

Protecting Intellectual Property – Why isn't it Obvious that My Stuff is Mine?

By Katheryn A. Andresen¹

The typical business contract may include various references to different forms of intellectual property (“IP”) such as: trademarks, copyrights, trade secrets or patents. If the contracting parties are developing intellectual property as part of the agreement, then the ownership of such developed IP needs to be expressly specified. Conversely, if the IP already exists, then a contracting party’s right to use such IP should be addressed in a license provision.

Intellectual Property Types

Intellectual property is usually broken down into four sub-categories: patents, trademarks, copyright and trade secrets. The first two types, patents and trademarks, may be registered with the United States Patent & Trademark Office and/or with another country’s IP registrar to secure rights. Copyright IP rights are automatic in the United States (and in most other countries under treaty with the US), but a copyright protected work may also be formally registered with the Library of Congress’ Copyright Office. Trade secrets are the one form of IP right which cannot be registered as doing so would eliminate the private trade secret right.

Patents and trademarks both provide the IP rights owner with an exclusive right to benefit from such registered patent or trademark. Registered patents grant the owner an exclusive 20 year period to control the sale and utilization of the patented subject. Patents may be issued for an invention in the traditional sense, or for a business methodology, including software or Internet technology. The traditional invention patent is commonly understood to protect an inventor’s right to profit from the patented invention. Even if the average person is unaware of the actual patent status of an invention, it is likely that a person would know that the inventor has the rights to profit from such an invention. Business method patents, on the other hand, are neither obvious subject matters of the patent world, nor easily identified by the average person.

While many people may have used Amazon.com’s site to buy items, it is not as obvious that Amazon has a business method patent for the ability to store a buyer’s information to allow for “one-click” shopping. For the consumer – whether it requires two clicks or one to buy an item online – is just a matter of ease of use of the site. For Amazon, the ability to exclusively offer the “one-click” option is a patented right. Other business method patents have very significant liability issues for companies, but the general public is mostly unaware of even the concept that a certain business practice may be patented. For example, one patent owner filed for a patent on a computerized telephone call center that screened issues before forwarding the caller to actual customer support person. The holder of this patent has

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successfully sued very large companies for millions of dollars and claims to have forced such companies to license his patented call center generating millions in license fees.²

Trademarks include the mark, sound, color or combination used to brand the goods sold by a company. For example, Apple Computer's apple icon is a classic trademark. Registered marks used to sell services are called service marks, but most people just use the term trademarks when referring to brand protection for either goods or services. In order for a mark to be capable of registration, it cannot be "merely descriptive." A merely descriptive mark would be an apple image for an apple grower, but when used to sell computers – the apple image is deemed "fanciful" and therefore capable of registration. A trademark allows the owner a 10 year period of exclusive rights which may also be renewed for an additional 10 year period.

Trade secrets are only a protected IP right when they are kept confidential. The moment a trade secret is published to the public, the actual trade secret right is lost. One famous trade secret is the recipe for Coca Cola. Typically any trade secret or component of a trade secret that must be revealed in a business deal is governed by a strict confidentiality obligation.

Ownership Considerations

If your contract is going to include the development of any IP right, then the agreement should expressly include an ownership provision which clarifies which party will own the developed IP at the end of the agreement. In a website development contract, for example, the ownership provision might be written as follows if the customer controlled the agreement:

Work-for-Hire / Ownership. Vendor acknowledges and agrees that all works developed, created or modified during Vendor's performance of Services under this Agreement (each a "Deliverable") shall belong to Company and shall be deemed to be a Work-for-Hire under Title 17 of the United States Code. To the extent any such Deliverable is not deemed to be a Work-for-Hire, Vendor hereby assigns all rights, title and interest, including all intellectual property rights and proprietary rights in such Deliverable to Company without further compensation. To the extent Vendor incorporates into any Deliverable, materials that are not assigned outright to Company by this Agreement, Vendor hereby grants to Company an exclusive, perpetual, world-wide, royalty free, assignable, and sub-licensable (through multiple tiers) license to reproduce, copy and distribute copies by sale, lease or any other means, perform and display publicly or privately, create derivatives, translate and modify that material into any media. In addition, to the extent that Vendor developed or created any materials prior to the Effective Date of this Agreement that may reasonably be construed as created in anticipation of this Agreement, such materials shall merge into the relevant work and be subject to the ownership and/or license provision in this Section.

² Ronald A. Katz holds patent 705/4 on call centers which were for the most part set to expire in 2009, but he made millions prior the expiration of the patent.

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The work-for-hire language is necessary as under United States copyright law, the original author or creator of a work is the owner. When the “work-for-hire” language is included, by statute this changes the original owner to be the contracting party who hired the author/creator to create the work on behalf of the contracting party. Generally, an employer owns the works created by its employees, especially if such works are made during the performance of the employee’s duties, during work hours and using the employer’s equipment. There is no need for “work-for-hire” language for a true employee unless such work is developed outside of normal business hours on the employee’s personal equipment and outside the scope of the employee’s business duties.

The Supreme Court in its 1989 Reid decision developed a twelve factor test to determine if an individual hired may be a “common law” employee or is truly an independent contractor. If an “employee,” even under a common law agency assessment, then the employee’s works of authorship are owned by the common law employer. If the individual is deemed an independent contractor, than the works of authorship are owned by the individual unless there is an express “work-for-hire” clause in the agreement with such individual. The twelve factors assess the individual’s ability to control the means-and-manner of the work:

1. The skill required;
2. The source of the instrumentalities and tools;
3. The location of the work;
4. The duration of the relationship between the parties;
5. Whether the hiring party has the right to assign additional projects to the hired party;
6. The extent of the hired party’s discretion over when and how long to work;
7. The method of payment;
8. The hired party’s role in hiring and paying assistants;
9. Whether the work is part of the regular business of the hiring party;
10. Whether the hiring party is in business;
11. The provision of employee benefits; and
12. The tax treatment of the hired party.

Apart from the ownership provision, a development agreement which includes IP that is going to be owned by the contracting party also usually includes an acceptance process whereby the parties identify acceptance criteria and a testing period of the developed work against those criteria. The parties usually specify the process for which the developed IP is to be accepted and rejected and whether or not there is any cure period for IP which does not meet the acceptance criteria. Unless the business owner contracting for IP development is sophisticated in the technology to be developed, it often makes sense to have a technology attorney or a technology consultant ensure that the acceptance provisions, including the acceptance criteria are reasonable and sufficient. The ability to control for acceptance may make the difference to having to litigate over developed IP that fails in its essential purpose.

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License Considerations

Your business contract may include a license for some type of IP right. As noted in the license for any materials not deemed a “work-for-hire” in the ownership clause example above, the following language is one type of license that might be included:

Vendor hereby grants to Company an exclusive, perpetual, world-wide, royalty free, assignable, and sub-licensable (through multiple tiers) license to reproduce, copy and distribute copies by sale, lease or any other means, perform and display publicly or privately, create derivatives, translate and modify that material into any media.

There are several key components of this particular license grant which should be understood. The first key component is the use right which can be broken down into various sub-use considerations: reproduce, copy and distribute copies by sale, lease or other means, perform and display, create derivatives, translate and modify into any media. Many licenses just say “use” without any further specification and unless there is a litigated dispute about the scope of the license, this may be sufficient. The problem is that if there is ever any litigation regarding the scope of the use grant, having all of the sub-details enumerated, makes it harder for the IP owner to claim the license did not extend to the license holder’s use. Please note, however, that some courts would consider a detailed list to be the only rights granted if the parties took the time to enumerate the rights. So, often in a contract you would find the language which says “including but not limited to” which says the parties are about to specify certain sub-elements, however those enumerated elements are not the only ones to be deemed included.

Another key component of a license grant is the duration of the license. In the above example, the license grant is perpetual. More often, a license grant is limited to the period for which the license is paid, or until the agreement is terminated. The duration consideration is particularly critical if the IP right involved is something for which the contracting party is paying significant license fees. An example of a simple, limited license grant is a website which allows access dependent on current fee payment. Many game sites are based on the premise that if the license user is current on the license fees, then the use of the game site is permitted. The actual language of the license granted in such a case would likely be written as “limited, non-exclusive” conditioned on being current in the payment of the license fee.

Other license components can deal with geographical limits, ability to assign or sub-license, and whether there are ongoing fees or royalties owed for the license grant.

Risk Protection

Another key consideration when addressing IP rights in a business contract is to provide for both the business and legal risks that are associated with that particular IP right. For example, if the contract addresses the development of an IP right (such as a website) the business risks are addressed by ownership provisions and/or license provisions. The legal risks should also be addressed and this

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extends to potential claims by third parties that the IP developed infringes that third party's IP rights. This risk is usually protected through an indemnification clause. Oftentimes the only indemnity right included by a software developer is strictly for third party claims of IP infringement related to the developed work. Please note that an additional protection would be to have a representation and warranty that the developed work does not infringe any third party's IP rights. Most software vendors will not agree to this warranty by claiming it's already covered under their indemnification obligation. Such a warranty, however, provides the purchaser of the developed work with an "innocent infringer" defense if the indemnification obligation is unmet.

In addition to indemnification, many development agreements would include an insurance obligation. The purpose of requiring the developer company to have both commercial general liability and error & omissions liability coverage is to offset claims/losses greater than the company could cover on its own. For example, if the website developer created an online store capability that used a one-click checkout procedure, this process could violate Amazon's one-click patent. If the claimed damages were millions, but the developer company was only worth about 250,000 a year, the developer company could elect to declare bankruptcy or go out of business, but the owner/user of the site might still be liable. The insurance coverage clause would insure that the developer would have insurance to offset the damages and would likely avoid the bankruptcy/going out of business concerns.

Conclusion

Prior to reviewing a business contract for IP rights, the business owner should know whether the IP the business is paying for the development of the IP, in which case an ownership clause needs to be included. If the IP right is simply going to be licensed, then the details in the license grant need to be considered. The legal risks with IP should also be addressed with an appropriate indemnification obligation as well as basic business insurance coverage.