentators note the implications of viewing a patent license
agreement as a covenant not to sue on other areas of the law,206 such as
the assignment of patent licenses in a bankruptcy proceeding.207

Perhaps the language of the pre-1952 statutes describing the rights
granted a patentee explains the incorrect definition of a patent license
found in the 1951 fourth edition of Black’s Law Dictionary.208 Another
potential reason for the inaccurate definition may be that Congress had
yet to centralize all appeals of patent cases into a single court, the
Court of Appeals for the Federal Circuit. Congress first created the

204 Id.; accord Rite-Hite Corp. v. Kelley Co., 56 F.3d 1538, 1552 (Fed. Cir.
1995) (“If the party has not received an [exclusive license] i.e., the right to exclude
others from making, using, or selling the patented invention, the party has a ‘bare
license,’ and has received only the patentee’s promise that that party will not be sued
for infringement”).

205 Metabolite Labs., Inc. v. Lab. Corp. of Am. Holdings, 370 F.3d 1354, 1367
(Fed. Cir. 2004) (“[A] license is, in essence, a licensor's covenant not to sue the
licensee”); see also John C. Phillips, Note, Sui Generis Intellectual Property
(“A ‘license’ in the patent law context may be defined as a covenant not to sue for
infringement in exchange for a royalty”).

206 Michelle Morgan Harner, Carl E. Black, and Eric R. Goodman, Debtors
Beware: The Expanding Universe of Non-Assumable/Non-Assignble Contracts in
are covenants not to sue-i.e., the licensor agrees not to sue the licensee for patent
infringement if the licensee uses the patented invention and performs (such as by
paying royalties) in accordance with the terms of the license agreement”).

207 Id. at 212.

208 BLACK’S LAW DICTIONARY 1068 (4th ed. 1951).
Court of Appeals for the Federal Circuit in 1982\textsuperscript{209} for the purpose of
unifying patent law\textsuperscript{210} among other things.\textsuperscript{211}

Nevertheless, none of these possible reasons for an erroneous
definition of a patent license excuses the Seventh Circuit for relying
on the 1951 definition found in Black’s Law Dictionary when the
Supreme Court and the Federal Circuit have explicated a correct
definition of a patent license.

2. A license may be retroactive.

In deciding the \textit{Waterloo} case, the Seventh Circuit also relied on
the notion that a license has only prospective qualities.\textsuperscript{212} To reinforce
that notion, the Seventh Circuit incorrectly defined a patent license as
a grant to the licensee of the right to use the patented invention, which
can only be forward looking.\textsuperscript{213} However, patent licenses may have
both prospective and retrospective qualities, in part because a patent
license is in essence a promise not to sue.\textsuperscript{214} Other types of intellectual
property also recognize retroactive licensing agreements.\textsuperscript{215}

\textsuperscript{209} The Federal Court Improvements Act of 1982 (FCIA) established the Court
of Appeals for the Federal Circuit (CAFC), Pub. L. No. 97-164, 96 Stat. 25 (relevant
\textsuperscript{210} Holmes Group, Inc. v. Vornado Air Circulation Sys., 535 U.S. 826, 838
(2002) (noting that the Federal Circuit “was created, in part, to promote uniformity
in the development [patent] law”).
\textsuperscript{211} See Rochelle Cooper Dreyfuss, \textit{The Federal Circuit: A Case Study in
Specialized Courts}, 64 N.Y.U. L. REV. 1, 2-4 (1989) (noting administrative
efficiency and reduced forum shopping as some other reasons).
\textsuperscript{212} Waterloo Furniture Components Ltd. v. Haworth, Inc., 467 F. 3d 641, 647
(7th Cir. 2006).
\textsuperscript{213} Id.
\textsuperscript{214} See Part IIIA1, supra.
\textsuperscript{215} See, e.g., Dov S. Greenbaum, Comment, \textit{The Database Debate: In
Support of an Inequitable Solution}, 13 ALB. L.J. SCI. & TECH. 431, 515 n.160
(2003) (noting that Texaco agreed to pay a seven-figure settlement and retroactive
licensing fee to the CCC for a copyright infringement claim).
The Federal Circuit has acknowledged on various occasions both implicitly and explicitly that a patent license may be retroactive. Additionally, the Sixth Circuit explicitly held that “a release [from past infringement] can, in certain circumstances, have the effect of and be construed as a license.” Various district courts have also recognized the retroactive nature of patent licenses in the form of a settlement for past infringement.

Moreover, most patent infringement cases settle with the parties entering some form of licensing agreement. Settlement in a general

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216 See Intel Corp. v. ULSI Sys. Tech., 995 F.2d 1566, 1567 (Fed. Cir. 1993) (noting that Intel and HP entered into a cross-licensing agreement granting each other “an ‘irrevocable, retroactive, nonexclusive, world-wide, royalty-free license’ under all patents and patent applications covered by the agreement”); Enzo APA & Son v. Geapag A.G., 134 F.3d 1090, 1092 (Fed. Cir. 1998) (“By its terms, the Spidem-Geapag License is retroactive, effective as of December 4, 1992, thus predating the first filed action”); Ethicon, Inc. v. United States Surgical Corp., 135 F.3d 1456, 1467 (Fed. Cir. 1998) (recognizing that a patent license may cover past infringement, although absent an agreement between co-owners, a license granted by one co-owner and not the others will only operate prospectively).

217 Studiengesellschaft Kohle, m.b.H. v. Hercules, Inc., 105 F.3d 629, 634 (Fed. Cir. 1997) (ruling that a MFL licensee was entitled to a retroactive license).


221 Id. at 275.
sense may occur before actual litigation begins or anytime thereafter. Because the parties settle usually after infringement has allegedly occurred, thus precipitating the lawsuit or the threat of litigation, licensing agreements typically have a retroactive effective date, and thus embrace both prospective and retrospective qualities.

To illustrate this point further, consider the first variation of the previous “Kate and Jon” hypothetical where Jon makes a widget having elements A+B+C, which infringes Kate’s patent for a widget having elements A+B. Kate has yet to file a lawsuit, but both agree that Jon has been infringing Kate’s patent for the past 3 years and that her patent would withstand a validity challenge. Because of the threat of litigation, Jon and Kate, enter into a licensing agreement a week before Kate’s patent expires although negotiations began just under a year ago.

Jon agrees to pay a lump-sum royalty to Kate within two months of the execution date of the agreement. The lump-sum royalty covers Jon’s past infringing acts as well as his future use of the invention for the remaining week left on the life of the patent. Although the licensing agreement contains mostly retrospective features and only marginally prospective ones, it is nevertheless a license: Kate has promised not to sue Jon for past and future infringement in exchange for a lump-sum royalty payment. Courts consider lump-sum royalties

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222 Id. at 256-57; see also Carl Shapiro, Antitrust Limits to Patent Settlements, 34 RAND J. ECON. 391, 392 (2003) (“I do not distinguish between settlements that take place after patent litigation commences and those that take place before the filing of a patent lawsuit. Both types of settlements take place in the shadow of an ultimate court ruling on patent validity and/or infringement”).

223 In fact, the licensing agreement between Haworth and Waterloo was executed in December 1992 but had an effective date of October 1, 1992. Waterloo Furniture Components v. Haworth, Inc., 402 F. Supp. 2d 950, 952 (N.D. Ill 2005). Thus, Waterloo paid Haworth a certain monetary amount to cover past infringing acts that occurred prior to the execution of the licensing agreement and any future ones up to the expiration date of the patent, a retroactive and prospective license. See, e.g., Shatterproof Glass Corp. v. Libbey-Owens-Ford Co., 482 F.2d 317, 318 n.2 (1973) (Shatterproof began negotiations in 1952, which concluded in 1955 with a license agreement having an effective date of Jan. 1, 1954); id. at 319 (In 1962, Libbey-Owens-Ford executed a license agreement with Ford having an effective date of Jan. 1, 1961).
the same as continuing royalty payments in that they fulfill the licensee’s obligation to pay the patentee for the license.\textsuperscript{224}

Consider the legal effects, if any, on the outcome when the facts of the hypothetical are altered. In this variation, the negotiation process took longer and an agreement was reached a week after the patent expired, but all the other terms were the same. Now the licensing agreement contains only retrospective features. Despite the patent’s expiration, the agreement is still a patent license: Kate has promised not to sue Jon for past infringement in exchange for a lump-sum royalty fee. A patentee’s authority to grant a retroactive patent license is what enables the settlement of a patent infringement suit and is indistinguishable from a settlement.\textsuperscript{225}

3. Expired patents retain some value to the patentee.

The Seventh Circuit also incorrectly implied that once a patent expires, the patentee can no longer enforce his patent rights based on the expired patent, bolstering its claim that a license has only prospective qualities.\textsuperscript{226} While the patentee’s power to exclude others no longer exists after a patent’s expiration,\textsuperscript{227} “a patent does have

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\item \textsuperscript{224} Hazeltine Corp. v. Zenith Radio Corp., 100 F.2d 10, 16 (7th Cir. 1938) (‘‘Royalty,’ when used in connection with a license under a patent, means the compensation paid by the licensee to the licensor for the use of the licensor’s patented invention’’); see Studiengesellschaft Kohle, m.b.H. v. Hercules, Inc., 105 F.3d 629, 633 (Fed. Cir. 1997) (‘‘The ordinary meaning of the term ‘paying licensee’ is one who gives money for a license . . . we see no distinction between one who makes an up-front, lump-sum payment and one who makes continuing royalty payments. Indeed, such a distinction would be doubly doubtful because a ‘paid-up’ license presumably includes potential future royalty payments discounted to their net present value’’).
\item \textsuperscript{225} See De Forest Radio Tel. Co. v. United States, 273 U.S. 236, 241-42, (1927) (settlement and license have the same legal effect); Shatterproof Glass Corp. v. Libbey-Owens-Ford Co., 482 F.2d 317, 320 (6th Cir. 1973) (settlement may be deemed equivalent to a retroactive license).
\item \textsuperscript{226} Waterloo Furniture Components Ltd. v. Haworth, Inc., 467 F. 3d 641, 647-48 (7th Cir. 2006).
\item \textsuperscript{227} 35 U.S.C § 154(a)(2) (2006).
\end{itemize}
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value beyond its expiration date.”228 By statute, a patentee may still sue an infringer for past infringement committed during the life of the patent.229

A patentee may still recover standard remedies when suing for past infringement of an expired patent. For example, a patentee whose right to exclude expired with the patent may yet be able to obtain post-patent-expiration injunctions.230 A patentee may want to seek an injunction after a patent has expired for two basic reasons. First, a patentee may request the injunctions to destroy infringing items made during the patent’s lifetime or “articles made from an infringing machine or process.”231 Another reason for a post-expiration injunction is to enjoin the infringer “from making the patented item for the amount of time it would take for the infringer to recreate the invention after the patent expired.”232

Injunctions are not the only remedy available to a patentee after a patent expires. A patentee may recover money damages as well.233 Although sometimes misunderstood as a statute of limitations,234 § 286 caps the amount of damages a patentee may recover from an infringer for any infringement committed more than six years prior to filing the lawsuit.235 In other words, “one starts from the filing of a [patent-infringement lawsuit] and counts backward [six years] to

228 In re Morgan, 990 F.2d 1230, 1232 (Fed. Cir. 1993).
229 35 U.S.C. § 286 (2000); accord In re Morgan, 990 F.2d at 1232. (tersely noting that “a patent may be sued on after it expires”).
231 Id. at 106-07.
232 Id. (This is because if the infringer had respected the patentee’s rights, they would not be able to recreate the invention until after the patent expires. In other words, by infringing the patent, the infringer received an unlawful head start on recreating the invention for lawful use after patent expiration. A post-expiration injunction would deprive the infringer of that head start).
235 35 U.S.C. § 286 (2000) (“Except as otherwise provided by law, no recovery shall be had for any infringement committed more than six years prior to the filing of the complaint or counterclaim for infringement in the action”).
A patentee may therefore still derive value from an expired patent either by commencing a lawsuit or seeking a licensing agreement with the alleged infringer up to six years after the patent expired. Remember, this is not an unlawful extension of the patent term because the patentee may not recover damages for use of the patented invention after the patent expires. Rather, if a patentee first discovers after the patent expired that an infringer committed infringing acts before the patent’s expiration, the patentee may recover those damages.

Logically then, a patentee can resolve any patent dispute with an infringer after the patent has expired by either entering a licensing or settlement agreement covering the past infringing acts. The infringer’s ability to enter into retroactive agreements confirms the notion that settlement agreements may be considered a licensing agreement, even if the patent has expired, and especially if a MFL clause is implicated. Thus, the Seventh Circuit erroneously concluded that a patent license has only prospective qualities. In reality, the legal effect of a license, a promise not to sue, may cover both past and future infringing acts in exchange for an agreed upon consideration.

B. Ignoring De Forest for the Trees and Disregarding the Federal Circuit

In the second misstep, the court arguably ignored the Supreme Court’s analysis of the legal effects of a patent license and should have been more deferential to the Federal Circuit, the court Congress especially created to determine patent issues and bring uniformity to patent laws.

236 Standard Oil Co., 754 F.2d at 348.
237 See, e.g., In re Morgan, 990 F.2d 1230, 1232 (Fed. Cir. 1993).

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The Seventh Circuit should have looked to the Supreme Court and the Federal Circuit for the correct definition of a patent license. The Supreme Court has held on multiple occasions that a license in the context of patent law “amounts to no more than ‘a mere waiver of the right to sue.’”\(^{240}\) In *De Forest Radio Telephone Co. v United States*,\(^{241}\) the pre-eminent Supreme Court case explaining the meaning of a patent license, the American Telephone Company released the United States and “all manufactures acting under its orders” from any infringement claims stemming from the United States’ use and manufacture of a patented invention for use in World War I.\(^{242}\)

The De Forest Radio Telephone Company, the holder of patents for the invention, later sued the United States for infringement.\(^{243}\) However, De Forest granted certain rights in the patent to Western Electric Company, who subsequently conveyed the rights to the American Telephone Company.\(^{244}\) The agreement included the right of De Forest and Western Electric to sue others for any of the patents “within the fields in which each respectively possessed rights,”\(^{245}\) and to license to the United States use of the patented technology.\(^{246}\) A license would serve as a complete defense to claims of patent infringement by either company.\(^{247}\)

In holding that American Telephone Company’s actions created an implied license with the United States Government,\(^{248}\) the Court also explicated the nature of a patent license. The Court noted, “No formal granting of a license is necessary in order to give it effect.”\(^{249}\)

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\(^{241}\) *De Forest Radio Telephone Co. v United States*, 273 U.S. 236 (1927).

\(^{242}\) *Id. at 239-40.*

\(^{243}\) *Id. at 237.*

\(^{244}\) *Id. at 238.*

\(^{245}\) *Id.*

\(^{246}\) *Id. at 240.*

\(^{247}\) *Id.*

\(^{248}\) *Id. at 242.*

\(^{249}\) *Id. at 241.*
Moreover, the court approvingly quoted an earlier Supreme Court case that declared a license is “a mere waiver of the right to sue.”250

The Federal Circuit stands with the Supreme Court in its case law, when explicating the nature of a patent license.251 Although Federal Circuit decisions do not bind the Seventh Circuit,252 even in matters of patent law,253 the Seventh Circuit should give deference to the Federal Circuit in matters implicating patent law,254 similar to the manner in which the Federal Circuit defers to its sister appellate courts when deciding matters not implicating patent law, such as procedural issues and substantive issues not involving patent law.255

One commentator argued for deference to the Federal Circuit while recognizing that the Federal Circuit’s decisions do not bind regional appellate and state courts, in this manner:

The most obvious law for the regional appellate courts and state courts to apply to patent issues is that of the Federal Circuit. However, federal appellate courts are

250 Id. at 242 (quoting Henry v. Dick Co. 224 U.S. 1, 24 (1912)).
251 See generally Part IIIA1, supra.
252 Kohler Co. v. Moen Inc., 12 F.3d 632, 644 (7th Cir. 1993) (Cudahy, J. dissenting).
254 But see Larry D. Thompson, Jr., Adrift on a Sea of Uncertainty: Preserving Uniformity in Patent Law Post-Vornado Through Deference to the Federal Circuit, 92 GEO. L.J. 523, 526 (“Generally, however, federal courts of appeals follow what can be called the ‘rule of no deference,’ which allows courts to treat the decisions of coordinate federal courts as persuasive, but prohibits deference to them”).
255 One commentator summarized the Federal Circuit’s deference as follows: [The Federal Circuit] applies regional circuit law to procedural issues that are not themselves substantive patent law issues so long as they do not (1) pertain to patent law, (2) bear an essential relationship to matters committed to [the court’s] exclusive control by statute, or (3) clearly implicate the jurisprudential responsibilities of [the court] in a field within its exclusive jurisdiction.

not bound by Federal Circuit law and do not have sovereignty-based reasons for following it, as they do with state law. Therefore, the basis for their deference to Federal Circuit law should come from three places. First, it generally is more efficient for regional circuits to follow the Federal Circuit so the appellate courts do not need to develop new law. Second, the courts should respect the congressional purpose of creating a uniform body of patent law. Finally and most tenuously, the regional circuits should honor Federal Circuit law to promote comity among the circuit courts, which the Federal Circuit has, at least in principle, supported. Perhaps such respect for the Federal Circuit law will generate a reciprocal respect in the Federal Circuit for regional circuit law, transforming its purported adherence to regional circuit law on nonpatent issues into actual adherence.256

However, what about issues before the courts that involve matters of both patent law and other areas of law, or issues that merely implicate patent law? For instance, some decisions that may have a “substantial effect on patent law” involve antitrust, contracts, copyrights, federal business law tort claims such as trade dress infringement, patent licensing disputes, and state law business disparagement claims.257 In those cases that implicate patent law or involve matters of patent law, other regional appellate and state courts should defer to the Federal Circuit in order to promote the congressional intent of a uniform body of patent law.258

Other regional appellate courts have understood the need for a uniform body of patent law, and have deferred to the Federal Circuit precedent when deciding issues implicating patent law. For example, the Ninth Circuit, in a bankruptcy proceeding, upheld the district court’s decision, preventing the assignability of a patent license by the debtor.\textsuperscript{259} In so doing, the Ninth Circuit looked to federal patent law, as promulgated by the Federal Circuit court, to govern its decision, even though federal patent law may have conflicted with California state law.\textsuperscript{260}

The court justified their conclusion by emphasizing the importance of federal patent policy and a uniform rule of “modern federal decision” regarding the non-assignability of nonexclusive patent licenses.\textsuperscript{261} Additionally, the Ninth Circuit cited Seventh Circuit precedent that also held that federal patent law governed the assignability of a patent license,\textsuperscript{262} which means the Seventh Circuit not only understands this principle but even applied it and incorporated it into its own case law. Notably, the Ninth Circuit also looked to the Supreme Court’s \textit{De Forest} decision for a definition of a patent license,\textsuperscript{263} which definition the Federal Circuit case law supports.\textsuperscript{264}

In order to follow the Congressional directive for a uniform body of patent law, the Seventh Circuit should have followed the Ninth Circuit’s example and looked to the Supreme Court and the Federal Circuit to inform its definition of a patent license, a key part of their construction of patent law is undoubtedly important’”); Cole, \textit{supra} note 257, at 725-26.

\textsuperscript{259} In re CFLC, Inc., 89 F.3d 673, 680 (9th Cir. 1996)

\textsuperscript{260} \textit{Id.} at 677-79.

\textsuperscript{261} \textit{Id.} at 679-80.

\textsuperscript{262} \textit{Id.} at 677-78 (citing Inc. v. Kelley Co., 465 F.2d 1303, 1306 (7th Cir. 1972) (“The question of assignability of a patent license is a specific policy of federal patent law dealing with federal patent law. Therefore, we hold federal law applies to the question of the assignability of the patent license in question’’)).

\textsuperscript{263} \textit{Id.} at 677 (noting that a patent license is a “‘mere waiver of the right to sue’ the licensee for infringement’”) (quoting \textit{De Forest Radio Tel. Co. v. United States}, 273 U.S. 236, 242 (1927)).

\textsuperscript{264} See Part IIIA1, \textit{supra}.
reasoning to hold that a settlement agreement may never be a patent license.265

C. The calculations for a payment of royalties in a license agreement and a settlement agreement are substantially the same.

Third and finally, the Seventh Circuit ignored the actual negotiation process and legal effects of both a licensing agreement and a settlement agreement for patent infringement. Instead, the Seventh Circuit focused on the label of an agreement ending disputes negotiated under threat of litigation or actual litigation and not its substance.266

The Seventh Circuit overlooked the fact that a calculation of royalty rates267 for a licensing agreement and a settlement agreement mimic each other, thus bolstering the notion that settlement agreements perform substantially the same function as licensing agreements—in other words, a means for the parties to enter some form of a covenant not to sue in exchange for an agreed upon consideration.268

265 Waterloo Furniture Components Ltd. v. Haworth, Inc., 467 F. 3d 641, 647 (7th Cir. 2006).
266 Id. at 647-48.
267 Royalty as used here means any compensation paid to the licensor for a license, See Hazeltine Corp. v. Zenith Radio Corp., 100 F.2d 10, 16.(7th Cir. 1938) (“‘Royalty’ when used in connection with a license under a patent, means the compensation paid by the licensee to the licensor for the use of the licensor’s patented invention”).
268 See, e.g., Metabolite Labs., Inc. v. Lab. Corp. of Am. Holdings, 370 F.3d 1354, 1367 (Fed. Cir. 2004) (“[A] license is, in essence, a licensor's covenant not to sue the licensee”); see also John C. Phillips, Note, Sui Generis Intellectual Property Protection for Computer Software, 60 GEO. WASH. L. REV. 997, 1041 n.212 (1992) (“A ‘license’ in the patent law context may be defined as a covenant not to sue for infringement in exchange for a royalty”). For a settlement as a covenant not to sue, see, e.g., Microchip Tech. Inc. v. Chamberlain Group, 441 F.3d 936, 942 (Fed. Cir. 2006) (noting that the parties’ settlement agreement was a covenant not to sue).
Because damages for patent infringement are calculated using lost profits or a reasonable royalty rate, and sometimes both, settlement amounts will, in large part, be based on either lost profits or a reasonable royalty rate. Thus, a settlement based on the reasonable royalty rate mimics the negotiation process the parties would have had if they instead entered into a licensing agreement.

When a court determines damages for past patent infringement employing a reasonable royalty calculation, it conjures up what royalty rate the parties hypothetically would have agreed to if they sat across the bargaining table on the day infringement began and had instead entered into a license agreement. In other words, if the parties had negotiated a license agreement on the day infringement began, the royalty rate the patentee would have charged the infringer for use of the invention is the same rate calculation that the court would use to assess the amount of damages the infringer owes the patentee.

The actions of the parties in negotiating a royalty rate for a license or a settlement agreement has the same legal effect, as the Supreme

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269 35 U.S.C. § 286 (2000); State Indus., Inc. v. Mor-Flo Indus., Inc., 883 F.2d 1573, 1577 (Fed. Cir. 1989) (“The [damages] award may be split between lost profits as actual damages to the extent they are proven and a reasonable royalty for the remainder”).

270 See, e.g., Shapiro, supra note 222, at 392 (“Virtually every patent license can be viewed as a settlement of a patent dispute: the royalty rate presumably reflects the two parties’ strengths or weaknesses in patent litigation in conjunction with the licensee’s ability to invent around the patent”).

271 Kesan & Ball, supra note 220, at 254 (“Obviously, an out-of-court negotiation of a licensing agreement is similar to a negotiation of a settlement agreement once the case has been filed”); see also Shapiro, supra note 222, at 392 (“I do not distinguish between settlements that take place after patent litigation commences and those that take place before the filing of a patent lawsuit. Both types of settlements take place in the shadow of an ultimate court ruling on patent validity and/or infringement”).

272 Hanson v. Alpine Valley Ski Area, 718 F.2d 1075, 1078 (Fed. Cir. 1983) (“Hypothetical negotiations should be the result of supposed meeting between the patentee and the infringer at the time infringement began”); accord Unisplay S.a. v. Am. Elec. Sign Co., Inc., 69 F.3d 512, 518 (Fed. Cir. 1995) (“The key element in setting a reasonably royalty is the need to return to the date when the infringement began”).
Court’s De Forest case supports.273 As a commentator put it, “royalties simply force the patentee to issue a retroactive license.”274 Recognizing that similar tactics, processes, and legal outcomes accompany license agreement and settlement agreement negotiations led one firm to advertise their skills in “Adversarial Patent Licensing Negotiations,” concluding that “adversarial patent licensing negotiations had many of the same qualities as settlement of pending litigation.”275

Because a settlement agreement and a license agreement are largely based on the same royalty rate calculations and result in the same legal effect, a settlement agreement should be considered a license.

IV. EFFECTS OF THE SEVENTH CIRCUIT’S RULING

Legal issues surrounding intellectual property continue to increase in importance and national attention,276 especially as intellectual property becomes an increasingly larger portion of a company’s assets, and by extension a nation’s economy.277 For example, some commentators note patent law’s newfound stature, due to the Supreme Court’s recent zeal to grant writs of certiorari in patent cases decided at the Court of Appeals for the Federal Circuit.278 In 2006 alone, the

273 See, e.g., De Forest Radio Tel. Co. v. United States, 273 U.S. 236, 241-42 (1927) (release and license have the same legal effect).
277 A. Tracy Gomes and Thomas George, Patent Value Continues to Soar in 2005, INTELLECTUAL ASSET MANAGEMENT, February/March 2006, at 34.
high court has granted certiorari in six patent cases, “more cases in a single year than any [year] since the 1960s.”

Compare that number to the period just after the mid twentieth century: “[D]uring the next three decades, the Court averaged barely one patent decision per year, or less than one-third its average from the first half of the [twentieth] century.” Consider the high court’s patent caseload even more recently. Since the 1982 inception of the Court of Appeals for the Federal Circuit, during “the twelve terms between 1983 and 1994 (inclusive), the Court heard five patent cases.”

No wonder a commentator declared in 2001 “[t]he Supreme Court has rendered itself well nigh invisible in modern substantive patent law.” The Supreme Court has reasserted its influence in patent law, given the recent uptick in patent cases heard by the Court, as evidenced in the previous five terms and the current term.


280 John R. Duffy, The Festo Decision and the Return of the Supreme Court to the Bar of Patents, 2002 SUP. CT. REV. 273, 275. For a more detailed discussion of the frequency with which the Supreme Court heard patent cases over the past two centuries, see id. at 285-301.

281 Id. at 297.


Given this backdrop, licensing of patented technology will likewise increase in importance, especially because of the Court’s recent decision in *eBay v. MercExchange*, where the Court eliminated the usual rule that a finding of patent infringement entitles the patentee to a permanent injunction. Because a court will no longer grant a permanent injunction to a patentee as a matter of course after proving infringement, the parties may be more inclined to enter licensing agreements for the technology covered by the disputed patents. Or, perhaps more worrisome to unwilling patent holders, the parties could even be forced to enter a license agreement as part of a court’s judgment.

Given the likelihood of increased emphasis placed on patent license agreements, the Seventh Circuit created a general rule that was not really well thought out. For example, under the new rule, a patentee could undermine the purpose of a MFL clause by entering a

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285 A. Tracy Gomes and Thomas George, *Patent Value Continues to Soar in 2005*, INTELLECTUAL ASSET MANAGEMENT, February/March 2006, at 34-35 (noting in 2005 $300-$500 million in patent litigation settlements, a $1.35 billion verdict, and a $525 future royalty payment buyout: “With patent applications up, patent awards/settlements up and more individuals, assertion companies and corporations asserting their IP rights, it is hard to imagine the future being anything other than more of the same). Compare those amounts with the recent record setting $1.52 billion verdict in the Lucent v. Microsoft cases discussed in Saul Hansell, *MP3 Patents in Upheaval After Verdict*, N.Y. TIMES, Feb. 23, 2007, at C1.


287 *Id.* at 1841.


289 This is commonly termed a compulsory license. In the post-eBay world where permanent injunctions are no longer a matter of course after a finding of patent infringement, a district court has already granted a compulsory license: Finisar Corp. v. DIRECTV Group, Inc., No. 1:05-CV-264, 2006 U.S. Dist. LEXIS 76380, at *4 (E.D. Tex. July 7, 2006).
settlement agreement at a lower royalty rate with the MFL licensee’s competitor during the course of a patent infringement suit. The patentee may worry that its patent will be found invalid if litigation continues, and therefore seek to avoid this outcome by inducing the MFL licensee’s competitor to accept a settlement at a lower royalty rate than the rate offered the MFL licensee. Under the Seventh Circuit’s new holding, the MFL licensee has no recourse to prevent this outcome.

At a minimum, a settlement agreement should be considered a license agreement for cases implicating a “most favored licensee” status. An exception to the Seventh Circuit’s general rule, at least in the case of MFL licensees, would prevent collusion between the patentee and the MFL licensee’s competitor from undermining the MFL clause. The outcome of the Waterloo case may have been correct assuming the court correctly interpreted the terms of the contract but the court should not have created a rubric that will govern other dissimilar circumstances.

What can patent practitioners do to take into account the effects of the Seventh Circuit’s Waterloo ruling when drafting license agreements in the future? Practitioners may want to explicitly contain language in a MFL clause to not only include that a MFL licensee is entitled to a more favorably rate granted in a future license agreement, but also more favorable rates agreed to during any settlement of patent infringement disputes covering the same technology outlined in the MFL license agreement. Alternatively, practitioners may not want to

290 See Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corp., 925 F. Supp. 193, 196 (S.D.N.Y. 1996) (“To conclude [that a settlement for prior patent infringement is not a license] would allow Willemijn to eviscerate the effect of SMC’s most-favored-licensee clause by, for example, ‘requiring’ a subsequent licensee to pay a higher royalty rate and then waiving the right to sue for all or part of that rate), vacated, Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corp., 103 F.3d 9 (2d Cir. 1997).

291 Waterloo Furniture Components Ltd. v. Haworth, Inc., 467 F. 3d 641, 645-46 (7th Cir. 2006) (The court held that the license agreement expired based on the contract’s terms, meaning Haworth had no more obligations to Waterloo at the time Haworth and SoftView entered the agreement).
label the agreement a license at all, but instead a “covenant not to sue.”

CONCLUSION

The Seventh Circuit put a “most favored licensee” at a competitive disadvantage with other potential licensees. The court created a general rule that settlement agreements are not patent licenses when the patent has expired. To support the new ruling, the court reasoned from an incorrect understanding of what constitutes a patent license and its associated prospective and retrospective qualities. The Seventh Circuit should have given more deference to the Federal Circuit in patent law issues and those cases that implicate substantive patent law. The court focused instead on the label attached to an agreement and not the processes by which the agreement is reached nor its legal effects.