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Imation v. Philips: Federal Circuit Holds That Patent License Extends to Subsidiaries Acquired After Expiration of License Agreement

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The Federal Circuit held in *Imation Corp. v. Koninklijke Philips Electronics N.V.*[1] that Imation's rights under a cross-license agreement with Philips extend to two subsidiaries that Imation acquired *after* the termination of the agreement. The decision is a reminder of how important it is that license agreements be drafted clearly, carefully, and consistently to avoid unintended consequences of economic significance for the parties.

FACTUAL BACKGROUND

In 1995 Philips and Minnesota Mining and Manufacturing Company (known as "3M") entered into a patent cross-license agreement ("CLA") covering, among other technology, optical disks and drives. It was undisputed that Imation, a spin-off from 3M, succeeded in 3M's rights and obligations under the CLA. The CLA, by its terms, expired on March 1, 2000, but also provided that "any patent license which *has been granted* under [the license provision]" (emphasis added) was to continue, as to each licensed patent, for the life of such patent. In 2003, after expiration of the agreement term, Imation formed a joint venture with Moser Baer India Limited ("Moser Baer") which was called Global Data Media FZ-LLC ("GDM"). Imation owns 51% of GDM and Moser Baer owns 49%. In 2006 Imation also acquired Memorex International, Inc. ("Memorex").

Under the relevant provision of the CLA, Philips "agrees to grant and does hereby grant to [Imation] and its Subsidiaries a personal, non-exclusive, indivisible, nontransferable, irrevocable, worldwide, royalty-free license under Philips Licensed Patents to make, have made, make for others, use, lease, distribute, offer to sell, sell, import, or otherwise dispose of Licensed Products." A "Subsidiary" is defined as any "corporation … or other form of business organization as to which the party *now or hereafter* has more than a fifty percent (50%) ownership interest" (emphasis added).

Both GDM and Memorex commercialize optical storage disk products that are covered by Philips's patents. In 2007 Imation filed a declaratory judgment action seeking, among other things, a declaration that GDM and Memorex are licensed under the CLA as "Subsidiaries" of Imation. To fully understand the background, it is important to note that Moser Baer supplies optical disks to GDM. While Moser Baer has its own royalty-bearing license agreement with Philips, Moser Baer, Imation, and GDM took the position that no royalties are owed to Philips under that agreement because GDM may exercise royalty-free "have made rights" under the CLA with respect to products supplied to it by Moser Baer.

THE DISTRICT COURT'S DECISION

The issue before the district court was whether GDM and Memorex have valid licenses to Philips's patents under the CLA

[1] 586 F.3d 980 (Fed. Cir. 2009).

in light of the fact that they became Imation subsidiaries only *after* the expiration of the CLA. The district court held for Philips. In interpreting the CLA it found that, pursuant to the termination provision, only licenses that "had been granted" survive the expiration of the agreement on March 1, 2000. Because GDM and Memorex were not Imation subsidiaries until 2003 and 2006, respectively, no licenses could "have been granted" to them as of March 2000. Moreover, the court held that GDM and Memorex were not "Subsidiaries" as defined in the CLA because the language "now or hereafter" in the definition of "Subsidiaries" must be read as referring only to the time period up until the expiration of the agreement.

THE FEDERAL CIRCUIT'S DECISION

The Federal Circuit disagreed and reversed. Applying New York law, the court rejected the interpretation of the CLA by the district court. The court concluded that the language in the license grant, wherein Philips "agrees to grant and does hereby grant to [Imation] and its Subsidiaries," constitutes a *present* license grant to a class comprised of Imation and each "Subsidiary," which class may shrink or grow over time as entities become or cease to be "Subsidiaries." Under this "group license" construction, as opposed to the district court's finding of a grant of multiple licenses over time, a single license "had been granted" and vested as of the effective date of the CLA even with respect to future "Subsidiaries."

Secondly, the Federal Circuit found that GDM and Memorex met the definition of "Subsidiaries" under the CLA. It refused to follow the district court's reading that the term "hereafter," without any express temporal limitation, is implicitly limited to the period of time up until the expiration of the CLA. The Federal Circuit reasoned that if the parties had intended to limit the group of "Subsidiaries" to those in existence at a certain time, they could have said so. Instead, the plain language of the relevant provision contains no such explicit temporal limitation, and the court stated that it is "extremely reluctant to interpret an agreement as impliedly stating something which the parties have neglected to specifically include." As additional support for its interpretation, the court pointed to the agreement's definition of "Licensed Patents," which does contain an explicit temporal limitation (*i.e.*, patents now or hereafter owned *and* having a filing date prior to the expiration date). "Where one provision of an agreement contains a particular reference," said the court, "the omission of this reference from any similar provision must be assumed to have been intentional."

As an aside, because "a proper interpretation of a contract generally assumes consistent usage of terms throughout the Agreement," it follows from the court's interpretation of "hereafter" in the "Subsidiary" definition, that the "Licensed Patent" definition[2] also covers patents acquired by a party after the expiration date of the CLA (as long as such patents meet the separate requirement of a filing date prior to the expiration date). Similarly, Philips would be licensed under any patents of GDM and Memorex, as "Subsidiaries" of Imation, that meet the filing date requirement.

CONCLUSION AND LESSONS

The ruling obviously has a significant economic effect on Philips which is not only prevented from recovering royalties from GDM and Memorex, but may also lose royalties from Moser Baer to the extent Moser Baer is now covered by GDM's have made right and therefore does not need to rely on its own royalty-bearing license from Philips.

The decision highlights the significance of fundamental contract interpretation rules that should be remembered when drafting agreements, including the following which the Federal Circuit expressly relied on in reaching its conclusion:

[2] The definition of "Licensed Patents" covers patents which "(1) are owned or controlled by the granting party or any of its Subsidiaries such that such party or its Subsidiaries now has or hereafter obtains the right to grant the licenses within the scope of this Agreement; (2) related to optical or magneto-optical storage and retrieval technology; and (3) have a filing date … on or before the expiration date of this Agreement [*i.e.*, March 1, 2000]."

- a contract will be construed so as to give full effect to its provisions and not render any portion meaningless
- a contract will be read as a whole and be interpreted as to give effect to its general purpose
- courts are reluctant to interpret a contract as impliedly stating something which the parties did not specifically state
- where a provision of an agreement contains a particular reference, the absence of this reference from a similar provision will be assumed to have been intentional
- courts will not adopt an interpretation that renders language in the agreement superfluous
- courts will generally assume consistent usage of terms throughout an agreement

Finally, the decision highlights the importance of clear, careful, and consistent drafting and the need to identify and address potential future problem areas. Specifically, the possibility of future acquisitions and other corporate transactions presents a variety of complex issues that should be addressed in license agreements. These issues include, for example:

- whether future subsidiaries will be licensed and how they are defined
- whether product lines acquired by the licensee through acquisition of a subsidiary or otherwise will be licensed
- whether there will be volume or "organic growth" restrictions with respect to the licensee's products so that volume increases due to an acquisition will not automatically be covered by the license
- whether patents of acquired or acquiring entities will be encumbered by the license granted
- whether licenses can be transferred or extended in connection with the divestiture of product lines, assets, business units, or entities
- whether licenses survive an acquisition of the licensee, and, if so, whether there will be restrictions with respect to the licensed products (such as a limitation to pre-acquisition product lines or models)
- the effects of an acquisition of an entity that is separately licensed (*e.g.*, under different terms that are more favorable to the licensor).

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