

PRACTICE FOCUS

CONTRACT CLAUSES OFFER PROTECTION IN INFRINGEMENT SUITS

BY TONYA M. GRAY

When a general counsel finds her company a defendant in a patent infringement suit, a myriad of vendor contracts may be in play. Computer systems or software platforms often evolve in fits and spurts as technology advances. One vendor's software gets merged with another vendor's services. Employees develop certain functions, while third-party vendors provide others that may reside on another company's servers.

Many in-house attorneys facing a suit seek indemnification in these vendor contracts, which may provide a shield against expending the company's resources. But in patent litigation, the indemnification provision is not the only protection a contract can provide. The remaining contractual provisions can determine liability.

Want to help protect your company from future patent infringement claims? Take advantage of a number of prophylactic contract clauses that can help defeat them.

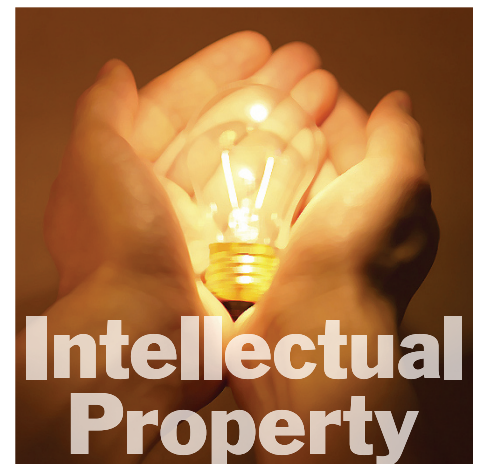
Liability in a patent infringement suit requires the company process accused in the suit to meet all the steps of the process claimed by the patent. A finding of direct infringement requires one actor — the direct infringer — to perform all those steps. Without a direct infringer, contributory infringement also cannot occur. When it takes multiple actors to complete all of the steps

claimed by the patent (known as joint infringement), liability exists only if there still is a direct infringer: one party that directs or controls the other necessary parties' actions. That is where vendor contracts come into play.

Although a company cannot avoid a finding of infringement simply by contracting out parts of a patented process to another entity, infringement likewise should not exist if it takes one company plus another to accomplish the invention claimed by the patent. In *BMC Resources Inc. v. Paymentech LP* (2007), the U.S. Court of Appeals for the Federal Circuit affirmed that if acts of multiple parties are required to perform each and every step of a patented process, direct infringement only exists if one party exercises "control or direction" over the others. There has to be a "mastermind."

A year after *BMC*, in *Muniauction Inc. v. Thomson Corp.*, the same court elaborated that "the control or direction standard is satisfied in situations where the law would traditionally hold the accused direct infringer vicariously liable for the acts committed by another." One significant factor in making that determination: the contracts.

Although the absence of a contract worked in the defendant's favor in *BMC*, it is unlikely that a GC's company will rely on another's provision of significant services or products without a



contract in place. Rather than avoid the benefits of contracts entirely, in-house lawyers should think about how the relationship with a vendor will work and what language contract drafters can employ to avoid future claims of joint infringement.

Courts agree that the mere existence of the contract is not sufficient to find direction or control by one party over another. Rather, they analyze the terms of the contract and specifically look for the presence or absence of clauses that dictate whether one company controls the other(s).

NO MASTERMIND

So how does the company attorney draft a contract so that no mastermind exists? First, the contract should reflect

that it is the result of an arm's length negotiation. The Federal Circuit has made clear that mere arm's length cooperation is insufficient to establish direction or control.

Second, is the contract an exclusive relationship, or does the vendor provide similar services or products to other businesses as well? If the latter, the contract should expressly state that the relationship is not exclusive. In a 2009 unpublished opinion by U.S. District Judge T. John Ward of the Eastern District of Texas finding no joint infringement, *Golden Hour Data Systems Inc. v. Emscharts Inc., et al.*, a key fact was that a distribution agreement between the alleged infringers was non-exclusive.

Third, the contract should include language establishing the vendor or software provider is an independent contractor, and specifically disclaim any agency relationship. The law of agency played a significant role in the *Muniauction* court's decision tying the direction-or-control standard to the vicarious liability test. Since then, in 2008's *Emtel v. Lipidlabs Inc.*, U.S. District Judge Lee H. Rosenthal of the Southern District of Texas further examined the agency issue in a case involving the provision of videoconferencing that allows physicians to communicate with medical caregivers in a remote facility. That an agency relationship did not exist between doctors and hospitals was noteworthy in the finding of no joint infringement.

Fourth, after the contract confirms there is no agency relationship, disavow the company's right to manage how the vendor's software works or how the vendor provides its services. The Federal Circuit, as well as the *Emtel* and *Golden Hour* courts, empha-



sized that a contracting party is not liable for the acts of an independent contractor unless it controls the details of the contractor's work to the point where the contractor cannot exercise independent judgment on how to perform its task.

Fifth, the contract should strike a balance between sufficiently describing the services (so the company lawyer knows what he is contracting for) and too much information (so he now knows every detail necessary to understand how that service works). A lack of knowledge as to how the other party provides its piece of the puzzle indicates a lack of control or direction, as found by U.S. District Judge Louis H. Pollak of the Eastern District of Pennsylvania in *Gammino v. Celco Partnership* (2007).

Sixth, make sure each party retains

the rights to its own property and limit how much access one party has to the other. It is difficult to direct or control a process if the company's access to it is limited or even non-existent.

Although avoiding patent infringement claims themselves likely is beyond a GC's control, she may be able to help her company avoid liability with proactive measures in vendor contracts for processes that require multiple players.

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