CLIENT ALERT

VIDEO: Supreme Court to Decide Lawfulness of Receiving Post-Expiration Royalties on Licensed Patents

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In a case that could have significant impact on any company that deals with technology as part of its business, today the Supreme Court will consider whether to overturn, or modify, its 1964 decision in the case *Brulotte vs. Thys*, where the Court held that it was per se unlawful to collect royalties on sales or use of an invention after the licensed patents have expired. The Court is expected to issue its decision in the case by the end of June.

Click below to watch this four-part video series, in which San Francisco partner **Mark Jansen** explores the issues at play in this case and discusses its potential impact on business.

Part 1: Impact of *Kimble v. Marvel Entertainment* Case

Part 2: Context for *Kimble v. Marvel Entertainment* Case

Part 3: Arguments in *Kimble v. Marvel Entertainment* Case

Part 4: Best Result in *Kimble v. Marvel Entertainment* Case

Transcript

What is the *Kimble v. Marvel Entertainment* case about?

> It essentially will decide whether or not technology licensing companies can license their technology and be paid royalties past the expiration date of their patents. Right now there's currently a restriction that's from a 1964 Supreme Court case which says that it's actually an antitrust violation per se to collect royalties on sales or use of the invention after the patents have expired.

Which companies will be most affected by the *Kimble v. Marvel Entertainment* decision?

This decision is really important for both sides of the technology negotiation. Especially research institutions such as universities that are inventing sort of foundational basic research tools that will be used by, say, drug development companies to develop a drug that won't go to market for maybe 15 years from now after it's gone through the FDA clearance process.

The patents on those platform tools may well have expired by the time the drug goes to market, so in the reality of the world and technology, it's really hard to negotiate a fair payment – a reasonable payment because nobody knows if the drug is going to be successful or not until you get practically to patent expiration and nobody's going to pay a huge amount of money up front for what might not get approved by the FDA. That's the critical issue and the current law that the Supreme Court is going to look at really inhibiting the ability to really work out good deals.

What is the *Brulotte v. Thys* Rule at issue here?

The 1964 Supreme Court case that is going to be decided is a case called *Brulotte v. Thys*. The critical doctrine or issues were (1) a patent gives a monopoly of sorts and (2) we don't – it's anti-competitive to extend that monopoly past the 17 year life of the patent. Therefore, the idea was that the Supreme Court said the collection of royalties for the use of the patent after its expiration is necessarily an unlawful anti-competitive result and basically the Supreme Court then held that any such license is unenforceable, which means that you can do the deal and it's completely fair everybody thinks it's the best way to do it, but if later on the patents expire, one party can say "I'm not going to pay you." That's the way it works right now and that was the situation in the *Kimble* case.

Why is this case so important to technology licensing?

My personal view is that, you can tell which side I'm on here, I believe that research institutions, innovators, need to have flexibility in what they can negotiate and so do the technology buyers. A technology buyer doesn't want to pay a huge upfront payment or even royalties before they know that a drug is going to be successful, but actually they do perceive a potential value that could be enormous. You're talking about drugs that could reach a value of $1.5 billion a year or whatever in sales so they're certainly willing to pay out a large amount of money over time as long as the percentage is relatively small. In some cases they may say we don't want to be locked into a huge royalty or any royalty or any significant royalty once the patent comes off patent because there will be other competitors coming in, we need to be able to compete. But the main thing is that this gives flexibility and makes it easier to basically negotiate what's a fair deal and a reasonable deal.

What are the arguments in favor of reversing the current technology licensing rule?

That the whole landscape of antitrust analysis has changed. It used to be that virtually any restraint, whether it was vertically imposed or horizontal, was considered per se unlawful.

The Supreme Court in the past has already reversed a similar case holding that geographical restraints by a manufacturer over its retailers was not per se unlawful. That happened in the late 70's and the same argument would be made here that really a patent doesn't automatically give a monopoly at all and it doesn't for close competitors because once that patent is expired it means that market is open for anybody else can come in and use that technology. In fact it's pro-competitive to be able to negotiate deals where the economics justify and

maybe necessitate having a royalty stream that starts substantially after the patents expired because the person who bought that technology and used it, used it before it expired and got a huge amount of value out of that exclusivity when the patent was valid.

What are the arguments to leave the rule as it is?

The arguments against changing the rule are essentially the idea of stare decisis. The U.S. government was actually asked to comment and submit a brief in support or against and they actually urged the Supreme Court not to take the case up in view of this strong interest in preserving and keeping existing law for certainty purposes.

What would be the best result in the *Kimble v. Marvel Entertainment* case to support technology licensing?

We shouldn't have a per se prohibition, instead it should be a case-by-case analysis under what's called rule of reason in antitrust parlance. That would give a lot more flexibility to the parties to negotiate an economically reasonable deal that makes sense to both parties without being constrained, which I think is actually more pro-competitive and certainly better for technology advancement.

What will technology licensing companies do if the Rule is not changed?

Technology companies have structured deals in a way that they hope would avoid the current rule if it stays in effect and there are certainly licensing deals out there that expressly state, for example, that the actual license will expire when the patents do but that the royalty stream will extend based on the use before the patent expired. Another way it's being handled right now by technology companies is they could transfer both patent rights and know-how.

There's no expiration on know-how, so as long as the company has a step down in royalty, from say 4 percent until the patents expire and then down to 2 percent, based on the know-how, they can extend that out as long as possible under the current rules and that is one technique that is used to avoid the current *Brulotte v. Thys* rule.

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