



NPE-Savvy Intellectual Property Defense and Indemnity Provisions in Sales/License Agreements

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The NPE Problem - Background

(Before NPE Lawsuits Became Common Place)

- Old Manufacturer/Licensors Business Model
 - “Stand Behind Your Product”
 - UCC Art. 2, Sect. 312 provides a warranty against patent infringement in a sale of goods
 - In order to manage potential liability, Sellers/Licensors typically disclaim the UCC warranty and instead provide a substitute indemnification provision
 - Many Sellers/Licensors expanded the indemnification provision to also include defense of Buyer/Licensee in patent infringement
 - “Hold Harmless” provisions became common

The NPE Problem

- Common NPE Business Model
 - File infringement lawsuits against multiple End-User Business Entities in a single/multiple market segments
 - Goal 1: Reasonable royalties base would presumably be higher based on value to end user rather than a single lawsuit against the manufacturer/licensor
 - Goal 2: Attempt to obtain settlements at litigation cost levels or higher from multiple end user defendants
 - The resulting potential cumulative liability to a Manufacturer/Licensors standing behind its products with blanket defense, indemnification and hold harmless provisions for multiple buyers/licensees can prove very costly and can and have driven companies out of respective market segments

IP Defense and Indemnity Provisions

- Memorialize Seller/Licenser and Buyer/Licensee agreement regarding their respective rights and obligations if Buyer/Licensee is sued for IP infringement based on purchased/licensed item(s)
- May be used to apportion liability risk in Sales/License Agreements to a certain extent to address the NPE business model goals

IP Defense and Indemnity Provisions

- IP Defense and Indemnity Provision Should Set Forth:
 - a) Defense/Indemnity Triggering Terms
 - b) Scope of Defense and/or Indemnity
 - c) Geographic Limitations, if any
 - d) Exceptions and Exclusions
 - e) Remedial Measures, if any

Example IP Defense and Indemnity Provision

Seller will defend, indemnify and hold Buyer harmless against a third-party action, suit or proceeding (“Claim”) against Buyer to the extent such Claim is based upon an allegation that a Product, as of its delivery date under this Agreement, infringes a valid **United States patent, trademark or copyright or misappropriates a third party’s trade secret**

IP Defense and Indemnity Triggering Terms

- IP defense and Indemnity provision should clearly state terms for triggering Seller's/ Licensor's defense and/or indemnity obligation
- Exemplary triggering events include:
 - Filing of action, claim or proceeding,
 - Infringement allegation, e.g., receipt of cease-and-desist letter, or
 - Receipt of a letter offering patent license
- Typical Seller/Licensor Goal
 - Triggering event limited to filing of lawsuit
- Typical Buyer/Licensee Goal
 - Triggering event based on infringement allegations or offers to license

Defense and Indemnity - Separate Obligations

- Historically - certain industry segments only provided an indemnity obligation by Seller/ Licensor
- Within last decade or so – It is common place for Agreements to include indemnify and defense obligations to Buyer/Licensee at Seller's/Licensor's expense
- Hold harmless provisions are more common place and further increase Seller's/Licensor's exposure to liability

Defense and Indemnity Hold Harmless Provisions

- Seller/Licenser holding Buyer/Licensee harmless against IP infringement claims ensures that Buyer/Licensee is placed in the same position as if the infringement claim was not brought

Scope of IP Defense and Indemnity – Geographic Limitations

- Seller/Licenser should consider limiting its defense/indemnity obligation to country or countries in which the purchased/licensed item will be used
- For example, if Buyer/Licensee of your client's product that was procured in the U.S. ships that product overseas for use in its U.K. factory, then Seller/Licenser should not have to defend/indemnify against infringement actions arising in the U.K.

Defense and Indemnity - Limitations of Liability

- Limitations of Liability are often employed with hold harmless provisions to further apportion potential liability
- Common limitations of liability exclude:
 - Lost profits
 - Indirect damages
 - Incidental and Consequential Damages
 - Business Interruption Expenses
- Limitations of liability that set maximum cap on liability-even for IP Infringement claims-are often used in certain product/service markets

Scope of IP Defense and Indemnity – Exceptions to Liability

- Common Exceptions for excluding Seller's/Licensors' liability include infringement based on:
 - Products modified by someone other than Seller/Licensor
 - Products modified by Seller/Licensor in accordance with Buyer's/Licensee's specifications or instructions
 - Buyer's/Licensee's other products or third-party products
 - Combination Exclusion – Example:
 - Seller shall have no defense or indemnity obligation for a Seller furnished product that has been used with or in combined with hardware or software not furnished by Seller

Scope of IP Defense and Indemnity – Remedial Measure Provision

- Contracting Parties often explicitly enable substitution of non-infringing products that provide necessary functionality for Buyer/Licensee to mitigate the impact of infringement claims
- Example:
 - Seller, at its own expense and option may:
 - (1) procure for Buyer the right to continue use of the Product;
 - (2) replace the Product with a non-infringing product; or
 - (3) refund to Buyer a pro-rated portion of the applicable Fees for the Product based on a linear depreciation monthly over a (X) year useful life, in which case Buyer will return to Seller the Product and cease all use of it

Scope of IP Defense and Indemnity – Capped Liability/Reverse IP Defense and Indemnity

- Capping Liability, *e.g.*, for a fixed amount or value of goods sold or software/services licensed should be considered
- In addition to the IP defense and indemnity exceptions, Seller/Licensors should also consider obtaining a reverse defense and indemnity obligation from Buyer/Licensee

Coordinating IP Defense and Indemnity and Any IP Representations and Warranties

- Narrow IP defense and indemnity provisions can be undone by inclusion of broad IP representations and warranties against IP Infringement
- Prudent Sellers/Licensors often refuse provisions warranting against IP infringement, especially if IP defense and indemnity provisions are included
- If Buyers/Licensees insist on IP representations and warranties against IP infringement, then consider adding:
 - (i) a knowledge qualifier to that IP representation and warranty; and
 - (ii) a disclaimer that the sole remedy for breach of IP representations and warranties is provided under the IP indemnification provision

NPE-Savvy IP Defense and Indemnity Provisions

Thank You