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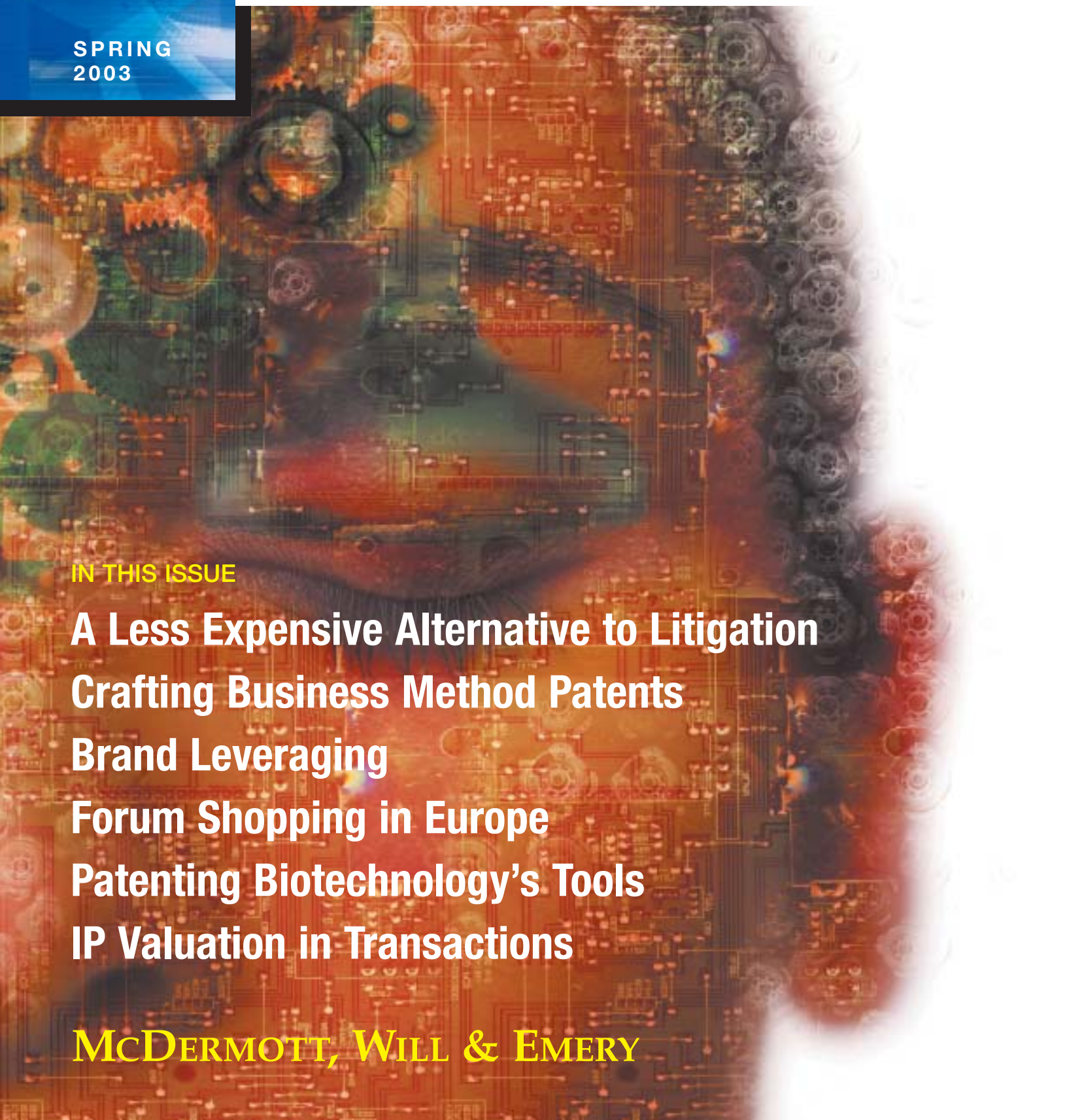
LEADING EDGE THINKING ON INTELLECTUAL PROPERTY

SPRING
2003



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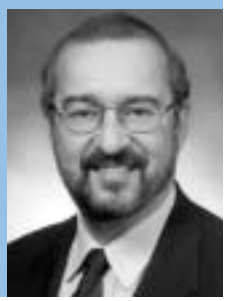
McDermott, Will & Emery publishes *IP Review* twice yearly to provide the latest news and information on intellectual property for professionals in business and law. *IP Review* may be considered advertising under the rules regulating the legal profession.

From the editor...



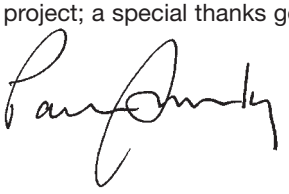
Welcome to the inaugural issue of *IP Review*.

The *IP Review* is a biannual publication of the IP Department of McDermott Will & Emery, to be issued during the second and fourth quarters of each year.

Many of you are familiar with our monthly IP publication, *IP Update*. *IP Update* provides readers with concise reports on current cases of interest, as well as legislative and regulatory developments relating to IP and its first cousins, information technology (IT) and e-commerce. Other than the occasional "Practice Note," the reports strive to be short, newsy in tone and editorially neutral. The articles in *IP Review*, on the other hand, are intended to provide the reader with insights into the nuances of the various topics and to express the authors' points of view. While most of the authors are partners of MWE, in each issue we will attempt to present the insights of at least one eminent guest author. We hope you will find the articles to be thought provoking, insightful and above all, useful. Your feedback as to how successful we are in meeting this editorial challenge is not only welcome it is earnestly solicited.

As even a cursory review of the table of contents will show, the current issue includes articles covering a wide range of topics relevant to both in-house and outside counsel. We thank the many friends of the Firm who assisted us in vetting and winnowing down topics of interest from the several dozen that were under initial consideration. In future issues, we plan to present articles that focus on a single topic. Many of you know McDermott, Will & Emery from its preeminent big ticket IP litigation capability, which (not so coincidentally) will be the topic for the articles appearing in the next issue.

Heartfelt thanks for the launch of the *IP Review* go to Dan Archabal, Amy Nigrelli and Jackie Borta of the Practice Development Group, who initiated the idea of the *IP Review* and without whose hard work it could never have reached fruition. Thanks also goes to Jack Lever and Ray Lupo, the present and past chairs of the IP Department, whose total support and timely guidance were invaluable. Sincere thanks also go out to each of the authors for interrupting their own busy schedules to take the time to participate in this project; a special thanks goes to Mark Grant, our guest author for this issue.



Paul Devinsky

Inter Partes Patent Reexamination –

a less expensive but sound alternative to litigation

By Kenneth L. Cage and Marc E. Brown

The authors review the pros and cons of the new *inter partes* reexamination statute, showing that in appropriate circumstances *inter partes* reexamination may be used as an effective alternative to litigation – at a fraction of the cost.

Over the years, many companies have been forced to bear the high costs of defending patent infringement litigation and have suffered as a result of decisions rendered by judges or juries who did not fully understand the technology involved. However, in those cases where the outcome is likely to turn on the defense of invalidity based on prior art patents or publications, there is now a far less expensive alternative to litigation – *inter partes* reexamination.

On November 2, 2002, President Bush signed into law significant revisions to the *inter partes* reexamination process. The revisions not only broaden the scope of the prior art that may be used to request *inter partes* reexamination; they also, grant the patent challenger the right of appeal to the U.S. Court of Appeals for the Federal Circuit on any final determination by the U.S. Patent and Trademark Office (USPTO) that is favorable to the patent owner.

Prior to the recent revisions, *inter partes* reexamination could not be based on prior art that had been relied upon by the patent examiner in issuing the original patent. As the U.S. Court of Appeals for the Federal Circuit had held in *In re Portola*, previously considered prior art would not raise the "substantial new question of patentability" that the reexamination statute required. This limitation has now been statutorily removed. The revised statute now states: "The existence of a substantial new question of patentability is not precluded by the fact that a patent or printed publication was previously cited by or to the Office or considered by the Office." This change gives the patent challenger the opportunity to convince the USPTO that it overlooked important aspects of prior patents or publications that the USPTO previously considered in granting the original patent.

In seeking *inter partes* (or for that matter, *ex parte*) reexamination, it is important to recognize that a *prima facie* case of unpatentability need not be present for the examiner to make the determination that a substantial new question of patentability is present. The request need only convince the examiner that a substantial new question of patentability is present to confer jurisdiction upon the USPTO to conduct the reexamination. In other words, an order granting reexamination, *inter partes* or *ex parte*, is not a final determination by the USPTO as to the unpatentability of any claim in the patent.

Prior to the new legislation, the patent challenger could not appeal to the Federal Circuit if patentability was confirmed. Nor could the challenger participate, as a party, in an appeal by the patent owner if the USPTO rendered a decision adverse to the patent owner. The new legislation gives the challenger these important rights. However, unlike the case for an original patent application or an *ex parte* reexamination, the new *inter partes* reexamination statute does not provide for either the patent owner or challenger, the right to appeal to the U.S. District Court of the District of Columbia.

On a cautionary note, the *inter partes* reexamination statute includes an "estoppel" provision that prevents an accused infringer who failed to overturn the patent during *inter partes* reexamination from later challenging the patent in a civil action or in a subsequent reexamination. The "estoppel" only applies to a challenge that is based on prior art that was or could have been urged during the *inter partes* reexamination. Still, the estoppel provision has some real teeth and will likely be the subject of some interesting discovery as accused infringers attempt to mount post *inter partes* reexamination validity challenges.

Inter Partes Procedures

Unlike an *ex parte* reexamination proceeding, the request for *inter partes* reexamination must disclose the real party in interest. The request must also certify that the requestor is not estopped, as per the provision noted above, from making the request. The USPTO must also be informed of any prior or concurrent USPTO or litigation proceeding involving the patent and the status of the proceeding.

The USPTO will determine whether the request raises a "substantial new issue of patentability" within three months from the filing date. The patent owner will not be permitted to file a response to the request before this decision is made.

If the USPTO does not find a substantial new question of patentability, the request will be denied; but in that situation the estoppel provisions do not apply. The denial of a request is not directly appealable but may be subject to review by a petition filed by the challenger to the Commissioner of the USPTO. The grant of an order cannot be appealed.

The USPTO will ordinarily assign the case for reexamination to a different examiner than the one that issued the original patent. If the examiner determines that the request raises a substantial new question of patentability, an order granting *inter partes* reexamination will be issued, usually accompanied by an Office Action on the merits of the patentability of the claims.

The patent owner must respond to the Office Action to avoid abandonment. Each time the patent owner files a response, the challenger may file comments about issues raised in the office action or in the patent owner's response. However, unlike during the original prosecution of the patent (or in *ex parte* examination), the patent owner cannot meet with and interview the examiner.

"The patent owner is, in effect, forced to go back to square one as in the examination of the original application for the patent; but now with a motivated third party dogging his every move."

At each round of office actions and responses, the examiner will consider comments from the patent owner and the challenger and will either continue prosecution or issue a right of appeal notice to the patent owner or challenger, allowing the patent owner or challenger to appeal to the Board of Patent Appeals and Interferences. A patent owner or challenger dissatisfied with the decision of the board may then request a rehearing, or appeal to the Federal Circuit.

A full *inter partes* reexamination through appeal can be expected to take about three years: a year to arrive at the examiner's final decision; a year to obtain a decision from the Board of Appeals; and a year to receive a decision from the Federal Circuit.

Advantages of Reexamination over Litigation

Stays If a lawsuit has already been filed and is in its early stages, there is a good chance that the district court will stay the litigation pending the outcome of the reexamination. This can result in very substantial savings. The International Trade Commission (ITC) has stayed a Section 337 proceeding where a patent is subject to *ex parte* reexamination. However, this may not be the case for a patent involved in an *inter partes* reexamination proceeding as the time frame required to complete all appeals is longer than the course of an ITC investigation.

Cost Savings An average single patent lawsuit costs $1-$2 million to get through trial. A patent can be reexamined through an appeal to the Board of Appeals for a small fraction of this amount. Of course, if the patent survives the reexamination process relatively intact and without any damaging prosecution history, there may not be much in the way of savings on the part of the accused infringer.

No Presumption of Validity An important, and possibly outcome determinative, advantage of reexamination over litigation from the challenger's perspective is that there is *no* presumption of validity in reexamination, let alone the strong presumption that applies in litigation. Consequently, there is no clear and convincing burden of proof imposed on the challenger to establish that a claim is unpatentable. The patent owner is, in effect, forced to go back to square one as in the examination of the original application for the patent; but now with a motivated third party dogging his every move.

USPTO Expertise As noted in the introduction, accused infringers often complain that judges and juries do not understand the technology involved in making patentability determinations. This concern should be alleviated in reexamination proceedings as patent examiners and board members usually have a technical background and are well versed in the applicable principals of patent law.

Disadvantages of Reexamination to the Challenger

No Discovery Unlike litigation, the challenger in a reexamination will not be entitled to discovery or to cross-examine any declarations or affidavits that the patent owner presents. This gives the patent owner the ability to stretch the facts somewhat and to deprive the challenger of evidence that might strengthen its case. Of course, the challenger in an *inter partes* reexamination can present its own expert declarations or affidavits to the patent examiner to counter any evidence presented by the patent owner.

Patent Owner Can Amend While a patent owner is not allowed to amend claims in litigation, during an *inter partes* or *ex parte* reexamination the patent owner has the opportunity to narrow the claims to avoid the prior art, while still focusing on the alleged infringement being marketed by the challenger. However, the challenger might also be afforded equitable "intervening rights" depending upon how the claims are narrowed in the USPTO.

Estoppel As noted above, if the patent emerges from reexamination, the challenger will not be able to reassert the same prior art challenge in court. The challenger will also be barred from asserting any other prior art defense in court that could have been raised during the reexamination process.

Conclusion

The new rules for *inter partes* reexamination and subsequent appeals remove much of the downside of the original but rarely used *inter partes* reexamination procedure[1]. The absence of any presumption of validity, coupled with decision makers that are likely to be technically and legally qualified, represent significant advantages of reexamination over litigation.

On the other hand, live testimony, cross-examination of witnesses and discovery are not permitted. In addition, the patent owner can amend his claims, and the issues that have or could have been asserted during reexamination cannot be re-litigated.

It should also be noted that *inter partes* reexamination can only be sought of patents that are based on applications that were filed after November 29, 1999.

While we are all waiting to see how the scales tip, it is clear that *inter partes* reexamination can be a far less costly, yet viable alternative to litigation.

[1]As of this writing, USPTO records indicate that since the advent of the *inter partes* reexamination statute in November 1999, a total of eleven requests for *inter partes* reexamination have been filed, six of those since the November 2002 amendments.

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Crafting Meaningful Business Method Patents

By Stephen A. Becker and Paul Devinsky

This framework for preparing and prosecuting business method patents includes analyses of the types of claiming strategies available to the drafter, consideration of the scope of national patent protection and an understanding of competitors' business operations. The focus is on how to obtain a commercially valuable patent likely to be directly infringed by competitors.

It is now well established that appropriately claimed business method inventions may be patented, if novel and not obvious over "prior art" methods of doing business. A business method patent is no more than an ordinary "method" patent, whose subject happens to be business. Nevertheless, business method patents are still considered sufficiently unique that precautions have been put into place by the U.S. Patent and Trademark Office to ensure that it does not issue excessively broad business method claims.

It is not difficult to draft a business method patent application. It is, however, challenging to draft one that is meaningful, particularly when the business is carried out by computer implementation or on the Internet. Computer and Internet involvement in a transaction, usually described under the umbrella term "e-commerce," is the mode by which most business methodologies that are candidates for patenting will be carried out. But Internet inventions create a variety of enforcement problems that result from two fundamental qualities of the Internet: distributed resources and lack of territorial boundaries. An Internet business system commonly will span more than one country.

For example, the system may be designed to provide a service, such as offering a transaction to a customer in the U.S. The starting point of the service, therefore, is the location of the customer's computer; let's call that the "client." Choices are presented to the client at a customer interface that is partially created by the client and partially by information sent to the client by the service provider. The service provider is a remote computer that may be located either within or outside the U.S.; let's call that the "server." In either case, the flow of information between the client and the server may span many computers at numerous different sites, as is characteristic of the Internet.

For instance, an order is placed by a customer in the U.S.; transmitted to a destination in Europe for processing; relayed to Asia for production of product; and returned to the U.S. for confirmation, tracking of status and accounting. The service provider probably owns the U.S. based server that takes the original order and may own the devices overseas that contribute to the transaction; but the provider almost certainly will not own or control the client.

These diversities – lack of common ownership or control of devices in the transaction flow and implementation of devices that reside in differing jurisdictional territories – could wreak havoc when it comes to drafting a readily enforceable U.S. patent providing meaningful protection for a business methodology.

The Scope of U.S. Patent Law

U.S. patent law is very careful not to extend the scope of a patent beyond what it claims, beyond its territorial reach or beyond its term. The territorial extent of a patent is the U.S., and a patent covers not only acts in the U.S. but also importation into the U.S. of the patented invention. A patent is enforceable only during its term, which expires 20 years from its application date. Consider that a patent gives its owner a right to exclude others from making, using or selling the patented invention within the U.S. An infringer of a patented invention can be prohibited by injunction from further violations. With limited exceptions, if an intended infringer practices the invention in a foreign country, the patent can only be used to prevent importation of the invention into the U.S.

U.S. patent law also provides that anyone who induces infringement of a patent is equally liable as an infringer. Contributory infringement will additionally result in liability. Contributory infringement arises when someone sells, offers to sell or imports into the U.S., a component of a patented invention, or a material or apparatus for practicing a patented process. The violator must have been aware that the component, material or apparatus is destined for an infringing use and is not merely a staple product that can be widely used in non-infringing ways. Finally, the law provides that infringement may arise when a product is imported into the U.S. that has been made abroad by a process covered by a U.S. patent.

Another statute, 35 U.S.C. § 105, colloquially known as the "space act," may become involved in evaluating infringement of a U.S. business method patent in the context of Internet activities. This statute determines what happens when an invention is used, at least in part, in outer space, as when a satellite is a part of a path of information flow in an Internet transaction. The invention is treated as having been made, used or sold in the U.S. if the satellite is under the jurisdiction or control of the U.S. An exception is where the satellite is used within an international agreement to which the U.S. is a party or is on the registry of a foreign state in accordance with a special convention.

How the distribution of resources among different controlling entities and lack of territorial boundaries impact infringement of a patent can be appreciated by reference to an example that reflects a modification of the system disclosed in U.S. Patent No. 5,960,411; a.k.a. the "one-click" patent, owned by Amazon.com. The `411 patent, in essence, describes a method and system in which a consumer can complete a purchase order for an item via the

"Whether there is infringement that is direct, contributory (or induced) or whether there is no infringement at all, depends in part on who owns or controls the components listed in the claims and where in the world the components are located."

Internet using only a single action (such as a single click of a computer mouse button) once information identifying the item is displayed to the consumer. Using the client/server definitions in the "one-click" system, an order is placed by a purchaser at the client and received by the server. The server receives purchaser information including identification of the purchaser, payment information, and shipment information from the client. The server then assigns an identifier to the client and associates the identifier with the received purchaser information. The server then sends to the client, along with the identifier, a document that identifies the item and includes an order button. The client stores the identifier and displays the document. In response to the selection of the order button, the client sends to the server a request to purchase the identified item. The server receives the request and combines the purchaser information associated with the client identifier to generate an order. In this hypothetical we will add a step to the "one-click" system in which the server receives and relays this information to an account verification facility, where authenticity of the account and account status are evaluated to authorize the purchase and return an approval to the server that enables the purchase to be completed.

Format Claims

For this analysis, assume that the "modified" `411 patent contains four differing format claims; namely, a method claim, two different system claims and a claim to a computer readable medium. Following are examples of how these claims might read.

Claim 1 – A method of placing an order for an item comprising:

- under control of a client system, comprising of display information identifying the item; and in response to only a single action being performed, sending a request to order the item along with an identifier of a purchaser of the item to a server system;
- under control of a single action ordering component of the server system, receiving the request; sending an inquiry to an account verification system having stored additional information relating to the purchaser, generating an order to purchase the requested item for the purchaser identified by the identifier in the received request; and upon receiving a purchase authorization from the account verification facility, fulfilling the generated order to complete purchase of the item whereby the item is ordered without using a shopping cart ordering model; and
- under control of the account verification facility, upon receipt of the inquiry from the server, querying the stored additional information relating to the purchaser identified by the identifier in the request, and sending to the server a purchase authorization.

Claim 2 – A system for processing orders comprising:

- a client terminal having a user interface that is interactive with a browser to communicate with entities via the Internet, the client station having an input device capable of sending an indication of an item being purchased, together with an identifier of the purchaser, upon only a single action manual request by the purchaser, at which interface an item to be ordered is displayed;
- a server configured for receiving the single action request from the client terminal, retrieving additional information previously stored for the purchaser identified by the identifier in the received request; and generating an order to purchase the requested item for the purchaser identified by the identifier in the received request using the retrieved additional information;
- an account verification facility for receiving the account verification data, comparing the account verification data with stored account data corresponding to the purchaser, and generating a transaction approval; and
- the server being further configured to receive the transaction approval generated by the account verification for fulfilling the generated order to complete purchase of the item whereby the item is ordered without using a shopping cart ordering model.

Claim 3 – A system for processing orders comprising:

- a client terminal having a user interface that is interactive with a browser to communicate via the Internet, the client station having an input device capable of sending an indication of an item being purchased, together with an identifier of the purchaser, upon only a single-action manual request by the purchaser, at which user interface an item to be ordered is displayed, and an account verification facility for receiving the account verification data, comparing the account verification data with stored account data corresponding to the purchaser, and generating a transaction approval; and
- a server configured for receiving the single action request from the client terminal, retrieving additional information previously stored for the purchaser identified by the identifier in the received request; and generating an order to purchase the requested item for the purchaser identified by the identifier in the received request using the retrieved additional information; the server being further configured to receive the transaction approval generated by the account verification for fulfilling the generated order to complete purchase of the item whereby the item is ordered without using a shopping cart ordering model.

Claim 4 – A machine-readable medium:

- having stored thereon instructions that, when executed by a computer at a server, controls the computer to send to a client data describing items to be offered to a purchaser at the client for purchase, and in response to a single manual action performed at the client to indicate an order to purchase a specific item, obtains from the client an identifier relating to the purchaser together with an identification of the specific item to be ordered, sends the identifier to an account verification facility where the identifier is compared with stored purchaser account information, receives from the account verification facility an approval to complete the purchase, and in response, fulfills the order.

Scenarios for Potential Infringement

There are a number of different scenarios under which infringement potentially could arise. Whether there is infringement that is direct, contributory (or induced) or whether there is no infringement at all, depends in part on who owns or controls the components listed in the claims and where in the world the components are located.

As a fundamental matter, the patent owner will prefer infringement to be direct, rather than contributory or induced, and will want the infringer to be a competitor, *i.e.*, a service provider (not a customer). Direct infringement arises when the patented (claimed) invention is used inside the U.S. For the patent owner to achieve the most desired outcome, including the possibility of an injunction, all components of the claimed invention must be shown to have been appropriated by a competitor in the U.S. On the other hand, if any component of the invention is owned by or under control of a third party, that third party must be joined as a contributory infringer. This will obviously be unacceptable if the third party is an existing or potential customer of the patent owner.

Assume initially that all components of the invention reside in the U.S. Whether direct infringement will occur in this example depends on whether a single entity owns or controls all components required in a claim. Claims 1 and 2 are troublesome in this respect, as three separate entities potentially are involved in what is required by these claims: a server, a verification facility and a purchaser. At best, in the event the competitor owns or controls both the server and verification facility, there is still the purchaser (customer) issue. To make a case of infringement, therefore, the patent owner must join the customer and competitor as contributory infringers. Claim 3, however, which is also a system claim, is cleverly drafted so that only the server is positively claimed and could be infringed directly by the owner of the server, who presumably is a competitor. Claim 4, the computer product claim, is similarly limited, and does not require activity other than by a competitor for infringement.

Next, assume that all components of the system reside outside the U.S. In that scenario, infringement in the U.S. probably would not arise under the U.S. law. There is a possibility that might arise under the provision of U.S. law, which provides liability where a product, produced as a result of the patented system, is imported into the U.S. This possibility will apply only to Claim 1, the method claim. Although the process of Claim 1 ultimately results in importation of a product that has been purchased online from the U.S., query whether the claimed method is what actually produced the product.

As a final example, consider a situation where some of the components reside in the U.S. and others outside. For example, assume that the purchaser and server are local, and the verification facility is in Europe. Claims 1 and 2 are not infringed because the verification activity and facility, a recited step or component of each claim, is not practiced in the U.S. Claims 3 and 4, however, are written from the perspective of the server, *i.e.*, only server activity is positively claimed. Because the server is located in the U.S., there would be direct infringement.

If the system were reoriented so that the server is located abroad, and the verification facility local, there would be no U.S. infringement of even Claims 3 and 4. Infringement under this scenario theoretically may arise under 35 U.S.C. §271(f), which was enacted to prevent copiers from avoiding infringement by exporting components of the patented invention for assembly abroad. Section 271(f)(2) applies even when only a single component of a patented invention is exported. However, the component must be specially adapted for use in the invention; it cannot be a staple article. That situation does not occur here, where the only component being exported is an account verification request that presumably is more staple than special.

Conclusion

E-business method claims must be drafted with a view to the commercial realities of the Internet. A patent will be useable for the purpose intended only if a competitor directly infringes it. The claims must be prepared with a focus on the U.S. domestic territorial extent of a patent, and on the inadvisability of reliance on contributory infringement that may implicate a customer or potential customer of the patent owner. A variety of claims of differing formats may advantageously be presented, so long as they require only components or acts within the U.S. by only a single entity – the competitor.

Stephen A. Becker **Paul Devinsky**

Stephen A. Becker leads McDermott, Will & Emery's patent prosecution group and concentrates his practice on patents, with special emphasis on semiconductor electronics, telecom and computer related inventions. Paul Devinsky concentrates his practice on patent, trademark and copyright litigation, counseling and prosecution, and on trade secret litigation. Both lawyers are based in Washington, D.C. and are in the Firm's Intellectual Property Department.

Brand Leveraging –

new income streams in a lukewarm economy

By Robert W. Zelnick and Michelle C. Burke

There are many opportunities available to companies with recognized brand names to leverage their brands into significant revenue streams. However, caution is required to avoid killing the brand name goose that laid the golden egg.

Do you know what Nivea, the hand and body lotion company, and Caterpillar, the maker of giant earth-moving machines, have in common? Both were included in the 2002 list of The World's 100 Most Valuable Brands, as compiled by brand consultancy, Interbrand, and published by *BusinessWeek* last summer. Both Nivea and Caterpillar were celebrated as brands that enjoyed marked increase in value, in part through successful brand extensions or brand leveraging. Nivea took a focused approach and cultivated a portfolio of dozens of products in the personal care and grooming areas from its core stable of skin-care products. Caterpillar, on the other hand, took its industrial brand into consumer categories such as footwear and apparel. The strategies reflect both companies' determination to create new opportunities and new revenue streams from existing brands.

Can brand leveraging work for your company? Many companies, particularly those in the B2B world, consider the value of branding and brand leveraging as a realistic opportunity only for consumer products companies. However, as Caterpillar and other B2B companies have discovered, brands are financial assets that can contribute significantly to the bottom line creating valuable new revenue streams and broader marketing opportunities. In some cases, profits and sales from the "extended" products or services can significantly exceed the profits of a company's core business.

What is a brand? In marketing terms, a brand is more than a single trademark such as a product name, corporate logo or tagline. Rather, it is the embodiment of a host of associations and perceptions that customers, investors and the general public experience when they encounter a company and its products in the marketplace. Most marketing experts agree that a brand is a promise, representing to purchasers an assurance of an expected level of quality and service.

While exploring leveraging possibilities is often a wise choice, brand leveraging is not without legal pitfalls. For example, only legally protectable (and protected) trademarks should be considered candidates for leveraging. In order to continue to enjoy broad legal protection, a brand must be used properly by its owner and protected against abuse by others. Moreover, the various strategies for leveraging brands, as described below, must be structured so that the brand necessarily continues to exercise careful control over the use of its trademarks.

Protecting Brand Assets

The strongest form of legal protection for trademarks is registration. In many countries, in fact, only registered trademarks can be protected against infringement. In the U.S., protection is afforded both through federal registration and under common law, the latter of which does not require registration. There are important benefits of federal registration, and any trademark that is being considered for brand leveraging should be federally registered, if possible.

If a trademark is already registered for a company's core goods or services, a trademark search should still be conducted to determine whether the mark is available for use on additional goods and services. The search should include both federal registrations and common law sources to determine whether the same or a similar mark has been used in local markets without the benefit of federal registration.

In addition to having distinctive and protectable trademarks, a company should have an active trademark enforcement program. A trademark that has been actively "policed" is more valuable than one that has been weakened through lack of enforcement. A well-managed trademark protection program often begins with a compliance manual drafted with the assistance of trademark counsel and the company's advertising agency. In addition, strategies should be developed to monitor improper usage or potential infringement of the mark by competitors or others.

Brand Leveraging Strategies

Some of the opportunities for brand leveraging include joint ventures, strategic alliances (teaming, strategic partnering, alliances, cross-licensing, co-branding), franchising and trademark licensing (merchandising).

Joint Ventures are typically structured as a partnership or as a newly formed and co-owned corporation where two or more parties are brought together to achieve a series of strategic and financial objectives on a short-term or a long-term basis. Each participant makes its respective contribution of skills, abilities and resources. Often, the names of joint ventures, or the names for the products offered by joint ventures, are derived from individual corporate or brand names. In some cases, one of the participants may license its mark to the joint venture. In 2000, for example, Dean Foods Company, a processor and distributor of regionally branded and private-label dairy products, formed a joint venture with Land O'Lakes, Inc., a producer-owned cooperative, to market and license certain dairy products to leverage the LAND O'LAKES brand name nationally. In a similar way, Starbucks Corp., which has been very successful in its brand leveraging efforts, has entered into a joint

"...trademark rights can be among a company's most valuable – yet often unmined – assets in today's competitive marketplace."

venture with PepsiCo Inc. to produce and market its FRAPPUCINO brand ready-to-drink coffee beverages and another with Dreyer's Grand Ice Cream Inc. to produce coffee-flavored ice cream.

Strategic Alliance is a term used to refer to any number of increasingly common collaborative working relationships where no formal joint venture entity is formed but where two independent companies become interdependent through mutual objectives, mutual strategy, mutual risk and mutual reward. The various relationships are commonly referred to as teaming, strategic partnering, alliances, cross licensing or co-branding. Starbucks, again, is in collaboration with Kraft Foods through which it has become the largest supplier in the premium coffee category. Harley-Davidson, Inc., another successful brand leverager, is part of a strategic alliance with U.S. Bancorp, under which U.S. Bank operates Harley-Davidson Financial Services' affinity card program – the HARLEY-DAVIDSON® CHROME VISA®. Nike Inc., which has traditionally licensed its mark to apparel manufacturers, teamed with Dynastream Innovations Inc. to create a device that attaches to shoelaces to measure running speed and distance on unmarked courses, offered under the NIKE mark. Finally, ValueVision International, Inc., a national home shopping network, announced an agreement under which it will team with NBC for the ShopNBC home shopping network and ShopNBC.com companion Internet site.

Co-branding involves two established brand names combining in order to bring added value, economies of scale and customer recognition to each product. Examples of co-branding include ingredient co-branding, where the strength of one brand appears as an ingredient to enhance sales and cross-consumer loyalty (*e.g.*, POST RAISIN BRAN using SUN-MAID raisins in its cereal); implied endorsement co-branding, where the co-branded name or logo is used to build consumer recognition even if there is no actual ingredient used in the product (*e.g.*, JOHN DEERE on the back of a FLORSHEIM boot, DORITOS® PIZZA CRAVER tortilla chips which features PIZZA HUT's logo on the packaging); actual composite co-branding, where the co-branded product uses a branded pairing of popular manufacturing techniques or processes (*e.g.*, TIMBERLAND boots with GORE-TEX fabric, DELL or GATEWAY computers labeled with INTEL® INSIDE or MICROSOFT® Windows®; and designer-driven co-branded products, where certain manufacturers have co-branded with well known designers to increase consumer loyalty and brand awareness (*e.g.*, the EDDIE BAUER edition of the FORD EXPLORER).

Franchising is a popular expansion strategy, especially for businesses that cannot afford to finance internal growth. There is a host of legal and business prerequisites that must be satisfied before any company can seriously consider franchising as a method for rapid expansion. In addition, the offer and sale of a franchise in the U.S. is carefully regulated at both the federal and state level.

Licensing is a contractual method of developing and exploiting a brand by transferring rights of use to third parties without the transfer of ownership. From a legal perspective, licensing involves complex issues of contract, tax, antitrust, international, tort and intellectual property law. From a business perspective, licensing involves a weighing of the economic and strategic advantages of licensing against other methods of bringing the product or service to the marketplace, such as direct sales, distributorships or franchises. Significantly, trademark owners must be very careful not to grant too many licenses too quickly. The financial rewards of a flow of royalty income from hundreds of different manufacturers can be quite seductive, but must be weighed against the possible loss of quality control and dilution of the trademark. Harley-Davidson is an example of a company that has carefully expanded its brand to a wide variety of products, from apparel to toys and games, and has enhanced the value of its brand in doing so.

Because brand leveraging presents attractive economic opportunities, trademark rights can be among a company's most valuable – yet often unmined – assets in today's competitive marketplace. The goodwill and customer recognition that trademarks represent have tremendous economic value and are therefore worth the effort and expense to register and protect them, both as enduring corporate assets and as a solid platform for strategic and creative growth.

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Forum Shopping in Europe

By Laurence Cohen and Boris Uphoff

Litigants who operate multi-nationally and who are possessed of worldwide patent rights face a spectrum of choices when selecting the forum most consistent with their litigation objectives and budget constraints. The authors provide help in selecting the right forum for each circumstance.

Europe's court system is fragmented, with no federal system for patent purposes (unless the core infringer is Dutch), and with courts having competence and jurisdiction only within their locality. However, patent enforcement actions in Europe can be worthwhile, especially where the effect of the infringement is likely to be severe price depression in a patent owner's product that competes with the subject of the infringement.

Litigants involved in patent litigations in the United States have a number of expectations regarding the speed and cost of a trial as well as the results that might be obtained. Patent litigants in various European Union (EU) jurisdictions have a different set of expectations. A table is presented at the end of this paper to provide a ready comparison between the U.S. and the most important EU forums for patent litigation.

In the U.S., patent litigants are used to hard fought and expensive litigation in which many issues are thoroughly investigated and litigated. Proceedings are likely to be trifurcated: the first stage being a Markman hearing to determine the proper construction of the claim(s) in issue; the second stage the liability trial itself; and the third stage the determination of damages. The typical motivation for a patent enforcement action is to take advantage of the patent owner's exclusionary right. It follows that, in many cases, an injunction is the most important remedy sought, although damages for infringement should not be belittled. In the U.S., declaratory judgment relief, to have a patent declared invalid, is not available to potential infringers unless the patent has been asserted against it.[1] Interim injunctions (also known as preliminary injunctions) are granted in the U.S. based on a showing of irreparable injury to the patent owner as well as the balance of hardships in the patent owner's favor. The hurdle for obtaining such interim relief is quite high, requiring the patent owner to prove a likelihood of success on the merits.

With all these difficulties, why do many patent litigants who have an option choose the U.S. as their venue? The great advantage of litigation in the U.S. is geographical scope of relief granted, covering the world's number one economy in a single action. This benefit, despite the large costs, usually makes litigation in the U.S. a reasonable value for the money spent. The obvious disadvantages of U.S. litigation are the cost and the amount of management time consumed, particularly in dealing with some of the pre-trial discovery issues that are unique to the U.S. With this background as a reference point, forum shopping in Europe is now considered.

England

In terms of overall advantages and disadvantages, the English courts fall intermediate between those of the U.S. and Germany. The UK covers a relatively small market, some 50 million people of the world's fourth largest economy. However, the UK has trained specialist patents judges who themselves were advocates (trial counsel) in the field of patent litigation before their appointment to the bench. It is, therefore, a knowledgeable tribunal.

Overall, we believe that the UK represents a relatively high-cost but nevertheless good forum for patent owners. It is a forum, which, in appropriate cases, will allow proceedings to go to trial despite a pending opposition in the European Patent Office (EPO). In UK cases involving a process patent, provided the claimant can make out a *prima facie* case of infringement, the defendant will have to either give discovery or a statement of process so that all issues of infringement can be considered with full knowledge of the activities involved. Cross-examination of witnesses is provided. What the inventor did or thought is essentially irrelevant to an English court and therefore the premium in English litigation is to find a good expert. Despite protestations of neutrality, the expert is in fact the primary mouthpiece for his client's case.

The high cost of English litigation has been a problem, which the judges have recognised. Steps have been taken to try to minimise cost, but they have not been totally successful; not least because the judges expect every point to be thoroughly explored and the papers to be absolutely immaculate. Of course, this costs money.

English procedure is deep; it is as deep as the U.S. procedure except in respect of discovery. As well, there are many experienced observers who suggest that a bench trial before a specialist judge as opposed to a jury trial, is more likely to produce the right result in absolute justice terms. The time to trial is reasonable, typically about a year. In appropriate circumstances, English courts will issue orders for speedier trial schedules; typically six to nine months. Interim injunctions are granted, based on irreparable harm, such as permanent price depression, and balance of convenience (justice). As in the U.S., such relief remains difficult to obtain.

In the UK the primary remedy has tended to be injunctive relief although the English courts are reasonably generous as to damages including claimant's loss of profits (subject to proof) and parasitic damages (where they are shown to have arisen directly out of the infringement). However the combination of a relatively small market and quick procedures has tended to militate against large claims to damages.

In short, UK proceedings are highly recommended in circumstances where a


process patent claim is involved as the defendant is required to disclose exactly what it is doing in terms of the processes involved; or where an opposition is pending in the EPO; or where the litigation is tactically viewed as a pathfinder for something bigger in the U.S. or the EPO, and the patent owner wishes to find any weaknesses in its position before contending for a bigger prize.

The Netherlands

In terms of market power, Dutch Kort Gedding proceedings are recommended where the "spider in the web," that is the company at the centre of operations, is Dutch. The Dutch Courts are the only EU courts to espouse pan-European injunctions. They presently do so only where the central company is Dutch based and the centre of operations is in the Netherlands. This has the great advantage of granting a pan-European injunction. Thus, where such an injunction is the primary remedy sought, efforts should be made if possible to invoke Dutch jurisdiction.

The Kort Gedding proceeding is a quasi-summary judgment proceeding and is merit based. The claimant must establish that it is highly likely to win on both infringement and validity. There is no discovery and all submissions must be in writing. It is rapid (typically four months from start to finish) and relatively inexpensive. The Dutch judges, who conduct a bench trial, are accustomed to dealing with patent matters. Therefore, the tribunal can be regarded as relatively specialised and familiar with the subject matter.

On the downside, in a Kort Gedding proceeding there is no cross-examination of witnesses. Also, if the proceeding in the Netherlands fails on a pan-European basis, not only will there be a possibility of jurisdictional difficulties in the rest of Europe; but because the Dutch court is the first to be seized of the matter, other EU courts may be prevented from taking up the matter under the European Jurisdiction Regulation EC/44/2001. Thereafter, awaiting a trial on the merits in the Netherlands is a slow affair taking some three years. Thus, if the Kort Gedding fails, all of the advantages of a rapid semi-summary procedure are lost.

"... Dutch Courts are the only EU courts to espouse pan-European injunctions."

Germany

Germany is one of the most important European forums for patent litigation. On the whole, litigation proceeds relatively quickly and inexpensively in Germany, but German judges sometimes have difficulty handling cases that involve complicated scientific issues.

Although each of the sixteen German states has one or two civil courts that specialise in intellectual property (including patents), cases are normally filed in the courts in Munich or Düsseldorf. The plaintiff may decide where to file its action, and the patent chambers of these courts are considered to be "plaintiff-friendly." The patent chambers are bench courts with three judges each. The judges generally do not come to the bench with a particular technical expertise, but acquire such knowledge on an *ad hoc* basis in the performance of their duties.

Litigation in the first instance may take less than one year. The German civil litigation system does not provide for discovery proceedings (or even mandatory initial disclosure) or depositions of witnesses, which attracts some claimants to Germany as a forum since they do not have to disclose information that could weaken their case. Experts are normally retained by the courts rather than by the parties themselves. However, parties can provide additional opinions from their own experts to support their view. An average pharmaceutical patent litigation typically costs approximately $200,000 in the first instance. Litigation involving other technologies may even be less costly.

One noteworthy characteristic of German patent litigation relates to the defense: the civil court dealing with the infringement issue will not hear invalidity applications filed by the defendant. If a defendant wants to argue invalidity, it must file a separate application with the Federal Patent Court in Munich (*Bundespatentgericht*). The Federal Patent Court is independent of the civil litigation system and sits with several judges that either have a legal or a technical background. Normally the civil courts will grant a stay until the Federal Patent Court has ruled on validity.

While the civil court rules in Germany provide for interim injunctions, such injunction proceedings rarely occur in patent cases. This is attributable to the fact that injunction proceedings require the plaintiff to provide full written evidence on its case, including expert opinions on the validity of the patent and on infringement issues. In most cases, the plaintiff cannot manage to gather the required evidence within the short four-week time period the courts allow between noticing the infringement and filing the injunction application.

Conclusion

When a patent owner requires a quick decision at relatively low cost, and where the defendant's activities are clear, Germany is a very attractive forum. Where a patent owner desires an in-depth consideration of many issues, or where there is doubt as to what the defendant's infringing activities are, and higher costs are bearable, England is a good forum. The Dutch Kort Gedding procedure for a pan-European injunction is the option of choice if the issues are reasonably clear so that the claimant is confident of prevailing; the patent has either been validated post-EPO opposition or had not been opposed, or where there are no obviously serious attacks to it; and the activities are being directed through the Netherlands.


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[1]However, as explained in the companion article by Messrs. Cage and Brown on *Inter Partes* Reexamination (page 2), there is a proceeding available at the USPTO enabling anyone to test the validity of a U.S. patent.

Comparison of U.S. and EU Forms for Patent Litigation

ISSUE	USA	England	Germany	Netherlands Kort Gedding
Speed to trial	1-3 years	0.75-1.5 years	0.5-1 years	0.4 years
Cost to trial (1 patent)	$2-3 million	$1-1.5 million	$0.2 million	$0.2 million
Disclosure	Full	Very limited	None	None
Depositions	Yes	No	No	No
Process patent	Disclosure	Disclosure or process description from defendant	No	No
Mode of trial	Jury	Bench-specialist patents judges	Bench	Bench-leading patent judge
Injunction	Yes	Primary remedy	Yes	Yes
Scope of relief	USA	UK	Germany	EU if prime defendant is "Dutch"
Damages	Triple possible, compensatory and parasitic	Single only, compensatory, but may include parasitic	Single, usually reasonable royalty or profit made by infringer	Single, usually reasonable royalty
Cross examination of witnesses	Yes, but only in relation to evidence given	Yes, on anything	Yes	No
Appeal	Normally one round, no new evidence, rehearing	Normally one round with permission (not refused), no new evidence, rehearing	Two rounds, but second is limited and new evidence is not admissible	Two rounds, new evidence possible
Good expert	Important	Essential	Essential Expert normally appointed by court	Essential
Effect of current EPO opposition	N/A	Stay possible, depends on the need to do justice	Stay possible and normally granted by court	Yes, unless very special factors (*e.g.* another EU court found patent valid)
Experimental use	Limited exception	Infringing unless on subject matter of patent (*i.e.* thought to be infringing if for approval purpose)	Infringing unless on subject matter of patent Experiment use for approval not considered infringement	Not known
Treatment of generics	Neutral	Generic company needs to sue for invalidity and/or declaration of non-infringement at earliest opportunity Interim injunctions readily granted	Generic company can sue for invalidity even during infringement litigation; court for invalidity is different from court in charge of infringement	Kort Gedding provides effective summary judgement procedure

Patenting the Tools of Biotechnology

By Cathryn Campbell, Ph.D.

While most biotechnology companies routinely protect novel compositions identified from research and development efforts, many overlook the potentially more valuable intellectual property – the research tools used to generate those novel compositions. Dr. Campbell explains what those tools are as well as how and why to protect them.

Over the last twenty-five years, the biological sciences have undergone a revolution that requires close attention from patent practitioners seeking to obtain meaningful protection for their clients' intellectual property. From the development of genetic engineering in the 70's through the sequencing of the human genome at the turn of the century, the pace and scope of the innovations that have spawned the biotechnology industry have been stunning. The innovations of the past quarter century have collectively brought about a radical change in the methodology of both biological and medical research, and the pace of discovery has not slowed.

Such rapid technological progress presents enormous challenges not only to the patent laws but to the patent practitioners as well. While the patent system by definition confronts new technologies, perhaps in no other field have the challenges to existing patent law been greater than in biotechnology. Many of the defining inventions in biotechnology – and the proprietary protection available to them – are qualitatively different from those in other technical fields. These differences reflect the fact that much of the valuable technology emerging from biotechnology involves methods and materials for designing or identifying new and useful compositions, rather than the novel compositions themselves. While the primary value of these biotechnology "research tools" lies in the commercial products they may generate, new intellectual property strategies are required to exploit the proprietary value of the research tools themselves.

Examples of these biotechnology research tools include phage display and combinatorial methods for generating vast libraries of peptides and non-peptide molecules; microarrays for displaying and screening libraries for useful compounds; nucleic acid sequencing and data mining methods for identifying useful genes and proteins; *in silico* methods for designing and testing new genetic networks; and synthetic methods for making and expressing whole genomes. In each case, various aspects of these research tools have been the subject of issued patents or patent applications. The claims of these patents do not cover the commercially valuable products that the methods have the potential to generate and inevitably raise the issue of how to obtain value from the patents.

Challenges to Patent Protection

Challenges to obtaining meaningful patent protection are amplified when the invention is a research tool so as to require particular attention and skill from practitioners seeking to protect such intellectual property. Included among these challenges are describing the invention sufficiently to satisfy the enablement and written description requirements and establishing acceptable utility in order to support claims of sufficient breadth to prevent competitors from "designing around." Even if a patent issues, enforcing claims that cover the methods of developing a commercial product, but not the product itself, can be difficult. In situations where licenses are offered or damages sought, determining the value of claims covering tools can be controversial.

These challenges require strategic planning to determine and effectuate appropriate and valuable proprietary protection. Decisions made without strategic forethought can result not only in a loss of the value of the research tool itself, but also have the potential to give competitors a head start in identifying a commercial product through use of the disclosed methods.

The purpose of the enablement requirement (as set forth in 35 U.S.C. 112, ¶1) is to permit others of skill in the art to practice the claimed invention using only the information contained in the patent in addition to art-known knowledge. The scope of enablement provided by the specification must be commensurate with the scope of the claims so that the entire claimed invention passes into the public domain once the patent protection terminates. In order to obtain broad claims whose scope is sufficient to prevent others from modifying the claim elements to avoid infringement, the specification must enable alternate elements. Independent of enablement, the written description requirement of §112, ¶1 further requires that the invention be sufficiently described as to establish that the inventor was in possession of the invention at the time the application was filed. The claimed invention must also have a utility as required by 35 U.S.C. 101. In other words, the invention must work as claimed and provide a specific, substantial and credible benefit to society.

The requirements of enablement, written description and utility are the roadblocks that prevent an applicant from obtaining claims to products resulting from the use of a claimed method. A description of the method alone does not provide an enabling description of the product nor does it establish that the inventor was in possession of the product. Furthermore, a description of the method cannot provide information with regard to the utility of a product yet to be generated. Certainly when the method is used and a particular novel product is identified and described, a patent can be filed claiming the particular product. However, products identified by sepa-

"In a field that is advancing as fast as biotechnology today's methods may be obsolete tomorrow."

rate use of the method may not fall within the claims of such a patent if the products are sufficiently dissimilar.

Structuring Claims

In a field that is advancing as fast as biotechnology, today's methods may be obsolete tomorrow. It is therefore important to structure the claims to research tools in such a way as to cover modifications to the basic methodology. Separate claims should be drawn to different aspects of the invention so as to cover competitors who modify one aspect while keeping others the same. For example, where peptide libraries are generated and screened for receptor binding, claims can be drawn separately to novel methods of making the libraries, to the libraries themselves, and to methods of screening the libraries. Further, where alternative elements are described in the application, separate sets of claims should be constructed which substitute generic elements for the more specific. In addition, because the field is moving so quickly, it is important to describe multiple embodiments so as to be able to claim around prior art that may arise after filing.

When a patent, which claims research tools, issues, determining whether infringement occurs can be difficult; the commercial product may not provide any evidence that the claimed research tool was used. The use of patented research tools to identify a compound – such as by screening a library of ligands for receptor binding – can be considered "one time" infringement. The method is used to identify the active ligand, but thereafter the ligand is synthesized using conventional techniques. In addition, because proprietary protection does not attach until a patent issues, publication of a patent application may effectively permit a competitor to practice the invention without recourse to the applicant. In such a case, trade secrets may provide more valuable protection than would a patent. Thus, a patent, which describes a research method, may allow competitors the benefit of using the method without providing evidence of infringement or in some cases without infringing at all.

Even if infringement can be established, determining the value of a license to use or the damages resulting from unauthorized use is problematic. Tying the value of the claimed method to the commercial value of a resulting product is akin to basing royalties on a patented paintbrush to the sales of artwork created using the paintbrush. On the other hand, where the product could not have been identified but for the method, high value may be justified and obtainable.

With all these caveats, can patents based on biotechnology research tools ever be valuable? Yes. Numerous examples are available which demonstrate that strategically planned and well-managed patent portfolios can be financially profitable. Dyax Corporation, for one, holds patents covering phage display methodology to identify useful nucleic acids and peptides. While the patents claim only the methods of performing phage display and certain intermediates useful in the process, the portfolio has been successfully licensed to over 60 biotechnology or pharmaceutical companies and non-profit institutions. The non-exclusive licenses to companies carry upfront signing fees, annual maintenance fees, transfer or service fees, milestone payments tied to the U.S. Food and Drug Administration process and royalties based on sales of products "discovered, made or developed using a method covered by a claim" in the licensed patents.

Summary

While the recent advances in biotechnology present new and unique challenges to the patent practitioner, strategic planning and careful implementation can create a valuable intellectual property portfolio. A well considered strategy must take into consideration the types of claims that can and should be obtained to maximize protection without unnecessarily surrendering proprietary information. The use to be made of the portfolio – whether to license or enjoin others – should be determined in advance. Finally, licensing and litigation require skilled professionals able to understand the technology and accurately assess the value of the portfolio.

Cathryn Campbell, Ph.D.

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Valuation of Intellectual Property in Sales and Licensing Transactions

By Mark A. Grant

Valuation of IP in connection with sale or licensing transactions is a notoriously inexact art. Mark Grant explores some of the considerations, risks and strategies involved in the valuation process.

In patent litigation, the patentee can rely on two alternate measures of damages: lost profits and/or reasonable royalties. In some cases, where the infringement has been shown to be willful, the court may increase the damage award up to three times the amount found. In exceptional cases, a court may even award reasonable lawyer's fees to the prevailing party.

Unfortunately, such awards only happen after the expenditure of millions of dollars, years of litigation and the almost incalculable loss of the valuable time of engineering and management talent – time better spent developing and marketing products. What can you do if you don't have the time, money or talent to invest in litigation and would prefer to resolve such issues outside of court? What should you do if you become aware of a patent that you believe your company may be infringing, putting the company at risk of future litigation? What can you do if your company has abandoned a particular market segment in which it has developed substantial intellectual property assets, and is looking to recover at least a portion of its investment? These are dilemmas that are confronted every day, and there is no one correct answer. There are, however, some general guidelines to help keep you on the right path.

Licensing Transactions

In the patent litigation world there exits the concept of a "hypothetical negotiation" that presupposes a potential licensee has three main choices: forgo all use of the invention; pay an agreed royalty; or infringe the patent and risk litigation. From the infringer's perspective, the third option assumes that the patent owner will win the lawsuit and perhaps even recover its litigation expenses. A deliberate infringer is likely to be crafty, calculating the patent owner's damages in advance and comparing those damages to the expected cost of litigation. If the calculus indicates that the potential exposure is small relative to expected litigation expenses, the infringer may not fear a lawsuit, feeling confident that litigation would result in a poor return on the patent owner's litigation investment dollar. Even if a company does sue, the infringer may believe that, from a cash flow analysis basis, it would be better to pay lawyers and drag out the process, rather than pay out a high initial license fee, running royalties, *etc.*

Such situations demand a "real" rather than "hypothetical" negotiation. Like many negotiations, it may be fraught with imperfect valuations, imperfect judgments, and inadequate or simply bad information. By putting yourself in your opponent's shoes, you can begin to formulate a negotiation strategy that will eventually guide you to the true value of the property you are licensing, whether it is patents, trademarks, copyrights or some other forms of technology protection.

For basic technology, the process is reasonably simple and predictable and it boils down to a few major factors. Ask yourself these questions: What would be the cost to my competitor to develop the technology himself or herself? What is the benefit to them of the decreased time to market realized by the proposed technology license/transfer? What penalty or competitive disadvantage will my company suffer if I transfer this technology to the target licensee?

If the technology barrier to enter a given market is low, chances are the target will not even be interested in talking to you at this juncture. Instead, they will simply enter the market, try to grab maximum profits and then consider their options in terms of spending a portion of that profit for licensing or litigation expenses if confronted. In any event, if you are talking, be mindful that because technology, and not a patent, is the true barrier to entry in this case, it is fairly easy to value the technology and feel comfortable that you negotiated a fair deal. If there are some improvement patents that cover aspects of the technology, that is a bonus and may add a margin to the valuation.

However, if the patent(s) in question cover basic, fundamental technology, the patents will drive the valuation of the deal. For example, in a situation where a license would involve only patents (no technology transfer) and where there is a strong patent that broadly covers a technology that otherwise presents a low technological barrier to entry, the valuation process is simple (although the result may vary widely due to the perceived strength of the technological barrier to entry). Notwithstanding such variations, bear in mind that in this situation it is not the technology, but rather the legally defined property right that is the true barrier to entry. Thus, the pertinent valuation questions are what does the patent cover, and even if infringed, what is the likelihood that it will be proven to be invalid? In this situation, in order to be successful in maximizing the value of the patent, the patent owner must not only convincingly demonstrate an interest in excluding others from the marketplace, but must also demonstrate a commitment to defend the patent. The anecdotal evidence is overwhelming that once a patent has been asserted and defended, its value in subsequent licensing negotiations commands a premium.

Thus, it is not realistic in a licensing environment to expect the value of an un-litigated patent to rise to the level of one that has survived the rigors of litigation. The trade-off in deciding whether to litigate, and thus realize a higher valuation down the road, reflects

"... a potential licensee has three main choices: forgo all use of the invention; pay an agreed royalty; or infringe the patent and risk litigation."

a balance between the risk the patent will be found to be not infringed or invalid, versus the likelihood of obtaining a high royalty or lost profits (and possibly even attorney fees), as well as higher royalty rates from others later on. Many companies choose to license their IP for less than top dollar rather than face these risks, thus changing the barrier to entry from one of exclusion to one of a "tax."

By any objective standard, patent valuation in a licensing context is a notoriously inexact science. Nevertheless, there are some standard factors to consider in connection with establishing a reasonable royalty for using the patented technology: cost savings realized by use of the technology; profitability improvements; incremental income associated with the next-best alternative; royalty based upon the incremental cash flows generated by the sales of patented technology; rates paid by others for similar or same technology; the nature and scope of the license; licensor's established policy of maintaining its patent monopoly by not licensing others; the remaining term of the patent and the term of the license; and the extent to which the infringer has made use of the invention.[1]

Of course patents are but one piece of the intellectual property bundle; most companies also count trade secrets, trademarks and copyrights in their IP inventory. In fact, many companies include their base technology or know-how in that inventory, even if it is not protected by any of the traditional "property rights." However, a full individual treatment of the valuation of each type of IP is beyond the scope of this article.

Sales Transactions

The value of a patent in a sales transaction presents many challenging issues, few of which are over-arching, as each such transaction tends to be unique. The typical trade-offs under consideration in a sales transaction are different from those in play in the licensing arena, as the seller typically has no current interest in exploiting the technology itself or places little or no value on the exclusionary benefits a patent accords to its owner. Such a situation might arise for many reasons. For example, it is not uncommon for companies to exit a business after investing in substantial research and development, where the only asset left from that investment is intellectual property. In this case the minimum value proposition is simple: the return on the sale should approximate the amount of money invested, with a generous profit for the property right. The investment calculation involves more than simply adding up what was spent to prepare and prosecute the application for the patent. The valuation should also take into account the R&D costs of the technology, especially in situations where a company was first (or at least early) to market with the patented technology.

Remember also that a typical sales transaction is fundamentally different than a license – it is final. The fact that information is intangible also means it is indivisible while a company theoretically may nonexclusively license its technology to an unlimited number of users, a sale may be completed only with a single party.[2] At the end of a typical transaction, the original patent owner will not have retained any rights in the IP![3]

What if a company is in a relatively mature market and its research led to the development of a major improvement *vis à vis* the state of the art, but it has decided to exit for business reasons unrelated to technology? The value of a patent, which covers the R&D development, may be significantly higher than that which would be calculated using the simple cost analysis described above because others in the industry may need access to the improvement to stay competitive. Therefore, it should be assumed that the patent provides its owner significant leverage relative to the remaining competitors. The value of such a patent will obviously be much higher than the sum of money expended during the R&D effort and to obtain the patent grant. In this case, an evaluation of the entire market, including profit margins, *etc.*, may be appropriate, and the valuation should include the likelihood that the new owner will (or at least will have the ability to) extract long-term royalties from one or more of its competitors. At stake in this example is the investment made by the industry – not just the patent owner's company.

One extremely lucrative, but difficult to implement strategy to maximize the sale value of a patent is to simply wait and look for a company in litigation for whom one's patent may have particular value. Frequently, a litigant's own portfolio may not include all the spears and arrows needed to win the fight. At such a unique moment, the value of this particular patent to a specific litigant may be much higher than to any other prospective purchaser at any other time. In those rare situations where a company is prepared to wait for such an opportunity (knowing that it may never materialize), this "pot-of-gold" strategy may be the best exit strategy.

Unsolicited Contact

What do you do when a party, directly or through their lawyer, contacts you asking for a license or sale of some of your intellectual property? In some situations you may not even know the final beneficiary, as the contact person may be simply a shell for a party who prefers not to be identified. This situation is more complex because you are unable to use the usual valuation tools under this circumstance: *i.e.* what is the value of this property to the ultimate purchaser at this time? Examples of critical information necessary to properly evaluate this situation are the buyer's position in the marketplace, its current sales and cash on-hand, its current or expected involvement in litigation, and whether it has sufficient IP rights or leverage to win its case. While you may have some educated guess as to whom the bidder is, such critical information (for accurate

valuation) will not be available when you do not know with certainty with whom you are really dealing. The bidding party may also be a current or potential competitor and may want to enter into a negotiation using a blind contact to obtain information for its own evaluation of the trade off between licensing and litigation. Be wary. A bare assignment of IP where you are exiting the market is one thing; all you stand to lose is some value left on the table at the end of the deal. However, licensing a property that you are currently using can be dangerous if you do not know the intended beneficiary of an unsolicited contact.

Conclusion

This short article is meant only to introduce the reader to some of the more salient issues encountered in connection with valuation of intellectual property. There are many other factors, unbounded as to the analytical methods that are available to ensure the proper valuation and negotiation strategy for each specific situation.

[1] Many of these factors, and more, are described in the seminal damage calculation case: *Georgia-Pacific v. United States Plywood Corp.*

[2] Theoretically a patent owner can sell its rights to many parties, the carve outs being limited only by the creativity of the party's imagination. Theoretically, patent rights can be sold by fields of use carved up geographically or even assigned with individual part interests being transferred to multiple parties. However, such transactions are rare as they make future enforcement of the patent difficult or impossible.

[3] Sellers should be careful to take a grant-back license; otherwise the purchaser may sue for patent infringement in the future!

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info

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