

Licensee Patent Validity Challenges Following *MedImmune*: Implications for Patent Licensing[©]

by ALFRED C. SERVER AND PETER SINGLETON**.

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· Partner, Wilmer Cutler Pickering Hale and Dorr LLP, fred.server@wilmerhale.com.

** Graduated Hastings College of the Law, *summa cum laude*, 2008,
petersingleton@earthlink.net.

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I. INTRODUCTION

In *MedImmune v. Genentech*,¹ the U.S. Supreme Court resolved a jurisdictional question in concluding that the case or controversy requirement of Article III of the U.S. Constitution does not require that a patent licensee terminate or be in breach of its license agreement before seeking a declaratory judgment that the licensed patent is invalid, unenforceable or not infringed. The Court's decision overruled the Federal Circuit's holding in *Gen-Probe v. Vysis*² that had established a jurisdictional barrier to a patent validity challenge by a nonrepudiating licensee in good standing with respect to its license agreement. The U.S. Supreme Court's *MedImmune* holding, however, raised questions as to the current status of the common law doctrine of licensee estoppel. According to the doctrine, a licensee operating under a patent license agreement and enjoying its benefits is estopped from challenging the validity of the licensed patent. In *Lear v. Adkins*,³ the U.S. Supreme Court had rejected the doctrine of licensee estoppel in the context of a licensee that had ceased paying royalties due under a patent license agreement on the basis of the licensee's contention that the licensed patent application could not issue as a valid patent. The question brought into sharp focus by the Court's *MedImmune* holding was whether the *Lear* Court's rejection of licensee estoppel extends to the nonrepudiating licensee in good standing, an issue addressed but not resolved by the Court in *MedImmune*.

The *MedImmune* Court's elimination of the jurisdictional barrier to a patent validity challenge by a licensee in good standing has been viewed by many as a pronounced shift in favor of the licensee in the balance of rights between licensor and licensee in patent license agreements. Moreover, the Court's ruling has given rise to a dilemma for patent licensors, namely, how to redress the shift in the balance of rights. Specifically, the questions to be answered are as follows: (1) Is there a vestige of the doctrine of licensee estoppel to protect a patent licensor from a validity challenge by a licensee in good standing, and (2) if one cannot rely on the doctrine, are explicit contract provisions that prohibit, reduce the incentive for, and/or

1. 549 U.S. 118 (2007).
2. 359 F.3d 1376 (2004).
3. 395 U.S. 653 (1969).

specify a consequence of, a licensee's challenge of the validity of a licensed patent enforceable?

This Article addresses the legal basis for resolving the licensor's dilemma following *MedImmune*. Part II of this Article discusses the Supreme Court's *MedImmune* holding and its implications for interpreting the legality of a patent validity challenge by a licensee in good standing. A review of the *MedImmune*'s Court's decision reveals a skepticism as to whether contract law can be relied on to prevent a patent validity challenge by a nonrepudiating licensee. As noted above, however, the *MedImmune* holding settled the jurisdictional question before the Court, but did not resolve the merits-based contract arguments against a patent validity challenge by a licensee in good standing. In particular, the Court was clear in its refusal to opine on the question of whether the Court's rejection of the doctrine of licensee estoppel in *Lear* was so broad as to cover a nonrepudiating licensee. In Part III of this Article we argue that the answer to that question is to be found in an analysis of the *Lear* decision itself. The holding in *Lear* and the Court's reasoning in support of its holding provide an adequate basis for assessing the scope of *Lear*'s rejection of licensee estoppel. We begin our argument with a brief history of the doctrine of licensee estoppel, which is essential to an understanding of the impact of the *Lear* holding. We then review the seminal U.S. Supreme Court decisions addressing licensee estoppel through the last decision of the Court in support of the doctrine, *Automatic Radio v. Hazeltine Research*.⁴ The *Lear* Court cited certain of these prior decisions regarding licensee estoppel as evidence that the doctrine had been sufficiently eroded over time to justify its rejection. We next provide a detailed discussion of the facts and the holding in *Lear*, and the public policy rationale relied on by the U.S. Supreme Court in deciding the case. We end our analysis of the scope of the *Lear* decision by reviewing relevant post-*Lear* case law, including a Supreme Court case that provided an interpretation of the holding, regional circuit and district court decisions—the majority of which aggressively applied the *Lear* public policy argument to encourage patent validity challenges by licensees—and the Federal Circuit's subsequent efforts to limit the applicability of the *Lear* decision. We conclude that if and when the issue is presented, the U.S. Supreme Court will interpret its prior *Lear* holding as having rejected the doctrine of licensee estoppel without limitations imposed by the particular facts

4. 339 U.S. 827 (1950).

in the case. According to this view, and despite Federal Circuit dictum to the contrary,⁵ a patent licensee may challenge the validity of the licensed patent even if it neither repudiates nor terminates its patent license agreement and intends to continue to reap the benefits provided pursuant to the agreement.

In Part IV of this Article, we argue that in light of the U.S. Supreme Court's elimination in *MedImmune* of the Federal Circuit's procedural bar to a patent validity challenge by a licensee in good standing and the broad scope of the *Lear* court's repudiation of the doctrine of licensee estoppel, a patent licensor would be ill-advised to rely on some vestige of the common law doctrine of licensee estoppel to prevent such a challenge. Rather, the concerned licensor should consider introducing explicit contractual provisions in the patent license agreement to account for the increased likelihood of a patent validity challenge by its licensee. The question then becomes which provisions are enforceable and, if not clearly enforceable, which are least likely to give rise to unintended consequences, including a reasonable claim of patent misuse. Part IV, therefore, explores the enforceability and effects of explicit contractual protections of the licensor. Recognizing the diversity of pro-licensor contract provisions that have been and will be introduced by creative patent licensors, Part IV provides an analytical framework to be used in assessing the potential benefits and risks of any such contract provision. A limited number of frequently encountered contract provisions are then analyzed through application of the proposed framework. Part IV concludes that certain pro-licensor clauses (e.g., one that constitutes an absolute bar to a patent validity challenge by a licensee in the context of a typical license agreement) are unenforceable, with some approaching patent misuse. Other provisions (e.g., one that results in an adjustment of contract terms following a failed validity challenge by a patent licensee) are likely to be enforceable. And some contract provisions (e.g., one that permits a patent licensor to terminate the license agreement in the event of a licensee patent validity challenge) fall within a gray zone where a finding of patent misuse is unlikely, but the question of enforceability will remain open until finally resolved by a court. The licensor inclined to incorporate such a provision will need to be advised of the risk of unenforceability, a risk that increases to the extent that the provision appears to penalize a licensee for a patent validity challenge in a manner and to a degree that is likely to

5. *Studiengesellschaft Kohle v. Shell Oil*, 112 F.3d 1561, 1568 (Fed. Cir. 1997).

prevent a challenge in the first place and, thereby, frustrates the important public interest expressed in *Lear* of eliminating worthless patents.

II. *MEDIMMUNE V. GENENTECH* AND THE NONREPUDIATING LICENSEE IN GOOD STANDING

In the minds of many, the U.S. Supreme Court's decision in *MedImmune v. Genentech* is as significant for the questions that it raised but did not answer as for its holding. The Court in *MedImmune* resolved a jurisdictional issue, namely that a patent licensee need not terminate nor be in breach of its license agreement to meet the case or controversy requirements of Article III of the U.S. Constitution to bring a declaratory judgment action challenging the validity, enforceability or scope of the licensed patent. With its holding, the *MedImmune* Court rejected the Federal Circuit's procedural bar (established in *Gen-Probe*) to a patent validity challenge by a patent licensee who remains in good standing under its license agreement. In so doing, however, the Court brought to the fore two substantive questions of law that had been largely irrelevant in light of the Federal Circuit's procedural bar, but that now require answers. First, are there contract-based arguments that a patent licensor can make to block a patent validity challenge by a licensee in good standing? And second, is an explicit contractual provision that prohibits or discourages a validity challenge by such a licensee enforceable, and will the inclusion of such a provision in a patent license agreement have unintended consequences, such as giving rise to a reasonable claim of patent misuse? Justice Scalia, writing for the Court in *MedImmune*, discussed some of the substantive contract arguments against a patent validity challenge by a licensee in good standing raised by respondent Genentech, but did not rule on these arguments. He did express doubts as to the merits of the arguments, and his skepticism, coupled with his refusal to decide the contract questions presented in the case, only added to the uncertainty generated by the Court's *MedImmune* decision for prospective patent licensors and licensees.

In this Part II of the Article, we provide a brief review of the facts in *MedImmune* and a summary of the Court's jurisdictional holding. We then discuss the contract-based arguments raised in the case, but not resolved by the Court. Finally, we conclude with a statement of the dilemma faced by a patent licensor post-*MedImmune* with respect to a potential patent validity challenge by

a licensee in good standing. As will be made clear in this Part II, resolution of the licensor's dilemma, made all the more necessary by the *MedImmune* holding, is not to be found through an analysis of *MedImmune*, but requires a review (as provided in Part III of this Article) of the history of the doctrine of licensee estoppel and of relevant pre-*MedImmune* U.S. case law, in particular the Court's seminal holding in *Lear v. Adkins*.

A. Holding of the U.S. Supreme Court in *MedImmune*

Petitioner MedImmune is a biotechnology company developing antibody products⁶ for use in the prevention or treatment of infectious diseases. Its largest selling product, Synagis, is a humanized antibody⁷ used to prevent respiratory tract disease in infants and young children.⁸ Sales of Synagis have accounted for more than 80% of MedImmune's revenues since 1999.⁹

In the early 1980s, Genentech and its co-inventor City of Hope did pioneering work on the production of therapeutic monoclonal antibodies using recombinant DNA technology.¹⁰ In 1983, Genentech and City of Hope applied for a patent which was issued in 1989.¹¹ This patent, known as the "Cabilly I patent" after its inventor, Shmuel Cabilly,¹² covered basic techniques for producing chimeric heavy and light immunoglobulin chains that make up a chimeric antibody molecule.¹³ In 1988, Genentech filed a continuation of the Cabilly I application on behalf of itself and City

6. An antibody is a protein produced by the immune system in response to a disease-causing antigen. Antibody molecules are composed of heavy and light immunoglobulin polypeptide chains. Antibodies are specific to a given antigen, and as a result, are an essential part of the body's immune response system. Antibodies produced by genetically altered cells using recombinant DNA technology represent a large percentage of the products currently marketed by the biotechnology industry.

7. Most marketed antibodies are "humanized" antibodies. Humanized antibodies are genetically engineered from nonhuman and human components. Utilizing non-human components, particularly from mouse antibodies, enables rapid development of antibody variants. Adding human components increases the eventual antibody's therapeutic effectiveness and reduces the possibility the body will reject the antibody itself as a foreign antigen.

8. *MedImmune*, 549 U.S. at 121.

9. *Id.* at 122.

10. Brief for Respondent at *1-2 *Medimmune*, 549 U.S. 118 No. 05-608. [hereinafter "City of Hope brief"].

11. *Id.* at *2.

12. Brief for Petitioner at *3 *Medimmune*, 549 U.S. 118 No. 05-608. [hereinafter "MedImmune's brief"].

13. *Id.* (Chimeric antibodies are genetically-engineered monoclonal antibodies "containing a relatively high proportion of animal to human components.").

of Hope (the Cabilly II application), which contained new claims that covered the coexpression of heavy and light immunoglobulin chains in the same cell to produce an assembled monoclonal antibody molecule. The subject matter claimed in the Cabilly II application was the same as that claimed in a patent application that had been filed by Celltech in 1984.¹⁴ As anticipated by Genentech, the filing of the Cabilly II application triggered a patent interference proceeding against Celltech before the U.S. Patent and Trademark Office (PTO).¹⁵ After a protracted administrative action before the PTO, and subsequent litigation in federal court, Genentech and Celltech settled their priority dispute and Genentech was issued the Cabilly II patent with broad claims covering the coexpression technology for producing assembled monoclonal antibodies.¹⁶

While MedImmune was still developing its Synagis product, it sought a license from Genentech for the Cabilly I patent, as well as for any patent issuing from the then-pending Cabilly II application.¹⁷ The license agreement between Genentech and MedImmune was signed in 1997.¹⁸ In 2001, after the Cabilly II patent issued, Genentech notified MedImmune of its conclusion that Cabilly II was infringed by Synagis, and that royalties were due under the 1997 license agreement.¹⁹ MedImmune responded that it believed the Cabilly II patent was invalid, and that, in any event, Synagis did not use the invention claimed in Cabilly II. MedImmune proceeded to pay royalties, stating it was doing so under protest, and brought a declaratory judgment suit asking for a judicial determination that the Cabilly II patent was invalid, unenforceable or not infringed by the Synagis product.

14. City of Hope brief at *2-3; MedImmune's brief at *4.

15. City of Hope brief at *3; MedImmune's brief at *5.

16. While not essential to the disposition of the case, the Supreme Court was undoubtedly aware that the Cabilly II patent arguably covers foundational techniques essential to a broad category of biotechnology products both on the market and under development, and it confers a right to exclude to Genentech for 17 years from issue—until 2018—for inventive work by Genentech and City of Hope from the early 1980s, almost 40 years prior to the expiry of the patent grant. *See* MedImmune's brief at *5-6.

17. *Id.* at *3-4.

18. *Id.*

19. According to MedImmune, "[w]hen Synagis® became available in September 1998, MedImmune concluded that respondents' Cabilly I patent—which dealt with chimeric, rather than humanized, antibodies—did not cover Synagis®, so that Synagis® was not a "Licensed Product" under the 1997 license Accordingly, MedImmune never paid any royalties to Genentech under the 1997 license of the Cabilly I patent for sales of Synagis® The Cabilly I patent expired March 28, 2006." *Id.* at *4.

During the pendency of MedImmune's suit in the district court, the Federal Circuit issued its opinion in *Gen-Probe v. Vysis*.²⁰ In *Gen-Probe*, the Federal Circuit held that a nonrepudiating licensee in good standing did not meet the case or controversy requirement of the U.S. Constitution to bring a declaratory judgment suit for non-validity.²¹ The *MedImmune* district court, while questioning the *Gen-Probe* rule,²² nonetheless acknowledged that *Gen-Probe* was binding, and granted Genentech's motion to dismiss for lack of subject matter jurisdiction.²³ The Federal Circuit, also citing *Gen-Probe*, affirmed.²⁴ The Supreme Court granted certiorari limited to the question of whether a nonrepudiating licensee in good standing was barred by the case or controversy requirement of Article III of the U.S. Constitution from bringing a declaratory judgment suit challenging the validity, enforceability or scope of the licensed patent.²⁵

The Supreme Court, in an eight to one decision, held that a nonrepudiating licensee could allege a sufficient case or controversy to bring such a declaratory judgment suit. Justice Scalia, writing for the majority, crafted the following argument in support of the Court's holding. He first cited *Aetna Life Insurance Co. v. Haworth*,²⁶ in which the U.S. Supreme Court concluded that the phrase "case of actual controversy" in the federal Declaratory Judgment Act refers to the type of "Cases" and "Controversies" that are justiciable under Article III of the U.S. Constitution.²⁷ He then addressed the standard that a declaratory judgment action must meet to satisfy the Article III case or controversy requirement. "Basically, the question . . . is whether the facts alleged, under all the circumstances, show that there is a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment."²⁸

According to Justice Scalia, that requirement would certainly have been satisfied in the instant case if MedImmune had ceased

20. 329 F.3d 1376.

21. *Id.*

22. *MedImmune*, 549 U.S. at 136 ("despite its 'serious misgivings' about the Federal Circuit's rule, [the District Court] considered itself bound to dismiss by *Gen-Probe*").

23. *Id.* at 122.

24. *MedImmune Inc. v. Genentech Inc.*, 427 F.3d 958 (Fed. Cir. 2005).

25. *MedImmune*, 549 U.S. at 120-21.

26. 300 U.S. 227 (1937).

27. *MedImmune*, 549 U.S. at 126-27.

28. *Id.* at 127 (quoting *Md. Cas. Co. v. Pac. Coal & Oil Co.*, 312 U.S. 270, 273 (1941)).

making royalty payments under its 1997 license agreement. It was MedImmune's decision to continue to meet its royalty obligations, albeit under protest, and thereby deprive Genentech of a basis for terminating the license agreement and for enjoining future sales of MedImmune's Synagis product, that created the jurisdictional question presented to the Court. "[T]he continuation of royalty payments makes what would otherwise be an imminent threat at least remote, if not nonexistent."²⁹

Justice Scalia then turned to the central question of whether a dispute can qualify as a case or controversy within the meaning of Article III if the risk of imminent threat of harm to a declaratory judgment plaintiff is eliminated by the plaintiff's own acts, as in the *MedImmune* case. Citing U.S. Supreme Court precedent, he noted that in the context of a threatened action by the *government*, the Court has not required a plaintiff to expose himself to liability prior to bringing a legal action to challenge the basis for the threat. "In each of . . . [the cited] cases . . . , the plaintiff had eliminated the imminent threat of harm by simply not doing what he claimed the right to do That did not preclude subject-matter jurisdiction because the threat-eliminating behavior was effectively coerced."³⁰ Justice Scalia next addressed the situation in which the self-avoidance of a declaratory judgment plaintiff is in response to the imminent threat of harm from a *private party*, such as a patent licensor as in *MedImmune*, and not the government. He cited *Altwater v. Freeman*,³¹ a U.S. Supreme Court case with significant parallels to *MedImmune* that involved a declaratory judgment claim of patent invalidity, for the proposition that "a licensee's failure to cease its payment of royalties did not render nonjusticiable a dispute over the validity of the patent."³² Justice Scalia concluded that the source of the imminent threat of harm (private party as opposed to government) does not alter the jurisdictional analysis and that, quoting the *Altwater* Court, "the requirements of [a] case or controversy are met where payment of a claim is demanded as of right and where payment is made, but where the involuntary or coercive nature of the exaction preserves the right to recover the sums paid or to challenge the legality of the claim."³³

29. *Id.* at 128.

30. *Id.* at 129.

31. 319 U.S. 359 (1943).

32. *MedImmune*, 549 U.S. at 130.

33. *Id.* at 131 (quoting *Altwater*, 319 U.S. at 365).

The Federal Circuit in *Gen-Probe* had distinguished the *Altvater* holding on the ground that in *Altvater* the royalty was paid by the challenging licensee under compulsion of a court-imposed injunction decree, rather than at the election of the licensee in order to preserve its patent license, as in *Gen-Probe* (and in *MedImmune*). Justice Scalia rejected this distinction, however, in stating that

contrary to the Federal Circuit's conclusion, *Altvater* did not say that the coercion dispositive of the case was governmental, but suggested just the opposite. The opinion acknowledged that the licensees had the option of stopping payments in defiance of the injunction, but explained that the *consequence* of doing so would be to risk "actual [and] treble damages in infringement suits" by the patentees. 319 U.S., at 365, 63 S.Ct. 1115. It significantly did not mention the threat of prosecution for contempt, or any other sort of governmental sanction.^{34, 35}

Justice Scalia concluded his jurisdictional analysis in *MedImmune* by stating that "[t]he rule that a plaintiff must . . . risk treble damages and the loss of 80 percent of its business, before seeking a declaration of its actively contested legal rights finds no support in Article III,"³⁶ and, accordingly, "petitioner was not required, insofar as Article III is concerned, to break or terminate its 1997 license agreement before seeking a declaratory judgment in federal court that the underlying patent is invalid, unenforceable, or not infringed."³⁷

34. *Id.* at 132.

35. In footnote 11 to his majority opinion in *MedImmune*, Justice Scalia commented that even if *Altvater* could be distinguished from *Gen-Probe* (and *MedImmune*) on the basis of the former being an "injunction" case, that would not provide support for the Federal Circuit's *Gen-Probe* holding, which relied on that court's "reasonable apprehension of suit" test for determining whether a declaratory judgment action meets the Article III case or controversy requirement. "A licensee who pays royalties under compulsion of an injunction has no more apprehension of imminent harm than a licensee who pays royalties for fear of treble damages and an injunction fatal to his business." Moreover, he criticized the Federal Circuit's reasonable-apprehension-of-suit test as in conflict with the U.S. Supreme Court's decision in *Maryland Casualty Co.*, 312 U.S. at 273, *Aetna Life Insurance Co.*, 300 U.S. at 239 and *Cardinal Chemical Co. v. Morton International, Inc.*, 508 U.S. 83, 98 (1993). *Id.* at 132.

36. *Id.* at 134.

37. *Id.* at 137.

B. Issues Not Decided In *MedImmune*

The *MedImmune* holding settled the jurisdictional question before the Court. It did *not* rule on the merits of Genentech's contract-based arguments against a patent validity challenge by a licensee in good standing. In particular, the Court was clear in its refusal to opine on the question of whether the Court's repudiation of the doctrine of licensee estoppel in *Lear v. Adkins* was so broad as to cover a nonrepudiating licensee. Justice Scalia, however, did address the contract-based arguments in his opinion for the Court, expressing skepticism as to their merits. In this section we provide a summary of the contract issues discussed but not resolved in the *MedImmune* decision.

Justice Scalia structured his opinion in *MedImmune* by first determining that there was a dispute between the parties in the case and then addressing the question (discussed above) of whether a federal court had subject matter jurisdiction to hear the case. He acknowledged that, having established the existence of a dispute, defining the nature of the dispute was not essential to his jurisdictional holding.³⁸ Nonetheless, he proceeded to do so and it was in that context that he first addressed a contract-related question. Genentech had argued that the case only involved a patent invalidity claim and not a contract-based claim that no royalties were due under the license agreement because of patent invalidity and noninfringement. Genentech had provided the following reasons in support of its contention that the case did not involve a contract claim: "(1) because there is no dispute that Synagis infringes the Cabilly II patent, thereby making royalties payable; and (2) because while there is a dispute over patent validity, the contract calls for royalties on an infringing product whether or not the underlying patent is valid."³⁹

On review of the record before the Court, Justice Scalia concluded that *MedImmune* had indeed alleged a contract claim. He dismissed the first reason offered by Genentech as inconsistent with the allegation of the petitioner's complaint; *MedImmune* had stated in unequivocal terms that the sale of its Synagis product did not infringe the Cabilly II patent. With respect to Genentech's second reason, Justice Scalia noted that *MedImmune* had made the

38. *Id.* at 123 ("At the onset, we address a disagreement concerning the nature of the dispute at issue here That probably makes no difference to the ultimate issue of subject-matter jurisdiction, but it is well to be clear about the nature of the case before us.").

39. *Id.* at 123.

nonfrivolous contention that “it had no obligation under the license to pay royalties on an invalid patent,”⁴⁰ i.e., that, contrary to the position taken by Genentech, the validity of the Cabilly II patent had a direct and immediate bearing on MedImmune’s obligation to pay the royalties sought by Genentech under the license agreement. As recognized by Justice Scalia, “the license requires petitioner to pay royalties *until* a patent claim has been held invalid by a competent body, and the Cabilly II patent has not. But the license at issue in *Lear, Inc. v. Atkins*, 395 U.S. 653, 673 . . . (1969), similarly provided that “royalties are to be paid until such time as the ‘patent . . . is held invalid,’” and we rejected the argument that a repudiating licensee must comply with its contract and pay royalties until its claim is vindicated in court.”⁴¹

At this point in his opinion, Justice Scalia presented the following disclaimer, reflecting his conclusion that the jurisdictional issue before the Court did not require a ruling on the merits of the contract-based arguments and that he did not intend to provide one:

We express no opinion on whether a *nonrepudiating licensee* is similarly relieved of its contract obligation [i.e. its obligation to pay royalties under the contract] during a successful challenge to a patent’s validity—that is, on the applicability of licensee estoppel under these circumstances. Cf. *Studiengesellschaft Kohle, M.B.H. v. Shell Oil Co.*, 112 F.3d 1561, 1568 (C.A.Fed.1997) (“[A] licensee . . . cannot invoke the protection of the *Lear* doctrine until it (i) actually ceases payment of royalties, and (ii) provides notice to the licensor that the reason for ceasing payment of royalties is because it has deemed the relevant claims to be invalid”). All we need determine is whether petitioner has alleged a contractual dispute. It has done so.⁴²

We will revisit the above-quoted language later in this Article.⁴³ For purposes of this section, suffice it to say that, while Justice Scalia was not prepared to apply the Court’s *Lear* holding to a nonrepudiating licensee in good standing such as MedImmune, he rejected Genentech’s claim that the expressed contractual intent of

40. *Id.* at 124.

41. *Id.*

42. *Id.* at 124–25.

43. See *infra* section III.C.4.c.iv.

the parties had already settled the alleged contract dispute in the case. In the view of Justice Scalia and the majority of the Court, there remained a question as to MedImmune's obligation to pay royalties for use of a potentially invalid and challenged patent, despite an explicit contractual provision requiring MedImmune to pay until the licensed patent had been held invalid by a court or other competent body.

Having established the existence of a contract dispute, Justice Scalia returned to a discussion of Genentech's contract-based arguments following his analysis of the jurisdictional issue before the Court. Genentech had offered an "insurance-policy" justification in support of its contention that a nonrepudiating licensee in good standing does not have a right to challenge the validity of the licensed patent. As restated by Justice Scalia, the Genentech argument was as follows:

When a licensee enters . . . [a patent license] agreement, . . . it essentially purchases an insurance policy, immunizing it from suits for infringement so long as it continues to pay royalties and does not challenge the covered patents. Permitting it to challenge the validity of the patent without terminating or breaking the agreement alters the deal, allowing the licensee to continue enjoying its immunity while bringing a suit, the elimination of which was part of the patentee's *quid pro quo*.⁴⁴

While not ruling on Genentech's contract arguments, Justice Scalia expressed doubts as to their merits. He first questioned the contention that a prohibition against a patent validity challenge by a licensee in good standing could be implied from the wording of the license agreement itself. "Promising to pay royalties on patents that have not been held invalid does not amount to a promise *not to seek* a holding of their invalidity."⁴⁵ He then addressed Genentech's "appeal to the common-law rule that a party to a contract cannot at one and the same time challenge its validity and continue to reap its benefits."⁴⁶ According to Genentech, since the licensee in *Lear* had repudiated its license agreement and, thereby, rejected the agreement's benefits *prior to* its patent validity challenge, the Court's decision in that case did not undermine the common law

44. *MedImmune*, 549 U.S. at 134-35.

45. *Id.* at 135.

46. *Id.*

rule nor apply to a nonrepudiating licensee in good standing such as *MedImmune*. Justice Scalia expressed his doubts as to the merits of this argument in the following comment:

Even if *Lear's* repudiation of the doctrine of licensee estoppel was so limited (a point on which, as we have said earlier, we do not opine), it is hard to see how the common-law rule has any application here. Petitioner is not repudiating or impugning the contract while continuing to reap its benefits. Rather, it is asserting that the contract, properly interpreted, does not prevent it from challenging the patents, and does not require the payment of royalties because the patents . . . are invalid.⁴⁷

In other words, *MedImmune's* challenge to the validity of the Genentech patent, which was not prohibited under the license agreement, was not a challenge to the agreement itself. Rather, the patent validity challenge was a permitted action on the part of *MedImmune* to demonstrate that no royalties were due Genentech under the contract because the licensed patent was invalid.

Despite the skepticism reflected in Justice Scalia's assessment of Genentech's contract-based arguments, he refrained from ruling on their merits. In particular, he was explicit in his refusal to opine on whether the holding in *Lear*, the U.S. Supreme Court's controlling decision on licensee estoppel, applies to a nonrepudiating licensee in good standing. Justice Scalia concluded his discussion of the contract dispute in *MedImmune* by reiterating his view that a decision on the merits of the contract arguments was not necessary to resolve the jurisdictional issue before the Court. In acknowledging the possibility that on further analysis Genentech's contract arguments may ultimately prove valid, he noted that "even if . . . [Genentech] were correct that the licensing agreement or the common-law rule precludes this suit, the consequence would be that respondents win this case *on the merits*—not that the very genuine contract dispute disappears, so that Article III jurisdiction is somehow defeated. In short, Article III jurisdiction has nothing to do with this 'insurance-policy' contention."⁴⁸

47. *Id.*

48. *Id.* at 135-36.

C. The Licensor's Dilemma

The *MedImmune* Court's rejection of the Federal Circuit's jurisdictional barrier to a patent validity challenge by a licensee in good standing, coupled with its refusal to rule on whether *Lear*'s repudiation of the doctrine of licensee estoppel applied to such a licensee, raised important questions for prospective patent licensors and licensees. The uncertainty that would be generated by the *MedImmune* decision and the need for ultimate resolution of the questions left unanswered in the case were not lost on the members of the Court. During the oral argument in *MedImmune*, Justice Ginsburg noted that a decision regarding subject matter jurisdiction, without more, may move the case "out of the jurisdiction box, but you're left with the same underlying question,"⁴⁹ i.e., can a licensee in good standing challenge the validity of the licensed patent. If such a licensee is barred on the merits from challenging the patent's validity, the licensor simply wins a dismissal under Fed. R. Civ. P. 12(b)(6) rather than under 12(b)(1) as it did in the district court in *MedImmune* pursuant to the Federal Circuit's subject matter jurisdictional bar.⁵⁰ Only in the absence of a valid merits-based contract argument against such a challenge will the court have authority to evaluate the licensee's patent invalidity claim. Not surprisingly, Justice Scalia concluded his opinion in *MedImmune* by inviting the lower court to which the case was remanded to consider any merits-based arguments for denial of declaratory relief, including those contract-based arguments discussed but not decided in his opinion.^{51, 52}

Contract-related questions that moved beyond the facts in *MedImmune* were also considered by the Justices as they engaged in

49. Transcript of Oral Argument at *8 *MedImmune* 549 U.S. 118 (2006) No. 05-608[hereinafter "*MedImmune* oral argument"].

50. *Id.* at *9 ("JUSTICE GINSBURG: But what good would it do? Suppose we said, 'Federal Circuit, you put the wrong label on it. It should be 12(b)(6), not 12(b)(1), or perhaps even 8(c), affirmative defense'? Then you go back to the Federal Circuit, and they'll come up with the same decision, that, as long as you are licensed and are paying your royalties, you have -- and they just put a different label on it . . . -- . . . not stated a claim.").

51. *MedImmune*, 549 U.S. at 136-37 ("Similarly available for consideration on remand are any merits-based arguments for denial of declaratory relief.").

52. On remand of the *MedImmune* case, the U.S. District Court for the Central District of California accepted Justice Scalia's invitation to evaluate the merits-based contract arguments raised in the case and held that the U.S. Supreme Court's rejection of the doctrine of licensee estoppel in *Lear* extended to a nonrepudiating licensee in good standing. *MedImmune v. Genentech*, 535 F. Supp. 2d 1000 (C.D. Cal. 2008). See *infra* section III.C.4.c.iv. of this Article for a detailed discussion of the district court's opinion.

their deliberations in the case, e.g., is an explicit contract provision that prohibits or discourages a patent validity challenge by a nonrepudiating licensee enforceable? In fact, the first question in the *MedImmune* oral argument, posed by Chief Justice Roberts and directed to the attorney for MedImmune, was whether MedImmune's position regarding its right to challenge the validity of the licensed Genentech patent would be different if the license agreement had contained an explicit provision specifying that the licensee was not permitted to challenge the patent?⁵³ The MedImmune attorney responded by expressing doubt as to the enforceability of such a provision under *Lear* but, in keeping with the overall thrust of his argument to limit the Court's deliberation to the jurisdictional issue before it, he stressed that such a question was not relevant to the issue that the Court had been asked to address. Not willing to let the contract question drop, Justice Kennedy commented that "as a matter of policy, we, at some point, either in this case or some later case, may have to address the question of whether or not such a provision is enforceable. If it is, we may . . . not be talking about much. It's just going to be boiler plate in every license agreement, and that's the end of it."⁵⁴

The oral argument in *MedImmune* is remarkable for the tendency of the Justices to deviate from a focused analysis of the jurisdictional issue before the Court in order to discuss substantive contract-based arguments regarding the right of a nonrepudiating licensee in good standing to challenge the validity of the licensed patent. The message reflected in the Justices' inquiries and comments was clear: While the Court was not ready to opine on the validity of the contract-based arguments against a patent validity challenge by a nonrepudiating licensee, the important contract-related questions highlighted by the case would need to be answered and in the near future. The remainder of this Article is intended to provide such answers. Specifically, we will offer our views on how the most pressing of these questions will be decided, if and when presented to the U.S. Supreme Court. In addition, we will provide guidance for prospective licensors and licensees in negotiating and drafting patent license agreements while they await the Court's decisions.

The *MedImmune* Court's elimination of the Federal Circuit's jurisdictional barrier to a patent validity challenge by a licensee in

53. *MedImmune* oral argument at *4.

54. *Id.* at *5.

good standing has been viewed by many as a pronounced shift in favor of the licensee in the balance of rights between a licensor and a licensee in a patent license agreement. The failure of the Court to resolve the contract-related issues in the case has presented a dilemma for licensors as to how to redress the shift in the balance of rights. Simply stated, the patent licensor must decide the following: Is there a vestige of the doctrine of licensee estoppel to protect a patent licensor from a validity challenge by a licensee in good standing and, if one cannot rely on the doctrine, are explicit contract provisions that prohibit, reduce the incentive for, and/or specify a consequence of, a licensee's challenge of the validity of a licensed patent enforceable? In Part III of this Article we argue that the solution to the licensor's dilemma is to be found in an analysis of the Court's *Lear* decision and, accordingly, we provide a detailed analysis of that case as well as a review of prior and subsequent case law necessary to fully appreciate the meaning and scope of the *Lear* holding.

III. LICENSEE ESTOPPEL AND THE SCOPE OF *LEAR*'S REPUDIATION OF THE DOCTRINE

In this Part III of the Article, we argue that the U.S. Supreme Court's holding in *Lear v. Adkins*⁵⁵ and the Court's reasoning in support of its holding provide an adequate basis for determining whether *Lear*'s rejection of the doctrine of licensee estoppel extends to a nonrepudiating licensee in good standing. We begin our argument with a brief history of licensee estoppel, which describes the limits and the recognized versions of, and the exceptions to, the doctrine and which is essential to an understanding of the *Lear* holding. We then review the U.S. Supreme Court's decision in *Automatic Radio v. Hazeltine Research*,⁵⁶ the last decision of the Court in support of the doctrine. The scope of the *Lear* Court's repudiation of licensee estoppel is, in part, defined by the version of the doctrine that was endorsed in *Automatic Radio* and was rejected by the *Lear* Court in overruling the estoppel portion of the *Automatic Radio* decision. Finally, we provide a detailed discussion of the *Lear* case, including the position taken by the Supreme Court of California⁵⁷ in *Lear*. The facts in *Lear* and the holding of the California Supreme Court in the case, subsequently vacated by the

55. 395 U.S. 653.

56. 339 U.S. 827.

57. *Adkins v. Lear*, 64 Cal. Rptr. 545 (1967).

U.S. Supreme Court, provide a basis for a narrow reading of the scope of the U.S. Supreme Court's *Lear* holding with respect to licensee estoppel. In contrast, the public policy rationale relied on by the U.S. Supreme Court in its *Lear* ruling and the actual wording of the Court's decision support the broad view of the impact of the holding. This is the position taken by the U.S. District Court for the Central District of California on remand of the *MedImmune* case, whose decision we review in detail.⁵⁸ We conclude that if and when the issue is presented, the U.S. Supreme Court will interpret its prior *Lear* holding as having rejected the doctrine of licensee estoppel without limitations imposed by the particular facts in the case. According to this view, and despite Federal Circuit dictum to the contrary,⁵⁹ a patent licensee may challenge the validity of the licensed patent even if it neither repudiates nor terminates its patent license agreement and intends to continue to reap the benefits provided pursuant to the agreement.

A. The Doctrine Of Licensee Estoppel

The Supreme Court of California provided the following description of licensee estoppel in the *Lear* case:

[O]ne of the oldest doctrines in the field of patent law establishes that so long as a licensee is operating under a license agreement he is estopped to deny the validity of his licensor's patent in a suit for royalties under the agreement. The theory underlying this doctrine is that a licensee should not be permitted to enjoy the benefit afforded by the agreement while simultaneously urging that the patent which forms the basis of the agreement is void⁶⁰

This concise description goes a considerable distance in providing a working understanding of the doctrine. However, the complex history of licensee estoppel, the different legal justifications for the doctrine, the important limits that distinguish the recognized versions of the doctrine and the numerous exceptions to licensee estoppel belie the view that a brief description such as that offered by the California Supreme Court in *Lear* can enable one to

58. 535 F. Supp. 2d 1000.

59. *Studiengesellschaft Kohle v. Shell Oil*, 112 F.3d at 1568.

60. *Adkins*, 64 Cal. Rptr. at 549-50, citing ANTHONY W. DELLER, *DELLER'S WALKER ON PATENTS* 607 § 403 Warranty of Validity of Patent and Estoppel of Licensee to Deny Validity (2nd ed., vol. 4 1965).

understand the evolution of the doctrine through to its ultimate repudiation in *Lear*.

In this section of the Article, we provide the background necessary to understand this evolution of the doctrine of licensee estoppel.⁶¹ We begin with a brief review of the 1846 Massachusetts case⁶² relied on by the U.S. Supreme Court in its first affirmation of the estoppel doctrine. The opinion in that early case articulated the most frequently cited legal justification for the doctrine, based on an analogy to landlord tenant law. We then review subsequent U.S. Supreme Court decisions that endorsed the doctrine. The limits of licensee estoppel that distinguish the recognized versions of the doctrine are then discussed. Finally, we review the exceptions to the doctrine crafted by the U.S. Supreme Court, which the *Lear* Court relied on to conclude that the doctrine had been sufficiently eroded over time to justify its rejection.

1. *Early U.S. Case Law*

An early U.S. case provided the basis for the U.S. Supreme Court's affirmation of the doctrine of licensee estoppel and offered the most widely accepted legal justification for the doctrine. In *Wilder v. Adams*,⁶³ plaintiff Benjamin G. Wilder entered into an agreement with defendants William Adams and others ("Adams") in which Wilder granted Adams a license under Wilder's patent that authorized Adams to make and sell safes covered by the patent. In consideration for the grant of the patent license, Adams agreed to pay Wilder a percentage of Adams' sales, calculated on the basis of the weight of the safes that were sold. Following Adams' failure to make the agreed upon payments, Wilder sued Adams for the

61. A contract-based prohibition to the challenge of a patent's validity developed in three distinct but related contexts: (1) a patent license agreement, where licensor sues licensee for recovery of royalties owed on the use of the licensed patent and licensee defends on the basis of a claim that the licensed patent is invalid (licensee estoppel), (2) an agreement between the assignor and assignee of an assigned patent, where assignor sues assignee for recovery of payment owed for the assignment and assignee defends on the basis of a claim that the assigned patent is invalid (assignee estoppel), and (3) an agreement between the assignor and assignee of an assigned patent, where assignee sues assignor for patent infringement and assignor defends on the basis of a claim that the assigned patent is invalid (assignor estoppel). While the justifications for the prohibition in the three contractual contexts are not identical, the doctrine of licensee estoppel has evolved through judicial decisions addressing each type of contractual arrangement. Accordingly, each type of case is discussed in this section, although licensee estoppel, and not assignee or assignor estoppel, remains the focus of this Article.

62. *Wilder v. Adams*, 29 F. Cas. 1216 (C.C.D. Mass. 1846).

63. *Id.*

amounts due. Adams defended by claiming that the Wilder patent was invalid. The question before the court was whether such a defense could be made in the case or was irrelevant to the claim made by the plaintiff for payment. The defendants argued that “the invalidity of the patent, if shown, would constitute a failure of consideration, on which the covenant to . . . pay rested, and hence would be a good bar to any recovery.”⁶⁴ Citing English and Roman law,⁶⁵ the court rejected this argument on the following grounds:

[The defendants] . . . have had the license to make and sell which they agreed for; they have received proceeds from it, and they are only asked to pay over the proportion of those proceeds which they agreed to; they have lost nothing in all this, if the patent was invalid; and why, then, should it be said that the consideration for this contract has failed?⁶⁶

The *Wilder* court supported its conclusion by reference to an analogy in property law regarding the payment obligation of a tenant to a landlord in a lease arrangement. As noted by the court, “[i]f a leasee be not actually evicted by some better or higher title in the third person, he is bound to pay rent as long as he continues to enjoy quietly the premises leased to him, though by one whose title may be invalid.”⁶⁷ For both a leasee granted the right to use the leased property and a licensee granted a right under a patent, as long as the recipient of the right continues to enjoy the benefit that it confers, the recipient is obligated to make the agreed upon payment for the granted right, irrespective of whether the basis for the right (title to the leased property or the statutory patent right to exclude) is valid. Rooklidge, in his detailed analysis of licensee validity challenges,⁶⁸ labeled this justification for the doctrine of licensee

64. *Id.* at 1217.

65. *Id.* at 1218 (“[I]t has been held, that if benefits have been obtained by the patent, the recovery back [of consideration already paid by the patent licensee] will not be sustained. *Taylor v. Hare*, 1 Bos. & P. (N. R.) 260; [Court of Common Pleas 1805]”) (“[B]y Roman law, a thief could regain articles of a borrower from him (Dom. Civil Law, pt. 13, tit. 6).”).

66. *Id.* at 1217.

67. *Id.* at 1217–18.

68. William C. Rooklidge, *Licensee Validity Challenges and the Obligation to Pay Accrued Royalties: Lear v. Adkins Revisited (Part I)* 68 J. PAT. & TRADEMARK OFF. SOC’Y 506 (1986), [hereinafter Rooklidge, *Lear v. Adkins Revisited (Part I)*]; William C. Rooklidge, *Licensee Validity Challenges and the Obligation to Pay Accrued Royalties: Lear v. Adkins Revisited (Part II)* 69 J. PAT. & TRADEMARK OFF. SOC’Y 5 (1987), [hereinafter Rooklidge, *Lear v. Adkins (Part II)*]; William C. Rooklidge, *Licensee Validity Challenges and the*

estoppel the relevance rule, which holds that “the licensed patent’s validity is irrelevant to the licensee’s obligation to pay royalties accrued under the license”⁶⁹ on the theory that “one cannot avoid the effect of an agreement once he has accepted its benefits.”⁷⁰ In applying the rule, the *Wilder* court held that the defendant licensees in the case could not raise the “irrelevant” defense that the licensed patent was invalid and, accordingly, they were obligated to make the payments due the patent licensor under the license agreement.

In reaching its decision, the court in *Wilder* considered another of the defendants’ arguments: this one supporting their right to challenge the validity of the plaintiff’s patent. According to this argument, the application of the doctrine of licensee estoppel requires a technical estoppel by deed that results from the language of the license agreement, and no such estoppel could be supported by the agreement between *Wilder* and *Adams*. This interpretation of the doctrine of licensee estoppel, attributed to the early English case *Hayne v. Maltby*,⁷¹ holds “that a licensee is ‘estopped by its deed’ from challenging validity if the license agreement stipulated that the patent was valid”⁷² and is based on “the strict legal concept which prevents one from disputing facts to which one has previously attested.”⁷³ While the *Wilder* court accepted the defendants’ contention that the agreement between the parties in the case did not contain any stipulation as to the validity of the licensed patent, it rejected the argument that that fact justified a patent validity challenge by the licensee. Relying on its prior conclusion that the licensed patent’s validity was irrelevant to the plaintiff’s claim for accrued payments due under the license agreement, the court rejected the defendants’ patent validity challenge on the basis of the relevance rule despite the absence of an estoppel by deed.⁷⁴ This line of reasoning offered by the *Wilder*

Obligation to Pay Accrued Royalties: Lear v. Adkins Revisited (Part III) 69 J. PAT. & TRADEMARK OFF. SOC’Y 63 (1987), [hereinafter *Rooklidge, Lear v. Adkins Revisited (Part III)*].

69. *Rooklidge, Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 509.

70. *Id.* at 511.

71. 100 Eng. Rep. 665, 3 T.R. 438 (English High Court of Justice 1789).

72. *Rooklidge, Lear v. Adkins Revisited (Part I)*, *supra* note 68 at 509 (quoting *Rooklidge’s* review of the relevant portion of *Hayne* 100 Eng. Rep. at 666, 3 T.R. at 441).

73. *Id.*

74. 29 F. Cas. at 1218 (“But the illustrations I have put are not grounded on the idea, that there is here any technical estoppel. They rest rather on the idea, that such a defence is not consistent with the position and relation of the defendants to the plaintiff; and, in this case itself, this defence not only contravenes the attitude in which the parties

court with respect to the proper justification for the doctrine of licensee estoppel prompted Rooklidge to remark that the term “licensee estoppel” is, in fact, a misnomer,⁷⁵ in that “the rule prohibiting a patent licensee from challenging validity had nothing whatsoever to do with estoppel.”⁷⁶

2. *The U.S. Supreme Court’s Affirmation of Licensee Estoppel*

Relying on the relevance rule articulated in *Wilder v. Adams*, the U.S. Supreme Court first endorsed the doctrine of estoppel to challenge the validity of a patent⁷⁷ in *Kinsman v. Parkhurst* in 1856.⁷⁸ The plaintiff, Parkhurst, owned a patent for improvements to a machine for ginning cotton and wool. Pursuant to written agreements with defendant, Kinsman, Parkhurst assigned a one-third ownership of the patent to Kinsman and granted to Kinsman permission to manufacture and sell machines covered by the patent. In consideration of the grant of these rights, Kinsman agreed, *inter alia*, to pay to Parkhurst a share of the profits generated on the sale of the machines. When Kinsman failed to make the agreed upon payments, Parkhurst sued to recover the amounts due and Kinsman defended on the basis of patent invalidity. In rejecting the invalidity defense and holding in favor of Parkhurst, the Court provided the following analysis:

The principal objection made by the appellant . . . [Kinsman] to the decree of the court below is, that Parkhurst was not the original and first inventor of the thing patented. We are not satisfied that this is made out. But we have not found it necessary to come to a decided opinion upon this point,

stand towards each other by the terms of the covenant, but as before shown, is not calculated to enforce justice towards either party.”).

75. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 518 (“the misnomer licensee estoppel”).

76. *Id.* at 516.

77. We intentionally avoided the term “licensee estoppel” in this sentence because the contractual arrangement between *Parkhurst* and *Kinsman* involved the assignment of a patent as well as the grant of rights under the patent. Nonetheless, the case is frequently cited as the U.S. Supreme Court’s first endorsement of the doctrine of licensee estoppel. See Justice Frankfurter’s dissent in *MacGregor v. Westinghouse Electric & Manufacturing Co.* (“Ninety years ago this Court unanimously announced the doctrine that a licensee under a patent is estopped from challenging the validity of that patent. *Kinsman v. Parkhurst*, 18 How. 289.”). 329 U.S. 402, 408 (1947); see also Hal D. Cooper, *Estoppel to Challenge Patent Validity: The Case of Private Good Faith vs. Public Policy*, 18 *Western Reserve Law Review* 1122, 1125 (1967); Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 516–17; *Lear*, 395 U.S. at 663.

78. 59 U.S. 289 (1856).

because we are all of opinion that, under the agreement . . . the invalidity of the patent would not afford a bar to the complainant's [Parkhurst] right to an account. Having actually received profits from sales of the patented machine, which profits the defendants do not show have been or are in any way liable to be affected by the invalidity of the patent, its validity is immaterial.⁷⁹

The Court cited *Wilder* in concluding that "[h]ere . . . it is simply a question of failure of title, and as that does not appear in any manner to have affected the profits which the defendants received, there can be no ground to allow it to be shown in defense."^{80, 81}

The U.S. Supreme Court repeated its endorsement of the estoppel doctrine in three subsequent cases, but in each instance without significant analysis. In *Dale Tile Manufacturing Co v. Hyatt*,⁸² the Court was asked to determine whether a federal question (as to a licensed patent's validity) needed to be answered for a patent holder to obtain from a licensee the agreed-upon payments for the rights granted under the patent. The Court concluded that the patent validity question did not need to be answered to resolve the contract dispute in the case. Relying on *Kinsman v. Parkhurst*, the Court affirmed the lower court's ruling that "in this action to recover royalties under the agreement, the defendant, while continuing to enjoy the privileges of the license, was estopped to deny the validity of the patent."⁸³

In *United States v. Harvey Steel Co.*,⁸⁴ a steel company sued the U.S. government for royalties due under an agreement pursuant to which the government was granted a license under the company's process patent. The government defended on the basis of its

79. *Id.* at 292-93.

80. *Id.* at 293.

81. The Court in *Kinsman* provided an additional ground for its holding that was expressed in terms of estoppel. In the words of the Court, "we think the defendants are estopped from alleging that invalidity. They have made and sold these machines under the complainant's title, and for his account; and they can no more be allowed to deny that title and retain the profits to their own use, than an agent, who has collected a debt for his principal, can insist on keeping the money, upon an allegation that the debt was not justly due." *Id.* at 293. Rooklidge has suggested that had the Court not offered this second basis for its holding, in addition to its reliance on the relevance rule, "the confusing term of licensee estoppel may never have been adopted in the United States." Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 517.

82. 125 U.S. 46 (1888).

83. *Id.* at 54.

84. 196 U.S. 310 (1904).

contention that the licensed patent was invalid and, therefore, no royalties were due. Justice Holmes, writing for the Court, held that an invalidity defense was not available to the government in that “a licensee, when sued for royalties, is estopped to deny the validity of the patent which he has been using.”⁸⁵

In *Automatic Radio v. Hazeltine Research*,⁸⁶ the U.S. Supreme Court provided its final endorsement of licensee estoppel prior to the repudiation of the doctrine in *Lear*. This case will be discussed in detail in Section III.B. below. For the purposes of this section, we need only note that the Court in *Automatic Radio* cited *Harvey Steel* for “[t]he general rule . . . that the licensee under a patent license agreement may not challenge the validity of the licensed patent in a suit for royalties dues under the contract.”⁸⁷ With little analysis, the court concluded that the “general rule” applied in the instant case and rejected the patent licensee’s attempt to challenge the validity of the licensed patent in a suit to recover royalties due.

The U.S. Supreme Court’s decisions in *Harvey Steel* and *Automatic Radio* were the controlling precedents with respect to licensee estoppel at the time that the Supreme Court of California heard the *Lear* case. The California court’s description of licensee estoppel, quoted in the first paragraph of this Section III.A., captured the generally accepted understanding of the doctrine as it had evolved in U.S. courts from *Wilder* to *Automatic Radio*.⁸⁸ However, as will be demonstrated in the next two sections of this Article which discuss the limits of, and the exceptions to, the doctrine, the California Supreme Court’s description oversimplified the state of licensee estoppel jurisprudence at the time of the *Lear* case. This fact was not lost on the U.S. Supreme Court in its review of the state court’s decision in the case, and recognition of the conflicting estoppel case law played a significant role in the Court’s decision to reject the doctrine.

85. *Id.* at 317.

86. 339 U.S. 827.

87. *Id.* at 836.

88. To support its description of the doctrine of licensee estoppel in the *Lear* case (quoted in the first paragraph of Part III.A.), the California Supreme Court relied on the U.S. Supreme Court’s decision in *Harvey Steel Co.* (in footnote 16) and on *Deller*, *supra* note 60, § 403, § 420, the latter citing early lower court cases that relied on the U.S. Supreme Court’s decision in *Kinsman* (in § 403) and the First Circuit’s decision in *Automatic Radio* (in § 420), which was later affirmed by the U.S. Supreme Court (*See infra* Part III.B); *Adkins*, 64 Cal.Rptr. 545.

3. *Limits to the Doctrine of Licensee Estoppel*

As will be demonstrated later in this section, different forms of the doctrine of licensee estoppel have been endorsed by the U.S. courts. Yet each form or version of the doctrine recognized some limit to the prohibition against a patent validity challenge by a licensee. In other words, no version held that once a licensee, a party is forever restricted from challenging the licensed patent; for each version of the doctrine, the occurrence of some event or events would release the licensee from the restriction on patent challenges. In fact, it was the difference in the accepted releasing events that distinguished the major forms of licensee estoppel.

a) The Eviction Limitation

The eviction of a licensee from the enjoyment of the benefits afforded by the grant of a patent license is an example of a releasing event that could free a licensee from the prohibition against a patent validity challenge.⁸⁹ This so-called “eviction limitation” to licensee estoppel⁹⁰ was recognized in early descriptions of the doctrine,⁹¹ and was justified through analogy to landlord-tenant law.⁹² As noted by Rooklidge, “[w]hen courts in the early patent cases analogized to landlord-tenant law to hold the licensed patent’s validity irrelevant to a suit to recover accrued royalties, the analogy included the concept of eviction. The bar against a tenant’s challenging its landlord’s title falls when the tenant is evicted from quiet enjoyment by one with paramount title.”⁹³ According to this line of reasoning, a patent licensee who is deprived of the benefits of the patent license is similarly evicted and, therefore, free to challenge the validity of the licensed patent.

89. See Cooper, *supra* note 77, at 1140–44; Rooklidge *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 513–15.

90. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 513.

91. See, e.g. Hayne, 100 Ung. Rep. 665, 3 T.R. 438; Taylor v. Hare, 127 Eng. Rep. 461, 1 Bos. & Pul. (N.R.) 260 (Court of Common Pleas 1805); Wilder, 29 F. Cas. 1216; White v. Lee, 14 F. Cas. 789 (C.C.D. Mass. 1882); see also, *supra* section III.A.1.

92. See Rooklidge *Lear v. Adkins (Part I)*, *supra* note 68, at 513 (citing Hayne, 100 Eng. Rep. at 666, 3 T.R. at 441; Taylor, 127 Eng. Rep. at 461, 1 Bos. & Pul. (N.R.) at 2601; Wilder, 29 F. Cas. 1216); Cooper, *supra* note 77, at 1140 (citing White, 14 F. Cas 789). Each commentator points out flaws in the landlord/tenant analogy that are apparent on closer examination. However, the arguments presented in this Article do not hinge on the strength of that analogy, which remains useful in understanding concepts relating to licensee estoppel.

93. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 513 (footnotes omitted).

The eviction event most frequently encountered in the relevant case law was the judicial invalidation of a licensed patent in an infringement suit brought by the patentee against a third party.⁹⁴ The U.S. Supreme Court recognized the eviction limitation in *Dale Tile Manufacturing Co. v. Hyatt* when it affirmed the lower court's conclusion that the defendant/licensee "could not, in this action to recover the royalties agreed upon, deny the validity of the . . . patent . . ., so long as it had not been declared void by a court of competent jurisdiction, and while the defendant retained and acted under its license from the plaintiff."⁹⁵

In *Drackett Chemical Co. v. Chamberlain Co.*,⁹⁶ the Court of Appeals for the Sixth Circuit discussed eviction based on the judicial invalidation of a licensed patent and the impact of such an eviction upon a licensee's right to challenge the patent. In that case, the Drackett Chemical Co. was granted a license by the Chamberlain Co. under the latter's patent covering a drainpipe solvent; the licensed right to sell the covered product was exclusive for the grocery trade and nonexclusive for the hardware and drug trades.⁹⁷ Subsequently, the parties to the agreement joined as

94. Another example of eviction, recognized by the courts, is the unrestricted use of the patented invention by a party without the authorization of the patent holder, resulting from a failure of a patent holder to enforce his patent. See *id.* at 515 ("[E]viction was also held to occur when the patent was defied by unlicensed persons so extensively as to deprive the licensee of the benefits of the license. Thus, widespread infringement resulted in eviction." (footnotes omitted)) and Cooper, *supra* note 77, at 1140 ("[C]ourts have suggested that an eviction may occur where there has been unlicensed competition rendering the license valueless.") (Citing White, 14 F. Cas. 789).

95. 125 U.S. 46, 49 (1888) (emphasis added).

96. *Drackett Chem. Co. v. Chamberlain Co.*, 63 F.2d 853 (6th Cir. 1933).

97. Some courts, noting the distinction between exclusive and nonexclusive licenses, rejected eviction on the basis of judicial invalidation in the context of a nonexclusive license. See Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 513-14 (footnotes omitted):

A patent does not grant the patentee the right to make, use or sell the claimed invention. Rather, the patent only gives the patentee the right to exclude others from making, using or selling the claimed invention. A nonexclusive patent license gives the licensee only an assurance of nonassertion of the licensor's rights to exclude. In effect, a licensee is "using" immunity from suit while practicing the patented invention. Just as the patent does not give the patent owner the right to practice the patented invention, invalidation of the patent does not deprive the licensee of the right to practice the invention. Thus, the basis for the eviction must be other than deprivation of the right to practice the invention.

An exclusive license affords the licensee an exclusive right additional to the right granted the nonexclusive licensee: a right, if not to bring suit in its own name, to compel the patentee to join in an enforcement suit. The right from which an exclusive licensee is evicted is readily apparent. Judicial invalidation of the licensed patent evicts the exclusive licensee from its right to exclude.

plaintiffs in a suit against a third party for infringement of the patent. During the pendency of the infringement suit, Drackett notified Chamberlain that it was withholding royalty payments due under the agreement until the decision regarding the validity of the Chamberlain patent was reached in the third party suit, and would not pay the withheld royalties if the patent was invalidated. After the patent was adjudged to be invalid, Chamberlain sued Drackett for the royalties owed. The Sixth Circuit held that Chamberlain was not entitled to recover royalties from Drackett that had accrued after Drackett was evicted from the enjoyment of its licensed patent rights as a result of the judicial invalidation of the Chamberlain patent.

In its opinion, the *Drackett* court first addressed the impact of an eviction based on judicial patent invalidation on a licensee's right to challenge the licensed patent. The court adopted the position taken by the Second Circuit in *White Co. v. Morton E. Converse & Son Co.*,⁹⁸ as succinctly expressed by Judge Learned Hand: "It is quite true that a licensee may not dispute the validity of the patent in a suit for royalties. *U.S. v. Harvey*, 196 U.S. 310 . . .; though the contrary is the case after decree of invalidity in another suit, *Ross v. Fuller* (C. C.) 105 F. 510; the theory being that this effects an 'eviction.'"⁹⁹

On the other hand, the right from which a nonexclusive licensee is evicted is not as readily apparent as that of the exclusive licensee. Some courts refused to extend the eviction analogy to nonexclusive licensees for this reason. Most courts reasoned, however, that judicial invalidation of the licensed patent deprives both the nonexclusive and exclusive licensee of the patent's deterrent effect: the mere existence of the apparently valid patent deters potential competitors. The royalty charged by the licensor is an economic barrier to entry.

The general rule was that judicial invalidation of a licensed patent, whether exclusive or nonexclusive, evicted the licensee, freeing it to challenge the validity of the patent.

See also Cooper, *supra* note 77, at 1140-44.

98. 20 F.2d 311 (2d Cir. 1927).

99. *Id.* at 313. The relevant language from the *Ross* holding is as follows:

[T]he court is convinced that there was a failure of consideration the moment the patent was declared invalid. The defendant agreed to pay the stipulated royalty in consideration of the monopoly. When deprived of this exclusive privilege by law the defendant occupied no vantage ground over any other manufacturer. The defendant took nothing from the plaintiff, for he had nothing to give. The estate which the parties supposed belonged to the plaintiff was judicially determined to belong to the public. The defendant should not be compelled to pay a large sum of money for exercising a right, which, after the patent was destroyed, was no longer exclusive, but was free and common to all. *Ross v. Fuller*, 105 F.510, 513-14 (C.C.N.D.N.Y. 1900).

With respect to the concept of eviction as a result of judicial invalidation of a licensed patent, the *Drackett* court provided the following analysis:

[I]n *United States v. Harvey Steel Co.*, 196 U.S. 310 . . . , it is held that a defense of invalidity is not open to the defendant in a suit for royalties in the absence of an outstanding decision against the patent. . . . But it seems to us that a different situation must of necessity arise where the monopoly, apparently created by the grant of a patent, has been destroyed by a decree of invalidity in a court of competent jurisdiction. The subject-matter of such a contract is essentially “the monopoly which the grant confers: the right of property which it creates” (*Gayler v. Wilder*, 10 How. 477, 493, 13 L. Ed. 504), and, when this monopoly has been destroyed, and the exclusive rights of manufacture, sale, and use, purported to have been created by the patent, are judicially decreed to be no longer exclusive, but are thrown open to the public at large, there has been a complete failure of consideration—an eviction—which should justify a termination of the contract. Prior to such eviction, the mere invalidity of the patent is properly held not to be a sufficient defense, because the licensee may still continue to enjoy all the benefits of a valid patent. It may be respected, and the licensee would then have just what he bargained for It is only when, by judicial decree or otherwise, it is published to the world that the monopoly is destroyed, that the licensee can claim a corresponding release from his obligation to pay royalties.¹⁰⁰

The *Drackett* court concluded its assessment of the eviction limitation to the doctrine of licensee estoppel by affirming the relevance justification of the doctrine. The court held “that the *Drackett Chemical Company* is estopped to deny the validity of the patent in respect to royalties accruing *prior to* that which constitutes an eviction, and . . . that all royalties accruing prior to that date [of eviction] must be paid.”¹⁰¹ Such a conclusion was entirely consistent with the relevance theory of licensee estoppel, which held that the validity of a licensed patent is irrelevant to a claim for royalties due under a patent license agreement during the period in

100. *Drackett Chem Co.*, 63 F.2d at 854.

101. *Id.* at 855 (emphasis added).

which the licensee had full “enjoyment of the monopolistic rights granted under the license.”¹⁰²

b) Expiration, Termination, and the Repudiation Limitation

Each of the recognized versions of the doctrine of licensee estoppel acknowledged that the estoppel applied only during the term of the license.¹⁰³ As stated by Rooklidge in his review of the topic, “[i]n addition to eviction, the bar against validity challenges [by a licensee] was held to cease upon expiration or termination of the license agreement.”¹⁰⁴ In *H. Tibbe & Son Manufacturing Co. v. Heineken*, the Circuit Court for the Southern District of New York recognized the expiration limit of the doctrine of licensee estoppel in holding that “there is no authority for the proposition that a former licensee is estopped from questioning the validity of a patent, after his license expires, in vindication of acts done subsequent to its termination.”¹⁰⁵ Regarding the termination of a patent license for reasons other than the passage of time, the Court of Appeals for the Sixth Circuit in *Eskimo Pie Corp. v. National Ice Cream Co.* noted the following, in the context of a license agreement that was terminated by the patent holder/licensor as a result of the licensee’s breach: “By the familiar rule, the defendant [licensee], while operating under—or probably while retaining and claiming the right to operate under—the license, cannot be heard to deny the validity of the patent; but we do not understand it to be claimed that this estoppel by rule of law would persist after the license and all the licensee’s rights thereunder were terminated.”¹⁰⁶

While it was generally agreed that licensee estoppel applied only during the term of a license agreement, the debate surrounding

102. *Id.*

103. See, e.g., Deller, *supra* note 60, at 622 (§ 405. No Estoppel After Termination of License); Cooper, *supra* note 77, at 1146 (1967); Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 515.

104. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 515.

105. 37 F. 686, 687 (C.C.S.D.N.Y. 1889); see also *Bucky v. Sebo*, 208 F.2d 304, 305–06 (2d Cir. 1953) (“During the existence of a patent license, the licensee may be estopped to contest validity. But even this estoppel usually vanishes when the license terminates . . . because of lapse of time . . .” (emphasis added) (footnote omitted)).

106. 26 F.2d 901, 902 (6th Cir. 1928); See also *Dueber Watch-Case Mfg. Co. v. Robbins*, 75 F. 17, 26 (6th Cir. 1896). (“The fact that for a time the defendant was a licensee of the . . . [licensed] patent cannot, of course, estop the defendant from disputing its validity in a suit for infringements charged to have taken place after the license was withdrawn.”); *Bucky*, 208 F.2d at 305–06 (“During the existence of a patent license, the licensee may be estopped to contest validity. But even this estoppel usually vanishes when the license terminates . . . by act of the licensor.” (footnotes omitted) (emphasis added)).

the doctrine centered on the question of whether a patent licensee could unilaterally repudiate the license agreement and thereafter challenge the validity of the licensed patent.¹⁰⁷ Rooklidge framed the issue as follows, noting the analogy to landlord-tenant law:

[N]ot all patent licensees were willing to wait for eviction or expiration of the license agreement and few had the right to terminate the agreement at will. This situation caused a problem for licensees who became convinced of the invalidity of the patent during the term of the license. Once again the courts returned to the roots of the doctrine—the analogy to the landlord-tenant law.

The common law of landlord-tenant provided that if the tenant surrendered possession of the premises and repudiated the lease, it could then dispute the landlord's title in an action for post-repudiation rents. This equitable rule gave rise to the repudiation concept in patent law. The early patent cases recognized that a licensee could avoid application of the bar against validity challenges by repudiating the license agreement. Despite repudiation, the licensee remained obligated to pay royalties which had accrued prior to the repudiation. By repudiating the license, the licensee chose to become an infringer for the period after the repudiation.¹⁰⁸

As noted in the Rooklidge comment above, a “repudiation limitation”¹⁰⁹ to licensee estoppel had been recognized in early English and U.S. case law. In *Lawes v. Purser*,¹¹⁰ an action for payment due under a patent license agreement, Judge Erle stated the following:

[I]t is clear to me that, if the defendants [licensees] go on under this agreement, using the patent right by the plaintiff's [patentee's] permission, they must pay him, whether the

107. Cooper, *supra* note 77, at 1146 (“Where the suit is brought seeking recovery of royalties allegedly accruing . . . after the contract has ended . . . , the doctrine of estoppel is inapplicable, and validity of the patent may be challenged. The major division of authority is whether a licensee may repudiate the license agreement and thereafter attack the validity of the patent.” (footnotes omitted)).

108. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, 515–16 (footnotes omitted).

109. *Id.*

110. 6 EL. & BL. 930 (Q.B.) (1856).

patent was valid or not, until, at least, they give notice that they dispute the validity of the patent, and will, in future, use the invention in their own right, and not under the permission of the plaintiff. Such a notice would change the position of the parties: after it the patentee might sue the defendants for an infringement of his patent . . . and perhaps in an action on the agreement . . . the invalidity of the patent might be a defence.¹¹¹

In *Brown v. Lapham*,¹¹² the licensees had “repudiated the license and continued their infringement in defiance of the patent.”¹¹³ In rejecting the patentee’s motion for a preliminary injunction to stop the licensees’ further use of the patented product, the court held “that a licensee under a patent is estopped to deny its validity on any question arising out of that relation between the parties. *Kinsman v. Parkhurst*, 18 How. 289. [However,] [i]t does not follow that he will be always estopped because he has stood in that relation. When he stands out from under the license, and claims nothing from it, and does nothing more under it, with full knowledge to the licensor of his position, he would appear to be at as full liberty to contest the patent as any one.”¹¹⁴

111. *Id.* at 936.

112. 27 F. 77 (C.C.S.D.N.Y 1886).

113. *Id.*

114. *Id.*; see also *Martin v. New Trinidad Lake Asphalt Co.*, 255 F. 93 (C.C.D.N.J. 1919); *Universal Rim Co. v. Scott*, 21 F.2d 346 (N.D. Ohio 1922) for district court decisions that support the repudiation limitation. In *Martin*, the District Court for the District of New Jersey stated the following:

A licensee under a license agreement . . . , when sued for royalties payable under the agreement, where the patent which is the subject-matter of the license, is apparently valid and in force (where it has not been declared invalid by a court of competent jurisdiction or revoked by the Patent Office before the royalties have accrued), may not set up the supposed invalidity of the patent and the consequent failure of consideration of the agreement, unless, prior to the period for which the royalties are sought to be recovered, he has given to the licensor a distinct, definite, and unequivocal notice to the effect that he no longer recognizes the binding force of the agreement, and that he will thereafter manufacture or use the article covered by the patent under a claim of right, founded upon the alleged invalidity of the patent, and in hostility to and defiance of the authority of the patent and the license, so that the licensor can thereafter proceed against him for an infringement of the patent, if he choose so to do.

255 F.93 at 94 (citations omitted). In *Universal Rim*, the District Court for the Northern District of Ohio, Eastern Division, provided the following endorsement of, and justification for, the repudiation limitation:

The contention is made, and some support therefor may be found in the books, that a licensee cannot, in the absence of a provision permitting the license to be terminated, contest the validity of patents covered by the agreement, even after renunciation and

The repudiation limitation was rejected, however, in a number of cases which held that a licensee could not unilaterally repudiate a patent license agreement in order to avoid licensee estoppel and thereby challenge the validity of the licensed patent.^{115, 116} In *St. Paul Plow Works v. Starling*,¹¹⁷ the U.S. Supreme Court had ruled that a licensee's unilateral repudiation, without more, did not effect a termination of the patent license agreement. In that case, plaintiff Starling granted a license to defendant St. Paul Plow Works, pursuant to which St. Paul was authorized to make and sell Starling's patented plow. In consideration for the grant of the patent license, St. Paul agreed to pay royalties to Starling based on its plow sales. St. Paul subsequently renounced the license but continued to make and sell the patented plows without paying the agreed upon royalties. Starling sued St. Paul for the unpaid royalties and St. Paul defended by challenging the validity of the licensed Starling patent. The U.S. Supreme Court held that St. Paul's unilateral repudiation of the license agreement was

notice. This contention originates in the common-law doctrine of estoppel by covenant . . . [However,] the true rule, in my opinion, now is that the licensee, whenever he ascertains that the patents covered by the license agreement are invalid, may refuse to be further bound thereby, and, upon repudiation and notice, may thereafter defend against an action for royalties or an infringement suit as freely as may a stranger . . . If the patents are in fact invalid, then there is no continuing consideration for the agreement, and, as was said by Mr. Justice Brown in *Pope Mfg. Co. v. Gormully*, 144 U.S. 234, 12 S.Ct. 636, 36 L.Ed. 414: 'It is as important to the public that competition should not be repressed by worthless patents, as that the patentee of a really valuable invention should be protected in his monopoly.' So long, however as the invalidity of a patent has not been judicially declared and the licensee continues to operate thereunder without repudiation or notice such as will place him in the attitude of an infringer, there is no such want or complete failure of consideration as will permit the licensee to refuse to pay royalties which have been previously earned.

21 F.2d. at 348-49.

115. See, e.g., *Thomson Spot Welder Co. v. Oldberg Mfg. Co.*, 240 N.W. 93 (Mich. 1932); *E. States Petroleum Co. v. Universal Oil Products, Co.*, 2 A.2d 138 (Del. Ch. 1938); *United Mfg. & Serv. Co. v. Holwin Corp.* 187 F.2d 902 (7th Cir. 1951); *Bowers Mfg. Co. v. All-Steel Equip., Inc.*, 275 F.2d 809 (9th Cir. 1960); see also, L. B. Dodds, *The Repudiation of Patent License Agreements*, 23 Geo. Wash. L. Rev., 151, 158-61 & n.22 (1954); Cooper, *supra* note 77, at 1146-47 & n.183; Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 521 & n.80-82.

116. According to Rooklidge, this rejection of the repudiation limitation in patent licensing paralleled its fate in landlord-tenant law. Citing the Restatement (Second) of Property § 4.3 (1977), Rooklidge noted that the "[repudiation] limitation eventually disappeared from landlord-tenant law. In that context, repudiation was viewed as opening the door to fraudulent claims and needless litigation. Now, unless the lease is silent about termination, the tenant may terminate the lease only pursuant to the provisions of the lease." Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 519 (footnotes omitted).

117. 140 U.S. 184 (1891).

ineffective and, accordingly, Starling had a right to sue for the royalties owed under the agreement. Regarding unilateral repudiation, the Court stated that:

We are of opinion that the license, in the absence of a stipulation providing for its revocation, was not revocable by the defendant [St. Paul], except by mutual consent, or by the fault of the other party. If the plaintiff [Starling], after receiving the notice, had sued the defendant for infringement, he would have been properly regarded as acquiescing in the renunciation; but, instead of that, he elected to regard the license as still in force, and brought an action to recover the royalties provided for by it, which he was entitled to do.¹¹⁸

It is noteworthy that while the Court in *St. Paul* rejected unilateral repudiation as a means of terminating a license agreement, it did not question St. Paul's patent invalidity defense in the case. This fact has led Rooklidge to remark that "[s]ub silentio, the Court in *St. Paul* approved of the principle that repudiation frees the licensee to challenge validity."¹¹⁹ A subsequent case, however, cited *St. Paul* in holding that a licensee's unilateral repudiation of its patent license agreement is ineffective, not only in terminating the agreement but also in avoiding licensee estoppel. In *Eastern States Petroleum Co. v. Universal Oil Products Co.*,¹²⁰ the Delaware Court of Chancery rejected a patent licensee's claim that it had unilaterally repudiated its license agreement and, accordingly, could challenge the licensed patent's validity in a suit brought by the patentee for royalties due under the agreement. The court provided the following concise assessment of the licensee's repudiation claim: "But [licensee] Eastern says it has repudiated the agreement and is therefore free to contest the validity of the patents. The answer to this is, that it is beyond the power of a licensee to revoke the agreement except by the consent or fault of the other party, neither of which is shown. *St. Paul Plow Works v. Starling*, 140 U.S. 184, 186."¹²¹

The position taken by the court in *Eastern* is an expression of the termination rule of licensee estoppel. According to Rooklidge,

118. *Id.* at 196.

119. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 521.

120. 2 A.2d 138.

121. *Id.* at 142.

who employed the term in his review on licensee validity challenges, the termination rule holds “that because the licensee could not unilaterally terminate the contract, and because the licensee is estopped from challenging validity as long as the contract is in existence, the licensee was not freed to challenge validity by his repudiation.”¹²² Under the termination rule, the accepted releasing events were the expiration of the patent license agreement and the termination of the agreement in accordance with its terms.¹²³ The occurrence of any such event would release the patent licensee from the bar against a patent validity challenge imposed by law under the doctrine of licensee estoppel. A licensee’s unilateral repudiation of the agreement, however, had no such effect.¹²⁴

The repudiation limitation and the termination rule defined irreconcilable interpretations of the doctrine of licensee estoppel. The former limit accepted a licensee’s unilateral repudiation of its license agreement as a means of avoiding the application of licensee estoppel; the latter required a termination of the agreement in accordance with its terms. It would appear that the cases reflecting the division of authority on the effectiveness of a unilateral repudiation could be easily categorized as having adopted one or the other of the limits to the doctrine of licensee estoppel. In practice, however, such a categorization is not so straight forward. In a number of cases, which we refer to in this Article as hybrid cases, the court accepted the repudiation limitation in general but concluded that, based on the particular facts in the case before the court, unilateral repudiation could not effect a termination of the license agreement freeing the licensee to challenge the validity of the licensed patent. In essence, the court adopted a termination rule exception to the repudiation limitation. As will be demonstrated in the remaining sections of this Part III, an understanding of this seemingly arcane exception is essential to an appreciation of the

122. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 521.

123. *Id.* at 522 (“The policy basis for the termination rule is contractual – the contract estops the licensee. The premise of the rule is that the licensor’s promise to forego an infringement suit is the consideration for the licensee’s payment of royalties, and therefore impliedly is the consideration for the licensee’s obligation to refrain from challenging validity. Under this notion, the obligations to pay royalties and refrain from challenging validity continue until termination or expiration of the license.” (footnote omitted)); *but, see infra* note 147 regarding an eviction that results from a judicial invalidation of the licensed patent in a third party infringement suit by the court of last resort.

124. *See supra* note 115.

debate regarding the scope of the U.S. Supreme Court's holding in *Lear*.

The decision of the Appellate Division of the New York Supreme Court in *Elgin National Watch Co. v. Bulova Watch Co.*¹²⁵ provides an example of a hybrid case in which the court applied the termination rule exception to the repudiation limitation. In *Elgin*, a patentee brought an action against its licensee for the recovery of minimum royalties payable under a nonexclusive patent license agreement. The licensee, having never utilized the patented invention, repudiated the license agreement and refused to pay any post-repudiation royalties, claiming as a defense that the licensed patent was invalid. The *Elgin* court acknowledged the effectiveness of a unilateral repudiation in the majority of circumstances, but rejected as ineffective the licensee's repudiation in the instant case, and ruled that the licensee was liable for all royalties owed the patentee under the agreement. The features that distinguished *Elgin* from the majority of cases involving a licensee's unilateral repudiation were that the suit was for recovery of minimum royalties that accrued irrespective of the licensee's use of the patented invention and that the licensee did not intend to utilize the patented invention following repudiation. On the basis of these features, the facts in *Elgin* met the essential requirement for application of the termination rule exception to the repudiation limitation, namely that the licensee can incur a royalty obligation following its unilateral repudiation of the license agreement without engaging in any activities that would infringe the licensed patent.

The court in *Elgin* framed the question before it on appeal as follows: "[Is] invalidity of a patent . . . a defense to an action for minimum royalties where the licensee has not used and does not intend to use the process or product of the claimed invention[?]"¹²⁶ The court began its opinion by acknowledging the long established rule that a licensee who has utilized the patented invention is estopped from denying the validity of the licensed patent in an action by the patentee to recover accrued royalties, citing *inter alia* *Kingsman v. Parkhurst*. It then recognized the generally applicable repudiation limitation in noting that "[i]t has become the law, however, that as to future . . . [use of the patented invention], a licensee may repudiate his license upon a challenge to the validity of the patent, posing a test of the patent and exposing himself to the claim

125. 118 N.Y.S.2d 197 (N.Y. App. Div. 1953).

126. *Id.* at 199

and consequences of infringement."¹²⁷ In restating the repudiation limitation, the court highlighted the fact that in the typical repudiation case, the royalty obligation incurred by the licensee following its unilateral repudiation of the license agreement resulted from the licensees' continued use of the patented invention, with the licensee assuming the role of a potential infringer. It is in that context, where the patentee can pursue an infringement claim against the licensee, that the licensee's unilateral repudiation permits it to challenge the validity of the licensed patent as a defense. In the case before the court in *Elgin*, however, the licensee would incur an obligation to pay minimum royalties under the license agreement following its repudiation of the agreement even if it honored its stated intent to avoid any further use of the patented invention. By repudiating its license agreement, "the licensee has simply sought to shed fixed obligations under the license, without . . . [acting] against the patent and incurring the risks of infringement."¹²⁸ According to the *Elgin* court, in such a circumstance, the unilateral repudiation of the license agreement is not effective in freeing the licensee from the bar against a patent validity challenge in an action by the patentee for royalties that accrued following the repudiation.

The *Elgin* court concluded its opinion by reviewing the rationale for its rejection of unilateral repudiation in the case before it. As a precursor to the balancing test employed by the U.S. Supreme Court in its *Lear* holding,¹²⁹ the *Elgin* court weighed the competing interests in respecting contracts and in the free use of inventions in the public domain. According to the court, the doctrine of licensee estoppel was justified under contract principles. "When the courts have held . . . that a licensee may not assert invalidity of the patent as a defense to a claim for accrued royalties, they have necessarily held that validity of the patent is not the essence of consideration for a licensing agreement and that freedom from an infringement claim, regardless of the validity of the claim, is good consideration."¹³⁰ The repudiation limitation, which frees the licensee to challenge the validity of the licensed patent in defense of a claim for royalties incurred for actual use of the patented invention following repudiation, was explained on the basis of patent law policy.

127. *Id.* (emphasis added).

128. *Id.* at 200.

129. See *infra* section III.C.3.

130. *Elgin Nat'l Watch, Co.*, 118 N.Y.S.2d at 201.

There is, of course, no public interest in affording patent protection to any art which is not novel and patentable. Therefore, a patent does not prove itself. In the interest of free . . . [use of an invention in the public domain], a . . . [user] assuming the risks of an infringement suit is allowed to test a patent. The interest in free . . . [use] is such that even a licensee is permitted to put himself in that position. Therefore, a licensee may announce for the future that he repudiates his license and will [use the invention] in opposition to the patent. That position is allowed to him not as a matter of contract law but as a matter of patent law and public policy.¹³¹

In the *Elgin* case, however, the court provided the following reason for its holding that the licensee's unilateral repudiation of its agreement was ineffective:

A licensee like the defendant here, however, does not put itself in . . . [the] position [of acting in opposition of the licensed patent] and is not serving any public interest by repudiating its license agreement. It does not wish to . . . [use the claimed invention] or promote the art. . . . This defendant has simply decided that it does not wish to employ the process . . . covered by the patent, apparently regardless of the validity of the patent. There is no public interest in allowing a licensee, merely because it repents of its bargain, to repudiate its agreement and shed its obligations.

Defendant has received and would receive the protection and consideration of its agreement. Whether it wished to . . . [use the claimed invention] or not was its choice. It could have . . . [used the claimed invention] under the protection of its license and pay royalties accordingly or it could have repudiated the license agreement and . . . [used the claimed invention] as an infringer. Having elected not to . . . [use the claimed invention], however, there is no reason why it should be freed of its considered commitment to pay minimum royalties. The license agreement, for practical purposes, was an option to

131. *Id.*

defendant, and the continuing option was good consideration for the agreed minimum royalty payments.¹³²

In *Elgin*, the court concluded that the consideration for the obligation to pay minimum royalties was the grant of the privilege to use the patented invention without the threat of an infringement claim, whether or not the invention was actually used. Such consideration was good irrespective of the patent's validity. Accordingly, a claim by the licensee that the patent was invalid was irrelevant to an action by the patentee for the minimum royalty due under the license agreement and therefore barred under the doctrine of licensee estoppel. The licensee's unilateral repudiation of the agreement did not release the estoppel since, in light of the licensee's stated intent to refrain from any use of the patented invention, the repudiation would not result in furthering the public's interest in testing the validity of a potentially worthless patent in an infringement suit. Only the expiration of the license agreement or the termination of the agreement in accordance with its terms (i.e., the releasing events specified in the termination rule) could free the licensee in *Elgin* from its minimum royalty obligation under the agreement and from the bar of licensee estoppel.^{133, 134}

132. *Id.* at 201-02.

133. Arguably, as a hybrid case that accepted the effectiveness of a unilateral repudiation in the majority of circumstances, the *Elgin* court would recognize an eviction as another releasing event that would free the licensee in *Elgin* from its minimum royalty obligation and from the licensee estoppel bar. *See also, infra* note 147 regarding an eviction that results from a judicial invalidation of the licensed patent in a third party infringement suit by the court of last resort.

134. For a case in which an appellate court applied the traditional version of licensee estoppel but rejected the termination rule exception to the repudiation limitation, *see Armstrong Co. v. Shell Co. of California*, 277 P. 887 (Cal. Ct. App. 1929). In an action to recover amounts allegedly due under a patent license agreement, Armstrong (the patent holder) claimed that its licensee's attempted unilateral repudiation of the license was ineffective and, accordingly, the licensee was liable for payments due under the agreement and could not raise patent invalidity as a defense. Under the terms of the agreement, the licensee was obligated to pay Armstrong a total of \$100,000 for the privilege of using the patented process, whether or not it actually used the process. Payments were to be made either in the form of a running royalty over a ten-year period (5% of the net amount it received from the sale of gasoline produced through the patented process) or, if the licensee elected to terminate its royalty obligation, as a lump sum representing the difference between \$100,000 and the aggregate sum of the royalties already paid. The licensee repudiated the license prior to paying \$100,000 in royalties, based on its determination that the licensed patent was invalid, and refused to provide Armstrong with the remaining amount due under the contract. In repudiating the license, the licensee indicated that it had no intention of continuing its use of the patented process. The facts in the case met the essential requirements for the application of the termination rule exception to the repudiation limitation of licensee

We will revisit the arguments made in *Elgin* in Section III.B. of this Article in our analysis of another hybrid case, *Automatic Radio*.¹³⁵ The First Circuit's holding in that case, affirmed by the U.S. Supreme Court and cited in *Elgin*, provides a key insight into the central question under consideration in this Part III, i.e., what is the scope of the U.S. Supreme Court's repudiation of the doctrine of licensee estoppel in *Lear*? As noted above, the scope of the *Lear* holding is, in part, defined by the version of licensee estoppel that was rejected by the *Lear* Court in overruling the estoppel portion of its *Automatic Radio* decision.

estoppel, i.e., that the licensee's payment obligation under the contract persisted following its repudiation of the license despite the licensee's stated intent to refrain from further use of the patented invention. Specifically, the licensee in *Armstrong* had agreed to pay \$100,000 for the right to use the patented process but the obligation was not contingent upon actual use of the process. The licensee's repudiation of the license, based on alleged patent invalidity, was an attempt to avoid its agreed-to post-repudiation payment obligation. Nonetheless, the appellate court in *Armstrong* recognized the licensee's repudiation as valid, permitting the latter to challenge the licensed patent. While the patent at issue would not be tested in the context of a patent infringement suit, in light of the licensee's plan to refrain from future use of the patented process, the court concluded that the patent's validity was relevant to a determination of the licensee's post-repudiation payment obligation. In permitting the patent challenge, the court would not only resolve the issue under consideration in the case but would also further the public's interest in eliminating worthless patents. In the end, the *Armstrong* appellate court affirmed the trial court's ruling that the licensed patent was invalid and that the licensee in the case had no further payment obligation. In rejecting the termination rule exception to the repudiation limitation, the appellate court stated the following:

We see no merit in plaintiff's [Armstrong's] contention that defendant [licensee] cannot avail itself of the renunciation [i.e., repudiation] exception to the general rule of estoppel because defendant has not notified plaintiff that it would manufacture in hostility to or in defiance of the authority of the patent and license so that the licensor could thereafter proceed against it for infringement of the patent. It is true that many cases apply the renunciation exception in favor of the licensee who abandons the license and thereafter infringes the patent. Nevertheless, it is inconceivable that defendant would be liable under the contract despite the alleged invalidity of the patent solely because it discontinued the use of the process, whereas if it had continued the use of such process in defiance of the patent it could now successfully defend itself against any liability by showing the invalidity of such patent. The authorities do not permit the invalidity of a patent to be asserted as a defense to any liability which accrued before renunciation. The alleged obligation in the present case did not accrue before the renunciation notice was given on April 19, 1923, and defendant thereby brings itself within the exception to the rule of estoppel.

Armstrong, 277 P. at 892.

135. *Automatic Radio Mfg. Co. v. Hazeltine Research, Inc.*, 176 F.2d 799 (1st Cir. 1949), *aff'd*, 399 U.S. 827 (1950).

4. *Two recognized versions of the doctrine of licensee estoppel*

Having reviewed the case law addressing the limits of licensee estoppel, we can now describe the two generally recognized versions of the doctrine. The two versions constitute irreconcilable interpretations of licensee estoppel and can be distinguished by their respective limits and justifications. As will be demonstrated in subsequent sections of this Part III, an understanding of these different versions of the doctrine is essential to an appreciation of the debate regarding the scope of the U.S. Supreme Court's *Lear* decision.

The majority of courts that have endorsed licensee estoppel have adopted a version of the common law doctrine that is based on the relevance rule.¹³⁶ The rule holds that the actual validity of a licensed patent is irrelevant to the obligation of a patent licensee to pay royalties that accrued over the period during which the licensee enjoyed the benefits of the patent pursuant to the license agreement and, accordingly, a licensee is barred from challenging the patent's validity as a defense to an action by the licensor to recover the royalties.¹³⁷ The licensee's benefits derive from (1) the grant of a license under a presumptively valid patent that frees the licensee from the threat of an infringement challenge and (2) the deterrent effect of the patent right which discourages nonlicensed potential competitors from utilizing the claimed invention. The estoppel bar ceases, however, upon expiration or termination of the license agreement, eviction of the licensee as a result of the invalidation of the licensed patent in a third party infringement suit (the eviction limitation) or the unilateral repudiation of the license by the licensee (the repudiation limitation). Each of these releasing events ends the licensee's enjoyment of the benefits of the patent license, thereby permitting a licensee who continues to utilize the claimed invention in the role of a potential infringer to challenge the patent's validity in defense of a claim by the patent holder for royalties owed under the agreement. Under each of these altered circumstances, the validity of the patent becomes relevant to the patent holder's claim for future payments.

136. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 519 ("The majority of courts . . . appl[ied] the repudiation rule and allowed the licensees to challenge the licensed patent's validity after repudiating the license." (footnote omitted)); *see also id.* at 537.

137. *Id.* at 516 ("In sum, the rule prohibiting a patent licensee from challenging validity . . . can be stated as follows: the validity of the licensed patent is irrelevant to the licensee's obligation to pay royalties accrued before eviction or repudiation."); *see also id.* at 527, 535, 537.

The justification for this traditional version of licensee estoppel, based on the relevance rule, was found in the application of contract principles. The licensee's continued enjoyment of the benefits of the patent license under the agreement, and *not* the actual validity of the licensed patent, was the consideration for the obligation of the licensee to pay royalties.¹³⁸ It was not until the occurrence of a releasing event that resulted in an end of the consideration (e.g., an agreement expiration or termination), a failure of the consideration (e.g., an eviction) or a rejection of the consideration (e.g., a unilateral repudiation) that the licensee was free to challenge the licensed patent's validity in defense of a claim for future royalties. However, the traditional version of licensee estoppel was grounded in more than contract principles. The version's acceptance of the repudiation limitation, which permitted a licensee to unilaterally repudiate the license agreement in order to challenge the licensed patent, evinced a recognition of the important public policy in eliminating invalid patents that claim inventions that are properly in the public domain.¹³⁹ Rooklidge summarized the justifications for the traditional version of licensee estoppel in the following comment:

Under licensee estoppel as originally applied, . . . the licensee was only prevented from challenging validity as long as he accepted the benefits of the license. Once the licensee repudiated the license, he not only gave up any exclusive or deterrent effect, but also exposed himself to an infringement suit. The repudiation limitation was consistent with the policy basis for licensee estoppel [i.e. that the continued enjoyment of the benefits of the license under the agreement estops the licensee] and further fostered the policy of allowing validity challenges to illegitimate patents¹⁴⁰

138. See *Elgin Nat'l Watch Co.*, 118 N.Y.S.2d at 201 ("When the courts have held . . . that a licensee may not assert invalidity of the patent as a defense to a claim for accrued royalties, they have necessarily held that validity of the patent is not the essence of consideration for a licensing agreement and that freedom from an infringement claim, regardless of the validity of the claim, is good consideration."); see also Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 519–20 ("[L]icensee estoppel is based on conduct, and by ceasing that conduct the licensee ends the 'estoppel.' No longer 'taking the fruits of the land,' —immunity from an infringement suit and any deterrent effect of the patent — the licensee was freed to contest validity." (footnote omitted)).

139. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 520 ("[T]he public interest favors challenging illegitimate patents. The repudiation rule facilitates validity challenges by licensees." (footnote omitted)).

140. *Id.* at 522.

A minority of courts, however, rejected the traditional version of licensee estoppel in favor of a version of the doctrine that endorsed the termination rule.¹⁴¹ This version, labeled the “termination”¹⁴² or “strong form”¹⁴³ version of licensee estoppel, required that a license agreement either expire or terminate in accordance with its terms for the licensee estoppel bar to end. A unilateral repudiation of the agreement by the licensee was not an effective means of freeing the licensee to challenge the validity of the licensed patent as a defense in a suit brought by the licensor to recover royalties due under the agreement.¹⁴⁴

Unlike the traditional version of the licensee estoppel, the “strong form” version is a rigid doctrine based on the law of contracts that holds that the agreement estops the licensee from challenging a licensed patent and that the estoppel persists for the life of the agreement.¹⁴⁵ As stated by Rooklidge, “the licensor’s promise to forego an infringement suit is the consideration for the licensee’s payment of royalties, and therefore impliedly is the consideration for the licensee’s obligation to refrain from challenging validity. Under this notion, the obligations to pay royalties and refrain from challenging validity continue until termination or expiration of the license.”¹⁴⁶ Neither an eviction of the licensee¹⁴⁷ nor a repudiation of the license by the licensee,¹⁴⁸

141. See *supra* note 115; Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 521 (“Despite the Supreme Court’s implied sanction of repudiation [in *St. Paul Plow Works v. Starling*], . . . *St. Paul* led to a small line of cases rejecting repudiation. Those cases . . . focused on termination of the license agreement rather than repudiation.”); see also *id.* at 537.

142. *Id.* at 535–36.

143. Brief for the American Bar Association as Amicus Curiae Supporting Respondents at 10–11, *MedImmune*, 549 U.S. 118.

144. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 521 (“The reasoning of those cases [that endorsed the strong form version of licensee estoppel which incorporated the termination rule] was that because the licensee could not unilaterally terminate the contract, and because the licensee is estopped from challenging validity as long as the contract is in existence, the licensee was not freed to challenge validity by his repudiation.”).

145. *Id.* at 522. (“The policy basis for the termination rule [that defines the strong form version of licensee estoppel] is contractual—the contract estops the licensee.”).

146. *Id.* (footnote omitted).

147. *Id.* at 518–19 (“An eviction exception is anathema to what some courts perceived to be a rigid doctrine estopping the licensee from challenging the licensed patent’s validity.”). It should be noted, however, that at least one court that had endorsed the strong form version of licensee estoppel had also recognized an eviction limitation to the termination rule (which bars a licensee’s patent validity challenge until

unless a recognized termination event under the agreement that ends the parties' contractual obligations, is effective in releasing the estoppel under the "strong form" version of the doctrine.

The essential distinction between the two versions of licensee estoppel is aptly expressed in Rooklidge's characterization of the "strong form" version as a rule of estoppel and the traditional version as a rule of relevance.¹⁴⁹ According to that commentator, "[t]he policy basis for the termination rule [that defines the "strong form" version of licensee estoppel] is contractual—the contract estops the licensee."¹⁵⁰ In contrast, the relevance rule that defines the traditional version of licensee estoppel holds that "the validity of the licensed patent is irrelevant to the licensee's obligation to pay royalties accrued before . . . [cessation of the licensee's enjoyment of the benefits of the license]."¹⁵¹ The Amicus Brief of the American Bar Association in support of licensor Genentech in *MedImmune* provided the following comparison of the two versions of the licensee estoppel:

The traditional doctrine of licensee estoppel, as opposed to the "strong form" version . . . was equitable and well-supported. Traditional licensee estoppel imposes no irrevocable waiver of licensee challenges. Instead, the traditional doctrine simply requires licensees to choose between enjoying the benefits of the license and asserting the invalidity of the licensed patent. Under the doctrine, a licensee may choose either but not both . . . a licensee may assert the invalidity of the licensor's patent, but only after forgoing the benefits that the patent license provides.¹⁵²

the license agreement expires or is terminated in accordance with its terms), where the eviction results from a judicial invalidation of the licensed patent in a third party infringement suit *by the court of last resort*. In *Thomson Spot Welder Co.*, the Supreme Court of Michigan concluded that, despite its application of the "strong form" version of licensee estoppel in the case before it, a licensee whose agreement had not yet expired or terminated in accordance with its terms could still raise patent invalidity as a defense to a claim for royalties owed under the agreement if the patent at issue had been invalidated by a court of last resort, thereby voiding the agreement for failure of consideration. 240 N.W. at 94.

148. See *supra* note 144.

149. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 509, 511, 516, 521–22, 527, 535–36.

150. *Id.* at 522. See *supra* note 145.

151. *Id.* at 516. See *supra* note 137.

152. Brief for the American Bar Association as Amicus Curiae Supporting Respondents at 11, *MedImmune*, 549 U.S. 118.

An understanding of the two versions of licensee estoppel is useful in addressing the question, raised in *MedImmune* and discussed below, of whether any vestige of the doctrine remains in effect today. In Part II.B. of this Article we review the U.S. Supreme Court's decision in *Automatic Radio*¹⁵³ in which the Court provided its final endorsement of the doctrine of licensee estoppel. In Part II.C. we analyze the U.S. Supreme Court's *Lear* holding¹⁵⁴ in which the Court overruled the estoppel portion of its *Automatic Radio* decision in rejecting the doctrine. What is clear in *Lear* is that the Court abrogated a version of licensee estoppel that had been eroded over the years through the recognition by the Court of a number of non-contract-based policy-driven exceptions to the doctrine that will be discussed in the next section of this Article. What is unclear is the scope of the Court's repudiation of licensee estoppel, i.e., was the Court's holding in *Lear* limited to only one version of the doctrine? While the U.S. Supreme Court's endorsement of license estoppel in *Automatic Radio* was without meaningful analysis, the First Circuit's ruling in the case¹⁵⁵ reflected considerable thought and suggests that the circuit court had endorsed a version of the doctrine that had incorporated the termination rule exception to the repudiation limitation described in our discussion of the *Elgin* case,¹⁵⁶ i.e., an atypical version that endorsed elements of the "strong form" version of licensee estoppel. Moreover, a compelling case can be made for the view that the California Supreme Court in its *Lear* decision¹⁵⁷ adopted the termination version of licensee estoppel. Accordingly, the possibility remains open that the U.S. Supreme Court's rejection of licensee estoppel in *Lear*, in which the Court overruled *Automatic Radio* and vacated the California Supreme Court's holding in the case, was nothing more than a rejection of the "strong form" version of licensee estoppel. According to that interpretation, the *Lear* Court did not undermine the vitality of the traditional form of the doctrine that would estop, on substantive contract grounds, a licensee in good standing (i.e., a licensee who is in full compliance with the terms of, and enjoying all of the benefits afforded by, a patent license agreement that had neither expired nor terminated, and who

153. 339 U.S. 827.

154. 395 U.S. 653.

155. 176 F.2d 799.

156. *Elgin Nat'l Watch Co.*, 118 N.Y.S.2d 197; see *supra* Part III.A.3.b.

157. *Adkins*, 64 Cal. Rptr. 545.

had neither been evicted nor had repudiated the license) from challenging the validity of the licensed patent. The question as to the scope of the *Lear* Court's rejection of licensee estoppel, raised but not resolved in *MedImmune*, will be addressed in the remaining sections of this Part III.

5. *Exceptions to the estoppel doctrine*

In the years between the U.S. Supreme Court's application of licensee estoppel in *Harvey Steel* and its final affirmation of the doctrine in *Automatic Radio*, the Court crafted a number of exceptions to the doctrine. These exceptions appear to differ from the limits to the doctrine that were discussed above in section III.A.3. The limits defined the scope of licensee estoppel, were generally justified on the basis of contract principles (e.g., a failure of consideration or the end of a bargained-for exchange), and did not by their acceptance tend to undermine the vitality of the doctrine, which itself was rooted in contract principles. In contrast, as will be discussed below, the exceptions crafted by the U.S. Supreme Court were justified under non-contract policy considerations that trumped contract principles (e.g., patent law or antitrust public policy concerns) and, accordingly, challenged the underpinnings of the estoppel doctrine. On closer analysis, however, the distinction between the limits and the exceptions to licensee estoppel tended to blur, especially with respect to the repudiation limitation. Recall that in *Elgin*, the repudiation limitation was justified on the basis of patent public policy and not contract principles. For purposes of this section, however, resolution of a debate regarding the distinction between limits and exceptions is unnecessary. What is significant is the fact that in the years preceding the U.S. Supreme Court's decision in *Lear*, the Court saw fit to identify exceptions to licensee estoppel and relied on these exceptions in *Lear* as evidence of a significant erosion of the doctrine that justified its repudiation.

a) Patent policy exceptions

In *Westinghouse Electric & Manufacturing Co. v. Formica Insulation Co.*,¹⁵⁸ the U.S. Supreme Court initiated its assault on the doctrine of licensee estoppel by endorsing what is most accurately described as a qualification of the estoppel doctrine. The case involved the scope of assignor estoppel, a contract-based

158. 266 U.S. 342 (1924).

prohibition to the challenge of a patent's validity that is considered closely related to the doctrine of licensee estoppel.¹⁵⁹ In assignor estoppel, the assignor of a patent is estopped from challenging the validity of the assigned patent as a defense to a claim of patent infringement brought by the assignee. The Court in *Westinghouse* acknowledged that the assignor was barred from challenging the validity of the assigned patent but qualified the estoppel doctrine by permitting the assignor to reference the prior art to narrow the patent claims to the scope that the government intended in granting the patent right.¹⁶⁰ In the words of the Court, "the state of the art can not be used to destroy the patent and defeat the grant, because the assignor is estopped to do this. But the state of the art may be used to construe and narrow the claims of the patent, conceding their validity. The distinction may be a nice one but seems to be workable."¹⁶¹

In *Scott Paper Co. v. Marcalus Manufacturing Co.*,¹⁶² another case involving assignor estoppel, the U.S. Supreme Court endorsed a more direct attack on the estoppel doctrine. Relying on patent law and public policy, the *Scott* Court allowed the assignor of a patent to defend an infringement suit by the assignee on the ground that the allegedly infringing device was an invention claimed in an expired patent and, accordingly, was in the prior art and available for

159. See *supra* note 61.

160. The Court in *Westinghouse* supported its holding by comparing the conveyance of land with the assignment of a patent:

The analogy between estoppel in conveyances of land and estoppel in assignments of a patent right is clear. If one lawfully conveys to another a patented right to exclude the public from the making, using and vending of an invention, fair dealing should prevent him from derogating from the title he has assigned, just as it estops a grantor of a deed of land from impeaching the effect of his solemn act as against his grantee. The grantor purports to convey the right to exclude others, in the one instance, from a defined tract of land, and in the other, from a described and limited field of the useful arts. The difference between the two cases is only the practical one of fixing exactly what is the subject-matter conveyed. A tract of land is easily determined by survey. Not so the scope of a patent right for an invention.

As between the owner of a patent and the public, the scope of the right of exclusion granted is to be determined in the light of the state of the art at the time of the invention. Can the state of the art be shown in a suit by the assignee of a patent against the assignor for infringement to narrow or qualify the construction of the claims and relieve the assignor from the charge? . . . We think, . . . [yes, since] the better rule, in view of the peculiar character of patent property, is that the state of the art may be considered. Otherwise the most satisfactory means of measuring the extent of the grant the Government intended and which the assignor assigned would be denied to the court in reaching a just conclusion. 266 U.S. at 350-51.

161. *Id.* at 351.

162. 326 U.S. 249 (1945).

unrestricted public use. In the words of the Court, “any attempted reservation or continuation in the patentee or those claiming under him of the patent monopoly, after the patent expires, whatever the legal device employed, runs counter to the policy and purpose of the patent laws.”¹⁶³ The Court concluded that:

the patent laws preclude the patentee of an expired patent and all others including petitioner [assignee] from recapturing any part of the former patent monopoly; for those laws dedicate to all the public the ideas and inventions embodied in an expired patent. They do not contemplate that anyone by contract or any form of private arrangement may withhold from the public the use of an invention for which the public has paid by its grant of a monopoly and which has been appropriated to the use of all. The rights in the invention are then no longer subject to private barter, sale, or waiver It follows that the patent laws preclude the petitioner assignee from invoking the doctrine of estoppel, as a means of continuing as against respondent, his assignor, the benefit of an expired monopoly, and they preclude the assignor from estopping himself from enjoying rights which it is the policy of the patent laws to free from all restrictions. For no more than private contract can estoppel be the means of successfully avoiding the requirements of legislation enacted for the protection of a public interest The patent laws preclude us from saying that the patent assignment, which they authorize, operates to estop the assignor from asserting that which the patent laws prescribe, namely, that the invention of an expired patent is dedicated to the public, of which the assignor is a member.¹⁶⁴

b) Antitrust-related exceptions

In the series of three cases, starting with *Sola Electric Co. v. Jefferson Electric Co.*,¹⁶⁵ the U.S. Supreme Court developed an expanding exception to licensee estoppel based on the public interest in support of the antitrust laws.¹⁶⁶ In *Sola*, the Court

163. *Id.* at 256.

164. *Id.* at 256-57 (citations omitted).

165. 317 U.S. 173 (1942).

166. *Id.*; *Edward Katzinger Co. v. Chicago Metallic Mfg. Co.*, 329 U.S. 394 (1947); *MacGregor*, 329 U.S. 402.

concluded that a patent licensee is not estopped “by virtue of his license agreement, . . . to challenge a price-fixing clause in the agreement by showing that the patent is invalid, and that the price restriction is accordingly unlawful because not protected by the patent monopoly.”¹⁶⁷ According to the Court,

[t]he contract provided that the license was granted on condition that the “prices, terms, and conditions of sale, for use or sale” throughout the licensed territory should not be more favorable to petitioner’s [licensee’s] customers than those prescribed from time to time by respondent [patent holder/licensor] for its own sales and those of its other licensees. Respondent sought recovery of unpaid royalties and also an injunction restraining further sales except in conformity to the terms of the license agreement.¹⁶⁸

In allowing the licensee’s validity challenge, the Court stated that “[l]ocal rules of estoppel which would fasten upon the public as well as the petitioner the burden of an agreement in violation of the Sherman Act must yield to the Act’s declaration that such agreements are unlawful, and to the public policy of the Act which in the public interest precludes the enforcement of such unlawful agreements.”¹⁶⁹

In *Edward Katzinger Co. v. Chicago Metallic Manufacturing Co.*,¹⁷⁰ the U.S. Supreme Court relied on its decisions in *Scott Paper* and *Sola* in holding that “the defendant [licensee], in a suit to recover royalties only [*i.e.*, no attempt to also enforce the price-fixing provisions] under a terminated patent license agreement containing price-fixing provisions, can challenge the validity of the patent despite a covenant in the license contract that he would not do so.”¹⁷¹ The Court concluded that:

[t]he royalties here claimed accrued, if they accrued at all, prior to the time the license agreement terminated. Consequently, the fact of subsequent termination does not free the promise to pay royalties from the taint of the price-fixing provision. Nor does the fact, if it be a fact, that [licensee]

167. 317 U.S. at 173.

168. *Id.* at 174.

169. *Id.* at 177.

170. 329 U.S. 394.

171. *Id.* at 395.

Metallic itself suggested the price-fixing provision, bar Metallic's challenge to the patent's validity. For the contract was still illegal, whoever suggested it, so that there is no less reason for leaving the way open to challenge the patent as a service to the public interest than if [patent owner/licensor] Katzinger had suggested price-fixing. Finally, Metallic's specific contract not to challenge the validity of Katzinger's patent can no more override congressional policy than can an implied estoppel.¹⁷²

As in *Katzinger*, decided on the same day, the Court held in *MacGregor v. Westinghouse Electric & Manufacturing Co.*¹⁷³ that a patent licensee can defend on the ground of patent invalidity "a suit for royalties only under a licensing agreement which contains a price-fixing provision."¹⁷⁴ In *MacGregor*, Justice Frankfurter provided his dissent from the decisions of the Court in both *MacGregor* and *Katzinger*.¹⁷⁵ He offered a compelling defense of the doctrine of licensee estoppel and particularly objected to the expansion of the antitrust exception that occurred in *Katzinger* and *MacGregor*. He emphasized that in *Sola*, the Court permitted a licensee to challenge the validity of a licensed patent as a defense in an action brought by the licensor to enforce a price-fixing provision that was a violation of the antitrust laws in the absence of a valid patent. As Justice Frankfurter explained:

the *Sola* case, like . . . [*Katzinger* and *MacGregor*], arose out of a claim for royalties under a patent license. But that there was a claim for royalties was hardly mentioned in the Court's opinion in the *Sola* case. The sole issue to which our attention was directed was a prayer that the licensee be enjoined from breach of his promise to abide by the prices fixed by the licensor for the sale of articles manufactured under the patent

The precise issue which we decided in the *Sola* case is not a matter for inference or conjecture. It was explicitly defined and delimited It was not whether a licensee may challenge the validity of a patent when sued for royalties. It

172. *Id.* at 401-02.

173. 329 U.S. 402.

174. *Id.* at 404.

175. *Id.* at 408-16.

was not whether a provision for price-fixing undermined rights under estoppel against a licensee. It was whether the licensor could show the special dispensation pertaining to the holder of a valid patent, which entitles him to fix the price of a commodity manufactured under his patent, although such a pricing agreement would be unenforceable in the generality of cases.¹⁷⁶

According to Justice Frankfurter, “[a]ll that the *Sola* case held, and the only thing it held, was that a valid patent is indispensable to . . . [the] right to fix prices.”¹⁷⁷

In *Katzinger* and *MacGregor*, however, the Court endorsed a licensee’s patent validity challenge in a suit by the patent holder/licensor only to recover royalties; while each of the relevant license agreements contained a price-fixing provision, no effort was made on the part of the licensor to enforce that provision. This “distinction with a difference”¹⁷⁸ served as the basis for Justice Frankfurter’s dissent.

In . . . [*Katzinger* and *MacGregor*] price-fixing is not an issue. We are not asked to allow the licensor to have the benefit of a practice available only under a valid patent. To grant relief here will not, unlike the *Sola* case, approve a practice *prima facie* in restraint of trade. What we here have to decide is whether we shall allow the licensee to repudiate an agreement for the payment of money made in an arm’s length transaction. For nearly a hundred years this Court has uniformly answered that question by using the legal shorthand of estoppel.¹⁷⁹

In his defense of the historic doctrine of licensee estoppel, Justice Frankfurter emphasized that the doctrine was unanimously endorsed in *Kingsman v. Parkhurst* ninety years before and was unanimously applied in *United States v. Harvey Steel Co.* fifty years later. He then noted that before and after those cases “a weighty body of cases affirmed and applied that doctrine with rare unanimity”¹⁸⁰ in all English-speaking jurisdictions. He also noted

176. *Id.* at 411.

177. *Id.* at 413.

178. *Id.* at 415.

179. *Id.* at 412-13.

180. *Id.* at 409.

that, despite four major patent statutes and numerous amendatory enactments, Congress never saw fit to abolish or limit the estoppel doctrine. He concluded his endorsement of the doctrine by stating that:

[i]f ever a doctrine has established itself as part of our law to be respected by the judiciary, this is it. If it is to be changed, Congress is there to change it. . . . We cannot do that. We can only adhere to the doctrine or overrule it. Until Congress does undo a principle so embedded in our law, we should leave it where we find it.

. . . But, in any event, if we are to wipe out so settled a phase of our law it should be done explicitly, not cryptically. In my judgment the *Sola* decision does not give adequate support for the Court's opinion. The cases before us necessarily involve the estoppel doctrine and cannot be disposed of without appearing to overrule a settled course of decision.¹⁸¹

Justice Frankfurter ended his dissent in *MacGregor* and *Katzinger* with the following words that have particular relevance in light of the uncertainty generated by the U.S. Supreme Court's subsequent decisions regarding licensee estoppel: "If a doctrine that was vital law for more than ninety years will be found to have now been deprived of life, we ought at least to give it decent public burial."¹⁸² As we will see in the next section, the doctrine survived, albeit in a somewhat eroded condition, to be endorsed again by the Court in *Automatic Radio*. It was not until the Court's decision in *Lear* that a "decent public burial" of licensee estoppel was held, and even with that decision the question remained as to whether any vestige of the doctrine survived. Answering that question is the goal of the remaining portion of this Part III.

B. *Automatic Radio Manufacturing v. Hazeltine Research*

In *Automatic Radio Manufacturing v. Hazeltine Research*,¹⁸³ the U.S. Supreme Court provided its final endorsement of the doctrine of licensee estoppel. The Court subsequently overruled the

181. *Id.* at 410.

182. *Id.* at 416.

183. 339 U.S. 827.

estoppel portion of its *Automatic Radio* holding in *Lear v. Adkins*.¹⁸⁴ Nonetheless, the *Automatic Radio* decision remains relevant in that the scope of the *Lear* Court's repudiation of licensee estoppel is, in part, defined by the version of the doctrine that was endorsed in *Automatic Radio* and rejected in *Lear*.

1. *Facts of the case and holding of the U.S. Supreme Court*

In *Automatic Radio*, the plaintiff Hazeltine Research (Hazeltine) brought an action against Automatic Radio Manufacturing (ARM) to recover royalties allegedly owed under a patent license agreement. Under the agreement, which had resulted from the settlement of a prior dispute between the parties,¹⁸⁵ ARM was granted a nonexclusive right to practice inventions relating to the manufacture of radio broadcasting apparatus, covered by a group of 570 patents and 200 patent applications. In consideration for the license grant, ARM agreed to pay a minimum annual royalty, as well as a running royalty calculated as a percentage of the total sales of its radio broadcasting receivers, whether or not ARM practiced any of the Hazeltine inventions covered by the licensed patents or applications in the manufacture of its receivers. Hazeltine's suit followed ARM's refusal to pay the agreed upon royalties, and ARM defended on the grounds that the royalty arrangement set forth in the license agreement constituted patent misuse, rendering the licensed patents unenforceable, that certain of the licensed patents were invalid, and that ARM had been evicted from its obligation under the license agreement based on the results of prior infringement litigation involving third parties. Five months after the initiation of the Hazeltine suit, ARM purportedly terminated its license agreement with Hazeltine by providing the latter with written notice of its repudiation of the agreement.

The district court in the case held for the plaintiff in granting Hazeltine's motion for summary judgment,¹⁸⁶ and the Court of

184. 395 U.S. 653.

185. Prior to the execution of the license agreement under consideration in *Automatic Radio*, Hazeltine had sued ARM for royalties allegedly owed under a prior license agreement between the parties relating to the Hazeltine radio receiver manufacturing technology. The suit was ultimately settled and a consent decree was entered by which ARM admitted its use of the Hazeltine technology and the validity of numerous Hazeltine patents. The license agreement under consideration in *Automatic Radio* was entered into as part of the settlement. *Hazeltine Research v. Automatic Radio Mfg.*, 77 F. Supp. 493, 495 (D. Mass. 1948).

186. *Id.* at 493.

Appeals for the First Circuit affirmed.¹⁸⁷ The U.S. Supreme Court “granted certiorari . . . in order to consider important questions concerning patent misuse and estoppel to challenge the validity of licensed patents.”¹⁸⁸ The Court, in affirming the decisions of the lower courts in favor of Hazeltine, first addressed ARM’s claim that the license agreement could not be enforced because the royalty provisions, which required a payment even if none of the licensed patents were used by ARM, was an impermissible extension of the patent monopoly constituting patent misuse. The Court agreed with the district court’s characterization of the license agreement “as essentially a grant by Hazeltine to petitioner [ARM] of a privilege to use any patent or future development of Hazeltine in consideration of a payment of royalties . . . [where] [p]ayment for the privilege is required regardless of use of the patents.”¹⁸⁹ However, the Court adopted the view of each of the lower courts that the royalty arrangement was “a convenient mode of operation designed by the parties to avoid the necessity of determining whether each type of petitioner’s product embodies any of the numerous Hazeltine patents.”¹⁹⁰ The Court concluded its patent misuse analysis with the following assessment:

We cannot say that payment of royalties according to an agreed percentage of the licensee’s sales is unreasonable. Sound business judgment could indicate that such payment represents the most convenient method of fixing the business value of the privileges granted by the licensing agreement. We are not unmindful that convenience cannot justify an extension of the monopoly of the patent. . . . But as we have already indicated, there is in this royalty provision no inherent extension of the monopoly of the patent. Petitioner cannot complain because it must pay royalties whether it uses Hazeltine patents or not. What it acquired by the agreement into which it entered was the privilege to use any or all of the patents and developments as it desired to use them. If it chooses to use none of them, it has nevertheless contracted to pay for the privilege of using existing patents plus any

187. *Automatic Radio Mfg.*, 176 F.2d at 799.

188. 339 U.S. at 830.

189. *Id.* at 833.

190. *Id.*

developments resulting from respondent's continuous research.^{191, 192}

The estoppel portion of the U.S. Supreme Court's *Automatic Radio* opinion was brief. The Court accepted without analysis that "[t]he general rule is that the licensee under a patent licensee agreement may not challenge the validity of the licensed patent in a suit for royalties due under the contract,"¹⁹³ citing *Harvey Steel*. It then rejected the argument that the antitrust-related exception to licensee estoppel articulated in *Katzinger* and *MacGregor* should apply in the instant case. In the words of the Court, "[t]here is no showing that the licensing agreement here or the practices under it were a misuse of patents or contrary to public policy The *Katzinger* and *MacGregor* cases are inapplicable. The general rule applies, and petitioner may not, in this suit, challenge the validity of the licensed patents."¹⁹⁴

2. *Uncertainty regarding the U.S. Supreme Court's licensee estoppel holding in Automatic Radio and insights from the First Circuit's*

191. *Id.* at 834 (citations deleted). The U.S. Supreme Court in *Automatic Radio* briefly addressed another contention of ARM in support of ARM's claim that the Hazeltine/ARM license agreement was unenforceable on the grounds that Hazeltine had misused its patents in granting a license to ARM. The license agreement contained a restricted use notice that required ARM to mark all licensed apparatus with the following statement: "Licensed by Hazeltine Corporation only for use in homes, for educational purpose, and for private, non-commercial use, under one or more of the following patents and under pending applications:" *Id.* at 835. According to ARM, the restriction on use was an impermissible extension of the patent monopoly and, therefore, patent misuse. Both the district court in the case and the First Circuit rejected this argument, holding that such a restriction on a patent licensee was enforceable under *General Talking Pictures Corp. v. Western Electric Co.*, 305 U.S. 124 (1938). The U.S. Supreme Court likewise rejected ARM's contention, but on the basis of its conclusion that any issue with respect to the restrictive notice provision in the agreement was moot in that Hazeltine had never sought to enforce the provision and had notified each of its licensees that it had authorized the deletion of the provision. In light of its conclusion, the Court did not address the legality of such a provision.

192. The holding of the U.S. Supreme Court in *Automatic Radio* with respect to the enforceability of the royalty arrangement set forth in the Hazeltine/ARM license agreement remains good law. The conclusion of the *Automatic Radio* Court that such an arrangement does not constitute patent misuse is frequently cited in support of the argument that a noncoerced extension of the physical scope of a patent in a patent license agreement (e.g., as in a total sales royalty or in a reach-through royalty arrangement) is permissible. See Alfred C. Server, Nader Mousavi and Jane M. Love, *Reach-Through Rights and the Patentability, Enforcement, and Licensing of Patents on Drug Discovery Tools*, 1 *Hastings Sci. & Tech. L.J.* 21, 75-92 (2009).

193. 339 U.S. at 836.

194. *Id.*

opinion in the case

The brevity of the estoppel portion of the U.S. Supreme Court's opinion in *Automatic Radio* is in stark contrast to the complexity of the relevant facts in the case, raising a question as to the actual basis for the Court's disallowance of ARM's patent validity challenge. Was the Court simply applying the traditional version of licensee estoppel, having rejected ARM's argument that the validity challenge should proceed under the antitrust-related exception to the doctrine articulated in *Katzinger* and *MacGregor*? Or did the Court in *Automatic Radio* block the validity challenge because ARM's attempted unilateral repudiation was ineffective in terminating its license agreement with Hazeltine, i.e., did the Court apply the "strong form" version of licensee estoppel that required the termination of a patent license agreement in accordance with its terms prior to a licensee patent validity challenge? Or, based on the particular facts in the case, did the Court rely on the termination rule exception to the repudiation limitation described above in Part III.A.3.b. of this Article? And of what relevance to the Court's estoppel holding was the fact that the license agreement in *Automatic Radio* had resulted from the settlement of a prior dispute between the parties involving the validity of certain of the licensed Hazeltine patents? As will be discussed later in this section, the First Circuit in *Automatic Radio* acknowledged the important public interest in respecting the settlement of litigation in its assessment of whether ARM should be permitted to challenge the Hazeltine patents and thereby reopen the issue of patent validity.¹⁹⁵

The uncertainty regarding the U.S. Supreme Court's licensee estoppel holding in *Automatic Radio* is evident in the conflicting interpretations of the case by commentators and in court briefs. According to Rooklidge, "*Automatic Radio* applied licensee estoppel as the rule had existed for over 100 years. Because the licensee had neither terminated nor repudiated the license agreement, the validity of the licensed patents was irrelevant."¹⁹⁶ In contrast, the authors of the ABA brief in *MedImmune* concluded that "the Court in [*Automatic Radio v.*] *Hazeltine* applied estoppel to the licensee without regard to whether the licensee had repudiated the benefit of the license. Thus, *Hazeltine* was an application of the 'strong

195. See *infra* section III.C.4.c.iii. (*Res Judicata* and Contractual Estoppel) for a discussion of Federal Circuit post-*Lear* case law endorsing estoppel following the settlement of patent litigation.

196. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 527.

form' licensee estoppel . . ."¹⁹⁷ In fact, neither the Rooklidge nor ABA view captures the complexity of the *Automatic Radio* holding. While the U.S. Supreme Court provided its approval of the doctrine of licensee estoppel with little analysis, the First Circuit in *Automatic Radio* (whose holding was affirmed by the U.S. Supreme Court) presented a more thoughtful discussion of the doctrine and ARM's defenses to Hazeltine's claim for royalties under the contract. Accordingly, we now turn to the First Circuit's opinion in the case for additional insights into the meaning of the U.S. Supreme Court's estoppel holding in *Automatic Radio*.

After rejecting ARM's patent misuse argument, which included an allegation of antitrust violations,¹⁹⁸ the First Circuit in *Automatic Radio* turned to the question of whether ARM should be permitted to challenge the validity of the Hazeltine patents. The court cited *Harvey Steel* for the proposition that in a suit for patent royalties under a license agreement the licensee is barred from challenging the licensor's patent, but noted that "this proposition can no longer be received without qualification"¹⁹⁹ in light of the U.S. Supreme Court's holdings in *Katzinger* and *MacGregor*. Each of the latter cases, however, involved a license agreement that contained a price-fixing provision, and the First Circuit refused to apply the antitrust-related exception to licensee estoppel to the facts in *Automatic Radio*, a case that did not implicate a price-fixing provision. In the words of the court, "[u]ntil we receive further light and leading from the Supreme Court, we are disinclined to extend the holdings in the *Katzinger* and *MacGregor* cases so as to throw into the discard altogether the long line of earlier cases disallowing a licensee to challenge the validity of the licensor's patent."²⁰⁰

The court then provided an additional justification for barring ARM's patent validity challenge, based on the fact that the patent

197. Brief for the American Bar Association as Amicus Curiae Supporting Respondents at 10, *MedImmune*, 549 U.S. 118.

198. In defense of Hazeltine's claim for royalties owed under the license agreement, ARM argued that Hazeltine had violated US antitrust law in its accumulation of large numbers of patents that would eliminate competition and create an unlawful monopoly. In rejecting ARM's defense, the First Circuit in *Automatic Radio* concluded the following: "[I]t appears that the defense of monopolistic practices is merely the assembling under a different heading of matters we have already considered. The district court correctly ruled that, even assuming arguendo that Hazeltine was engaged in an unlawful scheme to maintain a monopoly, the license contract in suit was not an integral part of it; that the license agreement, being itself a valid contract, will not be rendered unenforceable by collateral activities of the plaintiff in violation of the antitrust laws." 176 F.2d at 805.

199. *Id.* at 806.

200. *Id.*

license agreement under consideration resulted from the settlement of a prior litigation between the parties involving the validity of certain of the licensed Hazeltine patents. The court argued that:

[i]t is not uncommon for the parties to a patent infringement suit, in which there is a genuine issue as to the validity of the patent, to make a settlement of the litigation by an agreement under which the patentee gives a license to the alleged infringer in consideration of the payment of a stipulated royalty. Indeed, the license agreement in suit seems to have been by way of settlement of earlier litigation between the parties. It is not apparent to us that the public interest would be served by rendering such common-sense business settlements nugatory, which would be the result of a ruling that the licensee could reopen the issue of validity when sued for the stipulated royalty.²⁰¹

As will be discussed below in our review of the U.S. Supreme Court's *Lear* decision, this line of reasoning was not considered by the *Lear* Court in overruling the estoppel portion of the *Automatic Radio* holding.

The First Circuit concluded its assessment of whether ARM's patent validity challenge should be permitted by addressing the practical difficulties presented in the case. The court had determined that under the license agreement, ARM had agreed to pay royalties for the privilege of using any or all of the Hazeltine patents, which numbered well over 500, irrespective of whether ARM actually practiced any of the claimed Hazeltine inventions in the manufacture of its radio receivers. In considering this arrangement, the court acknowledged its uncertainty as to whether each of the licensed patents, only one of them or, if they could be identified, the most important of them would need to be invalidated for ARM to prevail in its defense. The court closed this part of its opinion by stating that "[i]f we are wrong in our conclusion that the licensee here cannot challenge the validity of the patents, then we confess we would be at a loss to know how to instruct the district court to precede with the case upon remand."²⁰² While the First

201. *Id.*

202. *Id.* at 806-07. ("In the case at bar, where a large number of patents were covered by a single license agreement containing no price-fixing stipulation, the result would be particularly awkward if it were held that the licensee may defend by putting in issue the validity of all these patents. Although *Automatic's* motion for summary judgment and

Circuit's practical argument against ARM's patent validity challenge is less than compelling from a jurisprudential standpoint, it undoubtedly factored into the court's endorsement of licensee estoppel in the *Automatic Radio* case.

Elsewhere in the First Circuit's *Automatic Radio* opinion, the court discussed two of the recognized limits to licensee estoppel, eviction and unilateral repudiation, which distinguished the traditional version of the doctrine from the "strong form" version.²⁰³ Significantly, the alleged occurrence of each of these events was raised by ARM as a defense to Hazeltine's claim for royalties owed under the license agreement and *not* as a justification for ARM's patent validity challenge.²⁰⁴ Nonetheless, the First Circuit's consideration of, and ultimate rejection of, the ARM defenses provides some insight into the version of licensee estoppel that the court endorsed in its *Automatic Radio* holding.

With respect to ARM's eviction defense, which the First Circuit understood to be a claim of failure of consideration, the court presented a number of arguments in support of its rejection of the defense. The basis of ARM's claim of eviction was the fact that ten of the licensed Hazeltine patents had been "litigated adversely to

its supporting affidavit make the general statement that none of Hazeltine's patents covered by the license are valid, no concrete attempt was made to buttress these assertions, and the district court concluded: 'Furthermore, the defendant does not purport to contest the validity of all plaintiff's patents.' D.C., 77 F. Supp. at page 497. We ourselves have been unable to find from the record that Automatic seriously attempted to raise a 'genuine issue' as to the validity of all the licensed patents. If the holding of the *Katzinger* and *MacGregor* cases were extended to the present situation, because of the restrictive use provision or otherwise, would the licensee, in order to make out its defense, have to establish that each and every one of the licensed patents is invalid? Or could the licensee maintain, in view of the fact that the stipulated royalties are payable whether or not any particular apparatus manufactured and sold by the licensee embodies any of the inventions covered by the patents, that the royalty agreement as an inseparable entirety becomes unenforceable if it can be shown that any one of the 500 licensed patents is invalid? Or, as a third alternative, would the licensee have to show that a substantial number of patents, or the more important patents constituting the 'substance' of the agreement, were invalid? If we are wrong in our conclusion that the licensee here cannot challenge the validity of the patents, then we confess we would be at a loss to know how to instruct the district court to proceed with the case upon remand. Whichever of the three alternatives above suggested were followed, it seems to us the resulting situation would be a mess, and the district court would likely be subjected to a well-nigh intolerable burden.") (citing Hazeltine Research., 77 F. Supp. at 497).

203. See *supra* section III.A.4.

204. The First Circuit in *Automatic Radio* began its discussion of the eviction defense as follows "Questions of direct attack upon validity aside, Automatic relies on the defense of eviction . . ." *Automatic Radio Mfg.*, 176 F.2d at 807.

Hazeltine”²⁰⁵ (all but one in lower courts only), and that these ten were considered by ARM to be the most important of the patents licensed under the agreement. The court dismissed this argument by noting that:

[t]he mere fact that Automatic may have regarded ten particular patents, out of the more than 700 patents and patent applications covered by the license agreement, as the most important ones licensed, in no sense means that *both* parties regarded those patents as the “substance” of the agreement and contracted accordingly. The record offers no significant suggestion that such was the case, and the district court concluded that Automatic “has not made any serious effort to show eviction here and could not show it”, and that Automatic got “by the contract, what it bargained for, namely, the right to use whatever patents are available for use in plaintiff’s large collection.” D.C., 77 F. Supp. at 497.²⁰⁶

The court then held that, even if ARM’s eviction defense had been properly presented, an eviction claim could not be supported in the context of a nonexclusive license. In the words of the court,

we may assume for present purposes that, where an exclusive license is granted and the patent is held invalid, even by a lower court, in a suit between the patentee-licensor and a third party, the licensee may successfully claim an eviction. An exclusive license agreement may be said to presuppose a grant to the licensee of a complete monopoly; if the patent is not upheld in even one suit against an infringer, the desired monopoly is pro tanto destroyed, and there may be said to be a failure of consideration But where the license, as here, is non-exclusive, this argument is inapplicable.²⁰⁷

The First Circuit concluded its analysis of ARM’s eviction defense by holding that such a defense by a nonexclusive licensee based on prior lower court judgments of patent invalidity in suits brought by the patentee/licensor against third parties was inconsistent with the U.S. Supreme Court’s ruling in *Triplett v.*

205. *Id.* at 807.

206. *Id.*

207. *Id.* at 808.

Lowell.²⁰⁸ The court cited *Triplett* for the proposition “that, even though in an earlier infringement suit against a third party some claims of a patent had been held invalid and the patentee had failed to disclaim them, the patentee might still maintain a suit against another alleged infringer for infringement of those same claims as well as other claims.”²⁰⁹ Based on the *Triplett* holding, the First Circuit argued that “it would be anomalous to give greater effect to a lower court’s judgment of invalidity in an infringement suit against a third party [in the instant case where ARM was a licensee] than would be given to such a judgment if . . . [ARM] had not been a licensee and had been sued as an infringer.”²¹⁰ According to the court, “a holding by one lower court that a patent is invalid is hardly a conclusive determination of that patent’s invalidity and hence the ‘worthlessness’ of a non-exclusive license of that patent.”²¹¹

In retrospect, a number of the First Circuit’s arguments in opposition to ARM’s eviction defense can be questioned. The contention that a licensee cannot be evicted from the enjoyment of the rights granted under a patent in the context of a nonexclusive license has been rejected by the majority of courts that have addressed the issue.²¹² Moreover, the U.S. Supreme Court’s *Triplett* decision, relied on by the First Circuit in *Automatic Radio*, was subsequently overruled in *Blonder-Tongue Lab v. University of Illinois Found.*²¹³ For purposes of this discussion, however, the strength of the First Circuit’s arguments regarding eviction is less significant than the suggestion in the court’s analysis that under appropriate circumstances an eviction defense could be supportable. Had ARM properly presented its eviction defense and had the license under which it had been granted rights to the Hazeltine patents been exclusive, the First Circuit may well have concluded that the invalidation of the licensed patents in infringement actions brought against third parties in lower courts effected an eviction, relieving ARM of its obligations to Hazeltine under its license agreement. Relieved of its obligations and, presumably, its patent rights under the license agreement, any subsequent use by ARM of the Hazeltine

208. 297 U.S. 638 (1936), overruled by *Blonder-Tongue Lab v. Univ. of Ill. Found.*, 402 U.S. 313 (1971).

209. 176 F.2d at 808.

210. *Id.*

211. *Id.*

212. *See supra* note 97.

213. 402 U.S. 313.

patents would be as an alleged third party infringer and not a licensee. In that capacity, ARM would be able to defend an action brought by Hazeltine for compensation by claiming that the Hazeltine patents were invalid, i.e., the eviction would work to free ARM from the licensee estoppel bar. In that eviction through judicial invalidation by lower courts is a recognized releasing event under the traditional, but not the “strong form,” version of licensee estoppel (the eviction limitation),²¹⁴ any suggestion by the First Circuit in *Automatic Radio* of its acceptance of the eviction limitation under any circumstance would indicate that the court had endorsed the traditional version of licensee estoppel in its opinion.

The First Circuit’s analysis of ARM’s attempted unilateral repudiation of its licensee agreement with Hazeltine provided further insight into the version of licensee estoppel under consideration by the court. As in the case of eviction, ARM’s unilateral repudiation argument was raised as a defense to Hazeltine’s claim for royalties owed under the license agreement and not as a justification for ARM’s patent validity challenge. The First Circuit began its assessment by noting that ARM’s repudiation defense had not been properly presented and that, even if the defense were successful, it would shield ARM from only a limited portion of its alleged liability for royalties owed, i.e., those that had accrued after ARM’s repudiation of its contract with Hazeltine, which occurred months after Hazeltine had initiated its suit. The court then addressed the question of whether ARM’s attempted repudiation was effective in terminating its license agreement with Hazeltine and concluded that a unilateral repudiation defense could not be supported in the instant case under either federal law or, “assuming that local law governs the matter,”²¹⁵ the law of the state of New York.

With respect to federal law, the court cited *St. Paul Plow Works v. Starling*²¹⁶ for the proposition that “in the absence of a cancellation option in the agreement, or of a substantial default by the licensor, the licensee cannot by any . . . unilateral notice of repudiation terminate its contract obligation under a license agreement having several years yet to run.”²¹⁷ As noted above in section III.A.3.(b), the U.S. Supreme Court in *St. Paul* rejected unilateral repudiation as a means of terminating a license agreement but did not question the

214. See *supra* section III.A.4.

215. 176 F.2d at 809.

216. 140 U.S. 184.

217. 176 F.2d at 809.

licensee's patent validity challenge in the case. Accordingly, the First Circuit's reliance on *St. Paul* in *Automatic Radio* adds little to our understanding of the court's views on the doctrine of licensee estoppel. However, the First Circuit's analysis of unilateral repudiation under New York law in the context of the particular circumstance of the *Automatic Radio* case was more nuanced and has relevance for interpreting the court's licensee estoppel holding. The court began by noting that "even if repudiation by the licensee is, in some circumstance, a defense in New York to a suit for royalties, Automatic's letter . . . [of repudiation] does not meet the stringent requirements set forth in . . . [the applicable New York case law]."²¹⁸ In other words, while the First Circuit acknowledged that a properly performed unilateral repudiation of a contract had been recognized as effective in the New York courts, ARM's "letter to Hazeltine formally advising the latter, without more, that . . . [it] 'has repudiated and terminated the License Agreement'"²¹⁹ failed to meet the applicable requirements for effectiveness. According to the First Circuit,

[t]he cases which have suggested the existence of some such doctrine of unilateral repudiation have explained that the licensee may announce unequivocally "that he no longer recognizes the binding force of the agreement, and that he will thereafter manufacture or use the article covered by the patent under a claim of right, founded upon the alleged invalidity of the patent, and in hostility to and defiance of the authority of the patent and the license, so that the licensor can thereafter proceed against him for an infringement of the patent, if he choose so to do." *Martin v. New Trinidad Lake Asphalt Co.*, supra, D.C.N.J., 1919, 255 F. at page 94. See *Skidmore v. Fahys Watch-Case Co.*, 1898, 28 App.Div. 94, 101, 50 N.Y.S. 1016, 1021-1022; *L. Heller & Son, Inc. v. Lassner Co.*, 1925, 214 App.Div. 315, 318, 212 N.Y.S. 175, 180.²²⁰

Of particular significance in the last excerpt is the requirement under New York law that for an effective unilateral repudiation of a patent license agreement, the licensee must go on record as having renounced the contract on the basis of the patent's alleged invalidity, with the intent to continue to practice the claimed

218. *Id.*

219. *Id.*

220. *Id.*

invention in the capacity of a potential infringer. This is a restatement of the repudiation limitation, recognized under the traditional (but not the “strong form”) version of licensee estoppel, that releases a licensee to challenge the validity of a licensed patent in an action brought by a patentee for royalties owed.²²¹ The fact that the First Circuit in *Automatic Radio* acknowledged the state of New York’s repudiation requirement, which itself incorporated a licensee’s allegation of patent invalidity, suggests that under the appropriate circumstances the First Circuit would have sanctioned the release of a repudiating licensee from the estoppel bar that the court had endorsed in its opinion, an outcome permitted only under the traditional version of the doctrine.

The First Circuit ultimately rejected ARM’s attempted unilateral repudiation, however, and would have done so even if ARM had met the procedural requirements for repudiation under New York law. According to the court, the nature of the license granted to ARM under the agreement did not allow for a unilateral repudiation by the licensee. The court presented the following analysis in support of its conclusion:

[U]nder the license agreement in suit Automatic’s liability for royalties does not depend upon its actual use of any of the licensed patents in the particular apparatus made and sold by it [because it had agreed to pay for the privilege of using the patented inventions regardless of its actual use]. If Automatic were permitted to repudiate the license agreement and in fact did not utilize any of the inventions covered by Hazeltine’s patents, Hazeltine could not prevail in an infringement suit even if all its patents were valid; and Automatic would thus achieve immunity from liability by non-use of Hazeltine’s patents, despite its contract undertaking to pay royalties, regardless of such use, for the right to make use of them. Hence, even assuming that a doctrine of unilateral repudiation might in some cases be recognized, such a defense certainly would not be available under the circumstance of the case at bar.²²²

The line of reasoning expressed in the First Circuit’s analysis is the same as that offered by the Appellate Division of the New York

221. See *supra* section III.A.4.

222. 176 F.2d at 809-10.

Supreme Court in *Elgin National Watch Co. v. Bulova Watch Co.*,²²³ a case that we described in section III.A.3.b as a “hybrid” in that the *Elgin* court had accepted as generally applicable the traditional version of licensee estoppel with its repudiation limitation but concluded that, based on the particular facts before it, unilateral repudiation could not effect the termination of the license agreement freeing the licensee from the estoppel bar, i.e., the court had adopted a termination rule exception to the repudiation limitation. In fact, the *Elgin* court relied on the First Circuit’s holding in *Automatic Radio* since both cases met the essential requirement for the application of the termination rule exception to the repudiation limitation, namely that the licensee can incur a royalty obligation following its unilateral repudiation of the license agreement without engaging in any activities that would infringe the licensed patent. The fact that *Automatic Radio* can be characterized as a hybrid case is additional evidence that the First Circuit had endorsed the traditional version of licensee estoppel in its opinion in the case, but with the above-noted exception to the doctrine.

3. *The Automatic Radio holding interpreted*

What then can be learned about the U.S. Supreme Court’s licensee estoppel holding in *Automatic Radio* from a review of the First Circuit’s opinion in the case? It is undisputed that the First Circuit applied licensee estoppel to block ARM’s patent validity challenge in *Automatic Radio* and rejected ARM’s claims of eviction and unilateral repudiation, recognized limits to the traditional version of the doctrine that defined circumstances under which a licensee was permitted to challenge the validity of a licensed patent. The First Circuit’s conclusion that ARM could not unilaterally repudiate its contract with Hazeltine, even if it had followed the procedure dictated by applicable state law, was of particular import in that it suggested that the court had adopted the “strong form” version of licensee estoppel which required that a license agreement either expire or terminate in accordance with its terms for the licensee estoppel bar to end. However, as noted above, ARM’s claims of eviction and unilateral repudiation were raised as a defense to Hazeltine’s pursuit of royalties owed, and not as a justification for ARM’s patent validity challenge. Moreover, the First Circuit’s estoppel ruling in *Automatic Radio* was significantly

223. 118 N.Y.S.2d 197.

influenced by the particular facts in the case, i.e., that (i) the license agreement between ARM and Hazeltine was entered into as part of a settlement of litigation between the parties, (ii) the license granted by Hazeltine was nonexclusive, (iii) the license granted by Hazeltine was to a “package” of over 700 patents and patent applications, and (iv) the royalties to be paid to Hazeltine were consideration for the privilege to use the licensed patents, irrespective of whether ARM actually practiced the claimed inventions. Whether the court would have come to the same conclusion in the estoppel portion of its holding had some of the facts in the case been different is open to speculation. But, as discussed in the preceding section, the First Circuit’s opinion in *Automatic Radio* can be interpreted as recognizing the applicability of the traditional version of licensee estoppel under the majority of circumstances, even if the facts in the case required a more nuanced approach.

Considering the complexity of the case, it is not surprising that knowledgeable commentators such as Rooklidge and the authors of the ABA brief in *MedImmune* have fundamentally different opinions regarding the meaning of the *Automatic Radio* holding. Recall that Rooklidge interpreted the *Automatic Radio* holding as applying the traditional version of licensee estoppel, while the authors of the ABA brief in *MedImmune* described the holding as an application of the “strong form” version of the doctrine.²²⁴ In fact, there is a measure of support for each of these views and our analysis in the preceding section suggests the following interpretation of the estoppel holding in *Automatic Radio* that would reconcile the seemingly inconsistent views of Rooklidge and the ABA authors: The First Circuit in the case endorsed the general applicability of the traditional version of licensee estoppel in the majority of circumstances, with its eviction and unilateral repudiation limitations and the antitrust-related exception previously crafted by the U.S. Supreme Court. The facts in the *Automatic Radio* case, however, did not justify the application of the antitrust-related exception nor support an eviction. Moreover, the nature of the license grant did not allow for a repudiation by the licensee, causing the court to invoke the termination rule exception to the unilateral repudiation limitation in concluding that ARM was estopped to challenge the validity of the Hazeltine patents. The U.S. Supreme Court affirmed the First Circuit’s estoppel holding in the case with limited analysis. Having agreed with the First Circuit that the

224. See *supra* section III.B.2.

antitrust-related exception to licensee estoppel did not apply, the Court found no need to even address ARM's eviction and repudiation defenses. The "general rule" of licensee estoppel that the U.S. Supreme Court endorsed in its holding, citing *Harvey Steel* in its sweeping affirmation, was the traditional version of the doctrine "as the rule had existed for over 100 years."²²⁵

In the end, however, it must be acknowledged that there is uncertainty as to the version of licensee estoppel that was endorsed by the U.S. Supreme Court in *Automatic Radio*. The significance of this uncertainty and its current relevance stems from the U.S. Supreme Court's rejection of the estoppel portion of the *Automatic Radio* holding in *Lear v. Adkins*, which remains the Court's controlling precedent on the doctrine of licensee estoppel and is reviewed in the next section of this Article. Uncertainty regarding the meaning of *Automatic Radio* results in uncertainty regarding the meaning of *Lear*.

C. *Lear v. Adkins*

In *Lear v. Adkins*, the U.S. Supreme Court vacated the California Supreme Court's decision in the case and overruled the estoppel portion of its prior *Automatic Radio* holding. As noted above, the Court's *Lear* decision remains the controlling precedent regarding the doctrine of licensee estoppel. An understanding of *Lear* is essential in determining whether any vestige of the doctrine of licensee estoppel survives that would bar a nonrepudiating licensee in good standing from challenging the validity of a licensed patent, and whether an explicit contract provision that prohibits, reduces the incentive for, and/or specifies a consequence of, a licensee's patent validity challenge is enforceable. In the section, we review the facts in *Lear* and the decisions of the California Supreme Court and the U.S. Supreme Court in the case. We then consider the scope of the *Lear* decision by assessing the direct effects of the holding, evaluating the language and reasoning of the Supreme Court's opinion in the case and reviewing relevant post-*Lear* case law. The latter review includes a discussion of a subsequent Supreme Court case that provided an interpretation of the *Lear* holding, regional circuit and district court decisions, the majority of which aggressively applied the *Lear* public policy argument to encourage patent validity challenges by licensees, and the Federal Circuit's efforts to limit the applicability of the *Lear* decision. We conclude

225. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 527.

this section with an analysis of the decision of the California district court that heard the *MedImmune* case on remand from the Supreme Court, a decision that relied on *Lear* in addressing the merits of the contract-based arguments against a patent validity challenge by a nonrepudiating licensee in good standing.

1. *The facts in Lear*

John Adkins was an inventor of improvements for gyroscopes. Lear, Incorporated, manufactured gyroscopes. In February 1954, Adkins filed a U.S. patent application covering his inventions. In September 1955 Adkins “entered into a written agreement with Lear under the terms of which he granted Lear a license to use these inventions in products manufactured by it, in exchange for which Lear was to pay a stated percentage of the net sales price to Adkins as royalties on all products incorporating his inventions.”²²⁶ The license agreement included two provisions pursuant to which Lear could terminate the agreement.

One was contained in paragraph 2(a) and provided: ‘Lear shall have the right on ninety days’ prior written notice to Adkins, to terminate any one or more of the licenses herein granted.’ The other, set forth in paragraph 6 of the agreement, stated, ‘In the event that *** the U.S. Patent Office refuses to issue a patent on the substantial claims of the application attached as Exhibit ‘B’, or if such a patent so issued is subsequently held invalid *** Lear at its option shall have the right forthwith to terminate the specific license so affected or this entire Agreement and no further royalties shall thereupon be payable under the license so terminated or under this Agreement if Lear shall have elected to terminate this Agreement in its entirety.’²²⁷

In March 1957, the U.S. Patent Office rejected certain of Adkins’ claims. Lear ceased paying royalties to Adkins on one type of its manufactured gyroscopes (the steel or Michigan gyros) in

226. *Adkins*, 64 Cal. Rptr. 545. Note that the initial license grant was exclusive, but became nonexclusive upon termination of Adkins’ employment by Lear in January 1958, prior to the filing of suit in the case, see *Adkins v. Lear*, 52 Cal.Rptr. 795, 806 (Cal.App. 1966). For an argument that the *Lear* holding should be limited to nonexclusive licenses and the rejection of that argument by the Seventh Circuit, see *Beckman Instruments, Inc. v. Technical Development Co.*, 433 F.2d 55 (7th Cir. 1970), discussed in note 337 *infra*.

227. *Adkins*, 64 Cal. Rptr. at 553.

September 1957 and on another type (the 2156 or California gyros) in April 1959. As summarized by the California Supreme Court in the case,

Lear wrote him [*i.e.*, Adkins] on September 10, 1957, that it had reviewed his patent application and concluded it did not disclose any inventions utilized in any Lear equipment except the 2156 gyro and certain components thereof, that the steel gyros manufactured by it did not come within the scope of the application, and that Lear had made a search of the Patent Office files [sic] and believed the method of bearing alignment used in assembling the steel gyros was not patentable. Lear also informed Adkins that it would no longer pay royalties on the steel gyros but would continue to do so on the 2156 gyro [A]fter another amendment of the application but before any action by the Patent Office on the amendment, Lear wrote Adkins on April 8, 1959, that it was exercising its right to terminate the license agreement under paragraphs 2(a) and 6. Royalty payments on the 2156 gyro were also discontinued.²²⁸

Despite its cessation of royalty payments and its letter of termination, Lear continued to manufacture and sell both types of gyroscopes.

In January 1960, the Patent Office granted a patent on Adkins' inventions. On the same day that the Adkins patent issued, Adkins sued Lear for failure to pay royalties, beginning in September 1957, due under the license agreement. Lear defended by claiming that it owed no royalties. Specifically, Lear argued that it had ceased paying royalties on the steel gyros because they did not embody inventions claimed in the Adkins patent, which nonetheless was invalid, and that it had ceased paying royalties on the 2156 gyros because it had terminated its license agreement with Adkins. The jury found in favor of Adkins, concluding that Lear had breached its license agreement and was liable for the royalties owed under the contract. Nonetheless, the trial court granted Lear's motion for judgment notwithstanding the verdict on the ground that the Adkins patent was invalid.²²⁹ The case was appealed to the California Supreme Court.²³⁰

228. *Id.* at 553-54.

229. The judgment notwithstanding the verdict applied only to the steel (and not the 2156) gyro, based on the argument made by Lear and accepted by the trial court that

2. *The holding of the Supreme Court of California – Application of the “strong form” version of licensee estoppel*

In *Adkins v. Lear*,²³¹ the Supreme Court of California focused its analysis on the fundamental question of whether or not Lear had validly terminated its license agreement with Adkins. The trial court in the case had granted Lear’s motion for judgment notwithstanding the verdict on the basis of its agreement with Lear’s assertion that the Adkins patent was invalid. And yet, as recognized by the California Supreme Court, the trial court’s opinion as to the validity of the Adkins patent had a bearing on the disposition of the case only if patent invalidity could be raised by Lear as a defense to Adkins’ claim for royalties owed under the license agreement. In other words, if licensee estoppel barred Lear from challenging the validity of the Adkins patent, the trial court had no basis for its judgment notwithstanding the verdict. And the question of whether the estoppel bar prevented Lear’s patent challenge hinged on whether Lear’s purported termination of the license agreement, which it relied on to justify its challenge, was in fact ineffective.

In addressing the questions before it, the California Supreme Court began with a discussion of its interpretation of the doctrine of licensee estoppel. In the words of the court, “one of the oldest doctrines in the field of patent law establishes that so long as a licensee is operating under a license agreement he is estopped to deny the validity of his licensor’s patent in a suit for royalties under the agreement. The theory underlying this doctrine is that a licensee should not be permitted to enjoy the benefit afforded by the agreement while simultaneously urging that the patent which forms the basis of the agreement is void This doctrine does not prevent one who is not a licensee from challenging the patent’s

(unlike the 2156 gyro) the steel gyro manufactured by Lear following its purported termination of the Adkins/Lear license agreement did not incorporate the Adkins invention. The California Supreme Court rejected this argument in concluding that both the steel and 2156 gyros incorporated the Adkins invention and, accordingly, Lear’s purported termination of the license agreement was not valid and it was prevented from challenging the validity of the Adkins patent under the “strong form” version of the doctrine of licensee estoppel endorsed by the court. This issue regarding the different gyros is not relevant to the discussion of the California Supreme Court’s interpretation in *Lear* of licensee estoppel that is provided in section III.C.2. of this Article and is not addressed in that section.

230. *Adkins*, 64 Cal.Rptr. 545.

231. *Id.*

validity.”²³² The court then provided its endorsement of the “strong form” or “termination” version of licensee estoppel.

Under the doctrine of licensee estoppel, Lear would be prohibited from challenging the validity of Adkins’ patent if the agreement had not been validly terminated. Where a license agreement specifies the conditions under which termination may occur, those conditions must be satisfied in order to effect a valid termination. (*Thomson Spot Welder Co. v. Oldberg Mfg. Co.* (1932) 256 Mich. 447, 240 N.W. 93, 94; see Ellis, *Patent Licenses* (3d ed. 1958) pp. 365–366 . . .) Here, the contract provided that it would continue in force until the patent relating to the subject matter of the agreement expired, unless sooner terminated pursuant to its provisions. We must, therefore turn our attention to the question whether Lear effected a termination of the license agreement.^{233, 234}

In a footnote to its opinion, the California Supreme Court rejected Lear’s argument in favor of the traditional version of licensee estoppel, with its repudiation limitation. “Lear relies on authorities holding that a licensee may terminate a license agreement upon notice to his licensor even though, prior to termination, there has been no adjudication of invalidity of the patent which is the subject of the agreement and that thereafter the licensee may challenge the validity of the patent. (See, e.g., *Armstrong Co. v. Shell Co. of Cal.* (1929) 98 Cal. App. 769, 778–779, 277 P. 887.) This rule has no application if the agreement sets forth the particular circumstances under which termination must occur. As stated above [in this opinion], such provisions must be complied with in order to effect a valid cancellation.”^{235, 236} In essence, the

232. *Id.* at 549–50.

233. *Id.* at 555.

234. See *Thomson Spot Welder Co.*, 240 N.W. at 94 (“If defendant [licensee] desired to terminate under the contract, it was required to fulfill the contract conditions thereof.”); ANTHONY W. DELLER, ELLIS, *PATENT LICENSES* 365–366 § 329(3d ed. 1958). “Types of Contract Provisions Which Bar Repudiation of License for Failure of Consideration Prior to Court Decision of Invalidity in Third Party Proceedings. . . . (4) Those by which the licensee has the right to terminate a specified interval of time after giving licensor notice to that effect. Where the parties specify the conditions under which termination can be made, it must ordinarily be presumed that the contract cannot be terminated otherwise.”

235. *Adkins*, 64 Cal.Rptr. at 555, n 15.

court held that under the circumstances in the instant case, where the license agreement at issue included two provisions that specified the requirements for early termination of the agreement, Lear was not able to unilaterally repudiate its contract with Adkins without complying with one of those requirements.

Having adopted the “strong form” version of licensee estoppel, the California Supreme Court presented its arguments in support of its conclusion that Lear had not validly terminated its license agreement with Adkins and, accordingly, was estopped from challenging the validity of the Adkins patent. Paragraph 2(a) of the license agreement stated that Lear had the right to terminate the agreement on ninety days’ prior written notice. The court concluded, however, that it was the intention of the parties that following such notice Lear would cease using the inventions claimed in the Adkins patent. In view of Lear’s continued use of the claimed inventions, the court held that Lear’s purported termination of the license agreement under paragraph 2(a) was not valid.

Under paragraph 6 of the license agreement, Lear had the right to terminate the agreement if either the U.S. Patent Office refused to issue a patent on the substantial claims of the patent application attached to the agreement or, if a patent issued, it was later invalidated. The court interpreted this provision as requiring a final rejection of the patent application, rather than the rejection of selected claims, and Adkins received no such final rejection. Moreover, the court held that the claims in the issued patent qualified as the substantial claims of the attached patent application. With respect to Lear’s right to terminate the agreement in the event that the Adkins patent was invalidated, the court noted that Lear could not exercise its right under this provision until after the patent issued. Lear’s notice of termination, however, preceded the issuance of the Adkins patent. The court cited *Harvey Steel*, a case that involved a similar contractual right to terminate on the invalidation of the licensed patent, for the proposition that “the licensee itself could not challenge the validity of the patent in a suit for royalties under the agreement.”²³⁷

The California Supreme Court concluded its analysis in the case by ruling that Lear’s purported termination of its license agreement

236. For a discussion of *Armstrong* as an example of a case that applies the traditional version of licensee estoppel, but rejects the termination rule exception to the repudiation limitation, see *supra* note 134.

237. *Adkins*, 435 P.2d at 331-32 (citing *Harvey Steel Co.*, 196 U.S. at 316).

with Adkins was ineffective. Lear had failed to meet the requirements for early termination specified in the contract. Moreover, under the “strong form” version of licensee estoppel adopted by the court, Lear was unable to unilaterally repudiate the contract. Accordingly, Lear remained a licensee under the agreement and was unable to challenge the licensed patent as a defense to Adkins’ claim for royalties owed under the contract. In that the validity of the Adkins patent was not open to question in the case, there was no basis for the trial court’s judgment notwithstanding the verdict and that judgment was reversed by the California Supreme Court, leaving Lear liable for the royalties owed.²³⁸

3. *The U.S. Supreme Court’s Lear decision*

The U.S. Supreme Court granted certiorari in the *Lear* case for the sole purpose of reconsidering the “general rule,” last endorsed by the Court in *Automatic Radio* and relied on by the California Supreme Court in *Lear*, that a licensee is estopped from challenging the validity of a licensed patent in a suit brought by the patent holder for royalties owed under a patent license agreement. As stated by the Court, “[s]ince the California Supreme Court’s construction of the 1955 licensing agreement is solely a matter of state law, the only issue open to us is raised by the court’s reliance upon the doctrine of estoppel to bar Lear from proving that Adkins’ ideas were dedicated to the common welfare by federal law.”²³⁹

The Court began its analysis by noting that since its *Automatic Radio* holding, the Court had decided two then-recent cases “emphasizing the strong federal policy favoring free competition in ideas which do not merit patent protection.”²⁴⁰ In *Sears, Roebuck & Co. v. Stiffel, Co.*²⁴¹ and *Compco Corp. v. Day-Brite Lighting, Inc.*,²⁴² cases decided on the same day, the Court addressed the issue of whether a party that manufactured and sold a copy of an

238. See Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 530 (“Application [by the California Supreme Court in *Lear*] of the termination rule, coupled with the requirement that the licensee cease manufacturing to effect a valid termination, effectively bound the licensee to pay royalties for the life of the agreement. The licensee was stuck despite the apparently liberal termination provisions in the license contract, its firm belief in the illegitimacy of the licensed patent, and its unequivocal repudiation of the agreement.” (footnote omitted)).

239. *Lear*, 395 U.S. at 661–62.

240. *Id.* at 656.

241. 376 U.S. 225 (1964).

242. 376 U.S. 234 (1964).

unpatented and uncopyrighted article could be enjoined from future sales and held liable for money damages as a result of unfair competition. In ruling against such an outcome, the Court had reasoned “that when an article is unprotected by a patent or a copyright, state law may not forbid others to copy that article. To forbid copying would interfere with the federal policy, found in Art. I, s 8, cl. 8, of the Constitution and in the implementing federal statutes, of allowing free access to copy whatever the federal patent and copyright laws leave in the public domain.”²⁴³

The Court then addressed the validity of the doctrine of licensee estoppel, acknowledging its long and complex history in the U.S. courts.

In considering the propriety of the State Court’s decision [in *Lear*], we are well aware that we are not writing upon a clean slate. The doctrine of estoppel has been considered by this Court in a line of cases reaching back into the middle of the 19th century. Before deciding what the role of estoppel should be in the present case and in the future, it is, then, desirable to consider the role it has played in the past.²⁴⁴

The Court cited *Kinsman v. Parkhurst*²⁴⁵ as the first U.S. Supreme Court case “that invoked estoppel in a considered manner,”²⁴⁶ but pointed out that it “was decided before the Sherman Act made it clear that the grant of monopoly power to a patent owner constituted a limited exception to the general federal policy favoring free competition.”²⁴⁷ The Court then noted that its decision in *St. Paul Plow Works v. Starling*,²⁴⁸ often cited as supporting the doctrine of licensee estoppel, in fact pointed in the opposite direction, in that the licensee’s challenge of the licensed patent was allowed without question. The Court next turned to its ruling in *Pope Manufacturing Co. v. Gormully*,²⁴⁹ in which the Court refused to enforce an explicit provision in the license agreement under consideration that prohibited the licensee from challenging the validity of the licensed patent. The *Lear* Court cited with approval

243. *Id.* at 237 (citing *Sears, Roebuck & Co.*, 376 U.S. 225).

244. *Lear*, 395 U.S. at 662–63.

245. 59 U.S. 289.

246. *Lear*, 395 U.S. at 663.

247. *Id.*

248. 140 U.S. 184.

249. 144 U.S. 224 (1892).

the reasoning relied on in support of the holding in *Pope*. “It is as important to the public that competition should not be repressed by worthless patents, as that the patentee of a really valuable invention should be protected in his monopoly.”²⁵⁰

The Court concluded its review of Supreme Court licensee estoppel jurisprudence by discussing its decisions in *Harvey Steel*²⁵¹ and *Automatic Radio*.^{252, 253} The former case, which had applied the estoppel doctrine, was criticized for neither citing nor considering the arguments set forth in *Pope*. The later case, which had provided the Court’s most recent endorsement of the “general rule” of licensee estoppel with limited analysis, was described as having ignored the teachings of a series of related decisions of the U.S. Supreme Court in the forty-five years since *Harvey Steel*. The cases referred to by the *Lear* Court – *Westinghouse Electric*,²⁵⁴ *Scott Paper*,²⁵⁵ *Sola Electric*,²⁵⁶ *Katzinger*,²⁵⁷ and *MacGregor*,²⁵⁸ – were each reviewed in the opinion and were discussed above in section III.A.5. of this Article. The point, according to the Court, was that each of these cases represented an exception to the estoppel doctrine that limited its scope and significantly diminished its vitality. The Court summarized the impact of these cases in the following excerpt:

During this [forty-five] period, each time a patentee sought to rely upon his estoppel privilege before this Court, the majority created a new exception to permit judicial scrutiny into the validity of the Patent Office’s grant. Long before [*Automatic*

250. *Lear*, 395 U.S. at 663–64 (quoting *Pope Mfg. Co.*, 144 U.S. at 234).

251. 196 U.S. 310.

252. 339 U.S. 827.

253. In a footnote, the *Lear* Court discussed two other early U.S. Supreme Court cases that touched on the right of the licensee to challenge a licensed patent (“There are two other early cases which enforced patent licenses without a thorough consideration of the estoppel issues that were presented. In *Eureka Co. v. Bailey Co.*, 11 Wall. 488 . . . (1871), the Court held that a licensee was obliged to overcome a ‘very strong presumption’ of patent validity in order to avoid his royalty obligations, without indicating how much more compelling a showing was required than was considered necessary in an ordinary infringement action. In *Dale Tile Manufacturing Co. v. Hyatt*, 125 U.S. 46 . . . (1888), this Court affirmed the decision of the New York state courts invoking the doctrine of licensee estoppel, on the ground that the estoppel question presented was one which involved only state law.”). 395 U.S. 653 n.11.

254. 266 U.S. 342.

255. 326 U.S. 249.

256. 317 U.S. 173.

257. 329 U.S. 394.

258. 329 U.S. 402.

Radio v.] *Hazeltine* was decided, the estoppel doctrine had been so eroded that it could no longer be considered the 'general rule,' but was only to be invoked in an evernarrowing set of circumstances.²⁵⁹

Following the review of its own relevant precedents, the Court in *Lear* looked to prior decisions of lower state and federal courts to further support its conclusion that the doctrine of licensee estoppel had been substantially eroded. Described as exceptions to the doctrine that "indicated a recognition of the broader policies pointing to a contrary approach,"²⁶⁰ the Court cited cases in which a licensee was permitted to challenge the validity of a licensed patent following an eviction from, or the unilateral repudiation of, the license agreement.

It is generally the rule that licensees may avoid further royalty payments, regardless of the provisions of their contract, once a third party proves that the patent is invalid. *See, e.g.,* Drackett Chemical Co. v. Chamberlain Co., 63 F.2d 853 (6 Cir., 1933). Some courts have gone further to hold that a licensee may notify the patent owner that he is repudiating his agreement, regardless of its terms, and may subsequently defend any action for royalties by proving patent invalidity. Note, The Doctrine of Licensee Repudiation in Patent Law, 63 Yale L.J. 125 (1953); R. Ellis, Patent Licenses § 328 (3d ed., A. Deller 1958).^{261, 262}

The Court's reliance on examples of eviction and unilateral repudiation to undermine the doctrine of licensee estoppel is of particular note. These so-called exceptions to the doctrine in fact established the limits of the traditional version of licensee estoppel, i.e., the relevance rule that incorporated the eviction and repudiation limitations. Rather than evidence of erosion of the

259. *Lear*, 395 U.S. at 664 .

260. *Id.* at 667.

261. *Id.*

262. The *Lear* Court cited a third exception to the doctrine of licensee estoppel recognized by lower courts: "And even in the 19th century, state courts had held that if the licensee had not actually sold products incorporating the patent's ideas, he could challenge the validity of the patent. *See* Forkosch, *Licensee Estoppel in Patent Law*, 20 Temp.L.Q. 515, 529, n.45 (1947)." *Lear*, 395 U.S. at 668.

“general rule” of licensee estoppel, the “exceptions” defined the “general rule.”²⁶³

In summarizing its review of the relevant case law, the *Lear* Court set the stage for the balancing test of competing interests that formed the basis for its holding in the case.

The uncertain status of licensee estoppel in the case law is a product of judicial efforts to accommodate the competing demands of the common law of contracts and the federal law of patents. On the one hand, the law of contracts forbids a purchaser to repudiate his promises simply because he later becomes dissatisfied with the bargain he has made. On the other hand, federal law requires, that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent. *Sears, Roebuck v. Stiffel Co.* . . . , *Compco Corp. v. Day-Brite Lighting, Inc.* When faced with this basic conflict in policy, both this Court and courts throughout the land have naturally sought to develop an intermediate position which somehow would remain responsive to the radically different concerns of the two different worlds of contract and patent. The result has been a failure. Rather than creative compromise, there has been a chaos of conflicting case law, proceeding on inconsistent premises.²⁶⁴

The *Lear* Court was now prepared to take a definitive stand on the estoppel question and began by considering the typical patent license agreement in which, in contrast to the instant case, a party obtains a license *after* the patent has issued. The Court identified the benefits afforded a licensee of an issued patent whose contents have already been made publicly available, namely, the freedom

263. See Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 534 (“The [*Lear*] Court cited eviction, repudiation, and the notion that a licensee could challenge the validity of the patent before it practiced the invention as further exceptions to licensee estoppel. These exceptions are fundamentally at odds with technical and equitable estoppel. However, these concepts were part and parcel of the doctrine of licensee estoppel. As the Court confused the policy behind licensee estoppel and inseparably twisted licensee estoppel with technical and equitable estoppel, these fundamental limitations were forgotten. *Lear*’s vilification of licensee estoppel as being fraught with exceptions was unwarranted. Rather, the Court should have separated the individual policies and rules making up licensee estoppel, technical estoppel, and equitable estoppel. Complexity and a history of poor application temporarily doomed all of these rules.” (footnote omitted)).

264. *Lear*, 395 U.S. at 668. (footnote omitted).

from the threat of an infringement suit and a reduction in competition from non-licensed third parties. The Court acknowledged that “[u]nder ordinary contract principles the mere fact that some benefit is received is enough to require the enforcement of the contract, regardless of the validity of the underlying patent.”²⁶⁵ According to the Court, however, this contract argument must be weighed against the important public interest in invalidating issued patents that claim subject matter that is, in fact, in the public domain. The Court explained that the typical patent results from a legal conclusion of the Patent Office which is reached in the context of an *ex parte* proceeding and is based on factors with respect to which reasonable persons can disagree. “Consequently, [the Court argued,] it does not seem to us to be unfair to require a patentee to defend the Patent Office’s judgment when his licensee places the question in issue, especially since the licensor’s case is buttressed by the presumption of validity which attaches to his patent.”²⁶⁶

The Court concluded this portion of its analysis with the most frequently cited statement from its opinion.

Surely the equities of the licensor do not weigh very heavily when they are balanced against the important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain. Licensees may often be the only individuals with enough economic incentive to challenge the patentability of an inventor’s discovery. If they are muzzled, the public may continually be required to pay tribute to would-be monopolists without need or justification. We think it plain that the technical requirements of contract doctrine must give way before the demands of the public interest in the typical situation involving the negotiation of a license after a patent has issued.²⁶⁷

On the basis of this reasoning and its review of the relevant case law, the *Lear* Court rejected the estoppel portion of its prior *Automatic Radio* decision with its statement that “[w]e are satisfied that *Automatic Radio Manufacturing Co. v. Hazeltine Research, Inc.* . . ., itself the product of a clouded history, should no longer be

265. *Id.* at 669.

266. *Id.* at 670.

267. *Id.* at 670-71.

regarded as sound law with respect to its ‘estoppel’ holding, and that holding is now overruled.”²⁶⁸

Having addressed the typical patent license scenario, the Court turned to the factors that distinguished the *Lear* case. As noted above, paragraph 6 of the Adkins/Lear license agreement provided that Lear’s royalty obligation was to continue during the term of the Adkins patent unless and until the patent was held invalid. Adkins argued that since the validity of his patent had not been finally determined in the case, Lear was required to pay the post-patent issuance royalties that Adkins sought, regardless of the licensed patent’s validity. The *Lear* Court rejected this view, arguing that enforcement of this explicit contract provision would significantly frustrate the important federal policy of eliminating specious patents, even if the licensee were permitted to challenge the validity of the licensed patent. In the words of the Court,

The parties’ contract . . . is no more controlling on this issue than is the State’s doctrine of estoppel, which is also rooted in contract principles. The decisive question is whether overriding federal policies would be significantly frustrated if licensees could be required to continue to pay royalties during the time they are challenging patent validity in the courts It seems to us that such a requirement would be inconsistent with the aims of federal patent policy. Enforcing this contractual provision would give the licensor an additional economic incentive to devise every conceivable dilatory tactic in an effort to postpone the day of final judicial reckoning. We can perceive no reason to encourage dilatory court tactics in this way. Moreover, the cost of prosecuting slow-moving trial proceedings and defending an inevitable appeal might well deter many licensees from attempting to prove patent invalidity in the courts. The deterrent effect would be particularly severe in the many scientific fields in which invention is proceeding at a rapid rate. In these areas, a patent may well become obsolete long before its 17-year term has expired. If a licensee has reason to believe that he will replace a patented idea with a new one in the near future, he will have little incentive to initiate lengthy court proceedings, unless he is freed from liability at least from the time he refuses to pay the contractual royalties. Lastly, enforcing this contractual provision would undermine the strong federal policy favoring

268. *Id.* at 671.

the full and free use of ideas in the public domain. For all these reasons, we hold that Lear must be permitted to avoid the payment of all royalties accruing after Adkins' 1960 patent issued if Lear can prove patent invalidity.²⁶⁹

The Court concluded its analysis by noting that Lear had been granted access to, and a license to exploit, trade secrets disclosed in Adkins' confidential patent application more than four years before the patent that claimed those secrets had issued. Accordingly, a portion of the royalties sought by Adkins i.e., the pre-patent issuance royalties, were in consideration for early access to those trade secrets. As stated by the Court, "[a]t the core of this case, then, is the difficult question whether federal patent policy bars a State from enforcing a contract regulating access to an unpatented secret idea."²⁷⁰ The Court rejected the "extreme position" taken by Adkins that, because of the special benefits provided Lear as a result of the early and privileged access to Adkins' invention, Lear was obligated to pay *all* of the royalties owed under the contract, i.e., those that had accrued prior to the patent's issuance, as well as those that had accrued and would continue to accrue during the term of the patent, regardless of the patent's validity. As noted above, the Court had also concluded that Lear could avoid paying the post-patent issuance royalties if Lear could prove that the Adkins patent was invalid. The Court declined, however, to determine whether Lear was liable for the royalties that had accrued *prior* to the issuance of the Adkins patent. As the Court explained:

we have concluded, after much consideration, that even though an important question of federal law underlies this phase of the controversy, we should not now attempt to define in even a limited way the extent, if any, to which the States may properly act to enforce the contractual rights of inventors of unpatented secret ideas. Given the difficulty and importance of this task, it should be undertaken only after the state courts have, after fully focused inquiry, determined the extent to which they will respect the contractual rights of such inventors in the future.^{271, 272}

269. *Id.* at 673-74 (paragraphing omitted).

270. *Id.* at 672.

271. *Id.* at 675.

272. The Court also declined to determine whether the Adkins patent was invalid, arguing that "... the California Supreme Court has yet to pass on the question of patent

For all of the reasons stated above, the *Lear* Court vacated the judgment of the California Supreme Court and remanded the case to that court for further proceedings not inconsistent with its opinion.

4. *The scope of the Lear decision*

A thorough understanding of the U.S. Supreme Court's *Lear* decision is essential in addressing the central questions posed in this Article, namely, can a nonrepudiating licensee in good standing challenge the validity of a licensed patent and is an explicit contract provision that prohibits or discourages a licensee patent validity challenge enforceable? While the Court's recent *MedImmune* decision, eliminating the jurisdictional barrier to a patent validity challenge by a licensee in good standing, may be the impetus for asking these questions, informed answers to the questions are to be found in an analysis of the Court's *Lear* decision. Insight into the meaning and scope of the U.S. Supreme Court's decision in *Lear* can be obtained through (1) an assessment of the direct effects of the Court's *Lear* holding i.e., the vacation of the California Supreme Court's decision in the case and the overruling of the estoppel portion of the Court's prior *Automatic Radio* holding, (2) an analysis of the Court's language and reasoning in *Lear*, and (3) a review of post-*Lear* case law, interpreting, endorsing and/or distinguishing the *Lear* holding. In the sections that follow, we pursue each of these approaches.

a) The direct effects of the *Lear* holding

Despite the uncertainty that the Court's *Lear* decision generated, it can be stated without equivocation that the Court in *Lear* vacated the California Supreme Court's holding in the case and overruled the estoppel portion of its prior *Automatic Radio* holding. Accordingly, a determination of the version of licensee estoppel that was endorsed in each of these earlier holdings provides valuable insight into the scope of the *Lear* Court's repudiation of the doctrine. Specifically, if both the *Automatic Radio* Court and the California Supreme Court in *Lear* had endorsed the "termination" or "strong form" version of license estoppel, then it can be reasonably argued

validity in that clear and unequivocal manner which is so necessary for proper adjudication in this Court" and, accordingly, "*Lear* must be required to address its arguments attacking the validity of the underlying patent to the California courts in the first instance." *Id.* at 675-76.

that the *Lear* Court's abrogation of the doctrine was limited to that version of licensee estoppel, leaving unaltered the viability of the traditional version of the doctrine. According to that view, a licensee in good standing (i.e., a licensee who is in full compliance with the terms of a patent license agreement that had neither expired nor terminated in accordance with its terms, and who had neither been evicted nor had repudiated the license) is estopped under the doctrine from challenging the validity of the licensed patent. On the other hand, if the "general rule" of licensee estoppel that was endorsed in *Automatic Radio* was the traditional version of the doctrine, then the *Lear* Court's rejection of the doctrine would necessarily extend beyond the "strong form" version applied by the California Supreme Court in the case to include the traditional version, thereby eliminating any vestige of licensee estoppel that would otherwise bar a licensee in good standing from challenging the validity of a licensed patent.

Earlier in this Part III, we presented arguments in support of a limited reading of the U.S. Supreme Court's *Lear* decision.²⁷³ That the California Supreme Court in *Lear* applied the "strong form" version of licensee estoppel is clearly demonstrated by a review of that court's opinion in the case and is generally accepted by commentators.²⁷⁴ In section III.B., we discussed the debate regarding the version of licensee estoppel that was endorsed in *Automatic Radio* and analyzed the view, expressed by some, that *Automatic Radio* was also an application of the "strong form" version of the doctrine. In adopting the above-stated interpretations of *Automatic Radio* and the California Supreme Court's decision in *Adkins v. Lear*—the cases most directly impacted by the U.S. Supreme Court's *Lear* holding—the authors of the ABA Brief in *MedImmune*²⁷⁵ reached the following conclusion: "Although the Court [in *Lear*] broadly articulated its holding, appearing to reject the doctrine of licensee estoppel in *toto*, what the Court necessarily

273. See the introductory paragraph of this Part III and sections III.B.3. and III.C.2.

274. See *supra* section III.C.2.; see also Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 530 ("In its discussion of licensee estoppel, the California Supreme Court [in *Lear*] adopted the termination rule. Rather than recognize the repudiation rule, the court harmonized the cases establishing repudiation as being without termination provisions." (footnotes omitted)); Brief for the American Bar Association as Amicus Curiae Supporting Respondents at 10, *MedImmune*, 549 U.S. 118 ("[T]he 'strong form' version of licensee estoppel [was] endorsed by the California Supreme Court [in *Lear*] . . .").

275. Brief for the American Bar Association as Amicus Curiae Supporting Respondents, *MedImmune*, 549 U.S. 118.

rejected in *Lear* was only the version of the doctrine applied by the California Supreme Court on the facts of the case. Accordingly, the true holding of *Lear* does not foreclose application of the doctrine to markedly different facts, including those here.”²⁷⁶ Even Rooklidge, who acknowledged that the *Automatic Radio* Court had endorsed the traditional version of licensee estoppel “as the rule had existed for over 100 years,”²⁷⁷ argued in favor of a limited reading of the U.S. Supreme Court’s *Lear* holding, largely on the basis of his conclusion that the Court’s *Lear* decision lacked precision and disregarded important aspects of the history of licensee estoppel.²⁷⁸ According to Rooklidge,

[i]n *Lear*, the [U.S. Supreme] Court correctly rejected a rule applied in a minority of courts—the termination variation of licensee estoppel. In doing so, however, the Court did not address the continued viability of the doctrine as it had been applied by the vast majority of courts since 1789

The history of licensee estoppel that preceded *Lear* has been universally ignored in analyses of that case’s holding. Nevertheless, in view of the history and true nature of the doctrine of licensee estoppel, *Lear, Inc. v. Adkins* should be narrowly limited to its holding, which is nothing more than a rejection of the termination version of licensee estoppel. Those with an appreciation of the history behind *Lear* will recognize that the case did not strike down the longstanding case law that validity of the licensed patent is irrelevant to the licensee’s obligation to pay royalties accrued before eviction or repudiation.²⁷⁹

276. *Id.* at 5.

277. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 527.

278. *Id.* at 527–28. (“In 1969, in *Lear, Inc. v. Adkins*, the United States Supreme Court rejected what it perceived to be the doctrine of licensee estoppel. However, *Lear* examined neither the doctrine, nor its history, with precision.”).

279. *Id.* at 537. (footnote omitted); see also Rooklidge, *Lear v. Adkins Revisited (Part II)*, *supra* note 68, at 5 (“In the celebrated case of *Lear, Inc. v. Adkins*, the United States Supreme Court struck down the patent law doctrine of licensee estoppel as applied by the California Supreme Court. The first part of this article concluded that the United States Supreme Court did not, in *Lear*, strike down another rule governing patent licensee validity challenges, one formulated in 1789 and long applied by the vast majority of courts. That rule states that the validity of the licensed patent is irrelevant to the licensee’s obligation to pay royalties accrued before eviction or repudiation. In simple terms, the general rule was that a patent licensee could not avoid its obligation to

While there is some support for the view that the *Lear* Court's abrogation of licensee estoppel was limited to the "strong form" version of the doctrine, our analysis leads to the conclusion that the U.S. Supreme Court in *Lear* rejected licensee estoppel in its entirety and not merely a variant of the doctrine accepted by a minority of courts. In section III.B. of this Article, we argued that *Automatic Radio* was a hybrid case in which the Court had accepted as generally applicable the traditional version of licensee estoppel with its repudiation limitation but concluded that, based on the particular facts before it, unilateral repudiation could not effect the termination of the license agreement freeing the licensee from the estoppel bar. According to this interpretation, the "general rule" of licensee estoppel that the *Automatic Radio* Court had endorsed, and the *Lear* Court had found to have been eroded by a series of Court-created exceptions, was the traditional and not the "strong form" version of the doctrine. The *Lear* Court's rejection of this "general rule" constituted a broad repudiation of the doctrine of licensee estoppel and eliminated any remaining bar to a patent validity challenge by a licensee, even if that licensee neither repudiates nor terminates its patent license agreement and intends to continue to reap the benefits provided under the agreement during the pendency of the challenge. The U.S. Government adopted this view in its amicus brief in favor of the petitioner in *MedImmune*,²⁸⁰ as indicated in the following excerpt:

The *Lear* Court carefully weighed the underlying justifications for the traditional contractual doctrine of licensee estoppel against the "important public interest" in encouraging challenges to potentially invalid patents, and concluded that "the technical requirements of contract doctrine must give way before the demands of the public interest in the typical situation involving the negotiation of a license after a patent has issued." 395 U.S. at 670-671. That determination forecloses any suggestion that vestigial notions of licensee estoppel can be employed to justify the creation of new obstacles to the adjudication of such challenges.²⁸¹

pay royalties on a license under a patent on the ground that the patent was held to be invalid." (footnotes omitted)).

280. Brief for the United States as Amicus Curiae Supporting Petitioner, *MedImmune*, 549 U.S. 118.

281. *Id.* at 29-30.

b) The language and reasoning of the *Lear* decision

The conclusion that the *Lear* Court rejected the doctrine of licensee estoppel in its entirety, based on the direct effects of the holding in the case, is bolstered by an analysis of the language and reasoning of the *Lear* opinion. The facts in the *Lear* case, however, did not require such a broad repudiation of licensee estoppel and this is the source of much of the uncertainty regarding the scope of the Court's holding. Unlike the licensee in *MedImmune*, which continued to honor its contractual obligations, including its commitment to pay royalties, during the pendency of its challenge of the licensed patent's validity, *Lear* had repudiated its license agreement with Adkins long before the Adkins patent had issued, alleging that the Adkins patent application claimed subject matter that was not patentable. The *Lear* Court's rejection of licensee estoppel in the context of a repudiating licensee has led some to conclude that the Court's holding does not extend to a licensee in good standing.²⁸² The authors of the ABA's amicus brief in *MedImmune* expressed this view in stating that "[o]n its facts, *Lear* properly stands for the proposition that a patent licensee may, upon repudiation of the license, contest the validity of the licensed patent *Lear* should not be read to permit a nonrepudiating licensee . . . to contest the patent's validity."²⁸³

The absence of any discussion in the body of the U.S. Supreme Court's *Lear* opinion regarding the impact of *Lear*'s purported unilateral repudiation of its license agreement on the Court's licensee estoppel holding added to the uncertainty regarding the reach of its decision. However, in a frequently neglected footnote to the opinion²⁸⁴ ("*Lear* Footnote 10"), the Court reviewed *Lear*'s repudiation argument and, in the course of its discussion, provided a critical insight into the scope of its licensee estoppel holding. *Lear* Footnote 10, offered by the Court in support of its jurisdiction to decide whether the California Supreme Court was correct in its reliance upon the doctrine of licensee estoppel to bar *Lear*'s patent validity challenge, reads as follows:

282. See Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 537; Brief for the American Bar Association as Amicus Curiae Supporting Respondents, pp. 2,5, *MedImmune*, 549 U.S. 118; *see also, supra* section III.C.4.a.

283. Brief for the American Bar Association as Amicus Curiae Supporting Respondents at 2, *MedImmune*, 549 U.S. 118.

284. *Lear*, 395 U.S. at 662 n.10.

Adkins claims that we have no jurisdiction to decide the federal question presented because the company did not adequately preserve it in its argument before the State Supreme Court. We do not agree. While it is true that Lear did not ask the Supreme Court to repudiate estoppel entirely, it did seek to persuade the court to carve out an exception to the estoppel principle which was so sweeping as to undermine the doctrine's vitality completely. The company argued, on the basis of federal as well as state cases, that a licensee may escape the impact of estoppel simply by announcing that it has repudiated the licensing agreement, regardless of the contract's terms. *See, e.g.,* Respondent's and Cross-Appellant's Opening Brief in Cases Nos. 28624 and 30089, at 110-111.

The California Supreme Court rejected this argument on its merits [based on its adoption of the "strong form" version of licensee estoppel, which did not recognize the repudiation limitation]

We clearly have jurisdiction to consider whether this decision is wrong. In doing so, we have the duty to consider the broader implications of Lear's contention, and vindicate, if appropriate, its claim to relief on somewhat different grounds than it chose to advance below, especially when the California court recognized . . . that matters of basic principle are at stake.²⁸⁵

In essence, the Court made the following points in *Lear* Footnote 10: (1) Lear had asked the Court to accept its argument, rejected by the California Supreme Court in the case, that its unilateral repudiation of the Adkins license agreement freed it from the estoppel bar; (2) such a request by Lear, which the Court viewed as "an exception to the estoppel principle which was so sweeping as to undermine the doctrine's vitality completely," justified the Court's decision to address the important federal question of whether licensee estoppel prevented Lear's patent challenge, and (3) the Court, in considering Lear's claim for relief, was not restricted to deciding the question presented by Lear regarding unilateral

285. *Id.*

repudiation, but could provide the requested relief “on somewhat different grounds than it [*i.e.*, *Lear*] chose to advance below,” such as “to repudiate estoppel entirely” for public policy reasons (which in the opinion of the authors of this Article, considering all of the available evidence, the U.S. Supreme Court, in fact, did).^{286, 287}

A broad reading of the *Lear* Court’s abrogation of the doctrine of licensee estoppel is also supported by the reasoning underlying the Court’s holding in the case. As will be discussed in the following paragraphs, the public policy argument relied on by the *Lear* Court in its rejection of licensee estoppel applies irrespective of whether a licensee who intends to challenge the validity of a licensed patent has repudiated, and thereby has forfeited the benefits of, its license agreement prior to the challenge.

The basis for the *Lear* Court’s abrogation of licensee estoppel is “the important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain.”²⁸⁸ As indicated above in section III.C.3., the Court in *Lear* structured its opinion around this fundamental policy consideration. It cited with approval the U.S. Supreme Court’s early articulation in *Pope v. Gormully* of the important federal policy favoring the elimination of worthless patents that repress competition.²⁸⁹ It criticized the decision in *Harvey Steel*, endorsing the doctrine of licensee estoppel, for ignoring “*Pope’s* powerful argument.”²⁹⁰ It characterized the Court-created exceptions to the estoppel doctrine in the years following *Harvey Steel* as repeated examples of the Court finding a way around the doctrine to permit judicial scrutiny into the validity of an issued patent, and faulted the *Automatic Radio* Court for disregarding the impact of those exceptions. In fact, the reason provided by the *Lear* Court for its granting of certiorari in the first place was to reconsider the

286. Quoted language taken from *Lear*, 395 U.S. at 662 n.10.

287. The content of *Lear* Footnote 10 provides further support for Rooklidge’s contention that the U.S. Supreme Court in *Lear* neglected important aspects of the history of licensee estoppel. See *supra* note 263; *supra* section III.C.4.a.; *supra* note 278. Specifically, the Court viewed the recognition by some lower courts of unilateral repudiation as a basis for permitting a licensee to challenge the validity of a licensed patent as a “sweeping” exception to the doctrine of licensee estoppel as opposed to a limit that defined the traditional version of the doctrine. See also, *supra* section III.C.3.

288. 395 U.S. at 670.

289. *Id.* at 663–64 (quoting *Pope*, 144 U.S. at 234 (“It is as important to the public that competition should not be repressed by worthless patents, as that the patentee of a really valuable invention should be protected in his monopoly . . .”).

290. *Lear*, 395 U.S. at 664.

Automatic Radio rule of licensee estoppel “in the light of our recent decisions [in *Sears* and *Compco*] emphasizing the strong federal policy favoring free competition in ideas which do not merit patent protection.”²⁹¹

The balancing test employed by the *Lear* Court in determining the fate of the doctrine of licensee estoppel pitted the above-mentioned public policy interest in eliminating specious patents against the “radically different concerns”²⁹² of contract law and, as we have already indicated, the policy encouraging patent challenges prevailed. The specifics of the Court’s argument are described above in section III.C.3. What is important for purposes of this discussion is that the line of reasoning relied on by the *Lear* Court to deprive a licensor of the protections of the common law doctrine of licensee estoppel applies even in the context of a patent validity challenge by a licensee in good standing.

The licensee in *Lear* did not seek the benefits of its license agreement following its cessation of royalty payments based on its conclusion that the Adkins’ invention could not be the subject of a valid patent. That fact, however, was not critical to the outcome of the *Lear* balancing test rejecting licensee estoppel. Nowhere in the Court’s discourse is there a suggestion that the outcome of its analysis would have come out differently and the equities favoring a patentee/licensor would have trumped the important public policy at stake if only the licensee had intended to continue to benefit under its license agreement while it pursued its challenge of the licensed patent. As noted in the preceding section, the *Lear* Court had introduced its balancing test in considering “the typical situation [in contrast to the situation in *Lear*] in which patent licenses are negotiated,”²⁹³ i.e., where the licensee obtains its license *after* the patent has issued. In this circumstance, the licensee invariably receives some benefit from the issued patent under the license agreement, even if the licensee subsequently repudiates its agreement and assumes the role of a potential infringer. The *Lear* Court acknowledged as much when it stated that “[u]nder ordinary contract principles the mere fact that some benefit is received is enough to require the enforcement of the contract, *regardless* of the validity of the underlying patent,”²⁹⁴ essentially restating the relevance rule of the traditional version of licensee estoppel. Yet the

291. *Id.* at 656.

292. *Id.* at 668.

293. *Id.* at 669.

294. *Id.* (emphasis added).

Court went on to reject this contract argument in concluding that receipt of a benefit under a contract did not justify depriving a licensee of the right to challenge the validity of the licensed patent (and thereby further the public interest in eliminating worthless patents) when pursued by the licensor for agreed-to payments due in consideration for the benefits received.²⁹⁵

The same logic applies even if the licensee is one in good standing who intends to continue to reap the benefits of the patent license during the pendency of its patent challenge. Such a licensee is furthering the same public interest by challenging the validity of the licensed patent that he is obligated by contract to continue to make payments to exploit. After all, a licensee in good standing “may . . . be the only individual . . . with enough economic incentive to challenge the patentability of an inventor’s discovery”²⁹⁶ and “it does not seem . . . to be unfair to require a patentee to defend the Patent Office’s judgment when his licensee places the question in issue, especially since the licensor’s case is buttressed by the presumption of validity which attaches to his patent.”²⁹⁷ As the *Lear* Court concluded, “the technical requirements of contract doctrine must give way before the demands of the public interest in the typical situation involving the negotiation of a license after a patent has issued,”²⁹⁸ and there is nothing in the Court’s opinion to suggest that this conclusion is contingent upon a licensee’s repudiation of its negotiated patent license agreement.

295. The *Lear* Court’s conclusion can be stated more precisely as follows: In the case of a typical patent license agreement that is ultimately repudiated by the licensee, neither the receipt by the licensee of benefits under the contract prior to the repudiation nor the prospect of ongoing benefits during the pendency of litigation for breach of contract (e.g., reduced competition based on the deterrent effect of a presumptively valid patent) is adequate justification for preventing the licensee from raising patent invalidity as a defense against the licensor’s contract claim. The basis for the Court’s conclusion was that a patent validity challenge by a licensee furthers the important public interest in eliminating worthless patents, and that that consideration trumps a licensor’s contract argument. The fact that a patent licensor may never receive compensation for *pendente lite* benefits received by a licensee (e.g., where the licensee withholds royalty payments during the litigation, as permitted under *Lear*, and is ultimately relieved of its obligation to make those payments because the licensed patent is found at trial to be invalid) did not alter the *Lear* Court’s conclusion. In essence, the Court in *Lear* ruled that the important public interest in eliminating worthless patents made the validity of a licensed patent “relevant” in an action brought by a patent licensor to recover royalties owed under a patent license agreement, irrespective of any benefits received by the licensee.

296. *Id.* at 670.

297. *Id.*

298. *Id.* at 670-71.

The *Lear* Court's balancing test has been criticized, largely on the basis of the Court's neglect of certain relevant factors that favored the patentee/licensor. For example, Rooklidge noted that the *Lear* Court failed to consider in its balancing of interests the important patent policy goals of fostering and rewarding inventions and promoting the public disclosure of those inventions.²⁹⁹ According to that commentator,

the Supreme Court in *Lear* considered only one of three policies underlying the patent system: the policy favoring invalidation of illegitimate patents. That lopsided policy balance was a product of the times, reflecting the then-prevalent hostility toward patent rights and the over-zealous application of antitrust principles to patent licensing. In fact, *Lear v. Adkins* marked the zenith of the ascendancy of antitrust law over patent law.³⁰⁰

Moreover, the *Lear* Court failed to consider the fact that the *Automatic Radio* license agreement had resulted from a settlement of litigation and that the Court in that case viewed the public policy interest in respecting settlements as relevant to its decision to bar the licensee's patent validity challenge. As will be demonstrated in the following section, the Federal Circuit relied on this policy consideration in barring certain licensee patent validity challenges in the context of a settlement. These criticisms of the *Lear* Court's balancing test, however, do not alter the fact that *Lear* remains the binding U.S. Supreme Court precedent with respect to licensee estoppel, nor do they undermine our conclusion that the *Lear* Court's abrogation of licensee estoppel was complete, leaving no vestige of the doctrine to protect a licensor from a challenge by a licensee in good standing. Moreover, there is little reason to believe that were the current Court to conduct the *Lear* balancing test that

299. Rooklidge, *Lear v. Adkins Revisited (Part I)*, *supra* note 68, at 534; Rooklidge, *Lear v. Adkins Revisited (Part II)*, *supra* note 68, at 15-16; Rooklidge, *Lear v. Adkins Revisited (Part III)*, *supra* note 68, at 69, 78. Rooklidge cited *Kewanee Oil v. Bicron Corp.*, 416 U.S. 470 (1974) and *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257 (1979) for an articulation of the three purposes of the federal patent system. ("First, patent law seeks to foster and reward invention; second, it promotes disclosure of inventions, to stimulate further innovation and to permit the public to practice the invention once the patent expires; third, the stringent requirements for patent protection seek to assure that ideas in the public domain remain there for the free use of the public." *Aronson*, 440 U.S. at 262 (citing, *Kewanee Oil Co.*, 416 U.S. at 480-81).

300. Rooklidge, *Lear v. Adkins Revisited (Part III)*, *supra* note 68, at 78. (footnotes omitted).

the outcome would be different, considering Justice Scalia's opinion for the majority in *MedImmune* expressing skepticism with respect to the merits-based contract arguments in support of the licensee estoppel bar³⁰¹ and the U.S. Supreme Court's recent decisions limiting the rights of patent holders.³⁰² One might say that the characterization of the U.S. Supreme Court, offered by Rooklidge in his critique of the *Lear* holding, as hostile toward patent rights is still appropriate today.

c) Post-*Lear* case law

A final perspective on the meaning and scope of the U.S. Supreme Court's *Lear* decision comes from post-*Lear* cases that interpreted, applied, and/or distinguished the *Lear* holding. As will be demonstrated in this section, the majority of these cases viewed the Court's *Lear* decision as a broad repudiation of the doctrine of licensee estoppel, although the Federal Circuit crafted a body of post-*Lear* case law that limited the *Lear* holding to its facts and set the stage for the dispute ultimately resolved by the Court in *MedImmune*.

i. The U.S. Supreme Court

In the years following the *Lear* decision, the U.S. Supreme Court has on occasion discussed the holding in the case.³⁰³ In no

301. See *supra* section II.B.

302. See Server, Mousavi & Love, *supra* note 192, at 21 n.143 ("See *Merck v. Integra*, 545 U.S. 193 (2005) (reversing the Federal Circuit's restrictive interpretation of 35 U.S.C. § 271(e)(1), which exempts from infringement liability the unauthorized use of patented inventions in the drug development process) . . . ; *Ebay v. Mercexchange*, 547 U.S. 388 (2006) (overturning the Federal Circuit's special rules regarding the granting of injunctions in patent infringement cases; rather, requiring the court to apply traditional principles of equity to the determination of whether to grant or deny injunctive relief) [see *infra* Part IV.B.2.]; *MedImmune v. Genentech*, 549 U.S. 118 (2007) (overturning the Federal Circuit's holding that a patent licensee must breach the license contract before there would be a constitutionally sufficient case or controversy to establish standing for a declaratory judgment action seeking a finding that the licensed patent is invalid) [see *supra* Part II of this Article]; *Microsoft v. AT&T*, 127 S. Ct. 1746 (2007) (reversing the Federal Circuit's holding that selling a copy of a master software disk outside the U.S. as a component in a computer, which master disk had originally been produced in and sent abroad from the U.S., gave rise to infringement liability under 35 U.S.C. § 271(f)); *Quanta Computer v. LG Electronics*, 128 S. Ct. 2109 (2008) (overturning the Federal Circuit's rule that the doctrine of patent exhaustion does not apply to method patents, and interpreting the scope of the doctrine more broadly than did the Federal Circuit).").

303. See, e.g., *Blonder-Tongue*, 402 U.S. at 334-45; *U.S. v. Glaxo Group, Ltd.*, 410 U.S. 52, 58 (1973); *Kewanee Oil Co.*, 416 U.S. at 475, 481, 492; *Aronson*, 440 U.S. at 261, 264; *General Motors Corp. v. Devex Corp.*, 461 U.S. 648, 658 (1983) (Stevens, J., Concurring);

instance, however, has the Court provided an answer to the question of whether the *Lear* Court's abrogation of the doctrine of licensee estoppel was so broad as to cover a nonrepudiating licensee in good standing. As indicated in Part II of this Article, the Court in *MedImmune* refused to opine on this question, although Justice Scalia in writing for the majority expressed skepticism as to the strength of the proffered merits-based contract arguments in support of the applicability of licensee estoppel to a licensee in good standing.³⁰⁴

Perhaps the most thoughtful analysis of the *Lear* holding was articulated by the Court in *Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation*.³⁰⁵ In that case, decided two years after the *Lear* decision, the Court ruled that a defendant in a patent infringement suit could estop the patent holder from pursuing his claim if the patent at issue had previously been held to be invalid in a suit involving a different alleged infringer. The reasoning of the Court, reflecting a recognition of the important public interest in eliminating invalid patents, was that requiring an alleged infringer to relitigate the issue of patent validity was wasteful and would likely result in the alleged infringer electing to pay royalties for the use of a worthless patent. According to the Court, the economic consequence of such an outcome is not only that "any royalties actually paid are an unjust increment to the alleged infringer's costs,"³⁰⁶ but that "any royalty payments passed on to consumers are as a practical matter unrecoverable by those who in fact paid them."³⁰⁷

In support of its conclusion that the holders of invalid patents should not be permitted to exact licensing agreements or other settlements from alleged infringers, the Court in *Blonder-Tongue* referenced its prior *Lear* decision. According to the *Blonder-Tongue* Court, the *Lear* holding was based on two lines of authority, each reflecting the Court's view that a patent, which is a government-sanctioned stimulus to invention, is nonetheless a monopoly with social and economic consequences and, accordingly, must cover only subject matter that meets the statutory requirements for patentability. The first line of authority was manifested in a "series

Bonito Boats, Inc. v. Thunder Craft Boats, Inc., 489 U.S. 141, 154, 160 (1989); *MedImmune*, 549 U.S. at 124.

304. See *supra* section II.B.

305. 402 U.S. 313.

306. *Id.* at 346.

307. *Id.*

of decision in which the Court has condemned attempts to broaden the physical or temporal scope of the patent monopoly.”³⁰⁸ These decisions,³⁰⁹ which characterized and condemned the illicit practice of patent misuse, demonstrated the Court’s commitment to ensure that patent monopolies are kept within their legitimate scope.³¹⁰ This first line of cases, relied on in the *Sears* and *Compco* decisions cited in *Lear*,³¹¹ provided support for the *Lear* Court’s conclusion that “federal law requires, that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent.”³¹²

The second line of cases that informed the *Lear* decision encouraged authoritative testing of patent validity. The *Blonder-Tongue* Court cited the decision in *Kerotest Manufacturing Co. v. C-O-Two Fire Equipment Co.*,³¹³ permitting a potential infringer to test the validity of a competitor’s patent by bringing an action under the

308. *Id.* at 343.

309. In the body of its opinion, the *Blonder-Tongue* Court provided the following excerpt from a representative decision, *Mercoid v. MidContinent Investment Co.*, 320 U.S. 661 (1944), in which the Court condemned an attempt to broaden the scope of the patent monopoly: “The necessities or convenience of the patentee do not justify any use of the monopoly of the patent to create another monopoly. The fact that the patentee has the power to refuse a license does not enable him to enlarge the monopoly of the patent by the expedient of attaching conditions to its use. *United States v. Masonite Corp.*, [316 U.S. 265,] 277 [(1942)]. The method by which the monopoly is sought to be extended is immaterial. *United States v. Univis Lens Co.*, [316 U.S. 241,] 251–252 [(1942)]. The patent is a privilege. But it is a privilege which is conditioned by a public purpose. It results from invention and is limited to the invention which it defines.” *Blonder-Tongue Laboratories, Inc.*, 402 U.S. at 343–44 (quoting *Mercoid*, 320 U.S. at 666). In a footnote at the conclusion of the above quoted excerpt, the *Blonder-Tongue* Court cited the following additional decisions: *Brulotte v. Thys Co.*, 379 U.S. 29 (1964); *Int’l Salt Co. v. United States*, 332 U.S. 392 (1947); *United States v. Gypsum Co.*, 333 U.S. 364, 389 (1948); *Scott Paper Co.*, 326 U.S. 249; *Morton Salt Co. v. Suppiger Co.*, 314 U.S. 488, 491–92 (1942); *Ethyl Gasoline Corp. v. United States*, 309 U.S. 436, 455–59 (1940); *IBM Corp. v. United States*, 298 U.S. 131 (1936); *Carbice Corp. v. Am. Patents Corp.*, 283 U.S. 27 (1931); *Motion Picture Patents Co. v. Universal Film Co.*, 243 U.S. 502 (1917). *Blonder-Tongue Lab., Inc.*, 402 U.S. at 344 n 40.

310. In support of this statement, the *Blonder-Tongue* Court provided the following excerpt from *Precision Instrument Manufacturing Co. v. Automotive Maintenance Machinery Co.*, 324 U.S. 806 (1945): “A patent by its very nature is affected with a public interest [It] is an exception to the general rule against monopolies and to the right to access to a free and open market. The far-reaching social and economic consequences of a patent, therefore, give the public a paramount interest in seeing that patent monopolies spring from backgrounds free from fraud or other inequitable conduct and that such monopolies are kept within their legitimate scope.” *Blonder-Tongue Laboratories, Inc.*, 402 U.S. at 343 (quoting *Precision Instrument Mfg. Co.*, 324 U.S. at 816).

311. See *supra* section III.C.3.

312. *Lear*, 395 U.S. at 668.

313. 342 U.S. 180 (1952).

Declaratory Judgment Act, without awaiting the filing of an infringement suit by the patent holder. The Court then referred to its prior decisions that “involved removal of restrictions on those who would challenge the validity of patents [citing *MacGregor*, *Katzinger*, *Scott Paper*, *Sola*, *Westinghouse*, and *Pope*],”³¹⁴ and noted that, as recognized in *Lear*, licensees often had the greatest economic incentive to bring a patent challenge. According to the *Blonder-Tongue* Court, “[t]he holding [in *Lear*] that licensee estoppel was no longer tenable was rooted in the second line of cases eliminating obstacles to suit by those disposed to challenge the validity of a patent.”³¹⁵ The Court in *Blonder-Tongue* concluded its analysis by indicating that its ruling in the case before it was based on “our consistent view—last presented in *Lear, Inc. v. Adkins*—that the holder of a patent should not be insulated from the assertion of defenses and thus allowed to exact royalties for the use of an idea that is not in fact patentable or that is beyond the scope of the patent monopoly granted.”³¹⁶

The *Blonder-Tongue* Court’s interpretation of the *Lear* decision is noteworthy in that in restating the basis for the *Lear* holding, the Court referred to cases that were not cited in *Lear*.³¹⁷ In particular, the *Blonder-Tongue* Court emphasized prior U.S. Supreme Court cases that addressed the issue of patent misuse, but these cases were only indirectly referenced in *Lear*.³¹⁸ While U.S. Supreme Court patent misuse jurisprudence is relevant to a discussion of the enforceability of pro-licensor contract provisions that prohibit or discourage patent validity challenges (as will become apparent in Part IV of this Article), the *Lear* Court did not consider prior

314. 402 U.S. at 345, n 42 (“See *MacGregor v. Westinghouse Electric & Mfg. Co.*, 329 U.S. 402, 407 (1947); *Katzinger Co. v. Chicago Mfg. Co.*, 329 U.S., at 398–401; *Scott Paper Co. v. Marcalus Co.*, . . . [326 U.S. 249 (1945)]; *Sola Electric Co. v. Jefferson Electric Co.*, 317 U.S. 173 (1942); *Westinghouse Electric & Mfg. Co. v. Formica Insulation Co.*, 266 U.S. 342 (1924); *Pope Mfg. Co. v. Gormully*, 144 U.S. 224, 234 (1892).”).

315. *Id.* at 345.

316. *Id.* at 349–50.

317. The *Lear* Court did not cite the *Kerotest* decision nor any of the patent misuse cases relied on in *Blonder-Tongue* (see *supra* notes 309 & 310), with the exception of *Scott Paper* (which was presented in *Lear* as an exception to the estoppel doctrine) and *Brulotte* (which was cited in a footnote in Justice White’s concurring opinion in reference to *Lear*’s royalty payment obligation).

318. The *Sears* decision, cited in *Lear* for the proposition that federal policy favors free competition in ideas that do not merit patent protection, cited certain of the U.S. Supreme Court’s prior patent misuse cases (*Masonite*, *Morton Salt*, *Univis Lens* and *International Business Machines*). The *Compco* decision, also cited in *Lear* for the same proposition, relied on *Sears*. See also, *supra* note 317.

Supreme Court patent misuse cases of sufficient relevance to even cite them in its opinion. The reason for the *Blonder-Tongue* Court's shift in emphasis in its description of the *Lear* holding is difficult to know. With seven of nine Supreme Court Justices contributing to both decisions,³¹⁹ the Justices who decided *Blonder-Tongue* were certainly well versed in the details of the *Lear* case. One possible explanation for the somewhat different perspective on *Lear* presented in *Blonder-Tongue* was that the *Blonder-Tongue* Court relied on *Lear* to support its holding in the case before it and described the *Lear* decision in a manner that was most persuasive for the task at hand. For purposes of this discussion, however, what matters is that, as in our assessment of the Court's opinion in *Lear*, the *Blonder-Tongue* Court's interpretation of the *Lear* holding is consistent with our conclusion that the arguments presented in *Lear* for abrogation of the doctrine of licensee estoppel are applicable irrespective of whether the licensee has repudiated its licensee agreement. Ideas that are in the public domain should be available for use for the common good without restriction. Patents that inappropriately claim those ideas should be eliminated and those with the greatest incentive for doing so, including current licensees, should be encouraged in that effort.

ii. Regional Circuits and District Courts

In the interval between the U.S. Supreme Court's *Lear* decision in 1969 and the establishment of the Court of Appeals for the Federal Circuit in 1982, the most active dialogue regarding the meaning and scope of the *Lear* decision was conducted by the federal district courts and regional courts of appeal.³²⁰ The majority of these courts adopted a broad interpretation of the *Lear* decision, relying on the U.S. Supreme Court's reasoning in the case to permit licensee patent validity challenges under circumstances not addressed in *Lear*. A comprehensive review of these post-*Lear*, pre-Federal Circuit cases is beyond the scope of this Article and can be found in various reviews written in the years following the *Lear*

319. Justices Black, Douglas, Harlan, Brennan, Stewart, White and Marshall participated in both the *Lear* and *Blonder-Tongue* decisions.

320. One pair of commentators, writing during this interval, noted that "[d]ecisions giving different interpretations of *Lear* have evolved every year since 1969. It seems that any paper which attempts to define the state of the law under *Lear* is obsolete within one year." Tipton D. Jennings IV & Carrol L. Bryan II, *The Ever Expansive Scope of Lear v. Adkins: Does it Have Limits?*, 59 J. PAT. OFF. SOC'Y 679, 703 (1977) (footnotes omitted).

decision.³²¹ In this section, we discuss only those cases that remain relevant to the central questions presented in this Article, namely, is there a vestige of the doctrine of licensee estoppel following *Lear* that protects a patent licensor from a patent validity challenge by a licensee in good standing and if one cannot rely on the doctrine, are explicit contract provisions that prohibit, reduce the incentive for, and/or specify a consequence of, a licensee's validity challenge enforceable?

Prior to a review of post-*Lear* case law, it should be noted that the U.S. Supreme Court's *Lear* holding addressed more than the right of a patent licensee to challenge the validity of the licensed patent. A second issue in the case involved *Lear*'s liability for royalties owed Atkins under the patent license agreement, and that issue was separable from, albeit related to, the patent challenge question. The *Lear* Court acknowledged as much in stating that "it may be suggested that although *Lear* must be allowed to raise the question of patent validity in the present lawsuit, it must also be required to comply with its contract and continue to pay royalties until its claim is finally vindicated in the courts."³²² As indicated in section III.C.3. above, the Court rejected that "suggestion" and held that requiring *Lear* to comply with the royalty provision of its contract "might well deter many licensees from attempting to prove patent invalidity in the courts"³²³ and, accordingly, "undermine the strong federal policy favoring the full and free use of ideas in the public domain."³²⁴ For purposes of the discussion in this section, the significance of the *Lear* Court's royalty obligation ruling is that it constituted the second prong of what has been referred to as the *Lear* doctrine.³²⁵ The U.S. Court of Appeals for the Sixth Circuit summarized the doctrine as follows:

321. Rochelle Cooper Dreyfuss, *Dethroning Lear: Licensee Estoppel and the Incentive to Innovate*, 72 VA. L. REV. 677 (1986); Jennings IV & Bryan II, *supra* note 320, at 679; J. Thomas McCarthy, "Unmuzzling" *The Patent Licensee: Chaos in the Wake of Lear v. Adkins*, (Part I) 59 J. PAT. OFF. SOC'Y 475 (1977) [hereinafter "McCarthy, (Part I)"]; J. Thomas McCarthy, "Unmuzzling" *The Patent Licensee: Chaos in the Wake of Lear v. Adkins*, (Part II-Conclusion) 59 J. PAT. OFF. SOC'Y 544 (1977) [hereinafter "McCarthy, (Part II)"]; Rooklidge, *Lear v. Adkins Revisited* (Part II), *supra* note 68, at 5; Christian Chadd Taylor, *No-Challenge Termination Clauses: Incorporating Innovation Policy and Risk Allocation into Patent Licensing Law*, 69 IND. L.J. 215 (1993).

322. *Lear*, 395 U.S. at 673.

323. *Id.*

324. *Id.* at 674.

325. *Studiengesellschaft Kohle*, 112 F.3d at 1568.

The two holdings of *Lear* are as follows: (1) a licensee is not estopped to interpose the invalidity of the licensed patent as a defense to an action brought by the licensor to enforce the license agreement, 395 U.S. at 656, 671, 89 S.Ct. 1902; and (2) a licensee cannot be required to continue to pay royalties during the time he is challenging patent validity in the courts, 395 U.S. at 673, 89 S.Ct. 1902. The policy underlying these holdings was to “‘unmuzzle’ licensees so that an early adjudication of invalidity could inure to the public interest.” *Atlas Chemical*, 509 F.2d at 6; *Troxel I*, 465 F.2d at 1257; see *Lear*, 395 U.S. at 670, 673, 89 S.Ct. 1902.³²⁶

A recognition of the two prongs of the so-called *Lear* doctrine is essential in interpreting post-*Lear* case law, not only because it helps to define the scope of the actual holding in *Lear* but because it aids in identifying those cases that address only one of the two prongs of the doctrine.³²⁷

The challenge for the lower federal courts in the aftermath of the U.S. Supreme Court’s *Lear* decision, however, was not in restating the two-part *Lear* holding but in applying the Court’s ruling in the case to facts not present in *Lear*. That latter exercise required that a court move beyond the holding in *Lear* to interpret and apply the “spirit of *Lear*.”³²⁸ In the words of one commentator, citing the U.S. Supreme Court’s interpretation in *Blonder-Tongue* of its *Lear* decision, “[t]he ‘spirit of *Lear*’ appears to be one of providing some incentive to licensees to encourage them to challenge patent validity and to eliminate obstacles to suit by those disposed to challenge the validity of a patent.”³²⁹ As will be demonstrated in the case descriptions that follow, the ultimate question frequently faced by a court in addressing a *Lear*-related issue was whether “the ‘spirit of *Lear*’ can . . . logically demand that any and all rules of

326. *PPG Indus., Inc. v. Westwood Chem., Inc.*, 530 F.2d 700, 705 (6th Cir. 1976).

327. For example, there are a number of cases that only consider a licensee’s royalty payment obligation, where the licensee’s right to challenge the validity of the licensed patent is undisputed. See, e.g., *Atlas Chem. Indus., Inc. v. Moraine Prods.*, 509 F.2d 1 (6th Cir. 1974); *PPG Indus., Inc.*, 530 F.2d 700; *Warner-Jenkinson Co. v. Allied Chem. Corp.*, 567 F.2d 184 (2d Cir. 1977); *St. Regis Paper Co. v. Royal Indus.*, 552 F.2d 309 (9th Cir. 1977); *Am. Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890 (3d Cir. 1980); *Precision Shooting Equip. Co. v. Allen*, 646 F.2d 313 (7th Cir. 1981); *Bristol Locknut Co. v. SPS Techs., Inc.*, 677 F.2d 1277 (9th Cir. 1982); *Rite-Nail Packaging Corp. v. Berryfast, Inc.*, 706 F.2d 933 (9th Cir. 1983); see *infra* section III.C.4.c.iii. (Licensee Patent Validity Challenges; Prerequisites and Jurisdictional Barriers).

328. *McCarthy*, (Part I), *supra* note 321, at 476.

329. *Id.* (emphasis added).

contract law, patent law, and civil procedure be ignored to give licensees *every possible incentive* to challenge patent validity . . . [?]"³³⁰ It is in the gap between "some incentive" and "every possible incentive" that the debate regarding the scope of the U.S. Supreme Court's *Lear* decision has been waged.

As indicated above, prior to the establishment of the Federal Circuit, the majority of federal courts aggressively applied the "spirit of *Lear*" to permit licensee patent validity challenges in a variety of circumstances not present in *Lear*. In the words of one commentator, "[w]hen the Supreme Court in *Lear* expressed the public policy of encouraging licensees to challenge patents, the lower courts saddled up and went charging off in several different directions. The 'spirit of *Lear*' became the battle cry of all patent licensees every time any rule of law came between a licensee and its desire to challenge a patent."³³¹ Specifically, federal district and appellate courts of the Second, Third, Fourth, Seventh, Ninth and D.C. Circuits ruled that an explicit contract provision that expressly prohibited a patent validity challenge by a party licensed under the patent (a licensee "no-challenge" clause) was unenforceable under *Lear*, despite the fact that the Adkins/*Lear* license agreement contained no such provision.³³² Courts in the Second, Seventh and Ninth Circuits permitted a patent validity challenge by a licensee that, unlike *Lear*, had entered into the patent license agreement as part of a settlement to end threatened legal action or litigation

330. McCarthy, (*Part II*), *supra* note 321 (emphasis added). McCarthy answered the question in the negative. His full comment is as follows: "The *Lear* decision was based upon a policy of 'eliminating obstacles to suit by those disposed to challenge the validity of a patent,' [*Blonder-Tongue Labs*, 402 U.S. at 345] but the 'spirit of *Lear*' cannot logically demand that any and all rules of contract law, patent law, and civil procedure be ignored to give licensees every possible incentive to challenge patent validity."

331. McCarthy, (*Part I*), *supra* note 321, at 477; *see also* Rooklidge, *Lear v. Adkins Revisited (Part II)*, *supra* note 68, at 14("The post-*Lear* decisions of the regional circuits have extended the rationale of *Lear* so as to conflict with long-established law and, indeed, common sense.").

332. *Plastic Contact Lens Co. v. W.R.S. Contact Lens Labs., Inc.*, 330 F. Supp. 441 (S.D.N.Y. 1970); *Wallace Clark & Co., Inc. v. Acheson Indus., Inc.*, 401 F. Supp. 637 (S.D.N.Y. 1975); *Congoleum Indus., Inc. v. Armstrong Cork Co.*, 366 F. Supp. 220 (E.D. Pa. 1973) (*aff'd* 510 F.2d 334 (3d Cir. 1975)); *Blohm & Voss AG v. Prudential-Grace Lines, Inc.*, 346 F. Supp. 1116 (D. Md. 1972) (*rev'd on other grounds*, 489 F.2d 231 (4th Cir. 1973)); *Kraly v. Nat'l Distillers and Chem. Corp.*, 319 F. Supp. 1349 (N.D. Ill., 1970) (*aff'd*, 502 F.2d 1366 (7th Cir. 1974)); *Panther Pumps & Equip. Co. v. Hydrocraft, Inc.*, 468 F.2d 225 (7th Cir. 1972); *Bendix Corp. v. Balax, Inc.*, 471 F.2d 149 (7th Cir. 1972); *Massillion-Cleveland-Akron Sign Co. v. Golden State Adver. Co.*, 444 F.2d 425 (9th Cir. 1971); *Robintech, Inc. v. Chemidus Wavin, Ltd.*, 450 F. Supp. 817 (D.C. 1978).

involving the licensed patent.³³³ Anticipating the jurisdictional holding of the U.S. Supreme Court in *MedImmune*, courts of the Second, Third, Sixth, Seventh and Eighth Circuits permitted a patent licensee that had not repudiated its license agreement to challenge the licensed patent in a declaratory judgment action, rather than (as in *Lear*) to raise patent invalidity as a defense to a claim by a patent licensor for royalties owed under the license agreement.³³⁴ Courts of the Seventh Circuit took the aggressive stance that a patent licensor was not permitted to terminate its license agreement despite a breach of the agreement by a licensee that was challenging the licensed patent.³³⁵ Finally, courts of the Second, Sixth and Seventh Circuits ruled that any payments made by a licensee during the pendency of a patent challenge would need to be refunded by the licensor in the event that the licensee's challenge was successful, a circumstance not addressed in *Lear* where the licensee had withheld royalty payments prior to its challenge.^{336, 337}

333. *Warner-Jenkinson Co.*, 567 F.2d 184; *Kraly*, 319 F. Supp. at 1349, 1366; *Crane Co. v. Aeroquip Corp.*, 356 F. Supp. 733 (N.D. Ill., E.D. 1973); *Crane Co. v. Aeroquip Corp.*, 364 F. Supp. 547 (N.D. Ill., E.D. 1973); *Crane Co. v. Aeroquip Corp.*, 504 F.2d 1086 (7th Cir. 1974); *Massillion-Cleveland-Akron Sign Co.*, 444 F.2d 425; *but see*, *Broadview Chem. Corp. v. Loctite Corp.*, 474 F.2d 1391 (2d Cir. 1973); *Wallace Clark & Co. v. Acheson Indus., Inc.*, 532 F.2d 846 (2d Cir. 1976); *Interdynamics, Inc. v. Firma Wolf*, 653 F.2d 93 (3d Cir. 1981); *Schlegel Mfg. Co. v. USM Corp.*, 525 F.2d 775 (6th Cir. 1975); *Aro Corp. v. Allied Witan Co.*, 531 F.2d 1368 (6th Cir. 1976); *Ransberg Electro-Coating Corp. v. Spiller and Spiller, Inc.*, 489 F.2d 974 (7th Cir. 1973); *American Equip. Corp. v. Wikomi Mfg. Co.*, 630 F.2d 544 (7th Cir. 1980); *U.S. ex. rel. Shell Oil Co. v. Barco Corp.*, 430 F.2d 998 (8th Cir. 1970). It should be noted that while the *Adkins/Lear* license agreement was not entered into to settle litigation involving the licensed patent, the license agreement at issue in *Automatic Radio* (a decision that was in part overruled by *Lear*) did involve a settlement agreement. *See supra* section III.B.1.; *supra* section III.B.2.; *supra* section III.C.4.b.; *supra* section III.C.4.c.iii.

334. *Warner-Jenkinson Co.*, 567 F.2d 184; *American Sterilizer Co.*, 526 F.2d 542; *Atlas Chem. Indus., Inc.*, 509 F.2d 1; *Precision Shooting Equip. Co.*, 646 F.2d 313; *Nebraska Eng'g Corp. v. Shivvers*, 557 F.2d 1257 (8th Cir. 1977).

335. *Crane Co.*, 356 F. Supp. 733; *Crane Co.*, 364 F. Supp. 547; *Crane Co.*, 504 F.2d 1086; *Lee v. Lee Custom Eng'g, Inc.*, 476 F. Supp. 361 (E.D. Wis. 1979); *Precision Shooting Equip. Co.*, 646 F.2d 313; *but see*, *Morton-Norwich Products, Inc. v. Int'l Salt Co.*, 183 U.S.P.Q. 748 (N.D.N.Y. 1974); *Metallurgical Int'l, Inc. v. Kawecki Berylco Indus., Inc.*, 171 U.S.P.Q. 348 (E.D. Pa. 1971); *Warner-Jenkinson Co.*, 567 F.2d 184; *Nebraska Eng'g Corp.*, 557 F.2d 1257.

336. *Warner-Jenkinson Co.*, 567 F.2d 184; *Atlas Chem. Indus., Inc.*, 509 F.2d 1; *Precision Shooting Equip. Co.*, 646 F.2d 313.

337. In *Beckman Instruments, Inc. v. Technical Development Corp.*, 433 F.2d 55, the Seventh Circuit endorsed another "extension" of the Supreme Court's *Lear* holding by permitting a licensee patent validity challenge in the context of an exclusive (as opposed to nonexclusive) patent license, where the licensee marked its product with the number of the challenged patent. With respect to the licensor-defendants' claim that the *Lear*

For our purposes, however, it is the reasoning of the post-*Lear* courts and not the facts of the cases that is of interest. A review of selected decisions provides a sampling of the different judicial interpretations of the scope of the *Lear* holding, as well as a preview of the arguments that a court today might rely on in determining the right of a licensee in good standing to challenge the validity of a licensed patent or in assessing the enforceability of a pro-licensor contract provision that has the effect of discouraging a licensee patent challenge. Federal courts that took an expansive view of the *Lear* decision did, in fact, endeavor to provide the patent licensee with “every possible incentive” to challenge the licensed patent’s validity. In contrast, the minority of courts that refused to extend the *Lear* holding expressed the view, later adopted by the Court of Appeals for the Federal Circuit, that the *Lear* decision did not grant

holding should be limited to nonexclusive licenses and that licensee estoppel should continue to apply to exclusive licensees, the Seventh Circuit acknowledged that at the time of the filing of suit in *Lear* the license had become nonexclusive (*see supra* note 226) but held that the status of the license was not relevant to the Supreme Court’s ruling in the case. As the Seventh Circuit explained,

[d]efendants suggest that . . . the basic rationale of *Lear* is inapplicable to exclusive licensees because outsiders also have a strong economic incentive to challenge the monopoly granted the exclusive licensee. In the case of nonexclusive licenses, defendants argue, all would-be competitors are free to become licensees, and henceforth would be barred from challenging the patent unless a limited exception to the doctrine of licensee estoppel were made. We reject the argument. Even if the failure to distinguish between exclusive and nonexclusive licenses was oversight [by the *Lear* Court], we are not convinced that the Supreme Court would rule differently on the facts of this case. Nor can we say that the distinction which the defendants suggest is so great as to require a limitation on the *Lear* rule, especially in light of the “strong federal policy favoring free competition in ideas which do not merit patent protection.” *Lear, Inc. v. Adkins*, . . . 395 U.S. [653] at 656

433 F.2d at 58 (paragraphing omitted). With respect to the defendants’ claim that a licensee that marks its product with the number of the licensed patent is estopped from challenging the patent’s validity, the Seventh Circuit concluded that such a restriction would undermine the important public interest, articulated in *Lear*, of eliminating worthless patents. In the words of the Seventh Circuit,

[d]efendants have not suggested any reason why the “strong federal policy” in favor of encouraging challenges to invalid patents should not apply when there has been marking with the patent number. Perhaps it is true that such marking provides the licensee with additional protection from competitors, thus making it seem all the more unfair to allow him to repudiate his obligations. However, it must be noted that the Supreme Court in *Lear* conceded that patent invalidity does not amount to total failure of consideration, but nonetheless held that patent invalidity must be made a complete defense to the obligation to pay royalties. We cannot say that the additional consideration or “benefit” flowing to the licensee who marks his products with the patent number is sufficient to make the *Lear* case and its policy rationale inapplicable. *Id.* at 59 (7th Cir. 1970).

every licensee the right to challenge the licensed patent in every circumstance.³³⁸

Representative of the decisions that reflected an expansive reading of *Lear* are the Ninth Circuit's ruling in *Massillion-Cleveland-Akron Sign Co. v. Golden State Advertising Co.*³³⁹ and the Seventh Circuit's ruling in *Kraly v. National Distillers and Chemical Corp.*³⁴⁰ Each of these cases involved a patent license agreement that was entered into to settle a dispute regarding the alleged infringement of the patent and contained an explicit no-challenge provision. In *Massillion*, the Ninth Circuit ruled that an express covenant by a licensee in a settlement agreement not to challenge a licensed patent was unenforceable under the rationale of *Lear*, despite the fact that the patent at issue was acknowledged as valid and infringed in the agreement. The court noted that the *Lear* decision did not specifically address the validity of a no-challenge provision. It reasoned, however, that such a provision "is in just as direct conflict with the 'strong federal policy' referred to repeatedly in *Lear*, as was the estoppel doctrine and the specific contractual provision [regarding a royalty payment obligation] struck down in that decision."³⁴¹ The *Massillion* court rejected the argument that the rationale of *Lear* was inapplicable in the context of a settlement agreement. In the words of the Ninth Circuit,

[w]e think it unimportant that in our case the covenant is part of a settlement agreement rather than of a typical patent licensing agreement. Were we to recognize such a distinction it would, in practice, be less than [sic] workable . . . [I]t would be . . . easy to couch licensing arrangements in the form of settlement agreements. If the recognized policy favoring settlement of disputes might be hindered by our holding on this question, that policy, in our opinion, must give way to the policy favoring free competition in ideas not meriting patent protection.^{342, 343}

338. *Gen-Probe Inc.*, 359 F.3d at 1381 ("The *Lear* doctrine, however, does not grant every licensee in every circumstance the right to challenge the validity of the licensed patent").

339. 444 F.2d 425.

340. 502 F.2d 1366.

341. *Massillion-Cleveland-Akron*, 444 F.2d at 427.

342. *Id.*

343. The Ninth Circuit bolstered its arguments in support of the application of the rationale of *Lear* to the facts in *Massillion* by citing *Katzinger v. Chicago Metallic Manufacturing Co.*, 329 U.S. 394 (1947), in which the U.S. Supreme Court permitted a

In *Kraly v. National Distillers and Chemical Corp.*,³⁴⁴ the Seventh Circuit adopted a position similar to that of the Ninth Circuit regarding the application of the *Lear* decision. In the Seventh Circuit case, an infringement action brought by patent holder Kraly against National Distillers' predecessor-in-interest was dismissed with prejudice when the parties entered into a settlement agreement that included a provision that prohibited the alleged infringer from making any future challenges of the validity of the patent at issue. National Distillers subsequently stopped paying royalties due under the settlement agreement and raised patent invalidity as a defense to Kraly's breach of contract claim. Kraly argued that the prior dismissal with prejudice was *res judicata* of the issue of patent validity and, accordingly, the rationale of *Lear* did not apply in the instant case to allow National Distillers' patent challenge. The Seventh Circuit rejected Kraly's argument. The court acknowledged that a dismissal with prejudice was generally binding, but concluded that the case before it presented an exception.

We do not quarrel with the general proposition that a judgment with prejudice entered upon a settlement or compromise is binding as to the parties and their privies. *See generally* 1B J. Moore, *Federal Practice*, P0.409 (2d ed. 1948). Nonetheless, this proposition is subject to qualification where overriding principles are implicated, and it is well-established that one such principle is 'the public interest in obtaining a judicial determination of the invalidity of a worthless patent.' *Id.* . . . In the circumstances of this case, therefore, the doctrine of *res judicata* has no applicability.³⁴⁵

The court first argued that the consent decree in the instant case did not embody an adjudication of infringement, considered necessary under Seventh Circuit precedent for *res judicata*. It then opined that, even if the consent decree had embodied an adjudication of infringement, the *Lear* rationale may still be applicable despite the presence of the no-challenge provision, since "allow[ing] the parties to consent to an adjudication of infringement

licensee patent validity challenge despite an explicit no-challenge provision in an agreement that resulted from an infringement dispute. *See also, infra* note 522.

344. 502 F.2d 1366.

345. *Id.* at 1368 (citation omitted).

would simply result in the erection of another obstacle to tests of patent validity.”³⁴⁶ The court concluded “that National Distillers, the licensee, is not estopped from challenging the validity of the patent even though a prior consent decree incorporated an understanding not to challenge the validity of the patent.”³⁴⁷

The Seventh Circuit further extended the application of the public policy rationale of *Lear* in *Crane v. Aeroquip Corp.*,³⁴⁸ demonstrating the potential force of the rationale in overriding the dictates of contract law. The central question in *Crane* was whether a patent licensor could unilaterally terminate its settlement agreement with a licensee that had failed to pay royalties owed under the agreement and had repeated its challenge of the licensed patent despite a prior consent decree declaring the patent valid. The district court in the case addressed three issues in its holding. Consistent with the Seventh Circuit’s ruling in *Kraly*, the court concluded that a prior consent decree of patent validity in the absence of a finding of infringement did not estop the licensee from again challenging the licensed patent. Citing case law from the Seventh and other regional circuits in support of its position, the district court noted that “[t]he foregoing decisions are founded on the policy that the undesirability of having the public pay royalties to one who does not have a valid patent outweighs the desirability of encouraging settlement of lawsuits.”³⁴⁹

The *Crane* district court then examined the basis for the licensee’s royalty obligation. While concluding that the patent at issue was valid but not infringed, the court relied on the doctrine of marking estoppel to hold that the licensee was still obligated to pay royalties under the settlement agreement. According to the marking estoppel doctrine, “marking with a patent number will estop the marker from denying that the marked product is within the scope of the patent.”³⁵⁰ Since the licensee in *Crane* had marked the product at issue in the case with the number of the *Crane* patent, it was estopped from raising the defense of noninfringement and, accordingly, was liable for the royalties owed under the settlement

346. *Id.* at 1369.

347. *Id.*

348. 356 F. Supp. 733; 364 F. Supp. 547; 504 F.2d 1086.

349. *Crane Co.*, 364 F. Supp. at 549–50.

350. *Crane Co.*, 356 F. Supp. at 741.

agreement, despite the court's conclusion that the product was not covered by the licensed patent.^{351, 352}

Having established that the patent validity challenge was permissible but that the licensee was nonetheless liable for royalties owed under the settlement agreement, the *Crane* district court turned to the question of whether the licensor had the right to terminate the agreement based on the licensee's failure to comply with its contractual obligation to pay royalties and its subsequent repudiation of the licensed patent. Relying on the rationale of *Lear*, the court concluded that the licensor in *Crane* was not permitted to unilaterally terminate its settlement agreement. In the words of the court:

Although the authority is somewhat insubstantial, the general rule of this Circuit appears to be that the mere failure to pay royalties is not, absent a specific provision in the license, sufficient to allow the licensor to unilaterally terminate the license With respect to the other alleged grounds for termination, irrespective of their merits as a matter of contract law, the policy considerations found to be determinative in the *Lear* case should have equal force here. Basically, Crane's [the licensor's] contention is that Aeroquip's [the licensee's] repudiation of the validity of the patent and its manufacture, sale and marking of the "modified" couplings, without payment of royalties thereon, are sufficient grounds for Crane to unilaterally terminate the license. Certainly the aforesaid facts would as a matter of contract law be persuasive support for Crane's argument. However, as the Court stated in *Lear*: "Surely the equities of the licensor do not weigh very heavily when they are balanced against the important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain. . . . We think it plain that the technical requirements of contract doctrine must give way before the demands of the public interest" *Lear, Inc. v. Adkins*, 395 U.S. 653, 670 . . . (1969). Although the

351. *Crane Co.*, 364 F. Supp. at 560. ("[Since] defendant is estopped to deny that the modified couplings [the product at issue in the case] are covered by the claims in suit, irrespective of whether they *in fact* are, defendant will be liable for royalties on said couplings.")

352. Citing *Beckman Instruments, Inc.*, 433 F.2d 55 (which relied on the rationale of *Lear*), the district court in *Crane* noted that the marking of a product by a licensee with the number of a licensed patent did not prevent the licensee from challenging the validity of the patent. *Crane Co.*, 356 F. Supp. at 741.

facts and issues in *Lear* required the court to go no further than to hold that the doctrine of licensee estoppel would no longer be a defense available to licensors and that a licensee would be able to challenge the validity of the patent without having to continue paying royalties or, in effect, having the license contract strictly enforced against it during the pendency of the litigation, the rationale of *Lear* must surely extend to the converse situation raised in this case. Instead of being asked to enforce the contract, even though the licensee has raised the validity defense, Crane has asked this court to adjudicate the license as terminated essentially *because* the licensee has raised the validity defense. Yet, just as the imposition of the doctrine of licensee estoppel would have a chilling effect on meritorious challenges to patents . . . , so would the threat of termination of the license have a similar effect.³⁵³

The Seventh Circuit in *Crane* affirmed the district court's ruling in the case that the licensee's failure to make royalty payments under the settlement agreement was not a sufficient ground to allow the licensor to unilaterally terminate the agreement.³⁵⁴ The circuit court expressed no opinion, however, regarding the district court's application of the doctrine of marking estoppel, since it had reversed the lower court's finding of noninfringement and relied on infringement rather than marking estoppel as the basis for the licensee's liability for royalties owed under the settlement agreement.

On first analysis, the *Crane* decision does not appear to be distinguishable from other opinions of the regional circuit courts that extended the rationale of *Lear* to cover circumstances not present in the original case. The reasoning relied on by the court in *Crane*, however, constituted a significant departure from that of other *Lear* progeny cases and has led a number of commentators to view *Crane* as the high-watermark of pro-*Lear* regional circuit case law. As one such commentator explained,

353. *Crane Co.*, 356 F. Supp. at 738–39 (cited cases omitted).

354. *Crane Co.*, 504 F.2d at 1092–93 (“The court below held that defendant’s failure to pay royalties on the accused couplings was not a sufficient basis for allowing plaintiff to terminate the license agreement, as it wished, particularly since there was ‘an honest dispute as to the coverage of the patent license.’ *Crane Co.*, 364 F. Supp. at 561. This decision was correct and was more fully explained in an earlier phase of the litigation, *Crane Co.* 356 F. Supp. 733, 737–740.”).

Crane took *Lear* to the extreme. No longer was the judiciary protecting a licensee's *capacity* to challenge validity as it did in *Lear* and in the areas of no-challenge clauses, settlement agreements, and consent decrees. Instead, the court articulated a willingness to eliminate any devices that may "threat[en]" or "chill" the licensee's *eagerness* to challenge the validity of the patent. This approach detrimentally affects the incentive to innovate and license.³⁵⁵

When viewed in this light, the *Crane* decision arguably represents an example of a court ignoring the dictates of contract law in order to provide the licensee with "every possible incentive to challenge patent validity."³⁵⁶

A minority of post-*Lear* regional circuit and district courts, however, resisted the temptation to apply the *Lear* holding to the facts under consideration. For example, in *Schlegel Manufacturing Co. v. USM Corp.*,³⁵⁷ the Sixth Circuit ruled that the public interest in the settlement of litigation outweighed the benefits of a patent validity challenge, rejecting the contrary position expressed by the Seventh Circuit in *Kraly* and *Crane*. The case involved an action for contempt brought by a patent holder for violation by the defendant of a consent decree enjoining the defendant from future uses of the patented invention. The consent decree, settling a prior infringement suit, stated that the patent at issue was both valid and infringed by the actions of the defendant. Following notice from the patent holder that the defendant's actions continued to infringe the patent, the defendant filed a declaratory judgment action for invalidity of the patent. The patent holder responded with its motion for contempt, claiming that the prior consent decree was *res judicata* of the issue of validity and could not again be raised as a defense in the action for contempt. The defendant countered by claiming that the public policy interest articulated in *Lear* "renders a

355. Taylor, *supra* note 321, at 242; see also McCarthy, (Part 1), *supra* note 321, at 518-19 ("[T]he *Crane* court found that the spirit of *Lear* was violated by . . . a termination [by a patentee of a license for nonpayment of royalties] [D]epriving the patentee of its normal right to terminate the license and sue for infringement leads to an inequitable balance of rights between patentee and licensee and discourages inventors from obtaining and licensing patents To denude the patentee of its normal infringement remedy would certainly remove an obstacle to the licensee's incentive to challenge, but at the sacrifice of an elemental balance of equities and remedies between patent owner and licensee." (footnote omitted)).

356. See *supra* note 330.

357. 525 F.2d 775.

finding of invalidity more important than the policies of finality served by the doctrine of *res judicata*.”³⁵⁸ The district court in *Schlegel* ruled in favor of the patent holder and the Sixth Circuit affirmed.

According to the Sixth Circuit, the principal issue in *Schlegel* was “whether the entire policy of *res judicata* is overridden by the public interest in purging an invalid patent of its status as a government-created monopoly.”³⁵⁹ The *Schlegel* circuit court recognized that the doctrine of *res judicata* is not inflexible and in rare instances may be rejected for public policy reasons. In the instant case, however, the court found no adequate justification for such a rejection. In the words of the Sixth Circuit majority, “[w]e are aware of no court which has entertained the suggestion that *Lear* abrogates the doctrine of *res judicata* after a fully litigated result. This would seem to be the logical extension of denying *res judicata* effect to a consent decree. . . . Even though the degree of judicial involvement is different between a consent decree and a litigated result, we are not prepared to find that judicial involvement in a consent decree is so inconsequential as to justify different treatment.”³⁶⁰ The circuit court emphasized the significant difference between the effect of a consent decree and that of licensee estoppel.

The parties to the patent suit are entitled to a full and fair hearing on the merits of the case up until the time a consent decree is entered. The doctrine of licensee estoppel closed the doors of the courts to a large group of parties who had sufficient interest in the patent to challenge its validity. By giving *res judicata* effect to consent decrees, we do not close the doors of the courts to litigation on the issue of patent validity, except as to parties or their privies, and only after they have had the opportunity to litigate the issue fully. Third parties are not affected by the consent decree.³⁶¹

The Sixth Circuit acknowledged that its decision in *Schlegel*, relying on *res judicata* to prevent a licensee patent validity challenge, was not consistent with the Seventh Circuit’s decisions in *Kraly* and *Crane* (although consistent with prior decisions of the Second and

358. *Id.* at 778.

359. *Id.* at 778.

360. *Id.* at 780 (citation omitted).

361. *Id.* at 781 (citations omitted).

Eighth Circuits).³⁶² However, the *Schlegel* circuit court attributed the inconsistency to a difference in the interpretation of *Lear*, and not a lack of recognition of the important public policy in the early invalidation of specious patents. As the *Schlegel* majority explained,

[t]he public interest requires that an invalid patent be stripped of its monopoly, and at as early a date as possible. When a consent decree is to be given *res judicata* effect, litigants are encouraged to litigate the issue of validity rather than foreclosing themselves by a consent decree. If they were given a second change to litigate the issue of validity, alleged infringers might well accept a license under a consent decree and forego an attack on validity until favored by a stronger financial position, or until threatened by other manufacturers who were not paying royalties. By giving *res judicata* effect to consent decrees this court protects the public interest in that an alleged infringer is deprived of a judicial device which could be used to postpone and delay a final adjudication of validity.³⁶³

In *Morton-Norwich Products, Inc. v. International Salt Co.*,³⁶⁴ a New York district court provided the counterargument to the Seventh Circuit's expansive reading of the *Lear* holding in *Crane*.

362. *Id.* at 780 ("We respectfully disagree with the Seventh Circuit's interpretation of *Lear*. In so holding we are in agreement with the Second Circuit, see *Broadview Chem. Corp.*, 474 F.2d 1391, 1395, and the Eighth Circuit, see *United States ex rel. Shell Oil Co.*, 430 F.2d 998, 1001-02.").

363. See also *Aro Corp. v. Allied Witan Co.*, 531 F.2d, 1368, 1373 (6th Cir. 1976), in which the Sixth Circuit relied on its reasoning in *Schlegel* to enforce an agreement entered into to settle a patent infringement suit and thereby prevent a licensee patent validity challenge ("We need add little herein to the comparatively exhaustive discussion by this court of the relationship between the public interest in getting invalid patents declared invalid and the public interest in peacefully settling lawsuits in *Schlegel Manufacturing Co. v. USM Corporation*, 525 F.2d 775, 187 U.S. P.Q. 417 (6th Cir. 1975) Whatever boon *Lear* may have provided those who take licenses under certain conditions, it cannot be interpreted so broadly as to condone a kind of gamesmanship, wherein an alleged infringer, after employing the judicial system for months of discovery, negotiation and sparring, abandons its challenge to validity, executes a license in settlement, and then repudiates the license and seeks to start the fight all over again in the courts. *Lear* does not require that the courts answer every beck and call of the fickle suitor whose transient affection is governed by such on-again, off-again strategies. The mantle of *Lear* ill befits him who would use and reuse the courts as pawns in a private game of varying design. The 'defender of the public interest' role is not available to him who would frustrate on whim the orderly conclusion of litigation. [paragraphing omitted]").

364. 183 USPQ 748.

The case involved an action by patent licensee Morton-Norwich for a declaratory judgment that International's licensed patent was invalid. International counterclaimed that its patent was infringed by Morton-Norwich on the theory that the latter's suspension of royalty payments due under the license agreement resulted in a termination of the agreement in accordance with its terms and Morton-Norwich's continued use of the patented invention was without authorization. Morton-Norwich argued "that the infringement charge is insufficient as a matter of law because the withholding of royalties pending the outcome of validity litigation was judicially sanctioned in *Lear v. Adkins*, 395 U.S. 653, 162 USPQ 1 (1969), and hence . . . International cannot use the nonpayment to declare a breach. From this it follows that the licensing agreement is still in force and, as such, forecloses an infringement suit."³⁶⁵ The single issue before the court was whether International's infringement counterclaim was dismissible under *Lear*.

In a decision intended to set a limit on the impact of the *Lear* holding, the *Morton-Norwich* district court ruled that International had the right to unilaterally terminate its license agreement and, accordingly, its infringement counterclaim was valid. The court began its opinion by noting the procedural differences between the *Lear* case and the case under consideration. In *Lear*, the licensor had elected to sue for royalties under the contract and the U.S. Supreme Court had ruled that the licensee was not estopped from interposing a patent invalidity defense or required to pay royalties during the pendency of the litigation. By contrast, Morton-Norwich was asserting patent invalidity in an offensive posture and was facing a patent infringement counterclaim by International. This procedural difference was dispositive of the issue in the case in that the *Morton-Norwich* district court adopted the view that "[n]othing in *Lear* prevents the licensor from treating a nonpayment of royalties due under the terms of the contract as a breach of it and a ground for termination in accordance with its terms. *Metallurgical Int'l*, . . . 171 USPQ at 350. Compare *Crane v. Aeroquip Corp.*, . . . 356 F. Supp. at 738-39, 177 USPQ at 669-670."³⁶⁶ A licensor could sue for royalties owed under a patent license agreement, as in the *Lear* case, or terminate the license agreement for nonpayment of royalties

365. *Id.* at 748-49.

366. *Id.* at 750, n 10. See also *Metallurgical Int'l, Inc.*, 171 USPQ at 350 ("Lear did not deal with whether or not a license could or should be terminated, but rather only with whether a licensee under a license that had not been terminated could challenge a patent's validity.").

and sue for patent infringement, as International had done. The *Morton-Norwich* court did not question a licensee's right to bring a declaratory judgment action challenging the validity of the licensed patent, but concluded that such a challenge, when coupled with a failure to pay royalties due under the license, had an associated cost, i.e., the risk of termination of the licensed right to the patent.

The *Morton-Norwich* district court reinforced its ruling by emphasizing the "inherent inequity" of extending the *Lear* holding to prevent International from terminating its patent license agreement:

At the core of *Lear* is a balancing of the equities among licensor, licensee and the public interest. To permit a licensee, as in this case, to enter into a license agreement after presumably good faith bargaining and receive the benefits of the inventor's investment in money, time and talent, and on the next day institute an action seeking a judgment declaring the patent invalid while at all times during the litigation withholding from the licensor the agreed upon consideration certainly does not score high on the scales of equity. . . . The licensor, having granted the right to use his presumptively valid invention, should not be cut off from the reward he has bargained for absent the circumstances set forth in *Lear* [in which the licensor elected to sue for royalties under the contract]. The plaintiff [licensee] can seek a declaration of invalidity and protect his rights under the license agreement by continuing to pay royalties. However, permitting the licensee to unilaterally and offensively ignore his contract obligation to make payments required under the contract, and at the same time denuding the licensor of the remedy of declaring a breach and seeking relief against the licensee as an infringer, . . . does violence to contract principles Considered from the standpoint of equitable treatment of the parties, the licensor is clearly being shortchanged.³⁶⁷

The *Morton-Norwich* district court ended its analysis by arguing that relying on the *Lear* holding to prevent International from terminating its license agreement would not be compatible with federal patent policy. The court noted that "[w]hile this policy favors the free dissemination of unpatentable ideas and the early judicial determination of validity challenges, it also provides for the

367. *Id.* at 749-50, 751 (footnotes omitted) (paragraphing omitted) .

limited grant of a secure monopoly to inventors as an incentive to develop new ideas and to disseminate them in the licensing marketplace so as to deter the 'hoarding' of new ideas and new patents."³⁶⁸ Discarding all relevant state law in an effort to promote the elimination of invalid patents would have the effect of "loading the scales against" the patentee/licensor in the process of negotiating a patent license and could, thereby, diminish the incentive to create, and reduce the inclination to license and/or publicly disclose, intellectual property in a way that would, on balance, frustrate the overarching goal of federal patent policy.³⁶⁹

The district judge writing for the court in *Morton-Norwich* provided the following closing comment: "In summary, I have concluded that it would be inappropriate to extend the scope of *Lear* to such a point that the licensee would be in a 'heads I win – tails you lose' situation [citing *Troxel Mfg. Co. v. Schwinn Bicycle Co.*, 465 F.2d 1253, 1257 (6th Cir. 1972)]. The shield that licensees would enjoy were *Lear* so extended might encourage more validity litigation, but at too high a price."³⁷⁰ In marked contrast to the position taken by the Seventh Circuit in *Crane*, the *Morton-Norwich* court rejected the view that "any and all rules of contract law, patent law, and civil procedure [must] be ignored to give licensees every possible incentive to challenge patent validity."³⁷¹ The decision of the *Morton-Norwich* court, like that of the Sixth Circuit in *Schlegel*, is representative of a minority of post-*Lear* federal court decisions in which the temptation to apply the *Lear* holding to the facts under consideration was resisted.³⁷² Such decisions set the

368. *Id.* at 750 (footnotes omitted).

369. *Id.* at 750–51.

370. *Id.* at 750.

371. McCarthy, (*Part II*), *supra* note 321, at 568.

372. See *Broadview Chem. Corp. v. Loctite Corp.*, 474 F.2d 1391 (2d Cir. 1973); *Morton-Norwich Prods.*, 183 USPQ 748; *Wallace Clark & Co. v. Acheson Indus., Inc.*, 532 F.2d 846 (2d Cir. 1976); *Metallurgical Int'l., Inc.*, 171 USPQ 348; *Interdynamics, Inc.*, 653 F.2d 93; *Schlegel Mfg. Co.*, 525 F.2d 775; *Aro Corp.*, 531 F.2d 1368; *Ransberg Electro-Coating Corp.*, 489 F.2d 974; *Amer. Equip. Corp. v. Wikomi Mfg. Co.*, 630 F.2d 544 (7th Cir. 1980); *U.S. ex. rel. Shell Oil Co.*, 430 F.2d 998; *Neb. Eng'g. Corp.*, 557 F.2d 1257; see also *Timely Products, Inc. v. Costanzo*, 465 F. Supp. 91, 96 (D. Conn. 1979) for a district court's interpretation of the limited scope of the U.S. Supreme Court's *Lear* decision. ("In its holding, *Lear* does not go so far as to invalidate an agreement that only reduces the incentive of a licensee to challenge patent validity. However, *Lear* did invalidate an agreement which, if enforced, would have left the licensee with 'little incentive' to challenge the patent. *Id.* [*Lear Inc. v. Adkins*, 395 U.S. 653] at 674 Thus, at a minimum, *Lear* means that the policy of the patent laws must displace contract provisions which, if enforced, leave the licensee without any incentive to challenge the patent.").

stage for the more methodical limitation of the reach of *Lear* later undertaken by the Federal Circuit, as discussed in the next section.

iii. The Federal Circuit

From its inception, the Court of Appeals for the Federal Circuit has rendered decisions that have recognized limits to the scope of the U.S. Supreme Court's holding in *Lear*. The Federal Circuit has rejected *Lear*-based arguments in preventing patent validity challenges (1) by patent assignors,³⁷³ (2) in the context of the settlement of litigation,³⁷⁴ and (3) under certain circumstances where such challenges were contractually prohibited.³⁷⁵ In addition, the court identified prerequisites to patent validity challenges that must be met by a patent licensee³⁷⁶ and established jurisdictional barriers to licensee patent challenges.³⁷⁷ Most significantly, for the purposes of this Article, the Federal Circuit has held that a patent licensee that challenges the validity of the licensed patent can be subject to consequences that could constitute a disincentive to make the challenge in the first place,³⁷⁸ despite the public interest, highlighted in *Lear*, in eliminating invalid patents. In this section, we review the Federal Circuit's important *Lear*-related decisions. While the U.S. Supreme Court's ruling in *MedImmune* rejected the Federal Circuit's position with respect to a jurisdictional barrier to a licensee patent validity challenge and called into question the Federal Circuit's pronouncement that there are prerequisites to a licensee patent challenge, other *Lear*-related holdings of the Federal Circuit remain good law. The extent to which one should rely on the implications

373. *Diamond Scientific Co. v. Ambico, Inc.*, 848 F.2d 1220 (Fed. Cir. 1988); *Shamrock Techs., Inc. v. Med. Sterilization, Inc.*, 903 F.2d 789 (Fed. Cir. 1990); *Acoustical Design, Inc. v. Control Elecs. Co., Inc.*, 932 F.2d 939 (Fed. Cir. 1991); *Intel Corp. v. U.S. Int'l Trade Comm'n*, 946 F.2d 821 (Fed. Cir. 1991); *Q.G. Prods., Inc. v. Shorty, Inc.*, 992 F.2d 1211 (Fed. Cir. 1993); *Carroll Touch, Inc. v. Electro Mech. Sys., Inc.*, 15 F.3d 1573 (Fed. Cir. 1993); *Mentor Graphics Corp. v. Quickturn Design Sys., Inc.*, 150 F.3d 1374 (Fed. Cir. 1998); *Pandrol USA, LP v. Airboss Ry. Prods., Inc.*, 424 F.3d 1161 (Fed. Cir. 2005).

374. *Foster v. Hallco Mfg. Co., Inc.*, 947 F.2d 469 (Fed. Cir. 1991); *Diversey Lever, Inc. v. Ecolab, Inc.*, 191 F.3d 1350 (Fed. Cir. 1999); *Flex-Foot, Inc. v. CRP, Inc.*, 238 F.3d 1362 (Fed. Cir. 2001); *Ecolab Inc. v. Paracclipse, Inc.*, 285 F.3d 1362 (Fed. Cir. 2002).

375. *Diversey Lever, Inc.*, 191 F.3d 1350; *Flex-Foot, Inc.*, 238 F.3d 1362.

376. *Studiengesellschaft Kohle*, 112 F.3d 1561.

377. *Gen-Probe Inc.*, 359 F.3d 1376; *MedImmune, Inc.*, 409 F.3d 1376; *MedImmune, Inc.*, 427 F.3d 958.

378. *C.R. Bard, Inc. v. Schwartz*, 716 F.2d 874 (Fed. Cir. 1983); *Cordis Corp. v. Medtronic, Inc.*, 780 F.2d 991 (Fed. Cir. 1985); *Sun Studs, Inc. v. ATA Equip. Leasing, Inc.*, 872 F.2d 978 (Fed. Cir. 1989); *Studiengesellschaft Kohle*, 112 F.3d 1561; *Dow Chem. Co.*, 226 F.3d 1334.

of such holdings, however, to craft explicit pro-licensor contract provisions that have the effect of reducing the incentive of a licensee to challenge a licensed patent remains an open question, as will be discussed in Part IV of this Article.

- **Assignor Estoppel**

In *Diamond Scientific Co. v. Ambico, Inc.*,³⁷⁹ the Federal Circuit was presented with one of its first opportunities to limit the reach of the *Lear* holding. In that case, the court was asked to consider the continued viability of the doctrine of assignor estoppel following the U.S. Supreme Court's decision in *Lear*. Assignor estoppel prevents the assignor of a patent from challenging the validity of the assigned patent as a defense to an infringement claim brought by the assignee.³⁸⁰ As noted elsewhere in this Article,³⁸¹ assignor estoppel is a contract-based prohibition to a challenge of a patent's validity that is considered closely related to licensee estoppel, and judicial decisions addressing the former have had a pronounced influence on decisions addressing the latter.³⁸² In *Diamond Scientific*, however, the Federal Circuit relied on an important difference between the two estoppel doctrines to conclude that, despite the U.S. Supreme Court's *Lear* decision, assignor estoppel remained a viable doctrine under appropriate circumstances and in the case before the court the doctrine prevented the assignor's patent validity challenge. The Federal Court distinguished the *Lear* decision by noting that:

Lear resolved the issue of licensee estoppel by writing its obituary; but for courts wrestling with assignor estoppel it was less clear whether *Lear* had also sounded the death knell for that doctrine. Certainly, there was nothing in its holding that eliminated the doctrine. Beyond the questioning dicta in *Lear*, the Court has left assignment estoppel untouched for the past nineteen years

379. 848 F.2d 1220.

380. Under the doctrine of assignor estoppel, a party in privity with the assignor is also estopped from raising patent invalidity as a defense to an infringement claim. See, e.g., *Diamond Scientific Co.*, 848 F.2d 1220; *Shamrock Technologies, Inc.*, 903 F.2d 789; *Intel Corp.*, 946 F.2d 821; *Carroll Touch, Inc.*, 15 F.3d 1573; *Mentor Graphics Corp. v. Quickturn Design Systems, Inc.*, 150 F.3d 1374.

381. See *supra* section III.A.; *supra* note 61; *supra* section III.A.5.a.

382. See, e.g., *supra* section III.A.5.a. for a discussion of the U.S. Supreme Court's decisions in *Westinghouse* and *Scott Paper* and *supra* section III.C.3. for the *Lear* court's reliance on those decisions in its abrogation of the doctrine of licensee estoppel.

In examining *Lear*, one important distinction between assignors and licensees becomes apparent – a distinction that cautions against the automatic application to assignment cases of the rationale underlying *Lear* and licensees. The public policy favoring allowing a licensee to contest the validity of the patent is not present in the assignment situation. Unlike the licensee, who, without *Lear* might be forced to continue to pay for a potentially invalid patent, the assignor who would challenge the patent has already been fully paid for the patent rights.³⁸³

The Federal Circuit's primary consideration in applying assignor estoppel in *Diamond Scientific* was "the measure of unfairness and injustice that would be suffered by the assignee if the assignor were allowed to raise defenses of patent invalidity."³⁸⁴ The court reasoned that "an assignor should not be permitted to sell something and later to assert that what was sold is worthless, all to the detriment of the assignee."³⁸⁵ According to the court, "it is the implicit representation by the assignor that the patent rights that he is assigning (presumably for value) are not worthless that sets the assignor apart from the rest of the world and can deprive him of the ability to challenge later the validity of the patent. To allow the assignor to make that representation at the time of the assignment (to his advantage) and later to repudiate it (again to his advantage) could work an injustice against the assignee."³⁸⁶

The Federal Circuit concluded its decision in *Diamond Scientific* with the following:

Our holding is that this is a case in which public policy calls for the application of assignor estoppel. We are, of course, not unmindful of the general public policy disfavoring the repression of competition by the enforcement of worthless patents. Yet despite the public policy encouraging people to challenge potentially invalid patents, there are still circumstances in which the equities of the contractual relationships between the parties should deprive one party (as

383. 848 F.2d at 1223–24.

384. *Id.* at 1225.

385. *Id.* at 1224.

386. *Id.*

well as others in privity with it) of the right to bring that challenge

. . . Although the doctrine of assignor estoppel may no longer be a broad equitable device susceptible of automatic application, the case before us is appropriate for its use³⁸⁷

Following its decision in *Diamond Scientific*, the Federal Circuit has continued to apply the doctrine of assignor estoppel on a case-by-case basis,³⁸⁸ including in a case in which the assignor was a licensee under the assigned patent.³⁸⁹ In *Acoustical Design*, the Federal Circuit rejected the argument that, because the assignor was also a licensee, the U.S. Supreme Court's abrogation of the doctrine of licensee estoppel in *Lear* was dispositive in the case and permitted the assignor's patent validity challenge. Relying on its decision in *Diamond Scientific*, the Federal Circuit concluded:

This argument [that *Lear* is controlling] is not persuasive. That a patent assignor takes back a license does not free him from the fact that he previously sold the patent for value. As the district court concluded, the assignor, in challenging the patent, is still asserting that what he sold is worthless, and the existence of a license back does not alter that fact We consider an assignor-licensee to be in a different situation from that of an ordinary licensee and view *Diamond Scientific* to be applicable even when there is a subsequent license back to the assignor³⁹⁰

- ***Res Judicata* and Contractual Estoppel**

In *Foster v. Hallco Manufacturing Co.*,³⁹¹ the Federal Circuit was presented with another opportunity to limit the application of the *Lear* holding. The issue before the court was whether "the patent

387. *Id.* at 1224–26 (footnote omitted).

388. See *Shanrock Technologies, Inc.*, 903 F.2d 789; *Acoustical Design, Inc.*, 932 F.2d 939; *Intel Corp.*, 946 F.2d 821; *Q.G. Products, Inc. v. Shorty, Inc.*, 992 F.2d 1211 (Fed. Cir. 1993); *Carroll Touch, Inc.*, 15 F.3d 1573; *Mentor Graphics Corp.*, 150 F.3d 1374; *Pandrol USA, LP v. Airboss Railway Products, Inc.*, 424 F.3d 1161 (Fed. Cir. 2005); but see *Sun Studs, Inc.*, 872 F.2d 978.

389. *Acoustical Design, Inc.*, 932 F.2d 939.

390. *Id.* at 943.

391. 947 F.2d 469 (Fed. Cir. 1991).

policy expressed in *Lear v. Adkins* . . . override[s] the *res judicata* effect of a consent decree declaring a patent valid"³⁹² and, accordingly, barred the patent validity challenge brought in the instant case. The Federal Circuit acknowledged the conflict in precedent of the regional circuits, citing, *inter alia*, the Ninth Circuit's decision in *Massillon*, the Seventh Circuit's decisions in *Crane* and *Kraly* and the Sixth Circuit's decision in *Schlegel*. Adopting arguments set forth in *Schlegel*, the Federal Circuit concluded "that general principles of *res judicata* apply, despite the policies favoring challenges to validity expressed in *Lear*."³⁹³

The Federal Circuit in *Foster* distinguished the *Lear* holding by noting that "[t]he application of *res judicata* principles . . . involves a public policy totally absent from *Lear*."³⁹⁴As the court explained,

[t]he Supreme Court in *Lear* did not consider the policy concerns evoked when preserving the finality of a judgment, but only the policies involved in resolving the right of a patent licensee to challenge the validity of the licensed patent in a suit for royalties under the contract. That question puts at odds only the binding effect of contract provisions under state contract law and the federal patent policy favoring free use of ideas rightfully belonging to the public domain³⁹⁵

In considering whether or not to bar the repeat patent validity challenge in the case before it, the *Foster* court cited the *res judicata* effect of a consent judgment that acknowledges both patent validity and infringement, the strong public interest in the settlement of patent litigation and the fact that enforcing the binding effect of *res judicata* encourages early and vigorous patent validity challenges favored by the U.S. Supreme Court in *Lear*.³⁹⁶ The Federal Circuit ended its consideration of the *Lear* holding by stating that "we cannot conclude that the public policy expressed in *Lear* is so overriding that challenges to validity must be allowed when under normal principles of *res judicata* applicable to a consent judgment, such challenge would be precluded."³⁹⁷

392. *Id.* at 474.

393. *Id.* at 475.

394. *Id.* at 476.

395. *Id.*

396. *Id.* at 476-77 (quoting from *Schlegel* with respect to the last point).

397. *Id.* at 477 (footnote omitted).

In an important respect, the Federal Circuit's decision in *Foster* was more nuanced than prior decisions of the regional circuits addressing the preclusive effect of a consent judgment of patent validity in the aftermath of *Lear*, in that the Federal Circuit considered claim preclusion and issue preclusion separately. The Federal Circuit in *Foster* held that a consent judgment respecting validity, where a device is adjudicated to infringe the valid patent, is to be given *res judicata* effect in the form of claim preclusion where the device in the second suit is essentially the same (i.e., identical or with only colorable differences or with changes unrelated to the limitations in the patent claim) as that in the first suit settled by the consent judgment. In such a circumstance, claim preclusion would block a subsequent patent validity challenge because of the *res judicata* effect of the consent judgment, despite the *Lear* public policy argument.³⁹⁸ The *Foster* court went on to note, however, that the situation is different with respect to issue preclusion. A consent judgment respecting validity has *res judicata* effect to preclude a patent challenge by the same alleged infringer with an allegedly infringing device that is *not* essentially the same as the device in the first suit *only* where the language in the consent judgment (or an associated settlement agreement) clearly indicates the intent of the parties to bar the defense of invalidity in *any* future dispute between the same parties with respect to infringement of the same patent irrespective of whether the allegedly infringing device is the same as that in the first suit, demonstrating the need for and enforceability of an unambiguous "no-challenge" provision (which, according to the Federal Circuit, was absent in the *Foster* consent judgment). The court concluded its analysis by stating that

398. The Federal Circuit's holding in *Panduit Corp. v. Hellermannntyton Corp.*, 451 F.3d 819 (Fed. Cir. 2006) (adjudicating a claimed breach of a settlement agreement, in the absence of a consent judgment) *may* qualify (by narrowing) the conclusion in *Foster* regarding the claim preclusion effect of a consent judgment. If the consent judgment (or, presumably, an associated settlement agreement) also contains an obligation of the alleged infringer to not engage in infringing activity with respect to a specifically identified product, then the claim preclusion effect of the consent judgment would only cover the specifically identified product (or a product that is physically the same as the specifically identified product) and *not* other products that are not physically the same as the specifically identified product, including ones that are, in the language used in *Foster*, "essentially the same" but not physically identical (i.e., those with only colorable differences or with changes unrelated to the limitations in the patent claims). This is a type of contractual override that narrows the effect of *res judicata* in the absence of a contract limitation.

[t]his position strikes a reasonable balance between the policy considerations enunciated in *Lear*, and those favoring voluntary settlement of litigation. While we have concluded that the *Lear* policy considerations do not mandate that future challenges to a patent's validity cannot be barred by a consent judgment, such considerations should weigh into the interpretation of the terms in a consent judgment for purposes of issue preclusion. Barring subsequent challenges favors the public policy of encouraging voluntary settlement; at the same time, a narrow construction of . . . provisions [in a consent judgment asserted to preclude litigation of the issue of patent validity in a subsequent infringement suit] favors challenges to validity. Thus, a balance in the policy expressed in *Lear* and the interest in encouraging settlement is achieved.³⁹⁹

The Federal Circuit's decision in *Foster* anticipated its subsequent decisions in two related cases. In both *Diversey Lever, Inc. v. Ecolab, Inc.*⁴⁰⁰ and *Flex-Foot, Inc. v. CRP, Inc.*,⁴⁰¹ the Federal Circuit found that issue preclusion barred a patent validity challenge based on an unambiguous agreement by the parties settling a prior patent-related suit. In *Diversey Lever*, the settlement agreement that accompanied a consent judgment acknowledged that the two patents-in-suit were valid and enforceable and provided that Ecolab, the alleged infringer, "will not directly or indirectly aid, assist or participate in any action contesting the validity of either [of] the . . . patents."⁴⁰² The agreement also prohibited Ecolab from making or selling products that utilized two specific chemical compositions. Interpreting the prohibition in the agreement to be limited to the use of the specified compositions, Ecolab developed products using other compositions, which it acknowledged were covered by the patents at issue. Diversey, the patent holder, brought suit against Ecolab challenging the latter's use of the different compositions and asserted that Ecolab was barred from contesting the validity of the patents allegedly infringed in the new suit and the subject of the prior, settled dispute. Relying on the legal reasoning in *Foster*, the Federal Circuit held that the "no-challenge" provision contained in the settlement

399. *Foster*, 947 F.2d at 481.

400. 191 F.3d 1350.

401. *Flex-Foot, Inc.*, 238 F.3d 1362.

402. 191 F.3d at 1351.

agreement precluded Ecolab from challenging the patents-in-suit. In the words of the court,

[w]e have recognized that a consent judgment of patent validity may preclude a party from asserting invalidity in subsequent litigation involving new accused products, as long as the agreement manifests an intent to be bound. See *Foster*, 947 F.2d at 481. However, any surrender of the right to challenge validity of a patent is construed narrowly. See *id.* In *Foster*, we refused to hold that a consent judgment had surrendered the invalidity defense as to future accused products, even though the agreement stated that the patents were “valid and enforceable in all respects.” See *id.* The settlement agreement between Diversey and Ecolab similarly declares “that the . . . patents [in suit] are valid and enforceable,” but *Foster* requires more for a waiver of the invalidity defense as to future accused products. To show that Ecolab’s right to contest validity of the patents has been unequivocally foreclosed, Diversey Lever points to the settlement agreement provision that Ecolab will not “directly or indirectly aid, assist or participate in any action contesting the validity” of the patents. Ecolab argues that this clause merely precludes it from voluntarily assisting third parties accused of infringement by Diversey Lever. We cannot agree. As the district court held, “only one interpretation flows from” the clause, which uses the broadest possible language in describing the prohibited activity – that Ecolab surrendered its right to challenge the validity of the patents in any context.⁴⁰³

In *Flex-Foot, Inc. v. CRP, Inc.*⁴⁰⁴ the Federal Circuit was faced with a fact pattern that differed slightly from that in *Diversey Lever*. The parties in *Flex-Foot* had settled a prior litigation relating to the validity of a Flex-Foot patent by entering into a settlement agreement and corresponding license agreement. While the parties agreed to a dismissal of the suit with prejudice, they did not enter into a consent judgment adjudicating the issues of infringement and validity. The settlement agreement, however, provided that CRP, Inc. d/b/a Springlite would not “challenge or cause to be challenged, directly or indirectly, the validity or enforceability of

403. *Id.* at 1352 (paragraphing omitted).

404. *Flex-Foot, Inc.*, 238 F.3d 1362.

the . . . patent . . . in any court or other tribunal, including the United States Patent and Trademark Office.”⁴⁰⁵ The agreement also required Springlite to “waive . . . any and all invalidity and unenforceability defenses in any future litigation, arbitration, or other proceeding,”⁴⁰⁶ with respect to any of Springlite’s products. The corresponding license agreement had similar language restricting Springlite’s right to challenge the Flex-Foot patent. Flex-Foot subsequently filed a complaint alleging that a Springlite product infringed its patent. Following an arbitration procedure that was decided in favor of Flex-Foot, Springlite filed a motion in a district court to vacate the arbitrators’ decision and to consider the patent invalidity defense that it had raised during arbitration. The district court confirmed the decision of the arbitrators’ in favor of Flex-Foot and held that “Springlite was ‘collaterally estopped’ from challenging the validity and enforceability of Flex-Foot’s . . . patent.”⁴⁰⁷ Springlite appealed the district court’s judgment to the Federal Circuit.

The Federal Circuit affirmed the district court’s judgment in favor of Flex-Foot, but rejected the lower court’s collateral estoppel argument, ruling instead that Springlite’s patent invalidity defense was barred on the basis of contractual estoppel resulting from the “no-challenge” provisions in the settlement and accompanying license agreements. The Federal Circuit acknowledged Springlite’s argument that it had not entered into a consent judgment in settling its prior dispute with Flex-Foot. It emphasized, however, that Springlite had agreed to a dismissal with prejudice following a settlement agreement that included a commitment by Springlite to not challenge the Flex-Foot patent. According to the Federal Circuit, these facts did not give rise to “collateral estoppel,” which the court defined in a footnote as “an affirmative defense barring a party from relitigating an issue *determined against that party* in an earlier action, even if the second action differs significantly from the first one.”⁴⁰⁸ The facts did, however, give rise to contractual estoppel of Springlite’s challenge to the validity of the Flex-Foot patent. The remaining question before the Federal Circuit, raised by

405. *Id.* at 1364.

406. *Id.*

407. *Id.*

408. *Id.* at 1368, quoting Black’s Law Dictionary 256 (7th ed. 1999) (with emphasis added by the court).

Springlite, was “whether such contractually created estoppel is void as against public policy pursuant to *Lear v. Adkins*.”⁴⁰⁹

In distinguishing *Lear*, the Federal Circuit noted that, unlike the agreements in the instant case, the license agreement in *Lear* was not entered into by the parties to settle litigation nor did it contain a promise by the licensee not to challenge the validity of the licensed patent. The court in *Flex-Foot* considered the altered circumstances in the instant case to be particularly meaningful in that they implicated “the important policy of enforcing settlement agreements and *res judicata* [which] must themselves be weighted against the federal patent laws’ prescription of full and free competition in the use of ideas that are in reality a part of the public domain.”⁴¹⁰ The court then cited Federal Circuit precedent, including *Hemstreet v. Spiegel, Inc.*⁴¹¹ and *Foster*, in concluding that the public interest in encouraging the settlement of litigation trumped that of eliminating invalid patents.

Hemstreet did not involve a licensee’s right to challenge the validity of the licensed patent, but a licensee’s contractual obligation to make payments under a patent license agreement entered into to settle a prior infringement suit. The license agreement in *Hemstreet* granted the alleged infringer a license to the patents-in-suit with an obligation to make payments “as they become due notwithstanding that said patents-in-suit may be held invalid and/or unenforceable in any other proceeding at a later date[.]”⁴¹² After the patents-in-suit were held to be unenforceable in a case involving another party, the licensee sought a court order to be relieved of having to make further payments, despite its contractual obligation. The licensee argued that the requirement to make payments with respect to an unenforceable patent would be inconsistent with the public interest, expressed in *Lear*, in encouraging patent licensees to challenge invalid patents and in relieving them of any royalty obligation during the pendency of a challenge. The Federal Circuit in *Hemstreet* rejected this argument in stating that “*Lear* . . . did not involve a settlement of litigation, but only the right of a patent

409. *Id.* (“Springlite does not contend that its intent in entering into the . . . Settlement Agreement and . . . Licensing Agreement was anything other than a waiver of future challenges to . . . [Flex-Foot’s] patent’s validity. Instead, Springlite argues that it should be entitled, under the public policy rationale set forth in *Lear*, to renege on its prior written agreement with Flex-Foot . . .”).

410. *Id.*

411. 851 F.2d 348.

412. *Id.* at 349.

licensee to challenge the validity of the licensed patent. The enforcement of settlement of litigation involves another public policy totally absent in *Lear*: the encouragement of settlement of litigation and the need to enforce such settlements in order to encourage the parties to enter into them.”⁴¹³ The Federal Circuit in *Flex-Foot* summarized its prior decision in *Hemstreet* as follows:

[T]he holding in *Hemstreet* was premised on the policy that while the federal patent laws favor full and free competition in the use of ideas in the public domain over the technical requirements of contract doctrine, settlement of litigation is more strongly favored by the law Clearly, the importance of *res judicata* and its hierarchical position in the realm of public policy was not a relevant consideration in *Lear* and therefore the Supreme Court never evaluated the importance of *res judicata* and whether it trumps the patent laws’ prescription of full and free competition in the use of ideas that are in reality a part of the public domain⁴¹⁴

The Federal Circuit in *Flex-Foot* cited *Foster* for the proposition that, despite *Lear*’s abrogation of licensee estoppel, a consent decree acknowledging patent validity and infringement gives rise to *res judicata* that can barr a subsequent patent validity challenge. The *Flex-Foot* court further noted that:

Foster echoes *Hemstreet*’s teaching that there is a strong public interest in settlement of patent litigation and that upholding the terms of a settlement encourages patent owners to agree to settlements—thus fostering judicial economy These interests are relevant to the instant case, even though this case deals with a settlement agreement and resulting dismissal with prejudice, rather than a consent decree.⁴¹⁵

The Federal Circuit concluded its holding in *Flex-Foot* with the following pronouncement:

Once an accused infringer has challenged patent validity, has had an opportunity to conduct discovery on validity issues,

413. *Id.* at 350.

414. *Flex-Foot, Inc.*, 238 F.3d at 1369.

415. *Id.* at 1369-70.

and has elected to voluntarily dismiss the litigation with prejudice under a settlement agreement containing a clear and unambiguous undertaking not to challenge validity and/or enforceability of the patent in suit, the accused infringer is contractually estopped from raising any such challenge in any subsequent proceeding.^{416, 417}

416. *Id.* at 1370.

417. For a post-*Foster* Federal Circuit decision in which the court failed to find evidence of the clear and unambiguous intent of the parties necessary to barr a subsequent patent validity challenge, see *Ecolab Inc. v. Paraclypse, Inc.*, 285 F.3d 1362, 1377 (Fed. Cir. 2002) (citing its prior decision in *Foster*, the Federal Circuit in *Ecolab* required explicit language in a consent judgment evidencing the parties' intent that the patent-in-suit not be challenged by the alleged infringer in any future action, if the allegedly infringing party is to be precluded from relying on an invalidity defense in an infringement suit brought by the patent-holding party involving the alleged infringer's sale of a product that is not essentially the same as the product in the parties' original suit. Since there was no such language in the *Ecolab* consent judgment, the patent validity challenge was permitted, despite the consent judgment's acknowledgement of patent validity and its infringement by the product involved in the original suit. In the words of the Federal Circuit, "[h]ere, the consent judgment is more analogous to the agreement in *Foster* than *Diversey Lever*. Paraclypse [the alleged infringer] merely agreed in the consent judgment that 'the '690 patent is a valid patent.' Greater clarity than this is required to foreclose a validity defense in a new infringement suit involving a new product. Because the language of the consent judgment does not, standing alone, preclude the validity challenge, we must determine whether the products are 'essentially the same' . . . [and] . . . the record demonstrates to our satisfaction that the Insect Inn II and IV devices are not 'essentially the same.'"). See also, *Baseload Energy, Inc. v. Bryan W. Roberts*, 619 F.3d 1357 (Fed. Cir. 2010) (relying on its prior decisions in *Foster*, *Flex-Foot*, *Diversey Lever* and *Ecolab*, the Federal Circuit in *Baseload* concluded that the language of the settlement agreement in the instant case was not sufficiently clear and unambiguous to prevent a subsequent patent validity challenge. As the court explained, "[i]n the context of settlement agreements, as with consent decrees, clear and unambiguous language barring the right to challenge patent validity in future infringement actions is sufficient, even if invalidity claims had not been previously at issue and had not been actually litigated. Here, however, there is no such clear language . . ." *Id.* at 1363 (paragraphing omitted)). For a recent district court holding that relied on *Flex-Foot* and related Federal Circuit jurisprudence regarding contractual estoppel in the context of a settlement agreement, see *Warrior Lacrosse, Inc. v. Brine, Inc.*, 2006 WL 763190 (E.D. Mich. 2006) (citing *Flex-Foot*, *Diversey Lever*, *Foster*, *Hemstreet* and *Ecolab*, the district court in *Warrior* held that contractual estoppel in the context of a prior settlement involving the patents-in-suit and a settlement agreement containing a no-challenge provision estopped the alleged infringer, Brine, from challenging the validity and enforceability of the patents-in-suit as a defense to an infringement challenge brought by the holder of the patents, Warrior. In the words of the *Warrior* court, "[g]overning Federal Circuit case law at the time . . . [the parties] drafted the Settlement Agreement established that the promise not to contest the validity and enforceability of an asserted patent, entered in connection with the settlement of litigation, had binding effect." *Id.* at *26.).

- **Licensee Patent Validity Challenges; Prerequisites and Jurisdictional Barriers**

With the exception of *Hemstreet*, in each of the Federal Circuit cases discussed thus far in this section, a licensee's patent validity challenge was barred on the basis of considerations not addressed in *Lear's* balancing test, e.g., the inequity of an assignor's challenge of the validity of a patent that it had assigned for value or the public interest in encouraging the settlement of litigation through either the recognition of the preclusive effect of a consent decree that gives rise to *res judicata* or the enforcement of a "no-challenge" provision in a settlement agreement. We now turn to Federal Circuit decisions in which licensee patent validity challenges were acknowledged as permissible, but only after a licensee fulfills certain prerequisites and meets the jurisdictional requirements to bring the challenge.

Two Federal Circuit cases, *Studiengesellschaft Kohle, m.b.H. v. Shell Oil Co.*⁴¹⁸ and *Gen-Probe Inc. v. Vysis, Inc.*,⁴¹⁹ set the stage for the dispute that was resolved by the U.S. Supreme Court in *MedImmune*. In *Shell Oil*, *Studiengesellschaft Kohle* ("SGK") granted a license to Shell under a patent that covered a process for the manufacture of polypropylene pursuant to a license agreement in which Shell was obligated to (1) pay royalties for the sales of polypropylene manufactured using the patented process and (2) provide SGK with a report regarding its entire polypropylene production, including polypropylene manufactured using methods not covered by the licensed patent. Shell subsequently introduced a new method of polypropylene manufacture (the Seadrift Process) which, according to Shell, was not covered by the licensed patent. Shell did not pay royalties on the sales of polypropylene manufactured by the new process nor provide SGK with an accounting of such sales. Upon discovering Shell's breach of its contractual obligation, SGK terminated the license agreement, brought an action for unpaid royalties owed prior to the termination of the license, and sued Shell for infringement based on Shell's use of the patented process following the termination of the license. In response, Shell challenged the validity of certain of the patent claims.

418. 112 F.3d 1561.

419. 359 F.3d 1376 (overruled in part by *MedImmune, Inc.*, 549 U.S. 118).

The district court in the case ruled that the challenged patent claims were invalid and that the question of infringement of the other claims was not properly before the court. With respect to SGK's claim for royalties owed under the license agreement, the district court certified the following question for consideration by the Federal Circuit: "Where the Court has found the relevant patent claims invalid, may the Licensor recover damages for breach of contract for past royalties due on processes allegedly covered by such claims, from the date of the alleged breach until the date that the Licensee first challenged validity of the claims?"⁴²⁰ On appeal, the Federal Circuit (1) affirmed the district court's invalidity judgment, (2) reversed the district court's judgment regarding infringement and remanded the issue for further consideration, and (3) answered the certified question in the affirmative. For purposes of this Article, it is the Federal Circuit's analysis of the certified question that is of significance.

The Federal Circuit began its assessment of the certified question in *Shell Oil* by evaluating the provisions of the patent license agreement under consideration. The court concluded that, based solely on the dictates of contract law, Shell was obligated to pay the royalties owed prior to SGK's termination of the license agreement, irrespective of whether the relevant patent claims were valid. "Enforcement of these contract terms is not contingent upon validity of the patent which defines the subject matter of the license. Assuming that the Seadrift Process infringes claim 1 of the . . . patent and thus fits within the terms of the license, Shell breached the license by failing to pay royalties. Enforcement of the license, if the Seadrift Process infringes the . . . patent, would require Shell to pay back royalties."⁴²¹ The Federal Circuit then "examine[d] . . . the contract for rare, but potential, conflicts between state contract law and federal patent law."⁴²² Citing the *Lear* decision,⁴²³ in which "the Supreme Court prevented the enforcement of a valid royalty payment agreement to facilitate a determination of patent

420. 112 F.3d at 1562.

421. *Id.* at 1567.

422. *Id.*

423. The Federal Circuit in *Shell Oil* described the U.S. Supreme Court's *Lear* decision in less than approving terms. In a frequently referenced clause from its *Shell Oil* opinion, the Federal Circuit began its restatement of the *Lear* Court's rationale for its decision to abrogate the doctrine of licensee estoppel with "In tones that echo from a past era of skepticism over intellectual property principles, the Court in *Lear* feared that . . ." *Id.* at 1567.

validity,"⁴²⁴ the Federal Circuit acknowledged its obligation in the case before it "to consider 'whether overriding federal policies would be significantly frustrated' by enforcing the license."⁴²⁵

In concluding that Shell was bound by its contractual commitment to pay royalties pursuant to its license agreement with SGK, despite the U.S. Supreme Court's holding in *Lear*, the Federal Circuit presented two arguments. The first was based on the "avoidance of injustice" argument that the Federal Circuit had relied on in *Diamond Scientific* in support of the doctrine of assignor estoppel. In the words of the court in *Shell Oil*,

[a]s in *Diamond Scientific*, this court detects no significant frustration of federal patent policy by enforcing the . . . license agreement between Shell and SGK, to the extent of allowing SGK to recover royalties until the date Shell first challenged the validity of the claims. First, as in *Diamond Scientific*, Shell executed a contractual agreement which produced significant benefits for the corporation and attested to the worth of the patent. Under the agreement (with its provision for Shell to notify SGK of all polypropylene production), Shell had the benefits of producing polypropylene insulated from unlicensed competition, insulated from investigations of infringement, and even insulated from royalties (until SGK's discovery of the Seadrift Process). To these benefits, Shell now seeks to add the benefit of abrogating its agreement and avoiding its breach of the contract. Following the reasoning of *Diamond Scientific*, this court must prevent the injustice of allowing Shell to exploit the protection of the contract and patent rights and then later to abandon conveniently its obligations under those same rights. See *Diamond Scientific*, 848 F.2d at 1224-25 . . .⁴²⁶

Simply stated, the Federal Circuit concluded that the facts in *Shell Oil* presented "circumstances in which the equities of the contractual relationship . . . between the parties."⁴²⁷ required that the agreement between SGK and Shell be enforced, in spite of the federal patent policy expressed in *Lear*.

424. *Id.*

425. *Id.* (quoting *Lear*, 395 U.S. at 673).

426. *Id.* at 1568.

427. *Id.* at 1567 (quoting *Diamond Scientific*, 848 F.2d at 1224-25).

The *Shell Oil* court then raised a second argument, based on its determination that “Shell’s apparent breach of its duty to notify under the agreement is itself more likely to frustrate federal patent policy than enforcement of the contract.”⁴²⁸ As the Federal Circuit explained,

Lear focused on the “full and free use of ideas in the public domain.” *Lear*, 395 U.S. at 674, 89 S.Ct. at 1913. By abrogating its notification duty, Shell delayed a timely challenge to the validity of the ‘698 patent and postponed the public’s full and free use of the invention of the ‘698 patent. Shell enjoyed the protection of the license from 1987 until SGK became aware of the Seadrift Process. Upon SGK’s discovery of its Seadrift process, Shell suddenly seeks the protection of the *Lear* policies it flaunted for many years. However, a licensee, such as Shell, cannot invoke the protection of the *Lear* doctrine until it (i) actually ceases payment of royalties, and (ii) provides notice to the licensor that the reason for ceasing payment of royalties is because it has deemed the relevant claims to be invalid. Other circuits addressing this issue have arrived at the same conclusion. See, e.g., *Rite-Nail Packaging Corp. v. Berryfast, Inc.*, 706 F.2d 933, 936–37 (9th Cir.1983); *Hull v. Brunswick Corp.*, 704 F.2d 1195, 1203 (10th Cir.1983); *American Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890, 897–98 (3d Cir.1980); *PPG Indus., Inc. v. Westwood Chem., Inc.*, 530 F.2d 700, 706, 708 (6th Cir.1976). [Emphasis added].⁴²⁹

The Federal Circuit concluded its opinion in *Shell Oil* by holding that “[i]n this factual setting . . . enforcement of the license according to its terms, even if this entails a determination of whether the Seadrift process infringes a now-invalidated patent, does not frustrate federal patent policy.”⁴³⁰ Accordingly, it remanded the case to the district court for enforcement of Shell’s contractual obligation to pay royalties owed prior to Shell’s patent validity challenge.

In retrospect, the Federal Circuit’s *Shell Oil* decision is significant for the italicized pronouncement in the above-quoted excerpt (“the prerequisite statement”), rather than for the actual holding in the case. The plain meaning of the prerequisite

428. *Id.* at 1568.

429. *Id.*

430. *Id.*

statement is that in order for a patent licensee to invoke the protection of the *Lear* doctrine (i.e., to be able to challenge the validity of a licensed patent and be relieved of its royalty payment obligation during the pendency of the challenge and thereafter, if the challenge is successful), the licensee must first cease the payment of royalties and provide notice to the licensor that it has ceased the payment because it has determined that the licensed patent is invalid. The problem with the prerequisite statement is that patent licensors and courts have attempted to expand its application to fact patterns that differ significantly from that in *Shell Oil* and, thereby, make the cessation of royalties with appropriate notice a requirement for a licensee patent challenge in any context. For example, in a series of post-*Shell Oil* decisions,⁴³¹ the District

431. See *Revson v. Claire's Stores, Inc.*, 120 F. Supp. 2d 322, 326-327 (S.D. New York 2000) (“[T]he doctrine of licensee estoppel is not entirely dead. The *Kohle [v. Shell Oil]* case . . . stands for the proposition that a licensee is estopped to challenge the validity of a licensed patent in defense of a claim for unpaid royalties ‘until it (i) actually ceases payment of royalties, and (ii) provides notice to the licensor that the reason for ceasing payment of royalties is because it has deemed the relevant claims to be invalid.’ [112 F.3d at 1568] But it does leave open the possibility that *Lear, Inc. v. Adkins* will be applied once the licensee stops paying royalties on the grounds of alleged invalidity’); *Advanced Card Technologies LLC v. Versatile Card Technology, Inc.*, 410 F. Supp. 2d 158, 160-61 (S.D. New York 2006) (“I did not mean . . . to suggest that the doctrine of licensee estoppel had not been dealt a severe blow by the United States Supreme Court’s opinion in *Lear v. Adkins*, 395 U.S. 653, . . . (1969). However, as my esteemed colleague, Judge Kaplan, noted several years ago, ‘the doctrine of licensee estoppel is not entirely dead.’ *Revson v. Claire's Stores, Inc.*, 120 F. Supp. 2d 322, 326 (S.D.N.Y.2000) VCT [the licensee] is estopped to challenge the validity of the patents in suit because it has neither ceased payment of royalties nor notified plaintiff that the reason for cessation was the claimed invalidity of the patents. See *Studiengesellschaft Kohle, M.B.H. v. Shell Oil Co.*, 112 F.3d 1561 (Fed. Cir.), cert denied, 522 U.S. 996, 118 S.Ct. 560, 139 L.Ed.2d 401 (1997); . . . It is undisputed that VCT has paid and continues to pay royalties to ACT [the patentee] for all products that VCT believes are covered by Claims 8 of the ‘158 patent and 1 of the ‘584 patent. It is also undisputed that VCT has refused to pay royalties to ACT for other products it manufactures-the royalties that are the subject of this action-only because it believes that those claims do not read on certain of its products, and not because the claims are invalid. No party has suggested, and I have no reason to believe, that VCT has ever notified ACT that the reason it is not paying the royalties that are the subject of this action is that the claims in suit are invalid. Thus, the *Kohle [v. Shell Oil]* exception to *Lear* applies. [Paragraphing omitted]’); *Pony Pal. LLC v. Claire's Boutiques, Inc.*, 2006 WL 846354 *3-4 (S.D. New York 2006) (“See *Shell Oil*, 112 F.3d at 1568, where the court held that, in order for a licensee to avail himself of the doctrine embodied in *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), i.e., that a licensee is not estopped from challenging the validity of a patent, and to avoid liability for royalty payments on the basis of patent invalidity, the licensee must (1) cease making royalty payments, and (2) give notice to the patentee that the licensee contests the validity of the patent. The Federal Circuit’s rationale in *Shell Oil* was that a licensee who fails to challenge the validity of a patent benefits by retaining the protection of the license while depriving the public of the full and free use of the patented product by withholding a successful challenge to validity. Accordingly, such a licensee should not be allowed to avoid

Court for the Southern District of New York spoke of the prerequisite statement as creating an exception to *Lear's* abrogation of the doctrine of licensee estoppel, leaving that court to conclude that, despite *Lear*, "licensee estoppel is not entirely dead."⁴³² And as discussed above in Part II of this Article, one of the contract-based arguments of the licensor in *MedImmune* was that the licensee's action for a declaratory judgment of patent invalidity was impermissible because the latter failed to meet the requirements to bring the challenge by continuing to pay royalties under the license, an argument that was acknowledged, but not resolved, by Justice Scalia in his opinion.

A more limited interpretation of the meaning of the prerequisite statement in *Shell Oil* is based on the recognition, noted above in this Part III, that the two prongs of the *Lear* doctrine, while related, are separable. It could be argued that the Federal Circuit's reference in the *Shell Oil* prerequisite statement to the protection of the *Lear* doctrine was not meant to include the patent challenge right but only the right to avoid a royalty payment obligation. After all, the question certified by the district court in *Shell Oil* involved the recovery of past royalties due and *not* the requirements for a patent validity challenge. The licensee's patent validity defense to the licensor's claim for unpaid royalties was raised after the license agreement had been terminated by the licensor for breach, eliminating any question of licensee estoppel in the case. The licensee in *Shell Oil* had breached the agreement by failing to pay royalties on product sales that the licensor was initially unaware of (i.e., a silent breach), and these were the payments that the licensee sought to avoid making in light of the court's finding of patent invalidity. For this reason, *Shell Oil* presented the unusual circumstance in which a non-payment-of-royalties breach continued to occur over a considerable period of time prior to the licensor becoming aware of the breach and to the licensee challenging the validity of the previously licensed patent. The language in *Shell Oil*

liability for royalties for any such time period on grounds of patent invalidity. See *Revson v. Claire's Stores, Inc.*, 120 F. Supp. 2d 322, 327 (S.D.N.Y.2000) (licensee cannot avoid liability for royalty payments on the basis of patent invalidity for that period of time before licensee both ceased making royalty payments and notified patentee that validity was contested) (citing both *Lear* and *Shell Oil*); see also *Advanced Card Tech., LLC v. Versatile Card Tech., Inc.*, 410 F. Supp.2d 158, 161 (S.D.N.Y.2006). ("[The licensee] is estopped to challenge the validity of the patents in suit because it has neither ceased payment of royalties nor notified plaintiff that the reason for cessation was the claimed invalidity of the patents.") (citing *Shell Oil*)." (footnotes omitted) (paragraphing omitted)).

432. *Revson*, 120 F. Supp. 2d at 326.

could be interpreted to mean that a licensee can challenge the validity of a licensed patent *whether or not* it stops complying with its royalty payment obligation; *but*, if the licensee wishes to avoid its royalty payment obligation in the event that the licensed patent is ultimately found to be invalid as a result of its patent challenge, the licensee must have indicated to the licensor at the time it stopped making the royalty payments that it stopped because it believed that the licensed patent was invalid.⁴³³

The major objection to this alternative interpretation of the prerequisite statement is Judge Rader's description in *Gen-Probe*⁴³⁴ of the Federal Circuit's *Shell Oil* decision, which description must be given special weight in light of the fact that Judge Rader also wrote the *Shell Oil* opinion. In *Gen-Probe*, Judge Rader provided the following explanatory comment after quoting the prerequisite statement from *Shell Oil*: "This language posits that a licensee must, at a minimum, stop paying royalties (and thereby materially breach

433. The declaratory judgment plaintiff in *MedImmune* appears to have argued in favor of this interpretation of the *Shell Oil* prerequisite statement on remand of the case to the U.S. District Court for the Central District of California. *MedImmune, Inc.*, 535 F.Supp.2d 1000. In noting that the Supreme Court in *MedImmune* had failed to resolve the question of whether *Lear* applied only to a repudiating licensee or whether the *Shell Oil* prerequisite statement was inconsistent with *Lear*, the district court repeated the Supreme Court's statement that "[w]e express no opinion on whether a *nonrepudiating licensee* is similarly relieved of its contract obligation during a successful challenge to a patent's validity—that is, on the applicability of licensee estoppel under these circumstances." *MedImmune, Inc.*, 535 F. Supp. 2d at 1016 (quoting *MedImmune, Inc.*, 549 U.S. at 124). The district court then provided the following information in a footnote: "At oral argument, MedImmune cited the 'successful challenge to a patent's validity' language in the Supreme Court's decision as implying that a licensee could challenge validity—and only the relief from the contract obligation under *Lear* was left undetermined." *Id.* at 1016 n.12. The district court did not comment further on this argument by MedImmune, that could be interpreted as suggesting that the *Shell Oil* prerequisite statement applied only to the royalty payment prong, and not the patent challenge prong, of the *Lear* doctrine. Rather, as will be discussed in section III.C.4.c.iv. of this Article, the district court in *MedImmune* ruled that the *Shell Oil* holding should be confined to the unusual facts in that case and it was, therefore, inapposite to the instant case. As to the above-quoted statement by the Supreme Court, it should be noted that it was made in the context of the Court's discussion of MedImmune's contractual obligation to pay royalties. While the statement is, perhaps, not as clear as it might be, moving from an assessment of MedImmune's contractual obligation to the applicability of licensee estoppel, it could be read to mean that the Court did not intend to express an opinion as to whether, as in the case of a repudiating licensee, a nonrepudiating licensee is permanently relieved of its contractual obligation to pay royalties that accrued during the pendency of its patent challenge (were such a challenge permitted following a ruling on the merits of any contract-based arguments against it, which the Court in *MedImmune* was not prepared to make), if the patent-at-issue were ultimately held to be invalid.

434. 359 F.3d 1376.

the agreement) *before bringing suit to challenge the validity or scope of the licensed patent.*"⁴³⁵ It would appear, then, that the *Shell Oil* prerequisite statement was intended to apply to a licensee's patent challenge right as well as the right to avoid a royalty payment obligation, at least under certain circumstances.

Perhaps a better interpretation of the meaning of the *Shell Oil* prerequisite statement can be derived from consideration of the policy argument underlying the U.S. Supreme Court's *Lear* decision and the regional circuit holdings that the Federal Circuit cited in *Shell Oil* as consistent with the prerequisite statement.⁴³⁶ Under this interpretation, the critical factor in determining whether or not a licensee is permitted to challenge the validity of a licensed patent is whether the licensee has taken an affirmative step to encourage the early adjudication of invalidity in order to eliminate a worthless patent. Such a step could come in the form of the cessation of royalty payments under the license agreement with notice provided to the licensor as to the reason (in the case of a repudiating licensee) or an action brought by the licensee to contest the validity of the licensed patent, even under circumstances in which the licensee continues to pay royalties under the license agreement (in the case of a nonrepudiating licensee in good standing). According to this view, it is immaterial as to whether the licensee had received benefits under the license agreement prior to its taking the affirmative step to encourage the patent challenge, or continues to receive benefits as a licensee in good standing following such step. Moreover, the date of the licensee's affirmative step determines the point at which the licensee's obligation to comply with the royalty payment provision of its license agreement terminates.

In each of the regional circuit court opinions cited by the Federal Circuit in *Shell Oil* (*PPG*, *American Sterilizer*, *Rite-Nail* and *Hull*), as well as in the *Shell Oil* case itself, a fundamental question before the court was whether the validity of the licensed patent was relevant to the licensee's obligation under its license agreement to pay royalties during the period that preceded an action by the licensee to encourage the patent challenge. And in each case, including *Shell Oil*, the court ruled that the answer to the question

435. *Id.* at 1381 (emphasis added).

436. See *Rite-Nail Packaging Corp. v. Berryfast, Inc.*, 706 F.2d 933 (9th Cir.1983); *Hull v. Brunswick Corp.*, 704 F.2d 1195 (10th Cir. 1983); *Am. Sterilizer Co.*, 614 F.2d 890; *PPG Indus., Inc.*, 530 F.2d 700.

was no.⁴³⁷ The licensee was bound by its agreement to pay royalties in consideration for rights under the licensed patent, irrespective of the patent's validity, until it undertook an action "of the type to prompt an early adjudication of invalidity,"⁴³⁸ thereby furthering the public's interest in eliminating specious patents. In *Bristol Locknut Co. v. SPS Technologies, Inc.*,⁴³⁹ the Ninth Circuit summarized the holdings in *PPG* and *American Sterilizer* as follows:

A licensee remains obligated to pay all royalties under a licensing agreement which accrue until it takes an affirmative step that would prompt the early adjudication of the validity of the patent, such as filing an action contesting the patent's validity or notifying the licensor that the payments were being stopped because the patent was believed to be invalid. *PPG*

437. On the few occasions, other than in *Shell Oil*, where the Federal Circuit was asked to specifically rule on a licensee's royalty payment obligation in the context of a patent validity challenge in the aftermath of *Lear*, the court expressed its willingness to interpret the reach of *Lear* in a manner consistent with prior rulings of regional circuit courts. In *RCA Corp. v. Data General Corp.*, 887 F.2d 1056 (Fed. Cir. 1989), the Federal Circuit reviewed a district court's denial of a claim for breach of contract damages resulting from the failure of the licensee to pay royalties owed under the contract following its purported notice to the licensor that it intended to challenge the licensed patent, which was ultimately held to be invalid. In affirming the lower court's ruling, the Federal Circuit provided the following view on the limits of the *Lear* decision:

RCA [the patent holder] appears to rely on *Lear* as mandating breach of contract damages where a licensee does not pay royalties. *Lear* simply does not address that issue. . . . *Lear* does not . . . dictate . . . what damages *must* be awarded for a breach, or under what circumstances, if any, a licensee can recover royalties paid. Those questions continue to be matters dependent on particular fact situations, contract provisions and state contract law, albeit they must be resolved in harmony with general principles discernible from *Lear*. See, e.g., . . . *Rite-Nail Pkg. Corp. v. Berryfast, Inc.*, 706 F.2d 933, . . . (9th Cir.1983); *Bristol Locknut Co. v. SPS Technologies, Inc.*, 677 F.2d 1277, . . . (9th Cir. 1982); *PPG Indus., Inc. v. Westwood Chem., Inc.*, 530 F.2d 700, . . . (6th Cir.), . . .

Id. at 1064. In *Go Medical Industries, Pty., Ltd. v. Inmed Corp.*, 471 F.3d 1264 (Fed. Cir. 2006), the Federal Circuit provided convincing evidence that its interpretation of the royalty payment prong of the *Lear* doctrine was consistent with those of the regional circuit courts discussed in this section that had opined on the matter. The issue on appeal in *Go Medical* was whether the district court was correct in its determination of the point in time at which the patent licensee in the case was relieved of its contractual obligation to pay royalties following a finding in a third party infringement suit that the patent-at-issue was invalid. Relying on its prerequisite statement from *Shell Oil*, the Federal Circuit concluded that the district court had erred in its application of the *Lear* doctrine, in that the lower court had prematurely relieved the licensee of its payment obligation while the patent invalidity finding was still pending appeal and the licensee had neither stated its reason for withholding its royalty payments nor filed its own declaratory judgment action challenging the validity of the licensed patent.

438. *PPG Indus., Inc.*, 530 F.2d at 706.

439. 677 F.2d 1277 (9th Cir. 1982).

Industries, Inc. v. Westwood Chemical, Inc., 530 F.2d 700, 701 (6th Cir.) . . . (1976); accord, *American Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890, 895–98 (3rd Cir.), . . . (1980).⁴⁴⁰

Echoing the position taken by the Sixth Circuit in *PPG*, the *Bristol Locknut* court concluded that “[e]ither method of giving adequate notice would fulfill the strong federal policy [articulated in *Lear*] of prompting an early adjudication of patent validity.”^{441, 442}

440. *Id.* at 1283 (footnote omitted).

441. *Id.* at 1283 n.7.

442. For additional regional circuit court cases addressing a licensee’s royalty payment obligation in the context of a patent validity challenge in the aftermath of *Lear*, see *Troxel Manufg. Co. v. Schwinn Bicycle Co.*, 465 F.2d 1253 (6th Cir. 1972) (Troxel I), *Troxel Manufg. Co. v. Schwinn Bicycle Co.*, 489 F.2d 968 (6th Cir. 1973) (Troxel II), *Atlas Chem. Indus., Inc.*, 509 F.2d 1, *Warner-Jenkinson Co.*, 567 F.2d 184, *St. Regis Paper Co.*, 552 F.2d 309 and *Precision Shooting Equip. Co.*, 646 F.2d 313. That the U.S. Supreme Court’s *Lear* decision was viewed principally as a call for the early adjudication of patent invalidity is underscored by the position taken by a number of regional circuit courts in post-*Lear* royalty refund cases. Two of the regional circuit courts (the Sixth and the Ninth) referenced by the Federal Circuit as supporting its *Shell Oil* prerequisite statement addressed the question of “whether a licensee can recover royalties on a patent paid before filing an action in which the patent was found to be invalid.” *St. Regis Paper Co.*, 552 F.2d at 313. In *St. Regis Paper*, the Ninth Circuit provided the following summary of the reasoning that it and the Sixth Circuit had relied on to conclude that no such royalty recovery by the licensee should be permitted:

The Sixth Circuit considered the *Lear* doctrine in light of the goals sought to be achieved and concluded that the federal policy which permits a licensee to assert invalidity of the underlying patent does not entitle the licensee to a refund of all royalties paid for the use of the invalid patent. See *Troxel Mfg. Co. v. Schwinn Bicycle Co.*, 465 F.2d 1253 (6th Cir. 1972) (Troxel I); The Sixth Circuit noted that the Supreme Court in *Lear* rejected the estoppel doctrine on the ground that it effectively “muzzled” licensees who might be the only individuals with sufficient economic incentive to challenge the patentability of an invention. As stated in *Lear*, . . . 395 U.S. at 668, . . . “federal law requires that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent.” This policy encourages full and free competition in the use of ideas which are in the public domain. *Lear*, therefore, is an inducement to an early adjudication of invalidity; but the Sixth Circuit cautioned that the possibility of a royalty refund might delay such a determination. The possibility of obtaining a refund of all royalties paid might induce a manufacturer to accept a license based on a patent of doubtful validity, derive the benefits of suppressed competition which the patent affords, and challenge validity only after the patent’s expiration. The licensee would have a chance to regain all the royalties paid while having enjoyed the fruits of the license agreement. Therefore, if a refund were permitted, licensees who were only recently unmuzzled by *Lear* would again be silenced by economic self-interest rather than by state law. We agree with the reasoning of the Sixth Circuit.

Id. at 314 (paragraphing omitted). An issue not addressed in *St. Regis Paper* and still unresolved is whether a nonrepudiating licensee in good standing that continues to pay royalties following its challenge of the licensed patent is entitled to a refund of those royalty payments. See *infra* note 498 for a discussion of this issue by the United States

It is noteworthy that in only one of the four regional circuit court cases referenced in the *Shell Oil* prerequisite statement was the licensee's patent validity challenge barred, and insight into the Federal Circuit's perspective on the patent challenge prong of the *Lear* doctrine may be found in the distinction between the facts of that case (*Hull*) and those of the other cited regional circuit court cases (*PPG*, *American Sterilizer* and *Rite Nail*). In each of *PPG*, *American Sterilizer* and *Rite Nail*, the patent licensee refused to make royalty payments due under the license agreement and took an affirmative step to encourage the early adjudication of the licensed patent's validity (either in the form of a declaratory judgment action or a notice to the patent holder challenging the patent). Moreover, in each of these cases the royalty payment obligation under consideration spanned a period that both preceded and followed the action by the licensee questioning the patent's validity that purportedly terminated the licensee's payment obligation. The issue regarding the licensee's post-challenge payment obligation made the patent's validity an essential element in the disposition of the case and justified the patent challenge permitted by the court. In *Hull*, however, the unpaid royalties sought by the patent holder all accrued prior to the licensee's patent challenge. The licensee in that case had ceased paying royalties due under a patent license agreement without indicating the reason and subsequently terminated the agreement in accordance with its terms. The patent holder was not informed that its former licensee questioned the validity of its patent until it received an answer to its complaint filed after the agreement had terminated. Based on these facts, the Tenth Circuit in *Hull* concluded that the validity of the patent had no bearing on the question before the court and, accordingly, the patent challenge was not allowed. As the *Hull* court explained,

Lear permits licensees to refuse to pay royalties on a patent they believe to be invalid and then to defend an action for royalties on the basis of patent invalidity. . . . [*Lear v. Adkins*, 395 U.S. 653, 673–674 (1969)]. Courts interpreting *Lear*, however, have focused on whether the suspension of royalty payments is connected to the challenge to the patent's validity. These cases hold that if licensees wish to preserve patent invalidity as a defense to litigation over unpaid

royalties, the licensees must notify the licensors that they are suspending payments because they question the validity of the patents. See *Bristol Locknut Co. v. SPS Technologies, Inc.*, 677 F.2d 1277, 1283 (9th Cir.1982); *American Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890, 895-98 (3d Cir.) . . . (1980); *PPG Industries, Inc. v. Westwood Chemical, Inc.*, 530 F.2d 700, 706 (6th Cir.) . . . (1976); We agree that this limitation best effectuates the policies enunciated in *Lear*.

One reason *Lear* permits licensees to suspend royalty payments prior to a final judicial determination of validity is to discourage licensors from delaying such a determination. The Court feared that if licensees were required to continue making royalty payments during the pendency of a validity challenge, licensors would be encouraged to stall a judicial determination as long as possible. See *Lear*, 395 U.S. at 673-74 If licensees are permitted to suspend royalty payments without notifying licensors that the reason for the suspension is to question the validity of the patents, they will be subject to a similar temptation to forestall validity litigation The longer they could . . . [stall] validity litigation, the greater the amount of royalties they could avoid while still enjoying the monopoly benefits conferred by the license. Permitting licensees to avoid royalties that they suspended for reasons other than to challenge validity would give the licensees "additional economic incentive to devise every conceivable dilatory tactic in an effort to postpone the day of final judicial reckoning." *Id.* at 673 Limiting the royalties licensees can avoid to those accruing after the licensees effectively notify the licensors that they question the validity of the licensed patents prevents the rule in *Lear* from being used to frustrate the policies enunciated there.⁴⁴³

By delaying the challenge of the licensed patent, the licensee in *Hull* failed to advance the public interest, as articulated in *Lear*, in the early adjudication of patent invalidity, and for that reason the Tenth Circuit concluded that "the trial court properly ruled that invalidity could not be a defense to the payment of royalties at issue in this case."^{444, 445} The holding in *Hull* can also be viewed as a

443. *Hull*, 704 F.2d at 1203-04.

444. *Id.* at 1204.

variation of the relevance rule of *Rooklidge*, discussed above in this Part III.⁴⁴⁶ The patent validity challenge in *Hull* was barred, not on the basis of a formalistic application of the doctrine of licensee estoppel which the *Lear* Court had rejected, but because the challenge was not relevant to the specific royalty payment issue before the court. However, unlike the relevance rule of *Rooklidge*, which held that the validity of a licensed patent is irrelevant to the obligation of a patent licensee to pay royalties that accrued over the period during which the licensee enjoyed the benefits of the patent pursuant to the license agreement, this variant of the relevance rule looks to the point at which the licensee takes an affirmative step to encourage the challenge of the licensed patent as the cut-off for the royalty payment obligation, irrespective of whether the licensee continues to enjoy a benefit under the license following such step.

One way, then, to reconcile the Federal Circuit's *Shell Oil* opinion with the *Lear* decision is to conclude that a patent validity challenge can be brought by a licensee if the validity of the patent is relevant to the issue to be resolved between the licensee and the patent holder. In *Hull*, the Tenth Circuit concluded that the validity of the licensed patent was not relevant to the single issue before the court, namely the obligation of the licensee to pay pre-challenge royalties and, accordingly, the patent challenge was not allowed. Whereas, in the other regional circuit court cases cited in *Shell Oil* (i.e., *PPG*, *American Sterilizer* and *Rite Nail*), as well as in the *Shell Oil* case itself, the resolution of at least one issue under consideration by the court was dependent on the validity of the patent (i.e., the licensee's obligation to make post-challenge payments) and the patent challenge was permitted. Whether this interpretation of patent challenge jurisprudence is reflective of the thinking of the Federal Circuit when it handed down its opinion in *Shell Oil* is open to question.

The problem with this interpretation of the *Shell Oil* opinion, based on a review of the cited regional circuit court cases, is that it does not support the broad reading of the *Shell Oil* prerequisite statement that holds that, in all circumstances, a licensee must stop paying royalties owed under its license agreement before it can

445. There is an important distinction between the facts in *Hull* and those in *Shell Oil*. Whereas in both cases the patent challenge followed the termination of the applicable license agreement, only in *Hull* was the payment obligation under consideration limited to a period prior to the patent challenge. In *Shell Oil*, *Shell's* obligation to make payments for its continued use of the patented technology following its patent challenge was also at issue in the case, making the validity of the patent "relevant."

446. See *supra* section III.A.4.; *supra* notes 136 and 137.

challenge the licensed patent. In particular, the interpretation does not explain why a patent licensee that hopes to avoid future royalty payments for rights under a licensed patent that it believes to be invalid without risking the loss of those rights, such as the licensee in *MedImmune*, cannot seek a declaratory judgment of invalidity while continuing to meet its contractual payment obligations. Unlike the circumstances in *Hull* and similar to the circumstances in *PPG*, *American Sterilizer* and *Rite Nail*, in the *MedImmune* scenario the validity of the patent under consideration is relevant to an issue before the court (i.e., the licensee's post-challenge payment obligation) and, accordingly, the licensee's patent challenge should be permitted.

This specific issue was considered in two earlier regional circuit cases that the Federal Circuit failed to address in its *Shell Oil* opinion. In both *Warner-Jenkinson Co. v. Allied Chemical Corp.*⁴⁴⁷ and *Precision Shooting Equipment Co. v. Allen*,⁴⁴⁸ the regional circuit court hearing the case on appeal permitted a patent licensee to bring a declaratory judgment action challenging the validity of the licensed patent while continuing to enjoy its benefit under the license agreement by paying post-challenge royalties.⁴⁴⁹ The Second Circuit in *Warner-Jenkinson* provided the following argument against the need to withhold royalties prior to a patent validity challenge by a licensee:

Addressing the question whether a patent licensee must actually withhold royalty payments before he can challenge validity, we conclude—as have most courts who have

447. 567 F.2d 184. The Federal Circuit did cite the *Warner-Jenkinson* case in its *Shell Oil* decision, but not in reference to its articulation in *Shell Oil* of the prerequisite statement. The *Shell Oil* court relied on the *Warner-Jenkinson* holding as support for its argument that it would be unjust to permit Shell to reap the benefits of its license agreement with SGK while avoiding its contractual obligation to pay royalties during the period that preceded its patent validity challenge. 112 F.3d at 1568.

448. 646 F.2d 313.

449. The holdings in the *Warner-Jenkinson* and *Precision Shooting* decisions differ in that in the former the Second Circuit required that royalty payments be made to the licensor directly while in the latter the Seventh Circuit permitted the royalties to be paid into the court's escrow account. This difference, which is not relevant to the point being made in this paragraph, does not reflect a conflict between the circuits in that the Second Circuit in *Warner-Jenkinson* had ruled that payments could be made into an escrow account where there is an indication that the licensor might be judgment-proof at the conclusion of the litigation, and the Seventh Circuit in the *Precision Shooting* case had concluded that if the licensee were to make payments directly to the licensor, the licensee "would have no adequate remedy at law to recoup the post-challenge royalties." 646 F.2d at 321.

considered the issue—that such repudiation of the licensing agreement should not be precondition to suit. . . . Under most licensing arrangements, as in the present case, withholding of royalty payments constitutes a material breach of the contract. A licensee who wishes to continue using the patented element cannot withhold royalty payments without laying himself open to large potential liability for infringement and an injunction against all future use of the patented substance. If forced to make the hard choice, many licensees will choose the less perilous course, and the patents under which they are licensed will remain uncontested. *Lear* established that removing restraints on commerce caused by improperly-held patents should be considered more important than enforcing promises between contracting parties. Thus, the seeming inequity of allowing a licensee to keep his license while he attacks the validity of the licensor's patent is outweighed by the public interest in placing no impediment in the way of those in the best position to contest the validity of the underlying patent.⁴⁵⁰

It is unclear as to why the Federal Circuit in *Shell Oil*, when it articulated its prerequisite statement, neglected to address the argument offered by the Second Circuit in *Warner-Jenkinson* against the need to withhold royalties prior to a licensee patent validity challenge. However, as noted above, the U.S. Supreme Court in *MedImmune* refused to opine on the merits of the Federal Circuit's *Shell Oil* prerequisite statement. Accordingly, the prerequisite statement is binding on the lower federal courts and must be taken into account by these courts when relevant to a matter under consideration. As will be discussed in section III.C.4.c.iv. below, this is precisely what happened in *MedImmune* on remand to the District Court for the Central District of California, where the court acknowledged that the Federal Circuit's *Shell Oil* prerequisite statement is controlling law but the *Shell Oil* holding was distinguishable on the basis of the peculiar facts in that case.⁴⁵¹

The *Shell Oil* decision remains a source of uncertainty regarding the scope of the right of a licensee to challenge the validity of a licensed patent. The impact of that uncertainty was diminished, however, with the subsequent introduction by the Federal Circuit in

450. 567 F.2d at 187–88 (citations omitted).

451. *MedImmune, Inc.*, 535 F. Supp. 2d 1000.

*Gen-Probe Inc. v. Vysis, Inc.*⁴⁵² of an additional barrier to a licensee patent validity challenge, one that was jurisdictional in nature. In that case, Gen-Probe took a license to practice the Vysis' patent as part of a settlement of an unrelated litigation. Gen-Probe then filed a declaratory judgment lawsuit alleging that the Vysis patent was invalid and that the Gen-Probe product did not infringe any claims of the patent. Gen-Probe, however, remained a nonrepudiating licensee in good standing by continuing to pay the royalties due under the license agreement, albeit under protest, and by complying with its other contractual obligations. The district court in the case ruled in favor of Gen-Probe, holding that the patent-at-issue was invalid. On appeal, the Federal Circuit vacated the district court's judgment in favor of the declaratory judgment plaintiff for lack of jurisdiction to hear the merits of the case in the absence of an actual controversy between the parties.

The Federal Circuit's holding in *Gen-Probe* formed the basis for its ruling in *MedImmune v. Genentech*⁴⁵³ and, as noted in Part II of this Article, was overruled by the U.S. Supreme Court in the latter case. Having already reviewed the jurisdictional arguments relied on by the Federal Circuit in *Gen-Probe* and rejected by the U.S. Supreme Court in *MedImmune*, we need not restate them here. The Federal Circuit's *Gen-Probe* opinion remains instructive, however, in that it may still reflect the Federal Circuit's views on the scope of the U.S. Supreme Court's *Lear* decision. In distinguishing the *Lear* decision, the Federal Circuit in *Gen-Probe* provided the following assessment:

The district court also relied on *Lear, Inc. v. Adkins*, 395 U.S. 653, 89 S.Ct. 1902, 23 L.Ed.2d 610 (1969), wherein the Supreme Court explained that a license does not alone bar the licensee from challenging the validity of a patent. *See, e.g., Flex-Foot, Inc. v. CRP, Inc.*, 238 F.3d 1362, 1368 (Fed. Cir.2001). The *Lear* doctrine, however, does not grant every licensee in every circumstance the right to challenge the validity of the licensed patent. In several instances, this court has declined to apply the *Lear* doctrine. *Id.* at 1368-70; *Studiengesellschaft Kohle m.b.H. v. Shell Oil Co.*, 112 F.3d 1561, 1567-68 (Fed. Cir.1997); *Foster v. Hallco Mfg. Co.*, 947 F.2d 469, 476-77 (Fed. Cir.1991); . . . *Hemstreet v. Spiegel, Inc.*, 851 F.2d 348, 350-51 (Fed. Cir.1988); *Diamond Scientific Co. v. Ambico, Inc.*, 848 F.2d

452. 359 F.3d 1376 (overruled in part by *MedImmune, Inc.*, 549 U.S. 118).

453. 427 F.3d 958.

1220, 1224–25 (Fed. Cir.1988). Among these clarifications of the *Lear* principle, *Shell Oil* is particularly relevant, though not factually identical, to this case. In *Shell Oil*, this court decided that a licensee is liable for unpaid royalties that accrued under the terms of the license before invalidation of the subject patent's claims. While that case did not discuss jurisdiction under the Declaratory Judgment Act, this court stated: "[A] licensee . . . cannot invoke the protection of the *Lear* doctrine until it (i) actually ceases payment of royalties, and (ii) provides notice to the licensor that the reason for ceasing payment of royalties is because it has deemed the relevant claims to be invalid." *Shell Oil*, 112 F.3d at 1568. This language posits that a licensee must, at a minimum, stop paying royalties (and thereby materially breach the agreement) before bringing suit to challenge the validity or scope of the licensed patent.⁴⁵⁴

With the elimination in *MedImmune* of the *Gen-Probe* jurisdictional barrier to a licensee patent validity challenge, the uncertainty generated by the Federal Circuit's *Shell Oil* opinion (which the U.S. Supreme Court has yet to rule on) assumes greater significance.

- **"Challenge-but-face-the-consequence" Decisions**

In *Gen-Probe*, Judge Radar interpreted his *Shell Oil* prerequisite statement as requiring a licensee to materially breach its license agreement by withholding royalty payments in order to bring a suit to challenge the validity of the licensed patent.⁴⁵⁵ As discussed in the preceding section, there is a question as to whether the Federal Circuit intended to have this challenge requirement apply in all circumstances. Judge Radar's comment is noteworthy for another reason, however, in that it highlights one of the central questions to be addressed in this Article, namely, is it consistent with the "spirit of *Lear*" to expose a licensee that brings a patent challenge in furtherance of the public's interest in eliminating worthless patents to the possibility of an unwanted consequence, e.g., the termination of its license agreement and its rights under the patent? Stated another way, does the U.S. Supreme Court's decision in *Lear*, which protects a patent licensee's right to challenge the licensed patent, require that the licensee be given *some* incentive to challenge or

454. 359 F.3d at 1381.

455. *Gen-Probe Inc.*, 359 F.3d at 1381.

every possible incentive? If the former is true, then the fact that a licensee faces the potential of a negative consequence in challenging a patent would not necessarily be inconsistent with the “spirit of *Lear*.” If the latter is true, however, a significant unwanted consequence resulting from a licensee’s patent challenge would be impermissible. In this section, we discuss a number of Federal Circuit holdings in which the court acknowledged that, in the event that a patent licensee materially breaches its license agreement in the exercise of its *Lear*-protected right to challenge the licensed patent, it could lose its rights under the patent license. While each of these “challenge-but-face-the-consequence” decisions preceded the U.S. Supreme Court’s decision in *MedImmune*, the *MedImmune* Court did not address the “incentive” issue, and the Federal Circuit’s holdings in these cases as they relate to this issue remain good law.

In *C.R. Bard, Inc. v. Schwartz*,⁴⁵⁶ a case that predated *Gen-Probe*, the Federal Circuit held that a patent licensee could meet the jurisdictional requirement to bring a declaratory judgment action to declare the licensed patent invalid while the license agreement was still in effect. At first glance, the holding in *Bard* would appear to conflict with the Federal Circuit’s subsequent holdings in *Gen-Probe* and *MedImmune*. However, as noted in *Gen-Probe*, the licensee in *Bard* was not a licensee in good standing.⁴⁵⁷ It had ceased paying royalties under the agreement to the licensor, enabling the licensor to terminate the agreement at any time and bring an infringement suit against the licensee. The *Bard* court concluded that, “[i]n light of the totality of the circumstances,” the licensee in the case had a reasonable apprehension of an infringement suit that qualified as a federal controversy required for jurisdiction.⁴⁵⁸

What is significant for purposes of this section is that the Federal Circuit’s jurisdictional argument in favor of the patent challenge was predicated on the ability of the licensor in *Bard* to terminate the license agreement as a result of the licensee’s having materially breached the agreement by bringing the challenge and withholding royalty payments. The license agreement in the case provided in pertinent part that “[i]n the event . . . [the licensee] asserts invalidity of any of the said Patents within the scope of this Agreement and refuses to pay royalties on account of such asserted

456. *C.R. Bard, Inc.*, 716 F.2d 874.

457. 359 F.3d at 1380.

458. *C.R. Bard, Inc.*, 716 F.2d 874.

invalidity, then GRANTOR may terminate this Agreement as to the Patent or Patents as to which invalidity is asserted.”⁴⁵⁹ While the licensor in *Bard* did not, in fact, terminate the license agreement, the court concluded that it could unilaterally do so “under the very terms of the agreement,”⁴⁶⁰ and the licensee had no ability to prevent the termination and a subsequent infringement suit.

The Federal Circuit did not consider the enforcement of the “termination-for-challenge-and-failure-to-pay-royalties” clause in the *Bard* license agreement as incompatible with the “spirit of *Lear*.” While the right of the licensee in *Bard* to bring the patent challenge was protected under *Lear*, the consequence of its challenge and its failure to pay the agreed-to royalties that created the controversy in the case necessary to meet the jurisdictional requirement put the licensee at risk for losing its rights under the agreement should the licensor elect to terminate it. This “challenge-but-face-the-consequence” ruling in *Bard* reflected the Federal Circuit’s view that the U.S. Supreme Court’s *Lear* holding did not require that a licensee be given *every possible incentive* to challenge the validity of a licensed patent, including relief from all related contractual obligations that would otherwise bind the licensee.

This view was also evident in the Federal Circuit’s subsequent decision in *Cordis Corp. v. Medtronic, Inc.*⁴⁶¹ That case involved an appeal of a district court’s order (1) permitting a licensee to deposit into an escrow account all future royalties due under a patent license agreement during the pendency of the licensee’s declaratory judgment action to invalidate the licensed patent, and (2) enjoining the licensor from terminating the license agreement based on the licensee’s failure to make royalty payments pursuant to the agreement, thereby protecting the licensee from a patent infringement counterclaim. In vacating the order of the district court, the Federal Circuit stated that “we find no authority in *Lear* for establishing an escrow account for royalties due *pendente lite* or preliminarily enjoining a licensor from cancelling the license agreement and, thus, from counterclaiming for patent infringement when this material breach of the license occurs.”⁴⁶² The court concluded that “[the] public policy statement [in *Lear*] does permit a licensee to cease payments due under a contract while challenging the validity of a patent. It *does not* permit the licensees to avoid

459. *Id.* at 881 n.5.

460. *Id.*

461. 780 F.2d 991.

462. *Id.* at 995.

facing the consequences that such an action would bring. The holding of *Lear* only prevents the affirmative enforcement by the licensor of the royalty payment provisions of the license agreement while the patent's validity is being challenged by the licensee."⁴⁶³ In adopting this "challenge-but-face-the-consequence" perspective, the Federal Circuit relied on the Second Circuit's reasoning in *Warner-Jenkinson*, a case in which a licensee challenging the licensed patent was prevented from paying royalties into an escrow account.⁴⁶⁴ Characterizing the *Warner-Jenkinson* reasoning as "in keeping with the holding of and policy statements in *Lear*,"⁴⁶⁵ the *Cordis* court offered the following excerpt from that Second Circuit case (where the licensees were the plaintiffs and the patent holder was the defendant):

We believe that if the plaintiffs wish to continue to invoke the protections of their licensing agreements, they should be required to continue paying their royalties to the defendant. Ultimately, all royalties paid after the filing of the complaint *may* have to be returned to the plaintiffs At present, plaintiffs already have the option of withholding royalties and thereby breaching the licensing agreement; of course, they would then run the risk of an injunction if they should lose on the merits. It would not be fair for the plaintiffs to be allowed simultaneously to reap all the benefits of the licensing agreement and to deprive the licensor of all his royalties. Patents are presumed to be valid . . . ; until invalidity is proven, the patentee should ordinarily be permitted to enjoy the fruits of his invention. The principal effect of an escrow arrangement would be to put undeserved pressure on the defendant.⁴⁶⁶

463. *Id.*

464. 567 F.2d 184; *see also* this section III.C.4.c.iii. (Licensee Patent Validity Challenges; Prerequisites and Jurisdictional Barriers).

465. *Cordis*, 780 F.2d at 995.

466. *Id.* (quoting from *Warner-Jenkinson*, 567 F.2d at 188–89, with emphasis added by the Federal Circuit in *Cordis*). *See also Nebraska Engineering Corp.*, 557 F.2d 1257, a decision favorably cited by the Federal Circuit in *Cordis* for its reliance on the reasoning set forth in *Warner-Jenkinson* ("*Lear* prevents only the affirmative enforcement of royalty payment provisions in license agreements against licensees engaged in patent validity challenges. Thus, . . . [the licensee] was free to cease paying royalties. Nothing in *Lear*, however, precludes defendant [licensor] from treating such nonpayment as grounds for termination under the agreement. Unless . . . [the licensee] is willing to forego the safety of the license agreement, it should continue to comply with the agreement's provisions." 557 F.2d at 1259–60).

In addition to serving as another example of the Federal Circuit's willingness to limit the scope of the *Lear* holding by subjecting a challenging licensee to an unwanted consequence, the *Cordis* decision is noteworthy for two other reasons. First, in contrast to the *Bard* case, the Federal Circuit in *Cordis* considered the withholding of agreed-to royalties by a patent licensee to be a material breach of the license agreement that provided the licensor with a right of termination, even in the absence of an express provision in the contract addressing that circumstance. Second, and more importantly, by concluding that the licensee in *Cordis* was required to pay royalties directly to the licensor if the former intended to maintain its benefits under the license agreement during the pendency of its patent challenge, the Federal Circuit implicitly sanctioned a declaratory judgment action seeking patent invalidity by a licensee in good standing that had neither complied with the dictates of the *Shell Oil* prerequisite statement nor met the jurisdictional requirement to challenge recognized in *Gen-Probe*. The Federal Circuit's *Cordis* decision is consistent with the view that a licensee may challenge the validity of a licensed patent whether or not it stops paying royalties to the licensor, but the licensee cannot avoid the risk of agreement termination by the licensor for material breach if it pays the royalties into an escrow account and not to the licensor. Interpreted in that way, the *Cordis* decision closely tracks that of the Second Circuit in *Warner-Jenkinson*, a case that was applauded in *Cordis*, but largely ignored in *Shell Oil* and not addressed in *Gen-Probe*. This apparent inconsistency in the Federal Circuit's rulings presents some difficulty in defining the position of that circuit with respect to the scope of *Lear*. However, looking at the more recent rulings of the Federal Circuit (*Shell Oil* and *Gen-Probe*) it would appear that, in the years leading up to the U.S. Supreme Court's decision in *MedImmune*, the Federal Circuit had solidified its stance against a broad reading of the *Lear* holding (that would permit a licensee in good standing to challenge a licensed patent) and took increasingly aggressive positions in limiting that holding when presented with the opportunity.

In *Dow Chemical Co. v. United States*,⁴⁶⁷ the last case to be discussed in this section, the Federal Circuit again ruled that a licensee that challenged the validity of the licensed patent risks

467. 226 F.3d 1334.

losing its rights under the patent if it fails to meet its contractual obligation to make royalty payments. The patentee/licensor in the case, Dow, commenced a suit against its licensee, the U.S. Government, for damages for the government's failure to pay royalties allegedly due under a patent license agreement. In the alternative, Dow sought reasonable royalties for the government's infringement of the licensed patent, having previously notified the government that it was terminating the license on the basis of the government's contractual breach in failing to pay royalties. The Court of Federal Claims "held that the . . . patent was not invalid and was infringed by the government" and "that the government's non-payment of royalties and repudiation of the license constituted a material breach that warranted voiding the contract *ab initio*."⁴⁶⁸ On appeal, the government challenged the court's holding that the patent-in-suit was valid and infringed and that the license was void *ab initio*.

The government's ability (as a licensee) to challenge the validity of the licensed patent was not at issue in this case. Even if the government were to prevail in its claim that the license agreement had not been properly terminated by Dow, the government had both withheld royalties allegedly owed under the agreement and had informed Dow of its doubts as to the validity of the licensed patent prior to its challenge, satisfying the requirements established in *Shell Oil*. Regarding the judgment that the license was void, the Federal Circuit concluded that although the patent license agreement was not rendered void *ab initio* by the actions of the government, Dow had the right to terminate the agreement, despite the absence of an express termination provision. The court first dismissed the lower court's ruling that because the government had never performed under the license agreement and had indicated to Dow that that was its intention, the termination of the agreement by Dow had *ab initio* effect, constituting a rescission that voided the contract from its inception. The Federal Circuit argued that "[b]ecause rescission is essentially an equitable remedy, it will not ordinarily be invoked where money damages—in this case damages for breach of contract—will adequately compensate a party to the contract . . . [and] [n]either Dow nor the Court of Federal Claims has pointed to any reason why contract damages for breach are not adequate here."⁴⁶⁹ The Federal Circuit then

468. *Id.* at 1337.

469. *Id.* at 1345–46.

addressed the government's claim that the license agreement could not be properly terminated by Dow in the absence of an express provision permitting such termination for nonpayment of royalties. It argued that a material breach or repudiation of an agreement gives rise to a right of termination. In the instant case, "[t]he government's challenge to the validity of the patent and the viability of the license, together with the refusal to pay any royalties, made the absence of a termination clause in the license immaterial . . . [and] . . . a termination right is properly implied."⁴⁷⁰

Interestingly, by the time the Federal Circuit rendered its decision in *Dow* (seventeen years after *Bard*, fifteen years after *Cordis* and three years after *Shell Oil*), any concern on the part of the court that permitting a licensor to terminate its license agreement based on a patent-challenging licensee's refusal to pay agreed-to royalties would violate the "spirit of *Lear*" was so significantly diminished that the *Dow* court addressed this issue in a lone footnote. In responding to the government's argument that its license agreement had been improperly terminated by *Dow*, the Federal Circuit offered the following succinct analysis:

In support of its argument the government cites the public policy arguments in *Lear, Inc. v. Adkins*, 395 U.S. 653 . . . (1969). The Court of Federal Claims noted that *Lear* does allow a licensee to cease payments due under a license while challenging the validity of a patent, but that it does not permit the licensee to avoid the consequences that such actions would bring. See *Dow II* [*Dow Chemical Co. v. United States*, 32 Fed. Cl. 11 (1994)] at 16 (citing *Cordis Corp. v. Medtronic, Inc.*, 780 F.2d 991, 995 . . . (Fed. Cir.1985)). The court concluded that the policy rationale of *Lear* does not prevent Dow from terminating the license agreement. In *RCA Corp. v. Data Gen. Corp.*, 887 F.2d 1056, 1064 . . . (Fed.Cir.1989), this court stated that "*Lear* does not . . . deal with a licensor's right to terminate or rescind a license agreement . . ." We therefore reject the government's contention as to the applicability of *Lear* to this case.⁴⁷¹

In sum, each of the three cases discussed in this section (*Bard*, *Cordis* and *Dow*) demonstrates a willingness on the part of the Federal Circuit to limit the applicability of the U.S. Supreme Court's

470. *Id.* at 1346.

471. *Id.* at 1344 n.11.

Lear decision and to hold a licensee that challenges the validity of a licensed patent accountable for a contractual breach related to the challenge.⁴⁷² In taking that position, the Federal Circuit adopted a narrow interpretation of the meaning of the “spirit of *Lear*” that was limited by the facts in *Lear* and the actual language of the opinion in the case, with little extrapolation. The Federal Circuit’s reference in *Dow* to its prior holding in *RCA Corp.* is instructive in this regard. The *Dow* court accurately quoted from *RCA Corp.* in noting that “*Lear* does not . . . deal with a licensor’s right to terminate or rescind a license agreement.”⁴⁷³ However, the Federal Circuit in *Dow* neglected to complete the thought expressed in *RCA Corp.* The sentence in the *RCA Corp.* opinion that followed the above-quoted language made the point that the question of whether a licensor had a right to terminate or rescind a license agreement in the aftermath of *Lear* “continue[s] to be [a] matter . . . dependent on particular fact situations, contract provisions and state contract law, albeit . . . [it] must be resolved in harmony with general principles discernible from *Lear*.”⁴⁷⁴

Restated in more general terms, the Federal Circuit in *RCA Corp.* was expressing the view that, with respect to an issue as to which the *Lear* opinion was silent, a court addressing that issue had the latitude to determine the applicability of the *Lear* holding, based

472. Another case that has been cited as an example of the willingness of the Federal Circuit to limit the applicability of *Lear* and bind a party that challenges the validity of a patent to its contractual obligations is *Sun Studs, Inc.*, 872 F.2d 978, *overruled on other grounds* by *A.C. Aukerman Co. v. R.L. Chaides Construction Co.*, 960 F.2d 1020 (Fed. Cir. 1992). See references to this case in *Studiengesellschaft Kohle*, 112 F.3d at 1567 and *Gen-Probe Inc.*, 359 F.3d at 1381. In *Sun Studs*, the Federal Circuit permitted a patent validity challenge by an assignor (not licensee) of a patent, but held the challenger liable for the consequences of the contractual breach caused by the challenge. In essence, the court in this case concluded that (1) the assignor’s contractual obligation to protect, defend and enforce the assigned patents (which the district court viewed as an agreement not to contest the assigned patents’ validity) was not against the public policy expressed in *Lear*, (2) the assignor was not estopped, however, under the doctrine of assignor estoppel from challenging the validity of the assigned patents (which doctrine, according to the court in *Diamond*, is not applied automatically but only when a balancing of the equities in a particular case justifies its application), and (3) nonetheless, the challenge by the assignor constituted a material breach of its contractual obligation to protect, defend and enforce the assigned patents and, accordingly, such breach relieved the assignee (under the relevant state law) of its contractual obligation to pay royalties to the assignor. In *Sun Studs*, then, the Federal Circuit provided yet another example of a “challenge-but-face-the-consequence” decision.

473. *Dow Chem. Co.*, 226 F.3d at 1344 n.11 (quoting *RCA Corp. v. Data Gen. Corp.*, 887 F.2d 1056, 1064 (Fed. Cir. 1989)).

474. 887 F.2d at 1064, citing, *inter alia*, the Federal Circuit’s *Cordis* decision. For a further discussion of *RCA Corp.*, see *supra* note 437.

on a consideration of the facts in the case, the dictates of any applicable state contract law and the “general principles discernable from *Lear*.” As evidenced by the holdings in *Bard*, *Cordis* and *Dow*, the Federal Circuit had determined that permitting a patent licensor to terminate its license agreement with a patent-challenging licensee that had failed to comply with its contractual obligation to pay royalties was compatible with the public policy rationale underlying *Lear* of encouraging early adjudication of patent invalidity. In keeping with its reputation for being protective of the rights of a patent holder, the Federal Circuit had concluded in these cases that “the ‘spirit of *Lear*’ cannot logically demand that any and all rules of contract law . . . be ignored to give licensees every possible incentive to challenge patent validity.”⁴⁷⁵

iv. *MedImmune* Revisited

As noted in Part II of this Article, the U.S. Supreme Court in *MedImmune* did not rule on the merits of the contract-based arguments against a patent validity challenge by a nonrepudiating licensee in good standing. In particular, the *MedImmune* Court failed to resolve the question of whether the Supreme Court’s prior holding in *Lear*, abrogating the doctrine of licensee estoppel, extends to a nonrepudiating licensee or whether the *Shell Oil* prerequisite statement is inconsistent with that holding. These questions were addressed, however, by the U.S. District Court for the Central District of California in its decision in *MedImmune* on remand of the case by the Supreme Court.⁴⁷⁶ After an analysis of the relevant case law, the district court in *MedImmune* concluded that (1) the Federal Circuit’s holding in *Shell Oil* was limited to the unusual facts in that case and was, therefore, inapposite to the instant case, and (2) the *Lear* Court’s abrogation of licensee estoppel applied to the dispute under consideration, protecting the right of *MedImmune*, a nonrepudiating licensee in good standing, to challenge the validity of the Genentech patent-at-issue. In this section of the Article, we review the arguments of the *MedImmune* district court in support of its conclusions in the case.

In the interval between the Supreme Court’s ruling in *MedImmune* and the district court’s hearing of the case on remand, *MedImmune* had stipulated that, but for its license agreement with Genentech, the production of its Synagis product would infringe

475. McCarthy, (*Part II*), *supra* note 321 at 568.

476. *MedImmune, Inc.*, 535 F. Supp.2d 1000.

one (but only one) of the claims (Claim 33) of the Genentech patent under consideration in the case (the '415 Patent). In response, Genentech had filed "an unconditional, irrevocable covenant not to sue [for infringement] or seek royalties (from MedImmune) with respect to Synagis on any Claim of the '415 Patent other than Claim 33."⁴⁷⁷ On the basis of analyses not relevant to our discussion here, the district court concluded that the Genentech covenant not to sue for infringement had extinguished subject matter jurisdiction as to all of the claims of the '415 Patent except Claim 33. With respect to that claim, however, an actual case or controversy adequate to support a declaratory judgment claim of invalidity existed. There remained, therefore, the need for the district court to address Genentech's argument that, as a nonrepudiating licensee in good standing, MedImmune was barred from challenging the validity of Claim 33 by the doctrine of licensee estoppel.

The district court summarized the Genentech position as follows:

Genentech asserts that licensee estoppel bars MedImmune's patent invalidity claim because MedImmune has not repudiated the contract. It argues that the 1969 Supreme Court decision in *Lear v. Adkins*, 395 U.S. 653 . . . (1969), which "resolved the issue of licensee estoppel by writing its obituary," *Diamond Scientific Co. v. Ambico, Inc.*, 848 F.2d 1220, 1223 (Fed.Cir.1988), should be distinguished on the grounds that MedImmune is a *nonrepudiating* licensee. Genentech buttresses this argument by explaining that recent courts, including the Federal Circuit, have declined to extend *Lear*. Moreover, it notes that the Federal Circuit in *Studiengesellschaft Kohle v. Shell Oil Co.*, 112 F.3d 1561 (Fed.Cir.1997) ("*Kohle*"), expressly imposes a repudiation requirement on the invocation of *Lear*. Because that requirement has not been met, Genentech reasons, MedImmune is estopped from challenging patent validity. . . .⁴⁷⁸

The MedImmune response was "that *Lear* does apply because its fundamental holding was broad enough to cover nonrepudiating licensees, and *Kohle* [v. *Shell Oil*] is inapplicable because of the narrow question in front of the Federal Circuit in that case."⁴⁷⁹

477. *Id.* at 1003.

478. *Id.* at 1012.

479. *Id.* at 1012-13.

The district court began its analysis of the patent challenge question in *MedImmune* by summarizing the Supreme Court's *Lear* decision, which it described as the "definitive statement on licensee estoppel doctrine."⁴⁸⁰ The district court then turned to a brief review of selected post-*Lear* regional circuit and district court cases that preceded the establishment of the Federal Circuit. It cited *Massillon*,⁴⁸¹ *Panther Pumps*,⁴⁸² *Atlas Chemical Industries*,⁴⁸³ *Beckman Instruments*,⁴⁸⁴ *American Sterilizer*,⁴⁸⁵ and *Timely Products*⁴⁸⁶ as cases that "if nothing else, indicate that courts applied the policy rationale behind *Lear*, [rather than a reliance on its specific holding,] to other factual scenarios where patent invalidity was raised in an agreement between licensor and licensee."⁴⁸⁷ The district court next addressed the Federal Circuit's treatment of the *Lear* decision. It concluded that, while the Federal Circuit had initially endorsed the policies behind the *Lear* holding (citing *Bard* and *Cordis*), that court had "[m]ore recently . . . distinguished *Lear* in several instances"⁴⁸⁸ (citing *Diamond Scientific*, *Hemstreet*, *Foster* and *Flex-Foot*). The Federal Circuit's decision in *Shell Oil* was reviewed in some detail by the *MedImmune* district court, which described the *Shell Oil* case as noteworthy for the unusual facts that it presented for consideration.

The district court ended its review of the relevant case law by noting that the Supreme Court provided "little doctrinal guidance"⁴⁸⁹ in its *MedImmune* decision regarding the right of a nonrepudiating licensee in good standing to challenge the validity of the licensed patent. As the district court explained,

[the Supreme Court] . . . stated only that *Lear* certainly applied to *repudiating* licensees, but "expressed no opinion on whether a nonrepudiating licensee is similarly relieved of its contract obligation during a successful challenge to a patent's validity-

480. *Id.* at 1013.

481. *Massillon-Cleveland-Akron Sign Co.*, 444 F.2d 425; see *supra* section III.C.4.c.ii. & notes 332 & 333.

482. 468 F.2d 225; see *infra* section IV.B.1 and *supra* note 332.

483. 509 F.2d 1; see *supra* notes 334, 336 and 442.

484. 433 F.2d 55; see *supra* note 337.

485. 526 F.2d 542; see *supra* note 334.

486. 465 F. Supp. 91; see *supra* note 372.

487. 535 F. Supp. 2d at 1014.

488. *Id.*

489. *Id.* at 1016.

that is, on the applicability of licensee estoppel under these circumstances." . . . [549 U.S. 118, 124 (2007)]. The Court cited the two-prong rule provided by the Federal Circuit in *Kohle* [v. *Shell Oil*] but did not address whether that rule was consistent with *Lear*, or whether that rule was inapplicable to the present scenario.^{490, 491}

In the absence of the necessary guidance from the Supreme Court, the *MedImmune* district court was required to provide its own assessment of the case law relevant to a patent validity challenge by a nonrepudiating licensee, recognizing its obligation to consider binding Federal Circuit precedent. It first argued in support of its conclusion that the Federal Circuit's *Shell Oil* decision "Does Not Prohibit MedImmune's Invocation of *Lear* Because It Dealt With a Significantly Different Factual Scenario."⁴⁹² According to the district court, while the language of *Shell Oil* appeared to prevent MedImmune's reliance on the protection of the *Lear* doctrine because it had failed to cease paying royalties as required by the first prong of the prerequisite statement, "that language taken out of context extends the holding far beyond the rest of the case."⁴⁹³ The *MedImmune* district court viewed the *Shell Oil* holding as addressing "whether Shell could be held liable for past-due royalties where [the] patent was later held invalid, in light of the fact that Shell had delayed adjudication of validity by clandestinely continuing to operate under the agreement."⁴⁹⁴ Narrowly interpreted in that way, two key distinctions between the factual scenario in *Shell Oil* and that in *MedImmune* justified the district court's conclusion that the *Shell Oil* holding was inapposite to the instant case. First, unlike Shell that had delayed a timely challenge to the validity of the licensed patent, MedImmune had affirmatively sought a declaratory judgment that the patent-at-issue was invalid. Viewed from that prospective, Shell's actions frustrated the *Lear* policy of early adjudication of patent invalidity while MedImmune's actions

490. *Id.* (footnote omitted).

491. The district court in *MedImmune* did note that the Supreme Court, in its prior opinion in the case, expressed skepticism as to the strength of the contract-based argument against a patent challenge by a nonrepudiating licensee. However, as discussed in Part II of this Article, the Supreme Court did not rule on this matter, as such a ruling would be a decision on the merits of the argument, which the Court was not required to make in order to resolve the jurisdictional issue before it in *MedImmune*.

492. 535 F. Supp. 2d at 1016.

493. *Id.* at 1016-17.

494. *Id.* at 1017 (emphasis added).

furthered that policy. The district court acknowledged that, as in *Shell Oil*, “MedImmune continues to benefit in some ways by retaining the protection of the license.”⁴⁹⁵ But the court emphasized that, unlike in *Shell Oil*, “MedImmune is not ‘depriving the public of the full and free use of the patented product by withholding a successful challenge to validity.’”⁴⁹⁶ This critical difference between *Shell Oil* and *MedImmune* led the district court to conclude that “[a] party can ‘challenge’ the validity of a patent [in a manner consistent with the *Lear* public policy rationale] by ceasing payment of royalties and notifying the licensor of its beliefs, or by affirmatively seeking declaratory judgment that the patent is invalid, as MedImmune has done here.”⁴⁹⁷

The second key distinction, in the opinion of the district court, was that the only royalties at issue in *MedImmune* were those that were owed on a “going forward” basis.⁴⁹⁸ In contrast, in *Shell Oil* and other cases that had relied on the *Shell Oil* prerequisite statement, e.g., *Revson v. Claire’s Stores, Inc.*⁴⁹⁹ and *Advanced Card Technologies LLC v. Versatile Card Technology, Inc.*,⁵⁰⁰ past-due royalties were at stake. And it was not simply past-due royalties, but royalties that had accrued prior to the licensee’s challenge of the

495. *Id.*

496. *Id.* quoting from *Pony Pal*, 2006 WL 846354, at *3, 2006 U.S. Dist. LEXIS 14962 at *8.

497. *Id.*

498. *Id.* at 1010 n.7 (“At oral argument, MedImmune stated that it may seek restitution if the patent is invalidated, but emphasized that ‘the highlight if [sic] [its] claim is that [it does not] owe any money *going forward*.’ See Jan. 14 Hearing Tr. 52:16-52:17 (emphasis added).”). It is noteworthy in this regard that the *MedImmune* district court declined to opine on whether MedImmune was entitled to recover royalties paid during the pendency of its patent challenge in the event that the Genentech patent-at-issue was ultimately held to be invalid or, more generally, on the point in time at which a licensee is relieved of its contractual royalty payment obligation in the event of a successful patent challenge. (“The Court expressly declines to reach the issue of whether MedImmune can recover *back* royalties (i.e. royalties already paid) if the patent is deemed invalid. As noted earlier, the Court also declines to address at this point whether MedImmune is immediately relieved of its contract obligation upon that event.” 535 F. Supp. 2d 1000, 1018 (C.D. California 2008)). The district court justified its decision to avoid these issues on the grounds that (1) any ruling would be advisory in that the Genentech patent had not been invalidated, and (2) the only question that the district court was required to answer in deciding the case before it was whether MedImmune’s royalty payment obligation was impacted by the validity of the Genentech patent (which the court had determined it was) and not the question of at what point in time is a licensee that successfully challenges the licensed patent relieved of its royalty payment obligation or whether it is entitled to restitution for royalties already paid.

499. 120 F. Supp. 2d 322; *see supra* note 431.

500. 410 F. Supp. 2d 158; *see supra* note 431.

licensed patent. While not explicitly stated in its opinion, the argument of the *MedImmune* district court appears to be that a patent licensee can invoke the protection of the *Lear* doctrine (i.e., the right to challenge the validity of the licensed patent and to obtain relief from its royalty payment obligations), only if and when it takes an affirmative step encouraging the challenge of the licensed patent, either through the cessation of royalty payments on the grounds of alleged patent invalidity or through a judicial action contesting the patent's validity.⁵⁰¹ Accordingly, a licensee cannot assert patent invalidity as a defense to a claim for royalties owed prior to an affirmative step by the licensee toward challenging the licensed patent and, if only those royalties are at issue in the case, the court can bar the licensee's patent challenge altogether. This argument has elements of the one that we presented above in our discussion of the *Hull* case. There we concluded that the patent validity challenge in *Hull* was barred because the licensed patent's validity was not "relevant" to the licensor's claim for pre-challenge royalties, where relevance was determined, not on the basis of any benefit received by the licensee under the license agreement, but by the public's interest in encouraging the early adjudication of patent invalidity, as expressed in *Lear*.

In sum, the district court in *MedImmune* rejected the view that the Federal Circuit's decision in *Shell Oil* created a broad exception to *Lear*. Rather, it interpreted the *Shell Oil* holding as standing for the proposition that a licensee that acts to delay a timely challenge to the validity of the licensed patent, and thereby frustrates the important federal policy of eliminating worthless patents, cannot invoke the protection of the *Lear* doctrine. *MedImmune*, with its declaratory judgment action seeking a timely adjudication of patent

501. Our conclusion regarding the district court's argument is based on that court's discussion of the first key distinction between *Shell Oil* and *MedImmune* and the excerpts from *Revson* and *Advanced Card Technologies* that the court had elected to include in its *MedImmune* opinion ("The *Kohle* [v. *Shell Oil*] case and other courts that have applied its rule relate to situations where past-due royalties are at stake. See, e.g., *Revson v. Claire's Stores, Inc.*, 120 F. Supp.2d 322, 326-27 (S.D.N.Y.2000) (applying licensee estoppel because 'the consequence of *Kohle* is that *Boutiques*' assertion of invalidity is no defense to plaintiff's claim for royalties due in respect of sales made prior to the filing of the complaint'); *Advanced Card Techs., LLC v. Versatile Card Tech., Inc.*, 410 F. Supp.2d 158, 161 (S.D.N.Y.2006) ('just as the defendant in *Revson* was barred from asserting an invalidity defense to royalty payments that accrued in respect of sales occurring prior to the filing of the in that action, so here VCT may not assert its [invalidity defense] to royalty payments that were [allegedly due] prior to the filing of this action.'). 535 F. Supp. 2d 1000, 1017-18 (C.D. Cal. 2008).

invalidity, was not such a licensee and, accordingly, its patent challenge was not prohibited by *Shell Oil*.

Having distinguished *Shell Oil*, the *MedImmune* district court argued that the *Lear* holding controlled the dispute in the instant case, protecting the right of MedImmune to challenge the Genentech patent, despite its status as a nonrepudiating licensee in good standing. The district court noted that in those instances in which the Federal Circuit had distinguished *Lear*, it had done so on the basis of policy considerations that had not been addressed by the *Lear* Court in its balancing test. It cited *Flex-Foot*, in which the public's interest in the settlement of litigation and the binding effect of *res judicata* were at stake, and *Diamond Scientific*, which addressed the injustice of permitting a patent assignor to receive full value for the assigned patent and later repudiate the patent to the assignor's advantage. As the district court had already argued, the *Shell Oil* holding turned on the fact that the licensee in that case had actually frustrated the policy rationale of *Lear* by delaying a timely adjudication of the licensed patent's validity. In that none of those "policy-altering distinctions" were relevant to the dispute under consideration and that "[t]he distinction that MedImmune . . . [was] a nonrepudiating licensee . . . [was] insufficient to depart from *Lear's* analysis,"⁵⁰² the *MedImmune* district court concluded that the U.S. Supreme Court's *Lear* holding was applicable to the case before it and MedImmune's patent validity challenge was not barred by licensee estoppel. The district court summarized its position on the relevance of *Lear* in the following excerpt:

In this case, where invalidity has been raised affirmatively by the licensee, the *Lear* Court's reasoning applies in full force even though MedImmune has not repudiated the license: to prevent MedImmune from challenging the validity of the patent would give greater weight to the technicalities of contract doctrine than to federal patent policy. Because the Court definitively answered that question for patent license agreements like this one, this is a case where the court will not "strike a balance which would result in an outcome different from that reached by the Supreme Court in *Lear*." *American Sterilizer Co.*, 526 F.2d . . . [542, 547 (3rd Cir. 1975)].⁵⁰³

502. 535 F. Supp. 2d at 1018.

503. *Id.* at 1018-19 (footnotes omitted).

D. Licensee Estoppel and the Nonrepudiating Licensee in Good Standing

The goal of this Part III of the Article has been to determine the scope of the U.S. Supreme Court's abrogation of the doctrine of licensee estoppel in *Lear v. Adkins*, the Court's definitive statement on the subject. Specifically, we have focused on whether *Lear's* rejection of licensee estoppel was sufficiently broad to cover a nonrepudiating licensee in good standing. Our analysis has yielded the following conclusions. One, the weight of the evidence indicates that the Supreme Court's endorsement of licensee estoppel in *Automatic Radio*, the last endorsement to be issued by the Court prior to its *Lear* holding, addressed the traditional version of the doctrine, with its eviction and repudiation limits, and not the "strong form" version of the doctrine defined by the termination rule. Two, in overruling its prior holding in *Automatic Radio*, the Supreme Court in *Lear* rejected the traditional version of licensee estoppel that already incorporated a repudiation limitation, and thereby determined that even a nonrepudiating licensee in good standing was permitted to challenge the licensed patent. Three, both the language and the reasoning of the *Lear* decision extend beyond the facts in that case, which involved a repudiating licensee, and apply with equal force to a nonrepudiating licensee in good standing. Four, the majority of post-*Lear* regional circuit and district court decisions that considered the estoppel doctrine evinced the adoption of a broad reading of the *Lear* Court's holding and a willingness to apply that holding to fact patterns that differed from that in *Lear*. Five, the Federal Circuit rulings that have distinguished *Lear* have done so on the basis of policy considerations not addressed by the *Lear* Court in its balancing test, e.g., the public's interest in the settlement of litigation and the binding effect of *res judicata*, or the injustice of permitting a patent assignor to receive full value for the assigned patent and later repudiate the patent to the assignor's advantage. Six, the Federal Circuit's *Shell Oil* holding, with its prerequisite statement, is best explained on the basis of the unusual facts in that case, which involved a licensee that had acted in a manner that delayed the early adjudication of patent invalidity; moreover, in reaching its decision, the *Shell Oil* court relied on another fact-specific holding in *Hull* (where a licensee's patent validity challenge was found to be irrelevant to the licensor's claim for pre-challenge royalties) and ignored prior regional circuit decisions (in *Warner-Jenkinson* and *Precision Shooting*) that had effectively argued in favor of permitting

a nonrepudiating licensee in good standing to challenge the licensed patent. Seven, and finally, the most recent comprehensive assessment of the scope of the Supreme Court's *Lear* holding, provided by the *MedImmune* district court, yielded the conclusion that barring a nonrepudiating licensee in good standing from challenging the validity of a licensed patent "would give greater weight to the technicalities of contract doctrine than to federal patent policy,"⁵⁰⁴ and was neither mandated by *Shell Oil* nor permitted under *Lear*.

On the basis of the above considerations, we conclude that if and when the issue is presented, the U.S. Supreme Court will interpret its prior *Lear* holding as having rejected the doctrine of licensee estoppel in its entirety. According to this view, and despite the apparent obstacle presented by the Federal Circuit's prerequisite statement in *Shell Oil*, a patent licensee may challenge the validity of the licensed patent even if it neither repudiates nor terminates its patent license agreement and intends to continue to reap the benefits provided pursuant to the agreement. Based on this broad reading of the Supreme Court's rejection in *Lear* of the doctrine of licensee estoppel, coupled with the Court's elimination in *MedImmune* of the Federal Circuit's jurisdictional barrier to a patent validity challenge by a licensee in good standing, we believe that a patent licensor would be ill-advised to rely on some vestige of the common law doctrine of licensee estoppel to prevent its licensee from challenging the validity of its licensed patent. Rather, the concerned licensor should consider introducing explicit contractual provisions in the patent license agreement to account for the increased likelihood of such a patent challenge. The question then becomes which provisions are enforceable and, if not clearly enforceable, which are least likely to give rise to unintended consequences, including a reasonable claim of patent misuse. Part IV, therefore, explores the enforceability and effects of explicit contractual protections of the patent licensor.

504. *Id.* at 1018.

IV. EXPLICIT CONTRACTUAL PROTECTIONS OF THE LICENSOR FOLLOWING *MEDIMMUNE*

The U.S. Supreme Court's *Lear* decision sounded the death knell of the common law doctrine of licensee estoppel and, as we concluded in Part III, abrogated the doctrine in its entirety. The license agreement under consideration in *Lear* did not contain an express contractual prohibition barring a patent validity challenge by the licensee (a licensee "no-challenge" clause). It did, however, include a royalty payment provision that could, according to the *Lear* Court, frustrate the important federal policy of eliminating specious patents, even if the licensee were permitted to challenge the licensed patent. The provision required the licensee to continue paying royalties during the pendency of the patent challenge and, if enforced, would have encouraged the patent licensor to postpone a final determination regarding the patent's validity and could have deterred the licensee from bringing the patent challenge in the first place. In holding that the *Lear* royalty payment provision was not enforceable (the second prong of the *Lear* doctrine), the Court placed the public's interest in the full and free use of ideas actually in the public domain above the technical requirements of contract doctrine.

As discussed in Part III, the majority of post-*Lear* regional circuit and district courts were aggressive in their application of the *Lear* holding and, when confronted with the issue, ruled that a contract provision that eliminated one of the protections of the *Lear* doctrine was unenforceable.⁵⁰⁵ In contrast, the Federal Circuit, which distinguished *Lear* when policy considerations not addressed in that case were at stake, held that a licensee "no-challenge" clause (as in *Flex-Foot*) and a contractual post-patent invalidation royalty payment obligation (as in *Hemstreet*) were enforceable in the context

505. For holdings that a licensee "no-challenge" clause is unenforceable under *Lear*, see *Congoleum Industries, Inc. v. Armstrong Cork Co.*, 366 F. Supp. 220 (E.D. Pa. 1973) (*aff'd*, 510 F.2d 334 (3d Cir. 1975)); *Kraly*, 319 F. Supp. 1349 (N.D. Ill. 1970); 502 F.2d 1366 (7th Cir. 1974); *Blohm & Voss AG v. Prudential-Grace Lines, Inc.*, 346 F. Supp. 1116 (D. Md. 1972) (*rev'd on other grounds*, 489 F.2d 231 (4th Cir. 1973)); *Panther Pumps & Equipment Co.*, 468 F.2d 225; *Bendix Corp. v. Balax, Inc.*, 471 F.2d 149 (7th Cir. 1972); *Massillion-Cleveland-Akron Sign Co.*, 444 F.2d 425; *Robintech, Inc.*, 450 F. Supp. 817; *Wallace Clark & Co., Inc.*, 401 F. Supp. 637; *Plastic Contact Lens Co.*, 330 F. Supp. 441. For a holding that a contractual obligation to pay royalties during the pendency of a licensee patent validity challenge is unenforceable under *Lear*, see *Bayer AG v. Housey Pharm., Inc.*, 228 F. Supp.2d 467 (D. Del. 2002).

of a settlement of prior patent infringement litigation. Moreover, the Federal Circuit's "challenge-but-face-the-consequence" decisions, discussed in Part III, supported the view that a patent licensee that challenged the validity of the licensed patent could be subjected to a contractually mandated unwanted consequence as a result of the challenge. However, the Federal Circuit's *Shell Oil* and *Gen-Probe* decisions, requiring that a licensee repudiate its license agreement prior to a patent challenge, functioned as deterrents to licensee patent validity challenges and thereby lessened the need for contractual protections of the patent licensor in the event of a challenge. But with the Supreme Court's rejection of *Gen-Probe* in its *MedImmune* decision and the growing uncertainty as to the general applicability of the *Shell Oil* prerequisite statement, interest in the enforceability of contractual protections of the patent licensor has been rekindled. As patent licensors have considered a variety of such provisions, including those that contemplate the patent license agreement surviving an unsuccessful patent challenge, attention has focused on the question of when an agreed-to consequence of a licensee patent challenge constitutes an impermissible disincentive to challenge that undermines the public policy, articulated in *Lear*, of encouraging the early adjudication of patent invalidity.

In this Part IV, we discuss the enforceability and effects of explicit contractual protections of the patent licensor intended to account for an increased likelihood of a licensee patent validity challenge. Recognizing that a detailed review of each of the various provisions that have been considered by patent licensors is beyond the scope of this Article, we present an approach to analyze any such provision. We then apply the approach to a number of representative provisions that are frequently encountered in patent license agreements.

A. An Approach to Contract Provision Analysis

It is important to note at the outset that many of the contractual protections that have been relied on by patent licensors to account for an increased likelihood of a licensee patent validity challenge have not been subjected to judicial review. Accordingly, an assessment of the enforceability and effects of provisions of this type frequently entails unavoidable uncertainty. There is, however, an approach to evaluating such a provision that can reduce the level of uncertainty.

A contractual provision that directly eliminates one of the protections of the *Lear* doctrine is unlikely to be enforceable unless a policy consideration not addressed in the *Lear* balancing test is at stake, and even then the enforceability of such a provision may depend on Federal Circuit jurisprudence that has yet to be endorsed by a U.S. Supreme Court that has had its issues of late with a number of Federal Circuit patent-related decisions. Provisions that do not directly eliminate a protection of the *Lear* doctrine but place an unwanted consequence on a licensee that contests the validity of the licensed patent present a greater challenge. There may be relevant case law that can provide some guidance regarding enforceability. In the absence of such case law, however, one is left with making a judgment as to enforceability on the basis of considerations such as whether the contractually mandated consequence of a licensee's patent validity challenge is such that it would likely prevent the challenge in the first place. Here the analysis focuses on whether the consequence constitutes a penalty for the mere act of challenging the patent or takes effect only after an unsuccessful patent challenge and reflects the enhanced value of a patent that has been adjudicated as valid. Provisions with consequences that fall into the latter category are more likely to be enforceable than those that fall into the former category. In the final analysis, one must determine where on the "disincentive-to-challenge" spectrum a contractual consequence falls and whether its position on the spectrum places it outside of the zone of enforceability under *Lear*. In essence, one is required to provide an answer to the question posed in section III C.4.c.ii. regarding the meaning of the "spirit of *Lear*," namely, where did the *Lear* Court draw the line of enforceability in the gap between providing a licensee with "some incentive" to challenge a licensed patent and providing a licensee with "every possible incentive?"

In addition to considering the enforceability of a contemplated pro-licensor contract provision, one must determine whether the provision protects the licensor as intended and whether the inclusion of the provision in a patent license agreement could have unintended consequences. For example, as we discuss in section IV.B.2., enforcement of a "termination-for-challenge" clause, which provides a patent licensor with the right to terminate the patent license agreement in the event of a patent validity challenge by the licensee, would place a terminated licensee that continues to practice the patented invention in the position of an infringer, should the patent challenge fail. However, the U.S. Supreme

Court's recent decision in *eBay Inc. v. MercExchange, L.L.C.*⁵⁰⁶ allows for the very real possibility that the former licensee may not be enjoined from the use of the patented invention, but rather be permitted to continue to practice the invention in consideration for the payment of an ongoing royalty.⁵⁰⁷ If the patent licensor has not taken this possibility into consideration by specifying in its contract that the royalty would (reasonably) increase in the event of an unsuccessful patent challenge, it may not have obtained the maximum available benefit from its "termination-for-challenge" provision. Another example, also discussed below, arises in the context of a patent license agreement that contains a provision that directly eliminates one of the protections of the *Lear* doctrine, e.g., a licensee "no-challenge" clause or a contractual royalty payment obligation that requires the licensee to make payments during the pendency of its patent challenge. While a licensor is unlikely to obtain the aid of a court in seeking the specific performance of the licensee's contractual obligation, the licensor may be permitted to terminate the license agreement on the basis of the licensee's material breach, a potential outcome of obvious significance to each of the parties to the agreement. Finally, a licensor should consider whether the inclusion of an unenforceable contract provision in the patent license agreement could have ramifications that extend beyond its agreement with the licensee. Here the example is the inclusion of an unenforceable contract provision that constitutes an act of patent misuse, which would prevent the enforcement of the licensed patent, even against a third party infringer, until the misuse has ended and its effects have been dissipated.

With the above considerations in mind, we propose that the following questions be answered in evaluating a contractual protection of a patent licensor intended to account for an increased likelihood of a licensee patent validity challenge:

(1) Does the contract provision eliminate the protection afforded by either of the two prongs of the *Lear* doctrine, and if it does, are there any policy issues at stake that were not considered by the U.S. Supreme Court in its balancing test in *Lear*?

(2) Is there any case law, other than the Supreme Court's *Lear* holding, relevant to the particular contract provision under consideration?

506. 547 U.S. 388 (2006).

507. See *Paice v. Toyota Motor Corp.*, 504 F.3d 1293 (Fed. Cir. 2007).

(3) Where does the contract provision fall on the “disincentive-to-challenge” spectrum; is the disincentive punitive in nature; does the disincentive constitute, in practice, a prohibition to challenge?

(4) Does the contract provision protect the patent licensor as intended; could the inclusion of the provision in a patent license agreement have unintended consequences?

(5) If the contract provision is determined to be unenforceable on the basis of the *Lear* public policy argument, is the inclusion of the contract provision in a patent license agreement an act of patent misuse?

B. Analysis of Representative Contract Provisions

1. Licensee “no-challenge” clause

While the wording may vary, a contract provision that prohibits a patent licensee from challenging the validity of the licensed patent during the term of the license agreement qualifies as a licensee “no-challenge” or “no-contest” clause. As noted above, the license agreement under consideration in *Lear* did not contain a licensee “no-challenge” clause. However, enforcement of such a provision would eliminate the protection afforded a licensee under the first prong of the *Lear* doctrine, namely, that a licensee cannot be barred from challenging the validity of a licensed patent. It is not surprising, therefore, that virtually every post-*Lear* court⁵⁰⁸ and commentator⁵⁰⁹ that has considered the matter has concluded that, in a typical licensing arrangement, an explicit licensee “no-challenge” clause is invalid and unenforceable under *Lear*. In fact, considering the extensive case law and commentary regarding the licensee “no-challenge” clause and the near uniformity as to its unenforceability, it might appear unnecessary to undertake the five-

508. See e.g., *Congoleum Industries, Inc.*, 366 F. Supp. 220, *aff'd* 510 F.2d 334 (3d Cir. 1975); *Kraly*, 319 F. Supp. 1349; 502 F.2d 1366; *Blohm & Voss AG*, 346 F. Supp. 1116, *rev'd on other grounds* 489 F.2d 231; *Bendix Corp.*, 471 F.2d 149; *Panther Pumps & Equip. Co.*, 468 F.2d 225; *Massillion-Cleveland-Akron Sign Co.*, 444 F.2d 425; *Robintech, Inc.*, 450 F. Supp. 817; *Wallace Clark & Co., Inc.*, 401 F. Supp. 637; *Plastic Contact Lens Co.*, 330 F. Supp. 441; *but see infra* note 529.

509. See e.g., *Rooklidge, Lear v. Atkins Revisited (Part III)*, *supra* note 68, at 69–70; *Taylor, supra* note 321, at 236–39; *McCarthy (Part II)*, *supra* note 321, at 566–67; David M. Treadway, *Has the Supreme Court Forgotten the Patentee? Recent Patent Licensing Decisions Contradict Patent Policy, Harm Licensors, and Alter Negotiation*, 33 U. DAYTON L. REV. 303, 327–328 (2007–2008); *but see* Richard W. Goldstucker, *Stop the Bleeding: MedImmune Ends the Unjustified Erosion of Patent Holders' Rights in Patent Licensing Agreements*, 16 J. INTEL. PROP. 137, 163–64 (2008–2009) (arguing that, while “*Lear* invalidated no-challenge clauses in patent licensing agreements” the enforceability of such clauses should be reconsidered in the wake of the U.S. Supreme Court’s *MedImmune* decision.)

part approach to contract provision analysis outlined in the preceding section with respect to such a clause. As will be demonstrated in this section, however, following such an approach yields useful insight into the possible effects of including a licensee “no-challenge” clause in a patent license agreement, even if such a clause is unenforceable, and provides a clear example of the value of addressing each of the questions included in the recommended approach.

Having established that a licensee “no-challenge” clause eliminates one of the protections of the *Lear* doctrine, the next question to answer is whether such a clause or the context in which it is used raises any policy issue that was not considered by the *Lear* Court in its balancing test. While a fact specific analysis, any agreement by a licensee to refrain from challenging the validity of a licensed patent arguably introduces elements not present in *Lear*, *i.e.*, freedom of contract and certainty in the contractual relationship between the parties to an agreement. As one commentator has pointed out, post-*Lear* courts that have “equated the demise of licensee estoppel in *Lear* with the unenforceability of no-challenge clauses”⁵¹⁰ have given “absolutely no consideration to the distinguishable fact that the licensees *agreed* not to challenge the patent’s validity.”⁵¹¹

The problem with this line of reasoning, attempting to distinguish a bar to a patent challenge based on a “no-challenge” clause from that based on the common law doctrine of licensee estoppel, is that the *Lear* Court rejected a freely negotiated royalty payment provision that was less restrictive than a “no-challenge” clause of a licensee’s patent challenge right, but was still considered impermissible as a result of its potential to frustrate the public’s interest in eliminating worthless patents. The fact that the rejected royalty payment obligation was set forth in an explicit contract provision in the license agreement was immaterial. Rooklidge summarized the basis for the widely accepted view that the *Lear* Court would have invalidated a licensee “no-challenge” clause in the following excerpt:

[T]he holding of *Lear* had nothing to do with no-challenge clauses, and the case did not consider the policies favoring such clauses [*e.g.* freedom of contract and certainty in

510. Taylor, *supra* note 321, at 237.

511. *Id.* at 236.

contractual relationships]. Nevertheless, the “spirit” of *Lear* is that policies rooted in contract law must give way to the policy favoring patent validity challenges. Further, in deciding whether the licensee can be required to pay royalties during its validity challenge, the Court stated that “[t]he parties’ contract, however, is no more controlling on this issue than is the State’s doctrine of estoppel, which is also rooted in contract principles.” . . . [*Lear v. Adkins*, 395 U.S. 653, 673 (1969)] If there had been a no-challenge clause in the *Lear* license agreement, the Court undoubtedly would not have hesitated in striking it down.⁵¹²

A more intriguing question regarding the impact of policy considerations on the validity of a licensee “no-challenge” clause is whether such a clause is enforceable in the context of the settlement of a prior patent infringement litigation involving the licensed patent. The license agreement in *Lear* did not result from a settlement of a prior patent infringement suit and the *Lear* Court did not consider the important public interest in encouraging the settlement of litigation in its balancing test. As discussed in section III.C.4.c.iii., the Federal Circuit relied on this distinction in *Flex-Foot* in its refusal to extend the Supreme Court’s *Lear* holding to block the enforcement of a “no-challenge” clause contained in a settlement agreement. The Federal Circuit’s holding in *Flex-Foot* remains good law and provides support for the view that the inclusion of a “no-challenge” clause in a settlement agreement will contractually estop a licensee from contesting the validity of the licensed patent. The risk of adopting this position is that if and when the U.S. Supreme Court considers the issue it will follow its recent pattern of showing little deference to the Federal Circuit’s pro-patentee jurisprudence and rule that a licensee “no-challenge” clause is unenforceable under any circumstance.⁵¹³

The conclusion that a licensee “no-challenge” clause is almost certainly unenforceable, at least in the context of the typical licensing arrangement, is bolstered by case law in which the validity of such a provision was directly ruled on, including a U.S. Supreme Court case that predated the *Lear* decision by more than three quarters of a century. In *Pope Manufacturing Co. v. Gormully*,⁵¹⁴

512. Rooklidge, *Lear v. Adkins Revisited (Part III)*, *supra* note 68, at 69–70.

513. For examples of recent decisions in which the U.S. Supreme Court reviewed and rejected a Federal Circuit holding favoring a patentee, *see supra* note 302.

514. 144 U.S. 224.

decided in 1892, the U.S. Supreme Court refused to enforce the specific performance of a licensee's contractual obligation to never dispute the validity of the licensed patent. The license agreement in the case provided that the licensee would not "in any way, either directly or indirectly, dispute or contest the validity of the letters patent hereinbefore mentioned"⁵¹⁵ and that the obligation of the licensee was irrevocable. The Court noted that the contract provision was "unusual and oppressive,"⁵¹⁶ and the fact that the no-challenge obligation survived the term of the contract suggested that the licensee did not fully comprehend the agreement that he had entered into. While these considerations clearly influenced the Court in refusing to grant specific performance in the case, the policy rationale relied on by the Court for its holding did not depend on these considerations and was the same as that relied on by the *Lear* Court decades later. The *Pope Lear* Court recognized the importance of the parties' "right to make such contracts as they please, . . . [but such contracts] shall not be against public policy."⁵¹⁷ The Court stated that "[t]he real question is whether the defendant can estop himself from disputing patents which may be wholly void."⁵¹⁸ Noting that "[i]t is as important to the public that competition should not be repressed by worthless patents, as that the patentee of a really valuable invention should be protected in his monopoly,"⁵¹⁹ the Court cited favorably a prior case in which it was held that a party "could not bind himself by contract not to avail himself of . . . [a] right if it be secured to him on grounds of public policy."⁵²⁰ The Court declined to determine whether or not the agreement in question was void as contravening public policy, but concluded that "it does not belong to that class of contracts, the specific performance of which a court of equity can be called upon to enforce."^{521, 522}

515. *Id.* at 228.

516. *Id.* at 237.

517. *Id.* at 233.

518. *Id.*

519. *Id.* at 234.

520. *Id.* (citing *Crane v. French*, 38 Miss. 503, 530, 532 (Miss. 1860)).

521. *Id.* at 236.

522. In *Edward Katzinger Co. v. Chicago Metallic Manufacturing Co.*, 329 U.S. 394 (1947), one of the U.S. Supreme Court cases that established the antitrust-based exception to licensee estoppel, *see* discussion *supra* section III.A.5.b., the Court was again confronted with an explicit "no-challenge" clause that prevented the licensee from challenging the validity of the licensed patent following the termination of the license agreement. In ruling that the clause was unenforceable, the Court reasoned that the

As noted above, a number of regional circuit and district courts ruled on the enforceability of the “no-challenge” clause in the aftermath of *Lear*. The clause was evaluated in the context of a typical licensing arrangement,⁵²³ as part of a prior settlement of patent infringement litigation,⁵²⁴ and in assessing whether a patent holder had misused its patent by including a “no-challenge” clause in a third party license agreement.⁵²⁵ In each of these post-*Lear* cases the “no-challenge” clause was found to be invalid and unenforceable. The cases were similar in another significant respect, namely, that the court’s conclusion regarding unenforceability was reached with a minimum of analysis. As one commentator noted, “[s]oon after the United States Supreme Court decided *Lear*, lower courts struck down no-challenge clauses in case after case without exception. Many lower courts invalidated these provisions without analysis. They simply assumed that *Lear* made the unenforceability of no-challenge clauses obvious.”⁵²⁶ Yet, despite criticisms regarding the limited analysis in each of these cases, the unanimous condemnation of the “no-challenge” clause effectively eliminated its use in licensing agreements. Commentators who argued that the “no-challenge” clause should not be considered *per se* invalid and still had a place in patent license agreements were forced to look to the Federal Circuit, with its traditional pro-patentee bias, or Congress for support.⁵²⁷ Writing in 1987, Rooklidge summarized the situation in the following excerpt:

The obstacle presented by the *Lear* progeny . . . is that there may be no more no-challenge clause cases. After *Lear*, prudent licensors stopped including no-challenge clauses in licenses and expressly disclaimed reliance on existing no-challenge clauses . . . Despite the potential for a fresh look at

licensee’s “specific contract not to challenge the validity of Katzinger’s patent can no more override congressional policy than can an implied estoppel,” *id.* at 402, although in *Katzinger* the congressional policy at stake was the Sherman Act’s proscription of a price-fixing provision in the absence of a valid patent monopoly.

523. See *Plastic Contact Lens Co.*, 330 F. Supp. 441; *Robintech, Inc.*, 450 F. Supp. 817.

524. See *Kraly*, 319 F. Supp. 1349; 502 F.2d 1366; *Massillion-Cleveland-Akron Sign Co.*, 444 F.2d 425; *Wallace Clark & Co., Inc.*, 401 F. Supp. 637.

525. See *Panther Pumps & Equip. Co., Inc.*, 468 F.2d 225; *Bendix Corp.*, 471 F.2d 149; *Blohm & Voss*, 346 F. Supp. 1116 (*rev’d on other grounds*, 489 F.2d 231 (4th Cir. 1973)); *Congoleum Indus., Inc.*, 336 F. Supp. 220.

526. Taylor, *supra* note 321, at 236 (footnote omitted).

527. See Rooklidge, *Lear v. Adkins Revisited (Part III)*, *supra* note 68, at 63.

no-challenge clauses in the courts, particularly the Federal Circuit, the courts may not get the opportunity. Assuming that the courts never get the chance to straighten out their post-*Lear* excesses concerning no-challenge clauses, Congress is the sole remaining hope.⁵²⁸

As we have already discussed, the Federal Circuit in *Flex-Foot* did subsequently rule that a licensee “no-challenge” clause in a settlement agreement was enforceable. However, to the knowledge of the authors, no court has challenged the consensus among the *Lear* progeny that a “no-challenge” clause in the context of a typical licensing arrangement is unenforceable.⁵²⁹ Moreover, while

528. *Id.* at 89 (paragraphing omitted).

529. A U.S. district court recently addressed, but did not rule on, the enforceability under *Lear* of a licensee “no-challenge” clause in a license agreement that did not result from the settlement of patent litigation. In *Mayo Clinic Jacksonville v. Alzheimer’s Institute of America Inc.*, 683 F. Supp. 2d 1292 (M.D. Florida 2009), the District Court for the Middle District of Florida considered, *inter alia*, whether the licensee in the case (Mayo) breached its license agreement by contesting the validity of licensed patents in response to a patent infringement claim brought by the licensor (AIA). The agreement at issue contained a provision that stated that Mayo was not permitted to “. . . ‘initiate or voluntarily participate in [] any action’ to undermine, invalidate, or declare unenforceable claims of AIA’s patents.” *Id.* at 1294. Notwithstanding the provision, Mayo asserted both an affirmative defense of patent invalidity and a defensive counterclaim seeking a declaration of invalidity in response to AIA’s patent infringement claim. The *Mayo* district court concluded that while federal patent policy, as articulated in *Lear*, may invalidate the “no-challenge” clause under consideration, the court need not decide that issue in that a strict reading of the clause indicated that Mayo’s actions in challenging the AIA’s patents did not constitute a breach of the agreement. (“Because the no-challenge clause is neither part of an agreement reached in settlement of litigation nor the result of a consent decree, federal patent policy may invalidate the clause and permit Mayo to challenge the validity of AIA’s patent. However, resolution of that question is unnecessary . . . Even assuming for a moment that federal patent policy permits enforcement of the no-challenge clause, the no-challenge clause, which gravitates against patent policy in a manner reminiscent of *Lear*, receives the strict construction warranted by a provision that constrains a constitutional, statutory, or other legal right. Applying a strict construction to the no-challenge clause and confining the reach of the clause to that defined by its terms, [AIA’s] count . . . fails to state a claim because the facts of this case present no event of breach of the no-challenge clause.” *Id.* at 1298.) In the view of the court, Mayo neither “initiated” nor “voluntarily participated in” an action in violation of its license agreement by raising patent invalidity as a defense, in that it was AIA’s patent infringement claim that initiated the action and prompted Mayo’s defensive assertions.

While the *Mayo* court did not resolve the question of whether a licensee “no-challenge” clause is valid, it provided the following arguments in support of the enforceability of such a clause in a license agreement that did not result from the settlement of litigation, at least under certain circumstances: One, the *Lear* decision does not address the enforceability of a “no-challenge” clause. (“*Lear* stands for the proposition that the law will not infer from a license a bar to a licensee’s challenging a patent. However, *Lear* fails to discuss whether (or under what circumstances) informed

Congress has considered the issue on a number of occasions,⁵³⁰ no legislation has been enacted to address the enforceability of a licensee “no-challenge” clause.

The next question to address in our analysis of a pro-licensor contract provision is where does the provision under consideration fall on the “disincentive-to-challenge” spectrum? As noted above, a

persons, acting from positions of substantial parity and benefitting from the advice of counsel, may negotiate a contract that, consequent upon the exchange of a valuable consideration, knowingly, intelligently, explicitly, and voluntarily waives the right to challenge a patent’s validity. . . . *Lear* holds, at most, that the mere existence of a license agreement is insufficient to estop a licensee’s challenge to a patent.” *Id.* at 1296, and footnote 7. Two, “[t]he law frequently permits an individual to waive either a constitutional or a statutory right [e.g., a licensee’s right to challenge the licensed patent] notwithstanding the strong public interest in preserving the right.” *Id.*, footnote 7 (citations deleted). Three, “[c]ritics argue that invalidation of a no-challenge clause erodes a patent holder’s liberty to contract, decreases economic efficiency, hurts the patent law’s goal of innovation, and renders more difficult the negotiation of a license agreement.” *Id.* at 1295, footnote 3 (citations deleted). Four, “no-challenge” clauses have been held to be enforceable in the context of the settlement or judicial disposition of litigation, but “neither *Lear* nor any case decided in consequence of *Lear* suggests a sound basis in law, fact, or policy to distinguish between, on the one hand, a licensee’s waiver in a settlement agreement formalized by the parties a day before litigation otherwise would have occurred (which waiver *Lear* may reject) and, on the other hand, a licensee’s waiver in a settlement agreement formalized a day after litigation began and which agreement is memorialized in a mere moment by court order (and which waiver *Lear* may accept). A less problematic result follows from focusing the governing distinction not on the occurrence of litigation but on whether the potentially estopped party knew the basis of the alleged invalidity before entering the waiver and whether the parties exchanged a consideration discretely attributable to the prospect of invalidity and waiver (i.e., by focusing on the resolution of a bona fide dispute and not merely on the resolution of a dispute in litigation). In the resolution of a bona fide dispute, both a licensor extending a distinct consideration to avoid an identified risk and a licensee accepting that consideration (e.g., a reduced royalty) should remain bound by the contract—the licensor with a more secure patent but receiving less money and the licensee paying less but unable to challenge. This distinction preserves the public interest in dispute resolution but discourages duplicity and deception.” *Id.* at 1296, footnote 7. And five, the courts have recognized a distinction between defensive assertions of patent invalidity (e.g., an affirmative defense or a defensive counterclaim) and aggressive assertions of invalidity, and while the “no-challenge” clause in the instant case failed to prohibit defensive assertions, it may have prevented aggressive assertions. (“If intended to bar a challenge to AIA’s patent validity, the no-challenge clause is clumsily and ineffectively constructed, omits to preclude even the typical challenge of invalidity by affirmative defense, and overlooks the potential for a counterclaim. If intended to prevent Mayo’s aggressive attack on patent validity, the no-challenge clause perhaps persists, although subject to the vagaries of *Lear*.” *Id.* at 1298 (footnote deleted)).

530. For discussions of legislative efforts to address the enforceability of licensee “no-challenge” clauses, see Rooklidge, *Lear v. Adkins Revisited (Part III)*, *supra* note 68, at 81–82; John W. Schlicher, *Patent Licensing, What to Do After MedImmune v. Genentech*, 89 J. PAT. & TRADEMARK OFF. SOC’Y 364, 392–394 & n.49 (2007); Goldstucker, *supra* note 509, at 160–61.

contractual disincentive that constitutes a penalty for the mere act of challenging a licensed patent is more likely to run a foul of the “spirit of *Lear*” than a consequence that takes effect only after an unsuccessful challenge and reflects the enhanced value of a patent that has been adjudicated as valid. With respect to the “no-challenge” clause, it might appear that such a question is irrelevant, in that a contractual disincentive that results from a licensee’s patentee validity challenge presupposes that there is a challenge in the first place. However, if we accept the reasonable conclusion that a “no-challenge” clause in the context of a typical licensing arrangement will not prevent the licensee from challenging the licensed patent, the inclusion of the unenforceable provision in the license agreement may still result in a consequence upon the licensee’s challenge that works to the detriment of the licensee. Viewed from that perspective, a “no-challenge” clause may discourage rather than necessarily prevent a licensee patent validity challenge, justifying an assessment of the provision’s disincentive effect. Moreover, evaluating the “no-challenge” clause in this way leads to a consideration of the final questions in our analysis of a pro-licensor contract provision, namely, might the inclusion of the contract provision in the license agreement have unintended consequences and can one such consequence be the rendering of the licensed patent unenforceable, even against third party infringers, as a result of patent misuse?

As we have already discussed, the applicable case law indicates that a “no-challenge” clause in a license agreement that did not result from the settlement of a prior litigation involving the licensed patent is not likely to be specifically enforced by a court. That does not mean, however, that the inclusion of the provision in the license agreement is without effect. A review of the oral argument before the U.S. Supreme Court in *MedImmune* is instructive in exploring this point. While the *MedImmune* decision was jurisdictional in nature and the case did not involve a “no-challenge” clause, the Justices (as evidenced by their questions during the oral argument in the case) were very much interested in the potential impact of such a provision or, for that matter, any contractual provision that would prevent or discourage a licensee from challenging the validity of the licensed patent, on the rights of licensors and licensees in a patent license agreement. In fact, the first question of the oral argument, posed by Chief Justice Roberts, was whether *MedImmune*’s position in the case would be different if the Genentech/*MedImmune* license agreement had contained a

licensee “no-challenge” clause.⁵³¹ Not surprisingly, the Chief Justice’s inquiry did not result in a ruling by the Court on the enforceability of such a provision. The discussion did, however, provide insight into the Chief Justice’s interpretation of the Court’s prior decision in *Pope* and the potential effect of the inclusion of a “no-challenge” clause in a patent license agreement.

In questioning Deanne E. Maynard, Esq., the Assistant to the Solicitor General speaking in support of MedImmune, Chief Justice Roberts provided the following response to Maynard’s contention that the “no-challenge” clause considered in *Pope* was unenforceable: “I think you overread *Pope*. All *Pope* said was that they’re not going to grant specific performance. In fact, they’ve

531. The oral argument before the U.S. Supreme Court in *MedImmune* began with the following exchange between the Justices and John G. Kester, Esq., speaking on behalf of MedImmune:

CHIEF JUSTICE ROBERTS: Mr. Kester, would it --

MR. KESTER: Yes?

CHIEF JUSTICE ROBERTS: -- would it -- would your position be different if the contract contained a specific -- the license -- a specific provision specifying that the licensee may not sue [i.e. bring an action for a declaratory judgment that the licensed patent is invalid]?

MR. KESTER: No, it would not, Your Honor, because --

CHIEF JUSTICE ROBERTS: You -- do you think such a provision would be enforceable?

MR. KESTER: I doubt it would be enforceable. It would be a matter -- under the *Lear* case, *Lear* against *Adkins*, it would be an -- it would be an affirmative defense if such -- if such a claim were raised. This case is here at the level of subject-matter jurisdiction.

JUSTICE SCALIA: Excuse me, I don’t -- I don’t understand what you just said. You mean, it would be enforceable; that if such a suit were brought, the licensor could raise that contractual provision as a basis for dismissing the suit. Is that --

MR. KESTER: Under 12-- under 12(b)(6) --

JUSTICE SCALIA: Okay.

MR. KESTER: -- perhaps.

JUSTICE SCALIA: So, then it is enforceable.

JUSTICE SOUTER: No, but --

MR. KESTER: No.

JUSTICE SOUTER: -- your point is, it’s not jurisdictional.

MR. KESTER: It’s not jurisdictional, exactly, Justice Souter. This is a jurisdictional ruling. And that’s all that this Court granted certiorari on.

JUSTICE KENNEDY: Well, but as a matter of policy, we, at some point, either in this case or some later case, may have to address the question of whether or not such a provision is enforceable. If it is, we may be -- not be talking about much. It’s just going to be boilerplate in every license agreement, and that’s the end of it

MedImmune oral argument, at *3-*6.

said, ‘Whatever you may think of the policy here, . . . specific performance calls on . . . equitable discretion, and we’re not going to do it.’ But, I don’t read Pope as holding that the clauses are otherwise unenforceable. In other words you’re maybe entitled to damages . . .”⁵³² Accepting the limitations of a comment made during an oral argument regarding a fact pattern not present in the case under consideration, the Roberts’ statement is nonetheless noteworthy for its suggestion that a “no-challenge” clause, if breached by the licensee, may result in a consequence detrimental to the licensee’s interests, even if it is not specifically enforced by a court. Whether the licensor would be entitled to damages, a right to terminate the license agreement or both, the inclusion of an unenforceable “no-challenge” clause in the license agreement could penalize the licensee if it were to exercise its *Lear*-protected right to challenge the validity of the licensed patent and might discourage the licensee from bringing the challenge in the first place.⁵³³ In that case, however, the consequence of a breach of a “no-challenge” clause, as dictated by contract law, may itself be considered incompatible with the “spirit of *Lear*” and, therefore, held to be unenforceable. While the Chief Justice’s comment on the Court’s *Pope* decision fails to clarify the effect of a “no-challenge” clause in a license agreement, the important point here is that care must be exercised in including such a provision in a patent license agreement if one is to avoid potential unintended consequences.

Another potential unintended consequence of the use of a “no-challenge” clause is that its inclusion in a license agreement may constitute an act of patent misuse.⁵³⁴ Patent misuse is an equitable defense to a claim of patent infringement analogous to the doctrine of unclean hands. Misuse will be found if a patent is used in an effort to extend the physical or temporal scope of the patent monopoly with anticompetitive effect or in the violation of the antitrust laws. Where a patent has been misused in negotiating a license agreement, the offending provision is invalid and the misused patent is unenforceable, even against third party infringers,

532. *Id.* at *19.

533. Where the consequence of a breach of a “no-challenge” clause is the right of the patent licensor to terminate the license agreement, inclusion of the “no-challenge” clause in the agreement is the functional equivalent of a “termination-for-challenge” clause, the enforceability and effects of which will be discussed in the next section.

534. For a summary of the doctrine of patent misuse see *Server, Mousavi, & Love, supra* note 192, at 65-75. See also *Princo Corp. v. Int’l. Trade Comm’n*, 616 F.3d 1318 (Fed. Cir. 2010), for a recent discussion by the Federal Circuit of the scope of the misuse doctrine.

until the misuse terminates and its consequences are fully dissipated.⁵³⁵

In the context of a “no-challenge” clause, the potential for a finding of patent misuse is noteworthy for two reasons. First, the misuse would occur whether or not the licensee actually challenges the licensed patent. The fact that the patent holder had used the leverage of its government-granted patent monopoly to force the inclusion of the offending provision into the agreement would constitute the misuse and lead to the associated consequences. Second, a finding of patent misuse could have a detrimental effect on not only the licensor, but the licensee as well. Obviously, the licensor would suffer from its inability to enforce the “no-challenge” provision (even if it were not unenforceable under *Lear*), as well as from its inability to enforce its patent until the misuse had been purged. However, a licensee may also suffer in the situation where it never intended to challenge the patent, but rather planned to rely on the enforceability of the licensed patent to prevent the unauthorized use of the patented invention by others. In fact, many of the cases that considered whether a “no-challenge” clause constituted patent misuse involved a claim by an alleged infringer that the patent-at-issue was not enforceable based on the patent holder’s inclusion of a “no-challenge” clause in its patent license agreements with third parties.⁵³⁶

One such case involving a patent misuse claim by an alleged infringer is *Panther Pumps & Equipment Co., Inc. v. Hydrocraft, Inc.*⁵³⁷ Noted for its thoughtful analysis and reliance on U.S. Supreme Court precedent for its conclusion, the Seventh Circuit in *Panther Pumps* ruled that “the ‘no contest’ clause in the . . . license, though unenforceable under *Lear*, does not constitute the kind of ‘misuse’ of the patent which forecloses recovery of damages from an unlicensed infringer”⁵³⁸ The court based its holding on the

535. See *supra* note 534.

536. See *Panther Pumps & Equip. Co., Inc.*, 468 F.2d 225; *Blohm & Voss*, 346 F. Supp. 1116, *rev'd on other grounds* 489 F.2d 231 (4th Cir. 1973); *Congoleum Industries, Inc.*, 336 F. Supp. 220; Note that in *Bendix Corporation v. Balax, Inc.*, 471 F.2d 149 (7th Cir. 1972) the alleged infringer also raised patent misuse as a defense, but rather than argue that the patents-at-issue (which had been held by the court to be invalid) were unenforceable, the alleged infringer sought (but was denied) damages for the patent holders alleged antitrust violation resulting from the inclusion of a “no-challenge” clause in its third party patent license agreements.

537. 468 F.2d 225.

538. *Id.* at 232.

interpretation of the *Lear* decision provided in *Blonder-Tongue*.⁵³⁹ In the words of the Seventh Circuit,

[a] fair evaluation of defendants' [the alleged infringers'] argument requires us to identify two different lines of authority. The first is "the series of decisions in which the Court has condemned attempts to broaden the physical or temporal scope of the patent monopoly." *Blonder-Tongue Laboratories, Inc. v. University Foundation*, 402 U.S. 313, 343 It is this line of cases in which the "misuse" doctrine developed. "A second group of authorities encourage authoritative testing of patent validity." *Id.* at 344 Although the Court explained that the *Lear* opinion relied on both lines of authority, it expressly stated that its "holding that licensee estoppel was no longer tenable was rooted in the second line of cases eliminating obstacles to suit by those disposed to challenge the validity of a patent." *Id.* at 345 In our opinion neither of these two lines of cases justifies the application of the "misuse" doctrine in this case.⁵⁴⁰

The *Panther Pumps* court concluded that "the policy of encouraging authoritative testing of patent validity . . . [endorsed in *Lear* and rendering the "no-challenge" clause unenforceable], is not served by a rule which enables an infringer to escape liability without challenging the validity of a patent."⁵⁴¹

A strict reading of the Seventh Circuit's wording in *Panther Pumps* might suggest that while the inclusion of a "no-challenge" clause in a patent license agreement would not prevent the enforcement of the licensed patent against third party infringers, it could prevent such enforcement against a licensee that elects to breach the provision by challenging the licensed patent and continues to practice the patented invention. However, the partial application of the doctrine of patent misuse, based on a distinction between patent licensee and third party infringer, has never been adopted by the courts.⁵⁴² Moreover, the adoption of such a policy in

539. See *supra* section III.C.4.c.i.

540. 468 F.2d 225, 231.

541. *Id.*

542. A partial application of the doctrine of patent misuse would be inconsistent with the policy rationale underlying the doctrine, which holds that the abuse of a government-granted patent monopoly, where found, constitutes a harm to the public as a whole that deprives the patent holder of the right to enforce its patent not only against

the context of assessing the effects of a “no-challenge” clause would be inconsistent with the public’s interest, articulated in *Lear*, in the early adjudication of patent invalidity, where patent licensees often have the greatest incentive to challenge patents. It is, perhaps, for these reasons that courts that have considered the effects of the inclusion of a “no-challenge” clause in a patent license agreement following the *Panther Pumps* decision have routinely rejected claims of patent misuse, and have done so (frequently citing *Panther Pumps*) whether the misuse claim was brought by an alleged third party infringer⁵⁴³ or by a patent licensee.⁵⁴⁴

Although there is a consensus among the courts that have considered the issue that the inclusion of a “no-challenge” clause that restricts a licensee during the term of the license agreement does not constitute patent misuse, the possibility of misuse has been recognized in cases in which the “no-challenge” clause remains in effect following the termination of the agreement. In *Bendix Corp. v. Balax, Inc.*,⁵⁴⁵ the Seventh Circuit considered a “no-challenge” clause in third party patent license agreements that provided that the “[l]icensee agrees that it will not contest the validity of any patent which is now a part of this agreement during the life of this agreement and thereafter”⁵⁴⁶ Unlike the typical “no-challenge” clause, the provision in *Bendix*, like the one in *Pope*, was irrevocable and survived for the life of the patent. The *Bendix* court concluded that while the “no-challenge” clause was unenforceable under *Lear*, the inclusion in the agreements of that portion of the provision that restricted the licensee during the term of the agreement was not patent misuse. However, as the court explained, “some misuse may be inferred from the mere presence of the ‘thereafter’ clause, . . . [since] [l]icensees . . . may have been induced to continue their licensing . . . arrangements with the plaintiff [patent holder] because if they terminated those arrangements to seek a deal with a competitor . . . they would, prior to *Lear*, have been unable to defend against an infringement suit by the plaintiff.”⁵⁴⁷ While the applicable case law suggests that something more than the typical “no-challenge” clause is required to support a finding of patent

a licensee victimized by the misuse but also against third party infringers that are not directly affected by the conduct that gave rise to the misuse. See *supra* note 534.

543. See *supra* note 536.

544. *Robintech, Inc.*, 450 F. Supp. 817; *Wallace Clark & Co., Inc.*, 401 F. Supp. 637.

545. 471 F.2d 149.

546. *Id.* at 155, n.10.

547. *Id.* at 158.

misuse, the *Bendix* decision makes clear that the inclusion of a “no-challenge” clause in a license agreement is not without risk as it relates to patent misuse, and that risk could work to the disadvantage of both the patent holder and its licensee.⁵⁴⁸

In sum, an analysis of the enforceability and effects of a “no-challenge” clause presents a consistent picture cautioning against the use of the provision in a typical license agreement. If enforced, a “no-challenge” clause would eliminate one of the protections of the *Lear* doctrine. Moreover, the same policy rationale relied on by the *Lear* Court in its abrogation of the doctrine of licensee estoppel and its rejection of a royalty payment provision that could discourage a licensee patent validity challenge was cited by the Court years earlier in *Pope* as the basis for its refusal to enforce the specific performance of a licensee’s contractual obligation to never contest the validity of the licensed patent. Regional circuit and district courts that have considered the issue have uniformly concluded that a “no-challenge” clause is unenforceable in the aftermath of *Lear*. In fact, only the Federal Circuit, with its pro-

548. Commentators have raised the question of whether the timing of the agreement not to challenge the licensed patent in relation to the *Lear* decision was relevant to a determination of patent misuse. McCarthy, for example, presented the following discussion:

From *Panther Pump* and *Bendix*, one may conclude that ordinary no-contest clauses which were inserted in licenses before 1969 [the year that *Lear* was decided] cannot form the basis for a misuse defense or an antitrust claim. To be safe, however, many licensors cancelled such clauses after *Lear* in an attempt to purge any possible misuse. The question remains whether a post-*Lear* inclusion of a no-contest clause in a patent license constitutes misuse. Of course, such a clause would be unenforceable under *Lear*, but many contractual clauses traditionally relied upon as misuse are equally unenforceable. The fact that a licensor fails to enforce a contractual clause does not preclude a holding of misuse, and mere existence of the clause can constitute misuse. Although the *Panther Pump* decision, unlike the *Bendix* opinion, did not rely upon the date of the no-contest clause, one may infer that a patent licensor endangers the enforceability of his patent by inclusion of such a clause in a post-*Lear* license. The courts would ask what is the purpose of having such an unenforceable promise made by the licensee? If the purpose is to provide a ground for termination if the licensee challenges but otherwise pays and performs under the license, then such a clause would appear to violate the spirit of *Lear* and amount to misuse.

McCarthy, (*Part II*), *supra* note 321, at 566–67 (footnotes omitted). As McCarthy himself points out, however, courts assessing “no-challenge” clauses that were agreed to or intentionally retained following the *Lear* decision continued to reject patent misuse claims, suggesting that the timing of the agreement not to challenge in relation to the *Lear* decision was not relevant to the misuse assessment. See, *Congoleum Indus., Inc.*, 366 F. Supp. 220, *aff’d* 510 F.2d 334; *Wallace Clark & Company, Inc.*, 401 F. Supp. 637; *Robintech, Inc.*, 450 F. Supp. 817.

patentee bias, has ruled in favor of contractual estoppel based on a “no-challenge” clause, and that was in the context of a prior settlement of litigation involving the licensed patent. Accordingly, with one notable exception, the only possible effects of the inclusion of an unenforceable “no-challenge” clause in a typical license agreement would be those that do not conform to the parties’ intention as expressly stated in the agreed-to provision. A licensee bound by a contractual “no-challenge” obligation could not be barred from exercising its *Lear*-protected right to challenge the licensed patent. In addition, the inclusion of a “no-challenge” clause in a license agreement could render the licensed patent unenforceable, if the provision was not carefully drafted in order to avoid patent misuse. The only instance in which a “no-challenge” clause would work as explicitly intended would be where a licensee elects not to bring a patent challenge in order to avoid a negative consequence that would result under contract law from a breach of the provision. In that case, however, the disincentive effect of the threatened consequence might itself violate the “spirit of *Lear*,” prompting a court to reject the consequence. Considering the various problems and uncertainties associated with the “no-challenge” clause, it is reasonable to conclude that its use in a typical license agreement should be avoided. As we will see in the sections that follow, other pro-licensor contract provisions can be used, whether alone or in combination, that have a far greater likelihood of being enforceable and are associated with significantly less risk of giving rise to unintended consequences.

2. “Termination-for-challenge” clause

A “termination-for-challenge” clause, also referred to as a “no-challenge termination” clause,⁵⁴⁹ confers upon a patent licensor the right to terminate the license agreement in the event that the licensee challenges the validity of the licensed patent. If enforceable, the provision provides a contractual means of counteracting the effect of the Supreme Court’s *MedImmune* decision, which relieved a licensee of the jurisdictional requirement of having to repudiate its patent license agreement before challenging the licensed patent. By permitting a licensor to terminate the license agreement upon the licensee’s patent

549. Taylor, *supra* note 321, at 230 (“An example of a no-challenge termination clause might be similar to the following provision: ‘[LICENSOR] retains the right to terminate this agreement if [LICENSEE] asserts in any judicial proceeding or document, during the lifetime of this agreement, that said patents are invalid.’”).

challenge, the “termination-for-challenge” clause places the licensee in the same position it would have been in prior to the *MedImmune* Court’s rejection of the Federal Circuit’s *Gen-Probe* holding, i.e., in order to bring a patent challenge, a licensee is required to risk losing the benefits of its patent license.⁵⁵⁰ Not surprisingly, the “termination-for-challenge” clause is encountered with increasing frequency in the aftermath of the Supreme Court’s *MedImmune* decision. However, the question of whether the clause is enforceable is not a simple one. As will be discussed in the analysis of the provision that follows, the “termination-for-challenge” clause has received little attention in the courts and a determination as to its enforceability is largely dependent upon whether one concludes that the disincentive effect of such a provision places it outside of the zone of enforceability under *Lear* in the gap between providing a patent licensee with “some incentive” to challenge a licensed patent and “every possible incentive.”

Unlike the “no-challenge” clause, a “termination-for-challenge” clause does not eliminate one of the protections of the *Lear* doctrine. In the words of one commentator, “[t]his type of contractual provision does not bar a licensee from challenging the patent’s validity. It merely gives the licensor the right to terminate the license in such a case, enabling the licensor to sue the licensee for infringement.”⁵⁵¹ The “termination-for-challenge” clause differs from the “no-challenge” clause in another important respect. While the latter has been the subject of judicial review on a number of occasions (as discussed in the preceding section), the “termination-for-challenge” clause has only rarely been evaluated by a court. One such evaluation was provided by the U.S. District Court of Delaware in *Bayer AG v. Housey Pharmaceuticals, Inc.*⁵⁵² In that case the court ruled on the validity of a contract provision that included a “termination-for-challenge” clause. Bayer, the plaintiff in the case, sought a declaratory judgment that the Housey patents were unenforceable as a result of Housey’s misuse of the patents. Among the alleged acts of misuse was the inclusion in patent license agreements with third parties of the following provision:

550. Schlicher, *supra* note 530, at 388 (“For years, I have recommended that patent owners use a termination provision that permits the patent owner to terminate the license, if the licensee alleges in any action that the licensed patent is invalid. This is the simplest and most direct response to *MedImmune*, because it puts the situation back to where it was before *MedImmune*.” (footnote omitted)).

551. Taylor, *supra* note 321, at 231.

552. 228 F. Supp. 2d 467.

[LICENSOR] acknowledges the LICENSEE is not estopped from contesting the validity or enforceability of the Licensed Patent Rights. However, LICENSEE acknowledges that such an attack on validity or enforceability of the Licensed Patent Rights is inconsistent with the purposes of this License Agreement. Accordingly, LICENSEE hereby agrees that if it decides to assert its right to contest the Licensed Patent Rights, in whole or in part, that . . . [LICENSOR] shall have the right, at . . . [LICENSOR's] option, to terminate this License Agreement by giving written notice thereof to LICENSEE. Further, unless terminated by . . . [LICENSOR], LICENSEE agrees to make all payments due under this License Agreement notwithstanding any challenge . . . by LICENSEE . . . to the Licensed Patent Rights, so long as the applicable patent(s) or patent application(s) remain in effect.⁵⁵³

Bayer contended that the provision was an attempt “to muzzle licensees in violation of *Lear*”⁵⁵⁴ and its presence in the Housey license agreements constituted patent misuse.

The district court in *Bayer* began its analysis by restating the dual protections afforded a patent licensee under the *Lear* doctrine, namely, that a licensee cannot be barred from challenging the validity of a licensed patent nor required to pay royalties to the licensor during the pendency of its patent challenge. Concluding that neither of these protections can be eliminated by the agreement of contracting parties, the court held that the portion of the Housey provision under consideration that obligated the licensee to continue to pay royalties while challenging the licensed patent was unenforceable. The court went on to note, however, that the inclusion of this unenforceable portion of the provision in the Housey license agreements did not constitute patent misuse, citing *Panther Pumps*, *Wallace-Clark*, *Congoleum Industries* and *Robintech*. We will revisit this aspect of the *Bayer* decision in the next section, which addresses royalty payment provisions. What is significant for the purpose of this section is that the *Bayer* court found no fault with the “termination-for-challenge” portion of the Housey provision. It is true that the “termination-for-challenge” portion of the provision was not explicitly endorsed by the district court, nor even analyzed in the *Bayer* opinion. However, the provision as a

553. *Id.* at 473.

554. *Id.* at 473.

whole was under review in the case and it could be argued that the risk of termination of the licensee's rights under the agreement upon a patent challenge would constitute as much or more of a disincentive to challenge, thereby "muzzling" the licensee, as an ongoing obligation to pay royalties. Had the *Bayer* court rejected the royalty payment portion of the Housey provision on the basis of its disincentive effect, it almost certainly would have found the "termination-for-challenge" portion of the provision problematic as well. The fact that the district court selectively rejected the royalty payment portion of the provision suggests that the basis for the rejection was that that portion of the provision, in contrast to the "termination-for-challenge" portion, directly eliminated one of the protections of the *Lear* doctrine.

The *Bayer* decision, however, is only a tacit endorsement of the "termination-for-challenge" clause, and questions as to the provision's enforceability remain to be answered. The uncertainty regarding the "termination-for-challenge" clause is reflected in the U.S. Government's Amicus Brief submitted to the Supreme Court in *MedImmune*.⁵⁵⁵ In supporting *MedImmune's* position that, from a jurisdictional standpoint, a licensee in good standing can challenge the validity of the licensed patent, the Government made the following argument:

Application of traditional "case or controversy" principles in the patent context [that would permit a patent licensee in good standing to bring a declaratory judgment action challenging the validity of the licensed patent] does not leave patent owners defenseless [A] patent owner may be able to negotiate license provisions that anticipate and ameliorate the effects of the filing of a declaratory judgment action by a licensee. This Court has held that a patentee cannot require a licensee to abandon forever its right to challenge a patent, see *Pope Mfg. Co. v. Gormully*, 144 U.S. 224, 232-237 (1892), and that a licensee who successfully challenges a patent cannot be required to pay royalties during the pendency of the challenge, see *Lear*, 395 U.S. at 673-674. But a licensor may be able to make the filing of a declaratory judgment action [challenging the validity of the licensed patent] a basis for terminating the license, changing the royalty rate to a specified higher rate, or otherwise adjusting the pre-challenge terms While the

555. Brief for the United States as Amicus Curiae supporting Petitioner, *MedImmune, Inc.*, 549 U.S. 118.

enforceability of such provisions is an open question in light of the strong public policy favoring patent challenges as reflected in *Pope* and *Lear*, those decisions do not necessarily entitle a licensee both to challenge the licensed patent and to retain all the benefits of his license agreement, if the agreement expressly provides otherwise. Cf. *Cordis Corp. v. Medtronic, Inc.*, 780 F.2d 991, 995 (1985) (explaining the Federal Circuit's view that *Lear* "does permit a licensee to cease payments due under a contract while challenging the validity of a patent. It does not permit the licensees to avoid facing the consequences that such an action would bring."), cert. denied, 476 U.S. 1115 (1986)⁵⁵⁶

While a number of the Supreme Court Justices expressed an interest during the *MedImmune* oral argument in the Government's suggestions regarding contractual protections for the patent licensor,⁵⁵⁷ neither the oral argument nor the Court's opinion in *MedImmune* provided an answer to the "open question"⁵⁵⁸ as to the

556. *Id.* at 27-28 (paraphrasing omitted) (emphasis added).

557. *MedImmune* oral argument, at *10-11.

CHIEF JUSTICE ROBERTS: So, there's no way, . . . under your view, that a patent holder can protect itself from suit through any license arrangement or any agreement of any kind.

MR. KESTER: I suspect there are many ways, Mr. Chief Justice, but not by throwing them out on a jurisdictional basis at the very first moment of the lawsuit.

JUSTICE GINSBURG: How about -

MR. KESTER: There may be ways this could be arranged at the second level, through --

JUSTICE GINSBURG: Well, what are those ways - I mean, the ones that have been mentioned as possibilities in the Government brief -- one, you rejected, and the other that was mentioned was: if you sue -- if the licensee sues, then the royalty fees will be upped. Would that be effective?

MR. KESTER: That is a question that would arise under *Lear* against Adkins. And the question before this Court in that situation, if it got to this Court, would be, Is that kind of a provision compatible with the policy that was so firmly expressed by Justice Harlan in *Lear*, and has been reiterated in so many subsequent cases of this Court?

JUSTICE GINSBURG: So, you have rejected both of the Government's suggestions on what the patent holder might do to protect itself. Do you have anything concrete that you would concede the patent holder could do?

MR. KESTER: I don't think that I have rejected both the Government's suggestions. I've said that they raise problems on -- as to the scope of *Lear*.

558. Brief for the United States as Amicus Curiae supporting Petitioner, *MedImmune, Inc.*, 549 U.S. 118, at 28.

enforceability of a “termination-for-challenge” clause. As indicated in the Government’s *MedImmune* Brief, the answer to the question is to be found in a determination of whether the “termination-for-challenge” clause runs afoul of “the strong public policy favoring patent challenges as reflected in *Pope* and *Lear*.”⁵⁵⁹ And the answer to that question is dependent on an assessment of the provision’s disincentive effect and on one’s conclusion as to where the *Lear* Court drew the line of enforceability in the gap between providing a patent licensee with “some incentive” to challenge a licensed patent and “every possible incentive.” It is instructive, therefore, to return to our approach to the analysis of pro-licensor contract provisions and consider the position of the “termination-for-challenge” clause on the “disincentive-to-challenge” spectrum.

Requiring a licensee to risk losing the benefits of its patent license through a license termination in order to bring a patent challenge constitutes a considerable disincentive to challenge and, arguably, frustrates the public’s interest in eliminating worthless patents to a greater extent than would the enforcement of the royalty payment provisions rejected in *Lear* and in *Bayer*. Based on this line of reasoning, one would conclude that a “termination-for-challenge” clause in a patent license agreement is an unenforceable violation of the “spirit of *Lear*.” Moreover, as discussed in section III.C.4.c.ii, a number of the post-*Lear* regional circuit and district courts that have considered the right of a patent licensor to terminate the license agreement in the context of a licensee patent validity challenge have concluded that such a termination is not consistent with the public’s interest in the early adjudication of patent invalidity.⁵⁶⁰ As the *Crane* court stated, “just as the imposition of the doctrine of licensee estoppel would have a chilling effect on meritorious challenges to patents . . . , so would the threat of termination of the license have a similar effect.”⁵⁶¹ In another case, *Lee v. Lee Custom Engineering*,⁵⁶² a district court held that once a patent licensee challenges the validity of the licensed patent, “the law neither requires the making of royalty payments nor permits the licensor to terminate the license agreements because the licensee

559. *Id.*

560. See *Crane Co.*, 356 F. Supp. 733; 364 F. Supp. 547; 504 F.2d 1086; *Precision Shooting Equip. Co.*, 646 F.2d 313; *Lee*, 476 F. Supp. 361; but see, *Nebraska Engineering Corp.*, 557 F.2d 1257; *Morton-Norwich Prods, Inc.*, 183 USPQ 748; *Metallurgical Int’l, Inc.*, 171 USPQ 348.

561. *Crane*, 356 F. Supp. at 738–39.

562. 476 F. Supp. at 361.

has failed to make such payments,”⁵⁶³ since “the fear of termination and its potentially harsh consequences”⁵⁶⁴ would undermine the public’s interest, as expressed in *Lear*, of the elimination of worthless patents. It is true that neither *Crane* nor *Lee* involved a “termination-for-challenge” clause and the alleged contractual breach that prompted the licensor’s attempt to terminate the patent license agreement in each case was a nonpayment of royalties. However, if the public policy articulated in *Lear* is sufficiently compelling to prevent a licensor from terminating a license agreement as a result of the licensee’s failure to meet its agreed-to royalty payment obligations in the context of a patent challenge, that policy would certainly prevent the licensor from terminating a licensee’s rights for merely challenging the licensed patent. While cases such as *Crane* and *Lee* have been described as the high-watermark of pro-*Lear* case law, reflecting the view that the *Lear* decision favors providing a licensee with “every possible incentive to challenge patent validity,”⁵⁶⁵ the rationale behind the holdings in *Crane* and *Lee* relied heavily on the very significant disincentive effect of a termination of a challenging licensee’s rights under the licensed patent.

Support for the enforceability of the “termination-for-challenge” clause can be found in a series of Federal Circuit cases that we characterized in Part III of this Article as “challenge-but-face-the-consequence” decisions.⁵⁶⁶ Recall that these cases stand for the proposition that a patent licensee that challenges the validity of the licensed patent can be subject to consequences that could constitute a disincentive to make the challenge in the first place, despite the public interest, highlighted in *Lear*, in eliminating invalid patents. The Government, in its *MedImmune* Brief, acknowledged the significance of this line of cases in citing the Federal Circuit’s holding in *Cordis*⁵⁶⁷ as support for the view that “[the *Pope* and *Lear*] decisions do not necessarily entitle a licensee both to challenge the licensed patent and to retain all the benefits of

563. *Id.* at 362.

564. *Id.* at 364.

565. *See supra* section III.C.4.c.ii.

566. *See supra* section III.C.4.c.iii. for a review of the Federal Circuit’s “challenge-but-face-the-consequence decisions”; *C.R. Bard, Inc.*, 716 F.2d 874; *Cordis Corp.*, 780 F.2d 991; *Sun Studs, Inc.*, 872 F.2d 978; *Dow Chem.Co.*, 226 F.3d 1334.

567. *Cordis*, 780 F.2d 991.

his license agreement, if the agreement expressly provides otherwise.”⁵⁶⁸

As discussed in section III.C.4.c.iii, the Federal Circuit in *Cordis* relied on the reasoning articulated by the Second Circuit in *Warner-Jenkinson*⁵⁶⁹ and endorsed by the Eighth Circuit in *Nebraska Engineering*⁵⁷⁰ to conclude that neither the holding of, nor policy statement in, *Lear* prevents a patent licensor from terminating the rights of a licensee that ceases paying royalties due under the license agreement during the pendency of a patent challenge. In ruling that a licensee could not avoid facing the consequences of its breach of its license agreement in the course of bringing a patent challenge, the *Cordis* court echoed the view previously expressed in *Morton-Norwich* that “permitting the licensee to unilaterally and offensively ignore his contract obligation to make payments required under the contract, and at the same time denuding the licensor of the remedy of declaring a breach and seeking relief against the licensee as an infringer, . . . does violence to contract principles”⁵⁷¹ in a manner that “might encourage more validity litigation, but at too high a price.”⁵⁷² Like the courts in *Morton-Norwich*, *Warner-Jenkinson* and *Nebraska Engineering*, the Federal Circuit in *Cordis* rejected the conclusion that, under *Lear*, “any and all rules of contract law . . . [must] be ignored to give licensees every possible incentive to challenge patent validity.”⁵⁷³

The decision in *Cordis*, as well as those in *Morton-Norwich*, *Warner-Jenkinson* and *Nebraska Engineering*, addressed a patent licensor’s right to terminate a license agreement but did not require an evaluation of a contract provision permitting the licensor to terminate the agreement on the basis of a licensee’s patent validity challenge. In each case, the material breach that triggered the licensor’s termination right was a nonpayment of royalties due under the agreement that would accompany the challenge. In *Bard*,⁵⁷⁴ however, the Federal Circuit considered the enforceability of a contract termination provision that was based, in part, on the patent challenge itself. In that case, discussed above in

568. Brief for the United States as Amicus Curiae supporting Petitioner, *MedImmune, Inc.*, 549 U.S. 118 at *28.

569. *Warner-Jenkinson Co.*, 567 F.2d 184.

570. *Nebraska Engineering Corp.*, 557 F.2d 1257.

571. *Morton Norwich Prods, Inc.*, 183 USPQ at 750 (footnote omitted).

572. *Id.*

573. McCarthy, (*Part II*), *supra* note 321, at 568 .

574. *C.R. Bard, Inc.*, 716 F.2d 874.

section III.C.4.c.iii., the court held that the enforcement of a “termination-for-challenge-and-failure-to-pay-royalties” clause in a patent license agreement was not incompatible with the “spirit of *Lear*.” While the right of the licensee in *Bard* to bring a patent challenge was protected under *Lear*, the consequence of its challenge and the failure to pay the agreed-to royalties put the licensee at risk for losing its rights under the agreement, should the licensor elect to terminate it.

The Federal Circuit’s *Bard* decision is consistent with that circuit’s other “challenge-but-face-the-consequence” decisions in holding that a licensee that challenges the validity of a licensed patent is accountable for a contractual breach related to the challenge, even if the consequence of the breach is the licensee’s loss of rights under the patent. However, neither the *Bard* decision nor any other Federal Circuit decision has answered the central question addressed in this section, namely, is a contract provision that permits a licensor to terminate a licensee’s patent rights for merely challenging the patent enforceable? The fact that this question has remained unanswered, despite the Federal Circuit’s prior consideration of a patent licensor’s termination rights, is not surprising. Under Federal Circuit jurisprudence prior to the U.S. Supreme Court’s *MedImmune* decision, a patent licensee was required to repudiate its license agreement by withholding agreed-to royalty payments before bringing a patent validity challenge. Basing a right of termination on the mere act by a licensee of challenging the licensed patent was not necessary in that the requisite nonpayment of royalties was an adequate termination trigger. In the aftermath of *MedImmune*, however, where the weight of the evidence indicates that a patent licensee in good standing can bring a patent challenge without repudiating the licensee agreement, the enforceability of a “termination-for-challenge” clause becomes a critical issue. Permitting a licensor to terminate a licensee’s patent rights for simply challenging the licensed patent, where the licensee has otherwise complied with all of its contractual obligations under its license agreement, involves a “balancing of the equities among licensor, licensee and the public interest”⁵⁷⁵ that differs from that presented in *Morton-Norwich*, *Warner-Jenkinson*, *Nebraska Engineering* or any of the Federal Circuit’s “challenge-but-face-the-consequences” cases, and may well be incompatible with the “spirit of *Lear*.” In the absence of a specific ruling by either the

575. *Morton Norwich Prods*, 183 USPQ at 749.

Federal Circuit or the U.S. Supreme Court on a “termination-for-challenge” clause, one can only speculate as to its enforceability, forcing those who negotiate patent license agreements to consider the effects of including such a provision in their agreements, whether the provision is enforceable or not.

Assuming that a “termination-for-challenge” clause is enforceable, there is a legitimate concern that if such a clause is included in a patent license agreement it will not operate to protect the licensor as intended. The purpose of such a provision is to provide a licensor with the right to terminate its agreement with a licensee that challenges the validity of the licensed patent, thereby depriving the licensee of authorization to operate under the patent. Should the now-former licensee continue to practice the patented technology, it would do so in the role of an infringer and a licensor whose patent had been adjudicated as valid could prevent such future use through obtaining injunctive relief while seeking damages for the prior infringement. The U.S. Supreme Court’s recent decision in *eBay Inc. v. MercExchange, L.L.C.*,⁵⁷⁶ however, raises serious questions as to whether a licensor can rely on this strategy to prevent the unauthorized use of its patented technology by a former licensee.

In *eBay*, the Supreme Court rejected the Federal Circuit’s “general rule” that, in the absence of extraordinary circumstances, the holder of a valid patent should be granted a permanent injunction to prevent an infringer from using its patented technology. Instead, the Supreme Court ruled that the traditional four-factor test must be applied in determining whether injunctive relief should be granted in an infringement suit arising under the Patent Act.⁵⁷⁷ In applying the standard set forth in *eBay*, a number of lower courts have subsequently denied injunctive relief in patent infringement cases.⁵⁷⁸ For example, in *Paice v. Toyota Motor Corp.*,⁵⁷⁹

576. 547 U.S. 388.

577. *Id.* at 391. (“According to well-established principles of equity, a plaintiff seeking a permanent injunction must satisfy a four-factor test before a court may grant such relief. A plaintiff must demonstrate: (1) that it has suffered an irreparable injury; (2) that remedies available at law, such as monetary damages, are inadequate to compensate for that injury; (3) that, considering the balance of hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction These familiar principles apply with equal force to disputes arising under the Patent Act.” (citations deleted and paragraphing omitted)).

578. For a review of relevant post-*eBay* case law, see Andrew Beckerman-Rodau, *The Aftermath of eBay v. MercExchange*, 126 S. Ct. 1837 (2006): *A Review of Subsequent Judicial Decisions*, 89 J. PAT. & TRADEMARK OFF. SOC’Y 631 (2007); Edward D. Manzo, *Injunctions*

the Federal Circuit reviewed a district court's ruling that a permanent injunction was not warranted in a patent infringement case and that the infringer should instead pay ongoing royalties for its continued use of the patented technology. The Federal Circuit affirmed the district court's denial of injunctive relief and concluded that "[u]nder some circumstances, awarding an ongoing royalty for patent infringement in lieu of an injunction may be appropriate"⁵⁸⁰ (although the district court's failure to articulate its reasons for the royalty amount that it imposed upon the infringer required that the case be remanded for reevaluation of that issue).

Commentators who have reviewed the relevant post-*eBay* case law have identified a number of factors that have contributed to a denial of injunctive relief in patent infringement cases.⁵⁸¹ Among the factors identified is a prior willingness on the part of the patent holder to grant royalty-bearing licenses under its patent, thereby undermining the argument that monetary damages are inadequate to compensate for another's use of the patent (one of the requirements of the traditional four-factor test).⁵⁸² In the case of a patent licensor that terminates its license agreement pursuant to a "termination-for-challenge" clause, this is particularly problematic. Should the trend detected in the federal courts' application of the four-factor test for a permanent injunction following *eBay* continue, a court would be less likely to enjoin the use of patented technology by a former licensee whose patent validity challenge had failed, electing instead to permit future infringement in return for the payment of ongoing royalties. In that case, the licensor may be no better off than had it not exercised its "termination-for-challenge" right, with the former licensee still practicing under the patent and paying the "reasonable" royalties originally negotiated in the terminated agreement. In the next section of this Part IV, we discuss the advantages of a contract provision that increases a

in Patent Cases After eBay, 7 J. MARSHALL REV. INTELL. PROP. L. 44 (2007-2008); Bernard H. Chao, *After eBay, Inc. v. MercExchange: The Changing Landscape for Patent Remedies*, 9 MINN. J.L. SCI. & TECH. 543 (2008); Kenneth R. Adamo, Ryan B. McCrum, and Chad A. Jira, *Licensing in the Wake of the Supreme Court's Decision in eBay v. MercExchange: How Can Non-Practicing Entities Maintain Leverage?*, 30 LIC. J. 1 (2010).

579. 504 F.3d 1293.

580. *Id.* at 1314.

581. *See supra* note 578.

582. Manzo, *supra* note 578, at 94 ("[A] patentee's offer of a royalty-bearing license . . . is a factor indicating that money damages are adequate"); Adamo, *supra* note 578, at 6 ("[T]he pursuit of licenses undermines the argument for the inadequacy of money damages . . .").

licensee's royalty payment obligation following an unsuccessful challenge of the licensed patent by the licensee, in order to reflect the added value of a patent that has been adjudicated as valid. This would be an effective means of establishing a reasonable ongoing royalty, more favorable to the patent holder, in the event that the license agreement is terminated. Suffice it to say at this point that a patent licensor that fails to consider the various possible effects of including an enforceable "termination-for-challenge" clause in its license agreement may be disappointed in the outcome upon exercising its termination right under the provision.

Should a "termination-for-challenge" clause prove to be unenforceable, there is still a question as to whether its inclusion in a patent license agreement would have unintended consequences. There is no basis for concluding that the inclusion of such a provision would void the entire agreement, especially if the agreement contains a standard severability clause that specifies that the validity of the remaining provisions of the agreement are not affected by an unenforceable provision.⁵⁸³ Moreover, it is unlikely that the inclusion of a "termination-for-challenge" clause would constitute patent misuse, rendering the licensed patent unenforceable against infringers. To the authors' knowledge, no court has specifically addressed this issue.⁵⁸⁴ However, as discussed in the preceding section, the relevant case law suggests that the inclusion of a typical "no-challenge" clause in a license agreement is not patent misuse, and it would be difficult to argue that the less restrictive "termination-for-challenge" clause would be judged any differently from the perspective of patent misuse.

In the end, a decision by a patent licensor to use a "termination-for-challenge" clause in its license agreement involves a degree of uncertainty that is not likely to be lessened in the near future, but such a decision is probably justified on the basis of the available information. Unlike in the case of a typical "no-challenge" clause, which eliminates one of the protections of the *Lear* doctrine and is almost certainly unenforceable, there is credible support for the

583. See, Brian G. Brunsvold & Dennis P. O'Reilly, *DRAFTING PATENT LICENSE AGREEMENTS*, 205-06 (5th ed. 2004).

584. While the district court in *Bayer AG*, 228 F. Supp. 2d 467, considered whether the inclusion in a patent license agreement of a contract provision that contained a "termination-for-challenge" clause constituted patent misuse, the court ruled that the "termination-for-challenge" portion of the provision was enforceable and, therefore, never reached the question of patent misuse as to that portion of the provision.

enforceability of a “termination-for-challenge” clause.⁵⁸⁵ As noted above, the effect of enforcing a “termination-for-challenge” clause may lead to an unintended result (i.e., that a terminated licensee is permitted to continue to use the patented technology), but such a result can be modified to the licensor’s advantage through the use of a related provision in the agreement (i.e., one that increases the royalty payment obligation of the licensee in the event of an unsuccessful patent challenge). If the “termination-for-challenge” clause proves to be unenforceable, the inclusion of the provision in the patent license agreement appears to present little risk, either from the standpoint of voiding the agreement or rendering the licensed patent unenforceable based on patent misuse. Taken together, the available information supports the view, adopted by an increasing number of patent licensors, that the “termination-for-challenge” clause is an effective counter to the impact of the U.S. Supreme Court’s *MedImmune* decision, and a licensor has little to lose by including such a provision in its license agreements, possibly in combination with other pro-licensor contract provisions (some of which are discussed in the sections of this Part IV that follow).⁵⁸⁶

585. It is noteworthy that European Union competition law recognizes the distinction between a “no-challenge” clause and a “termination-for-challenge” clause. According to the Guidelines on the Application of Article 81 of the EC Treaty to Technology Transfer Agreements (2004/C 101/02) (the “Guidelines”), “[a]ny direct or indirect obligation on the licensee not to challenge the validity of intellectual property rights held by the licensor in the common market [Guidelines ¶ 108(c)],” is excluded from the technology transfer block exemption regulation (TTBER), which exempts agreement provisions from individual assessment of their anti-competitive and pro-competitive effects. According to the Guidelines, “[t]he reason for excluding non-challenge clauses from the scope of the block exemption is the fact that licensees are normally in the best position to determine whether or not an intellectual property right is invalid. In the interest of undistorted competition and in conformity with the principles underlying the protection of intellectual property, invalid intellectual property rights should be eliminated. Invalid intellectual property stifles innovation rather than promoting it. [Guidelines, ¶ 112].” In contrast, “the TTBER does cover the possibility for the licensor to terminate the license agreement in the event that the licensee challenges the validity of the licensed technology. [Guidelines ¶ 108(c)].” As stated in the Guidelines, “[t]he TTBER covers the possibility for the licensor to terminate the license agreement in the event of a challenge of the licensed technology. Accordingly, the licensor is not forced to continue dealing with a licensee that challenges the very subject matter of the license agreement, implying that upon termination any further use by the licensee of the challenged technology is at the challenger’s own risk. [Guidelines, ¶ 113].”

586. For articles that endorse the use of a “termination-for-challenge” clause in patent license agreements, see Taylor, *supra* note 321 and Schlicher, *supra* note 530, at 388.

3. *Royalty payment provisions*

Another type of pro-licensor contract provision that is receiving increasing attention is one that links a licensee's patent validity challenge with its obligation to pay royalties under the license agreement.⁵⁸⁷ This type of provision can vary on the basis of the event that triggers a consequence (e.g., the patent challenge itself as opposed to the failure of the challenge) and the nature of the consequence (e.g., a continuing obligation to pay the agreed-to royalties as opposed to an increase in the royalty amount to be paid by the licensee). At least one variation of this type of provision has been ruled unenforceable in that it eliminated one of the protections of the *Lear* doctrine.⁵⁸⁸ Other variations, however, are likely to be enforceable, especially one that requires an increase in the royalty payment obligation of a licensee whose patent challenge fails, reflecting the added value of a patent that has been adjudicated as valid. As will be discussed below, this last version of a royalty payment provision lacks a punitive element that penalizes a licensee for merely challenging the licensed patent and, when used in conjunction with a "termination-for-challenge" clause, can benefit a licensor whether it elects to terminate the license agreement or not.

The relationship between a patent licensee's right to challenge the validity of the licensed patent and its obligation to pay royalties was originally explored in *Lear*. Recall that the Supreme Court in *Lear* ruled that an express contractual obligation of a licensee to pay royalties "until such time as the 'patent *** is held invalid,'"⁵⁸⁹ effectively requiring the licensee to pay during the pendency of any patent challenge, is unenforceable (the second prong of the *Lear* doctrine). According to the *Lear* Court, such an obligation would encourage a licensor to postpone a final determination regarding the licensed patent's validity and could deter the licensee from bringing the patent challenge in the first place, thereby frustrating the public's interest in eliminating worthless patents. Considering the holding in *Lear*, it is not surprising that a district court in *Bayer AG v. Housey Pharmaceuticals, Inc.*⁵⁹⁰ rejected a royalty payment provision that stated that "LICENSEE agrees to make all payments

587. For articles discussing examples of pro-licensor royalty payment provisions, see McCarthy, (*Part I*), *supra* note 321, at 538 and Schlicher, *supra* note 530, at 384-87 and 389-91.

588. See *Bayer AG*, 228 F. Supp. 2d 467.

589. *Lear*, 395 U.S. at 673.

590. 228 F. Supp. 2d 467.

due under this License Agreement notwithstanding any challenge . . . by LICENSEE . . . to the Licensed Patent Rights, so long as the applicable patent(s) or patent application(s) remain in effect.”⁵⁹¹ As was already discussed in the preceding section, the *Bayer* court concluded that the provision was unenforceable in that it impermissibly eliminated one of the protections of the *Lear* doctrine, but its inclusion in the license agreement was not patent misuse.

The *Bayer* court did not consider the question of whether a licensee that exercises its *Lear*-protected right to withhold agreed-to royalties during the pendency of its patent challenge and, thereby, breaches an unenforceable royalty payment provision such as the one under consideration in the case could have its license agreement terminated by the licensor on the basis of the breach.⁵⁹² This question has already been addressed, however, in our analysis in section IV.B.2. of the conflicting case law relating to a patent licensor’s right to terminate a license agreement in the context of a breach related to a licensee’s patent validity challenge. As discussed in that section, post-*Lear* district court decisions in *Crane*⁵⁹³ and in *Lee*⁵⁹⁴ support the view that the nonpayment of agreed-to royalties associated with a patent challenge is an insufficient basis for the termination of a license agreement, in light of the public’s interest in the early adjudication of patent invalidity. In contrast, the Federal Circuit’s “challenge-but-face-the-consequence” decisions take the position that a breach by a licensee of a contractual provision in the course of bringing a patent challenge can subject the licensee to an unwanted consequence, including the loss of rights under the license agreement, despite the public policy articulated in *Lear*. In *Cordis*,⁵⁹⁵ for example, the Federal Circuit relied on the reasoning of the Second Circuit in *Warner-Jenkinson*⁵⁹⁶ to conclude that the *Lear* decision did not prevent a patent licensor from terminating the right of a licensee

591. *Id.* at 473.

592. Addressing this question in the *Bayer* case was unnecessary from a practical standpoint in that the court’s tacit endorsement of the associated “termination-for-challenge” clause in the agreement under consideration (*see supra* section IV.B.2.) already provided the licensor with a termination right upon the licensee’s patent challenge, irrespective of whether the licensee ceased making royalty payments following the challenge.

593. 356 F. Supp. 733.

594. 476 F. Supp. 361.

595. 780 F.2d 991.

596. 567 F.2d 184.

that had ceased paying royalties due under a license agreement during the pendency of a patent challenge. The Federal Circuit's other "challenge-but-face-the-consequence" decisions are consistent with this position, although in no instance did that court directly consider a contractual provision such as the one in *Bayer* that, on its face, constituted such a blatant attempt on the part of the patent licensor to deprive its licensee of the protection of the royalty payment prong of the *Lear* doctrine.⁵⁹⁷ In the absence of additional guidance, the Federal Circuit's prior rulings on the scope of a patent licensor's termination right must be considered controlling law. A question remains, however, as to whether an unqualified application of Federal Circuit precedent should result in a licensee's loss of rights under a patent license agreement based on its breach of a royalty payment provision that could not be specifically enforced by a court, and whether the U.S. Supreme Court would reject such an outcome as incompatible with the "spirit of *Lear*." Suffice it to say that the potential effect of the inclusion in a patent license agreement of a royalty payment provision that is unenforceable under *Lear* is unclear and that, as in the case of the licensee "no-challenge" clause, the use of such a provision is best avoided.

While a royalty payment provision that eliminates one of the protections of the *Lear* doctrine (such as the one rejected in *Bayer*) is almost certainly unenforceable, assessing the enforceability of other pro-licensor royalty payment provisions presents a greater challenge. For example, one of the provisions that has been suggested in response to the Supreme Court's *MedImmune* decision would require a licensee that brings a patent validity challenge to pay increased royalties.⁵⁹⁸ The U.S. Government, in its *MedImmune* Brief, noted that such a provision could "anticipate and ameliorate the effects of the filing of a declaratory judgment action by a licensee [challenging the validity of the licensed patent]."⁵⁹⁹ However, as stated in the Government's Brief, the enforceability of such a provision "is an open question in light of the strong public

597. While a district court ruling in the *Bayer* case was appealed to the Federal Circuit, the appellate court's review was limited to an interpretation of the scope of 35 U.S.C. § 271(g) in the context of the facts of the case and did not involve an evaluation of the *Housey* contract provision under consideration in this Article. See *Bayer AG*, 340 F.3d 1367. For a more complete discussion of the *Bayer* case, see Server, Mousavi & Love, *supra* note 192, at 90-92, 105, n.195.

598. See Schlicher, *supra* note 530, at 390.

599. Brief for the United States as Amicus Curiae supporting Petitioner, *MedImmune, Inc.*, 549 U.S. 118, at 28.

policy favoring patent challenges as reflected in *Pope* and *Lear*.⁶⁰⁰ A provision that burdens a patent licensee with an unwanted consequence for the mere act of challenging the validity of the licensed patent could be viewed as too much of a disincentive to challenge to be compatible with the “spirit of *Lear*.”

One way to lessen the impact of a pro-licensor contract provision that calls for an increase in a licensee’s royalty payment obligation following a patent challenge is to have the increase triggered only by an *unsuccessful* challenge by the licensee, i.e., one in which the challenged patent is ultimately adjudicated as valid. There is a reasonable basis for such a royalty increase that is not punitive in nature, namely, that a patent that has been adjudicated as valid is of greater value than one that is merely presumed to be valid as a result of its issuance. This additional value has been recognized by the courts in a number of different contexts. For example, the Federal Circuit in *Atlas Powder Co. v. Ireco Chemicals*⁶⁰¹ held that a patent owner seeking a preliminary injunction to prevent an accused infringer from continuing its allegedly infringing actions is likely to make the requisite “clear showing” of probable success on the merits if the patent-in-suit had previously been found to be valid in a prior adjudication involving a third party infringer. In contrast, the mere presumption of validity that attaches to an issued patent is not adequate to support the granting of a preliminary injunction.⁶⁰² Another example, and one that is more germane to the topic of this section, is the Federal Circuit’s recent decision in *Amado v. Microsoft Corp.*⁶⁰³ that considered the appropriate royalty to be paid by an infringer for its ongoing, post-verdict, infringement during a court-ordered stay of an injunction. In this post-*eBay* case, the court concluded that the continued use by

600. *Id.* See also Schlicher, *supra* note 538, at 390 (“A patent owner should also consider a royalty provision under which royalties increase in the event a licensee challenges validity, and regardless of the outcome. Such an increase is more likely to run into *Lear* unenforceability issues.”).

601. 773 F.2d 1230.

602. See Chisum, *Remedies* 20-673, § 20.04[1][c] (“When a patent owner requests a preliminary injunction against infringement, the courts refuse to rely solely on the presumption of validity to establish a probability of success. Rather, the plaintiff must make a strong showing that the patent will likely be upheld as valid and enforceable Such a showing must usually rest upon either (1) a prior adjudication of the patent’s validity in a suit against another party, or (2) a long period of acquiescence by the industry in the patent owner’s rights. Absent prior adjudication or acquiescence, a patent owner may obtain preliminary injunctive relief only in exceptional circumstances.”).

603. 517 F.3d 1353.

an infringer of technology claimed in a patent that had been adjudicated as valid commanded a higher royalty than the reasonable royalty that was to be paid for pre-judgment infringement. In the words of the court,

[t]here is a fundamental difference . . . between a reasonable royalty for pre-verdict infringement and damages for post-verdict infringement. Cf. *Paice LLC v. Toyota Motor Corp.*, 504 F.3d 1293, 1317 (Fed. Cir. 2007) (“[P]re-suit and post-judgment acts of infringement are distinct, and may warrant different royalty rates given the change in the parties’ legal relationship and other factors.”) (Rader, J., concurring). Prior to judgment, liability for infringement, as well as the validity of the patent, is uncertain, and damages are determined in the context of that uncertainty. Once a judgment of validity and infringement has been entered, however, the calculus is markedly different because different economic factors are involved [justifying a post-verdict royalty that exceeds a pre-verdict reasonable royalty]. *See id.* at 1315.⁶⁰⁴

A contractual provision that requires an increase in the royalties owed under a patent license agreement following an unsuccessful patent validity challenge by the licensee is not only likely to be enforceable under *Lear*, but has additional value when used in conjunction with a “termination-for-challenge” clause. As discussed elsewhere in this Part IV, the holder of a patent that has been adjudicated as valid and infringed cannot be certain of obtaining a permanent injunction preventing future infringement in the aftermath of the Supreme Court’s *eBay* decision. Consider the scenario in which (1) a licensor whose patent is challenged by its licensee elects to terminate the license agreement pursuant to a “termination-for-challenge” clause, (2) the patent is ultimately adjudicated as valid and yet (3) the court concludes that a

604. *Id.* at 1361–62. Note that the Federal Circuit in *Amado* distinguished the facts in the instant case from those in *Paice*. In *Amado*, the royalties under consideration were to be paid for post-verdict infringement that had occurred during a court-ordered stay of an injunction. In *Paice*, the royalties to be paid were for post-verdict infringement under circumstances in which the court had concluded that an injunction was not warranted. While this distinction may require that the set of factors to be considered in determining the appropriate royalty in the two situations may differ somewhat, it does not undermine the fundamental point being made by reference to the *Amado* decision in this section, *i.e.*, that a court’s decision that a patent is valid, reducing uncertainty with respect to that issue, increases the value of the patent and supports the patent holder’s demand for increased post-judgment royalties.

permanent injunction preventing future infringement by the former licensee is not warranted but instead requires the payment of ongoing royalties. The presence in the license agreement of a royalty payment provision specifying the increased royalties to be paid by the licensee in the event of an unsuccessful patent challenge provides a reasonable basis for determining the ongoing royalties. In this instance, the royalty payment provision is not operating strictly as intended, in that the language of the provision contemplates that the licensee will pay the increased royalties under a license agreement that has not been terminated by the licensor and remains in effect. However, the increased royalty amount specified in the provision reflects an agreement between the patent holder and its licensee as to the value of the patent after it has been adjudicated as valid, and such amount can serve as a useful data point, favorable to the patent holder, for a court in making its determination of the ongoing royalties to be paid for future infringement of the patent by the former licensee.

A number of other royalty payment provisions have been proposed to account for the increased likelihood of a licensee patent validity challenge following the Supreme Court's *MedImmune* decision,⁶⁰⁵ although to the authors' knowledge none has undergone judicial review where compatibility with *Lear* was at issue. Some of these provisions are intended to maximize a licensor's return on a licensed patent prior to any patent challenge by the licensee (e.g., requiring the licensee to pay a higher royalty from the outset than would otherwise have been sought in the absence of the increased threat of a challenge).⁶⁰⁶ Other provisions are designed to guarantee

605. See Schlicher, *supra* note 530, at 364.

606. *Id.* at 389–90 (“A patent owner, who is not confident that other measures will deter *Lear* and *Medimmune* actions, should license at a rate appropriate for a patent that is certain to be valid, and that will require validity litigation costs to collect This rate is much higher than a rate appropriate to a legal setting free of *Lear* and *Medimmune* [However, a] licensee may not agree to a rate appropriate for a patent certain to be valid. To address this problem, a patent owner may propose that royalties be defined and paid at that rate, and that the patent owner pay back or rebate part of those royalties to the licensee so long as the licensee does not seek a declaratory judgment of invalidity (while paying). Under that approach, if the licensee does not assert a *Medimmune* claim, its effective royalty rate is the lower rate appropriate to the pre-*Medimmune* situation. Once it asserts a *Medimmune* claim, the rebate ends, and the patent owner retains the full royalty, appropriate for the risk that the payment will end if the patent is found invalid. In order to keep the license during a *Medimmune* action, the licensee must continue paying at the appropriate rate. If the patent is found valid, payments continue at the appropriate rate. [paragraphing omitted].”). See also McCarthy, *supra* note 321, at 538 (“A[n] . . . approach for minimizing *Lear* problems is to provide for higher royalties during the beginning of the license term. In this way, the

the continuation of a licensee's royalty payment despite a patent challenge (e.g., making the royalty payment obligation independent of the validity of the licensed patent).⁶⁰⁷ Putting aside the question of whether a licensee would agree to any of these royalty payment provisions, each such provision must be assessed for its enforceability and effect using an approach such as the one suggested in this Part IV. What can be said with respect to all of these provisions is the following: (1) the more punitive the provision, burdening a licensee for merely exercising its *Lear*-protected right to challenge the validity of the licensed patent, the greater the risk of unenforceability, and (2) the possibility that the inclusion of the provision in a patent license agreement constitutes patent misuse must be given careful consideration.

4. *Other pro-licensor contract provisions*

In the aftermath of the U.S. Supreme Court's *MedImmune* decision, patent licensors have been particularly active in crafting pro-licensor contract provisions to account for an increased likelihood of a licensee patent validity challenge. As noted in the introduction to this Part IV, a review of each of these provisions is beyond the scope of this Article and would, of necessity, be incomplete as novel strategies to address licensee patent challenges are regularly being incorporated into patent license agreements. Accordingly, we have proposed an approach to assess the enforceability and effect of any such provision in order to reduce the uncertainty associated with its use. In this section, we simply list a few of the more frequently encountered pro-licensor contract provisions that we have yet to discuss, leaving the assessment of these provisions to the interested reader.⁶⁰⁸

A contract provision that is increasingly popular among patent licensors requires that a licensee that intends to challenge the validity of the licensed patent provide advanced notice to the

patentee tries to ensure his return on the patent before the licensee challenges the patent.").

607. See Schlicher, *supra* note 530, at 385 ("In future licenses, patent owners should obviously define the products on which royalties are payable without reference [to] validity. They should not use the language Genentech used, and should not, as many have, define licensed products as those that would infringe a 'Valid Claim' but for the license Patent owners should also consider defining the products on which royalties are payable without reference [to] the patent." (footnotes omitted) (paragraphing omitted)).

608. For a more extensive list of pro-licensor contract provisions, see Schlicher, *supra* note 530. See also, Treadway, *supra* note 509, at 326-32.

licensor and disclose the basis for the challenge. The following is an example of such a provision:

In the event LICENSEE intends to assert in any forum that any LICENSED PATENT is invalid . . . , LICENSEE will, not less than ninety (90) days prior to making any such assertion, provide to LICENSOR a complete written disclosure of each and every basis then known to LICENSEE for such assertion and, with such disclosure, will provide LICENSOR with a copy of any document or publication upon which LICENSEE intends to rely in support of such assertion. LICENSEE's failure to comply with this provision will constitute a material breach of this Agreement.⁶⁰⁹

A provision of this type will allow for a dialogue between licensor and licensee that may avert a patent challenge and will, if necessary, aid the licensor in its preparation of a defense of its patent.

Other pro-licensor contract provisions are intended to limit the information available to a licensee in its challenge of the licensed patent. For example, a patent license agreement may contain a provision that expressly prohibits the licensee from using any confidential information of the licensor, provided to the licensee under the agreement, in challenging the licensed patent. An even more restrictive provision has been suggested that "requir[es] . . . that the licensee disclose the prior art it knows about before entering the license, and provid[es] . . . that the licensee will have the right to challenge validity in defense to an action for royalties, or as [a] declaratory judgment claim based only on other and closer prior art that the licensee learns of after entering the license."⁶¹⁰

One of the more frequently encountered pro-licensor provisions obligates a licensee that challenges the validity of the licensed patent to pay the patent holder's litigation costs, including attorney's fees, that result from the challenge. Such a provision varies on the basis of whether the licensee's payment obligation attaches irrespective of the success of its challenge or only in the event that the patent challenge fails.⁶¹¹ In endorsing the latter version of the provision, one commentator has opined that "Lear

609. Brunsvold & O'Reilly, *supra* note 583, at 169-70.

610. See Schlicher, *supra* note 530, at 392.

611. *Id.* at 391.

says that the royalty obligation must end when the litigation begins, if the licensee wins on invalidity. If the licensee loses, and the patent is found valid, the licensee (under *Lear* logic) has done nothing of value to anyone, and has wasted the patent owner's money. Therefore, this obligation should be enforceable."⁶¹²

The list of pro-licensor contract provisions, to be used alone or in combination, will grow as creative transactional attorneys continue to grapple with the increased likelihood of a licensee patent validity challenge following *MedImmune*. In the absence of case law confirming the enforceability of such a provision, its inclusion in a patent license agreement will entail a degree of uncertainty. The approach presented in this Part IV to assess the enforceability and effect of any such provision is intended to reduce that uncertainty. In the end, however, a number of pro-licensor contract provisions will fall within a gray zone where a finding of patent misuse is unlikely, but the question of enforceability will remain open until resolved by a court. The licensor inclined to incorporate such a provision will need to be advised as to the risk of unenforceability, which risk increases to the extent that the provision appears to penalize a licensee for a patent validity challenge in a manner and to a degree that is likely to prevent the challenge in the first place, thereby frustrating the important public interest, articulated in *Lear*, in eliminating worthless patents.

V. CONCLUSION

The U.S. Supreme Court's decision in *MedImmune v. Genentech* resolved a jurisdictional question in concluding that the case-or-controversy requirement of Article III of the U.S. Constitution does not require that a patent licensee terminate or be in breach of its license agreement before seeking a declaratory judgment that the licensed patent is invalid. The *MedImmune* Court's elimination of the jurisdictional barrier to a patent validity challenge by a licensee in good standing has been viewed by many as a pronounced shift in favor of the licensee in the balance of rights between licensor and licensee in patent license agreements. In this Article, we addressed the following questions relevant to the efforts of patent licensor's to redress this shift in the balance of rights: Is there a vestige of the doctrine of licensee estoppel to protect a patent licensor from a validity challenge by a licensee in good standing and, if one cannot rely on the doctrine, are explicit contract provisions that prohibit,

612. *Id.*

reduce the incentive for, and/or specify a consequence of, a licensee's challenge of the validity of a licensed patent enforceable?

Answers to these questions are to be found in the holding of, and policy argument articulated in, the U.S. Supreme Court's decision in *Lear v. Adkins*, the Court's controlling precedent regarding the common law doctrine of licensee estoppel. Based on an analysis of the *Lear* case and relevant case law and commentary interpreting the scope of its holding, we concluded that if and when the issue is presented, the U.S. Supreme Court will interpret its prior *Lear* decision as having rejected the doctrine of licensee estoppel without limitations imposed by the particular facts in the case. According to this view, a patent licensee may challenge the validity of the licensed patent even if it neither repudiates nor terminates its patent license agreement and intends to continue to reap the benefits provided pursuant to the agreement. A patent licensor would, therefore, be ill-advised to rely on some vestige of the doctrine of licensee estoppel to prevent its licensee from challenging the validity of its licensed patent. Rather, the concerned licensor should consider introducing explicit contractual provisions in the patent license agreement to account for the increased likelihood of such a patent challenge. However, the licensor must determine which provisions are enforceable and, if not clearly enforceable, which are least likely to give rise to unintended consequences, including a reasonable claim of patent misuse. Provisions that eliminate one of the protections afforded a patent licensee under *Lear* are almost certainly unenforceable when included in a typical patent license agreement and should be avoided. Other pro-licensor provisions, however, may fall within a gray zone where a finding of patent misuse is unlikely, but the question of enforceability will remain open until finally resolved by a court. Such provisions will need to be analyzed on a case-by-case basis to determine the likelihood of their being enforceable and their possible effects, if included in a patent license agreement. Recognizing that a detailed review of each of the various provisions that have been considered by patent licensors is beyond the scope of this Article, we presented an approach to analyze any such provision to reduce the uncertainty associated with its use. We concluded the Article with an application of the approach to a number of representative pro-licensor provisions that are frequently encountered in patent license agreements.
