REPRINT

CD corporate disputes

DEALING WITH INTELLECTUAL PROPERTY DISPUTES

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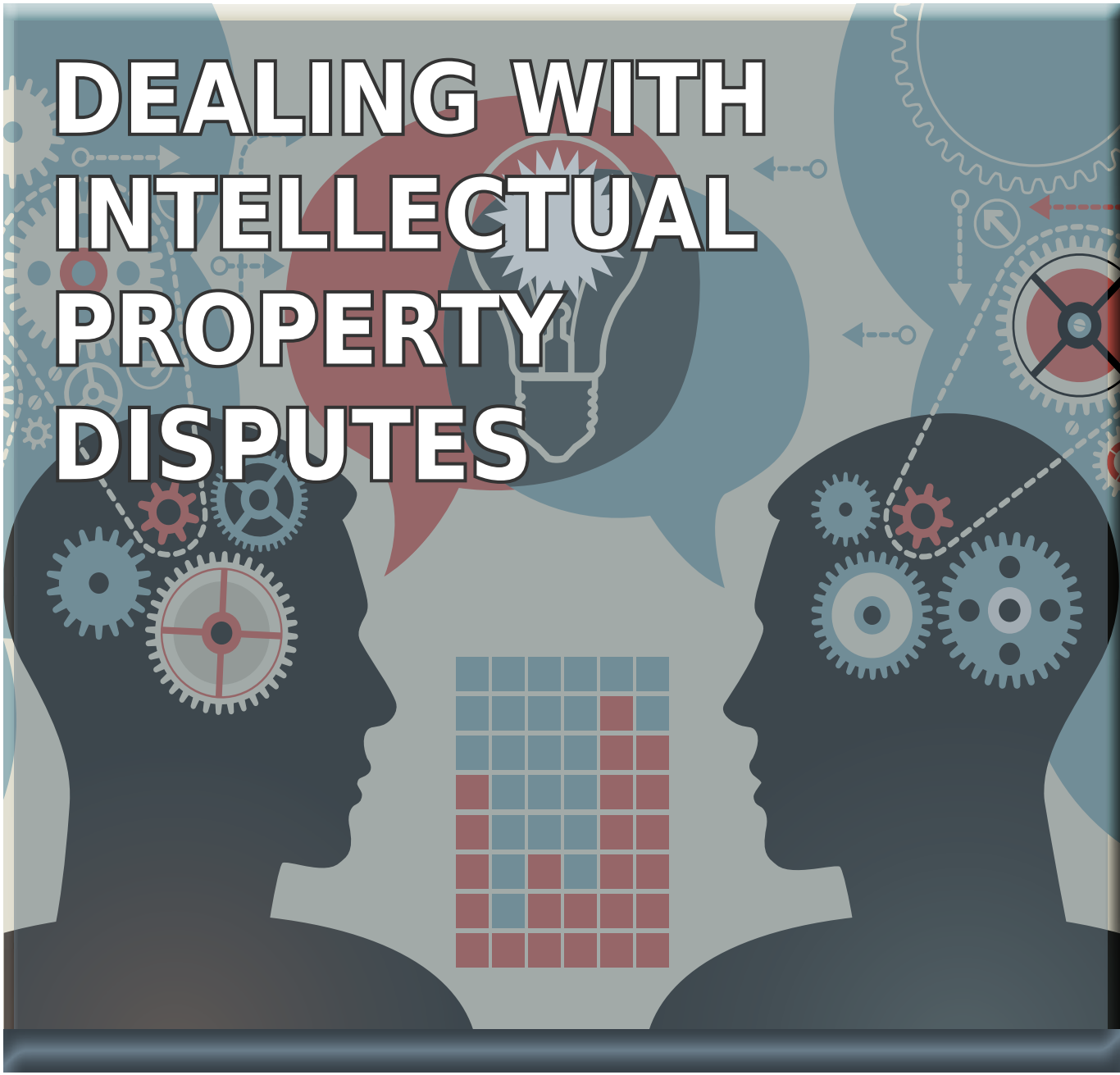

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Arndt Engelmann is a senior manager at PricewaterhouseCoopers AG based in Munich. He advises companies on the management and enforcement of their right portfolios. Mr Engelmann has performed numerous forensic based royalty examinations in different industries and was involved in various in and out of court proceedings evaluating the impact of contract breaches and patent infringements.

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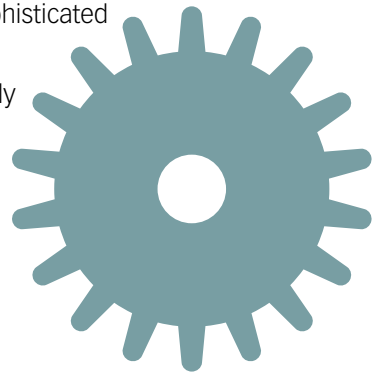
Anthony Dreyer is a commercial litigator concentrating on all aspects of intellectual property litigation. Mr Dreyer has handled a variety of intellectual property matters, including those involving trademark, trade dress, copyright, rights of publicity, false advertising and consumer fraud issues. Mr Dreyer has counselled clients on the protection of their intellectual property rights in the United States and abroad.

CD: In recent years, have you seen a rise in certain types of disputes involving intellectual property (IP)? What are some of the common sources of these conflicts?

Engelmann: There has been a considerable rise in intellectual property disputes over the last couple of years, which is associated with the ongoing financial crisis and the growing interest or need of the owners of IP rights to maximise their benefits. The ongoing importance of the internet and recent technological developments such as the 'Cloud' may also be seen as a reason for the rise of IP disputes. In particular, one can observe a rise of disputes relating to breaches of licensing agreements or the misuse of patents, copyrights and trademarks. However, intellectual property disputes focus on a wide range of matters involving but not limited to patent misuse, predatory pricing, tying, attempted monopolisation, barriers to entry and unfair competition.

Daniel: One of the areas that has seen increased activity involving IP disputes is bankruptcy or restructuring. In instances where IP assets comprise a significant portion of the bankruptcy estate, the valuation of these assets is often contentious. It is necessary for the company and its attorneys to have a thorough understanding about the scope and value of the company's IP, which in turn may provide significant negotiating advantage when deciding whether to retain assets or sell them to creditors, lenders, or other parties.

Dreyer: Just as the dotcom boom of the 90s spawned numerous domain name and search engine-related disputes, technology developments continue to be a principal driver of IP litigation. For example, technology has changed the way we consume media and other content to a mobile and internet-based model. This has given rise to numerous IP disputes, even where the underlying technology itself is not at issue. In particular, video streaming, user-generated content, and social media have created a seemingly unlimited variety of platforms for third parties to use IP rights of others – often without permission. While companies such as YouTube and Facebook struggle to stay ahead of the curve and out of litigation (often unsuccessfully), companies less sophisticated in these issues are finding it increasingly challenging to steer clear of infringement claims as they try



to capitalise on the growth of these new media forms.

CD: Are there any particular sectors that seem to be fuelling the bulk of IP disputes?

Daniel: IP disputes span a vast array of industries, technologies, and sectors – from consumer products to pharmaceuticals, low-tech manufacturing to high-tech electronics. With respect to patents and technology, computers and electrical machinery represent two of the largest segments of patent applications. Not surprisingly, and consistent with this high level of patent activity and robust commercial demand, there have been and will continue to be a significant number of patent disputes in these sectors. It's nearly unavoidable to watch the news or read a business periodical and not see the 'smartphone' wars and patent disputes between Apple, Samsung, Google, Motorola, Microsoft, and other ubiquitous technology companies.

Dreyer: In particular, the aggressive growth of mobile and streaming content providers like Aereo have proven to be a lightning rod for litigation. In a similar vein, as China-based internet and media companies seek to expand their reach outside of their home country, US-based rights holders are seeking to hale these companies before US courts for perceived violations of their IP rights.

Engelmann: IP is increasingly seen as a vital business asset and, therefore, enforcing IP rights to protect competitive advantages or to maximise the economic utilisation of one's own IP rights are important to all sectors. However, according to the case statistics of the World Intellectual Property Organization (WIPO) almost half of all mediation and arbitration cases are patent cases, with the majority involving the information technology industry. The information and communication technology appears to be a major sector for IP disputes as evidenced by the reciprocal claims against each other of

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Apple, Samsung, Motorola or by the recently issued UsedSoft decision, involving Oracle.

CD: What advice would you give to companies on effectively protecting their IP through monitoring potential infringements and enforcing their IP rights? Is undertaking an IP portfolio audit an essential part of the management process?

Dreyer: Whether through a formal IP audit or a more informal process, all rights holders should have a firm understanding of their IP assets, and what needs to be done to maintain those assets. This is particularly true in a global economy, where IP rights can easily be used – and misused – around the world, and where maintaining a worldwide registration and prosecution portfolio can be a full-time job. Filing requirements and filing deadlines can easily be overlooked, leading to the possibility that IP rights will be lost.

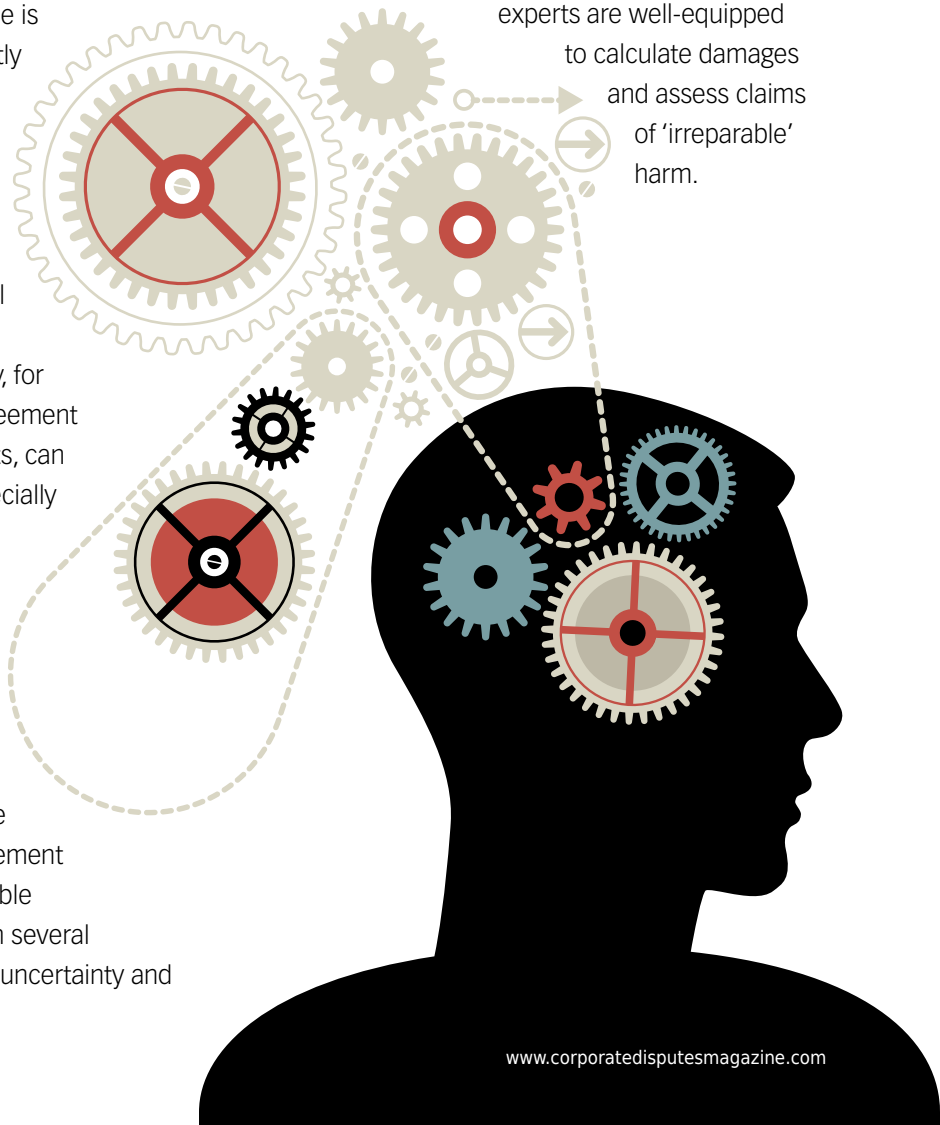
Engelmann: It is fundamental for companies to understand that IP rights are an important part of their business. However, monitoring and protecting IP is a dynamic and demanding process. Few companies have a consistent approach to safeguarding and ensuring the accurate and timely receipt of their licensing revenues. If a company has licensing agreements that are not being monitored and reviewed, it may lose money. In most of the royalty examinations we undertake, we uncover underreported revenues due to clerical errors, accounting mistakes or contract misinterpretation. Over the life of a long-term licensing agreement, the resulting revenue leakage can amount to hundreds of thousands – and in some cases, millions – in lost income. Therefore, an IP portfolio audit should be an essential part of the management process.

Daniel: Policies on IP monitoring and IP enforcement are several elements that may be part of a larger IP strategy and that should also be consistent with the company's business strategy. Conducting periodic IP audits is a useful way to assess the strengths and weaknesses of the IP portfolio and to prioritise and focus company resources in areas requiring immediate attention. A basic IP strategy may include a policy on IP exploitation, IP acquisition or divestiture, and IP development. Depending on the organisational structure, each of these policies may need to be tailored by business unit or geographic region.

CD: To what extent should companies deal with IP disputes quickly before they become expensive distractions or the damage done by an infringer becomes irreparable?

Engelmann: Resolving IP disputes is a difficult process. IP rights are often highly technical, turning the underlying dispute into a time consuming and costly exercise. The owner of the IP right needs to deal with infringements quickly to secure competitive advantages in the market. If the dispute arises, an early assessment of value is essential. Before commencing costly litigation or alternative dispute resolution proceedings, parties need to understand the size of the loss suffered and the expected recovery in order to decide how to deal efficiently with the potential infringement. In some cases early settlement discussions followed by, for example, signing of a licensing agreement or adjustments of existing contracts, can be favourable to both parties, especially when business relationship should be preserved.

Daniel: Companies that can more quickly assess the risks and rewards of potential IP disputes will be in a much better position to efficiently resolve disputes, plan and budget for settlement negotiations, and follow a sustainable IP enforcement strategy. As seen in several recent IP cases, there is increased uncertainty and ambiguity, in the US at least, about whether a patent holder can prevent continuing sales by the infringer. Early identification and dispute resolution offers one way of mitigating this risk and preserving the assets of a company. Of course, in the event that early detection and resolution is not possible, financial experts are well-equipped to calculate damages and assess claims of 'irreparable' harm.



Dreyer: IP disputes, perhaps like no other type of commercial dispute, require immediate care and attention. With in-house staff and litigation budgets stretched thin, we find our clients are often reluctant even to send cease and desist letters unless and until an infringement issue becomes significant enough in scope. Often times, however, the delay in taking action can prove fatal to securing preliminary injunctive relief when the violation ultimately proves to be pernicious. While courts generally are willing to excuse delays of a month, or a few months, longer delays can be devastating to a claim of irreparable harm, and thus fatal to a preliminary injunction. The irony of this, of course, is that securing a preliminary injunction gives a plaintiff tremendous leverage in seeking an early resolution of the case on the merits, well before extensive – and expensive – discovery has occurred. But by delaying seeking relief in an effort to save a little bit of money, a company may be foreclosing a useful avenue to bring about a quick end to a lawsuit.

CD: What are some of the key considerations companies need to make when developing a strategy to resolve IP disputes?

Daniel: Some of the key considerations include estimating and allocating the expected financial resources and time to litigate, assessing the precedent for future licence agreements, and evaluating the long-run implications for the company's business strategy. According to a well-regarded industry survey, the average cost through trial of a patent infringement case in which there is more than $25m 'at risk' is approximately $5m. If an entity is faced with a 'bet the company' litigation involving a core technology, then the time and financial resources required will be less of a factor in deciding to pursue the case. However, other matters may best be dealt with by viewing them as investment decisions, weighing the expected costs and benefits of pursuing litigation, licensing, or alternative means to resolve the dispute. Lastly, all of these decisions should be consistent with the company's long-run business and IP strategy. Not having a focused strategy may lead companies to expend valuable, limited resources unnecessarily.

Engelmann: Companies need to decide on the resolution mechanism to be applied in the case of an IP dispute. This can be agreed upon and included in the respective contractual framework or decided on a case by case basis. According to the case statistics of the WIPO arbitration and mediation centre, most of the arbitration and mediation cases are based on contractual clauses. Another key consideration is the calculation method to be used in case of a claim, for example to ask for a disgorgement of the profits made by the infringer, based on financial information disclosed by the infringer, or to ask for the compensation of damages suffered. This decision

will have a significant bearing on the final award of damages.

Dreyer: A company first needs to understand what its goals are and with whom they are likely to be in litigation. Are they principally a brand owner or rights holder whose disputes will mostly be with infringers? Are there likely to be many small disputes with infringers, or one or two more significant litigations? Will their IP disputes arise mostly over IP licence agreements? Is preliminary injunctive relief important? While many of these issues may seem obvious, it is through understanding the company's larger goals that one can best develop an IP dispute resolution policy.

CD: In what circumstances might alternative dispute resolution be an effective way of dealing with IP disputes? Does the nature and complexity of the underlying issues often lead to litigation?

Dreyer: In the licensing context, where the parties will likely have a continuing relationship after the dispute is resolved, ADR – and in particular, mediation – often makes sense from a cost and expedience standpoint, and may prove less destructive to the parties' ongoing relationship than litigation would be. In the classic IP rights enforcement context, however, ADR seems less suited to resolving disputes, especially those where the question is binary: Can the defendant continue its activity or not? But even in the trademark infringement and false advertising context, ADR forums such as the NAD or mediation can help the parties come to an agreement on modifications to the product or advertising that resolves the plaintiff's concerns while avoiding expensive litigation.

Engelmann: In recent years alternative dispute resolution has been used increasingly to resolve international IP disputes. The general advantages of ADR – neutrality, privacy, flexibility, finality and the enforceability of awards seem to be attractive to many parties together with the interest to protect themselves from the risk of litigation in a language they do not understand or under a law which they are unfamiliar with. ADR may also be the preferred choice if parties want to preserve their business relationships, especially when competitors are facing recurring disputes. In contrast, a company may be looking for precedent or wants to publicly deter other potential infringers. In such cases litigation might be the preferable dispute resolution mechanism.

Daniel: One of the more challenging aspects of IP disputes is being able to understand and properly analyse the technical elements of complex patents or other intellectual property. At times, what can be even more challenging is having to convey technical theories and opinions to a judge or jury that may be exposed to these concepts for the first time

during trial. With arbitration, the parties generally have more input into the selection of arbitrators who are familiar with specific patent or technology issues. Also, parties typically have more freedom to pursue procedural agreements or other conventions as opposed to pursuing a trial verdict. In fact, the potential advantages of arbitration are not limited simply to complex patent disputes but are also attractive in other circumstances, including situations in which the parties have broad product lines or overlapping sales territories.

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CD: Could you describe any recent cases that highlight important aspects of IP disputes?

Engelmann: The news headlines are full of IP disputes indicating increasing public interest, particularly in cases where IP rights relate to consumer products or where the disputing parties have strong and distinguishable brands or trademarks of common knowledge. Recent litigation cases such as *Apple Inc. vs. Samsung Electronics Co.* show the enormous effects of IP dispute judgments. Besides obvious financial and non-financial issues of the defeated party such as decreased sales volumes, reputation and market value and compensation payments, there may be even more significant impacts on customers due to limited product variety, higher retail prices or less innovative products. Therefore, it is important for both parties to consider the effects and to define clear objectives for the dispute and to choose the most efficient and appropriate resolution mechanism.

Daniel: The recent decision in the high-profile and closely followed *Apple v. Samsung* dispute highlights the importance of several key issues for the business and IP communities. The monetary award in excess of $1bn, as well as the strategic implications for IP enforcement and development, are eye-opening for attorneys and businesses alike. The case raises such issues as: How should companies approach dispute resolution in situations where competitors are also key suppliers? How should companies organise design teams

and develop IP strategies to minimise future risk of infringement? Will the ability to disgorge 'total profits' in disputes involving design patents, as opposed to 'apportioned profits' for utility patents, impact the future mix and type of high-stakes cases being litigated? These are difficult questions with no clear answers, but they are certainly questions that corporate boards, directors, and investors will be intently focusing on in the future.

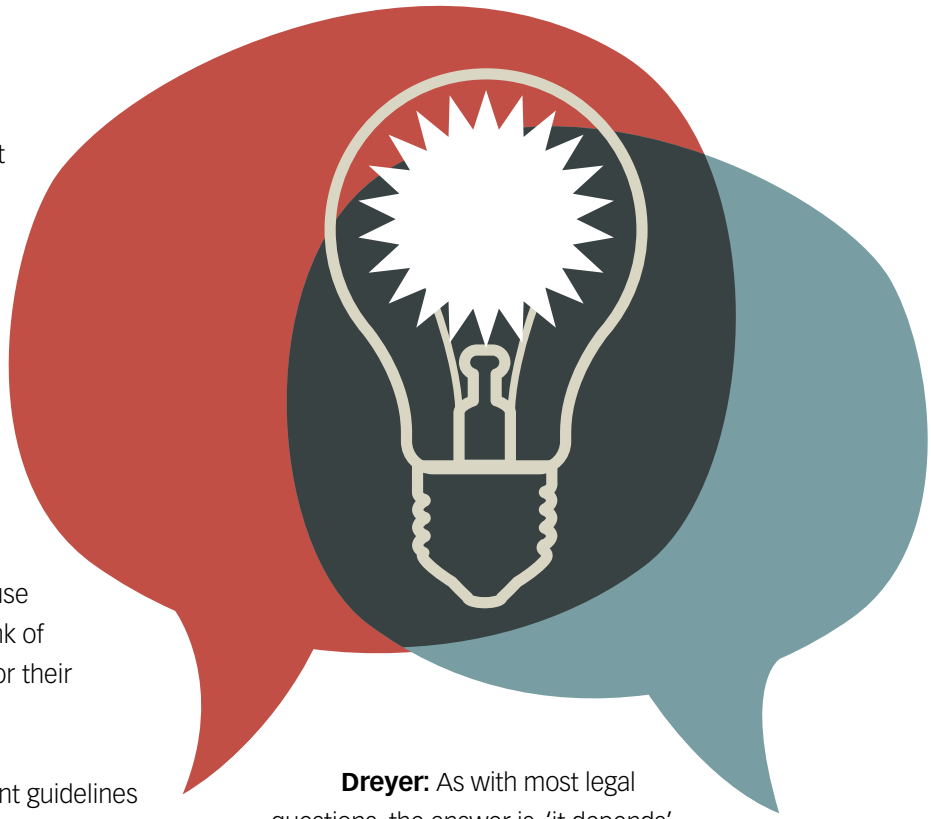
Dreyer: The recent *Aereo* decision out of the Southern District of New York underscores the difficulties courts face in applying traditional IP principles and precedent to new technologies. The court there grappled with broad Second Circuit precedent in the *ComedyCentral/Cablevision* case that involved copying of copyrightable content through ostensibly different technology – personal DVRs – than what is at issue in *Aereo*. Yet the court clearly felt bound to follow the *Cablevision* court's holding and apply it to analogous technologies. The case underscores the struggle that courts often face trying to establish workable precedent in the face of a rapidly changing technology landscape. Another area that continues to work its way through the various circuit courts is the interplay between the right of publicity and the First Amendment. Recently two district courts – one in the Northern District of California, the other in the District of New Jersey – came out on opposite sides of the same legal question: is Electronic Arts' alleged use of collegiate athletes' images protected by the First Amendment, or is it a right of publicity violation. Applying the same legal standards, the New Jersey court found for EA, while the California court rejected EA's First Amendment defence. The cases are now pending in the Third and Ninth Circuits.

CD: Are there any recent or forthcoming legal and regulatory changes that could spark an increase in IP disputes?

Daniel: One area worth mentioning is trademarks and domain names. A recent development involving domain names is the Internet Corporation for Assigned Names and Numbers (ICANN) decision to open up the generic top level domain (gTLD) name space to allow private entities and organisations to own a 'dot. anything' online space. In June, ICANN disclosed that it had received more than 1900 applications for new gTLDs from applicants in 60-plus countries. Even though brand owners have been involved in ICANN's application process, there is still a lot of uncertainty regarding the review and approval process. As a result, this will likely be a very closely followed topic for all brand owners over the coming months.

Engelmann: The recent judgment rendered by the Court of Justice of the European Union in *UsedSoft GmbH vs. Oracle International Corporation* implies certain major legal changes for the software industry. This somehow surprising decision includes some

complex legal requirements that may not be clear and precise to all parties affected by this decision. Leaving space for different interpretation by software producers and vendors may lead to an increase of future IP disputes related to software licensing agreements. Furthermore, existing licensing agreements may need to be reviewed because software producers need to think of new ways to protect and monitor their assets.



Dreyer: I think the FTC's recent guidelines on social media and viral marketing continue to be a source of potential disputes. While many companies that engage in product placement and celebrity endorsements appear to be cognisant of the guidelines, many others either do not seem to be aware of or understand the guidelines – or perhaps simply feel they will not get caught.

CD: What advice would you give to companies on contractual issues surrounding IP rights? What key clauses should be included in contracts to account for the possibility of future disputes arising from an agreement?

Dreyer: As with most legal questions, the answer is, 'it depends'. It depends, for example, on whether you are on the rights holder side or the licensee side. Drafting 101 tells you that as a rights holder, you want the grant of rights to be as specific and narrow as possible, so that you can preserve other rights and markets for yourself or other licensees. If a new media technology is not specified, the rights to exploit IP in that area should be reserved for the licensor. The licensee, of course, should have the opposite objective in mind when drafting the agreement. Moreover, to the extent there is a dispute over who has what rights under the agreement, both parties should want – and try to create a mechanism for – a quick and cost effective resolution of the issue.

For licensees in particular, where a licence may expire in a year or two, the last thing you want is to spend the remainder of the licence term litigating what your rights are under the agreement.

Daniel: I have worked on a number of matters involving disputes from IP agreements that did not anticipate future market changes and used ambiguous language in defining the rights of the parties. It is inevitable that markets, products and end-users change and evolve over time. Clauses dealing with ownership of IP rights and future improvements are one way to deal with this future uncertainty. Additionally, and perhaps more so than including specific clauses, it is important to use simple, clear and precise language and definitions in contracts. While it may not be possible to avoid all future disputes, it is much more cost-effective to draft a thorough agreement that minimises the likelihood, and narrows the scope, of future disagreements.

Engelmann: Business and in this context also IP rights are becoming more and more complex. Therefore, it is important to have clear and precise contract clauses in place that deal with highly technical and legal issues and, in the case of a licence agreement, address the licensor's right to monitor and conduct licensing audits. Licensing is one area where spending some money on preparation and prevention up front can ultimately result in major savings down the road. CD