Dangers in Joint Patent Ownership

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Obligations of parties in joint-ownership agreement must be unambiguously set out

Probably the worst thing anyone can do with a patent is divide ownership.

CO-OWNERS AT EACH OTHER'S MERCY

Title 35 U.S.C. § 262 provides, absent agreement to the contrary, a joint owner may use or license the patented invention without being held accountable to the other co-owner.[1] Courts have characterized each co-owner being at the other's "mercy." *Rail-Trailer Co. v. ACF Industries, Inc.*, 358 F.2d 15, 17 (7 Cir. 1966) citing *Talbot v. Quaker-State Oil Co.*, 104 F.2d 967, 968 (3 Cir. 1939); *Cilco, Inc. v. Copeland Intralenses, Inc.*, 614 F.Supp. 431, 434 (S.D.N.Y. 1985); *Bendix Aviation Corp. v. Kury*, 88 F.Supp. 243, 248 (E.D.N.Y. 1950); *Gibbs v. Emerson Electric Mfg.*, 29 F.Supp. 810, 812 (W.D.Mo. 1939).

One co-owner may provide a fully paid up license to the other co-owner's competitor and deprive its fellow co-owner of virtually all benefits from patent ownership including past damages, as discussed below.

Recently, the Federal circuit held a co-owner may grant licenses unilaterally that would deprive its co-owner of past damages, but licenses could not operate retroactively. *Schering Corp. v. Roussel-UCLAf SA*, 104 F.3d 341 (Fed. Cir. 1997).

The facts in *Schering* were fairly typical, a joint ownership agreement that "went south" and co-owners were then adverse. Schering and Roussel had agreed to divide a patent to settle a dispute. The agreement required the parties to undertake "jointly" enforcement actions to render "all reasonable assistance" to the other party (at 342-43).

Roussel then began negotiating a license with a third party, Zeneca. Schering learned about the negotiations and promptly filed suit against Zeneca. Roussel then licensed Zeneca.

Roussel's license to Zeneca included a provision that returned to Zeneca the $2,000,000 license fee if the license were held to be void, and an indemnity provision that required Rouseel to indemnify Zeneca if it were sued by Schering (at 346).

Schering argued its agreement with Roussel, provided for joint actions and "all reasonable assistance," prevented Roussel from granting licenses to third parties, like Zeneca, that effectively, destroyed the economic value of Schering's share of the patent. The court disagreed.

The court reasoned the license to Zeneca barred future damages and equitable relief but did not preclude Schering from obtaining damages for past infringement (but since Zeneca had not yet marketed the drug, there were no past damages; at 345-46).

The court held (at 346) the "reasonable assistance" obligation was in the nature of providing logistical assistance, documents, witnesses and so forth, but did not bar licenses.

Additionally, the court held Roussel's indemnity agreement with Zeneca and its agreement to refund the license fee were irrelevant to the license's interpretation. Those provisions recognized that courts might disagree with Roussel's view of the agreement. They were not a concession that Roussel was wrong.

Thus, *Schering* makes it plain co-owners could for business reasons (or perhaps vindictively within antitrust constraints), grant licenses while litigation was pending that would prevent co-owner plaintiffs from obtaining an injunction and damages that accrued after the date of the license. *Schering, supra*, 104 F.3d at 345. That license, however, cannot deprive the co-owner of any damages that accrued prior to the license. *Schering, supra*, 104 F.3d at 345.

Schering is consistent with a relatively long line of cases that hold there is no fiduciary relationship between joint owners, each is an independent entity that can pursue their own agenda regardless of any negative consequence to the other owner. *Drake v. Hall*, 220 F. 905 (7 Cir. 1914); see also *Talbot, supra*, 104 F.2d at, 968; *Bendix, supra*, 88 F.Supp. at 248.

JOINT OWNERS ARE/NOT INDISPENSABLE PARTIES

Frequently in litigation in which patents are jointly owned the question arises whether each co-owner is an indispensable party under Rule 19, F.R.Civ.P.

The answer is probably.

Some courts have held both co-owners are indispensable parties and have dismissed actions for lack of an indispensable party, others have overlooked the problem and have addressed the merits of the

1. 35 U.S.C. § 262 provides: "In the absence of any agreement to the contrary, each of the joint owners of a patent may make, use, offer to sell or sell the patented invention within the United States, or import the patented invention into the United States, without accounting to the other owners."

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suit. Compare *Cilco Inc. v. Precision-Cosmet, Inc.*, 624 F.Supp. 49, (D. Minn. 1985); *American Optical Company v. Curtiss*, 59 F.R.D. 644, 177 U.S.P.Q. 2d 726 (S.D.N.Y. 1973) with *International Business Machines Corp. v. Conner Peripherals Inc.*, 30 U.S.P.Q.2d 1315 (N.D. Cal. 1994); *Eickmeyer v. U.S.*, 231 U.S.P.Q. 820 (Cl.Ct. 1986); *Aberdeen Hosiery Mills Co. Inc. v. Kaufman*, 96 U.S.P.Q. 133 (S.D.N.Y. 1952).

The prevailing rule seems to be co-owners, like sole owners, are indispensable parties. The related questions is if all co-owners are indispensable parties, can an unwilling co-owner be joined as an involuntary plaintiff?

The involuntary plaintiff rule in patent litigation is generally thought to stem from the Supreme Court's holding in *Independent Wireless Telegraph Co. v. Radio Corporation of America*, 269 U.S. 459 (1926). In that case, the court held a patent owner could be joined as an involuntary plaintiff in a suit by its exclusive licensee, even if the court had no personal jurisdiction over the owner. This procedure is available if the owner was given notice of the action and refused to join.

This rule has been in effect for 70 years, some courts say codified in Rule 19 (see *Precision-Cosmet, supra,* 624 F.Supp. at 51), and has been applied in numerous decisions.

However, some courts have held this rule does not apply to situations where one co-owner seeks to join another co-owner, even if all parties are subject to the court's jurisdiction. Courts have given a variety of reasons, none in my view compelling, supporting holdings that co-owners cannot be joined involuntarily. *Cilco, Inc. v. Copeland Intralenses, Inc.*, 614 F.Supp. 431 (S.D.N.Y. 1985); *Precision Cosmet, supra,* 624 F.Supp. 49; *Bendix, supra,* 88 F.Supp. at 248, citing *Gibbs, supra,* 29 F.Supp. 810.

These decisions may be limited to the peculiar facts of the cases. In *Copeland*, the co-owners (Cilco and Jesen/Fetz) sued each other in prior pending litigation to resolve disputes over ownership. The ownership action was unresolved when the court addressed the joiner motion. The court in *Copeland* reasoned that Cilco could not join Jesen/Fetz because if Cilco were correct and it owned the entire patent, Jesen/Fetz would not be co-owners and would be strangers to the litigation. Thus, joinder would be improper. Alternatively, if Jesen/Fetz were owners, and Cilco was not, Cilco would be an infringer. Under either scenario, the court reasoned, it was inappropriate to join the warring co-owners.

The ruling, in part, is based on the open ownership dispute. The court determined, correctly, that joinder of co-owners would duplicate litigation concerning ownership that was already pending in another District Court.

The court in *Precision-Cosmet* took a slightly different tack, but reached the same result. That court held it was improper to join co-owners because they had conflicting positions. One co-owner argued the patents were invalid, the other supported validity. Under these circumstances the court held it was improper to join co-owners with differing positions as parties on the same side of an action. 624 F.Supp. at 52-53.

In *Gibbs*, the court simply held because of the "peculiar nature of a patent property" each owner is at the other's "mercy" and neither can compel the other to join. This, however, is relatively thin reasoning.

In *Bendix*, the court analyzed the dichotomy where a co-owner, a declaratory judgment defendant, could either license the patent to plaintiff or consent to a declaratory judgment (of invalidity or noninfringement) — but could not join an out-of-state co-owner and have the case adjudicated on the merits. In this case, the existence of co-owner worked a benefit to the owners by preventing a declaratory judgment action against them.

In *Aberdeen, supra,* 96 U.S.P.Q. 133, the court reached the opposite result. There, the court refused to dismiss a declaratory judgment action in which ownership had been purposefully divided to avoid the court's jurisdiction.

Aberdeen seems to be limited to its facts, *i.e.* to prevent parties from manipulating ownership during litigation to avoid jurisdiction. However, the holding is at least facilially inconsistent with *Bendix* (at 250):

> "If [a co-owner] would be an indispensable party to an action for infringement, he is nonetheless so in a declaratory judgment suit having for its objective a declaration that infringement does not exist, which is but the same thing in reverse."

After analyzing these opinions, there still seems to be no sound reason why a court with jurisdiction over a person cannot order that person to join an action, at least involuntarily. The court should be allowed to reach the merits. If the party decides not to participate that is its decision, but there is no question it will be bound by the judgment if it has notice of the action.

Interestingly, in *Kronos, Inc. v. AVX Corp.*, 23 U.S.P.Q. 2d 1972 (W.D.N.Y. 1992) (in dictum), the court cited *Copeland* for the proposition that Courts could join co-owners as involuntary plaintiffs. In *American Optical, supra,* 59 F.R.D. 648 n.5, the court noted, also in dictum, standards might be different if ownership rather than validity were at issue. The court suggested, if ownership were at issue, a co-owner might be able join another co-owner.

There is significant confusion on whether co-owner can be joined to infringement or declaratory judgment actions and uniform precedent is lacking. The majority of cases, however, hold one co-owner cannot join another.

If courts refuse to join co-owners, and dismiss patent actions unless all joint owners join voluntarily, jointly owned patents are at great risk of effectively becoming worthless. *Talbot, supra,* 104 F.2d 967. Those patents can never be asserted against any party unless all co-owners agree. That, in my view, takes section 262 to an unintended extreme.

Indeed, in *Schering* the court joined Roussel as an involuntary plaintiff and held neither party could unilaterally destroy the value of the patent. *Schering, supra,* 104 F.3d at 345.

From a policy perspective, the *Cilco* line of cases (including *Gibbs*) appear to be inconsistent with *Independent Wireless*. In *Independent Wireless*, an exclusive licensee was able to join the owner to pursue its claim against an infringer. Co-owners are owners. They plainly have greater ownership interests in patents than exclusive licensees, and perhaps greater economic investments at stake. It is anomalous to bar actions by co-owners, but to permit actions by nonowners. Co-owners should have more rights, not less. See generally *Bendix, supra*, 88 F.Supp. at 249 (discussing the incongruity of barring joinder of co-owners but, nevertheless adhering to the rule).

The *Cilco* cases might be harmonized with cases allowing joinder of co-owners by considering the underlying ownership dispute that existed in *Cilco* (in *Bendix*, there was a State Court action on appeal for unpaid royalties). In the *Cilco* cases, the courts refused to entertain the actions because neither party had clear title, and the court would have been required to resolve the ownership dispute before considering infringement and validity. A long line of cases hold Federal Courts do not have federal question subject matter jurisdiction to resolve ownership contests. *Beghin-Say Intern Inc. v. Rasmussen*, 733 F.2d 1568, 1571 (Fed. Cir. 1984) (Federal courts have "consistently held for over 130 years that contract disputes involving patents do not arise 'under any Act of Congress relating to patents.' " (citation omitted).

> "The general rule is that 'where a suit is brought on a contract of which a patent is the subject matter, either to enforce such contracts, or to annul it, the case arises on the contract, or out of the contract, and not under the patent laws.' " *Wade v. Lawder*, 165 U.S. 624, 627 (1897)(citations omitted).

In *Wade, supra*, 165 U.S. 624, the Supreme Court held contract disputes between co-owners did not raise questions arising under patent law. Contractual claims were properly resolved by State Courts.

Thus, the *Cilco* cases might be viewed as an extension of cases that hold patent ownership disputes do not "arise under any Act of Congress."

Recently, in *Arnold v. Hydrotech Systems, Inc.*, 109 F.3d 1567 (Fed. cir. 1997), the Federal Circuit held a plaintiff must come to court with patent ownership "in hand." Patent ownership disputes do not "arise under" any Act of Congress.

In *Arnold*, 109 F.3d at 1577, the Federal Circuit held:

> "[W]hen the infringement suit involves an assignment, unless the assignment may be declared null and void by operation of law — either through a forfeiture provision present in the agreement or under a provision of applicable state law — an assignee suing for infringement must first affirmatively seek equitable relief from a court to rescind or cancel the assignment. Until ownership is restored in the assignor, there can be no act of infringement by the assignee. Federal question jurisdiction must exist at the time the complaint is filed for a federal court to exercise authority over the case, and without first receiving equitable relief that restores to the assignor title to the patent, any claim of ownership by the assignor will be unfounded. (Citation omitted)."

To compound the problem, some courts have held standing must exist when the complaint is filed and defects in standing, for example where the plaintiff is not an owner, cannot be cured by later transfers or amendments. *Gaia Technologies, Inc. v. Reconversion Techologies, Inc.*, 93 F.3d 774 (Fed. Cir. 1996); *Switzer Brothers, Inc. v. Byrne*, 242 F.2d 909 (6 Cir. 1957); *Quiefen Company, Inc. v. Central Valley Builders Supply Company, Inc.*, 1993 U.S. Dist. Lexis 15238 (N.D. Cal. 1993) affirmed without published opinion 32 U.S.P.Q. 2d 1847 (Fed. Cir. 1994) compare *Proctor & Gamble Co. v. Paragon Trade Brands, Inc.*, 917 F.Supp. 305 (D. Del. 1995) (dismissing without prejudice).

In *Switzer*, the court held all co-owners must be plaintiffs at the commencement of the action and dismissed the action with prejudice.

Similarly, *Gaia*, the Federal Circuit held standing is determined when the complaint is filed, and subsequent transfers cannot cure defects.

> " 'As a general matter, parties should possess rights before seeking to have them vindicated in court. Allowing a subsequent assignment to automatically cure a standing defect would unjustifiably expand the number of people who are statutorily authorized to sue. Parties could justify the premature initiation of an action by averring to the court that their standing through assignment is imminent. Permitting non-owners and licensees the right to sue, so long as they eventually obtain the rights they seek to have redressed, would enmesh the judiciary in abstract disputes, risk multiple litigation, and provide incentive for parties to obtain assignments in order to expand their arsenal and the scope of litigation. Inevitably, delay and expense would be the order of the day.' " *Gaia, supra*, at 779-80 quoting *Procter & Gamble Co. v. Pargon Trade Brands, Inc.*, 917 F.Supp. 305 (D. Del. 1995); *see also Afros S.p.A. v. Krauss-Maffei Corp.*, 671 F.Supp. 1402, 1444 (D. Del. 1987) affirmed without opinion 848 F.2d 1244 (Fed. Cir. 1988).

Thus, if all co-owners do not file suit together, they risk dismissal with prejudice that will bar infringement claims against that defendant forever. This is another example of co-owner having fewer rights than licensees. A single co-owner, conceivably without other co-owner's knowledge, can effectively destroy any chance of recovery and injunctive relief for all co-owners by a single inartfully drafted complaint.

POSSIBLE CONTRACTUAL REMEDIES

Agree to Join Litigation

Contracts dividing patents must be unambiguous as each party's rights and obligations to the other. To avoid dismissal under the *Cilco* line of cases, which effectively destroys patents' value, parties should contractually agree to join actions voluntarily, or to permit one co-owner to sue on its own *Willigham, supra*, 555 F.2d 1340; *Michaels of Oregon v. Mil-Tech Inc.*, 38 U.S. P.Q. 1060 (D. Or. 1995); see also *Rawlings v. National Molasses Co.*, 394 F.2d 645 (9 Cir. 1968); *Schering, supra*, 104 F.3d at 344; cf. *Rail-Trailer Co., supra*, 358 F.2d 15.

Suitable provisions could be made to divide litigation costs according to some predetermined formula, to determine which if either party is the "lead," who selects counsel, and discovery provisions, *e.g. Willigham, supra*, 555 F.2d 1340.

The parties should agree in advance to the method in which proceeds from the litigation are divided. Co-owners unwilling to share litigation cost equally might agree to share costs and to divide proceeds on a pro rata basis.

The danger of not agreeing to join in advance are profound, as demon-

strated by the Cilco cases and others where the action was dismissed.

Other Provisions

Co-owners could agree to a preset amount to buy out the other co-owner's stake, if one party wanted to litigate and the other party refused. Such a provision could be made mandatory, if for example one co-owner refused to litigate, the other could buy out that co-owner's share at a set amount. This would help avoid the pitfalls set out above by uniting all ownership interests in one party.

Another possibility would be to convert the co-ownership agreement into an exclusive license, with suitable provisions that permitted the exclusive licensee to sue. In this situation, *Independent Wireless* permits the exclusive licensee to join the owner — again highlighting the logical inconsistency of the rule barring joinder of co-owners. If parties could easily remedy the standing problem by reformatting the agreement, there seems to be no reasons for this "hard and fast" rule. See also *Bendix, supra,* as F.Supp. at 249-50.

Choice of Law and Choice of Forum

Choice of law and choice of forum clauses in joint patent ownership agreements may be more important than in routine contracts.

Permitting joint owners to have a free rein seems to be unique to United States law. The law in France, for example, is quite different. French Intellectual Property Law Section 613-29 provides a regime in which joint owners are to treat each other more in the nature of joint venturers under U.S. law. Under that statute, neither joint owner may transfer its share in a way that would undermine the other owner's rights.[2]

Thus, in international transactions choosing which law will be applied in the event of a dispute can be dispositive.

RES JUDICATA

As a practical matter, *res judicata* principles will affect a co-owner, whether or not it agrees to join (assuming the case goes forward). If the patent were held invalid, the absent co-owner would be bound by that holding as a matter of law. *Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation,* 402 U.S. 1434 (1971); *Talbot, supra,* 104 F.2d 967. Similarly, if the patent is held valid and infringed, and the litigation co-owner is awarded damages, it seems extremely unlikely that a court would permit an absent co-owner to sue the same defendant again for damages.

CONCLUSION

Joint patent ownership is fraught with problems and should only be considered as a last resort.

If parties must divide ownership, each party's rights, in particular its obligations in the event of litigation, must be unambiguously set out. To give either party the right to sue, the underlying agreement must expressly permit each co-owner to sue individually, or must include a provision that requires each co-owner to join. The risk of not including this type of provision is an unenforceable patent.

2. In *Pfizer Inc. v. Elan Pharmaceutical Research Corp.* 812 F.Supp. 1352, 1370 n. 24 (D. Del. 1993), the court held foreign law could apply to license provisions, but standing in U.S. Courts was determined under U.S. law.