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Important Considerations In Licensing Know-How with Patents

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The Value of Know-How and Patents

PricewaterhouseCoopers Survey

Most Valuable IP Assets

Companies name the rights most crucial to their business.



- What is Know-How
 - When is it Licensed
 - Trade Secrets and DTSA
- Knowledge-transfer of the Patents and Know-How
- Defining Terms and Royalty Schedules
 - *Brulotte v Thys*
 - *Kimble v Marvel*
- Termination
- Confidentiality
- Assignment

What is Know-How?

- A. Unpatented Inventions
- B. Technical Information
- C. Trade Secrets
- D. Product Specifications and SOPs
- E. Data
- F. B and D
- G. All of the above

Know-How, What is it?

- Includes:
 - Unpatented inventions, designs, drawings, procedures and methods;
 - Skills and experience which assists in manufacture, use, and exploitation of the product;
 - Knowledge of the operation, maintenance, use/application of the product and of its sale, usage or disposition;
 - Unpublished patent applications, invention disclosures and invention summaries; and
 - Negative information (e.g., failed processes, abandoned applications and technical solutions that did not work).

Know-How also includes Trade Secrets

WHAT IS A TRADE SECRET?



Commercially
valuable
information



Creates a
competitive
advantage

Subject to
secrecy
protections



Not readily known,
identifiable, or
ascertainable



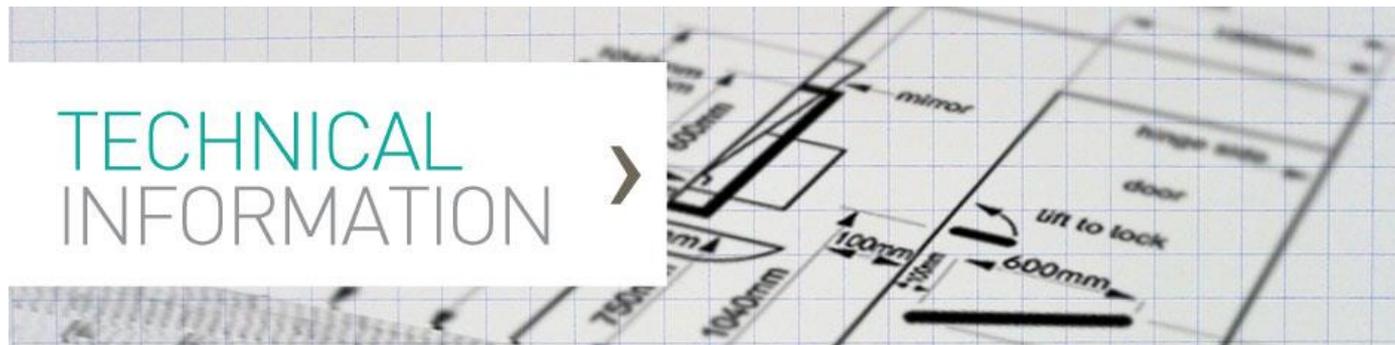
Licensing Know-How

When should you license know-how?

- Always when licensing patents.
- Never, you do not want to disclose your proprietary information.
- It depends on the patented invention.

When to License Know-How

If the know-how will enable the licensee to more fully and/or effectively use, exploit, or manufacture the patented invention.



Patents versus Know-How

The protection of know-how differs from other licensable rights such as patents and trademarks.

- Agree
- Disagree
- It depends
- Don't have a clue



Know-How v Other IP

- Know-how (trade secrets) enjoys both federal statutory protection and state law protection, which can vary in its application. No set expiration of protection (UTSA and DTSA 18 USC § 1839)
- A patent license combines matters of federal and state law. Furthermore, patent protection must be obtained on a country-by-country basis and there is a statutory expiration. Governed by 35 USC § 271, exclusive right to make, use, sell, offer to sell, import
- The owner of a copyrighted work has the exclusive right to reproduce, prepare derivative works, distribute copies, display, etc 17 USC § 106
- The owner of a trademark has the exclusive right to use in commerce (15 USC § 1114.)

Defend Trade Secrets Act

- **Definition of Trade secrets: Federal Law**

[A]ll forms and types of financial, business, scientific, technical, economic, or engineering information, including patterns, plans, compilations, program devices, formulas, designs, prototypes, methods, techniques, processes, procedures, programs, or codes, whether tangible or intangible, and whether or how stored, compiled, or memorialized physically, electronically, graphically, photographically, or in writing if —

(A) the owner thereof has taken reasonable measures to keep such information secret; and

(B) the information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by another person who can obtain economic value from the disclosure or use of the information.

[18 USC § 1839(3), as amended by Defend Trade Secrets Act § 2(b)(1)]

Uniform Trade Secret Act

- **Definition of Trade secrets: State Law (UTSA)**

“Trade secret” means information, including a formula, pattern, compilation, program, device, method, technique, or process, that:

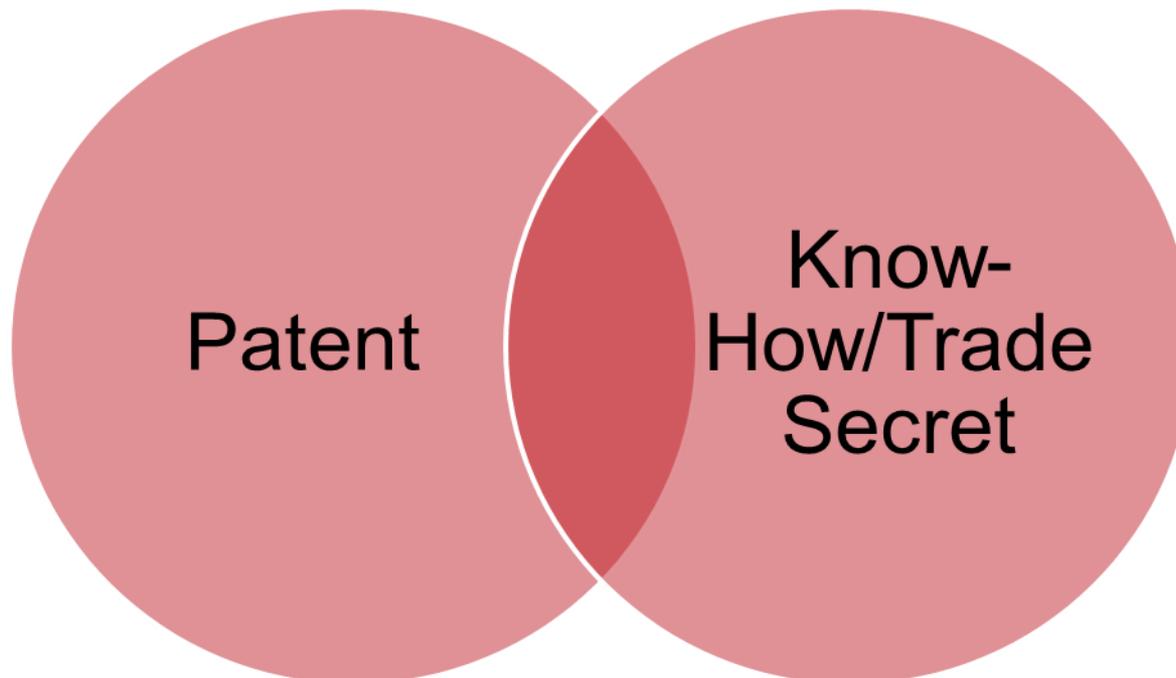
- (i) Derives independent economic value, actual or potential, from not being generally known to the public or to other persons who can obtain economic value from its disclosure or use; and
- (ii) Is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

- 47 states, including CA, adopted the Uniform Trade Secrets Act. States that did not adopt: MA, NY, NC.

Similarities When Licensing

Common provisions may include:

1. field of use,
2. territory,
3. exclusivity terms.



One Size Does Not Fit All

Tailor each license to the circumstances of the transaction:



- Scope of patents



- Complexity of the technology



- Importance of know-how to commercialization of the invention



- Are trade-secrets being licensed



- Field of use



- Value of the deal

Licensing Know-How

What is the most important objective of a know-how license?

- Including trade secrets.
- Defining the field of use.
- Defining the scope of the licensed know-how and how it will be transferred to the licensee.
- Ensuring that that the licensor retains the right to use the know-how even in the patent license is exclusive.

Scope of the Licensed Know-How

Information relating to the optimum commercial exploitation of the invention.

“**Know-How**” means unpatented, technical information, trade secrets, data, specifications, designs, procedures, studies, processes, or methods [*pertaining to the Licensed Patents*] [and] [*necessary/useful*] in the manufacture, sale or use of the Licensed Products [*that are useful in practicing the Licensed Patents*].

- Consider whether know-how has to be disclosed in writing.
- Consider whether to limit to know-how developed prior to the Effective Date of the Agreement or to include updates.
- Consider whether trade secrets will be licensed with the know-how.

Knowledge Transfer

The license agreement should address how the know-how will be provided to the licensee and whether the licensor will provide any implementation/support with respect to the know-how.



Know-How, Consulting and Training

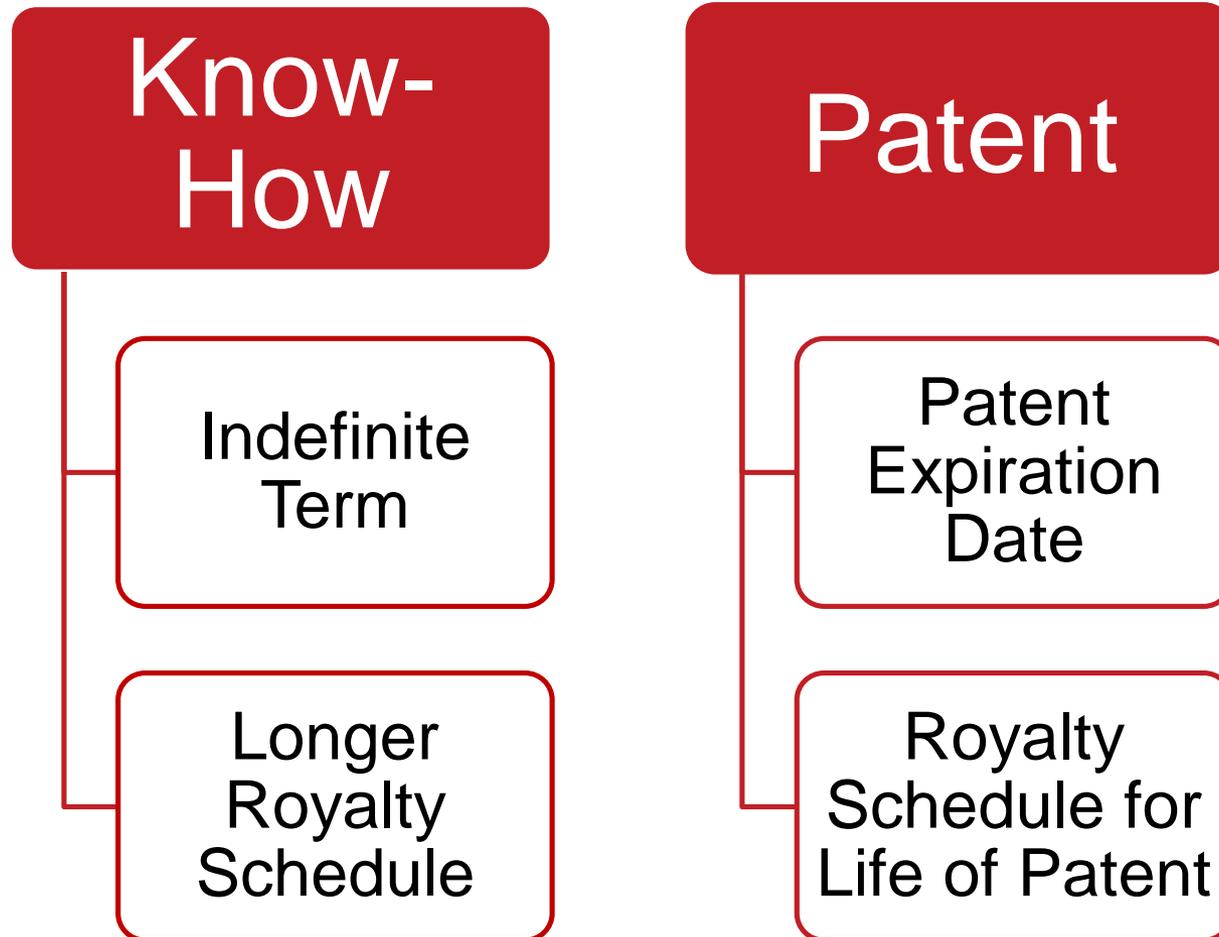
- Does the licensee need help from the licensor in terms of written documentation or materials that help the licensee understand how to use the technology?
- Does the licensee need the know-how of the licensor in order to exploit the technology?
- Does the licensee need or desire to have licensor personnel available to work with its employees?
- Who will own any IP results of such joint work?
- Will the licensee wish its employees to be trained by the licensor in the use of the technology? If so, how many hours?

Terms for Patents and Know-How

Why should know-how be licensed separately from patents?

- A. Differing Terms (length of the license).
- B. They are distinct forms of IP.
- C. Separate royalty schedules.
- D. Both A and C.

Differing Terms and Royalty Schedules

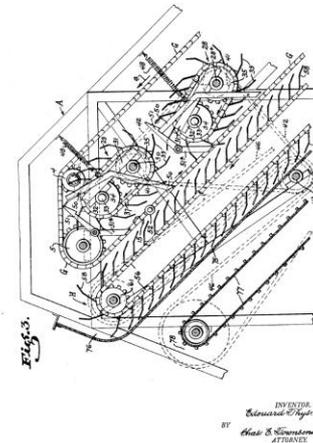


- License of know-how *is not* limited to the duration of the patent.



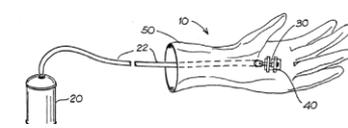
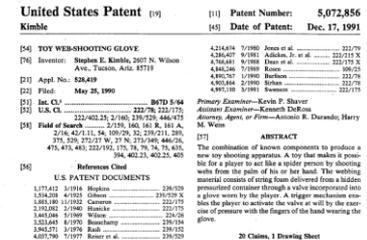
***Brulotte v Thys* 85 S. Ct. 176 (1964)**

- Thys sold a hop-picking machine to Brulotte that required pre- and post-patent royalty payments.
- Brulotte refused to pay post-patent royalty payments and Thys sued.
- The Court sided with Brulotte, holding that a royalty agreement that extends beyond the expiration date of the patent is unlawful *per se*.
- Thys, by charging the same rate and enforcing the same restrictions in the pre- and post-expiration periods, attempted to artificially extend the patent term.
- In response, the majority held that the patent terms were “[a] monopoly power in the post-expiration period when ...the patent has entered the public domain.”



Kimble v. Marvel 135 S. Ct 2401 (2015)

- Kimble was awarded U.S. Patent No. 5,072,856 for a toy comprised of a glove attached to a pressurized container containing foam string delivered to the glove by flexible tubing.



- Kimble met with Marvel Entertainment, makers of Spider-Man products, seeking to sell or license the ‘856 patent but the parties failed to execute a licensing agreement. Instead, Marvel began selling the “Web Blaster,” its own web-shooting glove, absent any license or contract.
- Kimble sued and was granted breach of contract, but not patent infringement.

***Kimble v. Marvel* 135 S. Ct 2401 (2015)**

- Both sides appealed and settled, with Kimble agreeing to sell Marvel the '856 patent for a \$500,000 lump sum and a three percent royalty on Marvel's future sales of the Web Blaster.
- The parties, unaware of *Brulotte*, set no end date for royalty, agreeing royalties would continue “for as long as kids want to imitate Spider-Man.”
- Marvel uncovered *Brulotte*, discovering that binding precedent meant prohibited royalty payments beyond the 2010 patent expiration
- The District Court agreed with Marvel that the “royalty provision was unenforceable after expiration of the Kimble patent.”
- The Court of Appeals for the Ninth Circuit reluctantly affirmed, criticizing *Brulotte* as “counterintuitive [with] rationale [that] is arguably unconvincing.”
- In response Kimble petitioned the Supreme Court to overrule *Brulotte* and certiorari was granted.

***Kimble v. Marvel* 135 S. Ct 2401 (2015)**

- Kimble argued that *Brulotte* should be overruled because 1) the holding rests on a mistaken view of the competitive effects of post-expiration royalties and 2) *Brulotte* suppresses technological innovation and as such harms the nation's economy.
- The Court, in a 6-3 decision, was not convinced a “special justification” or something significantly more than a belief “that the precedent was wrongly decided” was offered that justified overturning *Brulotte*.
- Kimble maintains precedent that licensing agreements cannot include royalty payments after patent expiration. Interestingly, although the Court appears to recognize that such a rule makes little sense, the majority was unwilling to challenge.
- Instead, the Court implied other types of “business arrangements” allowed for compensation to be paid in the post-patent expiration period.

***Kimble v. Marvel* 135 S. Ct 2401 (2015)**

- The Court offered three approaches for maximizing flexibility in negotiating patent licenses within the *Brulotte* framework.
 1. First, the Court noted, *Brulotte* permits parties to defer payments for pre-expiration use of a patent into the post-expiration period.
 2. Second, parties may tie post-expiration royalties to a non-patent right, which will not expire with the patent.
 3. Third, the Court pointed out, *Brulotte* leaves parties free to enter into business arrangements other than royalties that enable parties to share in the risks and rewards of commercializing a patented invention.

MARVEL



Know-How Term

Licensee's rights and obligations concerning the Licensed Know-How, shall continue:

- For [NUMBER] years after the Effective Date/the date of the first commercial use, sale, transfer or other disposition of Licensed Products; or
- Until such time as the Licensed Know-How ceases to be protectable as a trade secret or otherwise under applicable Law in such country other than as a result of any act or omission by or on behalf of Licensee.

How do you determine the royalty rate for the licensed know-how?

- A. It should be $\frac{1}{2}$ the patent royalty rate.
- B. It is an issue for commercial negotiation.
- C. It depends on the scope of the licensed know-how.
- D. It depends on the competitive advantage the know-how provides to the licensee.
- E. Both B and D.
- F. None of the above.



Capitalizing the Value of the Know-How

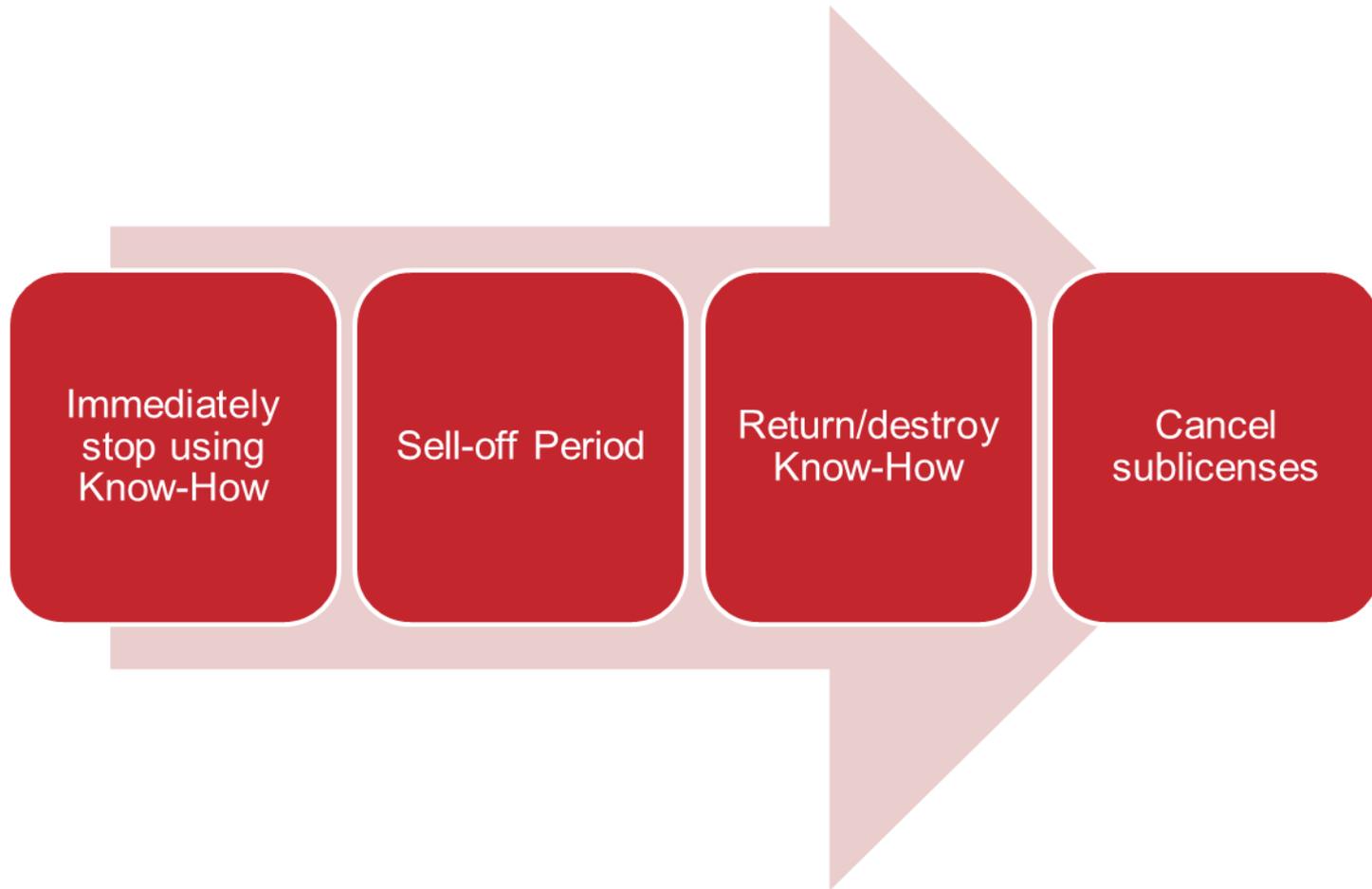
- Know-how provides a competitive advantage.
 - Royalty of X% on products covered by the Licensed Patents.
 - Royalty of X/2% on products that are only protected by the Licensed know-how, where “the manufacture of the Licensed Product used all or part of Licensed Know-how”, and for as long as the Licensed Know-How remains confidential.
- Should bear a reasonable relationship to the value of the know-how.
 - ✓ Manufacturing throughput
 - ✓ Product sales price
 - ✓ Cost savings



Royalties Post-Expiration Period

- *Brulotte* does not prevent collection of patent royalties in the post-patent expiration period.
- Royalty amortization can take the form of annual royalty payments, bonds, constant royalty amortization, and accelerated amortization payments.
- Amortization agreements require clearly defined financial details including deferral term, payment term, interest rates, deferment method utilized and amortization schedule in order to comply with *Brulotte*.
- Costs of royalty amortization and the long-term fiscal position of the licensee must be evaluated.

Termination Considerations



Important Provision

What provision must be included in a know-how license but is not integral to a patent license?



- Confidentiality
- Assignment
- Improvements
- Territory

Confidentiality

- Need to include protections for know-how, particularly if it includes trade secrets.
- Protections measures include security of the information, use, disclosure, and return/destruction upon termination.



Other Protections

Equitable Relief

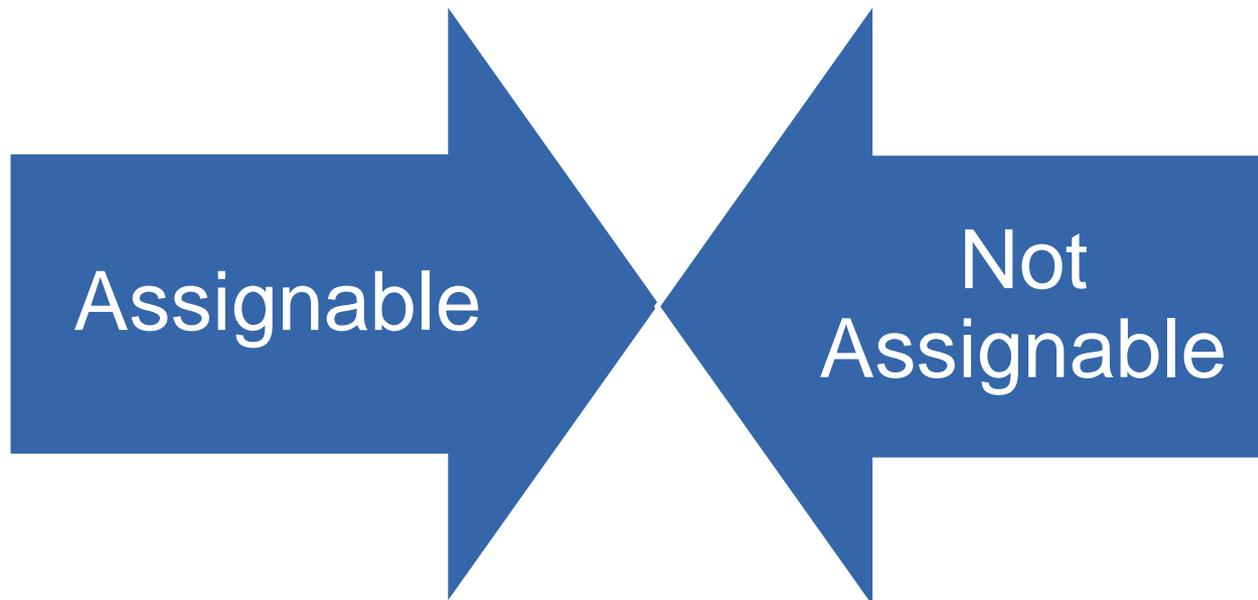


Limitations/Ownership
of Developments



Other limitations

If the license agreement is silent on the issue, know-how is?



Assignment

- Patents: the license is not assignable unless clearly stated otherwise.

- Know-how and trade secrets: ***no certain rule.***
 - Some courts find that the confidentiality provisions required in trade secret licenses prohibit assignability, even in a merger. *M.D. Mark, Inc. v. Kerr-McGee Corp.*, 565 F.3d 753, 761 (10th Cir. 2009).

 - Other courts find no assignment prohibition from confidentiality provisions alone. *Biosynexus, Inc. v. Glaxo Grp.*, 816 N.Y.S.2d 693 (Sup. Ct. 2006).

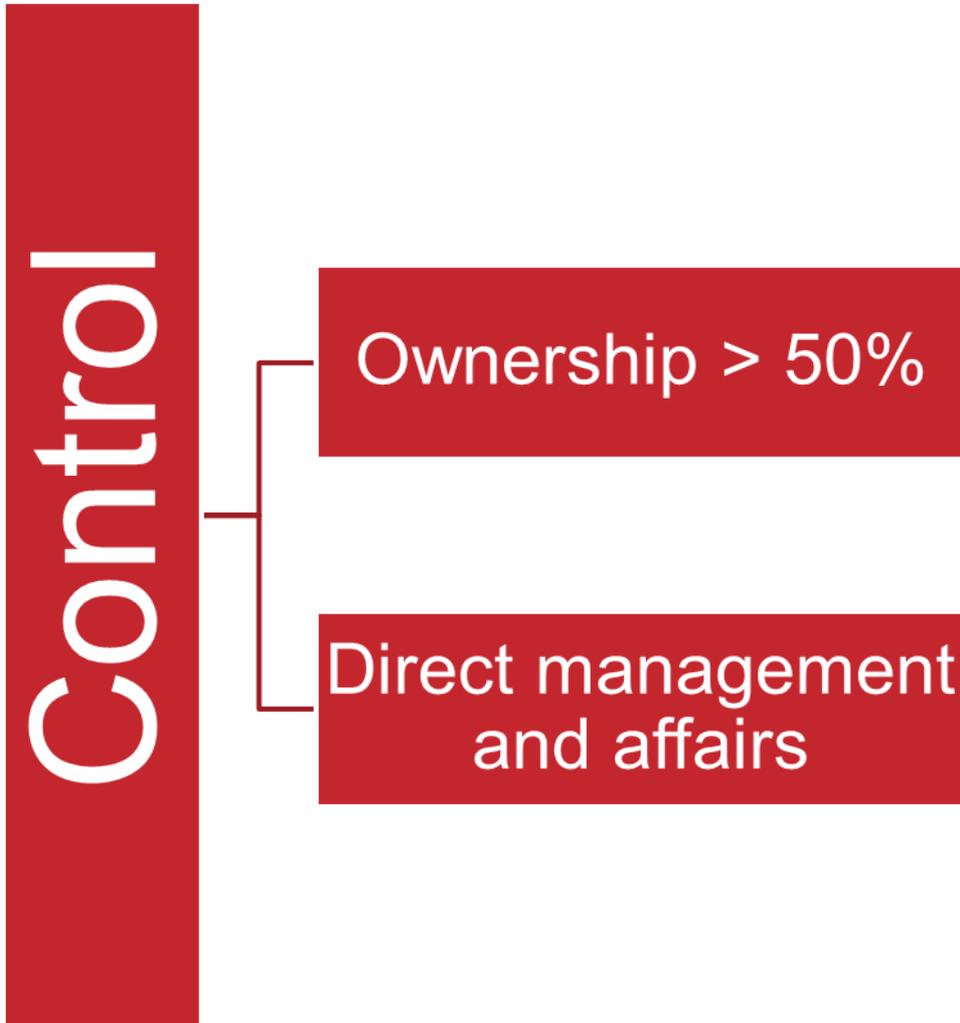
Assignment

- If the question is close, courts *may consider potential harm to the licensor*, such as loss of trade secret.
- “[I]f an assignment results merely from a change in the legal form of ownership of a business, its validity depends upon *whether it affects the interests of the parties protected* by the non-assignability of the contract.”
Trubowitch v. Riverbank Canning Co., 30 Cal. 2d 335, 344–45 (1947).

Assignment -Affiliates

- Licensors should *define the term “Affiliate”* narrowly in an agreement to restrict the license’s applicability or negotiate an expanded definition.
- For example, a *merger partner may not qualify as an affiliate* unless otherwise stated (probably a state corporate law issue, especially in California) *Superbrace, Inc. v. Tidwell, 124 Cal. App. 4th 388, 396 (2004)*.
- Licensors may also consider *establishing a window where third parties may become affiliates*, e.g. parties who merge with licensee in the agreement’s first two years qualify as affiliates.

Assignment-Change of Control



Questions?

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