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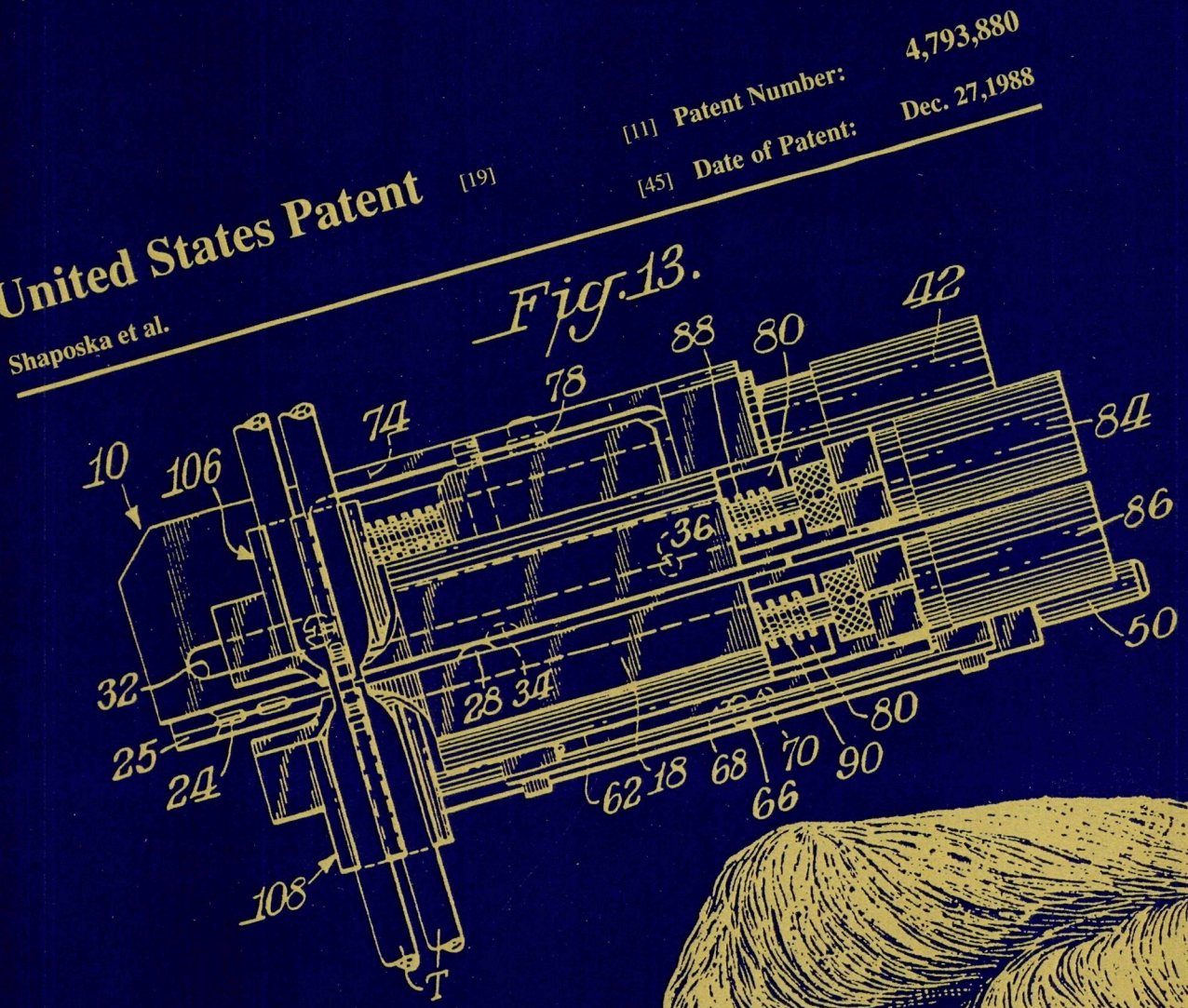

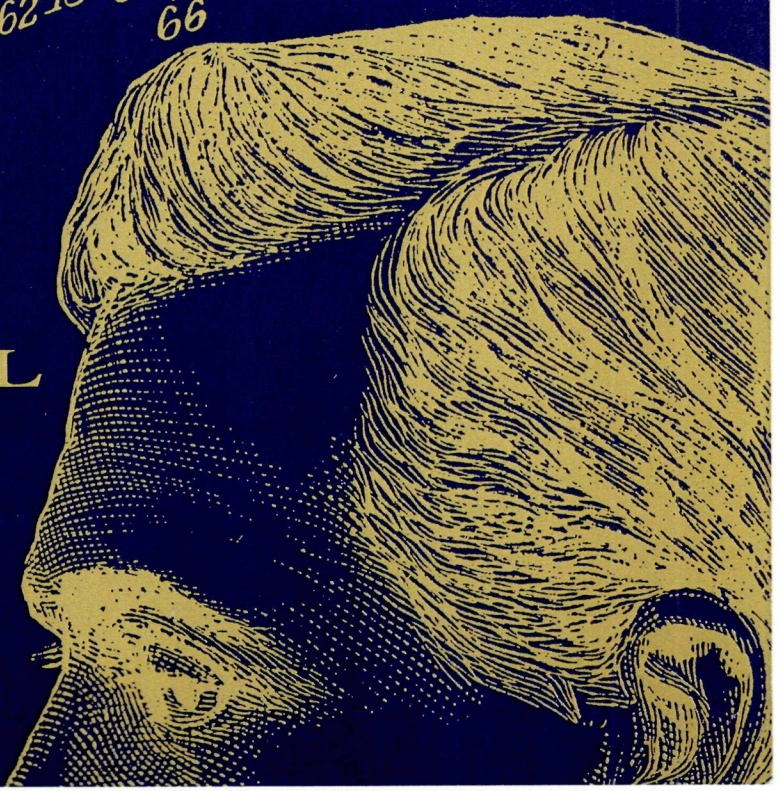

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CONTENTS

The cover: We wish to thank John B. Shaposka and Dudley W. C. Spencer for allowing us to reprint segments of U. S. Patent No. 4, 793,880, which was granted to them on December 27, 1988. We also thank their counsel, Harold Pezzner, Esquire of Connolly, Bove, Lodge & Hutz for bringing these pleasing graphics to our attention.The patent covers a device for welding together plastic tubes, such as are used in kidney dialysis. (See also page 27.)

Finally, our thanks to the talented Jon McPheeters of The Miller Mauro Group, who designed the cover. Jon's distinguished body of work includes the Delaware Bicentennial logo, the design of IN-RE:, the journal of the Delaware State Bar Association, and the new logo of that Association.

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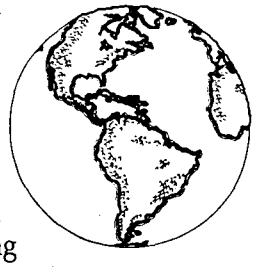

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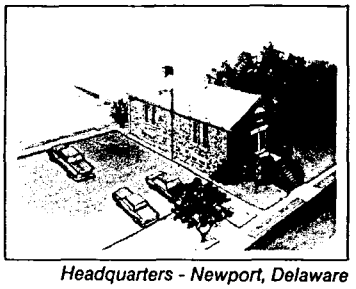

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EDITOR'S PAGE

I - THIS ISSUE

Our thanks to Jack Blumenfeld for assembling such a stellar group of writers on intellectual property! I knew the subject was important, but I had no idea how genuinely engrossing it could be. At a time when we are fighting to preserve our national scientific and industrial supremacy, this is front line law. Peter Stone's article on industrial espionage seemed to me like a spy thriller until the revelation of multi-million dollar extortion attempted against the DuPont Company, whereupon it took on the urgency of a headline.

There is also occasion for great local pride in the Connolly-Parsons tribute to Judge Caleb M. Wright. To most, lawyer and layman alike, the subject of patent litigation is rarified, if not downright inscrutable. Most of us had never fully realized the extent, the importance, and the brilliance of Judge Wright's achievement and the enormous respect in which it is held nationally by the bench and the patent bar.

II - THE JANUARY ISSUE

An article of mine ("Reflections of the Resident Crab") has drawn criticism from some members of the profession. It should be borne in mind that in expressing my views I spoke *not* on behalf of the Board of Editors, the Bar Foundation, or the Delaware State Bar Association. Those views were and are strictly my own. Secondly, we should not forget that the Bar Association is on record as opposing the so-called "tort reform" package of legislation. WEW

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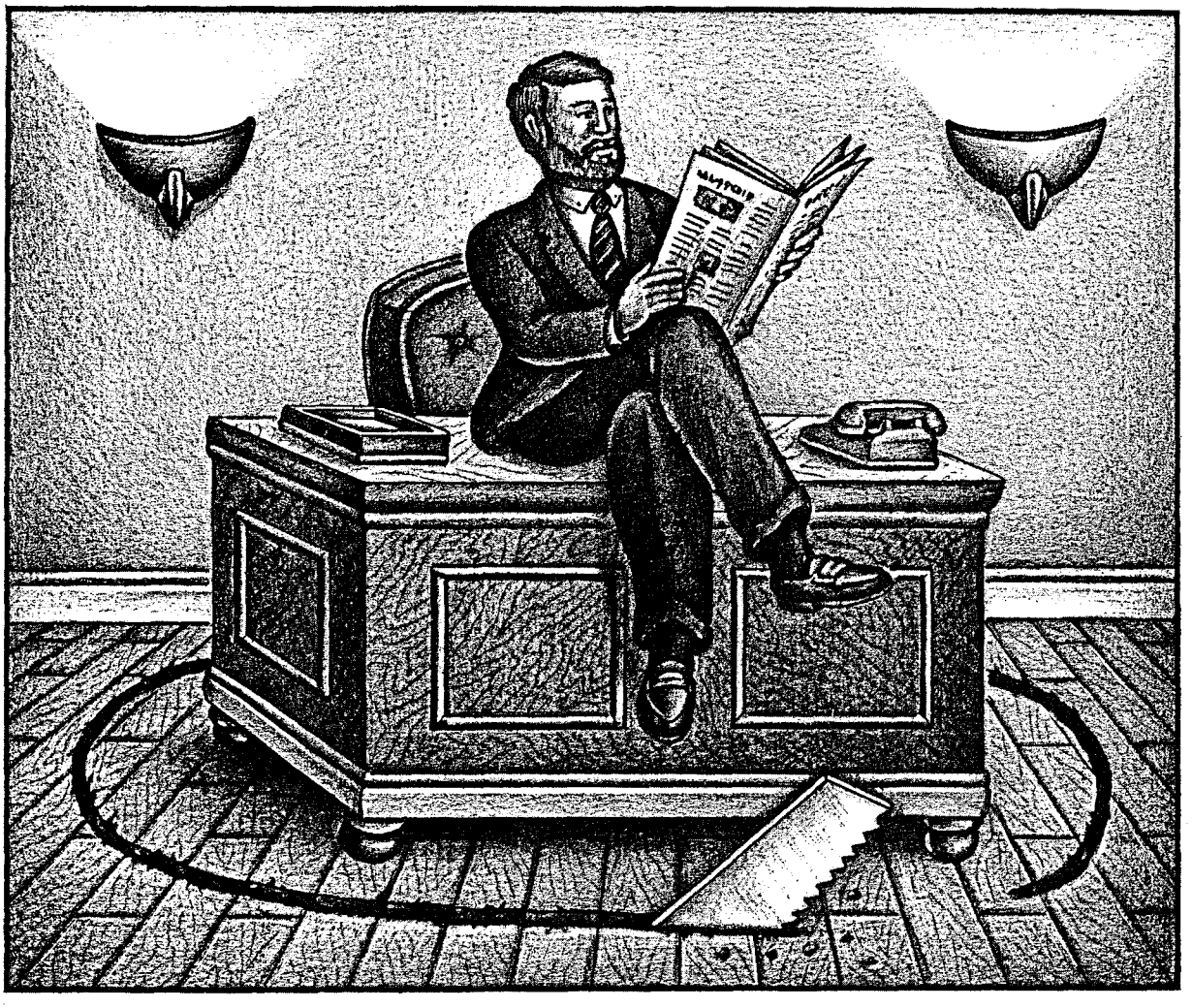

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SENIOR JUDGE CALEB M. WRIGHT'S

CONTRIBUTIONS TO THE TRIAL OF COMPLEX PATENT CASES

Arthur G. Connolly, Sr., and Donald F. Parsons, Jr.

When Senior Judge Caleb M. Wright left his active general practice in Sussex County thirty-three years ago to become a Federal Judge in Wilmington, he had never tried a patent case and probably had no interest in patents. We do not know whether Judge Wright presided over his early patent trials with apprehension or pleasure. But we do know that he speedily acquired an amazing knowledge of the complex patent laws and an ability to understand and evaluate the seemingly incomprehensible technical jargon of some patent witnesses.

These skills have been honed and applied by him to more than 100 patent cases during the past thirty years. In his decisions he has explained in clear and articulate language many intricacies of the patent statutes. He has also analyzed and rejected certain confusing or illogical principles which had long been followed by the patent bar.

The soundness of Judge Wright's patent decisions has been confirmed by his record on appeal and the frequency with which judges in other courts have cited them. His batting average before both the Third Circuit and the Court of Appeals for the Federal Circuit would undoubtedly qualify him for admission to the Judicial Hall of Fame, if and when such an establishment is created.

Judge Wright was admitted to practice in Delaware in 1933. He was appointed a District Judge in 1955 by President Eisenhower and served as Chief Judge of the District of Delaware from 1957 until October 7, 1973, when he assumed senior status. Since 1973, Senior Judge Wright has continued to handle an active caseload, including many patent cases. As recently as March 1988, for example, he presided over a patent trial involving an intraocular lens device. On August 29, 1988, with characteristic promptness, he filed a 57-page opinion holding the patent in issue invalid and not infringed. *Freeman v. Minnesota Mining & Manufacturing Co.*, 693 F. Supp. 134 (D. Del. 1988)

Judge Wright served as a member of the Judicial Conference of the United States from 1970-72. In recognition of his contributions to the development of patent law and practice, he was also made a member of the Advisory Committee to the United States Patent and Trademark Office from 1975-77.

Those active in the field took notice of Judge Wright's adeptness in handling complicated patent actions even earlier. In 1965, he accepted an invitation to address a conference of the Patent Office Society. In his remarks, which were published in the Society's Journal, he expressed concern about "the harmful effect upon the judiciary and the Patent System because of the protracted and repetitive nature of patent suits" (47 JPOS 727, 728 (1965)). He specifically criticized the then prevalent phenomenon of a patent owner whose patent had been declared invalid in a suit against one infringer, later suing a second infringer in another court and relitigating the validity issue. This practice had been condoned in *Triplett v. Lowell*, 297 U.S. 638 (1936).

Judge Wright's proposed response to that problem in 1965 presaged later developments. He stated (*id.* at 732):

> I must submit that the Court's determination of invalidity should be final to this extent, and to this extent only; that if the patentee sues for infringement of a part or all of the claims of his patent, a judgment should be final with respect to the claims declared invalid. Thus, the holder of the patent in a second suit against another defendant, who is an alleged infringer, would be estopped to relitigate the issues determined by the first court.

Attorneys today in all fields, not just intellectual property, probably would recognize that statement as a succinct summary of the current law of collateral estoppel enunciated by the Supreme Court in 1971 -- six years later -- in *Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation*, 402 U.S. 313 (1971).

Judge Wright also observed that patent cases are "notoriously complex and time consuming" (*id.* at 728). He therefore suggested that in complex cases it might be useful for the Court to have independent technical assistance. In recent years, more district judges have begun to make use of independent experts in patent cases. In addition, in 1982, Congress provided for technical experts to be included on the staff of the then newly-created Court of Appeals for the Federal Circuit to assist its panels in the adjudication of patent appeals, over which the new Court has exclusive jursidiction.

Regrettably, Judge Wright's concerns about the protracted nature of patent litigation have proved all well-founded. Indeed, his own experience simply underscores the wisdom of his concluding comment in 1965 (*id.* at 735):

> What is required to solve the problems facing the Patent System and the Courts are the same as Mr. Edison said were needed to invent, 10% inspiration and 90% perspiration.

During his tenure, Judge Wright has presided over several protracted patent cases, at least one of which has lasted over thirty years!

His most protracted case, *Devex Corp. v. General Motors Corp.*, Civil Action No. 3058, began in 1956 and is still pending through no fault of Judge Wright, who has issued *nine* reported opinions in the case. The plaintiff (Devex) filed its complaint in the federal court in Chicago, al-

leging infringement of a patented process for cold-forming automobile bumpers. After a separate trial on validity, the Chicago court held the patent invalid, but the Seventh Circuit reversed and remanded for a trial on the issues of infringement and damages. In 1965, Devex obtained a transfer to Delaware. Since then, the case has been shuttling back and forth among Judge Wright, the Third Circuit and the Supreme Court. The infringement issue was finally resolved after a lengthy trial and appeal. A Master tried the ensuing damages issue. After reviewing and affirming most of the Master's rulings, Judge Wright entered a final judgment in 1986. The portion of his decision awarding the patent holder prejudgment interest was later affirmed by both the Third Circuit and the Supreme Court, and has now become the controlling law in all federal courts.

After the Supreme Court's mandate issued, the question of postjudgment interest was briefed, argued and resolved by Judge Wright. Although additional appeals were taken, his judgments were again affirmed.

Judge Wright's batting average would undoubtedly qualify him for admission to the Judicial Hall of Fame, if and when such an establishment is created.

When the case was finally returned to the District Court, additional non-patent issues were raised by the plaintiffs and rejected by Judge Wright, who stated in his ninth reported opinion that the case "threatens to outlast all human participants." *Devex Corp. v. General Motors Corp.*, 638 F. Supp. 940, 941-42 (D. Del. 1986). His ruling was then appealed to the Federal Circuit which held that it did not have jurisdiction and transferred the appeal to the Third Circuit, which affirmed. Plaintiffs again petitioned for certiorari to the Supreme Court, attacking the decisions of both the Federal Circuit and the Third Circuit.

While the petitions were pending, the Supreme Court remanded the *Devex v. General Motors* case to the Third Circuit on jurisdictional grounds with instructions to review its earlier opinion in light of the Court's decision in another case regarding the Federal Circuit's jurisdiction. The Third Circuit recently complied with this mandate and affirmed its original decision (857 F.2d 197). Predictably, Devex's successor (Technograph) has filed another petition for *certiorari* (57 U.S.L.W. 3454). Thus, the *Devex* case persists -- having already outlasted many of the human participants.

Early in his judicial career Judge Wright concluded that discovery was the most expensive and abused stage in patent litigation. One or both parties frequently indulged in interminable discovery. Because of the complex technology involved it is sometimes more difficult to control patent discovery than discovery in ordinary civil litigation. Even though court rules provide for the early establishment of discovery cut-off dates, these dates are repeatedly extended in patent cases upon counsel's assurances that additional discovery is essential. In retrospect, however, the necessity for the extensions is frequently questionable.

Among Judge Wright's outstanding contributions to the patent field was his acceleration of customary discovery procedures. Years before the District Court's Local Rules were amended to formalize such requirements, Judge Wright insisted that counsel confer and attempt to reduce the areas of disagreement before filing a motion of any complexity. He has also urged a close liaison between trial counsel and house counsel because it facilitates more meaningful and productive discovery.

Patent litigation often involves discovery into the circumstances under which a patent was granted, the existence of any counterpart patents in foreign countries and the patentee's efforts to enforce the patent against others through licensing or litigation. In each instance, there may be communications between the patent owner and attorney or patent agent (a non-lawyer authorized to prosecute patent applications in the Patent and Trademark Office ("PTO")). Sometimes there are also communications with foreign patent attorneys or agents regarding counterpart applications or patents in countries such as England, Germany or Japan. Consequently, discovery in patent litigation tends to involve more claims of attorney-client privilege and work product immunity than other litigation.

In patent law, as in other contexts, privilege questions can be difficult and time-consuming. Judge Wright helped clarify this area when he decided *Hercules Inc. v. Exxon Corp.*, 434 F. Supp.

(Continued on next page)

(Wright continued)

136 (D. Del. 1977), a seminal opinion on the application of the attorney-client privilege and work product immunity to communications with patent attorneys and agents. *Hercules v. Exxon* manifests Judge Wright's ability to combine his knowledge and understanding of general legal principles with an appreciation of the practical aspects of patent practice, both before the PTO and in the courts. The principles he enunciated continue to provide the analytical framework for resolving most patent-related privilege issues in this District. Indeed, *Hercules v. Exxon* has been cited approximately 85 times by courts all over the country, including the United States Supreme Court, the Third Circuit Court of Appeals, and numerous state courts.

In *Hercules v. Exxon*, Judge Wright dealt with a panoply of privilege issues. After reviewing the general requirements for a claim of attorney-client privilege, he held that:

- Privileged communications to or from an attorney may, under appropriate circumstances, be protected regardless of whether the attorney is outside counsel, house counsel, or patent department counsel.
- Even an implicit request for legal advice can be sufficient to justify treating a communication as privileged.
- Communications with an attorney containing primarily business advice are not privileged.
- Routine transmittal and acknowledgment letters to or from attorneys generally are not privileged.
- Communications with a patent agent, as opposed to an attorney, can be privileged in certain circumstances.
- Technical information communicated to a patent attorney, not calling for a legal opinion or interpretation, but meant primarily for aid in completing a patent application is not privileged.
- Documents prepared for one case are generally entitled to work product protection in a later case involving closely related parties or subject matter.
- Neither the attorney-client privilege nor work product immunity applies to communications in furtherance of a crime or fraud.

In addition, Judge Wright outlined the principles for determining the applicability of privilege and work product protection in both *ex parte* patent prosecution matters and *inter partes* proceedings in the PTO, such as interferences. The frequent reliance of other courts on Judge Wright's privilege analysis in *Hercules v. Exxon* attests to his skills as a jurist.

At a later stage in the same action, he analyzed and explained several basic patent statutes dealing with the "prior art", the evidence necessary to prove or disprove that an invention is "obvious", the essential requirements of a patent specification, and the importance of appropriate claim language. *See* 497 F. Supp. 661 (D.Del. 1980)

Addressing another knotty procedural issue in *General Tire & Rubber Co. v. Watson-Bowman Associates, Inc.*, 74 F.R.D. 139, 141 (D. Del. 1977), Judge Wright held that a claim of fraud or inequitable conduct before the Patent Office is equitable in nature and does not, of itself, give rise to a right to a jury trial. Ten years later, the Federal Circuit explicitly approved Judge Wright's analysis and used it as a starting point in one of its more controversial decisions, *Gardco Manufacturing, Inc. v. Herst Lighting Co.*, 820 F.2d 1209, 1212 (Fed. Cir. 1987). The *Gardco* court held that the lower court had not abused its discretion in ordering a separate non-jury trial on inequitable conduct before the issues of infringement and validity were presented to a jury.

In one case Judge Wright stated in his ninth reported opinion that the case "threatens to outlast all human participants."

In his many years on the bench, Judge Wright has presided over cases involving a wide spectrum of inventions, ranging from relatively straightforward improvements in established technologies to pioneer inventions, which have revolutionized their fields. Many have involved ordinary household items, such as wet-strength paper towels, sour cream, potato buds, and Maxim freeze-dried coffee. One pioneer patent on a household item, litigated before Judge Wright in the mid-1960's, was the process for making Corning Ware. Other cases have involved inventions relating to products for stimulating hair growth, designs for portable and color televisions, soft contact lenses, cartridge-type fountain pens, carpet backing, reduced glare windows, and tomato harvesters.

Judge Wright is perhaps best known among patent attorneys for a number of landmark decisions he has rendered in the chemical area. In *Studiengesellschaft Kohle m.v.H. ("SGK") v. Dart Industries, Inc.*, 549 F. Supp. 716 (D.Del. 1982), *aff'd*, 726 F.2d 724 (Fed. Cir. 1984), for example, he held a patent on so-called "Ziegler catalysts" for the polymerization of ethylene, propylene, and other lower olefins, to be valid and infringed. He found that the invention represented a revolutionary new system and an important commercial breakthrough (*id.* at 736):

> There can be no doubt that the '115 [patent] was an enormous commercial success. By radically changing both the conditions under which commercial polymers would be made and the physical characteristics of the polymer product, Ziegler catalysts revolutionized the plastics industry.

In fact, the patentee Ziegler received the Nobel Prize in 1963 for his work. Even such a celebrated invention, however, resulted in protracted litigation. The action was filed in 1970. But it was not until September 30, 1987, after his decision on liability had been affirmed by the Third Circuit and he had resolved a complex damages proceeding, that Judge Wright entered a final judgment in favor of the patent owner in the amount of $43,756,784.71. The Federal Circuit affirmed all aspects of that damages award in a lengthy opinion, filed December 14, 1988 (9 U.S.P.Q. 2d 1273).

In the liability opinion in *SGK v. Dart*, Judge Wright explained the difference between anticipatory and non-anticipatory prior art, and he discussed the steps for construing a patent claim and the necessity of applying the same claim construction to the basic issues of validity and infringement. He also explained the types of evidence needed to establish laches or estoppel. The Federal Circuit affirmed his decision (726 F.2d 724), characterizing it as an "unusually thorough and meticulously detailed opinion." Although the patent in issue had been frequently litigated and was expired at the time, the court referred at length to Judge Wright's analysis of the numerous issues and agreed with his conclusions of law on each one.

Among the many other decisions by Judge Wright that analyze complex patent issues and explain the applicable statutes are: *In re Frost* 398 F. Supp. 1353 (D. Del. 1975), *modified*, 540 F.2d 601 (3d Cir. 1976); and *Standard Oil v. Montedison*, 494 F. Supp. 370 (D. Del. 1980), *aff'd*, 664 F.2d 356 (3d Cir. 1981), *cert. denied*, 456 U.S. 915 (1982). His opinion in the Frost case addressed the troublesome patent fraud defenses that were raised there. He held the Frost patent invalid because it had been fraudulently procured from the Patent Office. The Third Circuit affirmed the finding of fraud, but limited the resulting unenforceability to only those claims affected by the fraud. Years later, however, the Federal Circuit rejected the Third Circuit's position and adopted Judge Wright's view that inequitable conduct renders all claims of a patent unenforceable. *See J.P. Stevens & Co. v. Lex Tex, Ltd.*, 747 F.2d 1553, 1561 (Fed. Cir. 1984), *cert. denied*, 474 U.S. 822 (1985).

In the cluster of *Montedison* cases, Judge Wright's opinion of more than 75 pages dissected and decided a group of appeals from the Board of Patent Interferences. Interference practice had been encrusted over the years with pragmatic rules of evidence directed to the basic issues of when the invention was originally conceived, when it was reduced to practice, whether conception and reduction to practice was coupled by diligence, and whether there were any intervening publications or other activities that would have prevented one or more of the inventors from receiving a patent.

Judge Wright discussed, explained and applied these arcane interference doctrines to the voluminous evidence relied on by each of the alleged inventors, and concluded that Phillips' inventor was entitled to priority. He then authorized the Commissioner of Patents "to issue to Phillips the patent for solid crystalline polypropylene" (494 F. Supp. at 456).

Judge Wright has heard numerous other cases involving esoteric technologies foreign to the layman. He has considered patents pertaining to such diverse subjects as the manufacture of synthetic rubber and polyurethane foam insulation, zeolite cracking of petroleum to produce gasoline and other products, the manufacture of transistors, and the use of monoclonal antibodies to enhance blood clotting in hemophiliacs. In each instance, he has approached the litigation before him with a deep-seated confidence in our legal system, its patent laws, and his own ability and determination to decide all issues speedily and fairly. His skillful handling of these cases has helped establish on a national scale the reputation of the District of Delaware as a forum for the expeditious and knowledgeable resolution of patent disputes. ■

Arthur G. Connolly, Sr., indisputably the dean of that segment of the bar addressing its efforts to intellectual property, is a graduate of the Massachusetts Institute of Technology and the Harvard Law School. He began his career in the legal department of Universal Oil Products Co. and subsequently worked in the legal department of the Dupont Company. In 1942 he entered private practice upon the formation of the firm that bears his name. Aside from his membership in the bars of the Commonwealth of Massachusetts, the District of Columbia, and the State of Delaware, he is admitted to practice in all United States Circuit Courts of Appeals and the United States Supreme Court. He is a Fellow of the American College of Trial Lawyers.

Mr. Connolly's co-author, Donald Parsons, is a member of the firm of Morris, Nichols, Arsht & Tunnell, where he specializes in intellectual property litigation. He is also a registered patent attorney. Before joining the Morris firm in 1979 he clerked for The Honorable James Latchum, now Senior Judge of the United States District Court for the District of Delaware.

THE IMPACT OF THE FEDERAL CIRCUIT ON DELAWARE

PATENT LITIGATION: ADVANTAGE TO THE PATENTEE

Jack B. Blumenfeld

Since October 1, 1982, the United States Court of Appeals for the Federal Circuit has had exclusive jurisdiction of appeals from decisions of the district courts in actions arising under the patent laws. *See* 28 U.S.C. §§ 1295, 1338. The Federal Circuit was created to "reduce the widespread lack of uniformity and uncertainty of legal doctrine that exist in the administration of patent law." H.R. Rep. No. 97-312, 97th Cong., lst Sess. (1981) at 23.

In its six years, the Federal Circuit has made great strides toward uniformity of patent law jurisprudence. In doing so, however, that Court has overturned numerous principles of patent law that had been well established in the District of Delaware. As a result, patent litigation in Delaware - and there seems to be as much or more of it here than anywhere else[1] - has undergone important changes, as to both substantive law and procedure.

Indeed, so many of the rules - controlling validity, enforceability and infringement of patents, damages, preliminary injunctions, and jury trials - have changed that a patent lawyer who missed the last six years might no longer recognize the playing fields. One might also be surprised at how many of the newly established principles favor the patentee.

PRELIMINARY INJUNCTIONS

Before the creation of the Federal Circuit, it was virtually impossible for a patentee to obtain a preliminary injunction against continued infringement in the District of Delaware. The standards were far more stringent than in non-patent cases. First, the patentee had to demonstrate that the patent was valid and infringed "beyond question". *Jenn-Air Corp. v. Modern Maid Co.*, 499 F.Supp. 320 (D.Del. 1980), *aff'd*, 659 F.2d 1068 (3d Cir. 1981); *Rohm & Haas Co. v. Mobil Oil Corp.*, 525 F.Supp. 1298 (D.Del. 1981). Even if the patentee could meet that standard, in order to prove irreparable injury it also had to show that the infringer "was either in bankruptcy or so financially insecure that there was serious doubt as to its ability to pay any damages..." *Jenn-Air, supra* at 332; *Rohm & Haas, supra at 1307.*

The Federal Circuit changed the standards for preliminary injunctions, to become "no more nor less stringent in patent cases than in other areas of the law." *H.H. Robertson, Co. v. United Steel Deck, Inc.*, 820 F.2d 384, 387 (Fed. Cir. 1987). The Delaware "beyond question" standard was rejected in favor of the reasonable likelihood of success on the merits standard employed in other areas of the law. *Hybritech, Inc. v. Abbott Laboratories*, 849 F.2d 1446 (Fed. Cir. 1988); *Roper Corp. v. Litton Systems, Inc.*, 757 F.2d 1266 (Fed. Cir. 1985). The District of Delaware has applied that standard in *Upjohn Co. v. Riahom Corp.*, 641 F. Supp. 1209 (D.Del. 1986), and *Johnson & Johnson Consumer Products, Inc. v. Ormco Corp.*, slip op., C.A. Nos. 87-341 (JJF), 87-547 (JJF) (D.Del. Sept. 29, 1988).

Moreover, the patentee need not show financial insecurity of the alleged infringer to make out irreparable harm. Because a patent grants to the patentee the right to exclude others from making, using, or selling the patented invention in the United States (for seventeen years), 35 U.S.C. § 154, the Federal Circuit has recognized that money damages may not be a sufficient remedy for infringement, and that lost business can itself constitute irreparable harm. *See, e.g., Atlas Powder Co. v. Ireco Chem.*, 773 F.2d 1230, 1233 (Fed. Cir. 1985).

Furthermore, where that patentee has made a "clear showing" of validity and infringement - surely less stringent than "beyond question" - irreparable harm may be presumed. In *Smith International, Inc. v. Hughes Tool Co.*, 718 F.2d 1573, 1581 (Fed. Cir. 1983), *cert. denied*, 464 U.S. 996 (1983), the Court explained that such a presumption is dictated by public policy, because the "very nature of the patent right is the right to exclude others."

Whereas preliminary injunctions in patent cases were virtually impossible six years ago in the District of Delaware, the Federal Circuit's more easily satisfied standard provides patentees with a new and powerful weapon. Indeed, in the *Johnson & Johnson* case, where each side accused the other of infringing its patent, the Court granted cross motions for preliminary injunctions.

JURY TRIALS

Patent cases frequently turn on complex technical issues - involving chemistry, biotechnology, or electronics - relating to the state of the prior art, the nature of the invention, the differences between the prior art and the invention, and whether the accused devices are the same or equivalent to the claimed invention. The trials of such issues are often lengthy - taking several weeks, if not months.

The conventional wisdom (supported by statistics) is that patentees do better before juries than judges. Jurors inexperienced in patent law may give greater deference to the government's issuance of a patent, which enjoys a presumption of validity that can only be overcome by clear and convincing evidence of invalidity. Before the creation of the Federal Circuit, however, there was doubt as to the right to a jury trial in at least very complex patent cases in Delaware.

In *In re Japanese Electronic Products Antitrust Litigation*, 631 F.2d 1069 (3d Cir. 1980), an antitrust and antidumping case, the Third Circuit addressed the right to trial by jury in complex cases. The Court concluded that due process precludes trial by jury "when a jury will not be able to perform its task of rational decision-making with a reasonable understanding of the evidence and the relevant legal standards." 631 F.2d at 1086. The Third Circuit sanctioned the denial of a jury trial where a party (usually the defen-

dant) could demonstrate that the case was technically too complex for a jury. The implication for complex patent cases in Delaware was plain.

The Federal Circuit has held, however, that patent cases are not to be treated differently from other cases insofar as the right to a jury trial is concerned. In *Connell v. Sears, Roebuck & Co.*, 722 F.2d 1542 (Fed. Cir. 1983), it held:

> So long as the Seventh Amendment stands, the right to a jury trial should not be rationed, nor should particular issues in particular types of cases be treated differently from similar issues in other types of cases...The obviousness issue may be in some cases complex and complicated, on both fact and law, but no more so than equally complicated, even technological, issues in product liability, medical injury, antitrust, and similar cases.

Later, in *SRI International v. Matsushita Elec. Corp.*, 775 F.2d 1107, 1130 (Fed. Cir. 1985) (additional opinion), Chief Judge Markey expressly rejected the Third circuit view:

> We discern no authority and no compelling need to apply in patent infringement suits for damages a "complexity" exception denying litigants their constitutional right under the Seventh Amendment...There is no particular cachet which removes "technical" subject matter from the competency of a jury when competent counsel have carefully marshaled and presented the evidence of that subject matter and a competent judge has supplied carefully prepared instructions.
>
> There is thus no warrant for limiting even complex patent litigation to an exclusive professional ritual engaged in only by lawyers and judges.

The Federal Circuit was created to reduce the widespread lack of uniformity and uncertainty of legal doctrine that exist in the administration of patent law.

In contrast to the situation in the early 1980's, the right to a jury trial in even the most complex patent cases is now clear.[2] In the two patent jury trials in Delaware since 1985 - the only ones in at least recent history - the patentees have fared well. *See Schering Corp. v. Precision-Cosmet Co., Inc.*, 614 F.Supp. 1368 (D.Del. 1985); *Dragan v. L.D. Caulk Co.*, Order, C.A. No. 84-707 (JJF) (D.Del. Jan. 29, 1988).

THE PRESUMPTION OF VALIDITY

35 U.S.C. §282 provides that "[a] patent shall be presumed valid" and that "the burden of establishing invalidity...shall rest on the party asserting such invalidity". In the Third Circuit, the presumption of validity could be weakened or overcome, however, if relevant prior art had not been considered by the Patent Examiner during the prosecution of the patent application. *Northern Engineering & Plastics Corp. v. Eddy*, 652 F.2d 333 (3d Cir. 1981), *cert. denied*, 454 U.S. 1146 (1982); *Aluminum Co. of America v. Amerola Products Corp.*, 552 F.2d 1020 (3d Cir. 1977). In such case, "the degree by which the presumption is weakened depends on a balancing of the pertinence of the newly cited art against the pertinence of the art actually considered by the Patent Office." *Aluminum Co. v. Amerola, supra* at 1025.

The District of Delaware uniformly applied that rule. *See, e.g., General Battery Corp. v. Gould, Inc.*, 545 F.Supp. 731 (D.Del. 1982). For example, in *Grefco,*

(Continued on next page)

(Federal Circuit continued)

Inc. v. Kewanee Industries, Inc., 499 F.Supp. 844, 847 (D.Del. 1980), *aff'd*, 671 F.2d 495 (3d Cir.), *cert. denied*, 454 U.S. 1086 (1981), the presumption of validity was "substantially weakened" where "several important items of prior art...were not considered by the Examiner."

In *In re Cole Patent Litigation*, 558 F.Supp. 937, 951 (D.Del. 1983), the Court again applied those principles. On appeal, however, the new Federal Circuit "squarely rejected...the view of some circuits that, where art more relevant than that considered by the examiner is made of record, the presumption of validity is destroyed." *RCA Corp. v. Applied Digital Data Systems, Inc.*, 730 F.2d 1440, 1443 (Fed. Cir. 1984).

The Federal Circuit has frequently repeated that the presumption of validity is never weakened or destroyed, and that the challenger always has the burden of overcoming it by clear and convincing evidence. *See, e.g., Stratoflex, Inc. v. Aeroquip Corp.*, 713 F.2d 1530 (Fed. Cir. 1983). As it said in *ACS Hospital Systems, Inc. v. Montefiore Hospital*, 732 F.2d 1572, 1574-75 (1984) the "presumption is *never* annihilated, destroyed, or even weakened, regardless of what facts are of record." (original emphasis)[3]

That principle benefitting patentees has now been firmly established in the District of Delaware, displacing the earlier contrary authorities. *See, e.g. Afros S.P.A. v. Krauss-Maffei Corp.*, 671 F.Supp. 1402, 1412 (D.Del. 1987), *aff'd*, 848 F.2d 1244 (Fed. Cir. 1988) ("Evidence of material uncited art in the patent prosecution does not affect the presumption of validity..."), *Phillips Petroleum Co. v. United States Steel Corp.*, 673 F.Supp. 1278, 1293 (D.Del. 1987); *Mannesmann Demag Corp. v. Engineered Metal Products Co.*, 605 F.Supp. 1362, 1365 (D.Del. 1985), *aff'd*, 793 F.2d 1279 (Fed. Cir. 1986).

SECONDARY CONSIDERATIONS OF NONOBVIOUSNESS

Under 35 U.S.C. §103, a patent claim is invalid "if the differences between the subject matter sought to be patented and the prior art are such that the subject matter as a whole would have been obvious at the time the invention was made to a person having ordinary skill in the art to which such subject matter pertains." In the landmark case of *Graham v. John Deere Co.*, 383 U.S. 1, 17-18 (1966), the Supreme Court Set forth the following test for determining obviousness:

Under §103, the scope and content of the prior art are to be determined; differences between the prior art and the claims at issue are to be ascertained; and the level of ordinary skill in the pertinent art resolved. Against this background, the obviousness or unobviousness of the subject matter is determined. Such *secondary considerations* as commercial success, long felt but unsolved need, failure of others, etc., *might* be utilized to give light to the circumstances surrounding the origin of the subject matter sought to be patented. As indicia of obviousness or nonobviousness, these inquiries *may* have relevancy. (Emphasis added)

Before the creation of the Federal Circuit, the Third Circuit and the District of Delaware consistently applied the *Graham* test by its terms, treating "secondary considerations" such as commercial success as less than obligatory. The Third Circuit had held that "secondary considerations are entitled to 'only measured weight' in adjudging obviousness,...and they cannot, by themselves, support a finding of nonobviousness if it is otherwise established that a patent's disclosures are obvious in light of the prior art."*Tokyo Shibaura Electric Co. v. Zenith Radio Corp.*, 548 F.2d 88, 94-95 (3d Cir. 1977)(citations omitted). *See also Grefco, Inc. v. Kewanee Industries, Inc., supra*, 499 F.Supp. at 857-58.

Notwithstanding the *Graham* language, the Federal Circuit has made primary the evidentiary value of such supposedly secondary considerations. In *Stratoflex v. Aeroquip Corp.*, 713 F.2d 1530, 1538 (Fed. Cir. 1983), it held that "evidence rising out of so-called 'secondary considerations' must always when presented be considered en route to a determination of obviousness" and that "evidence of secondary considerations may often be the most probative and cogent evidence in the record. It may often establish that an invention appearing to have been obvious in light of the prior art was not."[4] Contrary to the Third Circuit authorities, the Federal Circuit has held that strong evidence of secondary considerations may even save a patented invention that otherwise would have been obvious from the prior art. *W. L. Gore & Associates, Inc. v. Garlock, Inc.*, 721 F.2d 1540 (Fed. Cir. 1983), *cert. denied*, 469 U.S. 851 (1984). In *Simmons Fastener Corp. v. Illinois Tool Works*, 739 F.2d 1573, 1575-76 (Fed. Cir. 1984) *cert. denied*, 471 U.S. 1065 (1985), the Court reversed a finding of obviousness where "the evidence of secondary considerations..., particularly commercial success, is extremely strong...", even though "the teachings of the prior art prima facie would have suggested to one of ordinary skill in the art of the claimed invention."

Thus, evidence which six years ago "might be utilized," was entitled to only "measured weight," "may have [had] relevancy", and could not support a finding of nonobviousness in the face of contrary technical evidence, now "must always...be considered", "may...be the most probative and cogent evidence", and may save an otherwise seemingly obvious invention. As Chief Judge Schwartz recently put it, now the "so-called 'secondary considerations'...are of primary importance in determining obviousness." *Afros S.P.A. v. Krauss-Maffei Corp., supra*, 671 F.Supp. at 1418. Still another significant change in the Delaware patent law now favors the patentee.

As a result of the Federal Circuit's efforts to make the administration of the patent laws uniform, the applicable legal principles in the District of Delaware have changed dramatically over the last six years. Those changes are largely in favor of patentees, perhaps signaling a more favorable climate for the enforcement of patents in Delaware.[5] Whatever the results, however, there is no question that the rules are different. ■

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Jack Blumenfeld, who designed and edited this issue of DELAWARE LAWYER is engaged primarily in commercial (including intellectual property) litigation. After graduating from Yale Law School in 1977, he clerked for The Honorable Walter K. Stapleton, then of the U.S. District Court for Delaware. In 1979 he joined Morris, Nichols, Arsht & Tunnell, of which he became a partner in 1985. He is a member of the American Intellectual Property Law Association and the New York Patent Law Association.

NO CORPORATE SNUG HARBOR FOR THE PIRATE?

Personal Liability of Directors and Officers for Corporate Patent Infringement

Robert C. Kline and Joseph M. Fitzpatrick

Carol Burg

Traditionally, the corporate structure has acted as a shield to protect officers and directors from personal liability for corporate acts. In the patent field, however, the Federal Circuit appears to have adopted a rationale that will make more officers and directors liable for infringement, especially where the corporation is owned or controlled by a few officers who direct or dominate acts of corporate infringement. This position conforms to the long standing rule in the Third Circuit, which, before the advent of the Federal Circuit, had been a minority one among the various circuits. We shall examine the Federal Circuit's thus far limited dealings with the topic, the Third Circuit's position, and the law as it existed in a majority of the circuits before the formation of the Federal Circuit.[1]

In the only two instances where the Federal Circuit has been faced with the issue, it has found personal liability of officers and directors for corporate patent infringement.[2] In both instances the corporations were small ones, dominated and controlled by a very limited number of people who played active roles in everyday operations, including the infringing acts. In *Power Lift v. Lang Tools, Inc.*, the infringing corporation was completely controlled by one man, Wendell Lang, who was its founder, majority owner, president, director, and the designer of the infringing product. Likewise, the infringing corporation in *Orthokinetics, Inc. v. Safety Travel Chairs, Inc.* was dominated by a small group: three men who owned all of the stock, were the directors, and designed the infringing product.

Analysis of these two decisions makes it clear that under the case law of the Federal Circuit corporate officers or directors who dominate and direct acts of infringement may find themselves personally liable either for active inducement of infringement under 35 U.S.C. §271(b)[3] or direct infringement under 35 U.S.C. §271(a)[4]. The standard for liability differs: active inducement under §271(b) does not require piercing the corporate veil, but direct infringement under §271(a) does.

In *Power Lift* there was only active inducement, and the Court made it clear that §271(b) "recites in broad terms that one who aids and abets an infringement is likewise an infringer."[5] It should be noted that the Court specifically rejected defendant's argument that active inducement required two separate entities, whereas the "[c]orporation and its president do not in law constitute separate entities for purposes of statutes requiring multiple actors".[6]

In *Orthokinetics*, the Federal Circuit reaffirmed this potential of personal liability for active inducement of infringement and this time made it clear that this was the law regardless of whether the corporate veil can be pierced, stating:

> "corporate officers who actively aid and abet their corporation's infringement may be personally liable for inducing infringement under §271(b) regardless of whether the corporation is the alter ego of the corporate officer."[7]

The Court then addressed direct infringement under §271(a) and noted that piercing the corporate veil was a prerequisite.

> "To determine whether corporate officers are personally liable for the direct infringement of the corporation under §271(a) requires invocation of those general principles relating to piercing the corporate veil."[8]

(Continued on page 16)

(Pirate continued)

The Federal Circuit found direct infringement having noted that the President and two others controlled the infringing corporations and "were directly responsible for the design and production of the infringing chairs and were the only ones who stood to benefit from sales of those chairs."[9]

The Federal Circuit's position is in accord with the long standing law in the Third Circuit, which, however, was the minority rule and not applicable in most other circuits. In a decision rendered in 1919 *Hitchcock v. American Plate Glass Co.*,[10] the Third Circuit examined infringement by a small corporation that installed glass grinding apparatus under the direction and control of its vice president. He had organized the corporation, and owned 92% of the stock. The Court found he "completely dictated and dominated the (corporation's) business acts . . . including its infringing acts."[11] The *Hitchcock* Court explained its views of personal liability for corporate torts:

> "Where a director or manager of a corporation -- who sustains to the corporation the relation of master or principal in the sense of being its dominate force -- himself commands the commission of a tort by the corporation, though he does it as an officer and in the name of the corporation, he is individually liable... An executive officer of a corporation 'cannot shield himself behind an artificial and sometimes irresponsible creation from the consequences of his own acts, even though performed in the name of an artificial body.'" (citation omitted)[12]

The *Hitchcock* Court speaking 70 years ago left no doubt that officers with power to command infringement of a patent by their corporation were potentially liable as joint tortfeasors.[13]

> "When a corporation infringes in obedience to the command of an officer with power to cause the corporation to commit or refrain from committing the infringing act, and when that officer participates in and contributes to the infringement, they are in the eyes of the law joint tortfeasors and both are liable, in the same or in different measures according to the circumstances, for the injuries they have jointly inflicted upon the one whose rights they have jointly invaded."[14]

The dominant vice president was found liable because the court found "as an officer of the corporation he inspired, directed and brought about the infringement."[15] This was consistent with the law at the time as exemplified by *National Cash-Register Co. v. Leland* which had applied a strict standard for liability to officers and directors of corporations that infringe patents.[16]

Faced with rising directors' and officers' liability insurance costs, Delaware added a section to the General Corporation law, relieving directors of some personal liability. However, no relief is afforded directors under Delaware law for violations of federal statutes.

Despite the passage of nearly seventy years, *Hitchcock* has remained the law in the Third Circuit. In 1963 the *Hitchcock* doctrine was used successfully to join the individual owners of a small Puerto Rican pharmaceutical manufacturer as defendants with their corporation because of their control, domination, and direction of the acts of the corporation.[17] As a result, after trial on the merits, a permanent injunction was issued in *Merck v. Chase* enjoining the sale of the infringing Vitamin B12 by the individual officers as well as by the corporation. Additionally, they were liable together with the corporation for damages resulting from the infringement.[18] The *Hitchcock* rule still surfaces from time to time whenever the Circuit is confronted with a small corporation engaged in illegal conduct.[19]

The Federal Circuit's decisions do not refer to the minority rule of *Hitchcock* nor do they refer to the previous majority rule typified by *Dangler v. Imperial Machine Co.*:

> "This court has heretofore taken the position first announced, namely, that the officers are not liable unless they act outside the scope of their official duties. *Crazier v. Mackie-Lovejoy Mfg. Co.*, 138 F. 654, 71 C.C.A. 104;
>
> ". . . we adhere to the *Crazier v. Mackie-Lovejoy Mfg. Co.*, decision, and hold that, in the absence of some special showing, the managing officers of a corporation are not liable for the infringements of such corporation, though committed under their general direction. The uncertainty surrounding the questions of validity and infringement make any other rule unduly harsh and oppressive."[20]

Under the *Dangler* rule, a finding of willful infringement was a requisite to establish the "special showing"[21] such as would establish individual liability of the officers. but the Federal circuit in *Orthokinetics* has expressly rejected willfulness as a prerequisite:

> "However, that does not mean that their acts must rise to the level recognized by the law as constituting willful infringement before they can be liable for infringement by their corporation."[22]

Recent district court decisions give a good overview of the potential liabilities faced by officers and directors of small businesses within the Circuit. In *Max Daetwyler Corp. v. Input Graphics, Inc.* it was held that when officers' acts are "willful or deliberate" the officers can be held personally liable along with the corporation.[23] In *A. Stucki Co. v. Schwam*,[24] a small corporation, 50% of which was owned by its president and director, Mr. Schwam, had infringed the plaintiff's patent on railroad car shock absorbers. Following the Federal Circuit's ruling in *Orthokinetics* the court held that now showing of willfulness or intent to infringe was required and went on to hold that merely a high level of personal participation, such as existed here, was necessary for personal liability to attach.

While Delaware has taken steps to shield corporate directors from personal liability, which may arise in various general corporate situations, these efforts are ineffective with regard to patent infringement. Faced with rising directors' and officers' liability insurance costs, Delaware added a section to the General Corporation Law, which relieves directors of some personal liability for money damages, provided that the corporation's original charter or an amendment to its certificate of incorporation so provides.[25] However, no relief is afforded directors under Delaware law for violations of the federal statutes, which, of course, would include any patent infringement violations of 35 U.S.C. §271.

In light of these developments in the Federal Circuit, it is more important than ever that officers and directors take precautions to protect themselves from possible liability for patent infringement. Thus far the cases have dealt with smaller corporations, but the potential for applying 35 U.S.C. §271(b) to larger corporations is clearly present. While it is not necessary for officers and directors of major corporations to insulate themselves

completely from the decision making process when infringing activity is contemplated, they must be sure to work within the corporate structure to avoid any possible appearance of inducing infringement and consequent liability under 35 U.S.C. §271(b). Carefully designed corporate committee procedures should be established and maintained requiring thorough study and approval before any infringing activity is commenced. Obtaining in good faith an opinion of competent counsel prior to any infringement should be an integral part of such procedures. While a finding of willfulness is no longer essential for a finding of personal liability, its clear absence will be of assistance in avoiding such a result.

In the case of smaller corporations where control is clearly in the hands of one or two officers or directors, the risk of personal liability for patent infringement will always be a fact of life.

As a standard practice counsel should advise corporate officers and directors of the risks of personal liability for infringing acts by the corporation, particularly in smaller, closely controlled companies. All steps possible to make the record clear that any infringement occurred only after competent legal advice and as a part of legitimate corporate practices should be taken to avoid all appearance of impropriety. ■

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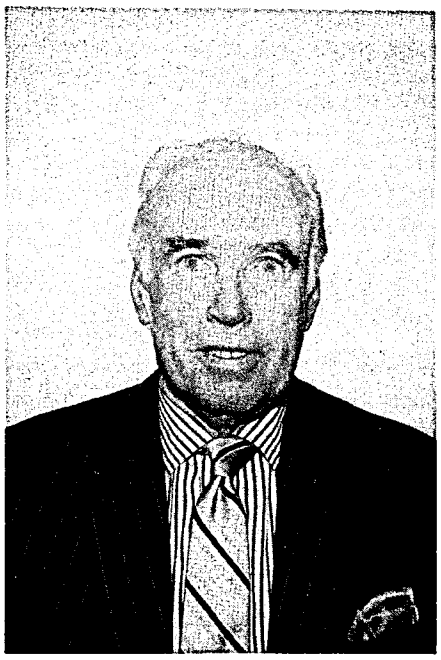

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AT THE END OF THE SECOND RAINBOW

CALCULATION OF DAMAGES IN PATENT CASES

N. Richard Powers

While patent law is viewed generally as an arcane or esoteric subject, the damages phase of a patent trial referred to as the "accounting proceeding," is often the most obscure and complex part.

Despite the obscurity of the term, accounting proceedings are high stakes litigation over millions of dollars. During my time as United States Magistrate, I presided over an accounting proceeding in the capacity of a Special Master and had a first-hand opportunity to observe the passage of a complex piece of litigation through its final trial phases. *Thomas & Betts Corp. v. Winchester Electronics Div. of Litton Systems, Inc.*, C.A. No. 78-552 (*"T&B"*). That experience serves as a backdrop for this discussion, which is intended to provide the general practitioner with an overview of the procedures and issues involved in the accounting phase of a patent trial. To begin, consider the following scenario:

X Corporation has finally prevailed in its long fight to enforce its patents. After more than five years since X filed suit, and after 30 months of post-trial briefing, the district issues a decision that X's patents are valid and infringed. Some six months later, the Federal Circuit Court of Appeals affirms. There is a subsequent denial of certiorari by the Supreme Court, and X Corp. is finally entitled to recover damages from the infringing Y Corp. All the Court has to do is enter judgment in its favor. Final vindication is in sight. Or is it? After each party has invested perhaps more than a million dollars in attorney fees contesting liability, it is not unusual for the parties to be literally ten of millions of dollars apart in their view of an appropriate measure of damages. Occasionally the parties will agree on the amount of damages, but if they do not, the dispute can lead to another trial (the accounting proceeding), and further appeals.[1]

The accounting proceeding may be quite time consuming, and not infrequently the district judge will appoint a special master to conduct a hearing and file a report with the Court. In some instances the accounting proceeding may actually be lengthier than the liability trial. The case on which I sat as Special Master several years ago is a good example. The trial on the liability issues lasted less than two days while the accounting proceeding consumed three weeks.

The statute governing a patentee's rights to damages is relatively straightforward. "Upon finding for the claimant the court shall award the claimant damages adequate to compensate for the infringement but in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court."[2] Such a generalized directive leaves the district court with wide discretion in choosing a methodology for assessing and computing damages in a patent infringement suit.[3] As the statutory language makes clear, the court is not limited to awarding a "reasonable royalty," but may also take into consideration the profits the patent holder lost as a result of the infringement.[4]

A. Lost Profits

For the patent holder, an award of its lost profits can be likened to finding the proverbial pot of gold. It is, however, subject to a comparatively strict standard of proof. Generally the patent holder must demonstrate that "but for" the infringement, it would have made the sales made by the infringer.[5] However, the patent holder is not required to disprove any possibility that the purchasers might have bought a different product or might have foregone the purchase altogether.[6] "It is impossible . . . for the patent owner to negate every possibility that the purchaser might not have bought another product."[7] The "but for" test only requires the patentee to adduce proof to a reasonable probability that some or all of the sales would have been made by the patent holder but for the infringement.[8]

In some instances the accounting proceeding may actually be lengthier than the liability trial.

The substantive element of the "but for" test as developed by case law is in four parts. The patent holder must show (1) demand for the patented device in the marketplace; (2) the absence of acceptable non-infringing alternatives to the patented device; (3) the production and marketing capacity to meet the increased demand; and (4) computations on the dollar loss of profits.[9] Each of these elements will be briefly discussed below.

(1) Demand

This is rather straightforward: a showing of a long history and continuous volume of sales by the patent holder.[10] Substantial sales of the potential device by the infringer is also considered compelling evidence of demand for the patented product.[11]

(2) Capacity

This requires proof of existing produc-

tion capacity, and the financial and marketing resources of the patent holder to cover expanded production capacity. A patent holder will only rarely be unable to establish that it had the capacity to make the infringer's sales. Reportedly, in only three cases have courts concluded that the patent holder did not have the capacity to make the infringing sales.[12] For example, where the patent owner had the *resources* to expand, the courts have not required it to show that it had a plant existing and ready to produce.[13] One court even concluded that the patent holder had the capacity to make the patented product on finding that it could have subcontracted out the work without adversely affecting its profit margin.[14]

(3) The absence of acceptable, non infringing alternatives

This element of proof can be broken down into three subquestions: (a) whether specific products were actually on the market and available for immediate purchase by customers, and if so, when; (b) whether such products were acceptable alternatives to the infringing device; (c) whether such products also infringed the patent in suit. Elements (a) and (b) can be proven by expert testimony as to what alternative products were available in the market place and whether purchasers of the infringing product would have been likely to buy the alternative products if the infringing product had not been present in the marketplace.[15] The patent holder will probably have introduced much of the same type of evidence during the liability phase of the litigation to establish that the patented product fulfilled a long felt need for a particular invention in the market place, which could not be met by existing products, evidence supporting the validity of the patent.[16] Element (c) permits the patent holder to prove that any specific acceptable alternatives to the infringing product also are infringements of the patent. As a matter of public policy, sales by third party infringers may not be relied on by the defendant, because those sales are likewise unlawful and the defendant should not be able to minimize his liability by pointing to other unlawful competitors in the marketplace.[17]

If the court determines that there is no acceptable, noninfringing alternative in the marketplace, the inference can be readily drawn that the patent holder would have made the infringing sales but for the infringer's tortious conduct.[18] Likewise in situations where the sales volume or market share of the acceptable non-infringing alternatives is inconsequential, the inference can be drawn that the patent holder would have made a substantial percentage of the infringer's sales.[19]

(d) Calculation of lost profits

In addition to establishing demand, capacity, and the absence of acceptable, noninfringing alternatives in the marketplace, in order to be entitled to lost profits, the patent holder must offer evidence from which the court can reasonably determine the amount of its loss. The burden is lessened by application of the general principle that determination of "what might have been" is not always amenable to a precise determination. While mere guesswork is not sufficient to determine lost profits, justice requires the risk of any uncertainty to be borne by the wrongdoer instead of the injured party.[20] Generally it is sufficient if the patent holder makes a reasonable estimate of the profit per device it would have made but for the infringer's unlawful competition. Proof of profit per

(Continued on next page)

device should be based on data the patent owner uses in the ordinary course of business for other purposes, such as standard unit costs, fixed operating expenses, variable operating expenses, etc.[21] When this figure is multiplied by the number of infringing products sold by the infringer, a calculation of lost profits attributable to the infringer's unlawful competition can be made.

Lost profits are not limited to lost sales. The patent holder may also recover lost profits from price erosion, that is, the decline in sales price occurring if the patent owner has been forced to sell its patented product at a price below its established price in order to avoid losing sales to the infringer.[22] The right to recover damages caused by price erosion stands on the same ground as the right to damages for unlawful or unfair competition, but proof is often more difficult. For example, in the case of lowered prices at times when the market includes several infringers, the situation I found in the *T&B* case, the patent holder simply could not establish that its lowered prices were a result of the defendant's unlawful competition as opposed to the third parties' unlawful competition. As another example, the patent holder may not be able to prove with reasonable probability that its lowered prices were the result of the infringer's unlawful competition, if the patent holder has a history of granting discounts to steady high volume customers.

A third aspect of a lost profits case is what is termed lost "convoyed sales" or "spillover profits", that is sales of unpatented items that the patent holder offers for sale in conjunction with its patented devices. Some examples of convoyed sales would be accessories sold with a patented machine, parts and supplies designed for the patented machine, and unpatented products used in the installation of the patented system.[23] As with lost sales, the patent owner must prove that in all reasonable probability it would have made the sales which the infringer made.[24] In addition to making a correlation between the infringer's sales mix and the patent owner's normal sales mix, the patent holder will also need expert testimony on such topics as the marketing approach used in the marketplace,[25] and whether the unpatented items can be used independently of the patented product.[26] Since there may be additional third party infringers in the marketplace who are also offering unpatented items for sale, as well as companies that are fairly competing in the business of supplying unpatented items, proof that the patent holder lost spillover profits as a result of the infringer's unlawful competition is probably even more difficult than proving price erosion.[27]

Reasonable Royalty

Even if the patent owner is not able to convince the court that it is entitled to lost profits, all is not lost. Section 284, cited earlier, provides that the patent holder is entitled to no less than a reasonable royalty. Developing case law has established a comprehensive list of factors that a court should consider in determining a reasonable royalty: (1) the royalties received by the patentee for the licensing of the patent in suit, proving or tending to prove an established royalty; (2) the rates paid by the licensee for the use of other patents comparable to the patent in suit;

In one case the original trial was confined to infringement by one product. The accounting proceeding examined a dozen more potentially infringing products, thereby transforming the later proceeding effectively into a dozen infringment trials, in which the damage tail wagged the liability dog.

(3) the nature and scope of any license granted; (4) the licensor's established policy and marketing program to maintain its patent monopoly by not licensing others to use the invention; (5) the commercial relationship between the licensor and licensee, such as whether they are competitors in the same territory in the same line of business; (6) the effect of selling the patented specialty item in promoting sales of other products of the licensee, the existing value of the invention to the licensor as a generator of sales of his non-patented items, and the extent of such derivative or convoyed sales; (7) the duration of any license granted and the term of such license: (8) the established profitability of the product made under the patent, its commercial success, and its current popularity; (9) the utility and advantages of the patent property over the old modes or devices, if any, that had been used for working out similar results; (10) the nature of the patented invention, the character of the commercial embodiment of it as owned and produced by the licensor, and the benefits to those who have used the invention; (11) the extent to which the infringer has made use of the invention, and any evidence probative of

the value of that use; (12) the portion of the profit or of the selling price that may be customary in the particular business or in comparable businesses to allow for the use of the invention or analogous inventions; (13) the portion of the reasonable profit that should be credited to the invention as distinguished from non-patented elements, the manufacturing process, business risks, or significant features or improvements added by the infringer; (14) the opinion testimony of qualified experts; and (15) the amount that a licensor and licensee such as the infringer would have agreed upon at the time the infringement began if both had been reasonably and voluntarily trying to reach an agreement.[28] Although many of the factors will have no relevance in a particular case, the list is broad enough to provide at least qualitative guidance in every patent case. It is noteworthy that all of the items of evidence required to be presented to support a claim for lost profits are also a relevant considerations in determining a reasonable royalty, so that even if the lost profits claim should fail for want of sufficiency of proof, nonetheless under the *Georgia - Pacific* list of factors, a court may take such evidence into account in determining a royalty sufficient to fully compensate the patent holder for infringement of its patent.

It is especially noteworthy that what a willing licensor and a willing licensee voluntarily trying to reach an agreement might have considered a reasonable royalty is but one factor for the court to consider in setting a reasonable royalty. As the Court made clear in *Panduit*, 575 F.2d at 1158-59, if a reasonable royalty were merely the equivalent of what was arrived at in negotiations between a willing buyer and a willing seller, every infringer would in effect be entitled to receive a compulsory license from every patent owner. Every infringer would be in a "heads-I-win, tails-you-lose" position since the patent owner, after years of expensive litigation and no guarantee of winning, could count on receiving no more than the normal routine royalty a licensee would have paid. As the court indicated, in rather colorful terms, the expression "reasonable royalty" is actually a misnomer:

"Determination of a 'reasonable royalty' after infringement, like many devices in the law, rests on a legal fiction. Created in an effort to 'compensate' when profits are not provable, the 'reasonable royalty' device conjures a 'willing' licensor and licensee, who like Ghosts of Christmas Past, are dimly seen as 'negotiating' a 'license'. There is, of course, no actual willingness on either side and no license to do anything, the infringer being normally enjoined. . . from further manufacture, use, or sale of the patented product."[29] Consequently, although the patent holder's proofs for lost profits may be insufficient, the same evidence should enable him to obtain a "reasonable royalty" adjusted substantially upward from what might have been determined in arms-length negotiations between a willing buyer and a willing seller.

INTEREST

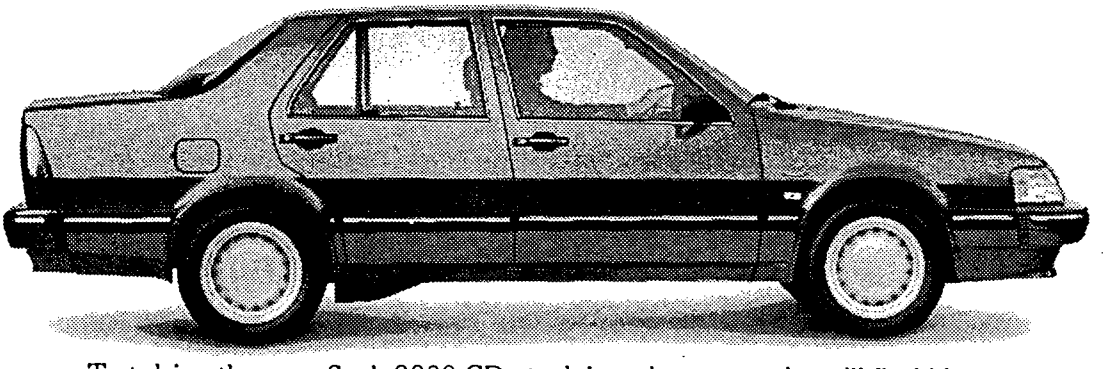
The Supreme Court has made clear that in patent infringement actions prejudgment interest should ordinarily be awarded where necessary to afford the patent owners full compensation for the infringement, to ensure that the patent owner is placed in as good a position as it would have been had the infringer entered into a reasonable royalty agreement.[30] Moreover, the compounding of prejudgment interest is a matter within the discretion of the trial court where compounding is appropriate in order to place the patent holder in as good a position as it would have been but for the infringer's unlawful competition.[31] The method of ascertaining an appropriate interest rate, as for example considering the patent owner's short-term borrowing and lending rates during the years of infringement, and the time within each year for accruing the damages, etc., are also matters within the court's discretion in order to make the patent owner whole.

In a long-running patent case, the amount of prejudgment interest at stake can be considerable. For example, in the *T&B* case, the patent holder was awarded damages in the amount of $3.7 million plus prejudgment interest of $2.0 million for a total judgment of $5.7 million. In *Devex* the amount of damages was approximately $8.8 million while prejudgment interest exceeded $11 million.

Just as a baseball game "is not over 'till it's over", the same may be said of patent litigation. The patent holder may succeed in convincing the courts that its patents are valid and infringed, but if it falters during the accounting stage, its reward

(Continued on page 23)

As nice as the new Saab 9000 CD looks, it can be mean if it has to.



Test drive the new Saab 9000 CD at a leisurely pace and you'll find it's a paragon of esthetic delights. After all, the 9000 CD has the handsome lines of a classic European touring sedan. It also has the interior comfort you'd expect in a world-class luxury car.

Drive a little faster and you'll discover delights of a more primal nature. The 9000 CD has front-wheel drive, rack-and-pinion steering, front and rear stabilizers and gas shock absorbers. It also has a 16-valve, intercooled, turbocharged engine.

The point is, instead of having to choose between luxury and performance, you can now have both...in the new Saab 9000 CD.

Test drive one soon.

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(Rainbow continued)

may be disappointingly small. That little understood but complex, final aspect of the patent litigation, the accounting proceeding, can determine the true winner and loser of the litigation. ■

Footnotes at page 26

Mr. Powers, a graduate of St. Joseph University and of the Villanova University School of Law, clerked for then Chief Judge James Latchum of the United States District Court for Delaware upon his graduation from law school. He subsequently became an associate and later a member of the firm Connolly, Bove, & Lodge. Between 1980 and 1988 he was the first full time United States Magistrate for Delaware. Since February 1988 he has been a partner and once again at his former firm, now Connolly, Bove, Lodge & Hutz.

THE INDEPENDENT INVENTOR

In which a practitioner shares some highly practical advice for safeguarding the products of intellectual labor.

Albert F. Bower

Every inventor of a discovery in a novel process, machine, manufacture, composition, or improvement thereof or in an ornamental design, and every author of a literary expression is entitled to an opportunity to seek for a limited time an exclusive right to the enjoyment thereof.[1] My intent here is to assist the independent inventor in ascertaining and protecting those rights provided under the U.S. Constitution and the Patent Statutes.

The "independent inventor" is an entity of one or more persons having rights in the subject idea without obligation to others at the time of the invention. Individual or independent inventors have been characterized as falling into a class separate from other inventors. The individual independent inventor is referred to as working alone on his own resources.[2] Under 37 C.F.R. 1.9(c) an independent inventor is one who has not assigned any rights in the invention and is not obligated to assign to anyone who is not an independent inventor or not qualified as a small business or nonprofit organization.[3] In general, the independent inventor is distinguishable from the person working in cooperation with others in a large business concern. "The Sources of Invention"[4], commenting on individual inventors, states on page 253:

> "...for the individual inventor or small producer struggling to market a new idea, the patent right is critically important..."

The intellectual property recognized by Article I, Section 8 of the United States Constitution mainly includes United States patents (utility, design, and plant) and copyrights, which give their owners exclusive rights for a limited number of years. Copyrights are registrable. Registration gives the owner the exclusive right to reproduce or distribute the work for the life of the author plus 50 years.[5] Utility patents are granted for invention in a new and useful process, machine, manufacture or composition of matter, or any new and useful improvement thereof.[6] Design patents may issue on an ornamental design for an article that presents a pleasing aesthetic appearance.[7] Plant patents may issue for a distinct and new variety of plant.[8] A patent gives the owner the exclusive right to make, use, sell or license novel subject matter for a period of years. The period is 17 years for utility patents.[9]

A trade secret is the subject of a right to withhold useful information from public knowledge because it was obtained by the owner through expenditures of time, money, or both. This form of intellectual property is not a subject of this article.

Most innovations produced by independent inventors or authors relate to utility patents or copyrightable works. Registration by the Copyright Office of a copyright in a "work of authorship" is a simple procedure consisting mainly of filling out the appropriate form. Prompt registration is advisable, but in obtaining registration independent authors do not require the kind of counseling that is advantageous in seeking a utility patent.

The copyright law provides protection for an original work, but only to the author's expression of the original idea found in his work and not to the substance when differently expressed.[10] Consequently, the copyright law does not provide effective protection to advances in technology. It is under the patent laws that ideas are protected, and protecting ideas is what is important to the independent inventor.

The American attitude toward mechanical ingenuity is that it should be applied to simple problems of living.[11] A purpose of the U.S. patent system is to foster this kind of invention by providing appropriate protection to this type of advance, and improvements in day-to-day experiences is the what independent inventors tend to produce. Thus protecting the novel ideas of independent inventors is a basic purpose of the U.S. Patent system.

It has been stated that most inventions by independent inventors have not resulted in patent protection because of the costs of obtaining it.[12] To avoid or reduce attorney costs, it has been proposed that the inventor file and prosecute his own case. In advocating the "pro se" prosecution approach, it is proposed that the inventor save expense by letting the Patent Office make the search and provide consultation on the procedural and technical matters.[13]

"Pro se" prosecution is recognized in the Patent Office Rule, 37 C.F.R. 1.31.[14] It has, however, serious shortcomings because of the problems encountered in providing an adequate disclosure in the application. The problems that arise with prosecution of a patent application "pro se" are reflected in the provisions of the Manual of Patent Examining Procedure.[15] This manual provides instructions on the practices and procedures for the prosecution of patent applications in the Patent and Trademark Office. In the instructions to the Examiners on handling "pro se" applications, the Manual conditions its authorization of assistance to the "pro se" applicant on the Examiner's finding that there is patentable subject matter disclosed in the application.[16] Thus, the assistance is provided to "pro se" applicants only after a determination by the Examiner of the presence of patentable subject matter in the application. In turn presence of patentable subject matter depends upon an adequate disclosure under the Patent Statutes, the Patent Office rules, and the Manual of Patent Examining Procedure.

The essentials of an adequate disclosure are set forth in the Patent Statute and in Title 37 of the Code of Federal Regulations, which contains the rules of

practice in the Patent and Trademark Office. For example, 35 U.S.C. Sec. 112, first paragraph requires:

> "... a written description of the invention, and of the manner and process of making it and using it, in such full, clear and concise and exact terms as to enable any person skilled in the art to which it pertains, . . . to make and use the same..."

7 C.F.R. 1.81 requires that the applicant furnish a drawing of the invention where it is necessary to understanding the subject matter. The Manual of Patent Examining procedure states that the lack of such drawing renders an application incomplete, and the application cannot be given a filing date.[17]

The existence of these requirements and the difficulty the "pro se" applicant may have in complying are reflected in the instruction to Examiners in the Manual at Section 401. The Manual provides that if it appears that the "pro se" applicant is unfamiliar with proper preparation and prosecution of patent applications, the examiner may suggest to the applicant the desirability of employing a registered patent attorney or agent. Furthermore, a pamphlet on patent issued by the U.S. Government Printing Office has stated that "the preparation of an application is a highly complex proceeding and cannot be conducted properly except by an attorney or agent trained in this specialized practice."[18]

It is under the patent laws that ideas are protected, and protecting ideas is what is important to the independent inventor.

Finally, in a recent decision Chief Judge Markey of the United States Court of Appeals for the Federal circuit stated:

> "the very important, statutorily-created necessity of employing the clearest possible wording in preparing the specification and claims of a patent, [makes it] one of 'the most difficult legal instruments to draw with accuracy' *Sperry v. Florida*, 373 U.S. 379, 383 (1963) (quoting *Topliff v. Topliff*, 145 U.S. 156, 171 (1892))[19]

It thus appears advisable for the independent inventor to employ a registered patent agent or attorney for the preparation of the specification and claims and a skilled patent draftsman for the preparation of a drawing if needed, despite the expense.

The first thing an independent inventor should do in seeking patent protection, is to find out whether the idea justifies the cost of preparing the application. It is essential in seeking patent protection to determine that the idea has not been previously described in a publication or that it would have been obvious to a skilled worker because of what has been described in prior publications. Therefore before incurring the expense of a skilled preparation of an application it is advisable for the inventor to investigate the available literature in the field of the development to ascertain what has already been described in publications.

A major cost in patenting is incurred in preparing and filing the application, mainly because of the attorney time required to make an adequate disclosure. In most instances, the cost of a patentability search is less than the cost of preparation and filing an application. A preliminary or patentability search can yield a number of results. First, it can discover whether the idea has already been described in a publication, as for example a patent, either U.S. or foreign. A search can enable an inventor to reach some conclusion about the patentability of the invented subject matter. It avoids filing on a wholly unpatentable subject. Next, it provides the inventor and the attorney with information on the closest prior art. Furthermore, by learning about what has been done or is being done, the inventor becomes better informed about the significance of his contribution to available knowledge.

Even a thorough search on a complicated subject should cost less than the preparation and filing of the application on the researched subject matter. While the results of a preliminary search do not insure the subject idea is patentable, it is relatively inexpensive and can spare the inventor the expense of filing unpatentable subject matter.

The best facility for making this search is provided by the United States Patent and Trademark Office in Crystal City, Arlington, Virginia. Relevant technical publications are available to the public at the Patent and Trademark Office. They are classified into classes and subclasses for search purposes. While the inventor may visit this Patent Office Search Room, which is open to the public, to conduct a search in the available literature, it can be better conducted by a professional searcher experienced in carrying out such an investigation. A group of skilled searchers is located in Arlington, Virginia in the vicinity of the Patent and Trademark Office. The U.S. Patent and Trademark Office maintains a roster of attorneys and agents registered to practice in the Office. The roster is available in selected public libraries or from the superintendent of Documents,[20] Government Printing Office. Also upon request the U.S. Patent and Trademark Office, Washington, D.C. 20231 will provide a free list of attorneys and agents residing in a specified geographic area.

Albert F. Bower, a graduate of Columbia College, Columbia University and of Brooklyn Law School, has been a registered patent attorney since 1943. Originally an associate at Connolly, Cooch & Bove, he became a partner of that firm (now Connolly, Bove, Lodge & Hutz) in 1960.

After the invention is made the inventor still must act further in order to obtain recognition and reward. This entails the expenditure of time, effort, and money. But inventors should keep in mind "No other country in the world rewards invention and entrepreneurship as strongly as the United States"[21]. ■

Footnotes at page 26

FOOTNOTES

Blumenfeld - pages 10-13

1 Over the last several years, an average of nearly forty patent cases have been filed in the District of Delaware, nearly three times the national average. The number of patent cases pending here is almost six times the national average.

2 If the patentee seeks only injunctive relief, there is no right to a jury trial. *SRI v. Matsushita, supra,* 775 F.2d at 1127 n.4. In *Gardco Mfg., Inc. v. Herst Lighting Co.,* 820 F.2d 1209 (Fed. Cir. 1987), the Federal Circuit sanctioned the use of a separate non-jury trial on inequitable conduct in appropriate circumstances, holding that the patentee was not entitled to have that issue tried to a jury because it is equitable in nature.

3 New pertinent prior art can, however, facilitate the challenger in carrying its burden. *Stratoflex, supra; American Hoist & Derrick Co. v. Sowa & Sons, Inc.,* 725 F.2d 1350 (Fed. Cir.), *cert. denied,* 469 U.S. 821 (1984).

4 In *Truswal Systems Corp. v. Hydro-Air Engineering, Inc.,* 813 F.2d 1207, 1212 (Fed. Cir. 1987), the Federal Circuit said that the fact that "evidence is 'secondary' in time does not mean that it is secondary in importance."

5 Not all of the changes in Delaware patent law by the Federal Circuit have favored the patentee. For example, in *J.P. Stevens & Co. v. Lex Tex, Ltd.,* 747 F.2d 1553, 1561 (Fed. Cir. 1984), *cert. denied,* 474 U.S. 822 (1985), the Federal Circuit overturned the rule of *In re Frost,* 540 F.2d 601 (3d Cir. 1976), that inequitable conduct rendered unenforceable only the patent claims directly affected by the conduct, holding instead that all the claims are rendered unenforceable. In *UMC Electronics Co. v. United States,* 816 F.2d 647 (Fed. Cir. 1987), *cert. denied,* 108 S.Ct. 748 (1988), the Federal Circuit made it somewhat easier for the accused infringer to prove an on-sale bar under 35 U.S.C. §102(b). And it has become more difficult for the patentee to prove infringement in some circumstances. *See, e.g., Pennwalt Corp. v. Durand-Wayland, Inc.,* 833 F.2d 931 (Fed. Cir. 1987), *cert. denied,* 108 S.Ct. 1474 (1988); *Texas Instruments, Inc. v. United States International Trade Comm.,* 805 F.2d 1558 (Fed. Cir. 1986), *reh. denied,* 846 F.2d 1369 (Fed. Cir. 1988).

Kline - Fitzpatrick - pages 14-17

1 For a general overview of the law as it relates to infringement, see 4 Chisum, *Patents,* §16.06[2] (1988) and Cooley, "Personal Liability of Corporate Officers and Directors for Infringement of Intellectual property." 68 J. Pat.& Tm. Off. Soc'y 228 (1986).

2 *Power Lift v. Lang tools, Inc.,* 774 F.2d 478 (Fed. Cir. 1985) and *Orthokinetics, Inc. v. Safety Travel chairs, Inc.,* 806 F.2d 1565 (Fed. Cir. 1986).

3 §271(b) Whoever actively induces infringement of a patent shall be liable as an infringer.

4 §271(a) Except as otherwise provided in this title, whoever without authority makes, uses or sells any patented invention, within the United States during the term of the patent therefor, infringes the patent.

5 *Power Lift Inc.,* 774 F.2d at 481.

6 *Id.* at 480.

7 *Orthokinetics,* 806 F.2d at 1578-79

8 *Id.* at 1579

9 *Id.*

10 *Hitchcock v. American Plate Glass Co.,* 259 F. 948 (3rd Cir. 1919)

11 *Id.* at 954

12 *Id.* at 953

13 §271(b) defining active inducement was not then in being.

14 *Id.* at 955

15 *Id.*

16 *National Cash-Register Co. v. Leland,* 94 F. 502 (1st Cir.1899).

17 *Merck & Co., Inc. v. Chase Chemical Co., Inc.,* 136 USPQ 629 (D.N.J. 1963).

18 *Merck & Co., Inc. v. Chase Chemical Co.,* 273 F. Supp. 68, 93-4 (D.N.J. 1967).

19 *See, e.g., Donsco, Inc. v. Casper Corp.,* 587 F.2d 602, 606 (3rd Cir. 1978) (Corporate president found liable for acts which he personally committed); *Brandywine Mushroom Co. v. Hockessin Mushroom Products, Inc.,* 682 F. Supp. 1307, 1313 (D. Del. 1988) (Complaint found sufficient to find corporate officer personally liable for trademark infringement).

20 *Dangler v. Imperial Machine Co.,* 11 F.2d 945, 947 (7th Cir. 1926).

21 *Id.* at 947.

22 *Orthokinetics,* F.2d at 1579.

23 *Max Daetwyler Corp. v. Input Graphics, Inc.,* 541 F. Supp. 115, 117 (E.D. Pa. 1982).

24 *A. Stucki Co. v. Schwam,* 634 F.Supp. 259 (E.D. Pa. 1986).

25 *See,* Knepper and Bailey, *Liability of Corporate Officers and Directors,* §7.04, 1988.

Powers - Pages 18-23

1 A case in the local District Court beginning to take on more than a passing resemblance to the mythical case of Jarndyce v. Jarndyce in Charles Dickens' *Bleak House,* is General Motors Corp. v. Devex Corp. (*"Devex"*), No. 3058. For a fuller discussion see Connolly and Parsons, elsewhere in this issue.

2 35 U.S.C. §284.

3 Seattle Box Company, Inc. v. Industrial Crating & Packing, Inc., 756 F.2d 1574 (Fed. Cir. 1985) (*"Seattle Box"*).

4 Paper Converting Machine Co., v. Magna-Graphics Corp., 745 F.2d 11, 21 (Fed. Cir. 1984) (*"Paper Converting"*).

5 *Id. Also* Bio-Rad Laboratories, Inc. v. Nicolet Instrument Corp., 739 F.2d 604,616 (Fed. Cir. 1984) (*"Bio-Rad"*).

6 *Paper Converting,* 745 F.2d at 21; American Hoist & Derrick Co. v. Sowa & Sons, Inc., 725 F.2d 1350, 1365 (Fed. Cir.), *cert. denied,* 469 U.S. 821 (1984).

7 Gyromat Corp. v. Champion Spark Plug Co., 735 F.2d 549, 551 (Fed.Cir. 1984) (*"Gyromat"*).

8 Central Soya Co., Inc. v. Geo. A. Hormel & Co., 723 F.2d 1573, 1579 (Fed.Cir. 1983) (*"Central Soya"*); also Lam, Inc. v. Johns-Manville Corp., 718 F.2d 1056, 1065 (Fed.Cir. 1983) (*"Lam"*). Livesay Window Co. v. Livesay Industries, 251 F.2d 469, 471-72 (5th Cir. 1958) (*"Livesay Windows"*).

9 *Seattle Box,* 756 F.2d at 1581; *Paper Converting,* 745 F.2d at 21; Bio-Rad, 739 F.2d at 616; Gyromat, 735 F.2d at 551; *Central Soya,* 723 F.2d at 1579. The seminal decision setting out the four-part test was authorized by Judge Markey, sitting by designation in Panduit Corp. v. Stahlin Bros. Fibre Works, 575 F.2d 1152, 1156 (6th Cir. 1978) (*"Panduit"*). Judge Markey has been the Chief Judge of the Federal Circuit Court of Appeals since its creation in 1982.

10 *Paper Converting,* 745 F.2d at 22.

11 *Gyromat,* 735 F.2d at 552

12 Conley "An Economy Approach to Patent Damages", 15 *AIPLA Quarterly Journal,* 354,367 (1987).

13 *Livesay Windows,* 251 F.2d at 473; W.L. Gore & Associates, Inc. v. Carlisle Corp., 198 U.S.P.Q.353,363 (D.Del. 1978).

14 *Gyromat,* 735 F.2d at 554.

15 *Bio-Rad,* 739 F.2d at 616.

16 *Panduit,* 575 F.2d at 1162.

17 In the *T&B* accounting proceeding over which I presided, more than half of the trial time was expended on the issue whether a dozen or so competing products on the marketplace were acceptable alternatives to the infringing product and, if so, whether they likewise infringed the product. It is fair to say that the original trial, involving the question of infringement by one product, proliferated into a dozen infringement trials, with an equivalent twelve-fold increase in trial time over the liability trial, truly an instance of the tail wagging the dog.

18 *Lam* 718 F.2d at 1065.

19 A market share of only 5 percent has been held to be inconsequential, *Bio-Rad,* 739 F.2d at 616.

20 *Paper Converting,* 745 F.2d at 22.

21 *Id.*

22 *Panduit,* 575 F.2d at 1157.

23 Conley *supra,* p. 371.

24 *Paper Converting,* 745 F.2d at 23.

25 Kori Corp. v. Wilco Marsh Buggies and Draglines, Inc., 761 F.2d 649, 656 (Fed. Cir.), *cert. denied,* 474 U.S. 902 (1985).

26 Kori Corp. v. Wilco Marsh Buggies and Draglines, Inc., 561 F. Supp. 512, 530 (E.D.La. 1982), *aff'd* 761 F.2d 649 (Fed.Cir.), *cert. denied,* 474 U.S. 902 (1985).

27 There are exceptions however. For example, in *Paper Converting,* the patent holder established that purchasers of its patented high speed paper enwinder for manufacturing rolls of paper towels and toilet tissue in all likelihood would purchase such unpatented auxiliary equipment as a stand for the roll of paper, a core loader that supplied paperboard cores to the enwinder, an embosser for texturing the surface of the paper, and a sealer for sealing the paper trailing end to the consumer-sized roll. 745 F.2d at 23.

28 *E.g.,* Hanson v. Alpine Valley Ski Area, Inc. 718 F.2d 1075, 1077 (Fed.Cir. 1983). The list of relevant factors was first proposed in Georgia-Pacific Corp. v. United States Plywood Corp., 318 F.Supp. 1116, 1120 (S.D.N.Y. 1970), modified 446 F.2d 295 (2d. Cir.), *cert. denied,* 404 U.S. 870 (1971). (*"Georgia-Pacific"*).

29 *Panduit,* 575 F.2d at 1150.

30 General Motors Corp. v. Devex Corp. 461 U.S. 648, 654 (1983).

31 *Gyromat,* 735 F.2d at 537.

Bower - pages 24-25

1 "The Congress shall have the power ... to promote the progress of science and useful arts, by securing for limited times, to authors and inventors, the exclusive right to their respective writings and discoveries". Article I, Section 8, U.S. Constitution.

2 Rossman, J. *Industrial Creativity,* University Books, 27 (1964).

3 Title 37 Code of Federal Regulations §1.9(c).

4 Jewkes et al., *Sources of Invention,* 253.

5 17 United States Code §§106, 302(a).

6 35 United States Code §101.

7 Chisum, D., Patents §104(5) (1988).

8 35 United States Code §161.

9 35 United States Code §154.

10 Chisum, Patents, supra n. 7.

11 Allen F., "Invention American Style", XL Journal of the Patent Office Society, 312, 318 (1958).

12 Norris, K. "The Inventor's Guide to Low-Cost Patenting", MacMillan Publishing, 10 (1985).

13 Id., 19.

14 Code of Federal Regulations, Title 37, §1.31.

15 Manual of Patent Examining Procedure, (MPEP), United States Patent and Trademark Office (1988).

16 Id. §707.07(j).

17 MPEP §608.02.

18 General Information concerning Patents, Superintendent of Documents, U. S. Government Printing Office, Washington, D.C. 20402.

19 *Laitram Corp. v. Cambridge Wire Cloth Co.,* ___ F.2d___ (Fed. Cir. 1988) (Slip op. at p.3, December 12, 1988).

20 Attorneys and Agents Registered to Practice before the U.S. Patent and Trademark Office, Superintendent of Documents, U.S. Government Printing Office, (1988).

21 Hagstrom, J. "America Remains Model For Rest Of The World" Vol. 29, no. 10 *AARP News Bulletin,* 1, 17 (1988).

Crawford - Smink - pages 28-32

1 *Sony Corp. v. Universal City Studios,* 464 U.S. 417 (1984).

2 The Broadcast of a copyrighted motion picture does not extinguish the copyright owners' reserved right to reproduce (copy) the motion Picture. Thus, copying the motion picture is a nominal copyright infringement (464 U.S. at 464).

3 Conversely, the copyright owner's performance rights are not violated by what is done in the home because only public (versus private) performances are protected under the Copyright Act. *See* 17 U.S.C.A. §101 (1977) and §110(4) and (5).

4 The preamble of §107 lists several uses (research, news reporting, scholarship, etc.) that are "classic" fair uses, as well as four general guidelines for determining fair use in other situations. The House and Senate reports on the Copyright Act note that these guidelines were purposely broad so that they would not be obsoleted by rapidly advancing technology. (464 U.S. at 448 n. 32).

5 To perform or display a work "publicly" means -

(1) to perform or display it at a place open to the public or at any place where a substantial number of persons outside of a normal circle of a family and its social acquaintances is gathered; or

(2) to transmit or otherwise communicate a performance or display of the work to a place specified by clause (1) or to the public, by means of any device or process, whether the members of the public capable of receiving the performance on display receive it in the same place or in separate places and at the same time or at different times." 17 U.S.C.A. §101 (1977).

6 An earlier decision held that transmission of a radio broadcast of copyrighted music to a hotel room was a violation of the copyright owner's public performance rights because "a hotel is a place of public accommodation". *Society of European S.A.A.C. v. New York Hotel Statler Co.*, 19 F. Supp 1, 5 (S.D.N.Y. 1937).

7 Of particular interest is the *dictum* in *Redd Horne* that "the *transmission* of a performance to members of the public, even in private settings, such as hotel rooms constitutes a public performance" (emphasis added) (749 F.2d at 159). Even though *Redd Horne* was cited in *Columbia Pictures v. Real Estate Investors, supra* at 746, this *dictum was not addressed, probably because a "transmission" of movie video was not featured in either Redd Horne or Real Estate Investors* and transmissions are *public* performances by nature.

8 The infringing activity in *Wihtol* was the copying of copyrighted music, not the public performance of that music. In fact, the Copyright Act specifically provides that public performance of copyrighted works "in the course of services at a place of worship or other religious assembly" (17 U.S.C. §110(3)) is not an infringement. Thus, if choral music is properly obtained from authorized sources the copyright owner's public performance right cannot be asserted against a choir singing in a church or temple.

9 In *Marcus v. Rowley*, 695 F.2d 1171, 1177 (9th Cir. 1983) verbatim copying of a cake decorating book distributed to students did not constitute fair use.

10 The library is probably isolated from liability by 17 U.S.C. §108 which generally absolves libraries from charges of copyright infringement provided they post appropriate copyright warnings on their photocopiers and have no knowledge that the photocopying is for commercial purposes.

Sudell - Lehr - pages 34-38

1 It is certain to come as a surprise to many people that one of the best known songs in the land -- "Happy Birthday To You" -- is copyrighted. Although the song was written in 1893, it was not copyrighted until 1935, and remains protected to this day.

2 Federal copyright laws had been on the books since 1790, but did not become fully developed until the 1909 Act. Musical compositions were mentioned for the first time in 1831. H.G. Ball, *Law of Copyright* § 5 (1944).

3 Early construction of the "for profit" limitation was broad. In 1917, the Supreme Court ruled that live musical performances in a restaurant and in a hotel dining room were "for profit", even though there was no charge for admission to hear the music, holding that the music was part of the total price which patrons paid through increased prices of the food and that the proprietor's purpose in employing the music was profit. With his characteristic wit, Mr. Justice Holmes noted, "that to people having limited powers of conversation . . . [music] give[s] a luxurious pleasure not to be had from eating a silent meal." *Herbert v. Stanley Co.*, 242 U.S. 591, 595 (1917).

4 A third organization, SESAC, Inc., formerly the Society of European Stage Authors & Composers, is a privately owned, profit making organization which licenses a smaller, more specialized repertoire than ASCAP or BMI.

Grimm - Grimm - pages 40-42

1 Trade names are used by manufacturers, merchants, and others to identify their business, etc., but they may not be registered under the Lanham Act unless actually used as trademarks. Trade names are protectible, however, under the common law of unfair competition. Therefore, while trade names are not themselves registrable, trade names can be used to prevent the registration of confusingly similar junior trademarks.

2 There are only two authorized statutory notices of registration: the letter "R" enclosed in a circle and the phrase, "Registered in U.S. Patent and Trademark Office" (or Reg. U.S. Pat. & Tm. Off.").

3 Market surveys have been successfully used in the absence of other evidence. *See, e.g., Draper Communications Inc. v. Delaware Valley Broadcasters Limited Partnership*, 505 A.2d 1283 (Del. Ch. 1985).

4 In cases seeking preliminary injunctive relief the usual test applies, requiring a balancing of the likelihood of success on the merits, irreparable injury if an injunction should not issue, harm to the alleged infringer if an injunction were granted, and the public interest.

5 These remedies are subject to limitations under certain circumstances. *See* 15 U.S.C. §§ 1111, 1114.

6 Unlike some other states, Delaware does not have a statute prohibiting trademark dilution.

Whitney - pages 44-49

1 The factors listed are novelty, secrecy, value, cost, and unobviousness. *Restatement of Torts* §757, comment b (1939).

2 Some of the facts and quotations from the two cases are taken from a *New Yorker* article, Brooks: *Annals of Business*, Jan. 11, 1964 (p.37).

3 *B. F. Goodrich Co. v. Wohlgemuth*, 137 U.S.P.Q. 804, 804-05 (Ohio Ct. App.), *reversing* 137 U.S.P.Q. 389 (Ct. C.P. 1963).

4 *E.I. duPont de Nemours & Co. v.American Potash & Chem. Corp.*, 141 U.S.P.Q. 447, 448 (Del. Ch. 1964).

5 Neither Delaware Court, in denying preliminary relief, cited *American Potash*.

6 The trial evidence revealed that DCC did not, as suggested at the preliminary injunction stage (*see* 297 A.2d at 435-36), engage in legitimate "reverse engineering" but rather, in outright copying (see 357 A.2d at 114). Reverse engineering is the time-honored practice, sanctioned by the Supreme Court's *Sears-Compco* decisions, of legitimately determining the design of an unpatented product by working backwards from the ultimate product. *See* 357 A.2d at 111, 114. Some courts, indeed, have limited an injunction to that period of time it would have taken to reverse engineer the misappropriated product. The Delaware Chancery Court seemed to defer to that position tentatively (*see* 297 A.2d at 436), but ultimately adopted the better (and sounder) position that the defense of reverse engineering is available only to one who actually did so legitimately, and not for the benefit of one who has misappropriated trade secrets (*see* 357 A.2d at 114).

7 The Court applied the Delaware Uniform Trade Secrets Act, 6 *Del. C.* §2001.

8 In *Equitable Life Insurance Co. v. Thomas L. Young, et al.*, (Del. Ch., May 6, 1985), a covenant not to compete was enforced by preliminary injunction against an insurance agent and her new company, based again on misuse of a customer list. Several other cases involving covenants not to compete, but no trade secrets, granted preliminary relief, *The Perolin Company, Inc. v. Mark A. West, et al.*, Del. Ch., Mar. 20, 1980); *Signal Finance of Delaware, Inc. v. J. F. Burns, Jr., and Commercial Credit Corporation*, (Del. Ch., Oct. 6, 1980). Similar cases with similar results, based on somewhat deeper analysis of trade secret cases, are *Peoples Security Life Insurance Company v. Rodney A. Fletcher, et al.*, (Del. Ch., June 6, 1986), *Trinity Transport, Inc. v. James Ryan, et al.*, (Del. Ch., Oct. 1, 1986) and *Custom Video v. N. A. Video*, (Del. Ch., Sept. 25, 1987). In other cases, relief was denied because controlling state law made the covenant unenforceable, *Century Industries, Inc. v. Paul H. Benoit, et al.*, (Del. ch., Sept. 5, 1979); *Music on the Move, Inc. v. James B. Satcher*, (Del. Ch., Jan. 8, 1985).

9 *ICI Americas Inc. v. Ronald Burke and Eastman Technology, Inc.*, (Aug. 8, 1988, Tr. 40-41).

Seitz - pages 46-49

1 The author's law firm was involved as counsel for the defendants in the *Science Accessories* case and the author was involved as counsel for plaintiffs in the *Wilmington Trust* and *Equitable Life Insurance* cases, all of which are cited in this article.

2 A sample covenant not to disclose confidential information reads as follows: "I agree that all engineering and production drawings, design data, inventions and developments, know-how and techniques of construction for Employer's products, details of Employer's equipment and circuits, customer and prospect lists, and other knowledge of Employer's business interests, to which I am exposed during the course of my employment, is trade secret and proprietary information, and shall be maintained confidential by me and shall not be disclosed to others or used for my own benefit or the benefit of third parties, without the written permission of Employer, and that such obligation shall continue so long as such knowledge remains legally protectible with respect to persons receiving it in confidence."

3 An example of a covenant not to compete during employment reads as follows: "Employee agrees to devote his entire working time to his activities as agent hereunder and to refrain from engaging in any other pursuit or calling from which he receives remuneration or profit."

4 A sample of covenant not to compete after employment reads as follows: "I further agree that, in order to protect the trade secrets and proprietary information of Employer against the disclosure of such information which I received in confidence, I shall not, for a period of two years after termination of my employment for any reasons engage, either directly or indirectly, in the design, development, manufacture, or sale of ____ and/or any other products or services upon which I have worked at Employer. Further, I specifically agree that I shall not divert trade from Employer by directly or indirectly, within (geographic area) and within _____ years after said termination, soliciting business from, or selling to, or agreeing to sell to, any customers of Employer with which I may have had direct contact on behalf of Employer within the _____ years preceding such termination; provided, however, that I am under no obligation with respect to products or services other than those named above. If any part of this paragraph (2) exceeds the limits in time or territory for enforceability of restrictive covenants in any jurisdiction, then such part shall be deemed diminished to extent necessary for enforceability of restrictive covenants in any jurisdiction. The covenants of this paragraph are severable, and this paragraph is severable from the remaining covenants of the Agreement. Invalidity of one part of the Agreement shall not affect other parts."

Stone - pages 50-52

1 *United States v. Bottone*, 365 F.2d 389 (2d Cir. 1966), *cert. den.*, 385 U.S. 974 (1966); *United States v. Lester*, 282 F.2d 75 (2d Cir. 1960); *Rohm and Haas v. Robert S. Aries, et al.*, 103 F.R.D. 541 (S.D.N.Y. 1984)

2 *E.g.*: "Robert S. Aries Plays A Return Engagement," Chemical Week, September 19, 1979, p. 24; "The Secret World of Robert Aries," Business Week, May 5, 1986, p. 125.

3 "The Secret World of Robert Aries," Business Week, May 5, 1986, p. 125, quoting George W. F. Simmons, Patent Counsel for Rohm and Haas Co.

4 *Id.*

5 *United States v. Bottone, supra.* at 393-94.

6 *Carpenter v. United States*, ____U.S.____, 108 S.Ct. 316 (1987); *cf, Formax, Inc. v. Hostert*, 841 F.2d 388 (Fed.Cir. 1988)

7 United States Constitution, Article I, Section 8; 35 U.S.C. §§ 100-307.

8 15 U.S.C. §§ 1051-1127.

9 17 U.S.C. §§ 101-810; 18 U.S.C. § 2319.

10 1 Milgrim on Trade Secrets, §§ 1.01[2], 2.03, 2.04

11 *Perrin v. United states*, 444 U.S. 37 (1979).

12 *United States v. Von Barta*, 635 F.2d 999 (2d Cir. 1980), *cert. den.*, 450 U.S. 998 (1981); *United States v. Bohonus*, 628 F.2d 1167 (9th Cir.), *cert. den.*, 447 U.S. 928 (1980); *United States v. Newman*, 664 F.2d 12 (2d Cir. 1981).

13 *Abbott v. United States*, 239 F.2d 310 (5th Cir. 1956).

14 1 Milgrim On Trade Secrets, § 2.05.

15 Cal. Ann. Penal Code, § 449(c).

16 11 *Del. C.* § 857(4).

17 *E.g.* McKinney's New York Laws Anno., Penal Law, §§ 155.00, 155.30, 165.07.

18 18 U.S.C. §1961 *et seq.*

19 18 U.S.C. § 1961(1).

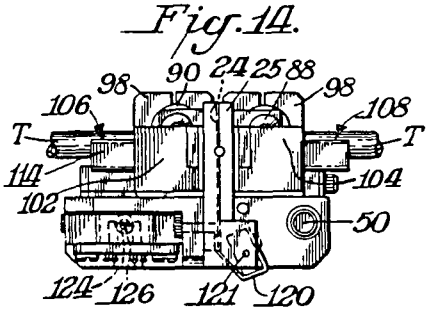
20 *FMC Corp. v. Boesky*, 852 F.2d 981 (7th Cir. 1988)

21 *Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. 479 (1985); *S.I. Handling Systems, Inc. v. Heisley*, 658 F.Supp. 362 (E.D.Pa. 1986).

22 *In re Von Bulow*, 828 F.2d 94 (2d Cir. 1987).

23 18 U.S.C. § 1964(c).

24 18 U.S.C. § 2511; 18 U.S.C. §1030.



YOU TOO CAN BECOME A COPYRIGHT INFRINGER

Paul E. Crawford and Patricia J. Smink

You may already be or may become a copyright infringer. Have you ever read the FBI warning displayed at the beginning of rented video cassettes? The next time the ghost of J. Edgar Hoover rolls up on the screen after you pop the video cassette tape into your video recorder (VCR) take it seriously. The Copyright Act of 1976 (17 U.S.C.A. §100 *et seq*) limits your use of that video cassette tape. Likewise, think twice about copying "E.T." or any other popular motion picture from your television if and when it appears on cable.

The courts' struggle to balance the rights of the copyright owners and public largely stems from the unique, multifaceted nature of a "copyright", which is a bundle of exclusive rights granted the copyright owner. Under the copyright law of the United States:

"The owner of copyright... has the exclusive rights to do and to authorize any of the following:

> (1) to *reproduce* the copyrighted work in copies or phonorecords;
>
> (2) to prepare *derivative works* based upon the copyrighted work;
>
> (3) to *distribute* copies or phono- records of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease or lending;
>
> (4) in the case of ... motion pictures and other audio-visual works, to *perform* the copyrighted work *publicly*; and
>
> (5) in the case of literary, musical, dramatic, and choreographic works, pantomimes,* and pictorial, graphic, or sculptural works, including the individual images of a motion picture or other audiovisual work, to *display* the copyrighted work publicly." (emphasis added) 17 U.S.C.A. §106(1977)"
>
> * A charmingly quaint term that summons up visions of magic lanterns, stereopticons, and hand-tinted post cards of Niagara Falls. Ed.

Each of these exclusive rights belongs to the copyright owner. He or she may authorize the exercise of one of these rights and reserve the others. Violation of any *one* of the exclusive rights is a copyright infringement. 17 U.S.C.A. §501(1977).

For example, because a copyrighted television program is "performed publicly" by broadcast (exclusive right (4)) does *not* entitle others to "reproduce" or make a copy of the program (exclusive right (1)). The copyright owner retains control over how this work is performed, copied, sold, displayed, or modified. This is illustrated in *Nat'l Football League v. McBee & Brunos', Inc.*, 792 F.2d 726 (8th Cir. 1986), where the copyright owner of a broadcast of a football game authorized this broadcast in all areas of the country except a 75 mile black-out region around the home team stadium. The copyright owner was entitled to control how the work was performed publicly and could prevent bar owners within the black-out region from intercepting the blacked-out home football game broadcast. *Nat'l Football League*, 792 F.2d at 733.

One further paradox under the copyright laws must be noted. Ownership of copyright is distinct from ownership of the material object embodying the copyrighted work. 17 U.S.C.A. §202 (1977). For example, a copyright owner typically distributes (sells) a video cassette copy of his copyrighted motion picture for a fee. Notwithstanding that sale, the copyright owner still retains the exclusive rights to reproduce, distribute copies, prepare derivative works of the copyrighted motion picture. However, the new owner of the video cassette has the right to sell, rent, transfer, or destroy that particular video cassette. 17 U.S.C.A. §109(a)-(c) (1977). Under this principle, the ownership of a particular video cassette, record album or book does not permit one to violate the exclusive rights *retained* by the copyright owner.

YOUR USE OF A VCR COULD BE A COPYRIGHT INFRINGMENT

One of the earliest and most celebrated clashes between copyright owners and the public reached the United States Supreme Court in 1983.[1] It pitted the motion picture industry, represented by Universal City Studios and Walt Disney, against Sony, the leading distributor of VCRs at that time. Universal complained that Sony's sales of VCRs contributed to the public's infringement of movie copyrights because it permitted copying of movies broadcast on commercially sponsored television.[2] Sony rejoined that VCRs are not used to copy films for archival purposes but merely to permit the owner to play back a movie at a more convenient time. Sony referred to such use as a "time shifting." At the trial, Sony relied on surveys conducted in 1978 that showed most VCR owners did use the VCR for time shifting purposes. Only a very small percentage of those surveyed used the VCR to build private film libraries. 464 U.S. at 423-4.

In a 5-4 decision the Supreme Court affirmed the District Court's denial of injunctive relief sought by the movie studios. The Supreme Court, analogizing the copyright infringement issues presented in *Sony* to infringement issues of a patent case, concluded that Sony's VCRs were capable of substantial non-infringing use ("time shifting") and, therefore, Sony should not be held culpable for the limited instances of copyright infringement in which VCR users copy

telecast movies for other than "time shifting" purposes.

The Supreme Court also analyzed Sony's actions under the fair use doctrine enunciated in the Copyright Act (17 U.S.C.A. §107) and found that time shifting was a "fair use" of Universal's copyrighted material. The Court adopted the District Court's findings that time shifting was a non-profit use of the copyrighted work that had "no demonstrable [adverse] effect upon the potential market for, or the value of, the copyrighted work ..."(464 U.S. at 449-50).

The majority's opinion in *Sony* closes and the dissent opens with a plea for Congressional guidance in the fair use of copyrights. Such is needed because it is unquestioned that copying of even a single copyrighted film, whether for time shifting or library building, violates a copyright owner's exclusive right under 17 U.S.C.A. §106(1) to reproduce the copyrighted work. 464 U.S. at 464.[3] Thus, Universal Studios was limited only by practical and economic concerns from bringing copyright infringement suits against individual VCR users. Universal Studios obviously could not be in every, or any, living room to monitor VCR use. However, under the "fair use" doctrine, a *de facto* infringing activity in the home will nevertheless be excused if the balance of the four factors set out in 17 U.S.C.A §107[4] favor characterizing a use as "fair". These are:

> (1) the purpose and character of the use, including whether such use is of a commercial nature of is for nonprofit educational purposes;
>
> (2) the nature of the copyrighted work;
>
> (3) the amount of substantiality of the portion used in relation to the copyrighted work as a whole; and
>
> (4) the effect of the use upon the potential market for or value of the copyrighted work.

The Supreme Court's dilemma and divided decision clearly point out the uncertainty surrounding the Copyright Act, especially in light of the rapid development and use of evolving technologies. The underlying *assumption* of the *Sony* decision was that predominant use of VCRs was for time shifting versus library building. A survey done today would no doubt puncture holes in that assumption.

Undeterred by the loss in *Sony*, the motion picture studios struck out at other uses of their copyrighted product. In *Columbia Pictures v. Professional Real Estate Investors*, 228 U.S.P.Q. 743 (C.D. Calif. 1986) the inquiry moved from the living room to the motel room. The defendant ran a resort motel and rented video cassettes (actually video discs) of copyrighted motion pictures for viewing in the motel room. There was no issue of piracy because the defendants had purchased the cassettes for full value from sales outlets authorized to sell plaintiff's copyrighted films.

The issue presented was a simple one: "whether guests at a hotel or similar accommodation are 'publicly performing' the video discs when they view the videos in the rooms they have rented." 228 U.S.P.Q. at 745. If so, the defendants (or their guests) would be infringing one of the copyright owners' bundle of exclusive rights, e.g., "to perform the copyrighted work publicly".17 U.S.C.A. §106(4).[5]

(Continued on next page)

(Infringer continued)

(That right was retained by plaintiffs even though their right to further compensation was extinguished by the authorized sale of the video to defendants (17 U.S.C.A. §109(a).) By lawful purchase of the video cassettes the defendants obtained the right to rent the videos at issue, provided that rental was not for the purposes of an unauthorized public performance. This is the same stricture that permits the plethora of video rental stores across the country to rent video cassettes -- but only for non-public performances in the home or like setting.

The California court concluded that hotel rooms were private, as evidenced by the Fourth Amendment and right to privacy protection extended to hotel guests in various other legal contexts. The court concluded that viewing a video in a motel room is no different from viewing it in a living room and, as such, was not a public performance in violation of the motion picture owner's rights.[6] 228 U.S.P.Q. at 746. See 17 U.S.C.A. §101.

The motion picture industry finally prevailed in a pair of cases involving the display of movie videos in settings outside the home or hotel. In *Columbia Picture Industries v. Redd Horne*, 749 F.2d 154, 160 (3rd Cir. 1984), the Third Circuit held that the display of copyrighted movies in a 4 foot by 6 foot viewing booth set up with seats for up to four people was an infringing "public performance". The Third Circuit analogized these booths to a mini movie theatre wherein any member of the public could view the movie in the booth for a fee.[7] 749 F.2d at 159.

As the mellow tones of your church choir float over the congregation in spiritually uplifting waves remember that the source of this inspiration may be illegal. There are definite limits on the extent to which choir music may be copied and distributed to choir members.

It is thus evident that the movie studios' success in enforcing their copyrights increases with the distance the infringing activity moves away from similarity with home viewing of copyrighted works in the living room. The studios have been particularly successful against video stores that rent pirated (unauthorized) video tapes of copyrighted movies. Their success is in no small measure due to some unique legal weapons available to stop tape pirates. More particularly, a copyright owner may file an *ex parte* petition in any district court, asking the court to seize, impound, and ultimately destroy any copy of a copyrighted work. 17 U.S.C.A. §503(a). If an adequate showing of copyright infringement is made out in the petition, the court may order a United States marshal to visit the accused infringer's store unannounced and seize the infringing copies and any means used to make the copies. *See* Rules 3-5 of Copyright Practice and Procedure promulgated by the Supreme Court of the United States.

The seizure and impoundment procedure under the Copyright Rules has withstood constitutional challenge. In *Universal Film Mfg. Co. v. Copperman*, 206 F.69, 70 (S.D.N.Y. 1913) the procedure was held to constitute procedural due process of law and, in addition, was "not obnoxious" to the Fourth Amendment. Further, the procedure does not violate the First Amendment. *Jondora Music Publishing Co. v. Melody Recordings, Inc.*, 362 F.Supp. 494, 499 (D.N.J. 1973), *vacated on other grounds*, 506 F.2d 392

(Continued on page 32)

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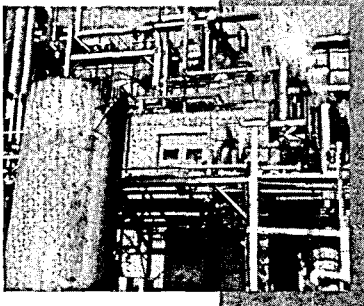

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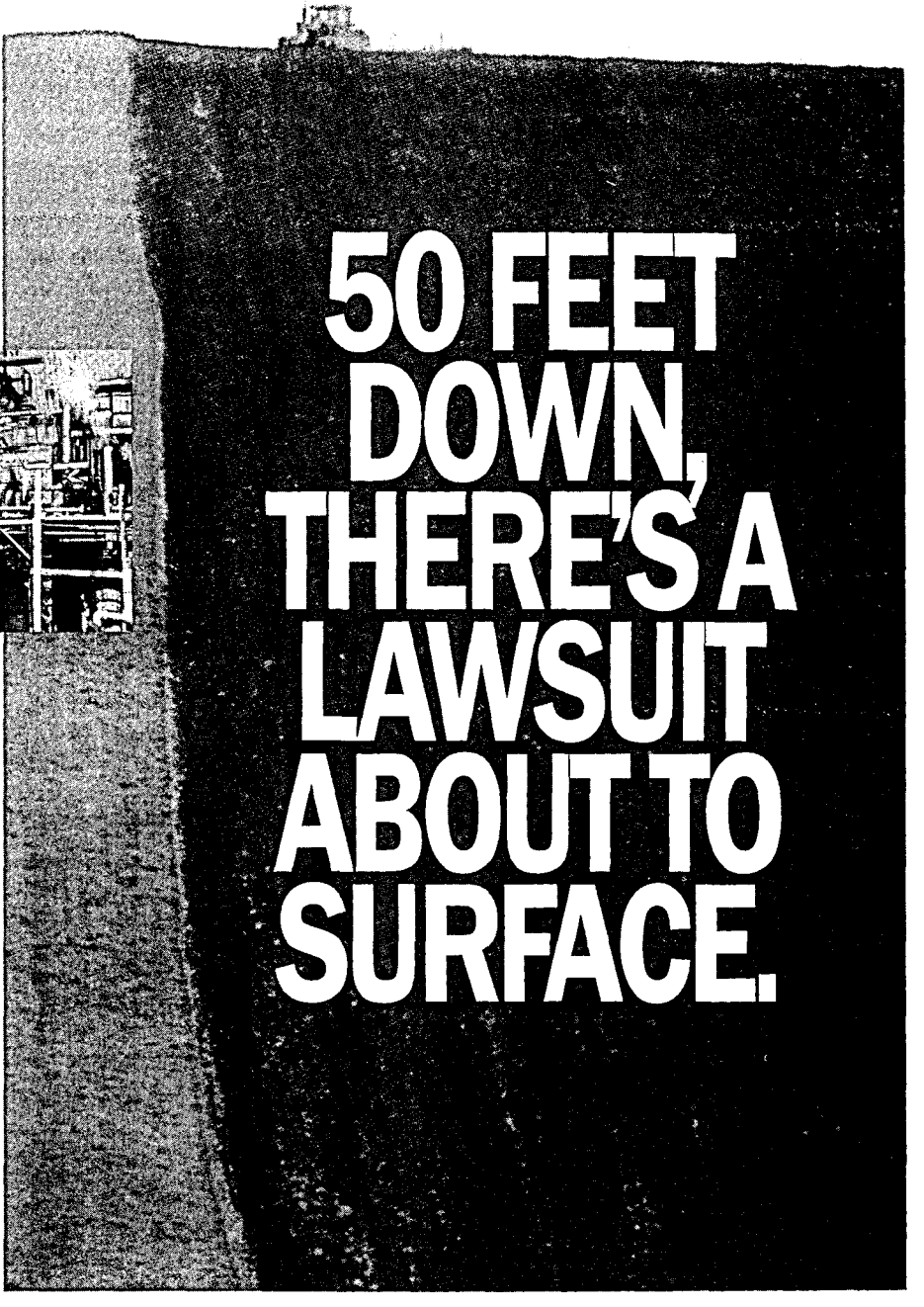

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(Infringer continued)

(3d Cir. 1975). *See also Dealer Advertising Development, Inc. v. Barbara Allan Financial Advertising, Inc.*, 197 U.S.P.Q. (BNA) 611, 615 (W.D. Mich. 1977).

PHOTOCOPYING CAN GET YOU IN TROUBLE

As the mellow tones of your church choir float over the congregation in spiritually uplifting waves remember that the source of this inspiration may be illegal. There are definite limits on the extent to which choir music may be copied and distributed to choir members. In a less uplifting scenario suppose you intend to buy a new refrigerator but are unsure what is the best brand on the market. Your friendly librarian loans you the issue of *Consumer Reports* dealing with refrigerators, which you copy in pertinent part for reference and guidance in your appliance shopping. That copying may very well have violated the copyright laws.

There is no question that use of a photocopier clashes with the rights of the copyright owner. A photocopy of an entire copyrighted work violates the copyright owner's exclusive right to reproduce the work. 17 U.S.C.A. §106(1). However, that violation may be excused under the fair use doctrine.

The uncertain balance of fair use factors makes it difficult to talk in *absolute* terms. Certainly photocopying entire copyrighted works for a profit will have a limiting effect on the potential market for those copyrighted works. Certainly photocopying services are at risk to copyright liability. Even the duplication of an entire copyrighted work without commercial intent has been held an unfair use. In *Wihtol v. Crow*, 309 F.2d 777, 780 (8th Cir. 1962) a choir director at a Methodist church in Iowa sought to excuse his copying and use of a copyrighted choral piece on the grounds he had slightly modified the piece to suit his choir's needs. An Eighth Circuit panel, including current Justice Blackmun, reversed a district court finding that the choir director's activities were a fair use of the copyrighted song. The Eighth Circuit rejected the fair use defense noting: "Whatever may be the breadth of the doctrine of fair use it is inconceivable to us that the copying of all or substantially all of a copyrighted [work] can be held to be a fair use merely because the infringer had no intent to infringe."[8]

Still, the copyright laws must make some accommodation to the widespread use of photocopiers, and the accompanying increase of access to copyrighted works the photocopier generates. Where photocopies are made for a scientific or educational purpose, without commercial motive, the courts are more likely to uphold a defense to an infringement charge. In *Williams & Wilkins Co. v. United States*, 487 F.2d 1345, 1353 (Ct. Cl. 1973), *aff'd per curiam*, 420 U.S. 376, 95 S.Ct. 1344 (1975), library photocopying of entire scientific and medical articles for scientists' and researchers' non-commercial use was deemed fair use. However, the library in *Williams & Wilkins* did not permit the copying of an entire book or journal. Further, the court's holding was heavily influenced by the concern that limiting the photocopying of these scientific materials would hamper important medical research.[9]

Since the photocopying required for most personal use does not further such lofty social goals, some photocopying of copyrighted works could constitute unfair use. For example, the hypothetical library user who copies a *Consumer Reports* article is doing so for nonprofit purposes, which supports a conclusion of fair use. 17 U.S.C.A. §107(1). However, the adverse effect of that copying "upon the potential market for or value of the copyrighted work" (17 U.S.C.A. §107(4)) is substantial because the main market for *Consumer Reports* consists of those average consumers looking for the very information copied. If a consumer can get information about an appliance purchases by photocopying a library copy of the magazine rather than by subscribing to it, *Consumer Reports* potential market is being eroded. For this reason, the potential infringement by the user of the library photocopier is very real.[10]

We hope that we have made you more aware of the copyright laws and how they impinge upon your everyday activities. Keep in mind, however, the matter of copyright infringement is not totally academic. Statutory damages for infringement range from $250 to $10,000 and can go as high as $50,000 if the infringement is proven to be willful. 17 U.S.C.A. §504(c)(2). ■

*Consider yourself warned! Ed.

Footnotes at pages 26-27

Paul Crawford, a member of the Wilmington firm of Connolly, Bove, Lodge & Hutz, has kept abreast of emerging law under the Copyright Act to a degree perhaps unprecedented among the members of our bar. He has an acute interest in the rapid advances in new technology that the Copyright Act attempts to address. After graduating from the Villanova School of Law in 1964, he spent two years in the United States Patent Office as an examiner before moving to Wilmington, where he has practiced with distinction to this date.

Patricia Smink, a member of both the Delaware and Pennsylvania bars is an associate at the Wilmington firm of Connolly, Bove, Lodge & Hutz. A Lehigh University graduate in mechanical engineering, and a 1987 graduate of the University of Pennsylvania Law School, Ms. Smink practices intellectual property law.

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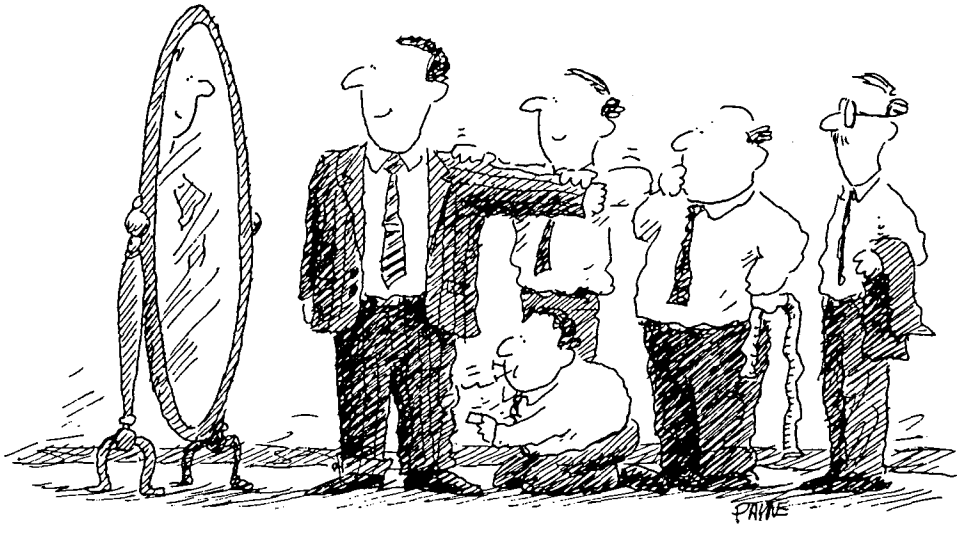

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PERFORMANCE RIGHTS:
LICENSING COPYRIGHTED MUSICAL COMPOSITIONS

William H. Sudell, Jr., and Matthew B. Lehr

It comes as no surprise that authors of musical compositions and lyrics are granted copyright protection for their creations. As the Supreme Court has stated, the economic philosophy behind Article I, Section 8 of the United States Constitution, from which Congress' power to grant copyright protection springs

> . . . is the conviction that encouragement of individual effort by personal gain is the best way to advance public welfare through the talents of authors and inventors. . . Sacrificial days devoted to such creative activities deserve rewards commensurate with the services rendered.

Mazer v. Stein, 347 U.S., 201, 219 (1954). Including composers and lyricists within the class so encouraged seems only right. Not so obvious, however, is the manner in which that protection is provided and the extent to which it permeates our everyday lives.

All of us come into contact with music in many ways, virtually everyday -- consciously listening to it on the radio, at a concert hall or nightclub, barely noticing it at the dentist's office, or when the organist plays between innings at the ball park, purchasing it in the form of sheet music, records, tapes, and compact discs, and performing it in choruses, glee clubs or during religious services. In each of those instances, and a myriad others, the issue of copyright protection of the musical composition being performed is present, often in ways that are not appreciated by those who are using the music.[1] However, the basic principles at work are the same -- how best to compensate the copyright holder for the performance and who should provide that compensation.

THE FEDERAL COPYRIGHT LAW

The origin of the federal copyright law is the United States Constitution. In Article I, Section 8, the framers vested Congress with the power to "promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." Although the common law offered some protection to authors, statutory protection was needed, as the common law protected only unpublished works. *Wheaton v. Peters*, 33 U.S. 591 (1834).

The first comprehensive federal copyright statute was enacted in 1909.[2] Although earlier state and federal law was aimed primarily at the protection of the written word, the 1909 Act explicitly authorized the protection of musical works and granted exclusive performance rights to the composer. 4 M.B. Nimmer, *Nimmer on Copyright* App. 6 and 13 (1988).

In 1976 Congress enacted a sweeping amendment to the 1909 Act. Given the immense technological advances between 1909 and 1976, it is not surprising that widespread changes were required. In 1909 a music writer's principle source of distribution of his or her work was through the sale of sheet music. By 1976, that industry had been largely supplanted by the recording, radio, and television industries.

An important aspect of the 1976 amendments was the modification of the duration of the copyright protection. Under the 1909 Act, the protective term was an initial 28 years, plus a renewal term of 28 years. With certain exceptions, the 1976 Act provides protection for the life of the author plus 50 years. 17 U.S.C. §302(a). Thus, a musical composition can now conceivably enjoy copyright protection for one hundred years or more.

MUSICAL COPYRIGHTS

The Copyright Act applies to many types of intellectual property, such as literary, dramatic and choreographic works, photographs, as well as musical compositions and sound recordings. 17 U.S.C. §102(a)(2), (3), and (7). The musical composition copyright protects both the musical work and the accompanying words. Performing lyrics or music alone will not prevent a copyright infringement, as the Act prohibits the unauthorized use of the music or the words alone or in combination. *Stratchborneo v. Arc Music Corp.*, 357 F. Supp. 1393 (S.D.N.Y. 1973).

Under the current Copyright Act, a musical composition may be copyrighted if it is fixed "in [any] tangible medium of expression." 17 U.S.C. §101. In contrast to the 1909 Act, which required that the composition be reduced to written form, the 1976 Act permits copyrighting by the use of a recording. 1 M.B. Nimmer, *Nimmer on Copyright* § 2.05[A] (1988). *Cf. White-Smith Music Pub. Co. v. Apollo Co.*, 209 U.S. 1 (1908). Thus, a musician cannot now escape the effect of the copyright laws by learning the composition by ear from a recording rather than from sheet music.

Similarly, musical arrangements are also copyrightable, as they constitute a derivative work. 17 U.S.C. §101. A derivative work is subject to copyright although the underlying music is also copyrighted or is in the public domain. Thus, an arrangement of a Bach cantata may be the subject of copyright although the music has been performed for centuries.

RIGHTS TO PERFORM COPYRIGHTED MUSICAL COMPOSITIONS

Perhaps most frequently litigated aspects of the copyright laws with respect to music are in the performance of musical compositions by persons other than the copyright owner.

The Copyright Act provides the copyright owner, subject to certain specific exemptions, with the exclusive right "to perform the copyrighted work publicly." 17 U.S.C. § 106(4). The term "perform" means "to recite, render, play, dance or act [a work] either directly or by means of any device or process . . ." 17 U.S.C. § 101. Whether or not something constitutes a "performance" and, indeed, how many performances are occurring, depends on who is playing, who is listening, and how the listener receives the music. For example, a radio broadcast of a concert is a separate performance from the concert itself -- both the orchestra and

the station must have permission to "perform" the copyrighted music. *Schumann v. Alberquerque Corp.*, 664F. Supp. 473, 476 (D. N.Mex. 1987).

Questions can also arise whether a particular performance is "public." The Act provides that to perform a work "publicly" means to perform it at a place -- or transmit the performance to a place -- "where a substantial number of persons outside of a normal circle of a family and its social acquaintances is gathered." 17 U.S.C. §101. Thus, music does not necessarily have to be performed in an area open to the public to be considered "public" under the Copyright Act.

It is certain to come as a surprise to many people that one of the best known songs in the land -- "Happy Birthday To You" -- is copyrighted. Although the song was written in 1893, it was not copyrighted until 1935, and remains protected to this day.

The language of the current statute is much broader than the language under the 1909 Act. In amending the statute, Congress intended to make it clear that "performances in semi-public places, such as clubs, lodges, factories, summer camps and schools, are public performances subject to copyright control." Senate Report No. 94-473, 94th Congress, First Session 60 (1975); H.R. Report 94-1476, 94th Congress, Second Session 64 (1976). Thus, musical performances of copyrighted compositions at "private" clubs may be subject to the copyright laws although the public at large is not able to attend.

Under the 1909 Act, the copyright owner's exclusive performance right protected only against public performances which were "for profit." 17 U.S.C. § 1(e) (1909); 4 M.B. Nimmer, *Nimmer on Copyright*, App. 6 (1988). Much litigation focused on the meaning of the "for profit" limitation,[3] and in the 1976 Act, Congress wrote out the "for profit" limitation, providing instead a list of exemptions from the Act.

Among the exemptions to the prohibition against publicly performing copyrighted music, are the classroom exemption and the religious services exemption. The classroom exemption exempts "performance .... of a work by instructors or pupils in the course of face-to-face teaching activities of a nonprofit educational institution, in a classroom or similar place devoted to instruction . . ." 17 U.S.C. § 110(1). Thus, for example, broadcasting instruction over the airwaves would not be an exempt activity.

The religious exemption applies only if the music is performed in a place of religious worship and if the music is of a religious nature. 17 U.S.C. §110(3). A performance of Handel's Messiah by a church choir in the course of a religious service would be exempt, but the performance of nonsecular music in that same service would not.

Often misunderstood is the issue of who is liable to the copyright owner if the exclusive right to perform the music publicly is violated. For example, if a nightclub hires a band to perform on Friday nights, who is liable to the copyright owner if his or her music is performed -- the band, the nightclub, or both? Clearly the band is, but by the time a copyright infringement suit can be brought the band may be long gone or out of existence. However, the law also holds the nightclub responsible for the copyright infringement and, depending on the ownership and management of the club, a manager, executive officer, or a stockholder may also be held personally liable for an infringement.

In *Hideout Records & Distributors v. El Jay Dee, Inc.*, 601 F. Supp 1048 (D.Del. 1984), the Court held the president, vice president, and corporate secretary personally liable for copyright infringement. Similarly, in certain cases a shareholder may be personally liable. In *Blendingwell Music, Inc. v. Moor-Law, Inc.*, 612 F. Supp. 474, 481-82 (D.Del. 1985), the Court held the defendant's sole shareholder liable for copyright infringement. The Court based its finding of liability on a theory of vicarious liability, and did not perform a veil-piercing analysis as is customary in other types of shareholder liability suits.

(Continued on next page)

HAPPY BIRTHDAY!
(Sentimental Infringement)
MARK VAVALA

(Performance continued)

LICENSING THE PERFORMANCE RIGHTS TO COPYRIGHTED MUSIC

The broad rights vested in a musical copyright holder require most users of that music to license the rights to perform or copy the music. With respect to the performance right, the obvious problem is the manner in which licenses to perform music can be secured from the copyright holder -- or, more important to the author at least, how he or she can collect payment for the multitude of performances of the copyrighted work.

For example, consider the difficulty the Beatles would face in attempting to license the performance right to their works. Their music is played on radio stations throughout the country, as background music in television programs and movies, in commercials, at nightclubs, and at high school dances. Similarly, other artists have re-recorded Beatles compositions, and we even have Muzak versions of those songs broadcast in supermarkets and on elevators. Securing licenses from the thousands of users of Beatles music would be a practical impossibility.

As a result of the impossible task faced by composers of copyrighted music in licensing and collecting fees for the performance right to their music, "performing rights societies" were formed. In 1914 the American Society of Composers, Authors and Publishers ("ASCAP") was created to provide a "clearing house for copyright owners and users to solve [the] problems associated with the licensing of music." *Broadcast Music, Inc. v. CBS*, 441 U.S. 1,5 (1979). Approximately 25 years later, Broadcast Music, Inc. ("BMI") was organized for the same reason. BMI and ASCAP today serve as the principal clearing houses for copyrighted music.Indeed, "[a]lmost every domestic copyrighted composition is in the repertoire either of ASCAP, with a total of three million compositions, or of BMI, with one million." Id.[4]

Both BMI and ASCAP are nonprofit organizations: all license fees, less operating expenses, are distributed to affiliated songwriters and music publishers. The existence of performing rights societies, such as BMI and ASCAP, which license the public performance of nondramatic musical works on behalf of copyright owners, is expressly recognized by the Copyright Act. 17 U.S.C. 116(3).

BMI and ASCAP each operates primarily through "blanket" licenses, which give the licensee the right to perform the entire repertoire of the licensor as often as the licensee desires for a specified period of time. *Broadcast Music, supra*, 441 U.S. at 5. The license fees are determined from a variety of factors, such as the size and dollar volume of the establishment, entertainment costs, and the number of days or nights per week music is performed.

Since the creation of BMI and ASCAP, the blanket license system has been challenged several times on antitrust grounds. In the 1940's BMI and ASCAP were investigated by the Department of Justice, resulting in consent decrees prescribing limitations on the blanket license system. An important limitation of the consent decrees prohibits composers from granting BMI and ASCAP exclusive rights to license their music. Thus, individuals who do not take a license from BMI or ASCAP can nonetheless enter into separate licensing agreements with the copyright owner. *Broadcast Music, Inc. v. CBS, supra* at 11.

In the *CBS* case, the blanket licensing of network television programming was challenged under Section 1 of the Sher-

man Act. Rejecting CBS's argument, the Supreme Court stated:

> "the blanket license . . . is not a naked restraint of trade . . .[but was] developed together out of the practical situation in the market place; thousands of users, thousands of copyright owners, and millions of compositions. Most users want unplanned, rapid, and indemnified access to any and all of the repertoire of compositions, and the owners want a reliable method of collecting for their use of their copyrights." *Id.* at 20.

The blanket licensing of such establishments like bars, night clubs and restaurants was also challenged unsuccessfully on antitrust grounds in Delaware. *Broadcast Music, Inc. v. Moor-Law, Inc.*, 527 F. Supp. 758 (D.Del. 1981), *aff'd*, 691 F.2d 490 (3d Cir. 1982).

PENALTIES FOR INFRINGEMENT

Failing to license the right to perform copyrighted music can be an expensive undertaking and the federal courts have not been reluctant to impose damages and grant other relief against copyright infringers. *See, e.g., Blendingwell Music, Inc. v. Moor-Law, Inc.*, 612 F. Supp. 474 (D. Del. 1985); *Broadcast Music, Inc. v. Moor-Law, Inc.*, 484 F. Supp. 357 (D. Del. 1980); *Hideout Records & Distributors v. El Jay Dee, Inc.*, 601 F. Supp. 1048 (D. Del. 1984).

In an infringement action the copyright owner may obtain injunctive relief and recover its actual damages, the infringer's profits, plus costs and attorneys' fees. 17 U.S.C. §§ 502, 504-05.As an often used alternative to actual damages, a copyright owner may obtain statutory damages in the amount of $250 to $10,000 for each copyrighted song performed publicly without a license (and up to $50,000 if the infringement is willful). 17 U.S.C. § 504(c). For example, if a local tavern hired a band to play live music, and the tavern was unlicensed, the copyright owner of the compositions played could obtain up to $10,000 for *each* copyrighted song performed, plus attorneys' fees and an injunction against future non-licensed performances.

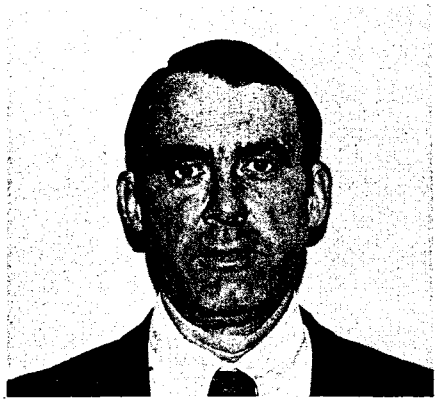
In 1783, the first copyright statute enacted in the United States was passed in the Connecticut legislature. 4. M.B. Nimmer, *Nimmer on Copyright*, App. 13 (1988). Eleven of the other twelve states followed suit -- all except Delaware. H. G. Ball, *Law of Copyright* §5 (1944).

(Continued on next page)

(Performance continued)

Since that time, and with the enactment of comprehensive federal copyright legislation, the legal landscape has changed markedly with respect to copyrights generally, and music copyrights specifically. The federal courts, including the Delaware district court, have been vigilant and can be expected to remain so in protecting the rights of composers against wrongful public performance of their music. ■

Footnotes at page 27



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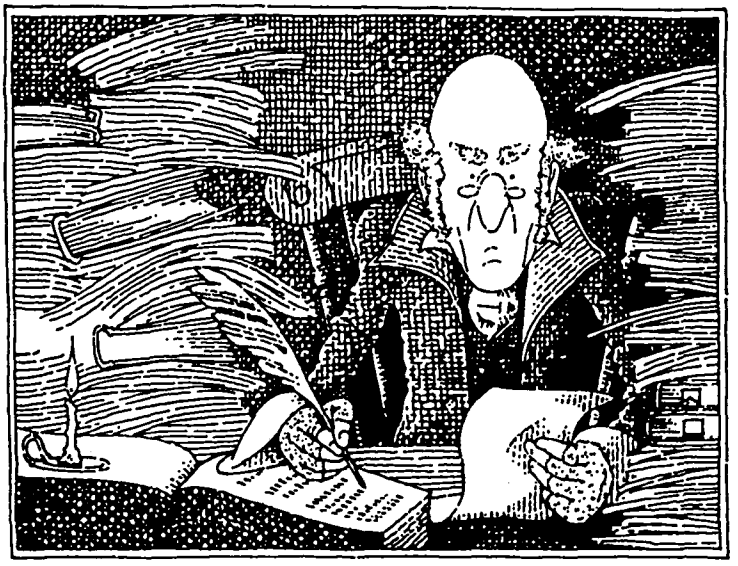
Mr. Sudell's collaborator, Matthew Lehr, brings an unusual background to his practice in commercial litigation, which includes copyright law. He holds degrees in philosophy from Loyola College and Johns Hopkins University. A law graduate of the University of Pittsburgh, he is an associate at the Wilmington firm of Morris, Nichols, Arsht & Tunnell.



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TRADEMARKS:

HOW TO GET THEM, KEEP THEM, AND ENFORCE THEM

Eugene L. Grimm and Thomas C. Grimm

Almost everyone will agree that, as human beings, we live by symbols. We also purchase goods by them. The protection of trademarks is the law's recognition of the psychological function of such symbols. A trademark is used to identify the product of a particular supplier and distinguishes that supplier's goods from the goods of others. The trademark's primary function is to disclose origin. The mark answers the question, "Whose goods are these?"

What May Be Protected As a Trademark

In the United States, ownership rights in trademarks depend on use, rather than registration. The first to use a trademark publicly, regardless of whether it has been registered with the United States Patent and Trademark Office (the "PTO"), becomes the owner of the mark with the attendant right to prevent others from using the mark or any other mark that is likely to cause confusion or mistake in the minds of consumers.

A trademark may be a word, name, symbol, or device. For example, "Fantastik" is a word mark, the name "Coca-Cola" is both a trademark and a trade name, the "Du Pont Oval" is a symbol, and McDonald's "golden arches" constitute a device. The word "trademark" is really a shorthand reference for four types of marks: trademarks that are used in the sale or advertising of goods; service marks that are used in the sale or advertising of services; certification marks that are used with the goods or services of persons other than the owner of the mark to certify some characteristic of such goods or services, such as quality; and collective marks that are used by members of a cooperative, an association, or other collective group or organization.

Not all words or symbols are suitable for trademark protection. Candidates for trademark protection are commonly evaluated along the following scale: generic words, descriptive words, suggestive words, and arbitrary or fanciful words. At one extreme are generic words, which describe the whole product category. A generic word is the common descriptive term that the public uses when shopping for that type of product; "soda", "furniture" and "integrated circuits" are examples. A generic term cannot be appropriated as a trademark by one supplier (or registered with the PTO) because competitors may not be deprived of their right to use that term in its ordinary meaning.

At the other end of the spectrum are arbitrary or fanciful words or terms that are created specifically to be trademarks. Such trademarks are commonly thought to be the strongest because the mark conveys what its owner wants it to convey and nothing more. Examples of such strong trademarks include "Kenmore" for Sears household appliances, "Formica" for American Cyanamid's countertops, and "Kodak" for Eastman-Kodak's cameras and film.

Somewhere in between on this sliding scale are suggestive and descriptive words or terms. The distinction between them is critical because, while suggestive words are protected under trademark law, merely descriptive words are not. Suggestive words or terms are protected as trademarks because they require some exercise of imagination to associate the mark with the goods. Du Pont's "Silverstone" for cookware coatings and Proctor & Gamble's "Head and Shoulders" for dandruff shampoo are strong, suggestive marks that help do the selling job. On the other hand, merely descriptive words are not suitable for trademark protection because they directly convey an immediate idea of some important or significant aspect of the product and the "law [will] not secure to any person the exclusive use of a trademark consisting merely of words descriptive of the qualities, ingredients, or characteristics of an article of trade." *Beckwith v. Commissioner*, 252 U.S. 538, 543 (1920). Obviously, the line distinguishing between what is suggestive (and protectable) from what is merely descriptive (and not protectable) is not a bright one. One commentator suggests this subjective test as a guideline:

> Generally speaking, if the mark imparts information directly, it is descriptive. If it stands for an idea which requires some operation of the imagination to connect it with the goods, it is suggestive.
>
> Seidel, Datroff & Gouda, *Trademark Law and Practice*, Sec. 406, p.77 (1963).

The proscription against using a merely descriptive word as a trademark is not without exception, however, because trademark law is sensitive to the realities of the market place. In circumstances where a descriptive term, through use, has acquired distinction - an identification by consumers of the descriptive term with a single source of origin - trademark law is willing to accommodate itself to later experience and afford protection to such a term under the doctrine of "secondary meaning". *See, e.g., American Waltham Watch Co. v. United States Watch Co.*, 173 Mass. 85 (Mass Supr. Ct. 1899). Proof that a mark has acquired secondary meaning with the public requires a rigorous evidentiary showing that the mark has become distinctive of the applicant's goods through use. Under the circumstances, it is said that the mark is no longer "merely descriptive." While no one factor is determinative, the Second Circuit Court of Appeals has noted that courts will look to (i) advertising expenditures; (ii) consumer studies linking the name to a source (iii) sales success, (iv) unsolicited media coverage of the product, (v) attempts to plagiarize the mark and (vi) length and exclusivity of use. *Thompson Medical Co. v. Pfizer, Inc.*, 225 U.S.P.Q. 124 (2d Cir. 1985). *See*, for example, *In re Minnetonka, Inc.*, 3 U.S.P.Q. 2d 1711 (TTAB 1987), holding that "Soft Soap" was merely descriptive for liquid hand soap but had acquired secondary meaning and, therefore, was eligible for registration with the PTO.

Protecting Your Trademark

Although there is no requirement that a trademark be registered with the PTO, there are advantages to be gained by doing so. Registration constitutes notice of a claim of ownership, creates certain presumptions regarding ownership and validity, and brings to the registered owner the remedies for infringement provided by the Lanham Act (15 U.S.C. §*1151, et seq.*). A certificate of registration is prima facie evidence of the registrant's ownership of the mark and exclusive right to use it. 15 U.S.C. § 1057(b). A mark that has been in continuous use for five years following registration becomes incontestable, except in certain circumstances. *See* 15 U.S.C. § 1065. This means that the mark has secondary meaning and cannot be challenged unless its registration was fraudulently obtained, it is (or has become) generic, or it has been abandoned. 15 U.S.C. § 1064.

An irony of trademark law is that a particularly strong trademark risks losing its distinctiveness and becoming generic. "Cellophane", "Lite", "aspirin", and "Gold Card" proved to be too good for protection.

To obtain registration the owner of the trademark must make application under Section 46 of the Lanham Act. Once a suitable word or symbol has been selected, a search should be conducted of the Principal Register maintained by the PTO. There are several statutory reasons for rejecting candidates for registration. By far, the most common reason is likelihood of confusion with a prior mark. A trademark is not registrable if it "so resembles a mark or a trade name previously used in the U.S. by another, and not abandoned, as to be likely, when applied to the goods of the applicant to cause confusion or mistake, or to deceive." 15 U.S.C. § 1052(d).[1] Search firms will provide this search service for a relatively modest fee. Since, as we have said, rights in a trademark are acquired only by use, prior to filing an application for trademark, the mark should be used with the goods in interstate commerce. Evidence of such use must be included in the application.

During October, 1988, however, Congress authorized an "intent to use" trademark registration system, whereby an applicant may apply to register a trademark based on a bona fide intention to use the mark in commerce. If the mark clears the allowance process, the applicant will then have six months to make use of the mark. Once the mark is used and registered, the registrant will obtain nationwide "constructive use" priority dating back to the date of its application for registration. Until regulations under the Trademark Law Revision Act are promulgated, however, actual use will be safer and success more certain.

If, after examination, the mark is deemed registrable by the Trademark Examiner, the mark is published in the Official Gazette, putting the world on notice of the registrant's claim to that trademark. A prior owner of a conflicting mark (registered or not) may assert his rights at this application stage by opposing registration on grounds, *inter alia*, that there exists a likelihood of confusion or mistake between the proposed mark and an existing mark. 15 U.S.C. §1063. The opposition is then considered by the Trademark Trial and Appeal Board. If the opposition is rejected, appeal may be taken to the Court of Appeals for the Federal Circuit and then, certiorari may be sought from the United States Supreme Court. Trademarks that are found to be entitled to registration have a term of 10 years, subject to the owner's continued use of the trademark. The registration period was reduced from 20 years to 10 years by the October, 1988 revision.

An irony of trademark law is that a particularly strong trademark risks losing its distinctiveness and becoming generic. When the public comes to regard the trademark as the common descriptive name for that type of product, rather than as identifying a particular source of the product, the trademark has become generic.Some famous cases include Du Pont losing "cellophane" as a trademark for transparent wrapping, *Du Pont Cellophane Co. v. Waxed Products Co.*, 85 F.2d 75 (2d Cir.), *cert. denied*, 299 U.S. 601 (1936) *and reh. denied*, 304 U.S. 575 (1938); Miller Brewing Company losing "Lite" as a trademark for reduced calorie beer, *Miller Brewing Co. v. Falstaff Brewing Corp.*, 211 U.S.P.Q. 665 (1st Cir. 1981); and Bayer losing "aspirin" as a trademark for a pain relieving drug, *Bayer Co. v. United Drug Co.*, 272 F. 505 (S.D.N.Y. 1921). A recent case is *American Express Co. v. Mastercard International, Inc.*, 7 U.S.P.Q. 2d 1829 (S.D.N.Y. 1988) holding "Gold Card" generic for credit card services.

As a result of these examples and many others, owners of trademarks must be alert to maintaining the status of their trademarks. King-Seely Thermos Co., which began using "Thermos" as a trademark in 1907, discovered that its trademark had acquired firm roots as a descriptive or generic word for vacuum-insulated bottles. It therefore intensified its efforts to educate those in the trade that "Thermos" was a trademark. But, King-Seely failed to police generic uses of its trademark by consumers and consumer publications, and "Thermos" was later held to be generic. *King-Seely Thermos Co. v. Aladdin Industries, Inc.*, 321 F.2d 577 (2d Cir. 1963). The Court's thoughtful decree, however, permitted the defendant to use "thermos" only when preceded by the possessive of the name "Aladdin" and prohibited any description of the defendant's product as "original" or "genuine". An example of a company that successfully avoided losing a valuable trademark is Xerox, which waged a campaign encouraging the public to cease using the "Xerox" trademark improperly when they wanted a photocopy made of a document. Most of us today, as a result of Xerox's efforts, ask for a "photocopy" instead of a "Xerox copy."

Good trademark usage, therefore, begins with practical considerations such as these: distinguishing the mark always with an initial capital letter and making it stand out in some way (*i.e.*, through italics, quotation marks or artwork); describing the mark by using an appropriate generic term with the trademark (*i.e.*, "Kleenex" tissue); relating the mark to the owner (*i.e.*, Du Pont "Teflon" TFE resins); and, if registered, identifying the mark as a registered trademark (*i.e.*, use the symbol ®).[2] Then, when the owner's attention is brought to an inappropriate or unauthorized use of the trademark, the owner should take steps to stop it. Continuous public use is essential, for just as trademark ownership is defined by use, so the owner may be found to have abandoned his mark and the rights that go along with it if he stops using it. The use must be on goods, the packaging for goods, display cards to which goods are affixed, or promotional or sales materials accompanying the goods. Care should be

Where a descriptive term has acquired distinction, trademark law is willing to accommodate itself to later experience and afford protection under the doctrine of "secondary meaning".

(Continued on next page)

(Trademarks continued)

taken, therefore, to use the trademark whenever appropriate and, if it is registered, to use the statutory notice with the trademark.

Remedies For Trademark Infringement

An owner of a registered trademark may look to a full panoply of remedies under federal law, state law, or common law for trademark infringement. Section 32 of the Lanham Act prohibits any "colorable imitation of a registered mark in connection with the sale. . . of any goods or services [where] such use is likely to cause confusion, or to cause mistake, or to deceive..." 15 U.S.C. §1114(1)(a). Section 43(a) prohibits any false designation of origin or false description of goods, or any misrepresentation as to goods. 15 U.S.C. §1125(a). Therefore, most actions under federal law for trademark infringement include counts for both trademark infringement and misrepresentation or misdescription or origin of the goods.

In most cases, the infringement question boils down to whether the simultaneous use of the two marks is "likely to cause confusion," a notion that is not subject to precise definition and is largely intuitive. Each case generally turns on its own peculiar set of facts, but the courts have identified various factors that will be considered, such as:

1. The strength of the earlier trademark -- is it a strong arbitrary mark, is it suggestive or descriptive, is it generic?

2. The similarity of the marks -- how close are they in spelling, appearance, and sound?

3. The geographical proximity of the products -- are consumers likely to believe that both products emanate from the same source?

4. Evidence of actual confusion -- does the prior owner have actual evidence that the public has been confused or misled by the existence of the two similar marks?[3]

5. The good faith of the junior user -- is there evidence of an attempt to capitalize on the favorable reputation of the earlier mark?

6. The sophistication of the buyers of the products -- how much attention are consumers likely to give in purchasing these goods or services?

7. The quality of the junior user's product and the nature of his trade practices -- an inferior product or disreputable trade practice will favor the prior user.

See, e.g., Polaroid Corp. v. Polarad Electronics Corp., 287 F.2d 492, 495 (2d Cir.), *cert. denied*, 368 U.S. 820 (1961); *Robarb Inc. v. Pool Builders Supply of the Carolinas, Inc.*, 7 U.S.P.Q. 2d 1616 (N.D. Ga. 1988); *Del Laboratories, Inc. v. Alleghany Pharmacal Corp.*, 516 F. Supp. 777 (S.D.N.Y. 1981); *Schoenfeld Industries, Inc. v. Britannia Sales, Ltd.*, 512 F. Supp. 979 (S.D.N.Y. 1981). *See also Specialty Brands, Inc. v. Coffee Bean Distributors, Inc.*, 748 F.2d 669 (Fed. Cir. 1984); *In re E.I. duPont deNemours & Co.*, 476 F.2d 1357 (C.C.P.A. 1973).

Remedies for infringement under the Lanham Act include injunction,[4] *see, e.g., Tree Tavern Products, Inc. v. ConAgra, Inc.*, 640 F. Supp. 1263 (D. Del. 1986), and monetary relief in the form of (i) defendant's profits, (ii) any damages sustained by plaintiff and (iii) costs of the action. 15 U.S.C. §1116, 1117(a).[5] The Lanham Act also affords the Court discretion to award treble damages -- an award up to three times the amount found as actual damages -- and to award reasonable attorneys' fees in "exceptional cases" to the prevailing party. *Id.* A declaratory judgment is also available in an appropriate case under 28 U.S.C. §2201. *See Ultronic Systems Corp. v. Ultronix, Inc.*, 217 F. Supp. 89 (D. Del. 1963).

Non-Federal Protection -- Delaware Law

Delaware law also affords a trademark owner a plentiful assortment of remedies for trademark infringement. The Delaware Trademark Act (6 *Del. C.* §3301 *et seq.*) provides those who register their mark with the Secretary of State in accordance with Section 3304 of the Act remedies of injunction and monetary relief in the form of defendant's profits and plaintiff's damages. 6 *Del. C.* §3314. Infringers are defined in much the same way as under the Lanham Act. *See* 6 *Del. C.* §3312. Section 3315 expressly reserves a trademark owner's common law rights: "Nothing herein shall adversely affect the rights or the enforcement of the rights in marks acquired in good faith at any time at common law." 6 *Del. C.* §3315.

Today, trademark law is only one aspect of the broader law of unfair competition, with trademark infringement constituting one kind of unfair competition. Thus, in bringing a trademark infringement suit, counsel should consider whether the client may also have a claim for other kinds of unfair competition, such as false advertising, or imitation of trade dress (product packaging or labeling) or misappropriation. "Likelihood of confusion" is also the test for common law unfair competition claims. Delaware's Uniform Deceptive Trade Practices Act (6 *Del. C* . §2531 *et seq.*) codifies Delaware's common law of unfair competition. The Act covers a wide array of deceptive trade practices, including the causing of "likelihood of confusion or of misunderstanding as to the source, sponsorship, approval or certification of goods of services." 6 *Del. C.* §2532(a)(2).[6] The Act provides for an injunction, treble damages and, in "exceptional cases," attorneys' fees to the prevailing party. 6 *Del. C.* §2533. This Act also makes clear that it provides remedies in "addition to remedies otherwise available... under the common law or other statutes of this State." ■

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The authors of this article, father and son (a DELAWARE LAWYER first), are both expert in matters of intellectual property law. Eugene Grimm is corporate counsel for the DuPont Company and adjunct professor of law at Widener University School of Law. His son, Thomas Grimm, is a partner in the Wilmington firm Morris, Nichols, Arsht & Tunnell.

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DELAWARE TRADE SECRET LAW: *AMERICAN POTASH* REVISITED

Douglas E. Whitney

This year marks the silver anniversary of Delaware's leading trade secret case, a case that brought needed clarity to the common factual setting where a departing technical employee threatens to compromise his employer's trade secrets. Twenty-five years ago, trade secret law was a swamp. As one commentator observed:

> ...one might justifiably classify as a 'trade secret' almost anything or everything useful or advantageous in business activity that is not generally known in the trade or easily or immediately ascertainable to members of the trade.

Stedman, *Trade Secrets*, 23 Ohio St. L.J. 4 (1962). Virtually all jurisdictions were guided by the Restatement formulation, which set out several subjective factors to define the term "trade secret" and make it a tort to acquire another's trade secret by "improper means".[1]

Irreconcilably different results abounded among the decisions from different state jurisdictions applying the *Restatement* guidelines and sometimes, indeed, within the same jurisdiction. There was no certainty even in Delaware. Essentially, most cases turned on relative culpability. If the accused was perceived by the Court as pursuing an unfair competitive advantage by gaining improper access to another's technology, the trade secret owner would usually prevail. On the other hand, if the plaintiff was seen as more interested in restraining its former employee's freedom than in protecting its own technology, usually a reasoned decision would favor the defense.

Naturally, the unpredictability of the law created an unhappy state for the courts and counsel alike. Comparison of the factual settings from an Ohio case and a Delaware case demonstrates this problem especially well.

In 1962, Donald W. Wohlgemuth, technical manager of space suit engineering for the B.F. Goodrich Company, at Akron, Ohio, received a phone call from an employment agent indicating that a large company located in Dover, Delaware, was interested in employment discussions. The request originated with the International Latex Corporation, and Goodrich, active in the development of space suits for Project Mercury, had recently lost to Latex a subcontract for the development of space suits for Project Apollo.[2] Wohlgemuth was given a tour of the Dover facilities by a division director, entertained at the home of a corporate vice president, shown housing in Dover by another executive and, finally, offered the position of division manager of engineering at an annual salary increase of 30 percent. Wohlgemuth accepted almost at once. Having submitted his resignation, he was then informed that "...he was taking with him a body of information which did not belong to him...but...to the company, and that there was a matter of company loyalty and ethics involved". He replied that "...loyalty and ethics had their price; insofar as he was concerned, International Latex was paying the price." Furthermore, when asked whether he "...could go into this position with a competitor and not use information which was proprietary to Goodrich," Wohlgemuth replied that "Once he was a member of the Latex team, he would expect to use all of the knowledge that he had to their benefit." In reply to a question of a Goodrich lawyer, asking whether he intended to use confidential information belonging to Goodrich on behalf of Latex, he retorted, "How are you going to prove it?"

At about the same time, Donald E. Hirsch, an engineer in Wilmington, read a local newspaper advertisement for one with titanium dioxide experience for a position as manager of plant technical services. Hirsch had been engaged in titanium dioxide design and development for DuPont for seven years, and was in the task force designing a new chloride process plant. Although DuPont had been the only successful developer of a commercial scale chloride process plant, American Potash had designed and was planning to build a similar plant in competition with DuPont. Hirsch was first required to sign an agreement that he would not disclose any trade secrets or other proprietary data of DuPont. Thereafter he was offered the managerial position at a salary substantially equal to his current earnings. Hirsch informed his supervisor of the opportunity and shortly thereafter resigned from DuPont. During the interview, Hirsch, apparently intending to respect DuPont's interests, agreed not to disclose "...any information that he [knew] to be proprietary or confidential information, data, development or trade secret of a third party without the prior written consent of said third party." And as Hirsch later testified: "I wanted to assure myself that they wanted my skills and general knowledge and not DuPont's secrets and proprietary know-how, and I received that assurance to my satisfaction." Although informed that DuPont was planning to block his employment with American Potash, Hirsch proceeded to undertake his new position.

In the Ohio case, where culpable intent was plain, the employer's relief was no greater than what DuPont's Hirsch had voluntarily given up. Wohlgemuth was restrained only from disclosure of "...any information or data relating to the design, manufacture and/or sale of [high-altitude pressure suits, space suits and/or similar garments][3] ... made known to him by virtue of his employment with Goodrich..." Hirsch, in the Delaware Chancery action, suffered a much more drastic restraint: he was "...prohibited... from divulging or disclosing...[DuPont's] trade secrets and confidential information relating to the manufacture of titanium dioxide...by its chloride process...[and] from accepting or undertaking any employment...with Potash in connection with or related to the operation and development of a chloride process or...[the manufacture of titanium dioxide] by a chloride process".[4]

It is ironic that the activities in the *Wohlgemuth* case occurred in Dover,

(American Potash continued)

Delaware, for if the Goodrich counsel had had the prescience to understand how the Delaware Court of Chancery would weigh the equities, it is quite likely that a better result would have been achieved. He certainly would have been restrained from his intended employment, as Hirsch was on far less compelling facts.

Unlike the Ohio Court, the Delaware Chancery Court recognized that new employment should be enjoined where trade secrets inevitably would be misused. The simple fact is that in virtually every case where an employee trained in a specialized technology is hired to work in the same area for a competitor, all concerned know very well what the real motivation is. Where disclosure or use would be inevitable, such employment should be restrained pending trial. In Delaware it consistently has been.

In the twenty-five years since *American Potash*, it has been cited in only seven Chancery decisions. This, in a way, is a measure of how settled the law has become, for most cases are settled between the TRO (For our non-lawyer readers: TRO: Temporary Restraining Order) and preliminary injunction stage - when the evidence becomes clear to both sides, and

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A thought for today:
"Loyalty and ethics have their price!" -- Donald W. Wohlgemuth, former B. F. Goodrich space suit expert.

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the result, based upon *American Potash*, predictable. The critical finding in *American Potash* was that DuPont's trade secrets would "inevitably" be used in the new employment.

In one case, perhaps the longest Delaware trade secret trial of recent times, misappropriation had occurred and the defendant was in production before the suit was filed. Accordingly, a TRO was inappropriate, and a preliminary injunction was denied, largely because the evidence preliminarily presented a *fait accompli*, tipping the status quo equities in favor of the defense. *Data General Corporation v. Digital Computer Controls, Inc.*, Del. Ch., 297 A.2d 433 (1971), *aff'd*, Del. Supr., 297 A.2d 437 (1972).[5] Nevertheless, after trial revealed the existence and misappropriation of valuable

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PROTECTION OF TRADE SECRETS THROUGH EMPLOYMENT AGREEMENTS

Collins J. Seitz, Jr.

The employer who turns to the Courts for relief against a former employee who has misappropriated trade secrets bears a heavy burden of proof.[1] In the absence of an agreement restricting an employee's post-employment activities, the employer must prove: (1) the existence of a trade secret; (2) communication of the secret to the employee; (3) the employee's understanding that the information was to be secret; and (4) the inevitable improper use or disclosure of the secret. An employer's failure to prove *any* of these elements is fatal to its claim.

The weapons in a former employee's arsenal are formidable. Proving the existence of a trade secret is no easy task. The former employee usually has intimate knowledge of the secret and where it might be found in the public domain. A former employee can also plead ignorance of the fact that the information was meant to be treated as a "secret". Unless the employer has a comprehensive system in place for protecting trade secrets, the Courts are sometimes sympathetic to this defense. Finally, an employee unrestricted by an employment agreement may engage in certain activities that might otherwise be prohibited, such as starting reasonable preparations to compete with the former employer *while still employed.*

For instance, in *Science Accessories Corp. v. Summagraphics Corp.*, Del.Supr., 425 A.2d 957 (1980), the employer sued three former employees, claiming that they misappropriated an invention, which should have been disclosed to the company. It also claimed that the employees wrongfully started preparing to compete before quitting. The Supreme Court ruled that, in the absence of an employment agreement restricting post-employment activity, employees may make reasonable preparations to compete both before and after termination of employment. *Wilmington Trust Co. v. Consistent Asset Management Co.*, C.A. No. 8867, slip op. (Del.Ch. March 25, 1987) (Allen, Ch.) reached the same result. The Court "accorded no weight" on a preliminary injunction motion to the fact that former employees accused of misappropriating trade secrets rented office space and took other actions while still employed by the company.

The Employment Agreement

To eliminate some of the problems in protecting valuable confidential information, an employer can impose certain duties on key employees through an employment agreement. The first basic protection is a covenant not to disclose confidential information both during and after employment.[2] Although the law implies a duty on the part of a current or former employee not to disclose trade secrets, the advantages of a contractual obligation are several. First, an agreement read and signed by the employee can negate a claim that the employee was never told of such an obligation. Second, the covenant is evidence of the employer's sensitivity to the existence of trade secrets within its organization, and a willingness to take steps to protect confidential information.

An employee is also under an implied obligation not to compete directly or indirectly with a former employer during the course of that employment. However, as is true for the covenant not to disclose confidential information, turning the implied obligation into a contractual commitment places the employee on notice of his obligations and stresses the importance of ethical conduct towards the employer. Therefore, a common covenant in employment contracts is a covenant not to compete with the employer during the term of employment.[3] Such a covenant is often extended to require an employee to devote full time and attention to the employer's business.

The additional obligation is intended to preclude "moonlighting" of any kind.

The covenant not to disclose confidential information and the covenant not to compete are, as stated previously, contractual obligations derived from duties every employee owes to an employer. These duties do not, however, necessarily preclude an employee's accepting employment with a competitor or starting a competing business. In the absence of a contractual obligation not to compete with the employer after termination of employment, a former employee may compete freely and openly. Although the former employee cannot use trade secrets and confidential information in the competing enterprise, the temptation to do so has led to a large number of lawsuits. An alternative to relying upon implied duties and their concomitant difficulties is a covenant not to compete after employment.[4]

Such a covenant has many advantages. Assuming the covenant is enforceable (discussed below), all that needs be shown to constitute a violation is acceptance of employment with a competing business. Moreover, by circumscribing employment with a competing enterprise, the likelihood of confidential information disclosure lessens, because only a competitor needs such information.

The protection provided by a post-employment non-competition agreement runs contrary to the equally important interest of a former employee to use the general skills he has acquired, and to make a living free from the servitude of former employers. Because of this tension, a non-competition agreement must meet certain requirements before it will be enforced by the Courts.

Faw, Casson & Co. v. Cranston, Del.Ch., 375 A.2d 463 (1977) established that a covenant not to compete will be enforced if it is reasonable in time and scope and essential for the protection of the employer's economic interests. Delaware Courts have generally upheld limitations of one to two years from the date employment is terminated. The geographical scope of the covenant must be reasonably related to the employer's business territory and the area in which the employee actually engaged in the

(Continued on page 49)

(American Potash continued)

trade secrets, involving elaborate copying of complex computer circuitry from proprietary drawings, a permanent injunction was entered, resting upon the authority of *American Potash. Data General Corporation v. Digital Computer Controls, Inc.*, Del. Ch., 357 A.2d 105 (1975).[6]

A few years later, again under the authority of *American Potash*, a computer programmer was restrained from working for a competitor. *American Totalisator Systems, Inc., et al. v. Automatic Totalisator, Inc.*, (Del. Ch., Mar. 31, 1978). The same corporate parties met again in a case involving a departing financial officer, and the Court held that a Strategic Planning Report, derived from a four-month secret study, constituted protectable trade secrets,[7] and under the authority of *American Potash* enjoined the corporate and individual defendants. *American Totalisator Co. v. Autotote, Ltd.*, (Del. Ch., Aug. 18, 1985). In another case, preliminary relief was denied and *American Potash* distinguished after the departing employee - a high school graduate and production foreman in a PVC plant - had testified that there was not any way the plaintiff's technology could be used in the defendant's "very different machinery." *American Hoechst Corporation v. Nuodex, Inc., et al.*, (Del. Ch., April 23, 1985). And in *McCann Surveyors, Inc. v. Carol A. Evans*, (Del. Ch., July 24, 1987), preliminary relief was denied and *American Potash* distinguished, because it did not entail a "valuable trade secret or other proprietary information".

In each of these cases citing *American Potash* its standard was precisely applied. This predictable application of clear legal standard was made even in the many other Chancery trade secret cases where *American Potash* was followed without citation. Most of these cases did not involve classic technological trade secrets.

The first such case rested only on the Delaware Uniform Trade Secret Statute, 6 *Del.* C-. §2001, and cited no case authority; it was a suit brought by a medical organization against an oncologist, who had "surreptitiously misappropriated" plaintiff's compilations of cancer patients. *Dickinson Medical Group, P.A. v. Foote*, (Del. Ch., May 10, 1984). With some misgivings Chancellor Brown reasoned that the compilation met the statutory definition and that an injunction was appropriate, but he conditioned it upon plaintiff's giving each patient written notice of the defendant's new location.

The most thorough Delaware analysis of trade secret law under the uniform statute is found in *Technicon Data Systems, Corp. v. Curtis 1000, Inc.*, (Del. Ch., Aug. 21,1 1984), which inexplicably did not cite *American Potash.* The defendant had successfully avoided a TRO, but a preliminary injunction was entered upon a strong showing of probability of success and irreparable injury. Many of the facts were not contested. The Court analysis of the Uniform Trade Secrets Act led it to the conclusion that proprietary rights existed, that defendants' actions constituted misappropriation and not reverse engineering, and concluded that a preliminary injunction was appropriate. It seems an analysis along the lines of *American Potash* (*i.e.*, whether in the new venture trade secrets would inevitably be used) would have reached the same end as well.[8]

A most significant case - one that Chancellor Allen recently suggested evidences the Court's "concern... with the rights of an individual to earn a living"[9] - is *Wilmington Trust Co., v. Consistent Asset Management Co.* Del. Ch., Mar. 25, 1987). While the fact of "inevitability" seems to have been met, in that the individual defendants certainly would make use of the alleged trade secrets, preliminary relief was denied because plaintiff had not met the threshold burden of showing that what would inevitably be used was a protectable trade secret. *American Potash* was cited for an unrelated point. The case centered on Wilmington Trust's successful market timing formula, called Benchmark, which Chancellor Allen found, in detailed analysis, was the product of the application of personal skills to well known market and mathematical phenomena.

A more recent case, decided from the bench by Chancellor Allen, makes it appropriate to revisit *American Potash.* A restraining order was entered, where, as in *American Potash,* a departing employee had been hired to work in advanced chemical technology, doing very similar work for a competitor that was trying to catch up technologically with the plaintiff. *ICI Americas Inc. v. Ronald Burke, supra.* Ruling from the bench, Chancel-

(Continued on next page)

(American Potash continued)

lor Allen spoke of recent cases like *Wilmington Trust* in weighing the purported right of the employee's "ability to make contracts of employment", which he concluded was outweighed by ICI's "supervening" risks. While the opinion did not refer to the *American Potash* standard, nevertheless *ICI* seems the sort of case where, as in *American Potash*, the departing employee would "inevitably" use the former employer's secret technology in his chosen employment. When a case turns on this simple standard of inevitability, the correct result is reached without the more subjective - and sometimes difficult - analysis along the lines of "right to earn a living" versus abstract proprietary interests.

Twenty-five years later *American Potash* still seems the best way to resolve motions for preliminary relief where complex proprietary technology of a former employer might be used in new employment. For to state the basic proposition is to answer the critical issue: can it be said that an employee has the right to make a new contract of employment that would inevitably require him to make use of valuable technology his former employer endeavored to keep confidential? ■

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Douglas Whitney, a member of the Wilmington firm of Morris, Nichols, Arsht & Tunnell, has extensive experience in the litigation of intellectual property issues. He has tried patent cases in the United States District Court for the District of Delaware and elsewhere, and trade secret cases in the Court of Chancery. He holds a degree in chemical engineering from Cornell University and a J.D. degree from Columbia.

(Employment Agreements Continued)

employer's business. Finally, the employer's interest protected by the covenant must be substantial. Obviously, it would be unsuitable to impose non-competition obligations on a convenience store clerk as opposed to a key employee with intimate knowledge of his employer's secret process.

Delaware cases addressing the enforceability of non-competition agreements have dealt primarily with sales personnel who have accepted employment with a competing business. For example, in *Comfort, Inc. v. McDonald*, C.A. No. 1066(s), slip op. (Del.Ch. June 1, 1984) (Brown, Ch.), the plaintiff was an electrical contracting firm conducting business on the Delmarva Peninsula. The defendant was a former sales representative who had agreed for a period of one year not to work in the heating, air conditioning, plumbing, or electrical field throughout the Delmarva Peninsula south of the canal. The interest of the employer protected by the covenant was confidential information about plaintiff's bidding procedures. After finding that the defendant was doing "exactly that which he covenanted not do to," the Court issued a temporary restraining order prohibiting defendant from participating in any bid preparations where his former employer was also bidding on the same contract.

Similarly, in *Equitable Life Insurance Co. v. Young*, C.A. No. 7993, slip op. (Del.Ch. May 6, 1985) (Berger, V.C.) an insurance salesperson executed a non-competition agreement agreeing for a period of one year after employment not to solicit existing policyholders within his district with an eye to replacing their coverage. Plaintiff was granted a temporary restraining order and later a preliminary injunction precluding the defendant from soliciting plaintiff's current policy holders. The employer's protected interests were its customer list and the particular knowledge about each customer's insurance requirements, which could be helpful to a competitor in replacing coverage.

The Courts are not always willing to side with the employer's interest when the result would prevent an employee from practicing his trade, or the claimed "competition" is insubstantial. In *Burris Foods, Inc. v. Razzano*, C.A. No. 1077, slip op. (Del.Ch. July 18, 1984) (Walsh, V.C.) the Court of Chancery refused to issue a temporary restraining order against a former sales representative. Although the Court found the time and territorial restrictions reasonable, it held that the former employee's new position was too indirect a form of competition to invoke the non-competition agreement. While employed by plaintiff, the defendant sold food products directly to *restaurants* in the Dover-Smyrna area. In the new position, manufacturer's representative, the defendant was hired to make sales to *distributors* (potentially including plaintiff) but not direct sales to restaurants. Because of the broader scope of the former employee's new business activities, and the absence of direct competition and consequent harm to plaintiff, the Court denied all relief. Thus, it is clear that the mere existence of a non-competition agreement will not guarantee its enforcement.

What happens if the covenant is too broad? The traditional view was to strike the covenant down and release the former employee from the contractual obligation. The modern view, however, favors enforcement of the covenant after it has been modified by the Court to make the onerous provisions reasonable. Indeed, even where non-competition agreements have been upheld, Court-ordered relief may fall short of the broadest protections extended by the covenant. This result is a reflection of the Court's attempt to balance the legitimate interests of the employer with the former employee's right in earning a living to use the general knowledge he has developed over the years.

Post termination non-competition agreements are not suitable for every business. Valuable employees will sometimes refuse to agree to such restrictions. Furthermore, non-competition agreements are not permitted in some professions, such as law and medicine, where the public's interest in valuable personal services outweighs the business interests of the employer.

Fundamentally, the enforceability of non-competition agreements will be decided by the shifting sands of "equity" -- what is the fair thing to do given the particular competing interests. The fairness of a covenant not to compete can be established and misunderstandings avoided if, at the beginning and end of the employment relationship, the employee is aware of the employer's expectations and the restrictions imposed by the agreement. The best way to accomplish this result is the use of entrance and exit interviews with new and departing employees. When the agreement is signed, it should be carefully reviewed by the employer's representative and the employee, along with a witness. What should the employer do if the prospective employee refuses to sign a non-competition agreement? From a morale point of view, it is undesirable to have some key employees bound by a non-competition agreement, while others are free from such restrictions. In the extreme case where a prospective employee's value outweighs uniformity concerns, the employment agreement should contain a detailed covenant not to disclose confidential information. Entrance and exit interview procedures should be followed scrupulously, and the prospective employee should sign a document recognizing the extent of his nondisclosure obligations. When an employee is leaving, the procedure should be repeated, and a document should be signed and witnessed whereby the employee once again reaffirms his post-employment obligations and leaves with a complete understanding and respect for the employer's expectations. Such a procedure undercuts any claim of ignorance, and heightens the "reasonableness" of imposing the non-competition obligations on an employee who freely and with full knowledge agreed to the restriction before accepting employment. ■

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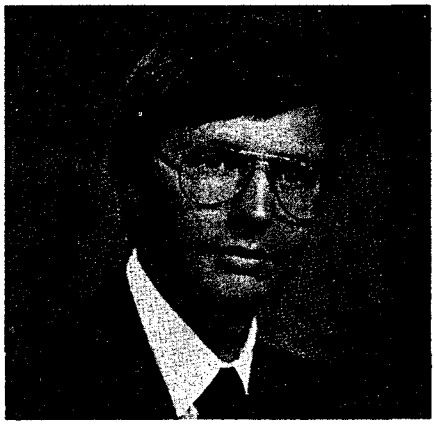

Collins J. Seitz, Jr., a graduate of the University of Delaware and Villanova University School of Law, is an associate at the Wilmington firm of Connolly, Bove, Lodge & Hutz. His article is drawn, in part, from the direct experience of Chancery litigation in recent cases construing the protection afforded trade secrets. He has lectured on this topic and has been a very active member of the Continuing Legal Education Committee of the Delaware State Bar Association.

INDUSTRIAL ESPIONAGE IS A CRIME

F. L. Peter Stone

A lab worker seldom seen at the Research Center in the evening inserts his key card in the security lock and enters the building carrying a briefcase. He shows his pass to the guard monitoring the TV screens and proceeds down a long corridor, past his office, to a nearby lab. Again he inserts his key card, enters the lab and walks to the large refrigeration unit. He rests his briefcase on a desk and removes several labeled test tubes from the refrigerator. Opening his case reveals inside a tiny battery operated refrigeration unit into which he places the test tubes. He takes several current lab notebooks from the shelf, photostats them in their entirety and places a neat stack of copies in the case next to the portable refrigerator. Minutes later finds him driving the Long Island Freeway to Kennedy Airport, where he boards a non-stop overnight flight to Milan. Over the Atlantic, he leans back in his seat and opens his wallet to re-examine the confirmation that the largest single sum he ever received is on deposit in his new Swiss bank account. He speculates absently about his role in the start of an industry. In the next few days in Italy he and his friends will be responsible for the birth of a new antibiotic manufacturer in Europe, producing and selling a revolutionary product. The little refrigerator under his seat contains otherwise unavailable, first generation live organic cultures, which are the basis for an effective antibiotic against a broad spectrum of dangerous diseases, while producing negligible injurious side affects. Before today, this recently approved antibiotic had been an exclusive, heavily protected innovation, the secrets of which were known only to his American employer. Also in his briefcase are copies of the inventor's lab notebooks which contain all necessary trade secrets and developmental information to enable any scientist skilled in organic chemistry to successfully reproduce this new medicine. Thus, in a few months, the new drug available from his company only, will also be produced and widely sold at great profit by his European friends. He further speculates that what he is about may really be a public service and a boon to humanity - besides fully funding his personal retirement program.

Mr. Stone brings the authority of experience to his chilling account of industrial espionage. He has been both a state and federal prosecutor. As United States Attorney for Delaware in 1969 until 1972 he conducted investigations and litigation bearing on industrial espionage and other forms of intellectual property misappropriation. A graduate of Dartmouth and Harvard Law School, he is today in private practice with the Wilmington firm Connolly, Bove, Lodge & Hutz.

A trade secret case can sometimes read more like a Robert Ludlum novel than the expected dry squabble between competitors in an abstruse field of technology. Complexity, intrigue, coupled with a criminal state of mind, are ingredients of the story. The above scenario is extrapolated from U.S. and European case law.[1] Involved in some of the cases was an American professor considered by many a "master spy" of international high technology: Dr. Robert S. Aries. His notoriety is not only evident from the case law involving such prominent companies as American Cyanamid, Merck, Sprague Electric Company, and Rohm & Haas Co., but even reached the national media.[2] Aries has been described as an expert at extracting closely guarded and valuable trade secrets from some of the world's best scientific companies, apparently with high financial reward and minimal risk of punishment. For decades he stayed at least one step ahead of the law, during which time, as described by one of his most persistent pursuers: "Aries has shown contempt for the law, and his experience justifies his attitude..."[3] However, criminal actions as well as civil were mounted by the various victim companies and Aries was in court or on the run for many years. In 1979, a French court sentenced him to two years in jail for attempted blackmail of a European drug manufacturer. But ultimately such serious legal ramifications were avoided. Typically, Aries moved to another country.[4]

Although Aries' substantial success in contesting or avoiding numerous civil and criminal actions illustrates that the remedies for alleged industrial piracy are not invariably sure and sufficient, the Aries saga also shows the potential involvement of true criminal conduct and the need for a comparable response based in the criminal law.

In general, the criminal statutes and case law in this country have evolved over the last 25 years to try to meet this challenge. Traditional criminal and law conceptions have been re-examined and reworked to provide a means of relief. In the seminal case, *United States v. Bottone*, 365 F.2d 389 (2d Cir.), *cert. den.*, 385 U.S. 974 (1966), it was held that when the items stolen were key documents or actual microorganism cultures, used to produce valuable antibiotics, the value of the theft will be judged in light of the intrinsic trade secrets contained therein, not the retail cost of the tangible items themselves. Thus 50¢ worth of paper can become a $1,000,000 stolen item. This arose in the context of the federal criminal statute, 18 U.S.C. §2314, which limits federal jurisdiction with respect to prosecution of the receipt of stolen goods to items with a value in excess of $5,000. When the true value of the stolen antibiotic cultures and associated papers was allowed, the jurisdictional limit was far exceeded, and the conviction of a number of conspirators who stole, transported, and sold drug company secrets was confirmed.[5] This view of trade secrets has recently been confirmed in terms of federal mail and wire fraud prosecution in the conviction of a Wall Street Journal employee who

embezzled stock information and sold it to outside parties.[6]

In general, civil intellectual property law encourages public registry of information with concomitant loss of secrecy. So doing obviously reduces or eliminates the potential for "theft". The civil sanctions thereafter are for "infringement" of certain rights retained by the originator or his company, even though the conception is publicly available.

For example, a patent constitutes a 17 year monopoly for what is described and claimed therein, which the owner can retain exclusively or totally or partially license to others.[7] However, on public file in the U.S. Patent and Trademark Office is a written blueprint of the invention which anyone can obtain for $1.50 per patent. Still, unlicensed copying runs the risk of an infringement lawsuit. Similarly, trademarks obviously are publicly known and widely distributed or they would have no value to the owner. Trademarks are also centrally registered in the Patent and Trademark Office and copies are easily obtained, but unlicensed use for trade advantage or which causes product or service "confusion" leads to a civil remedy for infringement.[8] Copyrights are customarily enforced by civil infringement actions as well, but there does exist a little-used criminal statute carrying penalties for certain kinds of copyright abuse.[9]

Trade secrets, however, are a different breed of intellectual property. They are not centrally registered and are valuable only so long as they are unknown to the general public and competitors. Because unlicensed disclosure actually destroys the trade secret, owners strictly limit access and are more cautious about licensing than with patents, trademarks and copyrights.[10] Trade secrets consequently are a form of property much more subject to criminal theft as opposed to mere civil infringement. A closely-guarded research report, unobtainable in any legitimate way, may have a value several times its weight in gold to competitors. Unfortunately there exists a technology black market in which a buyer can be located, if not in this country, then elsewhere in the world.

In our highly mobile and competitive society, with many competing players both in this country and abroad, success or failure is often so closely linked to evolving technologies that many illicit, as well as legitimate, means of advancing a company's fund of scientific knowledge have developed. In order to succeed quickly, individuals and companies with disturbing frequency have rationalized lowering their ethical standards to the point where the activities engaged in are no different from other forms of criminal theft and fraud, such as embezzlement, bunko schemes, and securities fraud. They include such elements as bribes, breaking and entering, and the flat out stealing of another's property. Thus the rubric of "industrial espionage" has emerged which lends the activity a more romantic air than it deserves. In fact, competing industrial organizations either directly or through go-betweens increasingly have acted with the same *scienter*, or conscious criminal intent, characteristic of the run-of-the-prison con man, thief, or robber. Larceny, bribery and fraud cannot be justified as just rough and tumble vigorous competition. Consequently, it is not surprising that victim companies have looked beyond civil suits to criminal sanctions under federal and state law to counteract the criminal state of mind of the industrial spy.

In recent decades a number of traditional Commerce Clause federal criminal statutes, on the books for many years have been interpreted to cover industrial espionage. A prime example is Interstate Transportation of Stolen Goods (18 U.S.C. §§ 2314, 2315) discussed in the *Bottone* case. Other examples are the Travel Act (18 U.S.C. §1952), which makes unlawful use of facilities of interstate and foreign commerce to promote bribery or extortion;[11] and the mail and wire fraud statutes (18 U.S.C. §§ 1341, 1343), which prohibit the use of mails or wire communication facilities in furtherance of a scheme to defraud.[12] The actual acts of transportation, travel, or use of the mail or wires can be quite tangential to the basic plot. For example, merely transmitting payoffs to fellow conspirators after the theft and sale of trade secrets has been successfully prosecuted under Section 1341.[13]

At this point the range of federal criminal statutes that may be employed in a trade secret misappropriation case has become very broad. At one end is the Espionage Act (18 U.S.C. §794), which, in the case of misappropriation of defense secrets, particularly if sold to a foreign

government, entails very severe penalties, even capital punishment. On the other end of the range is a mosaic of misdemeanor statutes. One example is the Toxic Substance Control Act (15 U.S.C. §2614(d)), which makes it a minor misdemeanor if a government employee leaks trade secrets acquired due to the regulatory provisions of the Act. This type of minor criminal threat hardly allays the fears of regulated companies, which in all likelihood lose more trade secrets through bureaucratic errors, the Freedom of Information Act, and the persistent inquiries of competitors, reporters and consumer groups, than they do by late night laboratory break-ins. Once the trade secret genie is out of the bottle, the competitive damage is done and full restitution is unlikely, if not impossible, particularly from the federal government.[14]

State criminal statutes also occasionally become relevant. Some specifically refer to trade secret theft.[15] Most are similar to federal theft statutes, but sometimes can be more useful because they define the offending acts more broadly and also contain a definition of property subject to theft that embraces intangibles like trade secrets. Under the Delaware Code theft fits into this latter category.[16] In other states the applicable statutes are based on traditional narrow conceptions of larceny and may present difficulty because they do not make allowance for the stealing of valuable but intangible property.[17]

The relatively new wild card of possible criminal sanctions is the Racketeer Influenced and Corrupt Organization Act (RICO).[18] Under this federal law, ostensibly designed to attack organized crime, concerted stealing of trade secrets can constitute a "pattern of racketeering activities" necessary to invoke the statute, and this is so even if the defendant appears far removed from drug trafficking and the mob. RICO can be the basis of direct criminal action by a federal prosecutor, but it can also be used by victim companies as a civil tort allegation. The civil action plaintiff must show use of criminal means, or what would ordinarily be considered criminal conduct, such as transporting or receiving stolen property, wire fraud, mail fraud, etc. Federal and state bribery statutes can also be used the the "predicate acts" that invoke RICO[19]

The notorious Ivan Boesky insider trading case is not just a criminal prosecution under the securities laws. Some individual victims have sued Boesky on various tort claims, including misappropriation of use of trade secrets in a pattern that constituted violation of RICO[20]

RICO has been used in a number of creative ways by civil plaintiffs in purely commercial situations where the traditional perception of "racketeering" is absent but fraud between the parties existed.[21] In-laws of Claus Von Bulow, disappointed that he was not convicted of attempted murder of his wife, Martha, are now suing him under RICO on exactly the same facts as grounded the criminal prosecution.[22] This kind of case has lead to the accusation that RICO is either too broad or too broadly interpreted and efforts are pending in Congress to restrict application of the statute. But at this juncture it is still a potent weapon for a company that believes it has been victimized by theft of its secrets by a competitor. It is particularly attractive because an award of treble damages and attorneys' fees is possible for the successful litigant.[23] Thus it is a potential weapon grounded in criminal law, which is particularly appropriate for use where a conspiracy against the technology owner presents the same high degree of willfulness and malice found in a conventional criminal prosecution.

Criminal law as a deterrent or a weapon for victims of intellectual property misappropriation is imperfect, but on balance is a useful adjunct to available civil remedies. New laws have been enacted to address more sharply the added problems of modern technology in the hands of industrial spies. They include statutes aimed at electronic eavesdropping and computer fraud and abuse.[24] However, drawbacks and deficiencies remain. Consequently there are pros and cons that must be considered by the technology owner before attempting to invoke criminal sanctions.

Probably the most common incentive for invoking criminal law is that the threat of a criminal or RICO case may be considered a quick way to rectify the situation and obtain a beneficial settlement, which includes return of any missing property and money damages. However, threatening criminal prosecution, whether by government officials or private citizens, for the purpose of obtaining a civil resolution may be unlawful in itself and must be approached cautiously. There are other possible benefits from encouraging federal or state prosecutors to act, including that a criminal conviction could be introduced as evidence in a civil action based on the same transaction; the same criminal conviction might also be a hindrance to government contracts by the offending competitor; and criminal prosecution and attendant publicity may be a deterrent to similar conduct, if the victim is interested in the public good, as opposed to restitution. As a practical matter, resort to prosecutors and criminal courts is usually the last resort of victim companies after civil remedies have failed, or judgments obtained proved uncollectable.

There are a number of drawbacks for intellectual property owners to the criminal avenue of relief. The most obvious is that in a criminal case federal and state government is in command, not the private company. Therefore, direction or control is in public prosecutor's hands. A corollary of this is that any relief granted inures to the State, i.e., fines, jail terms, etc. -- restitution to the victim being rarely awarded and enforced. Other problems, which may arise, include the danger that the trade secrets at issue will be publicly revealed during the course of the criminal action; that discovery of the victim company by the defendant may be overly comprehensive, because of broad rights constitutionally granted criminal defendants; that criminal actions are advanced on the court docket and may result in a stay of any parallel civil proceedings; and finally, if the intellectual property owner swings and misses in the criminal prosecution, the possibility exists such individual or company may face a retaliatory civil action by the defendant.

Although not the main line of defense for technology companies, criminal remedies have become increasingly important. The principal shield is still guarding secrets so they are not misappropriated in the first place; and failing this, civil suits seeking injunctions to prevent further distribution and monetary awards for damages suffered. However, because industrial espionage is often fully criminal conduct, as surely as a liquor store holdup, criminal remedies must be considered and probably need clarification and expansion to keep pace with the increasingly sophisticated industrial spy, now using computer intrusion, aerial surveillance, sophisticated listening devices and specialized cameras, as well as old fashion embezzlement, extortion, and bribery. The criminal law must continue to evolve to be sure current definitions, procedures and punishments fit the now all-too-common crime of theft of another's intellectual property. ■

Footnotes at page 27

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