Navigating Collaborations with Your Competitors: Key Considerations

April 4, 2017

WILMERHALE

Attorney Advertising

WILMER CUTLER PICKERING HALE AND DORR LLP ®

Webinar Guidelines

- Participants are in listen-only mode
- Submit questions via the Q&A box on the bottom right panel
- Questions will be answered as time permits
- Offering 1.0 CLE credit in California and New York*
- WebEx customer support: +1 888 447 1119, press 2

WilmerHale has been accredited by the New York State and California State Continuing Legal Education Boards as a provider of continuing legal education. This program is being planned with the intention to offer CLE credit in California and non-transitional CLE credit in New York. This program, therefore, is not approved for New York newly admitted attorneys. WilmerHale is not an accredited provider of Virginia CLE, but we will apply for Virginia CLE credit if requested. The type and amount of credit awarded will be determined solely by the Virginia CLE Board. Please note that no partial credit will be awarded. Attendees requesting CLE credit must attend the entire program.

Speakers

Belinda Juran
Partner
WilmerHale

Hartmut Schneider
Partner
WilmerHale

Sarah Petty
Partner
WilmerHale

Agenda

- Transaction Considerations
- Antitrust Law
- Litigation Perspectives

Navigating Collaborations with Your Competitors: Key Considerations

Transaction Considerations

WILMERHALE

WILMER CUTLER PICKERING HALE AND DORR LLP ®

I. Transaction Considerations

Strategic considerations

Confidentiality

Development & Commercialization

Financials

IP Rights

Termination

Questions to Consider:

- What is the long-term strategy for the relevant technology space for you? For the counterparty?
- What are you most worried about protecting:
  - If the deal doesn't work out?
  - If it does work out?

Confidentiality

- What should be protected as confidential information?
  - For how long? Are there true trade secrets?
  - Consider IP developed by one party for the other party
- How will it be shared?
- How do you avoid contamination in your other projects?
- Consider:
  - Gatekeeper
  - Residual information
  - Cleanrooms
  - Non-confidentiality agreement

Development Activities

- Understand the other side's capabilities
- Impose diligence obligations
  - Specific timeframes, amount of spend, milestones
  - Objective vs. subjective commercially reasonable efforts standard
- Develop a detailed R&D plan
- Allocate risks through reps and warranties and/or indemnification:
  - IP infringement
  - Product liability

Commercialization:

- Which party will sell the product?
  - Worldwide?
  - Field limitations?
  - Consider pricing arbitrage

Financials:

- How will each party be compensated:
  - R&D costs
  - Milestones
  - Royalties
  - Profit share
- Consider an option rather than an up-front commitment

Intellectual Property Rights:

- Ownership of foreground IP:
  - Based on inventorship/field/Improvements to underlying IP?
  - Does it differ for product-specific vs. platform IP?
- Licenses to background/foreground IP:
  - Purpose
  - Scope
  - Exclusivity
  - Include affiliates' IP?
- Consider possibility of counterparty's bankruptcy and/or failure to perform

Termination

- Termination triggers
  - Breach
  - Convenience
  - Change of control
  - Terminate in whole or in part
- Rights on termination (especially if they can't perform):
  - Tech transfer
  - Licenses
  - Assignment of contracts
  - Regulatory approvals
- Consider non-compete, non-solicitation provisions

Navigating Collaborations with Your Competitors: Key Considerations

Antitrust Law

WILMERHALE

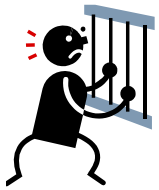
WILMER CUTLER PICKERING HALE AND DORR LLP ®

Antitrust 101

Many different forms of conduct with potential antitrust implications

Some conduct is always ("*per se*") illegal

- Think cartels: price fixing, market allocation, "bid rigging"
- Criminal offenses with large fines and long jail sentences



Other restrictive conduct is subject to the "rule of reason" (or similar tests outside of the U.S.)

- Default rule that applies to the vast majority of cases
- Requires a balancing of pro- and anticompetitive effects
- Often highly fact-specific

Antitrust in Competitor Interactions

Potential Questions

- Do we have to deal with our competitors?

Potential Questions

- What can we do together?
- What restrictions can we impose?
- What information can we exchange?

Potential Questions

- Which acquisitions raise issues?
- Do we have to make merger filings?
- How long will it take?

Good First Questions to Ask

No magic list, but a few basic questions can go a long way

Question	Good	Potential Issues
Why are we doing this?	To deliver better products or services, cheaper and faster	To avoid competition; or difficult to articulate customer benefits
Market share?	Significantly < 30-35%	> 30-35%
Number of competitors?	4 or more	3 or fewer
What's it like to compete in this market?	Constant innovation, many players, price pressure	High barriers to entry, few players, stable market shares
What is in our documents?	Reflect pro-competitive goals, lack of concentration	Emphasize concentration or benefits of elimination of competition
Who might complain?	Market reaction likely neutral or supportive; conduct does not negatively impact customer options	Customers concerned about prices, innovation, or quality; Competitors concerned about access to inputs or distribution channels

Technology Transfer (Licensing)

Virtually always present in collaborations involving technology

- Standing alone, generally procompetitive and subject to the rule of reason
- Extensive agency guidance, e.g. U.S. IP Licensing Guidelines (Jan. 12, 2017); EU Technology Transfer Guidelines and Block Exemption (2014)

Potential issues depend on market conditions and restraint:

Potential Red Flags (e.g.)
Provisions that consolidate IP or divide markets among companies that would have competed using different technologies
Provisions that restrict the parties' ability to exploit their own technology
Provisions that include restraints beyond the scope of patents
Concerted refusals to license (and certain unilateral refusals to license, especially outside of US)
Provisions that set prices or limit output of products made with the licensed technology (standards vary internationally)

R&D Collaborations

Typically subject to the rule of reason and often pro-competitive

- In US and EU, rarely challenged in markets where 3+ comparable independent research efforts remain
- EU Guidelines (and related Block Exemption) provide additional guidance, much of which is also relevant elsewhere

Potential Red Flags (e.g.)
Collaboration combines two of a very small number of promising R&D efforts
Collaboration involves at least one party that has market power in products that may be affected by the R&D efforts
Collaboration "spills over" into unrelated areas where the parties compete (e.g., through information exchanges)
Collaboration restricts independent R&D, especially after termination

Joint Production & Joint Marketing

Can be procompetitive, especially where collaboration combines complementary skills or assets

- E.g., one party has better technology, the other knows how to scale manufacturing
- In the US, “safe harbor” if market shares <20% and agreement is not per se illegal or subject to merger analysis

Potential Red Flags (e.g.)?
Collaboration leads to agreement on output levels or prices downstream
Collaboration is a means to divide markets or allocate customers
Collaboration “spills over” into unrelated areas where the parties compete (e.g., through information exchanges)

Mergers & Acquisitions

Two main questions:

- Is the transaction reportable?
- Does the transaction raise substantive issues?

To File or Not to File

Virtually everywhere in the world, depends on revenues (and sometimes assets or market shares)

- Often a combination of global and local revenue thresholds

The US is an outlier

- Reportability depends mainly on the value of the transaction (currently $80.8M, adjusted annually)
- Acquisition of exclusive licenses can be reportable

Filing typically triggers a two-stage review

- Initial stage of ~1 month to screen for issues
- In-depth review if initial look reveals potential problems

Which Mergers Raise Issues?

Those that “substantially lessen competition in any relevant market”

First questions to ask are the same as above:

Question	Potential Red Flags
Why are we doing this?	To avoid competition; or difficult to articulate customer benefits
Market share?	> 30-35%
Number of competitors?	3 or fewer post-transaction
What’s it like to compete in this market (and what do our documents say about it)?	High entry barriers; stable market shares; no history of entry
What would customers say?	Potential concerns about higher prices, slower innovation, lower quality; or concerns about access to inputs and distribution channels

Competitor Transactions and Documents

Antitrust cases are often built on documents

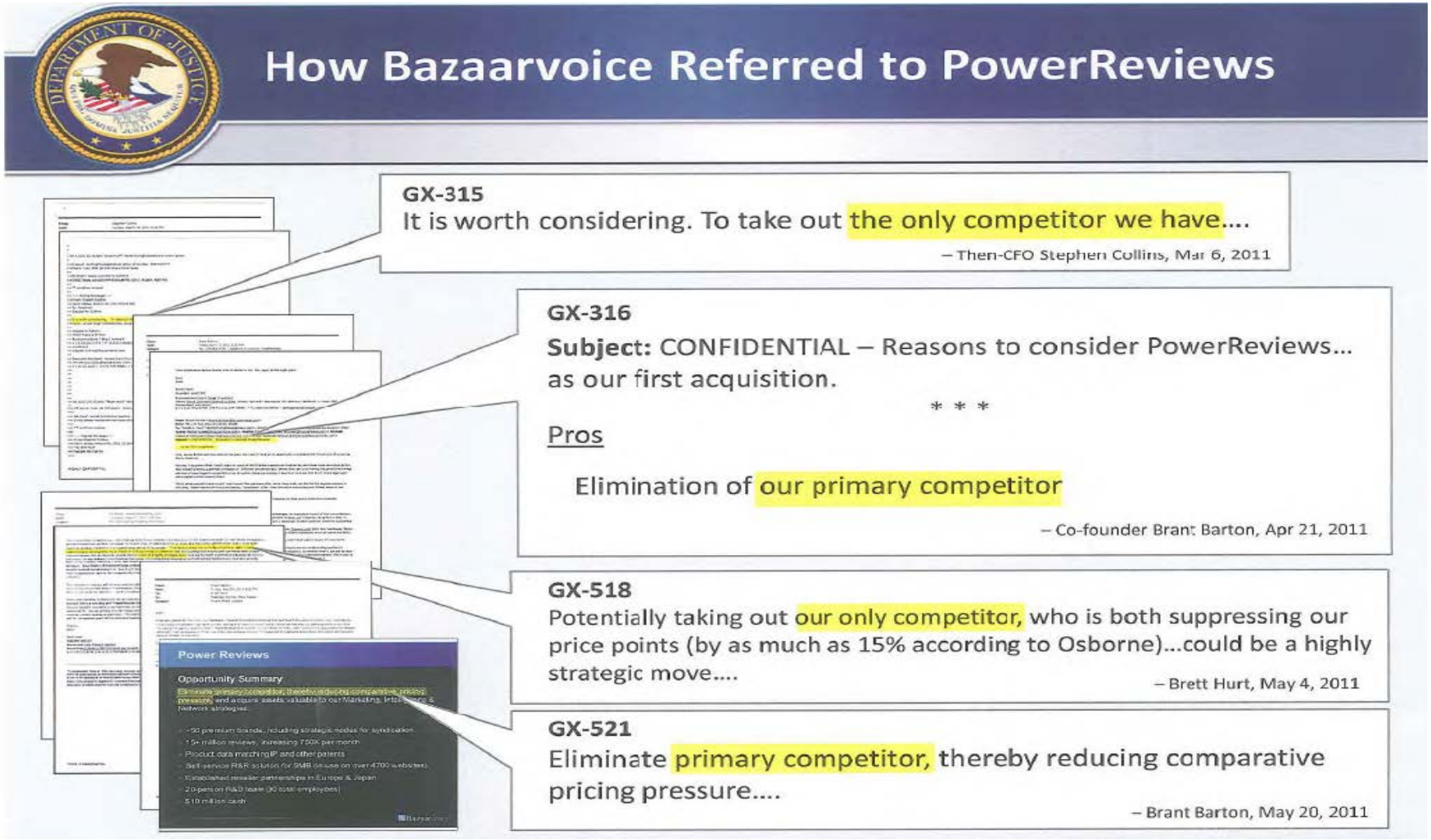
- Agency theory can rest heavily on a small number of “bad” documents

In mergers, US agencies use documents to determine how to approach a new case

- Often the only substantive information in the filing
- Other countries increasingly request documents as well

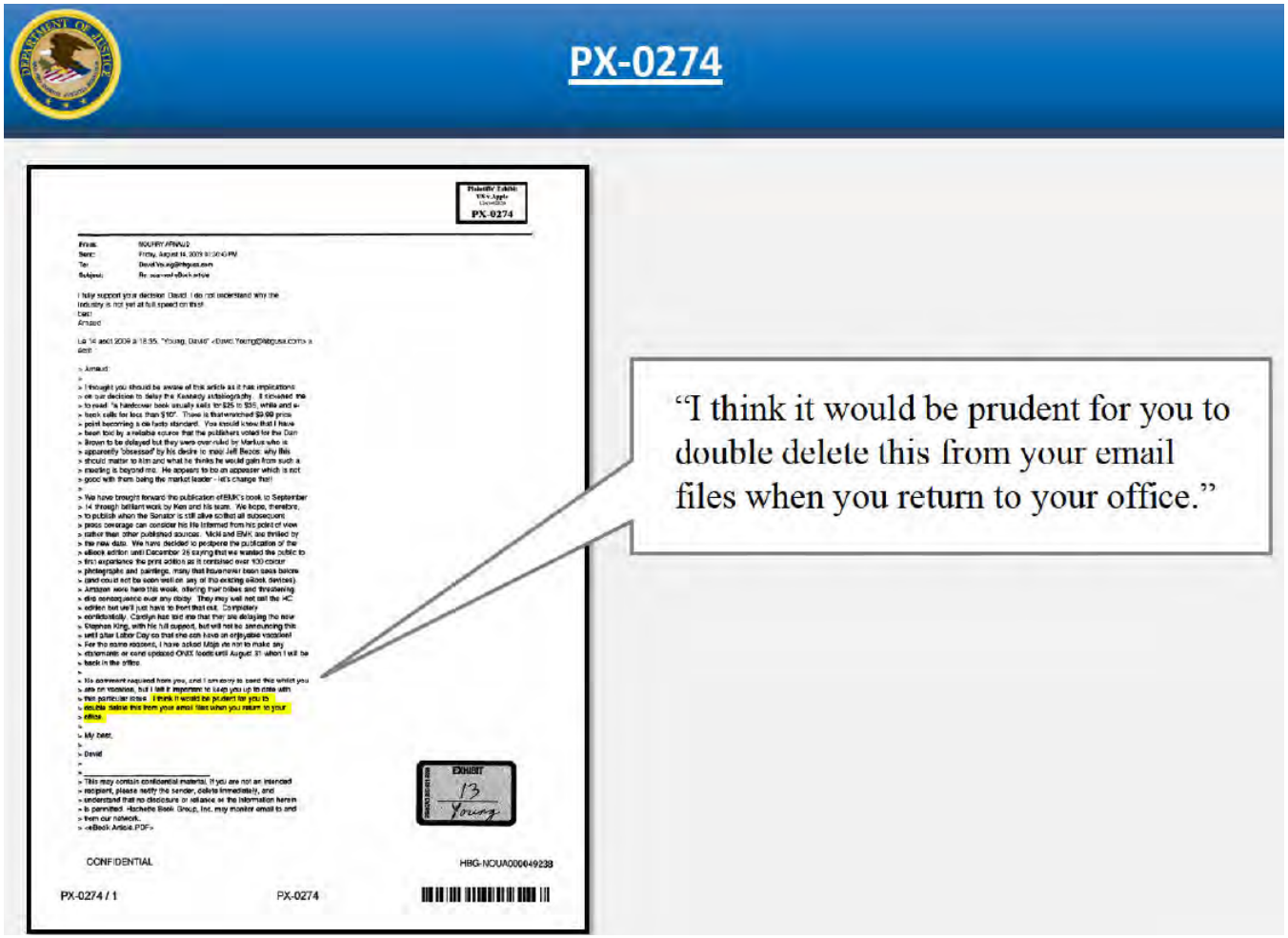
First impressions matter, **everything** is a document, and documents **never** go away!

Not a Good First Impression



Source: US v. Bazaarvoice, Opening Statement Presentation

Documents **NEVER** Go Away!



Source: US v. Apple, Inc., Opening Statement Presentation

Navigating Collaborations with Your Competitors: Key Considerations

Litigation Perspectives

WILMERHALE®

WILMER CUTLER PICKERING HALE AND DORR LLP®

III. Litigation Perspectives

Two scenarios:

A. If the deal falls apart

B. If the deal goes through

A. If the deal falls apart . . .

1. Trade secrets issues
2. Patent issues
3. Potential impact on trial themes

1. Trade Secrets Issues

- Failed deals can often lead to claims for misappropriation of trade secrets down the road.

1. Trade Secrets Issues

- ***Texas Advanced Optoelectronic Solutions, Inc. v. Intersil Corp.*, No. 4:08-cv-451, 2016 WL 1659926 (E.D. Tex. April 26, 2016)** (plaintiff awarded > $48M for trade secret misappropriation following failed acquisition; evidence suggested that defendant used confidential information provided by plaintiff during acquisition negotiations to create a line of products that competed with plaintiff's)

1. Trade Secrets Issues

- ***K-Sun Corp. v. Heller Investments, Inc.,* No. C4-97-2052, 1998 WL 422182 (Minn. Ct. App. July 28, 1998)** (following failed merger discussions between competitors, including allegation that defendant feigned interest in merger to get access to sensitive information, plaintiff prevailed in action for misappropriation of trade secrets and awarded ~ $800K in damages)

1. Trade Secrets Issues

- ***Patriot Rail Corp. v. Sierra R.R. Co*., No. 2:09-CV-0009 TLN AC, 2014 WL 1664898 (E.D. Cal. April 25, 2014)** (following failed acquisition, defendant awarded ~ $22m in counterclaim for misappropriation of trade secrets)

1. Trade Secrets Issues

Defend Trade Secrets Act of 2016

- Signed into law May 16, 2016
- Creates federal cause of action for trade secret misappropriation
- Replaces prior patchwork state-law system under UTSA
  - 18 U.S.C. § 1836 – creates civil cause of action for trade secret misappropriation, conferring original jurisdiction over such claims in U.S. district courts.
  - 18 U.S.C. § 1839 – defines “trade secret” and “misappropriation”
  - 18 U.S.C. § 1836(b)(3)(C)&(D) – provides for “exemplary damages” (up to double) for willful and malicious appropriation

2. Patent Issues

- Impact of failed negotiations on issues requiring notice, intent, and/or awareness of a patent
  - Induced infringement
  - Willfulness
- Impact of failed negotiations on proceedings before the Patent Office

Impact on issues requiring intent and/or knowledge

Failed negotiations are often found to be relevant to issues for which intent and/or knowledge of a patent are at issue – i.e., inducement and willfulness.

- ***PACT XPP Technologies, AG v. Xilinx, Inc.*, No. 2:07-cv-563, 2013 WL 4801885 (E.D. Tex. Aug. 30, 2013)** (affirming finding of willfulness and awarding enhanced damages of > $23M where defendant knew about plaintiff's patent protection and had received confidential information about the patented technology through failed licensing and business negotiations)
- ***WMS Gaming, Inc. v. International Game Technology*, No. 94 C 30262, 1996 WL 539112 (N.D. Ill. 1996)** (finding failed license negotiations and failed acquisition relevant to defendant's willfulness)

Impact on issues requiring intent and/or knowledge

- ***OPTi, Inc. v. VIA Technologies, Inc*., 65 F. Supp. 3d 465, 481 (Aug. 29, 2014)** (finding evidence of failed licensing negotiations relevant to jury's finding of induced infringement) ("It is undisputed that VIA knew of the '906 Patent during the relevant infringement period and engaged in licensing negotiations.")
- ***Fuji Photo Film Co., Ltd. v. Jazz Photo Corp.,* 394 F.3d 1368, 1377–78 (Fed. Cir. 2005)** (upholding jury's finding of intent to induce infringement where the record reflected that defendant was aware of plaintiff's patent as he "twice sought a license from Fuji"; further noting that, "This court has acknowledged the relevance of that kind of evidence supporting proof of intent for inducement.")

Impact on Proceedings before the Patent Office

- Interference proceedings
- Duty to disclose

3. Potential Impact on Trial Themes

- Consider the impact of failed discussions with an adversary on trial narrative

B. If the deal goes through . . .

1. Impact of pending litigation against target company
2. Impact on licensing program
3. Impact on damages issues
4. Impact on trial themes

B. If the deal goes through . . .

1. Impact of pending litigation against target company
   - Are you acquiring a significant liability? Even if parent not directly liable (and such liability is rare for separate corporations), is the target business at significant risk?
   - Does the pending litigation against the target potentially make you/your affiliated businesses targets as well?

B. If the deal goes through . . .

2. Impact on existing licensing program

- Terms of inherited licenses
  - Royalty rates
  - Obligations of parent/affiliated companies
  - Do licenses that the target needed to operate disappear with a change in control?

B. If the deal goes through . . .

3. Impact on damages issues
   - Effect on overall revenues for damages
   - Effect on comparable license analysis

B. If the deal goes through . . .

4. Impact on themes
    - Purchased versus home-grown technology
    - Impact of complex corporate relationships

Questions?

Sarah Petty

Patner, WilmerHale

+1 617 526 6755

Sarah.Petty@wilmerhale.com

Hartmut Schneider

Partner, WilmerHale

+1 202 663 6948

Hartmut.Schneider@wilmerhale.com

Belinda Juran

Partner, WilmerHale

+1 617 526 6987

Belinda.Juran@wilmerhale.com

WilmerHale has been accredited by the New York State and California State Continuing Legal Education Boards as a provider of continuing legal education. This program is being planned with the intention to offer CLE credit in California and non-transitional CLE credit in New York. This program, therefore, is not approved for New York newly admitted attorneys. WilmerHale is not an accredited provider of Virginia CLE, but we will apply for Virginia CLE credit if requested. The type and amount of credit awarded will be determined solely by the Virginia CLE Board. Please note that no partial credit will be awarded. Attendees requesting CLE credit must attend the entire program.