

## IP News

Patent Licensing Strategies After *MedImmune*

By: Howard G. Zaharoff and Michael J. Cavaretta  
May 26, 2008

## Effect of *MedImmune v. Genentech* on Patent Licensing

As a result of *MedImmune*, patent licensees should be more willing to enter into licenses, since this leaves them free to challenge the licensed patents while still enjoying the benefits of the licenses — which effectively would serve as “insurance policies” to insulate the licensees from suit. Licensors, on the other hand, must recognize that, in light of *MedImmune* and its progeny, licensees may be more motivated to seek orders declaring licensed patents invalid, particularly if the patents are of questionable validity or substantial royalties remain to be paid. Licensors will therefore want to adopt strategies and tactics that minimize such negative consequences.

What strategies should licensors and licensees consider when negotiating patent licenses in light of *MedImmune*?

### Licensor Strategies

Licensors may be tempted to include in their license agreements prohibitions against contesting the licensed patents. However, previous Supreme Court decisions cited in *MedImmune* suggest that such provisions would be unenforceable. Further, such provisions would be subject to scrutiny under U.S. antitrust and EU anti-competition laws and directives. So short of prohibiting challenges to licensed patents, what’s a licensor to do? Here are some strategies to consider.

- Include a right to terminate the license if the licensee contests the validity of the licensed patents. (While this approach technically doesn’t prohibit challenges, the effect would be essentially the same, so such provisions similarly run the risk of being found unenforceable.) Include a right to reduce the scope of the license if the licensee challenges the validity of the licensed patent. For example, an exclusive license could be converted to a non-exclusive license, or the field of use could be narrowed.
- Factor the financial risks of a patent challenge (e.g., defense costs and loss of revenue stream) into the economic terms of the license agreement. Essentially, licensors could demand higher royalties than they would have asked for pre-*MedImmune*.
- Front-load payments (e.g., by requiring non-refundable upfront payments and/or higher royalty rates during the earlier portion of the license term). This would have the effect not only of offsetting the financial risks of a patent challenge, but also of minimizing the royalties that could be contested by the licensee.
- Impose higher royalty rates if the licensee challenges the patent or if the licensee challenges the patent and does not prevail. Require the licensee to continue paying royalties during a validity challenge and prohibit it from recouping royalties paid during the challenge, even if successful.
- Require the licensee to reimburse the licensor for its attorneys’ fees and costs incurred in defending a challenge, regardless of outcome.

- Take an equity interest in the licensee as another means of ensuring that the licensor will benefit from the licensee's growth and success, even if the license terminates as a result of a challenge.
- Identify "know-how" that entitles the licensor to a continuing (albeit lower) royalty if a challenge succeeds in invalidating the patent.
- Require prospective licensees to conduct pre-licensing due diligence on the licensor's patent and recite in the agreement the licensee's conclusion that the patent is valid and that the licensee found no basis to invalidate it.
- Require pre-suit notification, with a description of all evidence of infringement or unenforceability known to the licensee. This would allow the licensor to evaluate the strength of the claim and negotiate with the licensee before the suit is filed or to take its own preemptive action.
- Include a "standstill" provision, requiring the licensee to hold off on filing its challenge until after a defined notice period. This would help avoid, or at least delay, a race to the courthouse, which is significant because a public lawsuit could weaken the licensor's ability to enforce the patent against third parties or other licensees.
- Require the licensee to agree that, if it challenges a patent, it must license-back any improvements it invents either on a royalty-free or most-favored royalty basis.
- Select a forum of the licensor's choice, at least for home court advantage, but also possibly to take advantage of any distinctions that may arise in the different federal circuits' approaches to these issues.
- Require confidential arbitration of all issues pertaining to the validity or enforceability of the patents. This would avoid publicly filed claims which, as noted above, could weaken the licensor's ability to enforce its patent against third parties or other licensees. Also, if the patent is found by the arbitrator to be invalid, the licensor would still avoid the "collateral estoppel" effect of a holding of patent invalidity.
- Include a suitable severability clause allowing for the severing and/or modification of any of the foregoing provisions that are held to be unlawful or unenforceable (e.g., by reason of public policy considerations).

Of course, a licensor could reduce its risk of having its patent challenged by a licensee if it only deals with licensees who do not have a reputation of challenging patents and it takes steps to increase the likelihood that the patents it intends to license are valid and enforceable by, among other things, including proper identification of all inventors, using proper IP ownership and assignment agreements, ensuring that inventors are trained to keep notebooks that contemporaneously record their developments, properly disclosing all prior art, and not engaging in improper conduct before the Patent Office.

## Licensee Strategies

What should a licensee do when negotiating a patent license?

- Generally resist any of the above licensor strategic moves, so the license agreement provides insurance against an infringement suit.
- Expressly retain the right to contest the licensed patent(s), at least if new evidence of invalidity and/or unenforceability appears.
- Seek a right to suspend or escrow royalty payments upon a *bona fide* patent challenge, to be paid only if the licensee loses. This provides protection against a licensor's subsequent bankruptcy.

- Similarly, seek the right to not pay royalties during any “standstill” period, as consideration for the licensee delaying the filing of the claim.
- Require the licensor to inform the licensee of any basis to invalidate the licensed patents disclosed to the licensor during any third party challenge to the patents.

If you would like to discuss patent strategies, please feel free to contact **Michael J. Cavaretta** or **Howard G. Zaharoff**.