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Cutting Edge or Bleeding Edge—Identifying, Avoiding and Allocating Intellectual Property Risks in Adopting New Technology

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I. OVERVIEW

Franchise companies have an inexhaustible appetite for incorporating new technology into business operations in an effort to obtain a strategic advantage over the competition. These new technologies (which often involve some type of intellectual property) range anywhere from electronic billing, mobile pay and order processing systems to mobile apps and software-based loyalty programs, to name a few. Sometimes the technology is developed by the franchisor or franchisee (i.e., an employee of either develops it as part of his or her job) or, other times, a third party vendor or contractor is hired for development.

Although incorporation of new technologies into a franchise can greatly improve the efficiency and performance, enhance the customer experience, and add significant revenue to the bottom line, implementation of such technological advances is not without risks. The unwary may find themselves facing exorbitant license demands or a lawsuit for patent infringement, copyright infringement, or trade secret misappropriation. When these issues arise, what can a franchisee or franchisor do to minimize litigation expenses? Which party bears the risk for infringement claims? Can an indemnification provision play a role in the risk analysis?

Although the specifics of each case must be analyzed by competent counsel, these issues will be explored in the paragraphs below. But first, to provide some context to the discussion, we briefly introduce the forms of intellectual property that exist.

II. INTRODUCTION TO DIFFERENT TYPES OF INTELLECTUAL PROPERTY

A. Patents

A patent is an official, legal grant by the U.S. government (aka limited monopoly) giving the patent owner the right to exclude others for a limited time from making, using, offering to sell, selling, or importing the invention claimed in the patent. Patents are authorized by the U.S. Constitution (Article I, Section 8, Clause 8) for the purpose of promoting “the progress of science and useful arts . . . .” The United States patent statute is the means by which Congress has implemented this provision of the U.S. Constitution.¹

One obtains a patent by filing with the U.S. Patent and Trademark Office (USPTO) an application for a patent. United States utility patents are effective for a period of 20 years from the date the application is filed. Notably, a patent may not actually issue for two or more years following the application filing date. Upon filing an application for a patent, the applicant is entitled to use the phrase “patent pending” on its products covered by the application. Though the applicant does not obtain the right to exclude others until the patent issues, “patent pending” provides competitors notice of potential future rights and starts the clock for any damages that might be recovered later in a patent infringement lawsuit.

¹ U.S. Code Title 35.
1. How are Patents Important?

A patent is a “negative right,” which means it gives the owner the legal right to exclude others from practicing the owner’s patented technology for the term of the patent in any market within the United States. Hence, if a patent covers commercially significant technology, the owner enjoys a commercial advantage until new and better technology is invented or the patent expires. This right could be of extreme importance to a franchise business.

Patents provide the inventor with a time period during which he or she can develop and manufacture the invention and market it without interference from competitors. The patent does not preclude the competition from developing further improvements based on the information provided by the patent, but at least the inventor should be able to prevent competition from a “knock-off,” or equivalent copy, of the patented invention. However, a patent does not give the inventor any affirmative rights. Even if an inventor holds a patent, the inventor may not have a right to practice the invention due, for example, to state or federal law (such as health or safety regulations) or because the invention infringes the claims of another patent.

A patent is unique in intellectual property protection because it can protect the underlying ideas and concept that make the invention useful. As will be discussed below, this is a significant difference between patents and copyrights, which do not protect the underlying idea. Further, it does not matter if a competitor independently develops technology that you have patented. That competitor may not practice the patented technology without being subject to liability for patent infringement. This distinguishes patent rights from trade secrets and copyrights, where independent development is a legitimate defense.

Patents can represent a formidable weapon in the marketplace. In recent years, successful patentees in patent infringement suits have been awarded hundreds of millions of dollars in damages and royalties. Additionally, patents provide a strong deterrent against competitors. For the right price, competitors may opt to license your patented technology rather than spend the time and effort necessary to challenge or design around it. Many companies and individuals thrive on royalties received through patent licensing. Further, cross-licensing of patented technology may prove to be a valuable bargaining chip in the event that a franchisor or franchisee becomes a defendant in an infringement suit.

Patents also offer significant intangible value to a franchise business. Companies often point to their patent portfolio as evidence of their preeminence in a particular industry and the unique competitive advantage of the company. Customers and investors are often affected in their purchasing or investing decisions by the strength of a company’s patent portfolio.

2. What Can Be Patented?

a. Patentable Subject Matter

The patent must be directed to patentable subject matter. Subject matter that can be patented includes “any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof.” Patents generally cover items such as

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machinery, industrial or business processes, electrical and computer goods, chemicals, and ornamental designs. Patents are not generally available for mathematical algorithms or principles of nature.

Patents are, however, available for computer software that implements algorithms and principles of nature. This area of the law is currently in flux. A 2014 opinion by the U.S. Supreme Court states that an inventor may only claim an application of an abstract idea, algorithm, or principle of nature. In *Alice*, the Supreme Court formulated a two-step process for assessing patent-eligible subject matter in the context of computer software inventions. The first step considers whether the claims are directed towards an “abstract idea” as identified by the courts, and if so, the second step requires that the court evaluate the claims to determine whether there is an “inventive concept” sufficient to find that the claims are nonetheless drawn to patentable subject matter.

Whether a patent claim is sufficiently drawn to the application of an abstract idea is still being worked out by the courts. It is clear, however, that simply limiting performance of an abstract idea to a general purpose computer is not sufficient. Nor is it sufficient to attempt to limit performance of the abstract idea to a specific technical environment, such as banking. Thus, simply using a computer to hedge risk in financial instruments is not sufficient to avoid ineligibility. In contrast, claiming the use of an algorithm in an improved computerized method for curing rubber is sufficiently specific to qualify as a patent-eligible application of the abstract idea embodied in the algorithm.

b. The Invention Must Be New

In order to be patentable, the invention must be new and not already in the public domain. It is possible for the inventor’s own invention to fall within the public domain and thereby render the invention “old” under the patent statute. In general, if the invention has been described in a printed publication, sold, offered for sale, or placed in public or commercial use more than one year before filing a patent application, the inventor’s patent rights are barred. Most countries other than the United States are even stricter, requiring that an application be filed before any public disclosure of the invention. In addition, if the invention is invented by another or is the subject of publications or patents filed by another, an inventor may be foreclosed from obtaining a patent.

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4 See *Alice Corp. v. CLS Bank*, 134 S. Ct. 2347 (2014).
5 Id. at 2355.
6 Id. at 2358; *Gottschalk v. Benson*, 409 U.S. 63-64, 67 (1972).
9 35 U.S.C. § 102(b) (2006). One major alteration made by the Leahy-Smith America Invents Act for all patent applications filed on or after March 16, 2013 is the change from a first-to-invent to a first-to-file system. However, under AIA 35 U.S.C. § 102(b)(1)(A), an inventor still has one year from the time he or she discloses an intention in which to file a patent application. This continues the one year grace period practice from the Patent Act of 1952 under the pre-AIA system.
c. The Invention Must Be Useful

The government gives a patent owner an extremely valuable right: a limited monopoly over the claimed invention. In order to make the deal “fair,” the inventor must give society something back: the disclosure of a useful invention. The standard for usefulness is not stringent; rather, to be considered useful, an invention must simply work to achieve its goal and that goal must not be illegal, immoral, or contrary to the public good.10

d. The Invention Must Not Be Obvious

During examination of a patent application, the USPTO will determine whether the invention is obvious in view of information known to the public. The determination of obviousness is generally made using a four-step test:

1. Determine the scope and content of the prior art from information that is publicly available in the field of the invention;
2. Ascertain the differences between the prior art and the claims contained in the patent application; and
3. Resolve the level of ordinary skill in the pertinent art.

To overcome an argument that an invention would have been obvious, it is not necessary to show that the invention represents any particular magnitude of advancement in the art. It is only necessary that the invention not be obvious. In that regard, it is not unusual for relatively small advancements or modifications of the existing art to be entitled to patent protection. For these reasons, it is important to identify patentable inventions and to file promptly for patent protection. It is generally recommended that a patent application be filed before any publication, sale, offer for sale, or public or commercial use of the invention. In this manner, it is possible to preserve United States patent rights and also to maintain the option of pursuing patent protection in most foreign countries.

B. Copyrights

Copyrights protect the particular expression of a thought or idea in the form of words, music, computer software, choreography, pictures, sculptures, audio-visual works, and sound recordings. Unlike patents, copyrights do not protect the idea itself, only the expression of the idea. Further, copyrights do not protect against true independent development by another.

Historically, copyrighted works consisted principally of works of art, such as paintings, songs, and plays. As the information age has matured, however, copyrights have been relied upon to protect other forms of expression such as catalogs, instruction manuals, seminars, computer software, and databases.

1. How Are Copyrights Important?

The copyright statute gives the owner five categories of exclusive rights -- the rights of reproduction, adaptation, public distribution, public performance, and public display. Also

10 Juicy Whip Inc. v. Orange Bang Inc., 185 F.3d 1364, 1366-68 (Fed. Cir. 1999); Lowell v. Lewis, 15 F. Cas. 1018, 1019 (C.C.D. Mass. 1817) (“For instance, a new invention to poison people, or to promote debauchery, or to facilitate private assassination, is not a patentable invention.”).
included in the adaptation right is the right to prepare other works, called “derivative works,” based on the original work. Furthermore, in the case of software programs and sound recordings, the owner has the additional right of restricting the rental of lawful copies. The copyright owner may elect to license others to exercise the rights provided by the copyright.\[11\]

The copyright owner may elect to grant any or all of these rights to others. This is generally done in a contract, such as a license or franchise agreement, which provides for the payment of royalties to the copyright owner.

2. What Is Copyrightable?

The Copyright Act provides that any “original work of authorship” fixed in any “tangible medium of expression” is copyrightable.\[12\] Congress has specifically provided that certain things are not copyrightable. These include “any idea, procedure, process, system, method of operation, concept, principle, or discovery, regardless of the form in which it is described, explained, illustrated, or embodied.”\[13\]

The Copyright Act requires that the work in which a copyright is claimed must be original. Hence, painstakingly repainting the Mona Lisa to produce an exact copy of the original, although requiring a great deal of talent, would not produce a copyrightable work. In contrast, a child’s crayon portrait of the Madonna would be copyrightable.

Virtually all creative works become “fixed in a tangible medium of expression.” Consequently, this element of the statutory test is hardly ever at issue. A painter’s canvas, a piece of paper, a cassette tape, and a compact disc are all examples of a tangible medium. An unrecorded speech, given extemporaneously, would be one example of a work not fixed in a tangible medium of expression, and as such, would not be afforded copyright protection.

The sole exception to the requirement of “fixed in a tangible medium of expression” exists for live musical performances. Under “anti-bootlegging” statutes, live musical performances do not have to be fixed in tangible form to be protected under copyright law. The performer’s consent is required for any fixation of sounds or images during the performance.

Although rights under copyright law come into existence automatically upon creation, there are some limitations to the scope of copyrights and to ownership of copyrights. Three principal limitations are independent development, fair use, and works made for hire. Each such limitation is discussed briefly below.

a. Independent Development

Copyrights protect only from copying. Hence, if someone does not “copy” a copyrighted work, there is no copyright infringement. Although an accused infringing work may be remarkably similar to a copyrighted work, if the accused work was truly developed independently from the copyrighted work, the copyright owner has no recourse under copyright law.

As one might imagine, an accused infringer rarely admits to copying a copyrighted work. As a result, the courts use a two-part test to assist the copyright owner in proving copyright infringement. If a copyright owner can prove that the accused infringer had access to the copyrighted work and that the accused work is “substantially similar” to the copyrighted work, then the courts will infer copying.14

b. Fair Use

The Copyright Act provides that, under certain circumstances, making copies of a copyrighted work constitutes “fair use” and does not require the permission of the copyright owner.15 Congress has specifically provided that reproducing the copyrighted work for “purposes such as criticism, comment, news reporting, teaching (including multiple copies for classroom use), scholarship, or research, is not an infringement of copyright.”16

Unfortunately, determining whether a particular instance of copying constitutes “fair use” can be a highly complex and fact-specific inquiry. Indeed, this is one of the most frequently litigated issues in copyright law.

Congress has set forth four factors to be considered in determining whether copying falls within the fair use exception:

1. The purpose and character of the use: If the purpose for copying was for non-profit use, rather than for a commercial use, fair use is more likely to be found.

2. The nature of the copyrighted work: The fair use exception is more readily available for published works than unpublished works that the author is trying to keep secret. Similarly, fair use is more likely to be applied to factual works than to artistic ones.

3. The amount and importance of the portion used: Fair use is more likely to be found when small, relatively insignificant aspects of the copyrighted work are copied.

4. The effect of the use upon the potential market for or value of the work: This is generally the most important factor. Fair use is more likely to be found if the copying has no commercial effect on the marketability of the copyrighted work.

14 See, e.g., Arica Inst., Inc. v. Palmer, 970 F.2d 1067, 1072 (2d Cir. 1992); see also, e.g., Sid & Marty Krofft TV Prods. v. McDonald’s Corp., 562 F.2d 1157, 1162 (9th Cir. 1977).
16 Id.
Although the fair use analysis depends on the particular facts of the case, a rule of thumb is that if the alleged copy provides a market substitute for the copyrighted work, the copying is not likely to be considered a fair use.17

c. Work Made for Hire

The other primary source of litigation in the copyright field arises out of the “work made for hire” doctrine. Simply stated, the Copyright Act provides that if an employee creates a copyrightable work in the course of employment, the work is considered a “work made for hire” and the copyright is owned by the employer.18 On the other hand, if the creator is not a true “employee” but is really a subcontractor, such as an outside consultant, or if the work is created outside the employee’s scope of employment, the copyright does not belong to the employer.

Many employers are disturbed to learn that after they have paid thousands of dollars to a consultant for the creation of forms, a computer program, or a book, they do not own the copyright to that work. This problem can easily be avoided by entering into a written contract which specifies that the copyright belongs to the employer.19 A verbal agreement is insufficient because the Copyright Act requires that such agreements be in writing.20

3. How is Copyright Protection Obtained?

Unlike a patent, rights are obtained under the Copyright Act automatically upon creation of an eligible work. Once a work becomes “fixed” in a “tangible medium of expression,” rights under the Copyright Act attach.

A copyright notice is no longer required.21 Prior to March 1, 1989, proper copyright notice was a condition for copyright protection. Even minor defects in the copyright notice could result in a loss of rights. Although works created after March 1, 1989 no longer require notice, it is still a good idea to include a copyright notice on all copyrightable works.

Although certain rights accrue automatically, the spectrum of rights under the Copyright Act can only be enforced in litigation through prompt formal registration of the copyright with the United States Copyright Office. In addition to enhanced rights, remedies for copyright infringement are also granted the owner of a registered copyright.22

Registration of a copyright is accomplished by submitting a copyright application along with two copies of the best edition of the work to the United States Copyright Office in Washington, D.C. The Copyright Office reviews the application to ensure that it is complete and

19 Id.
20 Id. at § 201(b).
that the work constitutes copyrightable subject matter. In most cases, the Registration Certificate is issued within two to three months from the filing date of the application.

Generally, copyright protection extends for seventy years beyond the death of the author. If the author of the work is anonymous or is a business entity, then the copyright protection extends for ninety-five years from the year of first publication, or 120 years from the year of creation, whichever expires first.

4. The Digital Millennium Copyright Act

The Digital Millennium Copyright Act\(^{23}\) (DMCA), signed into law in 1998, addresses many emerging issues in copyright law. Only a cursory review of the DMCA is covered in this paper.

One of the primary purposes of the DMCA was to bring United States copyright law into conformity with various worldwide treaties regarding copyright law. To this effect, the copyright law was amended to provide greater protection for original works created outside of the United States.

Another important part of this legislation was directed to technological advancements and their relation to copyrighted material. Without affecting the rights, remedies, limitations, or defenses of traditional copyright law, the DMCA was designed to prohibit devices or services that provide unauthorized access to copyrighted material by circumventing technological measures that served to prevent copyright infringement.\(^{24}\) The anti-circumvention law includes an exception for law enforcement and other governmental activities.\(^{25}\) It also includes limited exceptions for nonprofit libraries, archives, and educational institutions.\(^{26}\) Partial exceptions for reverse engineering, encryption research, protection of minors, protection of personal privacy, and security testing are also included in the DMCA.\(^{27}\) The DMCA also prohibits the removal, alteration, or falsification of Copyright Management Information (CMI).\(^{28}\)

The next major section in the DMCA is designed to further limit the liability of online service providers.\(^{29}\) The liability of service providers is limited for four categories of activity: 1) transitory communications; 2) system caching; 3) storage of information on systems or networks at direction of users; and 4) information location tools.\(^{30}\) Each of these categories is subject to its own rules and qualifications but some aspects are general to all of the limitations. If the service provider qualifies for a limitation, the entity is entitled to a complete bar on monetary damages and the injunctive relief available is also limited in a variety of ways. To qualify for any

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\(^{26}\) Id. at § 1201(d).

\(^{27}\) Id. at § 1201(f)-(j).

\(^{28}\) Id. at § 1202. CMI refers to information such as, for example, the title of a work, its author, its copyright owner, and license terms and conditions.

\(^{29}\) Id. at § 512.

\(^{30}\) Id.
of the limitations on liability, an entity must first qualify as an “online service provider.” This term is defined broadly in the DMCA and most companies with an online presence will qualify. The service provider must meet two additional requirements. It must implement a policy of terminating in appropriate circumstances the accounts of members who are repeat copyright infringers and it must accommodate standard technical measures that are employed to protect copyrights.

The DMCA is the first of what will certainly be many legislative attempts to keep up with rapidly changing technology. It provides for civil and criminal remedies for copyright owners and it is considered by some to be a good effort to balance the rights of copyright owners and users.

C. Trademarks

Most businesses encounter significant trademark questions. The selection of a strong trademark or service mark is a decision that may be critical to your franchise business.

Trademarks are typically words and symbols associated with a company’s goods or services which distinguish them from those manufactured or sold by others. A trademark or service mark must be capable of indicating the source or origin of the goods or services.

1. What Is a Trademark? What Is a Service Mark?

The most familiar trademarks are words and symbols used in association with a company’s goods or services to distinguish those goods and services in the marketplace. It will be helpful to begin with a clarification of the term “trademark.” Trademarks presently are defined under federal law as:

[A]ny word, name, symbol, or device, or any combination thereof. . . [adopted and used by a manufacturer or merchant] . . . to identify and distinguish his or her goods, including a unique product, from those manufactured or sold by others and to indicate the source of the goods, even if that source is unknown.31

Importantly, there is a distinction between a trademark and a trade name. A trade name commonly is a company name used to identify a business, a vocation, or occupation. GENERAL MOTORS is the world-known trade name for a corporation, General Motors Corporation, which manufactures and sells products under trademarks such as CHEVROLET, CORVETTE, OLDSMOBILE, and GMC. CHEVROLET is a trademark that is applied to particular goods (automobiles) which are sold by General Motors Corporation. If a trade name is used in conjunction with goods or services, it may also be a trademark or service mark.

The present definition of a “service mark” under federal law is:

[A]ny word, name, symbol, or device, or any combination thereof. . . [adopted and used by a manufacturer or merchant] . . . to identify and distinguish the services of one person, including a unique service, from the services of others and to indicate the source of the services, even if that source is unknown.32

32 Id.
A service mark serves a similar function as a trademark, except that it is associated with services rather than goods. Service marks such as HERTZ, HOLIDAY INN, McDONALD’S, and SPORT CLIPS illustrate the extent to which service marks are used in the world of franchising.

For convenience, throughout this paper the word “trademark” will be used in its broad sense to embrace both trademarks and service marks.

2. Why Are Trademarks Important?

Trademarks serve as the commercial identifiers symbolizing the goodwill developed in the goods or services of the business. A good trademark can have significant value to a company on the balance sheet as well as enhance a company’s reputation and recognition in the marketplace. Additionally, trademark rights may be enforced against a party who later adopts and uses a mark that when considered in connection with the goods or services offered is likely to cause confusion, or to cause mistake, or to deceive.

Not all words, names, symbols, or devices qualify as trademarks. To be a trademark, the word, name, symbol, or device must be used to identify the goods or services with which it is used and also distinguish those goods or services from those of others. If a mark distinguishes the origin of the goods or services with which it is used from the origin of other goods or services of the same kind, then it is “distinctive.” A mark may be distinctive when used in connection with one product (e.g., RED ROSE on tea) and not distinctive when used on another (e.g., RED ROSE on a rose bush).

A mark may lose its distinctiveness when it becomes the common or generic term for the goods or services. A trademark, even though distinctive in its initial use, may no longer be protected as a trademark after it becomes generic. Many famous trademarks have lost their distinctiveness and become generic terms, including ASPIRIN, THERMOS, SHREDDED WHEAT, ESCALATOR, CELLOPHANE, NYLON, and many others. The owners of the trademarks XEROX, FORMICA, BAND-AID, and KLEENEX, are working very hard to avoid loss of distinctiveness.

3. What Does a Trademark Cover?

Trademarks symbolize the goodwill and reputation of the owner of the mark. Rights under a trademark protect that goodwill and reputation against others using a mark that is likely to cause public confusion regarding the goods or services offered in connection with the mark. Trademark rights are potentially perpetual because they exist for so long as, and to the extent, the mark is used and trademark registrations can be renewed. Almost anything that is capable of distinguishing goods or services from the goods or services of others can serve as a trademark if it is used prominently as an identifier.

4. What a Trademark Does Not Cover

Trademarks do not protect the underlying process, manufacture, or technology of the goods or services bearing the mark. For example, an unpatented tennis racquet bearing a trademark may be copied exactly by a competitor so long as the competitor does not use a confusingly similar mark on the racquet. Trademarks also do not cover generic or commonly descriptive terms. Because trademarks are source identifiers, they should not be used as nouns or verbs.
5. How Are Trademark Rights Protected?

The most common way to protect one’s trademark rights is to obtain a state or federal registration. However, in the United States, even unregistered trademarks are entitled to common law protection.

Common law trademark rights are acquired through usage, and are defined by the geographical area of use and the goods or services with which the trademark is used. Under common law principles, trademark protection normally extends only to the specific areas of actual usage of the mark.

Most states have trademark registration statutes, some of which may offer statewide protection. Usually, the filing procedures are simple and inexpensive. Because the extent of review of most state trademark applications often consists of merely checking the application for form and a quick computer database search, marks that would not ordinarily pass federal registration standards may acquire state registration. Because rights in a trademark flow from its adoption and usage, in most situations a state registration provides little or no substantive rights not already possessed under common law principles. However, a state registration may provide evidentiary presumptions that can assist enforcement of the mark through litigation, and may provide enhanced remedies.

Federal registration of a qualifying mark, on the other hand, can provide the trademark owner with significant benefits. For example, federal registration gives rise to a cause of action in the federal courts for trademark infringement and also access to procedures for stopping importation of goods bearing infringing marks. Perhaps the most valuable benefit of a federal registration is that it affords nationwide constructive notice of the owner’s claim for the exclusive use of the registered mark in connection with its goods or services. Additionally, after a registration has been in effect for five years, the trademark registration may become “incontestable” (i.e., subject to cancellation only upon very limited grounds).

The United States has a dual system for trademark registration under which applications for registration may be filed on the basis of actual use or intent-to-use. An intent-to-use application provides trademark owners the ability to reserve the right to register a mark before making actual use of the mark.

Both intent-to-use and use applications undergo a comprehensive examination in the USPTO. If the trademark examiner, after a search, determines that the mark is distinctive and suitable for registration, the mark is passed through for publication. The mark is then published for the purpose of opposition, allowing members of the public to oppose the mark’s registration if registration would cause injury. If no opposition is lodged, a use application will register while an intent-to-use application receives a notice of allowance. Although allowed, the mark in an intent-to-use application will not register and the applicant will not receive a Certificate of Registration until the applicant has established actual use of the mark in commerce.

34 19 C.F.R. §§ 133.1, 133.22.
37 15 U.S.C. §§ 1051(a), (b).
One of the most significant aspects of the intent-to-use system is that filing of an application constitutes constructive use of the mark for the goods or services identified in the application. The constructive use afforded by statute has some limitations; it is contingent on the mark being registered and fixes the registrant's nationwide priority rights in the mark from the date on which the application was filed.

Trademarks may also be registered in foreign countries. Priority in most countries is based on who was first to file for registration, not on who first used the trademark. Foreign trademark laws also differ from United States law in other important ways, including the marks that may be registered, the procedures and grounds for challenging an application or a registration, and the term of protection.

Another way that certain trademark owners can protect their marks is through the Federal Anti-Dilution Act.\(^{38}\) This act protects against the dilution of a trademark through inappropriate use by others, even without a likelihood of confusion. The act originally defines the term “dilution” as the “lessening of the capacity of a famous mark to identify and distinguish goods or services, regardless of the presence or absence of . . . competition between the owner of the famous mark and other parties, or . . . likelihood of confusion, mistake, or deception.”\(^{39}\)

Dilution occurs primarily in two recognized ways: blurring and tarnishment.\(^{40}\) Blurring is the whittling away of the distinctiveness of a mark by the unauthorized use of the mark on dissimilar products or services. Tarnishment is an unauthorized use of a mark which links the mark to products or services that are of poor quality or which are portrayed in an unwholesome or unsavory context that is likely to reflect adversely upon the trademark owner's product.

The Anti-Dilution Act protects marks that are famous. The factors used to determine whether a mark is famous include:

1. the degree of inherent or acquired distinctiveness of the mark;
2. the duration and extent of use of the mark;
3. the duration and extent of advertising and publicity;
4. the geographical extent of the trading area in which the mark is used;
5. the channels of trade;
6. the degree of recognition of the mark in the trading areas and channels of trade used by the mark's owner and the person against whom the injunction is sought;
7. the nature and extent of use of the same or similar marks by third parties; and
8. whether the owner of the mark has a valid federal registration.\(^{41}\)

Many states have also passed state anti-dilution laws that in most cases parallel the federal law.

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\(^{40}\) 15 U.S.C. § 1125(c).

State trademark registration, federal trademark registration, foreign trademark registration, trade name registration, and Internet domain name registration are related in various ways. But in general, one form of registration is not a substitute for another. Businesses should consult with competent legal counsel to determine which registrations are most advantageous given their goals and other circumstances.

D. Trade Secrets

Trade secrets include information that is not generally known within the trade or industry and that provides a competitive advantage. Trade secrets must be maintained secret. If a trade secret is publicly disclosed, it is no longer a trade secret.

1. How Can Trade Secrets Be Protected?

Trade secret law can be an important tool in protecting information that gives a company its competitive edge. If the information can be kept secret, trade secret protection may be obtained more quickly and at less cost than patent protection. Additionally, trade secrets can cover information, such as client lists and vendor lists, which is not patentable. Trade secret protection may also extend to matter that is not protectable under copyright law, such as ideas, facts, and methods of operation.

2. What Can Be Protected As a Trade Secret?

Unlike patent law and copyright law, trade secret law historically has been governed by state law, and some aspects vary from state to state. Most states, however, have adopted some version of the Uniform Trade Secrets Act.42 That act, like other trade secret laws, protects valuable business secrets against misappropriation by theft, espionage, or other improper means.

Trade secrets are now also protectable under federal law.43 On May 11, 2016 the President signed into law the Defend Trade Secrets Act (DTSA) which defines a trade secret as any information for which “the owner thereof has taken reasonable measures to keep . . . secret”; and that “derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by, another person who can obtain economic value from the disclosure or use of the information.”44 The DTSA provides franchisees and franchisors a private right of action for trade secret claims in federal court. Therefore, any company having a trade secret that is “related to a product or service used in, or intended for use in, interstate or foreign commerce” can now sue in federal court for theft or misappropriation of trade secrets.45 Importantly, the DTSA does not preempt state law claims for theft or misappropriation; therefore, a company may still bring a claim in state court to protect its trade secrets.

42 The Uniform Trade Secrets Act (UTSA) was published by the Uniform Law Commission in 1979 and amended in 1985 as a model for states to adopt. All but two states (New York and Massachusetts) and the District of Columbia have adopted some version of the UTSA.


Information is not protected under trade secret law unless reasonable steps are taken to keep the information secret. What steps are adequate depends on the circumstances. Generally speaking, however, reasonable steps serve to warn those with legitimate access to secrets that they are obligated to maintain the secrecy, and serve to make it difficult (but not necessarily impossible) for others to gain access.

Because patents are public, nothing in a patent application is a trade secret after the patent application is published. However, material in the application may be a trade secret before it is published. Moreover, so long as the best mode for practicing the invention is disclosed in the patent application, certain material which is useful in connection with the patented invention but which is not revealed in or covered by the patent may remain a trade secret even after the patent issues. For instance, the software used to control a piece of patented hardware may be a trade secret even after the hardware patent issues from the USPTO.

3. What a Trade Secret Does Not Protect?

Trade secret law does not prevent competitors from gaining or recreating secret information by legitimate means. Two common legitimate means for gaining trade secret information are independent discovery and reverse engineering. These are commonly asserted defenses to any suit for misappropriation of trade secrets.

Unlike a patent owner, the owner of a trade secret has no recourse against someone who discovers the protected matter independently. For example, an owner of a patent for a process of manufacturing printed circuit boards has a cause of action against someone else who independently discovers and uses the same process. Patent rights can prevent that person or anyone else from using the process, even if that person has never read or even heard of the patent.

By contrast, suppose the process was not patented, but that reasonable steps had been taken to maintain the process as a trade secret. If someone else independently discovered the unpatented process, they can use it. Although in theory trade secrets can last forever, in practice many trade secrets have a limited life. The life span that a trade secret will enjoy is unknown, because one never knows when someone else might discover the secret on their own or through legitimate means.

A holder of a trade secret likewise has no recourse against someone who legitimately obtains the product and extracts its secrets by reverse engineering. For instance, suppose a competitor buys one of the printed circuit boards manufactured using the secret process and is able to learn the secret process by studying the board. The competitor is then permitted to use the process.

Additionally, an employee’s general knowledge or “tools of the trade” cannot be legitimately claimed by an employer as a trade secret. To permit this would unfairly restrict the employee’s freedom to make a living by practicing his or her chosen profession.46

46 Restatement (Second) of Employment Law § 8.02 (“An employer’s information is a trade secret . . . if: (a) it derives independent economic value from being kept secret; (b) the employer has taken reasonable measures to keep it secret; and (c) the information is not (1) generally known to the public or in the employer’s industry; (2) readily obtainable by others through proper means; or (3) acquired by employees through their general experience, knowledge, training, or skills during the ordinary course of their employment.”)
The line between general knowledge and trade secrets is sometimes difficult to draw, but these two examples may help. Sales techniques learned at a national conference open to any business are not trade secrets, while a client list ranked in order of receptiveness to prior promotions probably is a trade secret. Likewise, knowledge of a programming language such as C++ or LISP is a tool of the trade for a computer programmer, but an algorithm devised by another employee for validating passwords may be a protectable trade secret.

Despite these limitations, trade secret protection is often worth preserving. The reasonable steps needed for effective protection can be relatively easy and inexpensive. Moreover, trade secret law may protect matter that is not protected by patent or copyright law. Many valuable secrets are difficult to discover independently, expensive to reverse engineer, or both. Such secrets are worth some measure of protection. Unlike patent or copyright protections, which are administered by the government, the level of protection for trade secrets depends mainly on your ability to keep your valuable information secret.

III. REAL-LIFE SITUATIONS INVOLVING INTELLECTUAL PROPERTY: RISKS AND RESPONSES

A. Patent Infringement Claims

In the past, many business owners have been hit with suits under the Americans with Disabilities Act by plaintiffs claiming that numerous businesses somehow did not comply with the law and requesting a settlement for several thousand dollars from each defendant which collectively resulted in large settlements compared to the value of the case. Although several thousand dollars per defendant is a significant sum to some businesses, it is far less than the costs of litigating the dispute. In the intellectual property area, there have been similar suits by plaintiffs who sue multiple defendants for patent infringement and then offer to settle with each of them for a fraction of what it would cost to litigate the matter but what is collectively far more than the suit is worth.47 For example, eDekka purchased a low value patent and sued over 200 businesses in the Eastern District of Texas. eDekka settled these cases for less than the costs of litigation before the court could rule on the validity or infringement of the patent. Eventually, the court found eDekka’s patent to be invalid (and should not have issued), but not before eDekka had settled over 100 cases, extracting substantial settlement funds on an invalid patent.48 Similarly, plaintiff Eon-Net, LP who had sued multiple defendants for patent infringement was later found to have engaged in extortion-like behavior because Eon-Net had a history of filing nearly identical patent infringement complaints against a plethora of diverse defendants, and then demanding a price for settlement far lower than the cost to defend the litigation but which would have resulted in compensation far more than the value of the patent.48

A franchisee or franchisor who adopts new technology to facilitate improvements or enhancements in business operations could find itself facing a patent infringement suit by a plaintiff seeking to extract a settlement amount that far exceeds the value of the patented technology but which is a fraction of the cost to litigate. Although the specifics of each case must be analyzed by competent counsel, the following paragraphs discuss possible ways a franchisee or franchisor can minimize litigation expenses and avoid extortion-like demands when faced with a patent infringement suit.

47 American Intellectual Property Law Association, Report of the Economic Survey, at 37 (June 2015). The data collected from 2015 indicates that the average total litigation cost for patent infringement suits is typically around $3.1 million when the value of risk was determined to be around $10-$25 million for the parties involved.

1. Minimizing Litigation Expenses in Low-Value Suits from Patent Holders

Two of the most common methods of minimizing litigation expenses are through indemnification and joint defense arrangements. Indemnification means that another party is responsible for paying for, at least, part of the litigation. For example, the seller of a product or service may expressly indemnify the purchaser against legal claims for infringement. There could also be a scenario where the sale of goods gives rise to an implied indemnification under the Uniform Commercial Code. Separately, joint defense arrangements arise where more than one defendant has been sued for infringement and the multiple defendants agree to split defense costs and/or to divide up and coordinate activities.

a. Indemnification

Indemnification occurs where the provider of a good or a service agrees to accept responsibility for harm caused by the good or service. Where possible, a franchisor or franchisee should seek an indemnification agreement for all goods and services provided from a third party. Franchisees should also request that the franchisor provide indemnity for all equipment required by the franchisor.

Sample indemnification language includes:

[Seller/service provider] agrees to defend, indemnify, and hold harmless [Buyer] and its respective affiliates, employees, directors, and consultants against and from any liabilities, claims, actions, or suits arising out of or in connection with (i) [Seller’s] negligence in the conduct of the activities to be performed by [Seller] under this Agreement; (ii) any wrongful acts or omissions of [Seller], its employees, agents, representatives, subcontractors, or invitees; (iii) any harms caused by [Seller’s] product; (iv) any claims alleging that [Seller’s] product infringes the intellectual property rights of others; or (v) [Seller’s] failure to comply with applicable laws and regulations.

There are several key provisions of a typical indemnification agreement that a franchisee or franchisor should be aware of, including prompt notice, control of the litigation, and carve out language—each is explained in turn below.

i. Prompt Notice

Indemnification clauses typically require prompt notice of suit—often within a specific time period, such as 30 days—to the indemnifying party. For example:

This indemnity is conditioned upon an Indemnitee’s notifying Indemnitor of any claim falling within this indemnity within thirty (30) days after the Indemnitee receives notice of such claim.

The primary function served by prompt notice is to set proper reserves covering anticipated losses and to decide whether to exercise the indemnifying party’s right to associate
in the defense of a particular claim. In the instance a court finds that the notice given was not prompt, the party seeking indemnification will not be entitled to it. Where the terms of the contract are ambiguous, reference to extrinsic evidence provides guidance to the parties' intent, which may also include industry custom and practice.

ii. Control of the Litigation

Another aspect is control of the litigation. As the party paying for the litigation, the indemnifying party frequently wants to control selection of counsel and to have the ability to settle the litigation. The indemnified party may wish to retain separate counsel to monitor counsel selected by the indemnifier, and will want to include language that requires that any settlement agreement be reasonable. For example:

[Seller] agrees to defend [Buyer] and its respective affiliates, employees, directors, and consultants against and hold each of them harmless from all third-party claims, damages and liabilities resulting from a claim that any {product/service} provided by [Seller] under this Agreement infringes a United States patent, United States trademark or United States copyright or other United States intellectual property rights or resulting from [Seller's] negligence or willful misconduct or that of its employees, agents and/or representatives; provided that [Buyer] gives [Seller] prompt, written notice of any such claim, sole control of the defense and settlement of such claim, and all reasonable assistance to defend such claim. [Seller] shall not agree to settle the claim without [Buyer's] written consent, provided that such consent is not unreasonably withheld, conditioned or delayed.

Settlement may be a particular concern where there are multiple claims, only some of which may be resolved by the settlement agreement. For example, the buyer may have multiple products or services that are accused of infringing a patent, sourced from different vendors. Depending on the purchase agreements, only some of these vendors may indemnify the buyer, and if the indemnifying vendor settles early in the litigation, the buyer will likely be responsible for the rest of the litigation.

iii. Carve Out Language

Finally, because of the potential expense of infringement suits, indemnification clauses frequently include language carving out intellectual property suits from coverage. The party seeking indemnification will need to review the language of the agreement and, if possible, strike any language omitting intellectual property suits or infringement suits from indemnification coverage.


50 Id. at 578.

b. Implied Indemnification Under the Uniform Commercial Code

Goods sold under the Uniform Commercial Code (UCC) carry an implied warranty against infringement.

UCC Section 2-312(3) states:

Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications.

The paragraphs below discuss this section of the UCC.

i. Implied Warranty of Non-Infringement

The implied warranty in UCC Section 2-312(3) applies only to goods—not to services. Thus, if a franchisor or franchisee is accused of infringing a patent because of a service provided by a third-party, the implied warranty will not apply and an express indemnification agreement is necessary.

Software is not necessarily a “good” under the UCC. Sales of software often include maintenance and support services and are frequently governed by a license agreement where there is no transfer of title. Whether the UCC applies to software contracts that include services and licensing language varies by state, and may turn on whether a court construes the provision of services as ancillary to the sale of software and/or whether the agreement operates to transfer title to the buyer.

The implied warranty applies only to merchants that regularly deal in the type of goods accused of infringement. The implied warranty does not apply where the buyer supplies specifications for the goods. Thus, where an accused product is built to specifications set by the purchaser, there is no indemnification by the seller/builder.

ii. Disclaimer of Implied Warranties

Many sales and purchase agreements include a disclaimer of any implied warranties. For example:

Except as expressly provided in this Agreement, [SELLER] MAKES NO WARRANTIES OR REPRESENTATIONS RELATING TO THE PRODUCT, OR THE SERVICES, EXPRESS OR IMPLIED, AND SPECIFICALLY DISCLAIMS THE WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE.


Where such language is present, there will be no implied warranty of non-infringement. If possible, a buyer should strike such disclaimer language or insert an express warranty.

iii. Privity

Privity of contract generally refers to a connection between the parties to a contract. For example, parties to a contract such as an original seller and a direct buyer are always in privity. Frequently there are many parties in a manufacturing and distribution chain. For example, Company A can manufacture an infringing subcomponent that is distributed by Company B to Company C, who incorporates the subcomponent into a component that it sells to Company D, who incorporates the component into a device that Company E distributes to Company F for retail sale or for use. If Company F is sued for patent infringement, it could bring a claim for breach of the implied warranty of noninfringement against Company E in any state, because it has privity. Company E could then sue Company D, and so on down the chain.

Many states require that a party seeking indemnification be in direct privity with the indemnitor. If the indemnitor has limited resources or has gone out of business, an indemnification clause may be of limited value. In some instances, however, an indemnitee may be able to reach further down the production chain for indemnification without needing to daisy-chain privity. This is an issue of state law and will vary by state.

As an example, the Texas Legislature enacted a version of the UCC where privity for the purposes of establishing indemnification is “left to the courts for their determination.”54 Under this statute, the Texas Supreme Court has held that “privity is not a requirement for a Uniform Commercial Code implied warranty action for economic loss.”55 Thus, under Texas law, a party being sued for infringement can reach back through the manufacturing chain to seek indemnification. In contrast, in California “[t]he general rule is that ‘privity of contract is required in an action for breach of either express or implied warranty and that there is no privity between the original seller and a subsequent purchaser who is in no way a party to the original sale.”56 Thus, a party accused of infringement in California is unlikely to seek indemnification from manufacturers that are not parties to a purchase or supply agreement. As a fallback, where there is an express indemnification clause, an indemnitee should look to see if the upstream agreements include indemnification clauses and may then be able to claim indemnification as a third-party beneficiary of those clauses.

c. Joint Defense Groups and Agreements

When multiple defendants are sued together for common acts of infringement, they might determine it is in their mutual best interests to form a joint defense arrangement to defend allegations of patent infringement. Joint defense arrangements can take different forms, including two or more defendants retaining the same counsel and dividing up the costs of defense; different defendants hiring different counsel and agreeing to divide up which party will handle different aspects of defense; or separately represented parties agreeing to share certain expenses such as expert witnesses.

54 TEX. BUS. & COM. CODE ANN. § 2.318 (West 2015).
55 Nobility Homes of Texas Inc. v. Shivers, 557 S.W.2d 77, 81 (Tex. 1977).
Advantages of joint defense groups include potentially dividing the costs of litigation, receiving a broader consideration of legal issues from the perspective of different counsel, and being able to share some confidential information between counsel for the different defendants.

Disadvantages of joint defense groups include potentially different litigation goals which could negatively impact one party’s case. For example, in the context of patent litigation, if a co-defendant settles with a patentee the co-defendant is unlikely to expend any more time or energy in the suit. This may create a significant concern where different defendants have taken the lead on different aspects of the case. In such a situation, significant knowledge and work-product may be lost when some co-defendants settle but others remain in the litigation. To minimize such difficulties, the joint defense group should put in place a joint defense agreement that explicitly identifies the scope of each member’s participation in the group, and that describes what information each participant will provide to the group and how that information will be shared, and steps for authenticating evidence provided by settling co-defendants.

Another issue to consider in the context of joint defense groups is attorney-client privilege. Because the purpose of attorney-client privilege is to promote full and open discussions between clients and their attorneys without fear of revelation to others, courts have generally construed attorney-client privilege to be waived when “any holder of the privilege, without coercion, has disclosed a significant part of the communication or has consented to the disclosure made by anyone.”57 In the instance that attorney-client privilege is determined to be waived, the opposing party may request that such communications be disclosed and made available to it. However, not all privileged communications are deemed to be waived even when the privilege holder voluntarily and intentionally makes or authorizes a significant disclosure of confidential communications to a third party.

Courts have, however, recognized narrow exceptions where privilege is preserved even when the disclosure of confidential communications is shared with a third party. Such recognized exceptions include the common interest privilege—otherwise known as the joint defense doctrine. The common interest privilege is recognized in federal court and generally by all 50 states, but each state interprets it differently as some states construe it more narrowly than others, thus requiring a closer look at each jurisdiction when considering the applicability of the common interest privilege.

Courts generally do not require a writing to assert the common interest privilege, but it is ordinarily recommended.58 A written document will help the parties meet their burden of proving that such an agreement existed between them.59

2. Other Strategies to Minimize Litigation Expenses and to End Suit

Patent litigation is expensive. Often, the parties engage in a war of attrition with each trying to make the other spend more money, and then using the potential expense to gain

58 See Restatement (Third) of Law Governing Lawyers § 76 cmt. c (“Exchanging communications may be predicated on an express agreement, but formality is no required).
leverage in settlement discussions. In the past few years, however, changes in the law have given defendants accused of infringement new tools to minimize expense and exert settlement pressure on patentees. These changes include a much more favorable legal landscape in which to challenge the subject matter eligibility of a patent (particularly computerized business methods patents often favored by non-practicing entities) and new procedures to ask the United States Patent Office to review the validity of asserted patents. Motions to stay litigation are also another tool in a defendant's arsenal to reduce overall litigation expense and perhaps even end the suit.

a. Ineligible Subject Matter and Motions to Dismiss

Patent eligibility is governed by 35 U.S.C. § 101, which states:

Whoever invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent therefor, subject to the conditions and requirements of this title.

However, courts have created three (3) exceptions to this broad eligibility: “laws of nature, physical phenomena, and abstract ideas.”60 Prior to 2014, courts found relatively few patents were invalid for being drawn to patent ineligible subject matter. However, that year the Supreme Court decided Alice Corp. v. CLS Bank, holding that a computerized business method patent that covered a method of mitigating risk in financial methods was ineligible for being drawn to an abstract idea.61

Since the Alice decision, courts have been very hostile to patents covering computerized business methods. Patents most likely to fall to a challenge under Alice use a computer to perform a pre-existing business method faster or less expensively.62

Unlike most motions attacking the validity of a patent, a defendant can bring a motion to dismiss patent claims as ineligible for patent protection at the very beginning of a case—even before filing an answer. This allows for a significant potential savings in legal expenses if the motion is granted.

When bringing a motion challenging a patent covering an abstract idea, a defendant must first show that the patent claims are directed to an abstract idea. Courts have given little guidance on how to determine or show when patent claims are directed to an abstract idea. And to some degree, every patent claim can be reduced to an abstract principle or a natural law. This only further complicates the abstract analysis, especially since courts have provided

61 Supra note 4.
62 See, e.g., OIP Techs. v. Amazon.com, Inc., 788 F.3d 1359, 62-63 (Fed. Cir. 2015). OIP Technologies asserted a patent claiming a “method of pricing a product for sale” comprising several steps, which also included estimating the likely outcome of various prices based on statistical models and selecting a price based on the estimated outcomes. However, the Federal Circuit decided that the “claims are directed to the concept of offer-based price optimization... which merely recite] conventional computer activities or routine data-gathering steps. See also Intellectual Ventures I LLC v. Mfrs & Traders Trust Co., 76 F. Supp. 3d 536, 545, 551 (D. Del. 2014). The court determined that a patent directed towards electronically managing financial accounts using computer and database technology is essentially an abstract idea, especially since the practice of budgeting is a longstanding and fundamental practice of personal and business finances.
little guidance beyond somewhat extreme examples while additionally pointing out that the court
need not "labor to delimit the precise contours of the 'abstract ideas' category."63

After a challenger has demonstrated a patent claim is directed toward a patent ineligible
abstract idea, the challenger must show that the limitations of the claim do not contain an
"inventive concept." The Federal Circuit has described an inventive concept as claim elements
that limit the scope of the claim to less than the abstract idea as a whole. The Federal Circuit
has also identified an inventive concept as a contribution to the art—i.e., an element new in the
art.64 Notably, “[s]imply appending conventional steps, specified at a high level of generality
[is] not enough to supply an ‘inventive concept.’”65 Nor is limiting the claimed abstract “idea
to a particular technological environment” or claiming a “wholly generic computer
implementation” to practice the abstract idea sufficient to constitute an inventive concept.66

Absent clear guidance from the Supreme Court, the lower courts are finding it difficult to
determine what exactly constitutes an abstract idea and what amounts to an inventive concept
that is patentable subject matter. Indeed, Federal Circuit Judge Chen wrote, “Distinguishing
between claims that recite a patent-ineligible invention and claims that add too little to a patent-
ineligible abstract concept can be difficult, as the line separating the two is not always clear.”67
Given the lack of clarity in the Supreme Court’s Alice decision, the Federal Circuit has
recommended that parties examine its precedent to try to determine whether patent claims may
be directed to ineligible subject matter. A sampling of several recent Federal Circuit decisions
applying the Alice framework are provided below to demonstrate the current state of the law on
this issue.

Digitech Image Technologies, LLC v. Electronics For Imaging, Inc., 758 F.3d 1344 (Fed.
Cir. 2014)

Less than four weeks after the Supreme Court's Alice decision, the Federal Circuit held
patent ineligible claims directed to the use of two data sets to translate digital images between
devices.

Digitech’s claim 1 recites:

A device profile for describing properties of a device in a digital image
reproduction system to capture, transform or render an image, said device profile
comprising:

first data for describing a device dependent transformation of color
information content of the image to a device independent color space; and

second data for describing a device dependent transformation of spatial
information content of the image in said device independent color space.

63 Supra note 4, at 2347.
65 Id. at 1354.
66 Id.
The Federal Circuit noted that claim 1 is “comprised of two sets of data that describe a device dependent transformation” and “[t]he asserted claims are not directed to any tangible embodiment of this information (i.e., in physical memory or other medium) or claim any tangible part of the digital processing system.” The court then cited *Burr v. Duryee*, from 1863, as supporting the proposition that “[t]o qualify as a machine under section 101, the claimed invention must be a concrete thing, consisting of parts, or of certain devices and combination of devices.” Claim 1 did not meet this standard because it recites an intangible arrangement of information, and therefore does not fall into any of the categories of § 101. The Federal Circuit further noted that claim 1 required no physical embodiment at all.

The Federal Circuit also held Claim 10 ineligible. Digitech’s claim 10 reads:

A method of generating a device profile that describes properties of a device in a digital image reproduction system for capturing, transforming or rendering an image, said method comprising:

- generating first data for describing a device dependent transformation of color information content of the image to a device independent color space through use of measured chromatic stimuli and device response characteristic functions;
- generating second data for describing a device dependent transformation of spatial information content of the image in said device independent color space through use of spatial stimuli and device response characteristic functions; and

combining said first and second data into the device profile.

Applying Step 1 of *Alice*, the court held this claim was directed to the abstract idea of “a process of taking two data sets and combining them into a single data set, the device profile.” Applying Step 2, the court stated that “[w]ithout additional limitations, a process that employs mathematical algorithms to manipulate existing information to generate additional information is not patent eligible.” The Federal Circuit held the claimed method was not tied to a physical, tangible device and therefore did not sufficiently limit the scope of the claim to render less than a claim on the abstract idea itself.

*buySAFE Inc. v. Google Inc.*, 765 F.3d 1350 (Fed. Cir. 2014)

In *buySAFE, Inv. v. Google, Inc.*, the Federal Circuit affirmed the ineligibility of patent claims directed to creating a contractual relationship to guarantee performance of an online transaction.

Claim 1 of buySafe’s patent read:

A method, comprising:

- receiving, by at least one computer application program running on a computer of a safe transaction service provider, a request from a first party for obtaining a transaction performance guaranty service with respect to an online commercial transaction following closing of the online commercial transaction;
processing, by at least one computer application program running on the safe transaction service provider computer, the request by underwriting the first party in order to provide the transaction performance guaranty service to the first party,

wherein the computer of the safe transaction service provider offers, via a computer network, the transaction performance guaranty service that binds a transaction performance guaranty to the online commercial transaction involving the first party to guarantee the performance of the first party following closing of the online commercial transaction.

Applying Step 1 of Alice, the Federal Circuit held the asserted claims were directed to the fundamental economic practice of “creating a contractual relationship — a ‘transaction performance guaranty’ — that is beyond question of ancient lineage.” Accordingly, the claims were directed to an abstract idea.

The court next analyzed whether the claims’ recitation of computers constituted an inventive concept under Step 2 of Alice. The Federal Circuit held that merely reciting computer functionality “adds no inventive concept” because the functionality was “generic” in that the “computer receives a request for a guarantee and transmits an offer of guarantee in return” without further detail. Similarly, the Federal Circuit held that limiting the claims to the particular technological environment of “online transactions” did not sufficiently limit the claims to render them patent eligible.

**DDR Holdings v. Hotels.com, 773 F.3d 1245 (Fed. Cir. 2014)**

*DDR Holdings, LLC v. Hotels.com, L.P.* was the first case following *Alice* where the Federal Circuit upheld the validity of computer-implemented patent claims.

Representative claim 19 of the ‘399 patent recites:

“19. A system useful in an outsource provider serving web pages offering commercial opportunities, the system comprising:

(a) a computer store containing data, for each of a plurality of first web pages, defining a plurality of visually perceptible elements, which visually perceptible elements correspond to the plurality of first web pages;

(i) wherein each of the first web pages belongs to one of a plurality of web page owners;

(ii) wherein each of the first web pages displays at least one active link associated with a commerce object associated with a buying opportunity of a selected one of a plurality of merchants; and

(iii) wherein the selected merchant, the outsource provider, and the owner of the first web page displaying the associated link are each third parties with respect to one other;

(b) a computer server at the outsource provider, which computer server is coupled to the computer store and programmed to:
(i) receive from the web browser of a computer user a signal indicating activation of one of the links displayed by one of the first web pages;

(ii) automatically identify as the source page the one of the first web pages on which the link has been activated;

(iii) in response to identification of the source page, automatically retrieve the stored data corresponding to the source page; and

(iv) using the data retrieved, automatically generate and transmit to the web browser a second web page that displays: (A) information associated with the commerce object associated with the link that has been activated, and (B) the plurality of visually perceptible elements visually corresponding to the source page.

The Federal Circuit then discussed the Supreme Court’s precedent and the Alice inquiry, but never actually determined whether the claims were drawn to an ineligible abstract idea. Instead, it noted that distinguishing between a patentable invention and an abstract idea “can be difficult, as the line separating the two is not always clear” and then proceeded to Step 2 of the Alice inquiry.

In its Step 2 analysis, the Federal Circuit noted that even though the claims were drawn to a business method and could be implemented on a generic computer, they did not take a well-known existing business method and merely implement it on a computer. Rather, the claims addressed a technological problem that did not exist outside of the internet environment. That is, “the claimed solution is necessarily rooted in computer technology in order to overcome a problem specifically arising in the realm of computer networks.”

The court further held that the claims improved use of the internet browsing experience by making the browser itself act in a manner different from routine or conventional browsing. The patent claims “address the problem of retaining website visitors that, if adhering to the routine, conventional functioning of Internet hyperlink protocol, would be instantly transported away from a host’s website after ‘clicking’ on an advertisement and activating a hyperlink.” However, the patented invention “overrides the routine and conventional sequence of events ordinarily triggered by the click of a hyperlink,” and thus causes the browser to operate in a manner different from the ordinary use of a computer on the Internet. As a result, the Federal Circuit held the claims were directed to patent-eligible subject matter.

Thus, in this case, the Federal Circuit held that a computer business method patent that does not simply computerize an existing business practice, but instead makes a computer itself operate more efficiently or in an unconventional manner may be patent eligible.

**Ultramercial, Inc. v. Hulu, LLC, 772 F.3d 709 (Fed. Cir. 2014)**

In *Ultramercial, Inc. v. Hulu, LLC*, the Federal Circuit affirmed the district court’s determination that the asserted patent did not claim patent-eligible subject matter.68

68 This was the third time the Federal Circuit had addressed the patent eligibility of Ultramercial’s patent claims. Initially, the Federal Circuit reversed the district court and held the patent claims eligible. The Supreme Court vacated the Federal Circuit’s decision, and remanded for further consideration in light of Mayo Collaborative Services
Claim 1 from Ultramercial’s patent read:

A method for distribution of products over the Internet via a facilitator, said method comprising the steps of:

a first step of receiving, from a content provider, media products that are covered by intellectual property rights protection and are available for purchase, wherein each said media product being comprised of at least one of text data, music data, and video data;

a second step of selecting a sponsor message to be associated with the media product, said sponsor message being selected from a plurality of sponsor messages, said second step including accessing an activity log to verify that the total number of times which the sponsor message has been previously presented is less than the number of transaction cycles contracted by the sponsor of the sponsor message;

a third step of providing the media product for sale at an Internet website;

a fourth step of restricting general public access to said media product;

a fifth step of offering to a consumer access to the media product without charge to the consumer on the precondition that the consumer views the sponsor message;

a sixth step of receiving from the consumer a request to view the sponsor message, wherein the consumer submits said request in response to being offered access to the media product;

a seventh step of, in response to receiving the request from the consumer, facilitating the display of a sponsor message to the consumer;

an eighth step of, if the sponsor message is not an interactive message, allowing said consumer access to said media product after said step of facilitating the display of said sponsor message;

a ninth step of, if the sponsor message is an interactive message, presenting at least one query to the consumer and allowing said consumer access to said media product after receiving a response to said at least one query;

a tenth step of recording the transaction event to the activity log, said tenth step including updating the total number of times the sponsor message has been presented; and

v. Prometheus Laboratories, Inc., 132 S. Ct. 1289 (2012). On its second view of Ultramercial’s patent claims, the Federal Circuit again held the claims patent eligible. The Supreme Court vacated the Federal Circuit’s second decision, and remanded for further consideration in light of Alice Corp. v. CLS Bank International, 134 S. Ct. 2347 (2014). Following this second remand, the Federal Circuit applied the two-part test set forth in Alice and Mayo, and held that Ultramercial’s patent claims were not directed to patent-eligible subject matter.
an eleventh step of receiving payment from the sponsor of the sponsor
message displayed.

Applying Step 2, the Federal Circuit first examined whether the patent claims were
directed to an abstract idea. The court concluded the claim “describes only the abstract idea of
showing an advertisement before delivering free content.” Ultramercial argues that “the addition
of merely novel or non-routine components to the claimed idea necessarily turns an abstraction
into something concrete.” The Federal Circuit rejected this argument as inappropriate to Step 1;
“any novelty in [the] implementation of the idea is a factor to be considered only in the second
step of the Alice analysis.”

Applying Step 2 of the Alice test, the Federal Circuit considered “whether the claims do
significantly more than simply describe [the] abstract method.” The court held that despite the
eleven steps in the claimed method, the additional limitations did not transform the abstract idea
into patent-eligible subject matter because “the claims simply instruct the practitioner to
implement the abstract idea with routine, conventional activity.” Specifically, the additional steps
of updating an activity log, requiring a request from the consumer to view the ad, restrictions on
public access, and use of the Internet were only “‘conventional steps, specified at a high level of
generality,’ which [were] insufficient to supply an ‘inventive concept.’” The court further held that
limiting the use of the abstract idea to a particular technological environment is insufficient to
render a patent claim eligible so mere “invocation of the Internet also adds no inventive
concept.”

Content Extraction and Transmission, LLC v. Wells Fargo Bank, 776 F.3d 1343 (Fed. Cir.
2014)

In this case, the Federal Circuit affirmed that claims from four related patents were
ineligible for patenting.

Claim 1 of the patent read:

A method of processing information from a diversity of types of hard copy
documents, said method comprising the steps of:

(a) receiving output representing a diversity of types of hard copy
documents from an automated digitizing unit and storing information from said
diversity of types of hard copy documents into a memory, said information not
fixed from one document to the next, said receiving step not preceded by
scanning, via said automated digitizing unit, of a separate document containing
format requirements;

(b) recognizing portions of said hard copy documents corresponding to a
first data field; and

(c) storing information from said portions of said hard copy documents
corresponding to said first data field into memory locations for said first data field.

The Federal Circuit described the claimed invention as “a method of 1) extracting data
from hard copy documents using an automated digitizing unit such as a scanner, 2) recognizing
specific information from the extracted data, and 3) storing that information in a memory.”
Applying Step 1 of Alice, the Federal Circuit held the claims were directed to the “well-known”
abstract idea of “1) collecting data, 2) recognizing certain data within the collected data set, and 3) storing that recognized data in a memory.” The patentee argued the claims were not abstract because they involve a scanner, and “human minds are unable to process and recognize the stream of bits output by a scanner.” Nonetheless, the Federal Circuit rejected this argument as merely attempting to limit the claims to a specific technological environment.

Applying Step 2 of the test, the Federal Circuit stated “the asserted patents contain no limitations -- either individually or as an ordered combination -- that transform the claims into a patent-eligible application.” At oral argument the patentee conceded “that the use of a scanner or other digitizing device to extract data from a document was well-known at the time of filing, as was the ability of computers to translate the shapes on a physical page into typeface characters.” The Federal Circuit relied upon this concession to hold the patent claims were not drawn to a patent eligible inventive concept because the “claims merely recite the use of this existing scanning and processing technology to recognize and store data from specific data fields such as amounts, addresses, and dates.”

Internet Patents Corp. v. Active Network, Inc., 790 F.3d 1343 (Fed Cir. 2015)

In Internet Patents Corp. v. Active Network, Inc., the Federal Circuit affirmed the ineligibility of patent claims directed to retaining information on an internet form.

Claim 1 of the asserted patent recites:

A method of providing an intelligent user interface to an online application comprising the steps of:

furnishing a plurality of icons on a web page displayed to a user of a web browser, wherein each of said icons is a hyperlink to a dynamically generated online application form set, and wherein said web browser comprises Back and Forward navigation functionalities;

displaying said dynamically generated online application form set in response to the activation of said hyperlink, wherein said dynamically generated online application form set comprises a state determined by at least one user input; and

maintaining said state upon the activation of another of said icons, wherein said maintaining allows use of said Back and Forward navigation functionalities without loss of said state.

The claimed invention of the patent was a web browser that retained information that had been typed into a web-based form as the user navigated forward and back, even if that form had not yet been submitted or otherwise intentionally saved by the user.

Applying Step 1 of Alice, the Federal Circuit agreed with the district court that claims were drawn to the abstract idea of “retaining information in the navigation of online forms.” The Federal Circuit further noted that the patentee’s proposed interpretation of “maintaining state’ describes the effect or result [and therefore was] dissociated from any method by which maintaining the state is accomplished upon the activation of an icon.”
In Step 2, the Federal Circuit examined the limitations of claim 1 and the dependent claims to determine whether the limitations provided an “inventive concept.” The court held the “additional limitations of these dependent claims do not add an inventive concept, for they represent merely generic data collection steps or siting the ineligible concept in a particular technological environment.” Accordingly, the Federal Circuit held these claims were drawn to ineligible subject matter.

Intellectual Ventures I LLC v. Capital One Financial, 792 F.3d 1363 (Fed. Cir. 2015)

In Intellectual Ventures I, the Federal Circuit affirmed the ineligibility of patent claims of two patents.

A representative claim of the first patent recites:

A method comprising:

storing, in a database, a profile keyed to a user identity and containing one or more user-selected categories to track transactions associated with said user identity, wherein individual users elected categories include a user pre-set limit; and

causing communication, over a communication medium and to a receiving device, of transaction summary data in the database for at least one of the one or more user-selected categories, said transaction summary data containing said at least one user-selected category’s user pre-set limit.

With regard to the first patent, the Federal Circuit held that tracking financial transactions to determine whether they exceed a pre-set spending limit was directed to the abstract idea of budgeting. The court further held that the claimed invention did not claim an inventive concept because the use of a database, a user profile, and a communication medium were generic computer elements and that simply applying an abstract idea to a generic computer does not transform an abstract idea into patentable subject matter.

A representative claim from the second patent recites:

A system for providing web pages accessed from a web site in a manner which presents the web pages tailored to an individual user, comprising:

an interactive interface configured to provide dynamic web site navigation data to the user, the interactive interface comprising:

a display depicting portions of the web site visited by the user as a function of the web site navigation data; and

a display depicting portions of the web site visited by the user as a function of the user’s personal characteristics.

For this claim from the second patent, the Federal Circuit first looked to see whether the claim covered “a fundamental practice long prevalent in our system.” The court noted the claim “relates to customizing information based on (1) information known about the user and (2) navigation data.” The Federal Circuit held that tailoring information based upon user
information, such as a user’s location, is a well-known abstract idea. The Federal Circuit further held that customizing information based upon navigation data, such as when a user viewed certain content, was also a well-known concept from television commercials. Accordingly, the court held the claim was directed to an abstract idea. The court further held the claim lacked an inventive concept because merely adding a computer to increase the speed or efficiency of a process does not make an otherwise ineligible abstract idea patent eligible. The Federal Circuit specifically noted that adding steps to a claim that do nothing more than spell out what it means to “apply [an abstract idea] on a computer” do not confer patent eligibility.

**Versata Development Group, Inc. v. SAP America, Inc.**

In *Versata Development Group, Inc. v. SAP America, Inc.*, the Federal Circuit affirmed a decision by the Patent Trial and Appeal Board (PTAB) that a computerized method for determining the price of a product was drawn to an ineligible abstract idea. Following a Covered Business Method Review challenge, the PTAB applied the *Alice* test and found that Versata’s patent was abstract because it used organizational hierarchies for products and customers to determine a price and that this was essentially an abstract method of calculating. The PTAB further found the claims did not add meaningful limitations to the abstract idea. In particular, the recitation of generic general purpose computer hardware in the claims represented routine, well-understood conventional hardware that failed to narrow the claims. Similarly, the additional claim elements of storing, retrieving, sorting, eliminating, and receiving information were “well-known, routine, and conventional steps” and thus did not provide an inventive application of the abstract concept.

On appeal, the Federal Circuit affirmed the PTAB’s analyses:

[C]laim 17 is directed to a method of determining a price. Claim 27 is directed to a computer-implemented method of determining a price, and claims 26 and 28 are directed to computer-readable storage media comprising computer instructions to implement the methods of claims 17 and 28. Claim 29 is directed to an apparatus for determining a price that includes computer program instructions capable of performing the same method steps recited in claim 27. Using organizational and product group hierarchies to determine a price is an abstract idea that has no particular concrete or tangible form or application. It is a building block, a basic conceptual framework for organizing information, similar to the claims involving collecting, recognizing, and storing data in *Content Extraction* and the claims in *CyberSource*.

The Federal Circuit also agreed with the PTAB that, “after considering the limitations of each claim individually and as an ordered combination, none of the claims have sufficient additional limitations to transform the nature of any claim into a patent-eligible application of an abstract idea.” The computer operations were “purely conventional.” The limitations in the claims “are well-understood, routine, conventional activities previously known to the industry.” And the separate elements of the claims, “when considered as an ordered combination . . . add nothing that is not already present when the steps are considered separately.”

Versata argued that its invention resulted in “fewer software tables and searches, leading to improvements in computer performance and ease of maintenance.” The court would not consider these benefits, because “these supposed benefits are not recited in the claims at issue.” Versata also argued that the PTAB should have considered the commercial success of
the invention. The Federal Circuit rejected this argument stating, that commercial success does not “necessarily indicate that claims were drawn to patent eligible subject matter.

**Mortgage Grader, Inc. v. First Choice Loan Services Inc., 89 F.3d 1055 (Fed. Cir. 2015)**

In *Mortgage Grader, Inc. v. First Choice Loan Services Inc.*, NYLX, Inc., the Federal Circuit upheld a district court finding that patent claims directed to systems and methods for assisting borrowers to obtain loans were ineligible for patenting.

A representative claim reads as follows:

A computer-implemented system for enabling borrowers to anonymously shop for loan packages offered by a plurality of lenders, the system comprising:

- a database that stores loan package data specifying loan packages for home loans offered by the lenders, the loan package data specifying, for each of the loan packages, at least a loan type, an interest rate, and a required borrower credit grading; and

- a computer system that provides:

  - a first interface that allows the lenders to securely upload at least some of the loan package data for their respective loan packages to the database over a computer network; and

  - a second interface that prompts a borrower to enter personal loan evaluation information, and invokes, on a computer, a borrower grading module which uses at least the entered personal loan evaluation information to calculate a credit grading for the borrower, said credit grading being distinct from a credit score of the borrower, and being based on underwriting criteria used by at least some of said lenders;

  wherein the second interface provides functionality for the borrower to search the database to identify a set of loan packages for which the borrower qualifies based on the credit grading, and to compare the loan packages within the set, including loan type and interest rate, while remaining anonymous to each of the lenders and without having to post a request to any of the lenders, said second interface configured to display to the borrower an indication of a total cost of each loan package in the set, said total cost including costs of closing services not provided by corresponding lenders.

The Federal Circuit simplified these patented steps to: a borrower applies for a loan; a third party calculates the borrower's credit grading; lenders provide loan pricing information to the third party based on the borrower's credit grading; and afterwards the borrower discloses its identity to a lender.

The district court had found the asserted claims were directed to the abstract idea of “anonymous loan shopping” and lacked an “inventive concept.” On appeal the Federal Circuit applied the two-step test from *Alice.* In step one, the Federal Circuit agreed the claims were directed to the abstract idea of “anonymous loan shopping.”
In Step 2, the Federal Circuit held that the claims used generic computer components such as an “interface,” “network,” and “database” to perform the patented method, but the claims did not purport to improve the functioning of the computer itself or result in an improvement in a technical field. The Federal Circuit also noted that the claims also do not solve any problem unique to the Internet or to computers, and further held that the simplified steps of the patent could be performed by people without the use of a computer. Accordingly, the patent claims were deemed ineligible.69

Enfish, LLC v. Microsoft Corp., 822 F.3d 1327 (Fed. Cir. 2016)

In Enfish, LLC v. Microsoft Corp., the Federal Circuit reversed a district court’s finding that a patent directed to a method of storing, organizing, and retrieving data was ineligible for patent protection. Thus, in this case, the Federal Circuit not only held that a patent claiming a method of computerized data manipulation was patentable, but also reversed the district court’s finding of ineligibility.

Claim 17 of the asserted patent claims:

A data storage and retrieval system for a computer memory, comprising:

means for configuring said memory according to a logical table, said logical table including:

a plurality of logical rows, each said logical row including an object identification number (OID) to identify each said logical row, each said logical row corresponding to a record of information;

a plurality of logical columns intersecting said plurality of logical rows to define a plurality of logical cells, each said logical column including an OID to identify each said logical column; and

means for indexing data stored in said table.

The Federal Circuit began its analysis by stating that the “claims are not simply directed to any form of storing tabular data, but instead are specifically directed to a self-referential table for a computer database.” This self-referential requirement was found in the “means for configuring” algorithm. The Federal Circuit also noted “that the self-referential table functions differently than conventional database structures.”

Applying the Alice test, the Federal Circuit interpreted the first step as asking “whether the focus of the claims is on the specific asserted improvement in computer capabilities (i.e., the self-referential table for a computer database) or, instead, on a process that qualifies as an ‘abstract idea’ for which computers are invoked merely as a tool.” The Federal Circuit held that claim 17, and the other claims at issue, is focused on “an improvement to computer functionality itself, not on economic or other tasks for which a computer is used in its ordinary capacity.” Based upon this assessment, the Federal Circuit held “that the claims at issue in this appeal are not directed to an abstract idea within the meaning of Alice. Rather, they are directed to a

69 Significantly, from a procedural point-of-view, the Federal Circuit also stated that the existence in the record of dueling expert testimony does not necessarily raise a genuine issue of material fact precluding a finding of ineligibility.
specific improvement to the way computers operate, embodied in the self-referential table.” Based upon this analysis, the court held the claims were not directed to an abstract idea and therefore the court did not need to reach Step 2 of the *Alice* analysis.

The *Enfish* case is the only case where the Federal Circuit held a computer business method claim satisfied Step 1 of the *Alice* test (the *DDR Holdings* Court skipped Step 1 and resolved the issue by holding that the patent satisfied Step 2). This suggests that where a patent claim is directed to a specific limited method improving how a computer itself operates, that claim may be found patent eligible. It should be noted that the scope of the *Enfish* patent was limited in scope to the specific algorithm identified in the specification because the claim was written in means-plus-function form. The case may have turned out differently had the claim been more broadly written.

**In Re: TLI Communications LLC Patent Litigation, 823 F.3d 607 (Fed. Cir. 2016)**

In *In Re: TLI Communications Patent Litigation*, the Federal Circuit upheld a district court finding that patent claims directed to a method of recording and managing digital images was ineligible for patenting.

The representative claim reads:

A method for recording and administering digital images, comprising the steps of:

- recording images using a digital pick up unit in a telephone unit,
- storing the images recorded by the digital pick up unit in a digital form as digital images,
- transmitting data including at least the digital images and classification information to a server, wherein said classification information is prescribable by a user of the telephone unit for allocation to the digital images,
- receiving the data by the server,
- extracting classification information which characterizes the digital images from the received data, and
- storing the digital images in the server, said step of storing taking into consideration the classification information.

The district court found the claims were directed to “the abstract idea of taking, organizing, classifying, and storing photographs.” On appeal, the Federal Circuit applied the two step analysis from *Alice*. In Step 1, the Federal Circuit held the claims were directed to the well-known concept of attaching labels or classification data to images for the purpose of storing the images in an organized way.

In Step 2, the Federal Circuit held the claims merely recited the use of conventional components to perform well-understood conventional activity. The Federal Circuit specifically noted that the patent did not describe a new telephone, a new server, or a new physical combination of the two and described the components in vague and general terms consistent
with their use in the art. Thus, the components acted “exactly as expected according to their ordinary use” and this was not sufficient to transform the abstract idea into a patent-eligible application of that idea.

Viewing these cases as a whole, certain trends have become apparent. First, any time a party asserts a patent broadly claiming a computerized business method, a motion to dismiss for lack of patentable subject matter should be considered. Such a motion can be brought very early in a case and may resolve the litigation with minimal expense either through a judgment or by exerting pressure on the patentee to settle before the court rules on the motion. Second, claims that computerize pre-existing business methods are most susceptible to a patent eligibility challenge. Similarly, claims that use a general purpose computer or the internet to implement an otherwise known business method (or that claim a system using general purpose computers or the internet) are likely to be found ineligible for patenting. Generally, attempting to limit patent claims to a specific technological environment (for example, insurance contracts, or investing) will not render an abstract claim patent eligible. However, as shown by the DDR Holdings and Enfish cases, where a claim is limited to the operation of a computer itself (e.g., a type of computer database) or the an internet browser, and the claim teaches a method of making the database or browser operate more efficiently or differently from the conventional manner, a court may find that the claim is patent eligible. However, this area of the law is still in significant flux with new rulings being issued on a regular basis.

b. New Procedures at the USPTO

In 2012, the America Invents Act (AIA) established new procedures for challenging the validity of a patent before the United States Patent Office. Under the AIA, a person can petition the validity of a patent through a post-grant review proceeding, a covered business method patent review, and/or an inter partes review (IPR). Each of these proceedings have different criteria. A petition for post-grant review can be brought against any type of patent, and can challenge the validity of the patent on any ground, but it must be brought within nine months of issuance of the patent.70 A petition for a covered-business-method review is limited to patents covering financial products or services, can be brought by an entity that has been sued or charged with infringement, and can allege that the patent claims are drawn to ineligible subject matter (as discussed above) or are anticipated or rendered obvious by prior art.71 A petition for an IPR can be brought against any type of patent, can allege that the patent claims are anticipated or rendered obvious by prior art, but must be filed within one-year of service of any complaint alleging infringement.72 Of these different procedures, by far the most common is a petition for an IPR, discussed below.

c. Key Aspects of Inter Partes Reviews

Key aspects of IPRs which distinguish them from district court litigation include: reduced expense as compared to district court litigation; a focused invalidity inquiry with expedited discovery; potential estoppel from arguments that could have been raised in the IPR; and review by a panel of patent judges who are trained in patent law and who do not accord the patent claims a presumption of validity.

71 AIA § 18(a)(1).
Reduced Expense

Patent litigation is among the most expensive types of litigation, typically requiring multiple expert witnesses and attorney’s fees that can easily reach millions of dollars. The IPR process is also expensive, with an initial filing fee of approximately $9,000, and a post-institution fee of an additional $14,000. The cost to prepare the initial petition usually is estimated at around $70,000 - $100,000, and costs through trial at the PTAB can be $300,000 or more. But compared to traditional litigation, this expense is still much less expensive. Furthermore, the parties can reach a settlement while the IPR is pending and resolve both the IPR proceeding and the district court litigation before most of these costs have been incurred.

Focused Invalidity Inquiry with Expedited Discovery

In district court litigation, there are multiple potential defenses an accused infringer can bring. These include:

- whether the patentee has met its burden to prove infringement;  
- whether the patent is drawn to patent eligible subject matter;
- whether the patent lacks novelty because all its elements are already found in a prior art reference;
- whether the patent is obvious in light of the prior art;
- whether the specification properly supports the patent claims; and
- whether the patent claims are indefinite.

In contrast, in an IPR, the PTAB will only focus on whether printed publications in the prior art (e.g., prior art patents or articles) teach enough elements of the patent claims to render the claims anticipated under 35 U.S.C. §102 or obvious under 35 U.S.C. §103. During the IPR, the parties are entitled to conduct limited discovery, including expert depositions, focused on the validity of the patent claims. However, because the IPR is focused on a specific area of invalidity, discovery should be far less burdensome than standard litigation discovery, which would also examine the defendant’s products or services, and revenues and profits generated by the accused products or services. This limited discovery will largely be centered on expert discovery related to the patent claims and should create far less distraction to a defendant’s business than would occur in district court litigation.

The focused invalidity requirement also allows the PTAB to reach a decision on the validity of challenged patent claims more quickly than typically occurs in district court litigation. Patent litigation typically takes two or more years to complete. In contrast, the PTAB must rule

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73 37 CFR § 42.15.
on a petition requesting institution of an IPR within six (6) months.\textsuperscript{81} If the PTAB decides to institute the IPR, it must issue a decision on the validity of the challenged claims within one (1) year.\textsuperscript{82} Thus, an IPR proceeding is likely to reach a conclusion earlier than an infringement case with less disruption to the business, than district court litigation.

iii. A Patent is Not Presumed Valid in an IPR Proceeding

In district court litigation, a patent is presumed valid and a defendant must prove that the patent is invalid by clear and convincing evidence. This is a high burden that is difficult to meet. In contrast, in the IPR process, the PTAB does not presume a patent is valid and invalidity only needs to be proven by a preponderance of the evidence, which is a lower burden than the clear and convincing standard.\textsuperscript{83}

iv. Significant Expertise in Patent Law

The patent law judges overseeing IPR proceedings are patent law specialists, are familiar with the standards for determining invalidity, and have repeatedly shown a willingness to invalidate challenged patents. As of early this year, nearly 85\% of all completed IPR proceedings resulted in some or all of the instituted patent claims to be invalidated by the PTAB.\textsuperscript{84} In contrast, district court judges and juries are non-specialists with limited (if any) familiarity with patent law – thus, there is a risk that a district court judge or jury will conclude that even minor differences between the prior art and the claims of a patent are sufficient to defeat a validity challenge.

v. Focus on Invalidity

In district court litigation, there is a limited amount of time to present an invalidity defense, and as a practical matter, it is always a challenge to focus a judge and a lay jury on the details and complexity of a validity challenge. This is even more difficult when the judge and jury are also assessing non-infringement and damages defenses that will distract from the invalidity inquiry. In contrast, the technically trained administrative patent judges at the PTAB focus only on the issues relating to invalidity, and are adept at applying invalidity concepts to the challenged patent claims.

vi. Potential Estoppel

One potential down-side to the IPR process is the risk of estoppel. Under the IPR statute, upon conclusion of an IPR, a petitioner is estopped from raising in district court litigation or before the PTAB any argument that it could have raised in the IPR.\textsuperscript{85} However, this estoppel has not proven to be as broad as it might appear. As an initial matter, the estoppel provision only applies following a decision by the PTAB on an instituted IPR. Should the PTAB not institute an IPR, there is no estoppel. Furthermore, if the PTAB were to institute on only some requested grounds, there would be no estoppel for the grounds that the PTAB chose not to

\textsuperscript{81} 35 U.S.C. §§ 313; 314.
\textsuperscript{82} The PTAB may extend this one-year deadline by six months for good cause.
\textsuperscript{83} 37 C.F.R. § 42.1(d).
\textsuperscript{85} 35 U.S.C. § 311.
institute review on. 86 Thus, if a petitioner were to challenge the validity of patent claims on four separate grounds, and the PTAB were to institute on only one of those four grounds, there would be no estoppel against raising the non-instituted grounds in district court litigation. This lack of estoppel applies even where the PTAB elects not to institute review on certain grounds because it deems those grounds to be duplicative of grounds on which it does institute review. 87

Moreover, because the PTAB only considers printed publications in an IPR, there is no estoppel to raising in a district court case anticipation and obviousness defenses based upon non-printed prior art (e.g., physical products). In a subsequent district court case, such non-printed prior art can be combined with prior art that was reviewed by the PTAB, without running afoul of the IPR’s estoppel language.

d. The IPR Process

The first step in the IPR process is preparing and filing a petition. A petition can only challenge a single patent. If a petitioner is challenging multiple patents, it will need to file separate petitions for each patent and pay the fees for each. The petition must include the following mandatory notices: the name of each real party in interest; any related judicial or administrative matters (e.g., district court litigations, International Trade Commission proceedings, or other Patent Office proceedings) that may affect or be affected by the IPR; lead and back-up counsel; and service information for the petitioner. 88 In addition to the mandatory notices, the petition must state the precise relief requested; a detailed statement of the reasons for the relief requested, applying the evidence to the governing law; and a statement of material facts with each fact stated in a separately numbered sentence with citations to the supporting evidence in the record. 89

The detailed statement of relief requested must identify the challenged claim(s); the specific statutory ground on which the challenge is based and the prior art patents or printed publications relied upon for each ground; how the construed claim is unpatentable under the challenged ground (identifying where each element of the claim is found in the prior art); and the exhibit number of the supporting evidence. 90 The petition therefore should conspicuously set forth detailed arguments and supporting evidence for each ground challenging patentability. In general, patentability arguments should not be set forth only in footnotes, expert declarations, or claim charts, and the PTAB has previously declined to consider arguments only set forth in footnotes or incorporated from expert declarations. Finally, a petition requesting an IPR is limited to 14,000 words, not including a table of contents, a table of authorities, the mandatory notices, a certificate of word count, or an appendix of exhibits or claim listing. 91

After the petition has been filed, the patentee has the option of filing a preliminary response within 3 months from the date the PTAB issues a notice of the petition. 92

87 Id.; HP. Inc. v. MPHJ Tech. Investments, LLC, Case No. 2015-1427, slip op. 4 at 12-13 (Fed. Cir. Apr. 5, 2016).
88 37 C.F.R. § 42.8.
89 37 C.F.R. § 42.22.
90 37 C.F.R. § 42.104.
91 37 C.F.R. § 42.24.
92 37 C.F.R. § 42.107.
preliminary response is limited to setting forth the reasons an IPR should not be instituted, and may include supporting evidence, but may not include testimonial evidence unless it is already on the record or the PTAB has authorized inclusion of new testimonial evidence.93

The PTAB must decide whether to institute an IPR within three months of the patentee’s filing of a preliminary response or the date such a response would have been due, whichever date is earlier.94 The PTAB may only institute an IPR if it determines the petition has shown a reasonable likelihood that at least one challenged claim is unpatentable.95 The PTAB may deny some or all grounds of alleged unpatentability.96 A PTAB decision to institute an IPR is final and nonappealable.97

i. Discovery During the IPR

Limited discovery is available during the IPR process. However, unlike district court litigation, discovery in an IPR is narrowly focused on issues raised in the IPR and further narrows as the IPR progresses. During the first three months following institution of an IPR, the patentee may conduct routine discovery without special authorization from the PTAB and the scheduling order usually specifies the times for conducting routine discovery.

Routine discovery in an IPR includes: production of any exhibit cited in a paper or testimony; cross-examination of the opposing party’s declarants; and relevant information that is inconsistent with a position advanced during the proceeding.98 If a party seeks additional discovery, it must file a motion for additional discovery and show that the additional discovery should be allowed in the “interests of justice” (unless the parties agree to conduct additional discovery).99 The PTAB has typically considered the following factors when deciding whether additional discovery is in the “interests of justice”:

• Is there more than a possibility and mere allegation that something useful might be found?

• Does the request merely seek early identification of the opponent’s litigation position?

• Can the party requesting discovery generate equivalent information through other means?

• Are the instructions easily understandable?

• Are the requests overly burdensome to answer?

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93 37 C.F.R. § 42.107(c).
95 37 C.F.R. § 42.108(c).
96 37 C.F.R. § 42.108(b).
98 37 C.F.R. § 42.51(b).
99 37 C.F.R. § 42.51(b)(2).
ii. Patentee’s Response and Potential Motion to Amend

Within three months of institution of an IPR, the patentee may conduct discovery, file a response to the petition and the PTAB’s institution decision, and may file a motion to amend the patent claims that are subject to the IPR.100 Unlike the pre-institution preliminary response (where the patentee is limited to attacking allegations in the petition, in the post-institution response the patentee may substantively refute the arguments raised in the petition, address the institution decision, and introduce affirmative evidence. The patentee’s response should include arguments for all claims at issue, affidavits with supporting evidence, and an explanation of the relevance of the evidence. Like the petition, the patentee’s response is limited to 14,000 words.101

A patentee may also file a motion to amend any claims on which an IPR has been instituted. This motion is typically due with the patent owner’s response to the petition.102 The patentee must confer with the PTAB before filing the motion to amend so the PTAB and the parties can discuss how the motion to amend may affect the schedule. However, the patentee does not need the PTAB’s permission to file its initial motion to amend.

A motion to amend should identify the support in the original patent disclosure for the amended claims and “may not enlarge the scope of the claims of the patent or introduce new matter.”103 The PTAB rarely grants motions to amend. However, in the event the PTAB grants a motion to amend the claims, that amendment will likely cut-off any alleged pre-amendment damages under the doctrine of intervening rights.104

iii. Petitioner’s Reply and Opposition to Any Motion to Amend

After the patentee has filed its response to the petition and/or filed a motion to amend the claims, the petitioner is typically given three months to conduct discovery. Like the patentee, the petitioner may conduct routine discovery, including noticing depositions of the patentee’s declarants. The petitioner may also seek additional discovery through agreement or a motion for additional discovery. A motion for additional discovery by the petitioner will be treated in the same manner as a motion by the patentee. Similarly, the petitioner will need to follow the same expedited timelines for objections to evidence and depositions.

Approximately six months after institution, the petitioner may file a reply to the patentee’s response. The petitioner’s reply may only respond to arguments raised in the patentee’s response.105 Like a court, the PTAB will not consider issues raised for the first time in the petitioner’s reply.

If the patentee filed a motion to amend, the petitioner may also file an opposition to the motion. The opposition may raise new patentability issues related to the patentee’s proposed

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100 35 U.S.C. 316; 37 C.F.R. § 120.
101 37 C.F.R. § 42.24(b).
102 37 C.F.R. § 42.121.
104 35 U.S.C. § 318(c).
105 37 C.F.R. § 42.23.
substitute claims. Arguments frequently raised in oppositions to a motion to amend include: the amendment broadens the scope of the claims; the amendment introduces subject matter not supported by the original disclosure; and/or the amendment does not resolve a ground of unpatentability on which the PTAB instituted the IPR.

iv. Patentee’s Reply

The patentee has a second discovery period to address evidence raised in the petitioner’s reply and/or the petitioner’s opposition to a motion to amend. Typically, this discovery period lasts for about one month. If the patentee had filed a motion to amend, it can file its reply to the petitioner’s opposition at the end of the one-month discovery period. The reply may only respond to those arguments raised in the petitioner’s opposition. On a motion to amend, the patentee bears the burden of proving patentability, therefore the reply should clearly address each argument set forth in the petitioner’s opposition.

v. Motions to Exclude

After the final reply (either by the petitioner in support of the petition, or by the patentee in support of a motion to amend) either party may file motions to exclude evidence to which the party had previously objected. The deadline for filing motions to exclude should be set forth in the scheduling order and is usually about three weeks after the filing of the final reply. Opposition to motions to exclude are usually due two weeks later, with replies due one week after the oppositions.

A motion to exclude evidence should:  
Address the exhibits in numerical order;  
Identify where the objected to evidence was relied on by the other party;  
Identify where an objection was made; and  
Provide the basis and an explanation of each objection.

vi. Hearing Before the PTAB

After all the briefs and motions have been filed, either party may request oral argument on an issue raised in a brief. “The request must be filed as a separate paper and must specify the issues to be argued.”

The scheduling order should set the time for requesting an oral argument. Typically, the PTAB hears the petitioner first, followed by the patentee, and then hears petitioner rebuttal. During the hearing, the parties may only rely on evidence previously submitted on the record, and may not introduce new evidence. If a party intends to use demonstrative exhibits at the

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106 37 C.F.R. § 42.23(b).
107 37 C.F.R. § 42.64.
108 37 C.F.R. § 42.70(a).
hearing, it must serve the demonstrative exhibits no later than five business days before he
hearing and must file them with PTAB no later than the time of the hearing.109

The PTAB must enter a final written decision no later than one year after instituting an
IPR. The Chief Administrative Patent Judge may extend the one-year period by six months for
good cause.110 In its final written decision, the PTAB may cancel some or all of the reviewed
claims. Unlike the PTAB’s decision to institute an IPR, a party may appeal the PTAB’s final
decision directly to the Federal Circuit.111 Any appeal must be made within 63 days of the final
written decision.112

vi. Settlements

The IPR process provides a forum to attack the validity of a patent in a focused manner
at a reduced cost (compared to litigation). During the IPR proceeding, the parties may settle
both the litigation and the IPR.113 To settle an issue in the IPR, the parties must file a true copy
of any agreement between the parties with the PTAB before the termination of the IPR.114
Although the PTAB typically terminates an IPR if the parties settle before the IPR is fully briefed,
the PTAB is not a party to the settlement and may choose to continue its review of the
patentability of the challenged claims independently. The risk that the PTAB may continue to
review the patentability of claims even after the parties have settled, should place pressure on
the patentee to settle early in the IPR process rather than risk settling the matter late in the
process and then having the patent claims continue under review.

e. Motions to Stay Litigation

As mentioned previously, motions to stay district court litigation are another tool that may
be useful in curbing litigation expenses. Frequently district courts will stay litigation while the
PTAB considers an IPR petition. The decision to stay litigation is discretionary and courts vary
widely on whether to stay litigation before the PTAB has instituted an IPR. The factors courts
consider when ruling on a motion to stay are: (1) whether a stay would unduly prejudice or
tactically disadvantage the opposing party; (2) whether a stay will simplify the issues and
streamline the trial; and (3) whether discovery is complete and whether a trial date has been
set.115

There are significant differences between courts on whether to grant motions to stay
before the PTAB has instituted an IPR. Certain courts have a history of generally denying pre-
institution motions to stay. For example, the Eastern District of Texas as a general rule denies
pre-institution motions to stay a case and has stated that the “majority of courts that have
addressed the issue have postponed ruling on stay requests or have denied stay requests when

109 37 C.F.R. § 42.70(b).
113 37 C.F.R. § 42.74.
114 37 C.F.R. § 42.74(b).
the PTAB has not yet acted on the petition for review. However, other courts have granted pre-institution motions to stay and have expressly rejected the argument that there is a consensus to deny requests to stay prior to institution of an IPR. Thus, whether a court will grant a pre-institution motion to stay is uncertain. In contrast, once a petition is granted and an IPR has been instituted, district courts are nearly universal in granting motions to stay. In the few instances where courts have denied post-institution motions to stay, there were multiple patents at issue in the litigation, and the PTAB had not instituted IPRs on all of the asserted patents.

In general, a district court is more likely to grant a stay when a defendant files an IPR petition early in a case before the court has expended significant time or effort on the litigation, and the IPR petition(s) challenge all patent claims. Even in jurisdictions where courts generally do not grant pre-institution motions to stay, defendants should consider petitioning for an IPR early in the litigation so that they may request a post-institution stay as soon as possible and minimize the accrual of fees and litigation expenses.

Thus, an IPR proceeding not only may provide a faster and less expensive means to invalidate a patent, but may also result in a stay of the litigation even before the PTAB rules on the validity of the patent claims. To take advantage of this procedural mechanism a defendant should consider filing a petition requesting an IPR and bringing a motion to stay the district court litigation as soon as possible. The filing of an IPR petition, and the institution of an IPR by the PTAB, will also place considerable pressure on a patentee to settle before the PTAB can rule on the validity of the asserted patent claims.

B. Copyright Infringement Claims

A copyright vests in the author of a copyrightable work at the moment of creation. Registration with the Copyright Office is required before an infringement suit can be filed, but the copyright itself comes into existence immediately. Ownership of the copyright vests in the author(s) alone—not the person who might pay for the creation of the work—unless there is a work-for-hire agreement or an assignment agreement. A franchisor or franchisee may find themselves caught up in a copyright infringement action if attention is not paid to how copyrightable material is being created and used.

Consider the following scenario. A franchisor or franchisee hires an independent contractor or uses its employee to create a software program, a brochure, or to do website design for the business. Later, the employee or independent contractor sues the business for copyright infringement. Who rightfully owns the copyright in the work? As discussed below, the answer will depend on whether the employee performed work within the scope of his or her employment; or, in the case of an independent contractor, whether there is a written work-for-hire agreement or an assignment in place.

1. **Works Made For Hire**

Section 101 of the Copyright Act defines a “work made for hire” in two parts:

1. a work prepared by an employee within the scope of his or her employment or
2. a work specially ordered or commissioned for use as a contribution to a collective work, as a part of a motion picture or other audiovisual work, as a translation, as a supplementary work, as a compilation, as an instructional text, as a test, as answer material for a test, or as an atlas, if the parties expressly agree in a written instrument signed by them that the work shall be considered a work made for hire.\(^\text{120}\)

Thus, for works created by an employee, the copyright resides in the employee—not the business—for any work that is created outside the scope of employment. For example, a copyright in a sales brochure created by a receptionist would most likely belong to the receptionist because creating brochures are not normally part of the job duties of a receptionist. Similarly, for works created by independent contractors, the copyright resides in the contractor—not the business that hires the contractor—for any type of work described in paragraph (2) when there is no written work-for-hire agreement. If a business wishes to own the copyright in a software program or brochure that is created by an independent contractor, or by an employee that was not hired to create that type of material, the business must receive title to the material through an assignment agreement.\(^\text{121}\)

2. **Work-for-hire Agreements and Assignments**

Generally speaking, a work-for-hire agreement provides that an independent contractor has been commissioned to produce a work that falls specifically within one of the enumerated categories noted above. Notably, neither software, website design, nor brochures fall within the enumerated list under the work-for-hire statutory language and therefore are not properly the subject of a work-for-hire agreement. Thus, a franchisor or franchisee wishing to claim copyright ownership over software, website design, a brochure, or other work product created by a non-employee, independent contractor not covered by paragraph (2) will need an assignment agreement stating that the work is assigned to the business. Simple assignment language could state:

[The author] “hereby assigns” to [the business] all its rights, title and interest in the work entitled [Insert Name of Work] and described in Appendix A, as well as all rights, title and interest [the author] may hold in any derivative works.

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\(^{120}\) 17 U.S.C. § 101.

\(^{121}\) Id.
It is important to state “hereby assigns” in the assignment as this language immediately transfers title—even for future works—rather than “agrees to assign,” which only creates a promise to assign but does not actually transfer title.122

Where a business is purchasing work from a third party, the assignment agreement should also include representations and warranties that the work is an original creation by the author and does not infringe anyone else’s copyrights. This is particularly important where the author may be using material located on the internet as a starting point for the work. Materials that are widespread on the internet do not automatically become part of the public domain, and incorporating material found on the internet—for example, language from a competitor’s website, or photos found online—may subject a business to liability for copyright infringement.123

3. Copyright Registration – Leverage in Litigation

Registration of a copyright with the Copyright Office is relatively easy and fairly inexpensive,124 and it carries several benefits. As an initial matter, a copyright must be registered before it can be enforced in court.

Timely registration also permits significant damages and the possibility of recovering attorney’s fees in litigation. Under Title 17, Section 412, a copyright holder is entitled to statutory damages and attorney’s fees only if the copyright holder registered the work prior to infringement, or within three months after the work was first published or distributed to the public. Thus, lack of registration within the required time-frame could be a defense to the recovery of certain monetary remedies in an infringement action.

If the copyright is registered timely, the potential recovery of statutory damages and attorney’s fees may be used against the accused infringer as leverage to settle litigation and remove infringing material from the marketplace. Statutory damages allow recovery of up to $30,000 for each infringed work.125 If the infringement is willful, these damages can rise to $150,000.126 The copyright statute also provides that the prevailing party in an infringement suit may in certain cases recover its full costs from the suit, including reasonable attorney’s fees.127 Whether a prevailing party is entitled to recover its fees is at the discretion of the district court, however, among the factors a district court should consider are the substantive strength of a

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122 See Board of Trustees of the Leland Stanford Junior Varsity v. Roche Molecular Systems, Inc., 583 F.3d 832, 842 (Fed. Cir. 2009). The Court ruled that an inventor and author retains rights in his or her work unless he or she assigns it to another. Using the words “I agree to assign” does not create a present assignment of an expectant interest, and thus does not effectively or immediately transfer title of the work to another. Rather such future intentions is only a mere promise to assign rights, which then requires a subsequent assignment to effectively transfer proper title of the work.

123 Indemnification language and agreements in the context of purchasing products that become subject to a patent infringement claim are discussed in Section III.A.1.a. supra. Similar language should also apply to products and services that may be subject to copyright protection.

124 Registration can be done online and registering a single work online requires payment of a $55 fee.


126 id.

party’s claim, its motivation in bringing suit, whether its litigation positions and conduct are unreasonable, and considerations of compensation and deterrence.\textsuperscript{128}

Failure to register a copyright in a timely manner precludes a copyright holder from recovering statutory damages. Where a copyright holder does not register the copyrighted work until after infringement has begun, it cannot rely on statutory damages, and may only recover actual damages it can prove it suffered from the infringement, as well as the infringer’s profits attributable to the infringement.\textsuperscript{129} However, proving actual damages and an infringer’s profits is often expensive, requiring significant attorney time, discovery, and expert witness analysis and testimony. This may render an infringement suit not economically viable and provide a significant incentive to settle a litigation.

In addition to waiving statutory damages, late registration of a copyrighted work also precludes a copyright holder from recovering attorney’s fees under the Copyright Act. This preclusion, however, is only one-way. If the accused defendant prevails in a copyright suit, it may be entitled to receive its costs and attorney’s fees from the copyright holder. Thus, late registration of a copyrighted work can provide a defendant with significant leverage in settlement negotiations because of the expense of proving up damages, and risk that the copyright holder may have to pay the defendant’s attorney’s fees if the defendant is successful.

4. Minimizing the Risk of Attorney’s Fees Through an Offer of Judgment

Unlike most types a legal claims, there is a strong likelihood that the prevailing party in a copyright dispute will recover its attorney’s fees and costs.\textsuperscript{130} This likelihood of fees provides significant leverage to a copyright plaintiff to exert settlement pressure on defendants to avoid or minimize a fee award.\textsuperscript{131} One way a defendant can potentially minimize the risk of paying attorney’s fees and simultaneously place pressure on a copyright holder to settle suit is through an offer of judgment under Federal Rule of Civil Procedure 68. Rule 68(a) states:

At least 14 days before the date set for trial, a party defending against a claim may serve on an opposing party an offer to allow judgment on specified terms, with the costs then accrued. If, within 14 days after being served, the opposing party serves written notice accepting the offer, either party may then file the offer and notice of acceptance, plus proof of service. The clerk must then enter judgment.

If the plaintiff does not accept the offer within in the 14 day period, and later obtains a judgment less than the amount of the offer, then the plaintiff must pay the defendant’s costs

\textsuperscript{129} 17 U.S.C. §504(b).
\textsuperscript{130} In Kirtsaeng v. John Wiley & Sons, 136 S. Ct. 1979 (2016), the Supreme Court vacated Second Circuit precedent that suggested where a non-prevailing party had shown its claim was not objectively unreasonable, fees should be awarded unless this factor was outweighed by other factors. The Court held that substantial weight should be given to the reasonableness of a party’s litigation position, but that the “ouweighed” construct improperly suggested a presumption against awarding fees wherever a non-prevailing party had taken a reasonable position.
\textsuperscript{131} As discussed above, this potential fee award requires that the copyrighted material be registered with the Copyright Office before the alleged infringement. See 17 U.S.C. § 412; see also Reed Elsevier, Inc. v. Muchnick, 559 U.S. 154, 158 (2010) (“a condition – copyright registration – that plaintiffs ordinarily must satisfy before filing an infringement claim and invoking the Act’s remedial provisions.”).
from the date of the offer. In the context of copyright litigation, a Rule 68 offer has the additional benefit of not only requiring the prevailing plaintiff to pay the defendant’s costs, but also cutting off the plaintiff’s right to receive fees as a prevailing party. Thus, an offer of judgment under Rule 68 may be a significant tool to resolve a copyright case early in the litigation.

When making a Rule 68 offer of judgment it is very important to state precisely what is included in the offer. That is the offer should state whether the amount offered includes damages, fees, and/or costs. If a party fails to specify that the offer includes costs or fees, then the offer is presumed to be for damages only, and the prevailing party receiving the offer can bring a motion for fees and costs. Section 505 of the Copyright Act uses the term “full costs.” At least some federal courts have interpreted these costs to include expert fees. Accordingly, when calculating how much to offer, the offering party should factor expert witness fees into the offer.

If the plaintiff accepts the offer within the 14-day period, the offer is filed with the court and judgment will be entered pursuant to the terms of the offer. If the plaintiff does not accept the offer, it is deemed withdrawn. In that case, a defendant may make subsequent offers. The offer is not admissible at trial and should only be submitted to the court “in a proceeding to determine costs.”

Per Rule 68(d), “If the judgment that the offeree finally obtains is not more favorable than the unaccepted offer, the offeree must pay the costs incurred after the offer was made.” Should the plaintiff fail to accept an offer and then also fail to receive a better result in the litigation, Rule 68 may shift payment of costs from the prevailing plaintiff to the defendant.

When determining whether a party has exceeded a Rule 68 offer, the court will consider the scope of the offer. If a Rule 68 offer specifies that it includes fees and costs, then pre-offer costs and pre-offer fees will be added to the damage award to determine whether the plaintiff has beaten the Rule 68 offer. Courts differ on how to treat non-monetary relief when assessing the value of a Rule 68 offer. Some courts ignore non-monetary relief in comparing a Rule 68 monetary offer to a judgment. However, “most federal courts” try to put a value on

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133 See Marek v. Chesny, 473 U.S. 1, 6 (1985) (“If an offer recites that costs are included or specifies an amount for costs, and the plaintiff accepts the offer, the judgment will necessarily include costs; if the offer does not state that costs are included and an amount for costs is not specified, the court will be obliged by the terms of the Rule to include in its judgment an additional amount which in its discretion, it determines to be sufficient to cover the costs.”) (internal citation omitted).
135 See, e.g., Twentieth Century Fox Film Corp. v. Entertainment Distributing, 429 F.3d 869, 885 (9th Cir. 2005).
137 Id.
138 See Corder v. Gates, 947 F.2d 374, 380 n.9 (9th Cir. 1991); see also Marek, 473 U.S. at 7 (1985) (holding that a plaintiff did not beat a $100,000 offer where the plaintiff received $60,000 in damages and had only $32,000 in pre-offer costs and attorney’s fees – even though plaintiff’s total damage award, including post-offer costs and fees reached $172,000).
139 See Real v. Continental Group, Inc., 653 F. Supp. 736, 738-739 (N.D. Cal. 1987) (refusing to quantify the injunctive relief offered by defendant and therefore finding that plaintiff beat defendant’s Rule 68 offer).
injunctive relief received by a plaintiff.\(^{140}\) In *Reiter v. MTA New York City Transit Authority*, the court held that a plaintiff-employee was entitled to recover attorney’s fees and costs incurred after he rejected defendant’s $20,001 offer of judgment, because, although the monetary damages award was only $10,000, plaintiff also obtained equitable relief, including reinstatement, which also meant return to his corner office with an assistant and other perks that he lost when he was demoted.\(^ {141}\) The court determined that this equitable relief was worth more than the $10,001 difference between the Rule 68 offer and the final monetary damages award. Similarly, in *Andretti v. Borla Performance Industries, Inc.*, the Sixth Circuit explained: “a favorable judgment and an injunction can be more valuable to a plaintiff than damages.”\(^ {142}\) To address this concern, an offer of judgment should include injunctive relief (for example, ceasing sales or distribution of the accused product) if the injunctive relief is requested in the complaint.

In the context of copyright litigation, attorney’s fees may be awarded as part of costs.\(^ {143}\) Accordingly, if a plaintiff does not exceed a Rule 68 offer, it cannot recover its post-offer costs, inclusive of post-offer attorney’s fees. For example, in *Marek* the plaintiff’s post-offer attorney’s fees were not recoverable where the combined judgment and pre-offer costs and fees were less than the Rule 68 offer.\(^ {144}\) However, at the court’s discretion, the plaintiff may receive its pre-offer fees and costs.

Courts have split on whether failure to exceed a Rule 68 offer only cuts off a prevailing plaintiff’s right to fees, or also entitles a non-prevailing defendant to recover its post-offer fees and costs. The Ninth Circuit has held that only a prevailing party is entitled to a shift of fees under Section 505, and therefore Rule 68 cannot shift fees or non-taxable costs to a non-prevailing defendant.\(^ {145}\) Thus, under Ninth Circuit precedent a defendant is entitled to its fees and non-taxable costs only if it is the prevailing party. In contrast, the Eleventh Circuit has held because under *Marek* recoverable “costs” in copyright actions include attorney’s fees, and the language of Rule 68 requires shifting of costs, a non-prevailing defendant is entitled to its post-offer fees and costs when a plaintiff fails to exceed a Rule 68 offer.\(^ {146}\) The Southern District of New York has reached a similar conclusion.\(^ {147}\)

### 5. Key Points to Making an Offer of Judgment Under Rule 68

The offer of judgment should be for a specific amount and should state whether fees and costs are included or are to be determined separately by the court. The offer should state that it

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\(^{140}\) *Reiter v. MTA New York City Transit Authority*, 457 F.3d 224, 231-232 (2d Cir. 2006) (finding court may quantify the value of the injunctive relief received by plaintiff).

\(^{141}\) *Reiter*, 457 F.3d. at 232.

\(^{142}\) *Andretti v. Borla Performance Indus.*, 426 F.3d 824, 837 (6th Cir. 2005); see also *Lish v. Harper’s Magazine Found.*, 148 F.R.D. 516, 520 (S.D.N.Y. 1993) (that plaintiff in copyright suit was awarded no damages did not mean that plaintiff’s final judgment was less than defendant’s offer of judgment of $250); *Domanski v. Funtime, Inc.*, 149 F.R.D. 556, 558 (N.D. Ohio 1993) (“permanent injunctive relief, though admittedly difficult to quantify, adds considerable value to the ‘judgment finally obtained’ by [plaintiff] when compared to the judgment offered by [defendant]”); *Lightfoot v. Walker*, 619 F. Supp. 1481, 1485-86 (S.D. Ill. 1985) (considering offer of judgment consenting to prison health care reform).

\(^{143}\) 17 U.S.C. §505.

\(^{144}\) *Marek*, 473 U.S. at 3-5.

\(^{145}\) *UMG Recordings, Inc. v. Shelter Capital Partners LLC*, 718 F.3d 1006, 1035 (9th Cir. 2013).

\(^{146}\) *Jordan v. Time, Inc.*, 111 F.3d 102, 105 (11th Cir. 1997).

is an offer for judgment under Rule 68 and must be properly served on the plaintiff. An informal settlement offer does not constitute an offer for judgment. Should the plaintiff accept an offer of judgment under Rule 68, the court will enter judgment on the record and the terms of the offer will be public.

If the plaintiff seeks injunctive relief or other nonmonetary relief, the defendant should include similar relief in the offer of judgment. In the event there is a dispute over whether costs should be shifted under Rule 68, the parties should be prepared to address the value of any injunctive relief when arguing whether the judgment obtained by the plaintiff was “more favorable” than a rejected Rule 68 offer.

Thus, a defendant accused of copyright infringement should consider whether to make an offer of judgment to attempt to end the litigation at an early stage and potentially cut-off a plaintiff’s right to attorney’s fees and costs. In the event a plaintiff fails to accept a Rule 68 offer and the discovery or motion practice shows that the plaintiff’s potential damages are less than the amount of the offer, there will likely be significant pressure on the plaintiff to settle the litigation before incurring additional attorney’s fees and expense which it cannot recover.

C. Protecting Trade Secrets

Trade secret protection depends in many ways on a company’s ability to control the dissemination of information—specifically, secret information. Although control of information may be more straightforward for a small company, larger companies are often faced with the challenge of controlling the confidentiality of information which may ultimately be controlled by or housed in the minds of its employees and independent contractors. For example, consider a hypothetical company (franchisee or franchisor) has decided to hire two employees and two independent contractors to program a new, technologically advanced mobile fast-food ordering “app” (the App). There are at least two sets of trade secrets about which the company must be concerned relative to the development of the new software: (1) information relating to the App that the company considers proprietary and confidential; and (2) information considered confidential by previous employers that is still housed in the brains of the new employees or contractors. The franchisee/franchisor would like to protect legally its own trade secrets and avoid misappropriating the trade secrets of others.

1. Protecting the Secrecy of a Trade Secret

DTSA defines a trade secret as any information for which “the owner thereof has taken reasonable measures to keep . . . secret” and ; and that “derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by, another person who can obtain economic value from the disclosure or use of the information.”148 Similarly, most states have adopted a variation of the Uniform Trade Secrets Act (UTSA), which defines trade secret the same way.149 Accordingly, the franchisee or franchisor must take “reasonable measures” to protect the secrecy of any confidential and proprietary information relating to the App. The reasonableness of any safeguard will be determined based on the circumstances, including the type of information, cost of safeguarding the information, and industry practices.

149 Uniform Trade Secrets Act § 1(4).
a. Non-Disclosure Agreements

As a first step, the company should require employees and contractors who will have access to confidential information to sign non-disclosure agreements. The non-disclosure agreements may be separate instruments, or may be incorporated into the company’s independent contractor and/or employment agreements. These agreements should be reasonable in scope so as not to be considered unconscionable by a court. As such, there should be a reasonable term to the agreement, provisions for returning and/or destroying the confidential information at the end of the term, and provisions that allow disclosure of information in certain circumstances (e.g., if ordered by a court, or if the information becomes publicly known through other means). The DTSA adds another requirement to employers who may desire enforcing trade secret protections through federal law—the company “shall provide notice” to its employees and contractors that they will not be liable (under federal law) for disclosing a trade secret “in confidence to a Federal, State, or local government official, either directly or indirectly, or to an attorney” if the disclosure is “solely for the purpose of reporting or investigating a suspected violation of law.”150 The company should also understand that in some states, like California, using non-compete provisions, in addition to the non-disclosure agreement, to curtail “inevitable disclosure” of trade secrets known to former employees or contractors may be unenforceable as a matter of public policy. For example, in California, enforcement of a non-compete or confidentiality agreement by way of an injunction that prevents employee mobility has been deemed incompatible with California public policy.151 Similarly, under federal law, a court may enjoin “any actual or threatened misappropriation . . . provided the order does not . . . prevent a person from entering into an employment relationship, and that conditions placed on such employment shall be based on evidence of threatened misappropriation and not merely on the information the person knows.”152 In sum, reasonable non-disclosure agreements that do not function as non-compete agreements will be enforceable and necessary to protect the secrecy of the company’s trade secrets.

b. Security Measures

The franchisee or franchisor should also use reasonable security measures to protect confidential information. For example, information required to program the App should only be disseminated to employees or contractors who actually need that information. Computers or data storage housing such information should be encrypted and password protected using at least industry standard mechanisms; sensitive data should only be transmitted using secure and encrypted transmission protocols such as secure FTP; hard copies of documents should be kept in locked storage or offices that are only accessible to authorized personnel; and the company should have in place an explicit and enforced policy related to handling of confidential information, including prohibiting employees from removing the information. Other mechanisms may be reasonably deployed depending on the circumstances, the value of the trade secrets, and the cost of protecting them.

2. Avoiding Misappropriation through Cross-Contamination

The company must also be vigilant to avoid misappropriating any trade secrets housed in the minds of the new employees and contractors. For example, if employees formerly worked for a competitor in developing a similar (but inferior) order placement app, the employees may have knowledge of their former employer’s trade secrets that would be relevant to programming the App for the company. As a first step, the company should require the new employees and contractors to represent that they do not have such knowledge. If an employee or contractor cannot make such a representation but the franchisee/franchisor is willing to take on the expense of safeguarding against inevitable disclosure, the company should require that the employee agree not to use or disseminate any trade secrets of their former employer. A “clean room” protocol (similar to protocols used to protect against the dissemination of information during litigation) may be necessary to ensure that such information is not disseminated. Such a “clean room” would entail requiring the employee to work only on parts of the App that does not overlap with the trade secrets of their former employer, segmenting data accessibility via electronic firewall and physical segregation of workspaces and/or other security protocols, to limit cross-pollination of information between the new employees and other employees and contractors working on the App. These steps must be reasonable and clearly documented to protect against any possible future claim of misappropriation of trade secrets brought by the former employer.

IV. CONCLUSION

Franchise companies depend on new technology as a means for creating a competitive advantage over other franchises or non-franchised companies alike. Although implementation of new technologies into a franchise can improve business operations and provide a strategic advantage in the marketplace, companies doing so are at risk for being sued for an alleged violation of the intellectual property rights of others. A franchise company can take steps up front to minimize the risk of a future lawsuit by using work-for-hire agreements and assignments and by taking appropriate measures to protect against the unintended use of another’s trade secrets. If already faced with a lawsuit, a franchise company has an arsenal of tools available to help reduce litigation expense, such as indemnification agreements, defense groups, Rule 68 Offers of Judgement, new procedures at the USPTO, and motions to dismiss and/or stay litigation.
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