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Limiting Downstream Effects of Patent Licensing Activity in Software and Electronics: An Argument for Alienability of Patent Licenses to Licensees' Business Successors

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LIMITING DOWNSTREAM EFFECTS OF PATENT LICENSING ACTIVITY IN SOFTWARE AND ELECTRONICS: AN ARGUMENT FOR ALIENABILITY OF PATENT LICENSES TO LICENSEES' BUSINESS SUCCESSORS

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INTRODUCTION

A. The Problem

Consider a hypothetical scenario in which Small Inventor, Inc., located in Colorado, works long hours to perfect a wristwatch-like pedometer capable of wirelessly receiving calibration data from a remote computer and comprising a sophisticated motion-control mechanism, which makes the device particularly accurate. Small Inventor, Inc. attends a trade show, where she is unpleasantly surprised to see that the market of personal fitness trackers is already saturated with sophisticated products from FitBit™, Jawbone™, and similar manufacturers. The small inventor has no chance of competing because, as it turns out, current end users are more concerned with multi-functionality of wearable fitness devices than precision. Discouraged, the small inventor returns home, scales down production of motion-sensitive pedometers, and sells them to a limited number of local stores.

To further exacerbate the small inventor's frustration, two weeks later she receives a demand letter from a "patent troll", alleging that the remote calibration component of her pedometer product infringes a client/server database patent and demanding that she take a license. Small Inventor, Inc. begrudgingly agrees to do so, even though she disagrees that wirelessly receiving instructions for calibrating a pedometer is anything like sending data to a server for storage in a database.

The small inventor realizes that the "patent troll" sent a bulk mailing to many tradeshow participants but larger companies simply ignored the letter. Many of these companies are already members of defensive licensing programs that mitigate the risk of being sued for infringement. The annual cost of participating can be as high as $20,000,[1] which is prohibitive for Small Inventor, Inc. Furthermore, the small inventor, unlike large companies, would be unable to afford defending an infringement action in court, so she chooses to take a license and agrees to pay an 11% royalty[2] on her profits.

In the meantime, six thousand miles away in Israel, a medical device company, Medical Devices, Inc., makes a scientific breakthrough and invents a touchless blood glucose monitor, which measures a diabetic patient's blood sugar level without drawing blood.[3] The wristwatch-like monitor consists of an optical glucose sensor and a camera. The monitor is the first of its kind, and the $8 billion-

1. *LOT User Fee Schedule*, LOTNET, http://www.lotnet.com/how-to-join-lot-net/LOT_User_Fees.cfm (last visited Aug. 29, 2015).

2. *See* Jonathan E. Kemmerer & Jiaqing Lu, *Profitability and Royalty Rates Across Industries: Some Preliminary Evidence*, KPMG GLOBAL VALUATION INST. (Nov. 2012), http://law.unh.edu/assets/images/uploads/pages/ipmanagement-royalty-rates.pdf (the average 2007 royalty rate in the software industry was approximately 11%).

3. Medical Devices, Inc. is a fictional company created for the purposes of this hypothetical. The hypothetical scenario was informed by a 2014 publication in Biomedical Optics Express, in which a team of researchers described an experimental, wristwatch-like, touchless glucose monitor. *See* Nisan Ozana et al., *Improved Noncontact Optical Sensor for Detection of Glucose Concentration and Indication of Dehydration Level*, 5 BIOMEDICAL OPTICS EXPRESS 1926 (2014), http://www.opticsinfobase.org/boe/fulltext.cfm?uri=boe-5-6-1926&id=286417 [hereinafter Ozana] (the monitor includes a bracelet with a built-in camera and is "based on

a-year market in diabetes management devices[4] is optimistic about the invention. There is, however, a problem: there is not a suitable motion cancellation mechanism that would make the device's readings sufficiently precise.[5]

Medical Devices, Inc. finds out about Small Inventor, Inc., whose motion cancellation technology is the missing piece to the puzzle. Medical Devices, Inc. is enthusiastic about acquiring the small inventor's company and its technology for use in touchless glucose monitors.

Medical Devices, Inc. is unhappy when it learns of a cloud on Small Inventor, Inc.'s license to its intellectual property (IP) assets. When the inventor signed the licensing agreement, she agreed to a standard clause[6] stating that she could not assign the right to practice the "troll's" invention to anyone else. The "troll", seeking to capitalize on the profit potential of glucose monitors, wants to increase the royalties to 25% or, in the alternative, sue Medical Devices for patent infringement if it proceeds with buying Small Inventor, Inc. The medical device company's attorneys determined that, although the Court of Appeals for the Federal Circuit (CAFC) recently criticized the 25% rule of thumb for setting royalties as improper,[7] the holding did not extend to private contracts. Furthermore, the attorneys find out that the "troll" obtained a declaratory judgment[8] stating that its client/server patent was not invalid. Since invalidity is the main defense to claims

tracking of temporal changes of reflected secondary speckles produced in the wrist when being illuminated by a laser beam.").

4. Mark D. Hughes, *The Business of Self-Monitoring of Blood Glucose: A Market Profile*, 3 J. DIABETES SCI. & TECH. 1219 (2009), http://www.ncbi.nlm.nih.gov/pmc/articles/PMC2769893/.

5. *See* Ozana, *supra* note 3, at 1926 ("Further development is needed such as motion cancellation mechanism in order to [make the contactless glucose monitor] more robust.").

6. Elaine D. Ziff & John G. Deming, *IP Licenses: Restrictions on Assignment and Change of Control*, PRACTICAL L. PUBLICATION 1, 14 (2012) (licensor and licensee perspectives on assignability).

7. Uniloc USA, Inc. v. Microsoft Corp., 632 F.3d 1292, 1315 (Fed. Cir. 2011) ("This court now holds as a matter of Federal Circuit law that the 25 percent rule of thumb is a fundamentally flawed tool for determining a baseline royalty rate in a hypothetical negotiation.").

8. 28 U.S.C.A. § 2201(a) (West 2010) ("In a case of actual controversy within its jurisdiction . . . any court of the United States, upon the filing of an appropriate pleading, may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought. Any such declaration shall have the force and effect of a final judgment or decree and shall be reviewable as such."); *see, e.g.*, Windmoller v. Laguerre, 284 F. Supp. 563, 566 (D.D.C. 1968) (in a declaratory judgment action to determine validity of patents, denying a motion to dismiss and noting that the action was consistent with the policy underlying the Declaratory Judgment Act).

of patent infringement,[9] Medical Devices, Inc. is concerned that its defense would not stand.

Medical Devices, Inc. anticipates to make a 20% profit margin[10] and secure a 10% market share, which would make its annual profits from the sale of touchless glucose monitoring devices $160 million per year and would mean that the "troll" would receive $40 million, or 25% in royalties on profits. The "troll" is not willing to reassign the license on the original terms, which include 11% royalties, because it knows that it is likely to prevail at trial. Medical Devices, Inc. decides that it would be significantly cheaper to develop the motion-control technology in-house.

The corporate acquisition transaction does not go through. Small Inventor, Inc. eventually goes out of business because people become less and less interested in pedometers, albeit exceptionally accurate ones. "Patent troll" makes nothing and does not get to sue Medical Devices, Inc. for patent infringement because Medical Devices, Inc. does not acquire Small Inventor, Inc. or its technology and, further, develops a design-around. Diabetic patients continue to draw blood daily while Medical Devices, Inc. takes an additional three years to develop and test a motion control technology for its contactless devices to get around a monopoly created by the "troll's" patent.

The reason for this seemingly suboptimal outcome is the unassignability clause in the "troll's" license to Small Inventor, Inc. This Note presents an argument for relaxing these restraints on alienability of patent licenses by invalidating such clauses when a patent is licensed from a non-creative entity (NCE or "patent troll").

B. Legal Question

The legal question addressed in the hypothetical *supra* is whether corporate change-of-control transactions should limit the surviving entities' ability to use newly acquired intellectual property, if said property was previously licensed by the acquired business entity from a third party that itself does not practice the licensed invention (an NCE).

The answer to this question must be consistent with both contract law and patent law. On one hand, contracts have been traditionally presumed to be fully transferable, absent express provisions to the

9. 35 U.S.C.A. § 282(b)(2) (West 2012).
10. *See* Kemmerer, *supra* note 2, at 7 (the average EBITDA profit margin is 18.6%).

contrary.[11] On the other hand, courts have been reluctant to uphold the assignability of intellectual property licenses to third parties because of a strong policy interest in encouraging patentees to retain control of their inventions.[12] However, the United States Supreme Court (hereinafter, "SCOTUS") has acknowledged that sometimes the patent rights protection doctrine goes too far.[13]

This Note presents a synthesis of the principles of contract law, intellectual property law, and antitrust policy in order to find a middle-ground approach. The proposal includes filling in the gaps in the body of defenses to claims of patent infringement by supplementing the doctrine of patent misuse, one such defense, to invalidate patent anti-assignment clauses.

C. Roadmap to a Solution

Anti-assignability clauses in patent licenses, as restrictions on alienability, could lead to anti-competitive practices and are therefore similar to practices prohibited by antitrust law. Problematically, however, there is no room in the traditional body of defenses to patent infringement claims or, more generally, in patent law, to provide a mechanism for evaluating and relaxing these restrictions even in the face of suboptimal economic results. This Note proposes that this gap in law can be resolved by grounding the argument for alienability of patent licenses in the doctrine of patent misuse.

Part I discusses the economics of the issue, including the impact of NCE activity on operating companies. Part I also presents an economics-based argument for judicially limiting downstream effects of NCE licensing activity.

Part II introduces the legal background. Part II discusses the courts' efforts to curb NCE activities, which are demonstrative of the courts' readiness to consider alienability of licenses issued by NCEs.

11. Cincom Sys., Inc. v. Novelis Corp., 581 F.3d 431, 437 (6th Cir. 2009) ("State contract law will govern the interpretation of [an intellectual property] license because a license is merely a type of contract.").

12. *Id.*; *see also* In re CFLC, Inc., 89 F.3d 673, 679 (9th Cir. 1996) (federal law must govern to prevent free assignability and to promote creativity); In re Alltech Plastics, Inc., 71 B.R. 686, 689 (Bankr. W.D. Tenn. 1987) ("[Because the rights] of the patent owner to license the use of his invention is [sic] a creature of federal common law . . . [i]t follows that questions regarding the assignability of patent licenses are controlled by federal law.") (internal citations omitted).

13. Lab. Corp. of Am. Holdings v. Metabolite Labs., Inc., 548 U.S. 124, 126–27 (2006) (citing U.S. CONST. art. I, § 8, cl. 8) ("[T]oo much patent protection can impede rather than 'promote the Progress of Science and useful Arts,' the constitutional objective of patent and copyright protection.").

SCOTUS has recently taken steps to protect the industry from weak patents asserted by NCEs by clarifying, for example, the requirements for patentable subject matter,[14] indefiniteness,[15] and claims of induced infringement.[16] A discussion and analysis, in Part II, of the recent developments in the case law of patent litigation procedure shows that the proposal presented here is consistent with these developments. SCOTUS efforts, however, have not addressed the problems faced by companies that choose to license patents from NCEs rather than litigate against them. The recent changes in law also wreaked havoc on the computer engineering patent field because the patents invalidated by SCOTUS to curb NCE activity pertained mostly to computer technologies.[17]

Part III presents an argument, rooted in antitrust and patent policy, that anti-assignment clauses in patent licenses from NCEs constitute patent misuse. The doctrine of patent misuse is reflected in the *Princo* rule: to be considered misuse, a practice first must attempt to unduly broaden the scope of a patent right, and second, it must be linked to patents in suit.[18]

Part IV provides a roadmap for arguing alienability of patent licenses to business successors. First, Part IV reconciles the proposed rule with case law. Second, Part IV addresses procedural aspects of arguing license assignability, including timing, standing, and jurisdictional law.

Part V addresses counterarguments.

D. Intended Audience

The topic explored in this Note is of interest to legal and economics scholars, legal practitioners in contract and patent law, and the courts for several important reasons.

First, it is widely recognized that, in technology-intensive industries, intellectual property assets comprise a significant portion of a company's value. For instance, while in 1929 only a third of a typical

14. Alice Corp. Pty. Ltd. v. CLS Bank Int'l, 134 S. Ct. 2347 (2014).

15. Nautilus, Inc. v. Biosig Instruments, Inc., 134 S. Ct. 2120 (2014).

16. Limelight Networks, Inc. v. Akamai Techs., Inc., 134 S. Ct. 2111, 2118–19 (2014).

17. *See* Tristan Gray-Le Coz & Charles Duan, *Apply it to the USPTO: Review of the Implementation of Alice v. CLS Bank in Patent Examination,* 2014 PATENTLY-O PATENT L. J. 1, http://patentlyo.com/media/2014/11/GrayLeCozDuan.pdf (USPTO withdrew over 800 applications from allowance following the *Alice* decision).

18. Princo Corp. v. Int'l Trade Comm'n, 616 F.3d 1318, 1318–30 (Fed. Cir. 2010).

U.S. company's assets were intangible assets, by 1990, the ratio of intangible to tangible assets skyrocketed to approximately 63%, and today more than 70% of U.S. growth comes from exploitation of intangible assets.[19] It is therefore not surprising that there is currently a significant interest in the practitioner community in developing best practices for due diligence in corporate change-of-control transactions with respect to intellectual property licenses—after all, the target's existing license agreements encumber the target's use of the subject intellectual property and could give rise to expenses in the form of royalties[20] and, at the extreme, to infringement lawsuits.[21]

Second, the bargaining power of licensors is often disproportionately high—in change-of-control transactions, licensors impose exorbitant fees of up to 100% of the original license fee if the intellectual property at issue is valuable to the purchaser.[22] This state of affairs is particularly troublesome when the licensor accumulates patents largely for monetary gain, which many argue is the case with non-creative entities.[23]

Third, there is a question of balancing existing law with policy considerations while optimizing legal rules to help high technology markets function efficiently. Although, as a society, we are prepared to sustain certain transaction costs involved in procuring, licensing and litigating patent rights if the end result is innovation that benefits the public at large, such transaction costs become a threat to innovation when inefficiencies are exploited solely for the benefit of non-producers.[24] Such exploitations result in uncertainty in IP portfolio valuation, inhibit the operating capacity of inventors, and may leave them in the dark as to the identity of their competitors.[25] For example, one court said, citing an accused infringer (in this case, Capital One Financial Corporation) in a suit brought by an NCE:

19. INTELLECTUAL PROPERTY ASSETS IN MERGERS AND ACQUISITIONS xxvii (Lanning Bryer & Melvin Simensky eds,, 2002) [hereinafter INTELLECTUAL PROPERTY ASSETS].

20. *Id.* at 12.15.

21. *See, e.g.*, Elaine D. Ziff & Grace Del Val, *IP Due Diligence Issues in M&A Transactions Checklist*, Practical Law Checklist 3-501-1681.

22. INTELLECTUAL PROPERTY ASSETS, *supra* note 19, at 12.15.

23. RICHARD A. POSNER, REFLECTIONS ON JUDGING 79 (2013) (Judge Posner explains that many large IT companies spend a significant amount on simply maintaining large patent portfolios for purely defensive purposes).

24. *Id.* at 76 (noting that the current patent system provides a disproportionate reward to first-time inventors and through unnecessary complexity, expensive litigation and complex patent procurement rules discourages improvers from receiving protection for their inventions).

25. Intell. Ventures I LLC v. Capital One Fin. Corp., No. 1:13-CV-00740 AJT, 2013 WL 6682981, at *1 (E.D. Va. Dec. 18, 2013).

> [S]hell companies conceal [the NCE's] patents so that targets have no idea that it is building walls of patents around their businesses' and then when [the NCE] does launch its attack, its targets cannot assess or value its portfolio and thus among other things cannot determine whether they could avoid [the NCE's] infringement claims by redesigning their accused products or processes.[26] (internal citations omitted)

This Note presents a comprehensive yet narrowly tailored rule to address the problems outlined above.[27]

I. ECONOMIC BACKGROUND

A. Non-Creative Entities and the Software and Electronics Industry

The proliferation of non-creative entities (NCEs) is considered by some scholars and academics the most significant problem in the current U.S. patent system.[28] NCEs acquire and enforce patents but typically do not practice them.[29] Instead, they monitor the technological advancements made by operating entities and keep their patents alive through the USPTO[30] application continuation process,[31] mirroring, on paper, the real-world innovation.[32] When it becomes apparent that the real-world invention is about to realize commercial success, a typical NCE tactic is to offer the operating entity to license the patent

26. *Id.* at *1 (however, the NCE prevailed because the court noted that the respondent failed to identify a patent in suit. Note that the court indicated, citing F.T.C. v. Actavis, Inc., 133 S. Ct. 2223, 2231 (2013), that increased licensing fees would not be allowed if they were not entirely related to the patent in suit or if the patentee attempted to extend its power beyond the term of the patent). *See id.* at 10.

27. A streamlined solution is much needed. *See*, *e.g.*, POSNER, *supra* note 23, at 90 (Judge Posner points out that the current "patent doctrine . . . is such a tangle that even inventors have great difficulty understanding it").

28. Mark Lemley, *Should Patent Infringement Require Proof of Copying?*, 105 MICH. L. REV. 1525 (2007).

29. ROBERT P. MERGES, & JOHN F. DUFFY, PATENT LAW AND POLICY: CASES AND MATERIALS 895 (LexisNexis, 6th ed., 2013).

30. U. S. PATENT & TRADEMARK OFFICE, www.uspto.gov (a US government agency that regulates patents and trademarks) (last modified Oct. 26, 2015).

31. U. S. PATENT & TRADEMARK OFFICE, MANUAL OF PATENT EXAMINING PROCEDURE § 211 (9th ed. 2014), http://www.uspto.gov/web/offices/pac/mpep/s211.html [hereinafter MPEP] (procedure for claiming a benefit of an earlier filing date through divisional applications).

32. Lemley, *supra* note 28, at 2 (describing abuse by NCEs of continuation proceedings available in USPTO patent prosecution practice and used by NCEs to enhance and supplement existing patents).

held by the NCE in exchange for avoiding claims of patent infringement.[33]

Information technology companies are particularly vulnerable to NCE activity since a single patent on a component, which cannot be easily replaced because of complex interfaces with other components, can give NCEs enormous leverage even when the value of the patented technology itself is not very great.[34] For example, one study found that the most frequently litigated patents asserted in 2012-2014 by ten NCEs, which collectively brought infringement claims against 2,451 defendants, included those for geolocation, database, computer user interaction, and digital fingerprinting technologies.[35]

B. The Economic Case for Judicially Limiting Downstream Effects of NCE Licensing Activity

Companies often choose to license patents from NCEs, instead of litigating, for two main reasons. First, the costs involved in defending a patent infringement suit are significant. For example, one study found that infringement litigation cost small U.S. companies $11 billion in 2011.[36] Second, losing in an infringement suit could lead to a court-ordered injunction and company shutdown.[37] When patented technology is licensed from non-creative entities, such entities gain a disproportionate amount of power in directing the licensee's change-of-control decisions by enforcing non-assignability clauses in patent licenses.

33. Donald J. Chisum, *Reforming Patent Law Reform*, 4 J. MARSHALL REV. INTELL. PROP. L. 336, 340 (2005).

34. MERGES & DUFFY, *supra* note 29, at 895.

35. Colleen Chien, *Patent Assertion and Startup Innovation*, NEW AM. FOUND., OPEN TECH. INST. 14 (Sept. 5, 2013), http://ssrn.com/abstract=2321340 (This study was commissioned by the U.S. Congress as part of the America Invents Act of 2011, which sought to simplify the U.S. patent system).

36. Jeremy Quittner, *Supreme Court Deals Death Blow to Patent Trolls*, INC (Feb. 28, 2015, 6:38 PM), http://www.inc.com/jeremy-quittner/supreme-court-ruling-on-patent-trolls.html ("Small businesses mounted 3,400 legal defenses in 2011 for patent cases, a 32 percent increase over the prior year . . . . That cost to small companies was about $11 billion in 2011, also a 32 percent increase over the prior year. The total median awards to trolls is now nearly twice as high as those to legitimate patent holders, whose median reward fell about 30 percent to $4 billion, according to a 2013 report by PricewaterhouseCoopers.") (internal citations omitted).

37. MICHAEL J. KASDAN ET AL., PRACTICAL LAW CO., PATENT INFRINGEMENT CLAIMS AND DEFENSES 11 (2011), http://www.arelaw.com/downloads/ARElaw_PatentInfringementClaimsDefenses.pdf. ("[T]he most powerful remedy available to a patent owner is a preliminary or permanent injunction that prevents the accused infringer from importing, making, using, selling, offering for sale or importing into the US any product that infringes the patent.").

Since publicly available information does not include NCE licensing agreements, patent acquisition information, and cost and revenue data, the full economic impact of NCE activity is unknown.[38] However, we do know that startup companies are attractive targets for non-creative entities because of these companies' undercapitalization and vulnerability.[39] Moreover, startup companies are also attractive targets for merger and acquisition transactions (M&A) because of their valuable niche technologies, and non-creative entities frequently initiate their patent assertion efforts when a startup is about to issue an initial public offering or be acquired in an M&A transaction.[40]

A report commissioned by the U.S. Congress to study the impact of patent litigation on the U.S. economy as part of the America Invents Act of 2011 found that start-up companies are frequent targets for non-creative entities.[41] This is due to the prospect of quick monetary gain from "nuisance" settlements and the precedential value of settlements that gives NCEs additional leverage in licensing negotiations with larger companies.[42] Approximately 75% of surveyed venture capitalists and 20% of venture-backed startups with patent experience had been approached by non-creative entities, and approximately 80% of the time NCE demands included a licensing arrangement for the startup's own technology and 40% of the time an adoption of NCE-patented technology.[43]

Startups with information technology- and electronics-based products were NCE targets approximately 90% of the time.[44] Even with value-at-risk of under $1,000,000, the average cost of litigating a

38. *See* Public Comment by Mark Bohannon, Red Hat, Inc., FED. TRADE COMM'N (Dec. 16, 2013, 1:19 PM), http://www.ftc.gov/policy/public-comments/comment-00043-17 (proposing to send information requests to approximately 25 Patent Assertion Entities ("PAEs"), as well as to approximately 15 other entities asserting patents in the wireless communications sector as part of Project No. P131203). The author, who represents a company in the industry segment strongly impacted by NCE activity, supports the proposed FTC study and notes that the agency is uniquely positioned to collect this much needed information.

39. Eric Savitz, *Are Patent Trolls Now Zeroed In on Start-Ups?*, FORBES (Feb. 28, 2015, 6:45 PM), http://www.forbes.com/sites/ciocentral/2013/01/17/are-patent-trolls-now-zeroed-in-on-start-ups/.

40. Chien, *supra* note 35, at 11.

41. *Id.* at 31.

42. *Id.* (explaining nuisance value, ("[T]rolls know enough to peg [the] license fee just below [the] cost") and the precedential value of settlements, ("[Patent holders] go after startup companies to establish case precedent. Startups quickly agree to settle for a low amount because they have no money with which to stand up against an expensive legal battle. [The patent holder] then attacks larger companies for money, using those previously established case precedents.")).

43. *Id.* at 13.

44. *Id.*

patent infringement lawsuit is $650,000.[45] Because of the high cost of litigation, and because pending patent litigation diminishes the value of the entire company by as much as 20%, start-up companies choose, at the rate of one in five companies, to settle with NCEs rather than litigate with them.[46]

While the typical value of "nuisance" settlements and licensing costs are relatively small—with various estimates placing the value of licensing agreements at $1,000 to $50,000[47] and the value of an average settlement agreement at $340,000[48]—the downstream effects of these licensing arrangements are devastating. For example, one likely effect of NCE activity is the loss of start-up funding. One study estimates that NCE activity adds operating risk and thereby negatively impacts the U.S. economy by making venture capital unwilling to invest in start-up companies, costing the U.S. economy between $8.1 billion and $41.8 billion in venture capital losses over a five-year period.[49]

Another problematic effect is a cloud on the start-up's title to its intellectual property assets. When a target's technology is encumbered by a patent license, the first option a prospective purchaser of the target is likely to pursue is licensor consent to assignment, a new license, or a sub-license,[50] which introduces significant additional licensing fees as a condition of the transaction. In licensing transactions, the licensor typically receives a significant royalty amount—25% of the profit generated by the licensed invention.[51] While the Federal Circuit recently noted that the 25% Rule is not always appropriate,[52] the holding was limited to the calculation of damages and it is not binding on private parties negotiating a licensing contract.

At the same time, as illustrated in the hypothetical case of *Patent troll v. Small Inventor, Inc.* presented in the Introduction, NCEs are

45. Savitz, *supra* note 39 (citing a Report of the Economic Survey published by the American Intellectual Property Law Association).

46. Chien, *supra* note 35, at 11–12, 17.

47. *Conversant Takes Aim at Patent Troll Demand Letters*, CONVERSANT (Feb. 28, 2015, 6:49 PM), http://www.conversantip.com/news-article/conversant-takes-aim-at-patent-troll-demand-letters/.

48. *See generally* Chien, *supra* note 35.

49. Catherine Tucker, *The Effect of Patent Litigation and Patent Assertion Entities on Entrepreneurial Activity* 31 (MIT Sloan School of Mgmt., Working Paper No. 5095-14, 2014), http://ssrn.com/abstract=2457611.

50. Ziff & Deming, *supra* note 6, at 9–10.

51. INTELLECTUAL PROPERTY ASSETS, *supra* note 19, at 4.12.

52. Uniloc USA, Inc. v. Microsoft Corp., 632 F.3d 1292 (Fed. Cir. 2011).

unlikely to permit the licensees to transfer contracts to business successors if original royalty terms are significantly lower than what they are reasonably likely to recover as infringement damages.[53] Because breaching the terms of the license and proceeding with the corporate sale would force licensees or their successors to internalize the cost of increased royalties, recoverable by NCEs in the form of damages, the real-world effect of anti-assignability clauses in licenses is likely a failure to execute the change of control or assent to an increase in royalties.[54] Each of these outcomes is sub-optimal—the former because the public is deprived of the benefit of accessing the patented invention through the business successor,[55] and the latter because it represents a transfer of profits from an operating entity to a non-producer.

Yet another potential effect is a negative impact on the start-up's valuation. If the buyer is unable to reach an agreement with the licensor-NCE, the buyer will likely attempt to negotiate with the target a price discount for the lost value of the licensed intellectual property.[56] This, in turn, will negatively impact the valuation of the target company, and the resulting loss is likely to be disproportionately greater than the cost of the initial licensing arrangement with the NCE. Other than licensing, options that the buyer is likely to pursue include seeking indemnity for any patent infringement claims arising from the use by the buyer of licensed patents or reimbursement of the buyer's cost of acquiring replacement intellectual property.[57] Indemnification, not surprisingly, adds costs.

An average successful start-up sells for approximately $196.8 million.[58] Combined with expected valuation loss of 20% if a patent

53. 35 U.S.C.A. § 284 (West 2012) ("Upon finding for the claimant the court shall award the claimant damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer . . . .") (emphasis added).

54. Juliet P. Kostritsky, *Incomplete Contracts: Judicial Responses, Transactional Planning, and Litigation Strategies*,, 56 CASE W. RES. L. REV. 135, n.57 (2005) ("[T]he courts adopt a damage measure that forces a breaching party to internalize the costs of its breach . . . . [This] damage rule is efficient in the same way that strict liability rules in torts can be efficient: parties can estimate for themselves when it is efficient to breach [and] the breacher will take into account the damage that a court would assess and compare that amount to the benefits from breaching.") (internal citations omitted).

55. This is inconsistent with the goal of promoting "Science and Useful Arts." *See* U.S. CONST. art. I, § 8, cl. 8.

56. Ziff & Deming, *supra* note 6, at 9.

57. *Id.*

58. Eric Eldon, *CrunchBase Reveals: The Average Successful Startup Raises $25.3 Million, Sells For $196.8 Million*, TECHCRUNCH (Jan. 3, 2012), http://techcrunch.com/2012/01/03/crunchbaseexits/.

infringement lawsuit is pending, the cost of the initial "nuisance" licensing settlement with the NCE will now increase to up to $40 million— either because negotiations will position an average licensor-NCE to demand up to $40 million, or 20% of the target's valuation, in licensing fees from the purchasing company, or because the target will be expected to absorb up to this amount through indemnification and litigation cost-sharing with the buyer.

Problematically, even in the absence of an explicit non-assignment clause in a patent license between the NCE and the original licensor, intellectual property transfer is considered an asset sale in the context of corporate restructuring transactions, and, as such, the purchaser remains vulnerable to claims of infringement if a corporate transfer occurs by operation of law.[59] In other words, it is nearly impossible to circumvent a typical anti-assignment clause in a patent license.

It is unlikely that the judiciary contemplated such extreme results when the body of law that made licenses non-assignable was developed. It is likewise improbable that the drafters of the Patent Clause in the U.S. Constitution[60] contemplated rewarding non-producing patent holders to this extent.[61] In fact, many patents are simply ahead of their time, and the relaxed constructive enablement standard, which allows applicants to receive patents by explaining how an invention would work rather than producing a functioning model, was created to account for this possibility.[62]

It is, however, unlikely that the promulgators of the constructive enablement standard envisioned that an NCE would procure a patent

59. Ziff & Deming, *supra* note 6, at 2 ("[W]here an IP license is silent on assignability by the licensee, the majority of courts have found that a licensee's rights are presumed not assignable without the licensor's express consent.").

60. U.S. CONST. art. I, § 8, cl. 8; *see also* Ultramercial, Inc. v. Hulu, LLC, 772 F.3d 709, 717–18 (Fed. Cir. 2014) (Mayer, J. concurring) ("Unless we are to assume that the constraints explicit in the Intellectual Property Clause are mere surplusage, we are bound to ensure that the patent monopoly serves '[t]o promote the Progress of Science and useful Arts . . . . This is the standard expressed in the Constitution and it may not be ignored.'") (citing Graham v. John Deere Co., 383 U.S. 1, 6 (1966)) (internal citations omitted).

61. *Ultramercial, Inc.*, 772 F.3d 709 at 718 ("[T]he primary purpose of the patent system is to promote scientific progress, not to creat[e] . . . private fortunes for the owners of patents.") (citing Motion Picture Patents Co. v. Universal Film Mfg. Co., 243 U.S. 502, 511 (1917)) (internal citations omitted).

62. 35 U.S.C.A. § 112 (West 2012).

on a pre-populated drop-down box before interactive computing devices become feasible and then bring infringement actions against operating entities using this common technology.[63]

II. LEGAL BACKGROUND

A. Filling the Gaps in Traditional Defenses to Claims of Patent Infringement

Non-creative entities typically bring claims of patent infringement, and relaxing the rules for license alienability would therefore shield licensors and their successors from such claims.

Patent infringement is a statutorily defined concept.[64] The United States Code recognizes three primary categories of patent infringement: direct infringement, induced infringement, and contributory infringement.[65] The concept of direct infringement is codified in 35 U.S.C. § 271(a) and makes it unlawful to make, use, offer for sale or sell another's patented invention.[66] The doctrine of induced infringement is codified in 35 U.S.C. § 271(b) and prohibits actions that "actively induce[] infringement of a patent"[67] when the accused infringer knows that a patent exists. Contributory infringement, codified in 35 U.S.C. § 271(c), makes it unlawful to import, sell, or offer for sale a component that constitutes a material part of a patented invention.[68] Both contributory and induced infringements require proof of direct infringement and impose an additional scienter requirement on the accused infringer.[69]

63. Soverain Software LLC v. Newegg, Inc., 705 F.3d 1333, 1341 (Fed. Cir. 2013), *aff'd*, 728 F.3d 1332 (Fed. Cir. 2013) ("We conclude that the prior art . . . by clear and convincing evidence, rendered obvious the 'shopping cart' claims."), *cert. denied*, 134 S. Ct. 910 (2014); *see also* Daniel Nazer, *Bad News for Patent Trolls! FTC to Look Under the Hood of the Trollmobile*, ELEC. FRONTIER FOUND. (Feb. 28, 2015, 6:49 PM), https://www.eff.org/deeplinks/2013/06/bad-news-patent-trolls-ftc-look-under-hood-trollmobile (noting that a Federal Trade Commission spokesperson used this case as an example of frivolous patent enforcement when FTC announced an investigation into the conduct of "patent trolls").

64. 35 U.S.C.A. § 271 (West 2010).

65. *Id.*

66. 35 U.S.C.A. § 271(a) (West 2010).

67. 35 U.S.C.A. § 271(b) (West 2010).

68. 35 U.S.C.A. § 271(c) (West 2010).

69. Plastering Dev. Ctr., Inc. v. Perma Glas-Mesh Corp., 371 F. Supp. 939, 949 (N.D. Ohio 1973) (discussing Aro Mfg. Co. v. Convertible Top Replacement Co., 365 U.S. 336 (1961) and Aro Mfg. Co. v. Convertible Top Replacement Co., 377 U.S. 476 (1964)) ("The fundamental basis of patent law requires that a patent holder establish acts of direct infringement before liability for inducement or contributory infringement can be found.").

Traditional defenses to claims of patent infringement can be broadly grouped into three categories. The first category is simple non-infringement—that is, the accused infringer establishes that its actions do not meet the elements of patent infringement.[70] This statutorily codified category of defenses includes non-infringement, absence of liability for infringement, and unenforceability.[71] This Note proposes linking license alienability, via a doctrine of patent misuse, to this category of defenses—specifically, to unenforceability—because the unenforceability defense, if sustained, does not invalidate the underlying patent. This is, advantageously, a narrowly tailored solution.

The second, frequently litigated, category of defenses challenges patent validity in view of statutory requirements for patentability.[72] Likewise, this category is statutorily codified[73] and includes failure to meet the statutory requirements of patentability on the grounds of indefiniteness,[74] anticipation[75] and obviousness[76] of patented subject matter in light of prior art consisting largely of patents previously issued to the patent-holder and any third parties.[77]

This doctrinal body of defenses is predicated on the concept that a patent cannot be infringed if it is invalid, and the burden is on the defendant to establish patent invalidity.[78] As discussed in Part II *infra*, relying on patent invalidity to defend against claims of patent infringement is problematic because, unlike the enforceability-based solution introduced here, invalidity-based defenses result in court holdings that generate substantive and procedural uncertainty.

The third category of defenses includes equitable defenses, such as inequitable conduct in the process of procuring a patent, patent exhaustion, laches, and equitable estoppel.[79]

70. KASDAN, *supra* note 37, at 5.
71. 35 U.S.C.A. § 282(b)(1) (West 2012).
72. KASDAN, *supra* note 37, at 5.
73. 35 U.S.C.A. § 282(b)(2) (West 2012).
74. 35 U.S.C.A. § 112 (West 2012).
75. 35 U.S.C.A. § 102 (West 2015).
76. 35 U.S.C.A. § 103 (West 2015).
77. KASDAN, *supra* note 37, at 5–7.
78. *See*, *e.g.*, Soverain Software LLC v. Newegg, Inc., 705 F.3d 1333, 1341 (Fed. Cir. 2013) (citing the "clear and convincing evidence" standard).
79. Quanta Comput., Inc. v. LG Elec. Inc., 553 U.S. 617, 625 (2008) ("The longstanding doctrine of patent exhaustion provides that the initial authorized sale of a patented item terminates all patent rights to that item."); *see also* KASDAN, *supra* note 37, at 6.

The doctrine of patent exhaustion is of particular interest in the context of NCE activity. Patent exhaustion negates infringement if the accused infringer shows that it has an express or implied license from the patentee to practice the invention.[80] Equitable defenses illustrate the need for relaxing the rules for alienability of patent licenses. For example, under the doctrine of patent exhaustion, the patentee loses the ability to block others from using its invention after it places the patented article in the stream of commerce.[81] This makes the operating entity-patentee unable to take advantage of the entire economic value chain[82] and precludes recovery when, for example, purchasers refurbish and competitively resell the patented product.[83]

Thus, entities that practice their patents by making products lose the right to control their inventions as soon as patented articles are sold. On the other hand, NCEs, who do not themselves produce any articles based on their patents and therefore commercialize patents by licensing them rather than selling manufactured patented articles, control their patents long after these are licensed. This inequity is yet another reason for relaxing the rules for alienability of NCE licenses, at a minimum to the licensee-operating entity's business successors.

B. Why the Courts Are Ready to Look at NCE Contracts—a Historical Progression of Anti-NCE Litigation

1. Patent Infringement Litigation

The U.S. Supreme Court recently issued a number of decisions intended to limit the impact of NCE activity. SCOTUS, in developing its body of precedential case law, has focused, in succession, on limiting the remedies available to NCEs,[84] refining the rules on whether and when NCE patents are infringed,[85] and determining whether NCE

80. *Id.*

81. *Quanta Comput. Inc.*, 553 U.S. at 633–35 (patent rights to products that "constitute a material part of the patented invention" are exhausted when such products are sold).

82. Timothy J. Sturgeon & Momoko Kawakami, *Global Value Chains in the Electronics Industry* 3 (The World Bank, Policy Research Working Paper No. 5417, 2014), http://secnet087.un.org/unsd/trade/s_geneva2011/ref-docs/RDs/GVC%20in%20Electronics%20Industry%20(Sturgeon%20-%20Sep%202010).pdf ("Intermediate electronics and automotive goods dominate total trade in the top-50 manufactured intermediate products." In other words, the electronics industry relies on modular financing, where a component may become more valuable when combined with other components in a finished product).

83. LG Elecs., Inc. v. Hitachi, Ltd., 655 F. Supp. 2d 1036, 1045–46 (N.D. Cal. 2009).

84. eBay Inc. v. MercExchange, LLC, 547 U.S. 388 (2006).

85. Limelight Networks, Inc. v. Akamai Techs., Inc., 134 S. Ct. 2111 (2014).

patents are valid.[86] Additionally, lower courts limited the binding power of contracts in technology licensing.[87] It is clear that the courts are now well-positioned to consider a logical extension to this body of law by developing rules for invalidating anti-assignment clauses in NCE licensing contracts.

SCOTUS first tackled remedies. In *eBay, Inc. v. MercExchange, L.L.C.*, SCOTUS, following a finding of patent infringement, denied the plaintiff a permanent injunction because the suit arose from a non-competitor.[88] The Court affirmed that the purpose of the Patent Act was to protect innovation by excluding others from infringing,[89] but employed a policy-based analysis to conclude that the status of the parties as competitors is dispositive on the issue of whether injunctions can be granted.[90] The Court grounded its decision in an equity-based four-factor test to determine when an injunction is appropriate[91] and indicated that it saw no public policy benefit in putting an accused infringer out of business and, by doing so, granting NCEs additional leverage to negotiate favorable licensing terms.[92]

Notably, SCOTUS held that the status of parties as non-competitors is key to restricting availability of injunctive relief to NCEs. Forcing the accused party to shut down operations in response to a suit

86. Nautilus, Inc. v. Biosig Instruments, Inc., 134 S. Ct. 2120 (2014); Alice Corp. Pty. Ltd. v. CLS Bank Int'l, 134 S. Ct. 2347 (2014).

87. *See infra* notes 128–30; *see generally* A.L.I., PRINCIPLES OF THE LAW: SOFTWARE CONTRACTS 44 (2010) (noting that clauses that constitute IP misuse should be unenforceable).

88. *eBay Inc.*, 547 U.S. at 396–97 (Kennedy, J., Stevens, J., Souter, J., and Breyer, J., concurring) ("When the patented invention is but a small component of the product the companies seek to produce and the threat of an injunction is employed simply for undue leverage in negotiations, legal damages may well be sufficient to compensate for the infringement and an injunction may not serve the public interest.").

89. *See id.* at 396 (J. Kennedy, J. Stevens, J. Souter, J. Breyer concurring) ("In cases now arising trial courts should bear in mind that in many instances the nature of the patent being enforced and the economic function of the patent holder present considerations quite unlike earlier cases. An industry has developed in which firms use patents not as a basis for producing and selling goods but, instead, primarily for obtaining licensing fees. . . . For these firms, an injunction, and the potentially serious sanctions arising from its violation, can be employed as a bargaining tool to charge exorbitant fees to companies that seek to buy licenses to practice the patent.")

90. *See id.* at 391 (majority opinion) ("According to well-established principles of equity, a plaintiff seeking a permanent injunction must satisfy a four-factor test before a court may grant such relief. A plaintiff must demonstrate: (1) that it has suffered an irreparable injury; (2) that remedies available at law, such as monetary damages, are inadequate to compensate for that injury; (3) that, considering the balance of hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction.")

91. *Id.*

92. *Id.* at 397 (Kennedy, J., Stevens, J., Souter, J., and Breyer, J., concurring).

from an NCE arguably yields a loss to the economy without a corresponding benefit.[93] The proposal, advanced in this Note, to relax the rules of alienability of licenses from NCEs to the licensor's business successors is premised on the same principle.

In further attempts to limit the fallout from NCE activity in the information technology industry, SCOTUS tightened the standard for determining whether infringement occurred, making it more difficult for NCEs to prevail in infringement suits. For example, in *Limelight Networks, Inc. v. Akamai Technologies, Inc.*, the Court held that proof of induced infringement first required proof of direct infringement.[94] The effect of this decision is a heightened standard for establishing induced infringement, and this effect is of particular significance to information technology patents, where method claims, comprising discrete steps, are frequently used to define patented subject matter.[95] Under the standard upheld by SCOTUS, to establish infringement, it is necessary for the moving party to show that a single infringing actor had performed all the steps.[96] The holding helped assure peace of mind for technology companies that would otherwise be vulnerable to infringement suits because the technologies they make are highly interactive and many steps that take place as a matter of practicing these inventions are carried out by end users.[97]

In their brief supporting the petitioner, key actors in the information technology industry warned the Supreme Court that modifying

93. *See id.* at 396 ("In cases now arising trial courts should bear in mind that in many instances the nature of the patent being enforced and the economic function of the patent holder present considerations quite unlike earlier cases. An industry has developed in which firms use patents not as a basis for producing and selling goods but, instead, primarily for obtaining licensing fees. . . . For these firms, an injunction, and the potentially serious sanctions arising from its violation, can be employed as a bargaining tool to charge exorbitant fees to companies that seek to buy licenses to practice the patent.").

94. Limelight Networks, Inc. v. Akamai Techs., Inc., 134 S. Ct. 2111 (2014).

95. 35 U.S.C.A. § 100(b) (West 2015) ("The term "process" means process, art, or method, and includes a new use of a known process, machine, manufacture, composition of matter, or material.").

96. *Limelight Networks, Inc.*, 134 S.Ct. at 2117.("[A] method's steps have not all been performed as claimed by the patent unless they are all attributable to the same defendant, either because the defendant actually performed those steps or because he directed or controlled others who performed them.").

97. Kimberly Atkins, *Supreme Court Rulings Could Create Issues for Patent Trolls*, NEW ENGLAND IN-HOUSE, http://newenglandinhouse.com/2014/07/15/supreme-court-rulings-could-create-issues-for-patent-trolls/#ixzz3KOrL3E4D (last visited Aug. 2, 2015) ("If [the lower court, to which the case was remanded] upholds the single-actor standard, it will be good news for software companies like Microsoft, one of many amici that filed briefs in the case. Those briefs expressed concern that under a different standard, companies could face infringement suits even if they were unaware of customer actions that could be seen as implementing certain steps in a competitor's patent process.").

the single-actor standard would increase both uncertainty and complexity in discovery and would thus encourage abusive infringement litigation and force the settlement of even non-meritorious claims.[98] SCOTUS clearly agreed with this argument when it held for the petitioner.

The Supreme Court, during the 2014 term, also attempted to clarify the standards of patentability and made it easier for accused infringers to challenge NCE infringement claims by advancing a defense of patent invalidity. For instance, in *Nautilus, Inc. v. Biosig Instruments, Inc.*, SCOTUS clarified the standard of definiteness in claim language,[99] and in *Alice Corp. Pty. v. CLS Bank Int'l*, SCOTUS took steps to limit the subject matter that is eligible for patenting.[100]

While the Supreme Court should be commended for its efforts to limit NCE activity, the body of precedential law illustrated by its recent decisions is not yet complete. Under *eBay*, NCEs can still seek monetary damages. Under *Limelight*, pharmaceutical companies, another industry that drives innovation, are left unable to bring valid claims of infringement against copycats who change the drug delivery mechanism by splitting the practice of the invention between the manufacturer and the end user. Finally, the *Nautilus* and *Alice* decisions have been welcomed in the information technology sector but they still require accused infringers to put up an expensive defense. Todd Moore, a member of the Application Developers Alliance and CEO and Founder of TMSOFT, an application publisher for mobile devices, commented on the *Alice* decision: "This ruling is definitely a win and I hope the USPTO will stop issuing patents on abstract ideas. But what

98. Brief for Google, Inc. et al. as Amici Curiae Supporting Petitioner, Limelight Networks, Inc. v. Akamai Techs., Inc., 134 S. Ct. 2111 (Mar. 3, 2014) (No. 12-786), at 16 ("Far-reaching discovery into the geographically, temporally, and functionally disparate operation of unrelated suppliers of complementary goods and services will provoke settlements driven by cost rather than the merits of the parties' claims.").

99. Nautilus, Inc. v. Biosig Instruments, Inc., 134 S. Ct. 2120, 2129 (2014) ("[W]e read § 112, ¶ 2 to require that a patent's claims, viewed in light of the specification and prosecution history, inform those skilled in the art about the scope of the invention with reasonable certainty. The definiteness requirement, so understood, mandates clarity, while recognizing that absolute precision is unattainable.").

100. Alice Corp. Pty. Ltd. v. CLS Bank Int'l, 134 S. Ct. 2347, 2356 (2014) (holding that the concept of intermediated transaction settlement embodied by the patented system is an abstract idea and is therefore unpatentable).

about the thousands that were already issued? It's too expensive to let companies fight every bad patent out there."[101]

Indeed, litigating bad patents is expensive because a USPTO-issued patent is presumed valid,[102] and a successful invalidity defense requires proof "by clear and convincing evidence."[103] The solution proposed in this Note avoids problems associated with high costs of litigating patents because the argument for alienability of patent licenses issued by NCEs is tailored precisely to avoid the litigating issue of patent validity.

2. Problems with Invalidity-Based Defenses to Claims of Infringement

Two main problems with the recent judicial trend of invalidating patents to dispose of claims of infringement are substantive and procedural uncertainty. The proposal advanced in this Note avoids these problems because it focuses on patent unenforceability as to the licensee or its successor rather than invalidity.

As to substantive uncertainty, an adverse effect of *Nautilus*, *Alice* and their progeny is the uncertainty they have introduced by changing the rules of patentability. In *Alice*, for example, SCOTUS held that the concept of intermediated transaction settlement embodied by a patented computer system was an abstract idea and is therefore unpatentable in the absence of factors that would amount to "significantly more" than a mere idea.[104] The holding allowed an accused infringer to prevail over an NCE's claim of patent infringement by arguing that the NCE's patent was invalid.

On the flipside, the holding drastically impacted patentability of software inventions, especially in the financial services industry. Within two months of the *Alice* decision, USPTO withdrew 830 previously granted patents from allowance[105] even though these patents

101. *U.S. Supreme Court Software Patent Decision: What Alliance Members Are Saying*, APPLICATION DEVELOPERS ALL. (June 20, 2014), https://www.appdevelopersalliance.org/news/2014/6/20/us-supreme-court-software-patent-decision-what-apps-alliance-members-are-saying.

102. 35 U.S.C.A. § 282(a) (West 2012).

103. Microsoft Corp. v. i4i Ltd. P'ship., 131 S. Ct. 2238, 2246 (2011).

104. *Alice Corp.*, 134 S. Ct. at 2353.

105. Gray-Le Coz & Duan, *supra* note 17 (assignees with the most withdrawals of allowances included technology and financial services giants IBM, Microsoft, eBay, IGT, and JPMorgan Chase Bank).

were directed to processes, which is a statutorily patentable category.[106] CAFC followed *Alice* by invalidating patents directed to image data processing and correlation,[107] algorithm processing in online gaming,[108] and online transaction processing.[109] Prior to *Alice*, similar technologies were found patent-eligible.[110]

The *Alice* rule did not provide a clear standard for evaluating patent-eligibility of software and online technologies. Following the *Alice* decision, patent claims directed to online advertising technologies were invalidated in *Ultramercial v. Hulu, LLC* in part because they contained "insignificant data gathering steps",[111] yet similar claims were upheld in *DDR Holdings, LLC v. Hotels.com, L.P.* because the abstract idea was not easily identifiable from the patent claim at issue.[112] Post-*Alice*, the strength of patents directed to computer technologies appears to rest not in the inventive value of the patented systems, but rather in the patent drafter's skill to avoid describing the systems as abstract ideas. Arguably, the *Alice* approach to patent invalidity results in a high degree of uncertainty in the industry because numerous patents drafted and issued pre-*Alice* may be found ineligible.

Another problem with *Alice*-like defenses to infringement, which are based on patent invalidity, is procedural uncertainty. Findings of invalidity require the court to construe patent claims to determine the scope of the patented invention.[113] However, courts, sympathetic to accused infringers, recently introduced procedural shortcuts aimed at avoiding the question of patent validity, including modification of the evidentiary standard and issuing decisions of invalidity without formal claim construction hearings.

For example, in *Bose Corp. v. SDI Tech.*, CAFC held that a summary judgment of non-infringement was appropriate if the accused

106. 35 U.S.C.A. § 103 (West 2015).

107. Digitech Image Techs., LLC v. Elecs. for Imaging, Inc., 758 F.3d 1344,1347 (Fed. Cir. 2014).

108. Planet Bingo, LLC v. VKGS LLC, 576 F. App'x 1005, 1006 (Fed. Cir. 2014).

109. buySAFE, Inc. v. Google, Inc., 765 F.3d 1350, 1351 (Fed. Cir. 2014).

110. *See, e.g.,* SiRF Tech v. ITC, 601 F.3d 1319, 1322 (Fed. Cir. 2010) (a method for calculating an absolute position of a GPS receiver).

111. Ultramercial, Inc. v. Hulu, LLC, 772 F.3d 709, 716 (Fed. Cir. 2014) (citing CyberSource Corp. v. Retail Decisions, Inc., 654 F.3d 1366, 1370 (Fed. Cir. 2011)).

112. DDR Holdings, LLC v. Hotels.com, L.P., 773 F.3d 1245 (Fed. Cir. 2014).

113. Markman v. Westview Instruments, Inc., 517 U.S. 370, 372 (1996) ("We hold that the construction of a patent, including terms of art within its claim, is exclusively within the province of the court.").

infringer relied in good faith on counsel's opinion[114] that the opposing party's patent was invalid.[115] Similarly, in *Commil USA, LLC v. Cisco Sys., Inc.*,[116] CAFC disposed with the "clear and convincing evidence" requirement to prove invalidity by using the accused infringer's good-faith belief that the patent was invalid as a basis for a finding of no infringement liability.[117] As a result, the "clear and convincing evidence" standard is now grounded in the accused infringer's subjective belief[118] rather than in invalidity of a patent in light of its claims.[119]

Finally, courts have increasingly relied on USPTO grant of *inter partes* reviews, which USPTO grants when "there is a reasonable likelihood that the petitioner would prevail with respect to at least [one] of the claims challenged in the petition,"[120] as evidence of good-faith belief that the accuser's patent is invalid. However, this is not a good proxy because USPTO grants such review more often than not and because a mere likelihood of invalidity may not translate to a finding of invalidity at trial. USPTO appears to recognize this as a problem because the number of *inter partes* review petitions that have been denied has been steadily increasing: in FY 2013, 13% of such petitions were denied; in 2014, this number increased to 25%, and in FY 2015, it further increased to 29%.[121]

Another recent decision indicative of procedural uncertainty is CAFC's finding of patent invalidity in *Ultramercial v. Hulu, LLC*[122] discussed *supra*. The court, in reviewing a district court's dismissal for

114. Underwater Devices, Inc. v. Morrison-Knudsen Co., 717 F.2d 1380, 1389–90 (Fed. Cir. 1983), *overruled on other grounds by* In re Seagate Tech., LLC, 497 F.3d 1360 (Fed. Cir. 2007)) (accused infringer has a "duty to seek and obtain competent legal advice from counsel before the initiation of any possible infringing activity").

115. Bose Corp. v. SDI Techs., Inc., 558 Fed. App'x. 1012, 1024 (Fed. Cir. 2014).

116. Commil USA, LLC v. Cisco Sys., Inc., 720 F.3d 1361 (Fed. Cir. 2013), *reh'g denied* (Oct. 25, 2013), *cert. denied*, 135 S. Ct. 704 (2014) and *cert. granted in part*, 135 S. Ct. 752 (2014).

117. Brief of Biotechnology Industry Organization as Amicus Curiae Supporting Petitioner, Commil USA, LLC v. Cisco Sys., Inc., 2015 WL 394343 (2015) (No. 13-896), at 14 ("By permitting an inducer to avoid liability by virtue of a good-faith belief of invalidity, the Federal Circuit provides a pathway by which one accused of inducement may effectively assert an invalidity defense that runs up against no presumption of validity, and that can be established on evidence that is less than 'clear and convincing.' As demonstrated by the facts of this case, an inducer may avoid liability by a mistaken belief of invalidity. So long as it is held in good faith, the inducer's invalidity defense can be entirely meritless.") (internal citations omitted).

118. *Id.*

119. *Id.*

120. 35 U.S.C.A. § 314(a) (West 2012).

121. U. S. PATENT & TRADEMARK OFFICE, PATENT TRIAL AND APPEAL BOARD STATISTICS (2015), http://www.uspto.gov/sites/default/files/documents/2015-06-30%20PTAB.pdf.

122. Ultramercial, Inc. v. Hulu, LLC, 772 F.3d 709 (Fed. Cir. 2014).

failure to state a claim, issued a holding that an NCE's patent was invalid[123] in the absence of a claim construction hearing.[124] In 1996, SCOTUS, in *Markman*, held that claim construction is a question of law, and, following this decision, *Markman* hearings, or proceedings solely limited to determining the scope of patent claims at issue and distinct from proceedings on infringement, became common practice. *Markman* hearings[125] provide an opportunity for both sides to introduce technical experts and evidence to aid in claim construction[126] on "case dispositive" claim terms.[127]

The decisions discussed above represent impressive judicial efforts to limit NCE activity.[128] The resulting procedural uncertainty, however, is a significant drawback of relying on patent invalidity to challenge infringement claims because it renders legal analysis imprecise, as in *Commill*, and makes the judicial decision-making process less transparent, as in *Ultramercial*. This, although reducing the cost of litigation, may diminish the value of patents for the industry. On the other hand, addressing the relationship between NCEs and accused infringers in the context of their contractual relationship without viewing such relationships through the lens of the NCE patent would avoid these problems.

3. Patent Licensing Litigation

When courts make it easier to legally challenge and wholly or partially invalidate licensing agreements, NCEs lose incentives to enter into these contracts. As such, promoting license alienability will help accomplish several important objectives. First, the problem of

123. *Id.* at 714.

124. *See* Markman v. Westview Instruments, Inc., 517 U.S. 370, 372 (1996) (holding that claim construction is a question of law).

125. John D. Love, U.S. Magistrate Judge, U. S. Dist. Court for the E. Dist. of Tex., Standing Order Regarding Letter Brief and Briefing Procedures for Early Markman Hearing/Summary Judgment of Non-Infringement Requests (Jan. 9, 2012) [hereinafter Standing Order], http://www.txed.uscourts.gov/cgi-bin2/view_document.cgi?document=21674.

126. En Liung Huang v. Auto Shade, Inc., 945 F.Supp. 1307, 1308 (C.D. Cal. 1996) ("Expert testimony upon this question is both permissible and appropriate if the court finds it to be of assistance in reaching its determination of the meaning of the language of the patent.") (citing Markman v. Westview Instruments, Inc., 517 U.S. 370 (1996), *aff'g*, 52 F.3d 967 (Fed. Cir. 1995)).

127. *See* Standing Order, *supra* note 125 (limiting claim construction requests to no more than three "case dispositive" terms).

128. Ultramercial, Inc. v. Hulu, LLC, 772 F.3d 709, 718 (Fed. Cir. 2014) (J. Mayer citing Motion Picture Patents Co. v. Universal Film Mfg. Co., 243 U.S. 502, 511) (1917) (explaining that "the primary purpose" of the patent system is to promote scientific progress, not to "creat[e] . . . private fortunes for the owners of patents.") (emphasis added).

existing bad patents will cease to exist because the parties will be able to challenge the license agreement rather than patent validity. This, in turn, will promote certainty and stability within the patent system. Second, the costs of litigation and the burdens on the court system will significantly diminish. Furthermore, companies that purchase intellectual property assets where the title is encumbered by a license with an NCE will be less likely to infringe and will therefore not be subject to monetary damages. This, in turn, will strengthen their negotiating position with NCEs.

Courts have already successfully undertaken the task of invalidating some aspects of intellectual property licensing contracts by, for example, disfavoring non-producers when defining succession rights to IP assets in bankruptcy proceedings and by limiting the doctrine of licensee estoppel. Licensee estoppel disfavors operating entities in comparison to NCEs by limiting the reach of patents held by operating entities to the products they sell.

In *Rates Tech., Inc. v. Speakeasy, Inc.*, the United States Court of Appeals for the Second Circuit concluded that a no-challenge clause in a settlement agreement is unenforceable if settlement occurs before litigation.[129] In *Stanford v. Roche* and *Preston v. Marathon Oil Co.*, CAFC held that a contract presently assigning future inventions takes precedence over a contract promising to assign such rights in the future.[130] These holdings granted more control over the patented subject matter to the inventor and its business successor, thus diminishing the amount of power given to intermediaries, such as the "patent troll" introduced in the beginning of this Note, who do not contribute to the creative process.

Another important development, aimed at discouraging licensing attempts by NCEs, is the recent trend in judicially limiting the power of patent holders to argue licensee estoppel to foreclose the other party from advancing infringement defenses.

NCEs routinely threaten infringement litigation to coerce operating entities to license because patent invalidity is one of the primary

129. Rates Tech., Inc. v. Speakeasy, Inc., 685 F.3d 163 (2d Cir. 2012*), cert. denied*, 133 S. Ct. 932, 184 (2013); *but see* Indus. Eng'g & Dev., Inc. v. Static Control Components, Inc., No. 8:12-CV-691-T-24-MAP, 2014 WL 4206584 (M.D. Fla. Aug. 25, 2014) (holding that a no-challenge clause was enforceable; however, note that here at issue was a claim for breach of a cross-licensing agreement).

130. Bd. of Trustees of Leland Stanford Junior Univ. v. Roche Molecular Sys., Inc., 583 F.3d 832 (Fed. Cir. 2009), *aff'd*, 131 S. Ct. 2188 (2011); Preston v. Marathon Oil Co., 684 F.3d 1276 (Fed. Cir. 2012).

defenses to claims of patent infringement, and the doctrine of licensee estoppel prevents licensees of patents from challenging patent validity.[131] The Supreme Court attempted to optimize this legal rule in *Lear, Inc. v. Adkins*, noting that the interest in protecting property rights granted by a patent must be balanced against the need to remove invalid patents from the patent system so that only valuable inventions are protected.[132] The lower courts subsequently narrowed the *Lear* doctrine when they held it to be inapplicable to patent assignment agreements, consent judgments, and litigation settlement agreements.[133] The lower courts also held that, in order to bring an action seeking a declaratory judgment of patent invalidity, the licensee first had to repudiate the licensing agreement by, for example, failing to pay royalties.[134]

Lower court decisions were favorable to patent-holders, including NCEs. The Supreme Court, however, reversed the trend of limiting the *Lear* doctrine when, in 2007, the Court relaxed the standing requirements in *MedImmune, Inc. v. Genentech, Inc.* and held that patent licensees did not need to repudiate or breach a licensing agreement in order to challenge the validity of the licensed patent.[135] SCOTUS thus demonstrated that it was ready to carve out an exception to the doctrine of licensee estoppel by disallowing licensors to seek immunity from patent validity challenges when they enter licensing agreements. NCEs could no longer enter licensing agreements to shield themselves from litigation by licensees.

The *MedImmune* decision discouraged NCEs from aggressively pursuing patent licensing.[136] In an apparent effort to further discourage NCEs from attempting to collect licensing fees on possibly weak

131. Ronald A. Bleeker & Michael V. O'Shaughnessy, *One Year After Medimmune-the Impact on Patent Licensing & Negotiation*, 17 FED. CIR. B.J. 401, 402 (2008).

132. Lear, Inc. v. Adkins, 395 U.S. 653, 664 (1969).

133. *See* Bleeker & O'Shaughnessy, *supra* note 131 ("[T]he Federal Circuit has repeatedly narrowed and limited the ruling's scope. For example, subsequent decisions held that *Lear* only applied to patent license agreements and not to patent assignment agreements or to consent judgments in patent cases. In addition, the courts held that *Lear* did not apply to litigation settlement agreements.").

134. Gen-Probe, Inc. v. Vysis, Inc., 359 F.3d 1376, 1380 (Fed. Cir. 2004), *abrogated by* MedImmune, Inc. v. Genentech, Inc., 549 U.S. 118 (2007).

135. MedImmune, Inc. v. Genentech, Inc., 549 U.S. 118, 135 (2007) ("Promising to pay royalties on patents that have not been held invalid does not amount to a promise not to seek a holding of their invalidity.").

136. PATENT REFORM AS IT APPLIES TO NON-PRACTICING ENTITY PATENT LITIGATION, AM. BAR ASSOC., http://www.americanbar.org/content/dam/aba/administrative/intellectual_property_law/archive/2012/patentreform-as-itapplies.authcheckdam.pdf (last visited Aug. 29, 2015) ("After MedImmune, patent trolls are less likely to aggressively pursue licensing under the idea

patents, CAFC extended the *Medimmune* holding in *SanDisk Corp. v. STMicroelectronics, Inc.* when it held that protracted licensing negotiations gave the prospective licensee the necessary standing to challenge the underlying patent's validity without even having to enter a licensing agreement with an NCE.[137] A similar effort was undertaken by USPTO when it introduced *inter partes* proceedings where any party may challenge a patent.[138]

In summary, it is apparent that, first, courts did not favor non-producers in their recent decisions; second, courts wanted to give licensee operating entities more freedom to seek legal redress against NCE tactics; and third, courts signaled that taking licenses from NCEs does not completely extinguish the rights of operating entities. It is logical for the courts to now focus on developing a principled approach to determining when anti-assignment clauses in intellectual property licensing agreements are invalid.

III. LEGAL THEORY

This Note proposes extending one of the traditionally available defenses to claims of patent infringement, the doctrine of patent misuse, to facilitate acquisition by a third-party of technology licensed from NCEs. The proposed mechanism for expanding this doctrine is a rule for invalidating anti-assignment provisions and covenants not to sell, which are typically present in intellectual property licensing agreements. The proposed rule addresses scenarios where, in a corporate restructuring (for example, M&A) transaction, the target's assets are encumbered by such licensing agreements. A synthesis of the concepts of patent unenforceability, patent misuse, and antitrust policy is used to arrive at the proposed analytical result.

The following sections will present the proposed rule and discuss a policy-based approach for reconciling the legal frameworks of pa-

that once they lock up the license, the licensee can't challenge the patent's validity. This takes some of the pressure off companies to investigate the validity before entering the contract, but licensors can still use provisions such as upfront license payment, forum selection clauses, licensor's right to attorney's fees from a successful defense of the patent.").

137. SanDisk Corp. v. STMicroelectronics, Inc., 480 F.3d 1372, 1383 (Fed. Cir. 2007) (holding that prospective licensee had standing to challenge the patent because "[the patent holder] has engaged in a course of conduct that shows a preparedness and willingness to enforce its patent" even in the absence of a direct threat to sue the prospective licensee for patent infringement).

138. MPEP, *supra* note 31, at § 2609 ("Any third party requester can request *inter partes* reexamination at any time during the period of enforceability of the patent . . . .").

tent, contract, and antitrust to the extent these theories inform the proposal for upholding alienability of patent licenses under the doctrine of patent misuse.

A. Summary of the Proposed Rule

As stated in *Princo v. Int'l Trade Comm.*,[139] patent misuse is an attempt to unduly extend the scope of the patent right in a manner that has anti-competitive effects and in the presence of a clearly identifiable patent at issue.[140] Mere "misuse in the air" is not sufficient.[141]

The rule proposed here supplements the *Princo* rule. The proposed rule can be summarized as follows: first, refusal by NCE-patentees to assign licenses to the licensee's business successors on the same terms constitutes patent misuse in light of the *Princo* rule because NCE licensing activity is an attempt to unduly extent the scope of a patent; and, second, case law establishes that patent misuse renders the underlying patent unenforceable as to the licensee or its business successor. As illustrated below, each analytical step in the proposed rule is informed by policy considerations and case law.

The proposed rule solves several problems. The rule focuses on patent unenforceability, providing a narrowly tailored solution. It is consistent with the principle, found in patent law, of avoiding disruptions to limited-term monopolies secured by patents[142] because the NCE is free to continue to receive royalties from the licensee's business successor. Also, the proposed rule is consistent with freedom of contract[143] because the underlying contract is not invalidated and because the proposed rule supplements rather than overrides contract interpretation principles and applies only to federally adjudicated issues of patent licenses.[144] Finally, the rule is mindful of the distinction between productive and non-productive entities insofar as such distinction relates to their competitor status, which is a principle rooted in antitrust policy.

139. Princo Corp. v. Int'l Trade Comm'n, 616 F.3d 1318 (Fed. Cir. 2010).

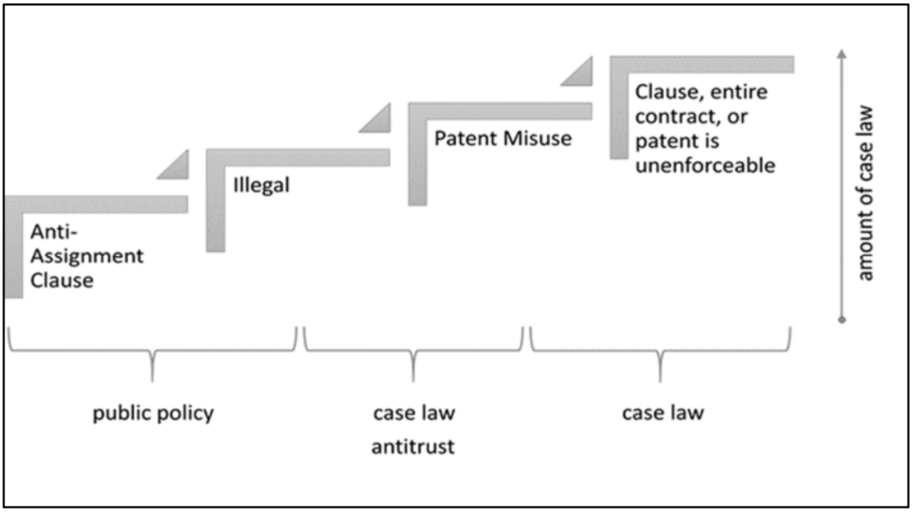
140. *Id.* at 1318–34.

141. *Id.* at 1329.

142. Aronson v. Quick Point Pencil Co., 440 U.S. 257, 262 (1979).

143. *See* W. Coast Hotel Co. v. Parrish, 300 U.S. 379 (1937).

144. Karen E. Sandrik, *Formal but Forgiving: A New Approach to Patent Assignments*, 66 RUTGERS L. REV. 299, 305 (2014).



B. The Princo Rule as a Starting Point

Patent misuse is an attempt to unduly extend the scope of the patent right in a manner that has anti-competitive effects and in the presence of a clearly identifiable patent at issue. Mere "misuse in the air" is not sufficient. We adopt this rule because it provides a clear roadmap and illuminates critical analytical components of interest with respect to NCE licensing activity: effect on the reach of the patent monopoly, non-producer status of NCEs, and focus on NCE activity after such entities procure patents.

C. Policy Considerations to Supplement the Princo Rule Analysis

1. Patent

In order to develop a viable solution to the problem of unduly restrictive licensing agreements, it is necessary to understand the policy objectives that underlie patent law. The doctrine of patent law is primarily concerned with, first, stimulating innovation; second, rewarding invention; and third, assuring that innovative ideas do not remain indefinitely in the private domain.[145]

Our proposal does not disrupt these objectives. Promoting alienability of patent licenses from licensee-operating entities to their business successors is consistent with the principles of patent law. The principle of discouraging patentees from retaining a long-time monopoly on their invention is not disrupted because, when a license is transferred to a business successor, such successor should be able to assume the original licensee's contractual obligations to the NCE.

Furthermore, invention is still rewarded because the NCE retains the ability to maintain its royalty stream from the business successor, but on the same terms as those of the original license, and the value of protecting inventive activity through patents is preserved because patent misuse is linked to the question of enforceability rather than validity of patents. Therefore, the proposal avoids disrupting the patent system because it does not invalidate the patent that underlies the license.

To understand NCE activity, it is further necessary to distinguish between the doctrines of patent law and real property law. In direct contrast with patent law, which seeks to harmonize the interests of the public with the interests of the individual, real property law is primarily concerned with an individual's right to exclude others.[146] Although recent scholarship attempted to refocus the property doctrine on relationships rather than boundaries, it is still arguably true that the focus in real property law remains on relationships between private parties,[147] whereas in patent law, the focus is on the relationship between the inventor and the public.[148] An important consequence of this distinction is that the grant of a patent is viewed as a bilateral contract between an individual and society, where a limited-term monopoly right is granted in exchange for disclosure.[149] At the same time, patent monopoly must serve a useful end, and NCEs do not further this objective because they do not practice their patents.

145. *Aronson*, 440 U.S. at 262.

146. Thomas W. Merrill, *Property and the Right to Exclude*, 77 NEB. L. REV. 730 (1998) (arguing that a right to exclude is a *sine qua non* in property law).

147. JOSEPH W. SINGER ET AL., PROPERTY LAW: RULES, POLICIES, AND PRACTICES 39 (Wolters Kluwer 6th ed. 2014) (legal rights as jural relations among people); Gregory S. Alexander, *Property as a Fundamental Constitutional Right? The German Example*, 88 CORNELL L. REV. 733, 748 (2003) (discussing the "social obligation" of ownership in German jurisprudence).

148. MERGES & DUFFY, *supra* note 29, at 627, n. 2.

149. 1 MOY'S WALKER ON PATENTS § 1:38 (4th ed.).

2. Contract

It is also important to be aware of the differences between the contract law doctrine and patent law while keeping in mind that the contract doctrine alone cannot be used to uphold license alienability because it protects freedom of contract and does not provide defenses to contract formation that would apply in the NCE licensing context.

The contract law doctrine, other than requiring that the parties conform with the principles of good faith and fair dealing,[150] seeks to protect the freedom of individuals to craft their own terms so as to maximize the private right to contract.[151] Contract law therefore offers very few mechanisms for rendering a contract unenforceable—namely, mistake, unconscionability, and duress.[152] When courts use the principles of contract law to adjudicate disputes in patent licensing, licensees cannot effectively rely on any of these doctrines to invalidate unduly restrictive non-assignment clauses.[153] These doctrines are often predicated on the imbalance of power between the licensor and the licensee,[154] and courts are unlikely to find a power inequity where both parties to a transaction are equally sophisticated business entities.[155]

Therefore, the licensees are left with the only viable option—challenging the validity of the patent itself. This option, however, is expensive to litigate, and, furthermore, court decisions wreak undue havoc on the patent industry. Instead, this Note proposes an approach that

150. RESTATEMENT (SECOND) OF CONTRACTS § 205 (1981). ("Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.")

151. *But see generally* W. Coast Hotel Co. v. Parrish, 300 U.S. 379 (1937) (freedom to contract is subject to restraints imposed by public policy unless the imposition of such restraints as against individuals is unconstitutional).

152. Lorelei Ritchie, *Reconciling Contract Doctrine with Intellectual Property Law: An Interdisciplinary Solution*, 25 SANTA CLARA COMPUTER & HIGH TECH. L.J. 105, 156 (2008-2009) (citing Sherwood v. Walker, 33 N.W. 919, 923 (Mich. 1887) (mistake); Austin Instrument, Inc. v. Loral Corp., 272 N.E.2d 533, 535 (N.Y. 1971) (duress); Wollums v. Horsley, 20 S.W. 781 (Ky. 1892) (unconscionability).

153. *See* Content Extraction & Transmission LLC v. Wells Fargo Bank, Nat. Ass'n, 779 F.3d 1343 (Fed. Cir. 2014) (attempts by NCE to license patents do not amount to extortion).

154. ROBERT E. SCOTT & JODY S. KRAUS, CONTRACT LAW AND THEORY 509 (LexisNexis, 4th ed. 2007) (contract law generally enforces only voluntary, informed agreements between mentally competent adults).

155. *Id.*; *see also* AT&T Mobility LLC v. Concepcion, 131 S. Ct. 1740, 1746 (2011) (deferring to state law to interpret unconscionability and noting that a finding of unconscionability required undue "oppression" or "surprise"); Agri-Mark, Inc. v. Niro, Inc., 233 F.Supp.2d 200, 212 (D. Mass. 2002) (a high contractual limitation on damages was not unconscionable because both parties were sophisticated business entities).

would allow the courts to invalidate unduly restrictive non-assignability clauses in patent licensing agreements.

As discussed above, a license is a contract governed by the principles of contract law.[156] However, standard defenses to contract formation, which allow a licensee to ask the court to invalidate an unduly restrictive license agreement, are unlikely to apply. For example, the unconscionability defense to contract, as articulated in *Seabrook*, relied on the facts that one party "(1) possessed superior legal knowledge and (2) a scarce commodity that [the other party needed], (3) knew [the other party] had not read or understood, nor (4) received legal counsel regarding (5) the legally technical terms in (6) the fine print of the [offending party's] (7) lengthy contract."[157] Clearly, a license agreement between two business entities is unlikely to have been formed under the conditions that meet these criteria and, in fact, non-assignability clauses, no-challenge clauses, and similar provisions are standard tools of the trade in crafting licensing agreements for both the contract and patent attorneys.[158]

3. Antitrust

To supplement the law of contracts, which alone does not provide mechanisms to support alienability of patent licenses to business successors, a viable analytical framework is needed that would allow the courts to correctly take into account the public-policy dimension of patent law. One such exemplary framework is antitrust-based.

Under antitrust law, "an illegal provision in a patent license will generally constitute patent misuse, which, as a matter of patent law, renders the patent unenforceable."[159] Also, and more significantly, the presence of an illegal provision in a licensing agreement may invalidate the agreement itself without invalidating the underlying patent.[160]

156. McCoy v. Mitsuboshi Cutlery, Inc., 67 F.3d 917, 920 (Fed. Cir. 1995) (citing Power Lift, Inc. v. Weatherford Nipple-Up Sys., Inc., 871 F.2d 1082, 1085 (Fed. Cir. 1989) ("A [patent] license agreement is a contract governed by ordinary principles of state contract law.")).

157. SCOTT & KRAUS, *supra* note 154, at 510 (summarizing the Seabrook unconscionability criteria).

158. *See* Ziff & Deming, *supra* note 6.

159. LOUIS ALTMAN & MALLA POLLACK, CALLMANN ON UNFAIR COMPETITION, TRADEMARKS AND MONOPOLIES § 4:56 (4th ed. 2010) (citing E. Venetian Blind Co. v. Acme Steel Co., 188 F.2d 247 (4th Cir. 1951)).

160. *Id.* (discussing Sanford Redmond, Inc. v. Mid-America Dairymen, Inc., No. 85 Civ. 4574, 1992 WL 57090 (S.D. N.Y. 1992), *aff'd,* 993 F.2d 1534 (2d Cir. 1993)).

Antitrust law seeks to level the playing field for producers with the ultimate goal of benefiting the public.[161] Therefore, as a matter of antitrust law, a business practice, which in itself may be lawful and appropriate from a business perspective, could be considered unlawful if it is part of an unlawful scheme.[162] Furthermore, the term "anti-competitive" is reserved for lawsuits that seek socially undesirable exclusion,[163] and it therefore fits well in a scenario where NCEs wield a disproportionate amount of power over other parties' economic transactions. Consider the hypothetical presented in the Introduction *supra*: the "patent troll" included in its agreement with the small inventor a term so restrictive that it effectively gave the "troll" undue control over the small inventor's ability to sell its motion-control mechanism, an invention only partially related to the "troll's" data transfer patent, to Medical Devices, Inc. The Israel-based company was therefore unable to enter the U.S. market.

The policy principles that underlie antitrust law are consistent with the Supreme Court's recent decisions, discussed in Part II, to limit the reach of NCEs by disfavoring non-producers in patent infringement disputes. For example, echoing the industry feedback in a 2012 congressional hearing on antitrust,[164] the International Trade Commission (ITC) recently introduced a pilot program to determine whether NCEs meet the domestic industry requirement needed to bring an infringement suit in the ITC administrative forum.[165]

Additionally, the ITC tightened the domestic industry requirement in a judicial decision requiring that NCEs, in addition to demonstrating

161. *See*, *e.g.*, Fed. Trade Comm'n v. Actavis, Inc., 133 S. Ct. 2223, 2232 (2013) (citing United States v. Line Material Co., 333 U.S. 287, 308-311 (1948)) ("[I]n Line Material . . . the Court held that the antitrust laws forbid a group of patentees, each owning one or more patents, to cross-license each other, and, in doing so, to insist that each licensee maintain retail prices set collectively by the patent holders.").

162. The licensee and its successor are also subject to antitrust regulation. *See* INTELLECTUAL PROPERTY ASSETS, *supra* note 19, at § 16.4. However, it is unlikely that the licensee, typically a small entity, and its business successor would be direct competitors "in the absence of the licensing arrangement." *See* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY § 5.7 (1995), http://www.justice.gov/atr/public/guidelines/0558.htm#t57 [hereinafter DOJ AND FTC IP ANTITRUST GUIDELINES].

163. Michael J. Meurer, *Controlling Opportunistic and Anti-Competitive Intellectual Property Litigation*, 44 B.C. L. REV. 509, 521 (2003).

164. Ryan Davis, *'Patent Troll' Suits Face New Obstacles at the ITC*, LAW360 (Feb. 11, 2014, 7:21 PM), http://www.law360.com/articles/509094/patent-troll-suits-face-new-obstacles-at-itc.

165. *Id.*

a patent, show that at least one product practicing the patent exists.[166] Although this decision is not binding on federal courts, it is significant in two respects. First, it recognizes that the constructive enablement standard, which allows patents in the absence of practicing products, may result in patent enforcement for monetary gain rather than to promote competition. Second, the ITC decision finds a way to restrict NCE activity in a way that is not disruptive to the patent system, by limiting standing rather than seeking to change the enablement standard in patent law.

Similar to patent and contract law, the antitrust doctrine alone is not sufficient to support license alienability because it does not provide all the necessary doctrinal mechanisms for doing so. In the context of patents, one applicable antitrust provision is the anti-monopolization provision articulated in Section 2 of the Sherman Act.[167] However, in order to show that a practice is anti-competitive under the Sherman Act, a patentee must have fraudulently procured its patent.[168] Additionally, to prevail in a Section 2 argument under, for example, the essential facilities doctrine,[169] both parties must be competitors.[170] Neither is necessarily the case with NCEs.

Notwithstanding the foregoing, then, the antitrust-based approach recognizes that NCEs, as non-competitors, should enjoy a narrower field of opportunities to bring infringement suits and shows that it is possible to implement judicial rules that accomplish this policy objective without disrupting the law of patentability.[171] These two principles inform the argument for license alienability.

166. *Id.*

167. 15 U.S.C.A. § 2 (West 2004).

168. Fed. Trade Comm'n v. Actavis, Inc., 133 S. Ct. 2223, 2231 (2013) (citing Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp., 382 U.S. 172, 174 (1965) ("[E]nforcement of a patent procured by fraud may violate the Sherman Act") (internal citations omitted).

169. Abbott B. Lipsky, Jr. & J. Gregory Sidak, *Essential Facilities*, 51 STAN. L. REV. 1187, 1190–91 (1999) ("A monopolist in control of a facility essential to other competitors must provide reasonable access to that facility if it is feasible to do so"); *see generally* Elaine Johnston, *Intellectual Property as an 'Essential Facility'*, PRACTISING LAW INST. (2004), http://jp.whitecase.com/files/Publication/c93f2d08-b2c5-492c-804b-bd5dc51f74ed/Presentation/PublicationAttachment/15b3c953-2983-4ede-a055-c17043b5c00d/00817_Elaine_Johnston_byline.pdf (discussing limited applicability of the essential facilities doctrine to intellectual property).

170. *See, e.g.*, Kobe, Inc. v. Dempsey Pump Co., 198 F.2d 416 (10th Cir.), *cert. denied*, 344 U.S. 837 (1952).

171. Actavis Inc., 133 S. Ct. 2223, 2231 (holding that a pharmaceutical substance patentee's attempt to set higher-than-average licensing fees in a settlement agreement with competitor was not immune from antitrust scrutiny, even if the agreement's anticompetitive effects fell within the scope of the exclusionary potential of the patent).

IV. ARGUING LICENSE ALIENABILITY

A. Restraints on Alienability as Patent Misuse in Light of Case Law

This section reconciles the proposed rule with case law, presents an additional doctrine (shop right) to supplement the *Princo* rule analysis, and discusses procedural aspects of litigating alienability of patent licenses to business successors of the licensee.

1. NCE Activity as an Anti-Competitive Practice under the Princo Rule

Attempts by non-creative entities to exclude business successors of a licensee by enforcing anti-assignment clauses run counter to the principle of patent misuse, which seeks to protect market participants from anti-competitive actions by third parties. The doctrine of patent misuse applies when an improper attempt exists on the part of the patent holder to extend the scope of the patent, and such attempts are especially likely to be considered improper if they contravene antitrust law.[172] Because patent grants create monopolies, the misuse doctrine is intended to check the temptation to manipulate the intellectual property system to ends that it was never intended to serve.[173] In the licensing context, conduct that has been challenged as patent misuse includes tying arrangements,[174] territorial, field-of-use, and customer restrictions,[175] grantbacks that are broader in scope than improvements to the licensed patents,[176] and bad-faith enforcement of intellectual property rights.[177]

A typical anti-assignment clause in a patent license will prohibit the right or power to assign the contract to third parties.[178] Therefore, of particular interest here is the application by courts of the doctrine of patent misuse in the context of contracts that attempt to unduly exceed the scope of the patent right.

172. AM. BAR. ASSOC., SECTION OF ANTITRUST LAW, INTELLECTUAL PROPERTY MISUSE: LICENSING AND LITIGATION 1, at 1 (2000) [hereinafter INTELLECTUAL PROPERTY MISUSE].

173. *Id*. at 127–28.

174. *Id*. at 75.

175. *Id*. at 82–84.

176. *Id*. at 86–87.

177. *Id*. at 66.

178. Jessica L. Braeger, *Antiassignment Clauses, Mergers, and the Myth About Federal Preemption of Application of State Contract Law to Patent License Agreements*, 50 DRAKE L. REV. 639, 642 (2002).

CAFC, in *Princo*, held that attempts to impose conditions on a licensee that exceed the scope of the patent right constitute patent misuse.[179] CAFC also noted that, if patent misuse is established on public policy grounds, the underlying contract is rendered unenforceable.[180]

At the same time, however, courts have also upheld non-assignability clauses and refused to recognize NCE licensing arrangements as anti-competitive. For example, in *In Re CFLC* the Ninth Circuit held that a patent holder had an exclusive right to prevent such an assignment,[181] and the United States District Court for the Eastern District, in an unpublished opinion, refused to recognize NCE patent infringement allegations as patent misuse.[182] Additionally, CAFC, in *Sanofi-Aventis v. Apotex, Inc.*, has recently held that the defense of patent misuse is not available to a presumptive infringer simply because a patentee engages in some kind of wrongful commercial conduct, even conduct that may have anticompetitive effects.[183]

Notwithstanding these recent decisions, the proposal that anti-assignment clauses in NCE licensing contracts constitute patent misuse under the *Princo* rule is not inconsistent with case law. The *In Re CFLC* decision, for example, pertained to a situation where the licensee declared bankruptcy, and, in this scenario, it was appropriate to resolve the conflict between the patent holder and the licensee's successor in favor of the patent holder because the patent holder was in a better position than the licensee's debtor to use the patent license in a productive fashion.

In *Sanofi-Aventis*, the parties were competitors disputing the extent to which statutorily permissible[184] manufacture and sales of generic medication constituted infringement. Further, the court

179. Princo Corp. v. Int'l Trade Comm'n, 616 F.3d 1318, 1318–30 (Fed. Cir. 2010).

180. *Id*. at 1328 ("When [] contractual conditions violate public policy, however, as in the case of price-fixing conditions and tying restraints, the underlying patents become unenforceable, and the patentee loses its right to sue for infringement or breach of contract."); *accord.*, Lexmark Int'l, Inc. v. Ink Techs. Printer Supplies, LLC, No. 1:10-CV-564, 2014 WL 1276133, at *6 (S.D. Ohio Mar. 27, 2014).

181. In re CFLC, Inc., 89 F.3d 673, 680 (9th Cir. 1996) ("Because federal law governs the assignability of nonexclusive patent licenses, and because federal law makes such licenses personal and assignable only with the consent of the licensor, the . . . license is not assumable and assignable in bankruptcy . . . .").

182. Intell. Ventures I LLC v. Capital One Fin. Corp., No. 1:13-CV-00740, 2013 WL 6682981 (E.D. Va. Dec. 18, 2013).

183. Sanofi-Aventis v. Apotex, Inc., 659 F.3d 1171, 1182 (Fed. Cir. 2011).

184. 21 U.S.C.A. § 355 (West 2013) (the Hatch-Waxman Act).

distinguished *Princo*, noting that wrongful commercial conduct at issue was a failure to comply with notice requirements rather than attempts to unduly enlarge the scope of the patented invention.[185]

2. Linking License Alienability with Patent Misuse though the Shop Right Doctrine

The shop right doctrine presents an additional mechanism to argue that NCE restrictions on license alienability to licensee's business successors constitute patent misuse. This doctrine supports both the *Princo* rule and license alienability, and further underscores the importance of considering the licensee and its successors' ability to productively use a patent.

The first prong of the *Princo* rule posits that unduly extending patent scope constitutes patent misuse.[186] This Note argues that restrictions on license assignments to business successors in effect unduly extend the reach of an NCE patent, and this proposal finds support in the doctrine of shop right, rooted in patent law. Although a shop right confers on the licensee the right to practice a patent but not to assign it,[187] courts have made an exception to this rule when there is "a complete succession of the entire business and good will of [the licensee]".[188]

Policy principles underlying license alienability are discussed, for example, in *Speedplay, Inc. v. Beebop, Inc.*, where CAFC noted, in *dictum*, that a patent owner does not hold an absolute right to withhold permission to the licensee to assign the license to a third party.[189] The court interpreted the parties' licensing agreement, which stipulated that the right to assign shall not be withheld "unreasonably," to mean that the only reasonable basis for prohibiting assignment of the license would be an impediment to the owner's consideration for entering the original agreement.[190] Such consideration, as determined

185. *Sanofi-Aventis*, 659 F.3d at 1182 ("'[T]he key inquiry under the patent misuse doctrine is whether . . . the patentee has impermissibly broadened the physical or temporal scope of the patent grant and has done so in a manner that has anticompetitive effects.' BMS's failure to disclose the oral side deal with Apotex, and its false certification to the FTC regarding the same, in no way broadened the scope of the 265 patent grant." (quoting Princo Corp. v. Int'l Trade Comm'n, 616 F.3d 1318, 1328 (Fed. Cir. 2000)).

186. *Princo*, 616 F.3d at 1318–30.

187. Ushakoff v. United States, 179 Ct. Cl. 780 (Ct. Cl. 1967).

188. Neon Signal Devices v. Alpha-Claude Neon Corp., 54 F.2d 793, 796 (W.D. Pa. 1931).

189. Speedplay, Inc. v. Bepop, Inc., 211 F.3d 1245, 1251–52 (Fed. Cir. 2000).

190. *Id.*

by the court, consisted largely of protecting the owner's ongoing royalty stream.[191]

If we apply the reasoning articulated in *Speedplay* to the hypothetical scenario discussed in the Introduction, where the licensee, Small Inventor, Inc., unsuccessfully attempted to transfer its license rights to a business successor, Medical Devices, Inc., it becomes clear that permitting the licensee to assign its contract, presumably on the same terms, would not adversely impact the patent owner's royalty revenues. Any other conclusion would effectively afford the patent owner a benefit not commensurate with the scope of the patent at issue by allowing the owner to exercise undue influence over the licensee's business decisions. Such an outcome would constitute patent misuse as defined by CAFC in *Princo*.[192]

The second prong of the *Princo* rule states that misuse in the air is not sufficient.[193] Similar to the Ninth Circuit, the District Court for the Eastern District, in *Intellectual Ventures*, refused to uphold the doctrine of patent misuse as a defense to allegations of bad-faith patent enforcement because the attempted licensor, an NCE, attempted to enforce a portfolio of patents. The prospective licensee pointed to this activity in the aggregate rather than to any specific patent to support its allegations of bad-faith enforcement, and at issue was the appropriateness of claiming patent misuse by the attempted licensee before a license was finalized.[194] The court, citing a long line of precedent, noted that allegations of "misuse in the air" were not sufficient.[195]

The facts, however, are radically different when an established licensor-licensee relationship exists. Because there was not a clearly identifiable patent in *Intellectual Ventures*, the court concluded that the prospective licensor had not demanded from the prospective licensee any "concessions beyond the monopoly power created by an enforceable patent,"[196] which, as discussed above, is not the case when an unqualified right to withhold an assignment to a business

191. *Id.*

192. Princo Corp. v. Int'l Trade Comm'n, 616 F.3d 1318, 1318–30 (Fed. Cir. 2010).

193. *Id.* at 1329.

194. Intell. Ventures I LLC v. Capital One Fin. Corp., No. 1:13-CV-00740, 2013 WL 6682981, at *9 (E.D. Va. Dec. 18, 2013) ("Ulterior or bad motives do not deprive a patent holder of its right to enforce a patent; and a patent misuse defense cannot be based on 'misuse in the air.' Rather, '[t]he misuse must be of the patent in suit.'").

195. *Id.*

196. *Id.* at *10.

successor would effectively exceed the scope of such monopoly power.

B. Procedural Aspects of Arguing Illegality of Anti-Assignment Clauses through Patent Misuse

1. Timing[197]

This Note proposes expanding the doctrine of patent misuse to support claims that anti-assignment clauses in patent licenses, when the licensor is an NCE, may be unduly restrictive because they exceed the scope of the patent. The first question with respect to procedural aspects of bringing such claims is the question of timing, and, inasmuch as timing affects ownership of the disputed license, the related question is who can bring an action.

Complaints seeking to invalidate restrictions on assignment could be brought before or after infringement is alleged.[198] If brought pre-infringement, the licensee or its successor could seek a declaratory judgment invalidating the restrictive clause in the licensing agreement.

If brought post-infringement, the licensee or its successor could bring a counter-claim seeking to invalidate the clause or, in the alternative, supplement its defense of patent unenforceability.[199]

Additionally, the licensee or its successor could bring such claims or counter-claims either before or after the change-of-control transaction occurs. As such, the analytical framework proposed here does not impose restrictions on either timing or the parties in suit.

2. Jurisdiction and Choice of Law

The second question related to procedure is jurisdiction and choice of law. The issue of alienability of patent licenses should be litigated in federal courts, similar to other patent-related disputes, and, notably, this approach does not conflict with existing jurisdictional law

197. For an in-depth discussion *see* Andrew Schwerin, *Declaratory Judgment Suits Against Patent Trolls*, RIIPL INST. FOR INFO. POLICY & LAW (2014), http://riipl.rutgers.edu/andrew-schwerin-declaratory-judgment-suits-against-patent-trolls/.

198. *See* Jennifer R. Saionz, *Declaratory Judgment Actions in Patent Cases: The Federal Circuit's Response to Medimmune v. Genentech*, 23 BERKELEY TECH. L.J. 161 (2008) (discussing the "reasonable apprehension" standard relaxed in light of *MedImmune*'s "totality of the circumstances" test).

199. *Id.* at 189.

in either contracts or patents. While state contract law governs interpretation of patent licenses,[200] federal patent law controls on the issue of license alienability in order to promote innovation and because the analysis of license alienability issues is rooted in the law of intellectual property rights.[201] CAFC successfully harmonized state contract law with the law of patents.[202]

Additionally, federal courts have jurisdiction over counter-claims or defenses to infringement.[203] As to the choice of law, interpretation of the contract language as to the extent to which assignability is restricted and determining whether a change-of-ownership transaction occurred would be a matter of state law,[204] whether contractually stipulated or not, and arguments related to establishing patent misuse on the ground of the presence of an anti-assignment clause in the license agreement could be interpreted under federal law of patents.[205]

V. RESPONSE TO COUNTERARGUMENTS

Likely counterarguments to the proposal advanced in this Note include the following: first, NCE activity should not be limited because NCEs are valuable market players that provide much-needed liquidity in the market of intellectual property rights; second, patent misuse has already been unsuccessfully argued in the context of NCE licensing; third, the proposal may adversely affect non-practicing entities that add value, such as universities; and fourth, the proposal may run counter to the well-established principle of freedom of contract. These counterarguments are addressed below.

200. Cincom Sys., Inc. v. Novelis Corp., 581 F.3d 431, 437 (6th Cir. 2009) (noting that "state contract law will govern the interpretation of a license because a license is merely a type of contract.").

201. *Id.*, *see also* In re CFLC, Inc., 89 F.3d 673, 679 (9th Cir. 1996) (federal law must govern to prevent free assignability and to promote creativity); In re Alltech Plastics, Inc., 71 B.R. 686, 689 (Bankr. W.D. Tenn. 1987) ("Because '[t]he rights of the patent owner to license the use of his invention is [sic] a creature of federal common law False [i]t follows that questions regarding the assignability of patent licenses are controlled by federal law'") (internal citations omitted).

202. Karen E. Sandrik, *Formal but Forgiving: A New Approach to Patent Assignments*, 66 RUTGERS L. REV. 299, 305 (2014).

203. 28 U.S.C.A. § 1338 (West 2011).

204. *See, e.g.,* Gunn v. Minton, 133 S. Ct. 1059, 1061 (2013) (refusing to interpret a legal malpractice claim, a matter of state law, under federal patent law because the federal issue needed to be "necessary for resolution," "actually disputed," "substantial," and consistent with public policy); *see also* Ziff & Deming, *supra* note 50, at 3.

205. Princo Corp. v. Int'l Trade Comm'n, 616 F.3d 1318 (Fed. Cir. 2010) (noting, however, a narrow application of misuse to limit patent scope because 28 U.S.C. § 1338 misuse is a judicially created doctrine); *but see Gunn*, 133 S. Ct. at 1061.

A. NCEs As Market Intermediaries

Opponents of limiting NCE activity argue that NCEs provide market liquidity.[206] For example, one study, commissioned by the Federal Trade Commission, found that non-creative entities account for 75% of all activity in patent licensing markets.[207] The same study, however, found that less than 25% of this licensing activity leads to innovation in industries that heavily rely on intellectual property.[208]

In other words, it is questionable whether the increased transaction costs associated with procuring, managing and litigating patents are justified by patent commercialization facilitated by NCEs. Market intermediaries play an important role in facilitating property exchange but, as noted *supra*, the anticompetitive effects of such economic activity must not exceed the aggregate benefits that market intermediaries provide to the economy.[209] Market disintermediation benefits both producers[210] and consumers.[211]

The largest technology companies clearly view NCEs as a problem rather than as facilitators of commercial activity, as indicated by recent efforts of these companies to avoid infringement litigation by NCEs by entering alternative licensing arrangements with other operating entities that practice the patents they own. Defensive patent aggregators and cross-licensing arrangements are examples of these efforts.[212]

Technology companies form alliances to jointly purchase patents from smaller inventors, thereby taking these patents off the market so as to prevent NCEs from acquiring and enforcing them. Technology

206. *See generally* Hannibal Travis, *Patent Alienability and Its Discontents*, 17 TUL. J. TECH. & INTELL. PROP. 109 (2014).

207. Mark S. Popofsky & Michael D. Laufert, *Patent Assertion Entities and Antitrust: Operating Company Patent Transfers*, 12 AM. BAR. ASSOC.: THE ANTITRUST SOURCE 1, 2 (2013).

208. *Id.*

209. DOJ AND FTC IP ANTITRUST GUIDELINES, *supra* note 161, at § 3.4 ("The Agencies' general approach in analyzing a licensing restraint under the rule of reason is to inquire whether the restraint is likely to have anticompetitive effects and, if so, whether the restraint is reasonably necessary to achieve procompetitive benefits that outweigh those anticompetitive effects. . . .).

210. ERIC J. ARNOULD ET AL., MARKET DISINTERMEDIATION AND PRODUCER VALUE CAPTURE: THE CASE OF FAIR TRADE COFFEE IN NICARAGUA, PERU AND GUATEMALA 4 (2006), http://digitalcommons.unl.edu/marketingfacpub/11.

211. *Case Study: Dell—Distribution and Supply Chain Innovation*, MARS (2011), http://www.marsdd.com/mars-library/case-study-dell-distribution-and-supply-chain-innovation/.

212. Martha Belcher & John Casey, *Hacking the Patent System: A Guide to Alternative Patent System for Innovators* 3-5, ELEC. FRONTIER FOUND. (May 2014), https://www.eff.org/files/2014/05/29/hacking_the_patent_system.pdf.

companies also form alliances aimed at creating common pools of patents.

Once such initiative is Google's License on Transfer (LOT) program, which aims to reduce the number of patents available to NCEs.[213] Under this program, participants agree to license, royalty-free, their patent portfolios to each other, but agree that licenses will become enforceable only if a participant decides to transfer its patent portfolio to an NCE. Thus, participants intentionally encumber their intellectual property title with licenses to other operating entities, receiving, in exchange, an assurance that in the event some of these patents are transferred to NCEs, the risk of infringement litigation by NCEs against other LOT participants will dissipate because the patents will already have been licensed to these participants.[214] In summary, technology companies aim to reduce the number of enforceable patents available to NCEs, thereby reducing liquidity, which shows that these companies see NCE activity as costly rather than beneficial to the industry.[215]

Notably, the LOT licensing agreement includes an exception stipulating that licenses transferred to participants' business successors rather than NCEs remain unenforceable as against other participants. Specifically, as articulated by Google, Inc.,

> "[t]here are two principal exceptions where the transfer of patents will not trigger a license under the LOT Agreement. The first is a transfer of patents to another current LOT Network participant. *The second is a transfer that is part of a legitimate M&A or spin-out activity. . . . These exceptions allow companies sufficient room to utilize and dispose of their intellectual property in ways that maintain value to support the growth and performance of their business*, while giving active participants a royalty-free license to protect them from patent sales to non-participants, e.g., PAEs." (emphasis added).[216]

213. *Id*.

214. LOTNET, http://www.lotnet.com/lotnet-solution/index.cfm (last visited Aug. 9, 2015).

215. *Id*. at http://www.lotnet.com/patent-assertion-problem/index.cfm ("The balance of revenue obtained by operating companies versus costs expended to defend against [NCEs] is orders of magnitude in favor of costs.").

216. *Id*.; *see also LOT Agreement*, LOTNET (July 7, 2014), http://www.lotnet.com/userfiles/files/LOT%20Agreement%20(v1_3-7_7_14).pdf.

Consistent with the proposal advanced in this Note, the LOT agreement defines business successors as entities that assume ownership of a participant's patents as a result of mergers, change-of-control transactions, and spin-offs.

In the event the successor chooses not to become a member of the LOT network within six months, the licenses simply expire. This provision is fully in accord with the proposal advanced in this Note in two ways: first, the industry views title encumbrances as harmful, rather than beneficial, to operating entities, and, second, the industry supports the free choice of successor companies to continue or terminate the cross-licensing arrangement, with an apparent goal of minimizing the impact of title encumbrances on change-of-control negotiations and thus preserving the value of patents at issue.

B. B&N v. MOSAID, Inc. As Distinguishable Legal Precedent

Patent misuse has already been unsuccessfully argued in the context of NCE licensing. Barnes & Noble (B&N), a licensee of Google, Inc.'s Android™ operating system used in computer tablet technology, recently accused MOSAID, Inc., a patent aggregation alliance (an NCE) formed by Microsoft, Inc. and Nokia, Inc., of patent misuse. The alleged goal was to make Android™, and consequently B&N tablet computers, prohibitively expensive, and thus perpetuate Microsoft's dominance in PC operating systems.[217] After several rounds of unsuccessful licensing negotiations, Microsoft, Inc. brought suit, alleging that B&N infringed its patents.[218] B&N brought a counterclaim with the ITC alleging patent misuse as an affirmative defense to infringement.[219] The ITC court did not find patent misuse.[220]

The proposal advanced in this Note is not inconsistent with the court's reasoning. Notably, the court relied on the *Princo* rule stating that, first, misuse must be related to specific patents, and, second, the goal of the licensing activity must have been intended to broaden the scope of the patent.[221] The court found that B&N failed to identify particular patents in controversy because Microsoft had attempted to

217. *In re* Certain Handheld Elec. Computing Devices, Related Software, & Components Thereof, Inv. No. 337-TA-769, USITC Order No. 32 (Jan. 31, 2012) (order granting motion for summary determination).

218. *Id.*

219. *Id.*

220. *Id.*

221. *Id.*

license a portfolio without identifying each individual patent.[222] This situation is drastically different from the scenario addressed in this Note, where a licensing agreement would already exist and, thus, the patent at issue would be clearly identifiable. Thus, a complaint or defense brought by the licensee would not fail the patent-in-suit prong[223] of the *Princo* test.

Further, CAFC noted that B&N did not meet the second prong of the *Princo* test—undue extensions of scope of the patent.[224] First, the court stated that, in light of case law,[225] Microsoft's attempt to extract high royalties was permissible because the doctrine of patent monopoly does not impose a ceiling on royalties.[226] In the license assignability scenario, however, the monetary value of royalties due to the NCE would not be at issue. Rather, the proposal simply attempts to remove the barriers to the freedom of operation of the licensees and their successors. In fact, limiting NCE ability to negotiate with licensee successors would protect the NCE's position—because one version of the proposal articulated in this Note would invalidate the anti-assignability clause rather than the entire licensing agreement, the NCE could continue receiving royalties from its licensee's successor on the same terms as before.[227]

Second, the ITC court in *MOSAID* noted that Microsoft did not unduly expand the breadth of scope of its patents when it attempted to impose field-of-use restrictions on B&N by limiting operating system versions and upgrades.[228] In contrast, field-of-use restrictions are not at issue in regards to the licensor-licensee relationship.

222. *Id/*

223. *Id*.

224. *Id*.

225. *Id*. ("A patent empowers the owner to extract royalties as high as he can negotiate with the leverage of that monopoly." *Brulotte v. Thys Co.,* 379 U.S. 29, 33 (1964). Indeed, the patent laws even permit unilateral refusals to license patents. *See SCM Corp. v. Xerox Corp.*, 645 F.2d 1195, 1204 (2d Cir. 1981); *see also* 35 U.S.C. § 271(d)(4). Accordingly, this is not misuse.")

226. *Id.* However, note that CAFC denounced the 25% rule. Uniloc USA, Inc. v. Microsoft Corp., 632 F.3d 1292, 1315 (Fed. Cir. 2011) ("This court now holds as a matter of Federal Circuit law that the 25 percent rule of thumb is a fundamentally flawed tool for determining a baseline royalty rate in a hypothetical negotiation.").
Also, Fed. Trade Comm'n v. Actavis, Inc., 133 S. Ct. 2223, 2231 (2013) created a multi-factor analysis to follow under § 271(d)(4).

227. This would have passed the test articulated in *Actavis*. *See* Fed. Trade Comm'n. v. Actavis, Inc., 133 S. Ct. 2223, 2231.

228. *In re* Certain Handheld Elec. Computing Devices, Related Software, & Components Thereof, Inv. No. 337-TA-769, USITC Order No. 32 (Jan. 31, 2012) (order granting motion for summary determination).

Field-of-use restrictions arise when both parties to the agreement practice the technology covered by the patent at issue or when one practicing entity attempts to use its patents as a sword through an NCE.[229] Because NCEs do not practice their patents, the first scenario involving two competitors in a licensor-licensee relationship is not within the scope of this proposal, and, with respect to the second scenario, a distinct advantage of the proposal as articulated in this Note is that there is not a need to examine the provenance of the NCE to determine whether it was created by the licensee's competitor. The restriction at issue is the anti-assignability provision rather than a field-of-use limitation, and our proposal borrows from the antitrust framework to extend the doctrine of patent misuse rather than rely on the antitrust doctrine exclusively as was done by B&N.[230]

In summary, the B&N argument in *MOSAID* required a showing of patent misuse to prove an antitrust violation by a competitor, and the court was understandably reluctant to make a policy decision on whether it was allowable for practicing entities to use patents against competitors.[231] The scope of the issue presented in this Note, in contrast, is much narrower and aims to encourage corporate investment in innovation by making it easier for companies to acquire potentially profitable resources. To that end, field-of-use issues would not be raised, and the licensee's argument for assignability would not fail the second prong of the *Princo* test.

C. Effect on Non-Practicing but Value-Adding Entities

Proponents of the free-market approach to regulating NCEs argue that any restrictions on NCE activity will adversely impact non-practicing entities that add value—for example, universities.[232] In-

229. *See Intellectual Property Misuse*, *supra* note 172.

230. Certain Handheld Elec. Computing Devices, Related Software, & Components Thereof, Order No. 32, USITC Inv. No. 337-TA-769 (Jan. 31, 2012) (order granting motion for summary determination).

231. For an examination of possible arguments to support the assertion that transfers of IP assets to NCEs may violate antitrust laws, *see* POPOFSKY & LAUFERT, *supra* note 207.

232. Dennis S. Corgill, *Competitive Injury and Non-Exclusive Patent Licensees*, 71 U. PITT. L. REV. 641, 642–43 (2010). ("Consider, for example, a university that owns a patent on a medical device invented by one of its professors. The university may choose not to practice the invention itself for the simple reason that the university does not have the requisite manufacturing facilities or distribution channels.").

deed, universities are in a position to conceive of inventions and reduce them to practice without commercializing them. Instead, they may assign or license their patents to private-industry entities.[233]

This proposal, however, would not negatively impact productive non-practicing entities for several reasons. First, a key strength of the proposal is its focus on contracting activity between NCEs and practicing entities rather than on patent validity. A targeted solution for curtailing NCE activity eliminates the need to invalidate the entire patent held by the NCE: as explained above, the argument that restrictions on assignability are illegal can be raised outside the context of raising patent misuse as a defense to effectuate patent invalidity in infringement litigation. This can be done in two ways: first, the licensee may seek a declaratory judgment pertaining only to its contract with the NCE and not to the underlying patent.[234] Second, patent misuse supports unenforceability rather than patent invalidity.[235]

As a result, the outcome of the analytical process proposed here would have no impact on the legal status of non-creative entities or on the requirements for patentability. Non-creative entities, including universities, could continue to operate without the need to show evidence of use in order to obtain or retain rights to a patent.

Arguably, making it more difficult for NCEs to control transferability of licenses to their patents could make these entities unwilling to procure patents from universities.[236] However, it is unclear whether "patent trolls" are big purchasers of university patents, especially in light of the fact that university research projects are funded by private industry and government,[237] which increases the likelihood that these entities will become owners of the patents resulting from such research, either by contract or statutorily,[238] which, in turn, will create

233. *Id.* ("That leaves the university with the option of licensing. Depending upon a variety of economic circumstances, the university may opt for non-exclusive licensees. For example, the university may not want a single, exclusive licensee to obtain monopoly power, which would permit the exclusive licensee to raise price and restrict output. Instead, the university may prefer a system of non-exclusive licensees who will compete on price and expand output.").

234. 28 U.S.C.A. § 2201 (West 2010).

235. 35 U.S.C.A. § 282(b)(1) (West 2012).

236. *See* Hannibal Travis, *supra* note 206.

237. ASSOC. OF AM. UNIVS., UNIVERSITY RESEARCH: THE ROLE OF FEDERAL FUNDING (Jan. 2011), http://www.aau.edu/WorkArea/DownloadAsset.aspx?id=11588 [hereinafter AMERICAN UNIVERSITIES].

238. 35 U.S.C.A. § 202(c)(4) (The university may elect to retain rights, provided that it timely files a patent. However, "with respect to any invention in which the [funded party] elects rights, the Federal agency shall have a nonexclusive, nontransferable, irrevocable, paid-up license to

title encumbrances that would make such purchases unattractive for "patent trolls". In fact, 60% of university research spending comes from federal funding.[239]

D. Freedom of Contract

Another potential counterargument is rooted in the principle of freedom of contract, which stipulates that private entities should be free to enter contracts without judicial or government interference.[240] The proposal articulated in this Note, however, is not contrary to this principle. NCE licensing contracts cannot be considered contracts of adhesion,[241] which are subject to invalidity under the doctrine of unconscionability, because both the NCE and its licensee are likely business entities sophisticated enough to bargain over the terms of the contract.

An argument could be made, however, that licensees are not free to refuse to enter licensing agreements because they would otherwise be subject to infringement actions. For example, an accused infringer recently brought a counter-claim of extortion, which was rejected by CAFC in *Content Extraction & Transmission LLC v. Wells Fargo Bank* on the ground that the patent owner's filing of an infringement lawsuit did not rise to the level of extortion sufficient to support an extortion claim.[242] At the same time, the law of patents is firmly rooted in the doctrines of patent monopoly and market choice, and neither of these doctrines provides mechanisms for prospective licensees to reject restrictions on license assignment to third parties in license negotiations. Therefore, a narrowly tailored judicial solution articulated in this Note could fill the gaps by helping licensees challenge restrictions on assignment without disrupting the patent system and without disrupting freedom of contract; the proposal does not seek to invalidate entire license agreements.

practice or have practiced for or on behalf of the United States any subject invention throughout the world.").

239. *See* AMERICAN UNIVERSITIES, *supra* note 237 ("In 2009, [the federal government supported] about $33 billion of universities' total annual R&D spending of $55 billion").

240. W. Coast Hotel Co. v. Parrish, 300 U.S. 379 (1937).

241. Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1173, 1176–77 (1983) (a contract of adhesion is standard form contract presented on a take-it-or-leave-it basis).

242. Content Extraction and Transmission LLC v. Wells Fargo Bank, Nat. Ass'n, 776 F.3d 1343, 1351 n.2 (Fed. Cir. 2014) ("Treating meritless litigation as form of extortion punishable under RICO would substantially chill even valid court petitioning . . . ." (citing Deck v. Engineered Laminates, 349 F.3d 1253, 1258 (10th Cir. 2003)).

Another counterargument is potential liability for tortious interference with contractual relations.[243] When a corporate transfer occurs by operation of law or despite the license holder's objections, the business successor would not be held liable. Tortious interference, importantly, requires a deprivation of the contract holder of its consideration.[244] In this case, no such deprivation would occur because the NCE would be free to agree to continue receiving royalties from the business successor on the same terms. The NCE's position, therefore, would not be compromised. In a similar vein, no disruption of a business relationship[245] would occur because the successor would be free to assume the licensee's contract and because the licensee is unlikely to enter a contract that reduces rather than increases revenues from practicing the invention.

In addition, the proposal articulated in this Note would not disrupt the existing jurisdictional framework. Although contract issues are a matter of state law,[246] it is not inconceivable that licensees may seek redress in federal courts that have jurisdiction over patent matters. In fact, federal courts, in adjudicating these disputes, could apply contractually agreed upon choice-of-law provisions[247] stipulated by the NCE and the licensee or its successor.

CONCLUSION

Non-creative entities contribute to rising costs of innovation by contractually requiring their licensees to seek NCE consent to subsequent license transfers. However, while courts are working to develop solutions to address this problem, drastic changes to the patent system are not desirable. One possible way of gradually limiting the reach of NCEs is to expand the doctrine of patent misuse, which supports the unenforceability defense to patent infringement, to construe restraints on alienation of patent licenses as patent misuse under the *Princo*[248] rule. This approach is consistent with substantive and procedural requirements of both federal patent law and state contract law. Additionally, it is consistent with the case law on the treatment of

243. PROSSER AND KEETON ON TORTS 978 (W. Page Keeton et al. eds., 5th ed. 1984).

244. *Id.* at 989 (the defendant must cause the interference and the resulting loss).

245. *See*, *e.g.*, McGreevy v. Daktronics, Inc., 156 F.3d 837 (8th Cir. 1998) (interference with business relations).

246. Cincom Sys., Inc. v. Novelis Corp., 581 F.3d 431, 437 (6th Cir. 2009).

247. SOFTWARE CONTRACTS, *supra* note 87, at 87.

248. Princo Corp. v. Int'l Trade Comm'n, 616 F.3d 1318 (Fed. Cir. 2010).

IP licensees. Finally, the proposed approach is tailored with a precision sufficient to minimize shock to the patent system because it avoids the question of patent invalidity and does not seek to alter the ability of NCEs to procure patents.