

LICENSING BEST PRACTICES

STRATEGIC, TERRITORIAL, AND TECHNOLOGY ISSUES

ROBERT GOLDSCHIEDER AND ALAN H. GORDON
EDITORS



JOHN WILEY & SONS, INC.

MANAGING INTELLECTUAL PROPERTY ALLOCATION IN JOINT VENTURES

BY RON LAURIE

INTRODUCTION

The term “joint venture” is commonly used to mean “an association of economically independent business entities . . . for a common commercial purpose of defined scope and duration, by contract or in the form of a new business entity, and by means of which the [v]enturers pool resources and share risks, rewards and control.”¹ Typically, each joint venturer contributes one or more unique attributes (e.g., technology, capital, management expertise, or product distribution and marketing) toward a shared common objective and acceptance of risk.² Other terms that are commonly used to describe joint ventures include “strategic alliance” and “partnership.”³

This chapter examines issues of intellectual property strategy for those joint ventures (*JVs*) in which the development or acquisition of intellectual property rights (*IPRs*) is contemplated. An analysis of the relevant considerations for forming, administering, and unwinding the intellectual property-related aspects of the *JV* is presented. The first section describes possible models for structuring the *JV*, the second and third sections describe possible models for allocating *IPRs* in subject matter developed by the *JV*, and the last section describes strategies for disposition of the intellectual property assets following unwinding of the joint venture.

JV STRUCTURAL MODELS

In negotiating a joint venture, the potential joint venturers often focus their attention on the future profitability of the joint venture, leaving it to their counsel to work out the form and structure that the *JV* should actually take. Thus, counsel must establish a dialogue with the client to ask questions such as: why the client wishes to form a joint venture; whether the client’s goals can be achieved

in other ways; what makes the other party or parties an attractive joint venturer; what rewards the client envisions; whether the parties' goals are compatible; and whether the parties, as business entities, are themselves compatible (i.e., in terms of business culture, background, experience, and organizational values).⁴ These preliminary determinations will assist counsel in advising the client on a suitable JV structural model, which in turn will inform the possible intellectual property allocation models for the subject matter arising out of the JV.

THE CONTRACTUAL MODEL. As the name suggests, under this model, the joint venturers establish and form the joint venture through a contractual agreement, as opposed to forming a separate legal entity such as a partnership, limited liability company, or corporation. The parties tend to prefer a contractual relationship when, instead of being continuous, the collaboration between the joint venturers will be of "narrow scope and finite duration."⁵ Generally, a purely contractual relationship is appropriate when the joint venturers' activities are sufficiently distinct (in either a technology or business sense) that they can simultaneously co-exist without harming each other. For example, in the technology sector, contractual JVs are commonly formed for purposes of early-stage (e.g., precommercialization) research & development or for late-stage (e.g., postproductization) co-marketing.⁶

From a general legal perspective, the specific and narrow objective of the contractual JV is likely to result in a more limited construction of any fiduciary duties⁷ among the joint venturers compared with those found in a partnership or corporation.⁸ In addition, a purely contractual JV offers the advantage of minimizing complex tax issues and avoiding the administrative burden of managing a separate entity.⁹

From an intellectual property perspective, the contractual model means that the joint venturers will each conduct their own activities in the JV's space. Depending on the contractual agreement, these activities may be restricted to mutually exclusive fields, they may be in partially overlapping fields, or they may be wholly unrestricted. Typically, there will be preexisting intellectual property relevant to the joint venturers' activities, and the agreement must provide for such intellectual property to be licensed from its owner to the other joint venturers in a defined field of use. Similarly, the joint venturers usually will create new intellectual property relevant to the JV's activities. The contractual agreement must vest ownership of such newly created intellectual property in one or more of the joint venturers, with appropriate licenses to the other joint venturers in defined fields of use. Such allocation and licensing will be addressed in greater detail in the next two main sections.

THE ENTITY MODEL. Under this model, the joint venturers create an independent corporate entity to conduct the JV's business pursuant to a joint venture agreement. Typical forms of the new JV entity include partnerships, limited liability companies (LLCs), or corporations. Multiple joint venturers may contribute intellectual property to the nascent JV entity or, alternatively, one joint

venturer may be the sole contributor of intellectual property while the other contributes operating capital, managerial know-how, or specific domain expertise. The joint venturers manage, participate in, and share the risks and returns of the JV entity by way of their respective equity ownership and/or pursuant to its specified corporate governance structure (e.g., an operating agreement in the case of an LLC).

Joint venturers tend to prefer a separate JV entity when their relationship is a multifaceted, long-term continuing business relationship. For example, in the technology sector, entity-based JVs are commonly formed for development of product lines wholly new to the joint venturers (although often based on combining or integrating preexisting technologies), or for commercializing new markets (e.g., foreign ventures).

From a general legal perspective, the new JV entity can take the form of either a corporation, partnership, or LLC. The corporate form offers the advantage of limiting liability of shareholders for the obligations of the enterprise but carries the disadvantage of double taxation of corporate profits at the corporate and shareholder levels.¹⁰ In contrast, under a partnership or LLC, profits are taxed only once at the partner or LLC member level, but general partners may have unlimited liability for obligations of the partnership.¹¹

From an intellectual property perspective, because the entity itself generally will conduct the JV's activities going forward, the entity provides a convenient place for any newly created intellectual property to be held. Of course, the joint venturers' preexisting intellectual property may have to be licensed to the entity, as needed. The joint venturers also will need to agree, in the JV agreement, whether and to what extent the JV entity is entitled to grant licenses to other parties (perhaps including the joint venturers themselves) in defined fields of use. Specifically, the joint venturers must determine whether the new JV entity is the exclusive vehicle for them to participate in the JV's market space.

Such exclusivity—plus appropriate restrictions against apportioning the JV entity's intellectual property back to the joint venturers upon dissolution of the JV entity—can deter a devious joint venturer from using the JV entity to develop technology that it could not develop on its own and then dissolving the JV in order to have the benefit of such intellectual property.

Conversely, if the joint venturers themselves are authorized to conduct parallel (or non-JV) activities using the JV-created intellectual property, the JV entity will need to grant appropriate licenses to the joint venturers in defined fields of use. In some extreme cases, the joint venturers may even structure the JV entity to conduct the JV business but may vest ownership of all intellectual property in the joint venturers themselves. This would, of course, require appropriate licenses from the joint venturers to the JV entity.

THE TWO-STAGE MODEL. Yet another possibility is a two-stage model, a hybrid of both the contractual and entity structural models. The first stage consists of the execution of the JV agreement followed in a second stage by the formation of the independent JV entity.

This model is significantly more complex, and thus less frequently used, than the purely contractual or entity-based models. It is, however, useful when the joint venturers wish to begin a limited (contractual) collaboration (e.g., to determine technical and commercial viability of a proposed new product or process), followed by the formation of a “NewCo” if and when such viability is demonstrated. For example, formation of NewCo could be conditioned on achieving certain technology development, productization, or financial milestones. If, on the other hand, the parties elect not to form NewCo, then the contractual JV terminates.

INTELLECTUAL PROPERTY ALLOCATION IN GENERAL

To operate the joint venture—whether under the contractual, entity-based, or two-stage model—the joint venturers and/or the JV entity will need to either own, or be licensed under, IPRs related to their respective business. The choice of ownership versus licensing depends on a variety of factors. One factor is whether the intellectual property arose independently of the JV (e.g., preexisting or created by one of the joint venturers outside the JV) or arose from operation of the JV. The former is often referred to as “Background Intellectual Property,” whereas the latter is often referred to as “Foreground Intellectual Property.”

Another factor is whether the JV is contractual, entity-based, or established pursuant to the two-stage model. If the JV is entity-based or follows from the two-stage model, the relevant intellectual property can be owned by the JV, owned by one or more of the joint venturers and licensed to the JV, or some combination of the foregoing. For example, Background Intellectual Property might be owned by its creator (one of the joint venturers) and licensed to the JV entity, or even assigned to the JV entity. Similarly, Foreground Intellectual Property (which in this instance would have been created by the JV entity) could be owned by the JV entity, or allocated to the joint venturers individually, who would then grant appropriate licenses to the JV entity. If the JV is contractually based, both the Foreground and Background Intellectual Property must be owned by one (or both) of the joint venturers and licensed to the other. Nevertheless, many other variations are also possible.

THE DEFAULT ALLOCATION PARADIGM: JOINT OWNERSHIP. When intellectual property is to be owned by the joint venturers themselves (under either the contractual, entity, or two-stage model), the most common form of allocation is some form of “joint ownership.” For example, Foreground Intellectual Property is often allocated as follows: intellectual property developed solely by one joint venturer is solely owned by that joint venturer, whereas intellectual property developed jointly by the joint venturers is owned jointly by those joint venturers. Indeed, even if the joint venturers fail to expressly allocate ownership under the contractual JV model, this type of allocation will arise under default law, because (at least in the United States) ownership initially vests with the creators of the subject matter in question.

Conflicting Rights under Default Laws. The default rights of joint owners (to exploit and/or to enforce) are governed by respective national laws applicable to the type of intellectual property asset in question.

THE RIGHT TO EXPLOIT

For example, consider U.S. patent rights. Absent an agreement to the contrary, the default rule is that each joint owner can exploit the patent without the permission of the other and without any duty to share royalties.¹² Furthermore, the joint owner's right to exploit includes the right to license third parties.¹³ The freedom to license without accounting enables a savvy prospective patent licensee to play the joint owners against one another other to maximize favorable deal terms for the licensee.

The situation becomes even more complicated when one is dealing with multiple types of intellectual property. For example, whereas U.S. patent law imposes no duty of accounting among exploiting joint owners,¹⁴ U.S. copyright law does impose such a duty.¹⁵

THE RIGHT TO ENFORCE

The counterpart of exploitation is enforcement and, here as well, joint ownership presents pitfalls for the unwary. Again taking U.S. patent law as an example, normally, each joint owner must join in a suit to enforce the patent against a third party. This requirement protects a defendant from defending against multiple suits on the same patent and protects an absent joint owner from a finding of invalidity or unenforceability that could negatively affect his or her rights. Consequently, any joint owner can block an offensive patent infringement action by refusing to join as a plaintiff.

Thus, joint owners of a U.S. patent find themselves in a situation in which each can freely license without obligation to the other, but each can prevent the other from suing an infringer by refusing to join the suit. In such a case, the rewards of licensing go to the joint owner, who either grants a license first or undercuts another joint owner's offer with a more favorable deal. It is no wonder that courts have characterized patent joint owners as being "at the mercy of each other."¹⁶

A nonlitigant joint owner can grant the defendant a license—even after initiation of the suit—which will cut off part or all of the relief the litigant joint owner may obtain by exercising its unilateral right to sue.¹⁷ Specifically, the grant of a nonexclusive license by the nonlitigant joint owner (even post suit) will prevent the litigant joint owner from obtaining injunctive relief and will also protect the defendant from liability for postgrant (but not pregrant) damages.¹⁸ However, if the nonlitigant joint owner grants the defendant an exclusive license (even post suit), the nonlitigant joint owner no longer can consent to join the suit as a joint owner of the patent, and the suit must be dismissed.¹⁹

INTERNATIONAL CONSIDERATIONS

Further complexity as to joint owners' rights ensues because different countries have different default laws. For example, consider the copyright joint ownership laws of three major industrialized countries: the United States, the United Kingdom, and Japan. Under U.S. law, joint owners of a copyright can freely exploit for

themselves. Under U.K. law, the joint owners cannot exploit for themselves without consent of the other joint owners.²⁰ Under Japanese law, the joint owners cannot exploit without consent, but such consent cannot be unreasonably withheld.²¹

Indeed, parties in different countries—looking at joint ownership through the prism of their individual national laws—may have entirely different expectations of what it means to be a joint owner. Based on the example above, American and British joint owners of a copyright might have had entirely different expectations regarding their individual rights to exploit. Some lawyers have been called to renegotiate joint ownership agreements when it became apparent, years after execution, that the joint owners had no meeting of the minds on their respective rights to exploit and enforce jointly developed subject matter.

Enforceability of Contractual Provisions

AGAINST THIRD PARTIES

The previous two sections demonstrate the considerable variation in the default rules for the different types of intellectual property, as well as under the different national laws. An astute joint owner therefore will negotiate provisions in the JV agreement setting forth, in detail, the joint owners' respective rights and obligations. For example, such provisions might include covenants regarding unilateral exploitation in particular fields, licensing of competitors, sharing of royalties, joining suits, and sharing of enforcement costs and proceeds. However, the effectiveness of these covenants remains uncertain as they may not always be enforceable.

Consider, for example, that the joint owners may have agreed not to exploit a jointly owned intellectual property asset unilaterally for the benefit of third parties. Such a covenant may be unenforceable against a third party who is held by a court to be a *bona fide* purchaser for value (*BFP*) from one of the joint owners.

AGAINST JOINT OWNERS THEMSELVES

Unlike the uncertainty surrounding restrictive contractual covenants with respect to third parties, such agreements should be enforceable against the joint owners themselves. For example, breach of a joint owner's covenant not to use for itself should be enforceable against that joint owner. However, this may not be the case in some situations.

For example, when a joint owner goes bankrupt, the bankruptcy court (or trustee) generally has the power either to assume or reject a contract held by the bankrupt party.²² If the court rejects the JV agreement, the nonbankrupt joint owner may lose the benefit of the contractual provisions restricting the activity of the bankrupt joint owner. Conversely, the court (or trustee) might assume the JV agreement but assign it to a third party (typically in connection with a sale of the joint ownership interest). In this scenario, the bankrupt joint owner would effectively be divested of its joint ownership rights and those rights would vest in a new joint owner (i.e., the third party)—perhaps even a competitor.

Recommendations. Joint ownership is fraught with pitfalls and should be avoided wherever possible. However, joint ownership may sometimes be unavoidable. For

example, one joint venturer may oppose the formation of the joint venture on any other terms. In such a situation, the joint venturers must think through all issues and carefully provide for all contingencies. The joint owners cannot simply rely on default rules because, as discussed above, the rights to exploit and enforce vary with the type of intellectual property and applicable national laws. Such variation makes it impossible for the joint owners to effect an integrated and consistent plan for development, use, and distribution of the subject matter covered by the jointly owned intellectual property. Instead, the joint venturers should use the JV contract or NewCo formation agreement to override the hodgepodge of inconsistent default laws by clearly delineating all the rights and responsibilities of the joint owners.

There are many possible alternatives to joint ownership, all of which involve some form of allocating intellectual property ownership to individual parties (whether the joint venturers or the JV entity), who would then grant appropriate licenses to other parties as needed. The next section explores some of these allocation options.

PREFERRED INTELLECTUAL PROPERTY ALLOCATION STRATEGIES. *Intellectual Property Ownership: Background, Non-Derivative Foreground, and Derivative Foreground Intellectual Property.* To allocate ownership of intellectual property properly under the preferred approach, the first step is to classify the intellectual property based on its nature. Indeed, the election of a JV structural model and an associated allocation strategy are interdependent and, in turn, the allocation strategy is contingent on whether the intellectual property asset represents Background, Non-Derivative Foreground, or Derivative Foreground technology.

Background intellectual property includes such property both in technology developed by the joint venturers prior to the formation of the JV (Preexisting Background Intellectual Property) and in technology developed during the existence of the JV, but not pursuant to it (New Background Intellectual Property). Specifically, Preexisting Background Intellectual Property comprises intellectual property in technology created by each joint venturer prior to JV formation, which is necessary or useful in conducting the business of the contemplated joint venture or required to commercially exploit the Foreground Intellectual Property (as defined below). New Background Intellectual Property also constitutes such property in technology necessary or useful in conducting the business of the JV or required to exploit the Foreground Intellectual Property commercially, but the difference lies in its development taking place during the JV and yet not pursuant to the JV development activity. The concept of New Background Intellectual Property becomes more relevant when one or more joint venturers is a large enterprise having multiple groups working on similar developments.

In contrast, Foreground Intellectual Property is that associated with technology developed pursuant to the JV by the joint venturers, either individually or jointly, and in furtherance of the purpose of the JV. Finally, Derivative Foreground Intellectual Property is a subset of Foreground Intellectual Property comprising that developed pursuant to the JV that extends the core technology of one (and only one) joint venturer.

Optimizing Rights to Use of the Non-Intellectual Property Owning Joint Venturers

LICENSES: EXCLUSIVITY, FIELD OF USE, AND ROYALTIES

Once intellectual property ownership is allocated, the rights of the other (non-owning) parties to use such property are defined under appropriate license provisions. These licenses include licenses among joint venturers, from a joint venturer to the new JV entity (*NewCo*) if applicable, or from *NewCo* to the joint venturers. In this respect, many combinations of licensing parameters are possible, and the joint venturers should decide at the outset, which is suitable to their relationship. These licensing parameters include, e.g., whether the license is exclusive or nonexclusive, whether it is limited to a specific field of use, and whether it is royalty bearing or royalty free. The parameters are used in various combinations to prescribe (i.e., enable and/or restrict) permissible competitive use of the Background and Foreground Intellectual Property by the joint venturers and *NewCo* with respect to one another.

NON-COMPETITION COVENANTS

Non-competition covenants are a useful adjunct to intellectual property licenses in terms of restricting competitive activity among the joint venturers on the one hand, and between the joint venturers and *NewCo* on the other. Non-competition covenants can be both more restrictive and less restrictive than intellectual property licenses. They are less restrictive because they typically have a shorter term. Thus, whereas the licenses may extend during the existence of the JV (and possibly beyond), non-competition covenants are typically for a much shorter term, e.g., several years. They are more restrictive because they extend beyond use of the licensed intellectual property by proscribing all competitive activity within a defined field. The scope of the non-compete is usually co-extensive with the area outside any field-limited licenses.

APPLICATION OF INTELLECTUAL PROPERTY ALLOCATION STRATEGIES TO THE JV STRUCTURAL MODELS

Intellectual property allocation represents one of the most significant challenges facing the joint venturers. The allocation tools, discussed previously, are used to give each joint venturer and *NewCo* (if applicable) the rights needed to ensure the success of the venture while preserving competitive relationships among the joint venturers. Ultimately, when negotiating the JV agreement, the joint venturers must allocate ownership and rights of the nonowning joint venturers in a manner suitable to their relationship and objectives. Thus, this section presents exemplary intellectual property allocation maps under the different JV models, rather than suggesting a rigid allocation paradigm applicable in all cases.

THE CONTRACTUAL MODEL. Ownership of Background Intellectual Property generally remains with the developing joint venturer (see Exhibit 15.1). The joint venturers will then grant one another nonexclusive licenses to their Pre-existing Background Intellectual Property within a field of use determined by

When Created	What		Who	Ownership	Licenses (typically royalty free)
Pre-JV	Preexisting Background IP		Individually developed	Developing joint venturer	Nonexclusive to the other joint venturer(s) within the JV field of use (FofU)
During JV	New Background IP		Individually developed	Developing joint venturer	Nonexclusive to the other joint venturer(s) within the JV FofU.
	Foreground IP	Derivative IP wholly derived from only one joint venturer's Background IP	Individually or jointly developed	Whichever joint venturer owns the underlying Background IP	Nonexclusive license to other joint venturer(s) (could be FofU limited)
		Non-Derivative Any other Foreground IP	Individually or jointly developed	One joint venturer only; to be negotiated in advance Could be "blanket" allocation of ownership (i.e., always to one joint venturer) or by predefined area of technology	Exclusive license to other joint venturer(s) in agreed FofU

EXHIBIT 15.1 CONTRACTUAL JV MODEL: EXEMPLARY INTELLECTUAL PROPERTY ALLOCATION MAP

the objectives of the JV. New Background Intellectual Property is treated in a similar fashion (if it is to be licensed at all).

Ownership of the Derivative Foreground Intellectual Property created during the term of the JV, whether individually or jointly developed, will vest in the joint venturer whose core technology (and intellectual property) is extended. The other joint venturers will have nonexclusive licenses under the Derivative Foreground Intellectual Property, possibly limited to fields of use corresponding to their non-JV-related businesses.

Allocation of ownership of the Non-Derivative Foreground Intellectual Property will take the form of either: (1) a predetermined or "blanket" allocation to one joint venturer; or (2) an ongoing allocation among the joint venturers based on predefined areas of technology. Under either ownership allocation method, the nonowning joint venturers will have an exclusive license within carefully defined and preferably nonoverlapping fields of use. If the parties cannot agree on nonoverlapping fields of use, they should consider adopting an entity-based

JV that would own the Non-Derivative Foreground Intellectual Property or, as a last resort, revert to the joint ownership paradigm for ownership of the Non-Derivative Foreground Intellectual Property, and carefully define their respective rights and restrictions with regard to exploitation and enforcement.

“Blanket” allocation typically is feasible when the relationship between the joint venturers is one of nonequals, namely, the joint venturer who is to own the Non-Derivative Foreground Intellectual Property enjoys significant leverage in the transaction (i.e., is the larger joint venturer or contributes more capital or core technology). Also, it is critical to establish this allocation early in the JV formation process. The business principals and counsel for the dominant joint venturer must drive the negotiations to impress on the other joint venturer(s) that the relationship is one of developers and not collaborators. From a legal perspective, because the joint venturers will be deemed joint inventors of any jointly developed subject matter under the default rules of ownership, the JV agreement should contain an affirmative assignment of the other parties’ right, title, and interest in any such jointly developed material to the intended sole owner. This allocation presents the cleanest solution to complex transactions or when three or more joint venturers are involved. This allocation is also favored in the case of a long-term relationship involving many product development teams and life cycles and in the case of complicated technology development interrelationships.

Ongoing allocation by predefined area of technology is preferred when the contemplated transaction is well defined with respect to the joint venturers’ business and the time frame and process of the intellectual property to be developed.

THE ENTITY MODEL. As in the case of the contractual model, the first step comprises providing NewCo with access to the joint venturers’ Background Intellectual Property (see Exhibit 15.2). Ownership of Preexisting Background and New Background Intellectual Property remains with the developing joint venturer. Preexisting Background Intellectual Property is preferably licensed to NewCo exclusively in its field of use to prevent the developing joint venturer and the other joint venturers from using their Background Intellectual Property to compete with the JV, thereby maximizing the likelihood that NewCo will be successful. Alternatively, such licenses could be nonexclusive. New Background Intellectual Property is preferably licensed to NewCo nonexclusively in its field of use when the intellectual property is developed by another business unit of the developing joint venturer that needs to continue to use the intellectual property. Alternatively, such licenses could be exclusive when such continued use is unnecessary or the developing joint venturer is willing to consolidate all activities involving the intellectual property in NewCo. In this case, the developing joint venturer could even assign the New Background Intellectual Property (and perhaps also the Preexisting Background Intellectual Property) to NewCo, with a grantback license outside NewCo’s field of use. The Background licenses to NewCo are typically royalty free.

When Created	What	Who	Ownership	Licenses (typically royalty-free)	
Pre-JV	Preexisting Background IP	Individually developed	Developing joint venturer or NewCo	Exclusive for NewCo in FofU (could be nonexclusive) Nonexclusive grantback outside NewCo's FofU	
During JV (NewCo)	New Background IP	Individually developed	Developing joint venturer or NewCo	Nonexclusive for NewCo in FofU to prevent joint venturers from competing with the JV (could be exclusive) Nonexclusive (could be exclusive) grantback outside NewCo's FofU	
	Foreground IP	Derivative IP wholly derived from only one joint venturer's Background IP	Individual joint venturer, multiple joint venturers, or NewCo	Whichever joint venturer owns the underlying background IP	Nonexclusive to NewCo in FofU
			NewCo	Exclusive to joint venturer who owns the underlying IP outside NewCo's FofU (possibly with further restrictions)	
Non-Derivative Any other Foreground IP	Individual joint venturer, multiple joint venturers, or NewCo	NewCo	Exclusive/ nonexclusive to joint venturer(s) in defined field(s) of use (could be royalty free or royalty bearing)		

EXHIBIT 15.2 ENTITY/NEWCO JV MODEL: EXEMPLARY INTELLECTUAL PROPERTY ALLOCATION MAP

Derivative Foreground Intellectual Property may be developed by a single or multiple joint venturers, or by NewCo itself. Ownership will vest in the joint venturer whose core technology is extended by the Derivative Foreground Intellectual Property, or in NewCo. Under this option, NewCo will be granted a non-exclusive license to the Derivative Foreground Intellectual Property in its field

of use. Alternatively, if NewCo owns the Derivative Foreground Intellectual Property outright, the joint venturer owning the underlying intellectual property will be granted an exclusive license outside NewCo's field of use. Under either option, the other joint venturers should not be licensed under such Derivative Foreground Intellectual Property, especially when they are competitors of the joint venturer owning the underlying intellectual property. Here as elsewhere, exclusivity and field of use limitations (possibly supplemented with appropriate non-competes) serve to regulate competition among the joint venturers and between the individual joint venturers and NewCo.

Non-Derivative Foreground Intellectual Property, whether developed by a single joint venturer or multiple joint venturers or by NewCo, will be owned by NewCo, and all joint venturers will be licensed under such intellectual property. The licenses may be exclusive or nonexclusive and will be limited to carefully defined fields of use, in effect shielding NewCo from the joint venturers' development of competing technology to the Non-Derivative Foreground Intellectual Property. Also, such fields of use are often mutually exclusive as between the individual joint venturers. Vesting ownership of the Foreground Intellectual Property in NewCo and granting only nonexclusive licenses to the joint venturers allows NewCo to also license third parties. The joint venturers must decide whether any licenses granted by NewCo should be royalty free or royalty bearing. Here, arguments exist for both types of licenses. On the one hand, NewCo should be able to generate revenue from Non-Derivative Foreground Intellectual Property, and thus these licenses should be royalty bearing. On the other hand, the joint venturers bore the risk in forming NewCo and thus should be rewarded with royalty-free licenses, in contrast to third parties, whose licenses (if any) should be royalty bearing.

Generally, intellectual property allocation under the entity model favors the sharing of each joint venturer's core technology or "crown jewels" with the newly formed JV entity while at the same time shielding the related intellectual property from the other joint venturers. Moreover, this allocation facilitates NewCo's licensing of Foreground Intellectual Property and enforcement of rights against third parties.

THE TWO-STAGE MODEL. The two-stage model contemplates an initial (sometimes called "interim") contractual joint development phase, followed by the formation of an independent JV entity (i.e., NewCo) in which the joint venturers would participate as equity owners. The contractual phase is used to allow preliminary collaboration while conducting technical and/or commercial feasibility studies. If feasibility is demonstrated, the contractual phase is terminated in favor of NewCo formation. If feasibility is not demonstrated, the contractual phase is terminated and the JV does not proceed any further.

As usual, there will be pre-JV intellectual property that has to be licensed to the JV (contractual and/or NewCo). This is addressed in Exhibit 15.3.

When Created	What	Who	Ownership	Licenses (typically royalty free)
Pre-JV	Preexisting Background IP	Individually developed	Developing joint venturer (If any NewCo FofU-specific IP in Background, consider assignment to NewCo if/when formed)	Limited (nonexclusive) FofU cross-licenses among all joint venturers for use incident to JDP duties; terminates upon conclusion of JDP or if NewCo is not formed Upon NewCo formation, nonexclusive FofU license to NewCo (or exclusive FofU to support non-compete); no license to other joint venturer(s) NewCo may sublicense its rights only to second-source manufacturers

EXHIBIT 15.3 TWO-STAGE JV MODEL: EXEMPLARY INTELLECTUAL PROPERTY ALLOCATION MAP, PRE-NEWCO

Pre-JV. Preexisting Background Intellectual Property, developed and owned by one joint venturer prior to JV formation, will be licensed: (1) to the other joint venturers for limited use during the contractual phase of the JV; and (2) to NewCo in its field of use thereafter. Typically, the licenses to the individual joint venturers would be nonexclusive and terminate upon conclusion of the contractual joint development phase (whether NewCo is formed or not). Typically, the licenses to NewCo would be nonexclusive in NewCo’s field of use. Alternatively, these licenses could be exclusive in NewCo’s field of use to ensure that the licensor-joint venturer will not compete with NewCo.

Joint Development (Contractual) Phase. New Background Intellectual Property would be owned by the joint venturer that developed it. Derivative Foreground Intellectual Property would be owned by the joint venturer whose underlying intellectual property was extended. In either case, such a joint venturer would license other joint venturers (in the contractual phase) and NewCo (in the entity phase) in a similar manner as Preexisting Background Intellectual Property previously discussed.

Ownership of the Non-Derivative Foreground Intellectual Property will vest initially in the developing joint venturer(s) with subsequent assignment to NewCo upon formation (see Exhibit 15.4). Pending NewCo formation, all joint venturers will be cross-licensed for use incident to their duties relating to the contractual joint development phase. These licenses will terminate upon conclusion of that phase (whether NewCo is formed or not).

Additionally, if NewCo is never formed, ownership of the Foreground Intellectual Property will remain with the developing joint venturer(s), possibly with

When Created	What	Who	Ownership	Licenses (typically royalty-free)
Joint Development Phase (JDP)	New Background IP	Individually developed	Developing joint venturer	Limited (nonexclusive) FofU cross-licenses among all joint venturers for use incident to JDP duties; terminates upon conclusion of JDP or if NewCo is not formed Upon NewCo formation, nonexclusive FofU license to NewCo (or exclusive FofU to support non-compete); no license to other joint venturer(s) NewCo may sublicense its rights only to second-source manufacturers
	Derivative Foreground IP	Individually or jointly developed	Joint venturer whose core technology is extended (Does a joint venturer who fails to enter into the NewCo formation agreement forfeit ownership?)	Limited (nonexclusive) FofU cross-licenses among all joint venturers for use incident to JDP duties; terminates upon conclusion of JDP or if NewCo is not formed Upon NewCo formation, nonexclusive FofU license to NewCo (or exclusive FofU to support non-compete); no license to other joint venturers NewCo may sublicense its rights only to second-source manufacturers
	Non-Derivative Foreground IP	Individually or jointly developed	Developing joint venturer(s), but assigned to NewCo upon NewCo formation If NewCo is not formed, ownership remains with developing joint venturer(s), but with prohibition on use for X years	Limited (could be exclusive) cross-licenses between all joint venturers for use incident to JDP duties; terminates upon conclusion of JDP or if NewCo is not formed Upon NewCo formation, nonexclusive license back to developing joint venturer or joint venturers outside of NewCo's FofU (or exclusive within their Primary Business FofU [could be nonoverlapping and non-NewCo]); developing joint venturer who fails to enter into Definitive Agreements forfeits this license

EXHIBIT 15.4 TWO-STAGE JV MODEL: EXEMPLARY INTELLECTUAL PROPERTY ALLOCATION MAP, JOINT DEVELOPMENT PHASE

a prohibition on use for a specified number of years (to give an incentive for formation of NewCo).

NewCo (Entity) Phase. New Background Intellectual Property created post NewCo formation would be owned by the developing joint venturer and licensed nonexclusively to NewCo in its field of use (see Exhibit 15.5). Alternatively, NewCo’s license could be exclusive. NewCo may also be granted a right to sublicense, limited to second-source manufacturers. Nonowning joint venturers will have no rights to the owning joint venturer’s New Background Intellectual Property.

Derivative Foreground Intellectual Property may have been created by NewCo or by one or more of the joint venturers. Such Derivative Foreground Intellectual Property typically will be owned by the joint venturer whose core technology is extended or, in some cases, by NewCo. When ownership of the Derivative Foreground Intellectual Property vests in the joint venturer, NewCo will have a nonexclusive royalty-free license in its field of use. In contrast, when

When Created	What	Who	Ownership	Licenses (typically royalty free)
NewCo Phase	New Background IP	Individually developed	Developing joint venturer	No license to other joint venturers; nonexclusive FofU license to NewCo (or exclusive FofU to support non-compete) NewCo may sublicense its rights only to second-source manufacturers
	Derivative Foreground IP	Individually or jointly developed, or NewCo developed	Joint venturer whose core technology is extended or NewCo	Nonexclusive royalty-free FofU license to NewCo; no license to other joint venturers Exclusive within FofU of joint venturer whose core technology is extended (could be in all areas outside of NewCo FofU)
	Non-Derivative Foreground IP	Individually or jointly developed, or NewCo developed	NewCo	Nonexclusive royalty-free FofU license to joint venturers or Exclusive within FofU of joint venturer whose core technology is extended (could be in all areas outside of NewCo FofU)

EXHIBIT 15.5 TWO-STAGE JV MODEL: EXEMPLARY INTELLECTUAL PROPERTY ALLOCATION MAP, POST NEWCO FORMATION

ownership vests in NewCo, the joint venturer owning the underlying technology will have an exclusive license within its primary business field of use, or in all areas outside NewCo's field of use.

Non-Derivative Foreground Intellectual Property may also have been created by NewCo or by one or more of the joint venturers. In any event, such property will typically be owned by NewCo with nonexclusive royalty-free licenses to the joint venturers outside NewCo's field of use. Alternatively, these licenses could be exclusive within each joint venturer's field of use, provided there is no overlap between the joint venturers' respective fields (or with NewCo's field). Finally, the licenses from NewCo to the joint venturers could be royalty bearing.

EXIT STRATEGIES

This section examines disposition of the intellectual property assets under different exit strategies available for the unwinding of the joint venture business. Possible exit strategies include merger or acquisition, dissolution, and bankruptcy. The intellectual property assets of concern include owned intellectual property (e.g., patents, trademarks, and copyrights for which the JV itself is the registered owner, and trade secrets) and licensed-in intellectual property (e.g., inbound intellectual property licenses from the joint venturers and from third parties).

For convenience, the disposition of these assets will be discussed in the context of a separate JV entity, although many of the concepts will be equally applicable to rights held by an individual joint venturer for the benefit of itself and its partners in the joint venture.

MERGER OR ACQUISITION OF THE JV ENTITY. If the joint venturers wish to allow for the possibility of merger or acquisition of the independent JV entity, they should negotiate appropriate provisions at the time of forming the JV entity. For example, all inbound licenses should be negotiated and drafted so that they are freely transferable to a potential acquirer of the JV business (i.e., without requiring consent by the licensor).

On the other hand, a joint venturer might wish to be protected in the event the JV is acquired by a competitor, for example, by a provision automatically terminating any inbound license from such joint venturer upon a change of control of the JV to a competitor of the minority joint venturer. These competitors may be expressly identified or not. If the license is not terminated, its scope can be "frozen," limiting it to the portion of the acquirer's business represented by the JV before the acquisition. These provisions ensure that, after the acquisition of the JV entity by a competitor of a joint venturer, any inbound licenses from such a joint venturer to the JV entity do not accrue (or only accrue in a limited way) to the benefit of the competitor.

DISSOLUTION OF THE JV ENTITY. Dissolution of the JV entity as an exit strategy must be analyzed in terms of three distinct considerations: intellectual property owned by the JV entity, that licensed from third parties, and that licensed from the joint venturers.

Intellectual Property Owned by the JV Entity. Analysis of the disposition of the owned intellectual property must be further divided into two competing objectives: protecting the joint venturers' right to use such property and preventing the joint venturers' continued right to use it.

When the joint venturers wish to continue to make use of the intellectual property owned by the JV following its dissolution, assignment of the intellectual property to the joint venturers as joint owners should be avoided because doing so raises the problems of joint ownership already discussed. Instead, ownership of these assets should vest in one joint venturer with grantback licenses flowing to the other former joint venturers. Alternatively, the joint venturers can choose to maintain the JV solely as an intellectual property holding company (i.e., a shell company) in which the joint venturers in turn have a license under the intellectual property. The latter alternative, establishing a holding company, is especially advantageous for enforcing the joint venture's IPRs against third parties and for the further licensing of the intellectual property to third parties if so desired by the joint venturers. In either case, the scope of any licenses to the former joint venturers (e.g., term of the license grant, exclusivity provision, right to sublicense, field of use, royalty payment, and so on) should be negotiated at the time of forming the JV entity.

Another option is to structure the JV agreement to prohibit grantback licenses. This has the benefit of discouraging dissolution of the JV in the first instance. However, there is a risk that the intellectual property assets will be wasted unless a third-party buyer can be found. Alternatively, the JV agreement could provide that a specified joint venturer has the right to buy out the other joint venturers upon dissolution of the JV and thus to gain sole ownership of the owned intellectual property. The proceeds from the owned intellectual property will be distributed to the joint venturers in accordance with their original equity stakes in the JV.

Inbound Licenses from Third Parties. Inbound licenses from third parties represent an asset of the JV just like the owned intellectual property and thus will be treated in a similar manner. Issues relating to the inbound licenses, such as their transferability, divisibility, and sublicensing, should be specified at the time these licenses are negotiated.

Inbound Licenses from Joint Venturers. Joint venturers' inbound licenses typically cover Background Intellectual property of the joint venturers closely related to their individual fields of business. Thus, upon dissolution, these licenses usually revert back to the granting joint venturer. However, in some instances, the licensor subsequently may grant equivalent field-of-use licenses to the other former joint venturers under separate license agreements. Again, these options should be contemplated at the time of JV formation.

Outbound Licenses from the JV Entity. The JV also may have granted licenses to third parties (i.e., outbound licenses). Upon dissolution, such licenses can either be: (1) left with the JV to be disposed of as part of the corporate

unwinding process; or (2) transferred to an entity that obtains ownership of the underlying (intellectual property, technological and/or human) assets related to the subject matter of the license. If the license is a “naked” license that includes no obligations on the part of the licensor (i.e., the JV), then option (1) is acceptable. However, if the license imposes any such obligations (e.g., support, updates, maintenance, further development, and so on), then choice (2) is appropriate (and the licensee will so insist).

CONCLUSIONS

Intellectual property allocation represents one of the most important strategic assessments when one is considering a joint venture and should be addressed in the JV agreement itself at the time of formation. Preferably, the joint venturers are advised to avoid joint ownership of the developed intellectual property in favor of one of the alternate allocation models described in this chapter or otherwise. In these alternative models, ownership of each distinct intellectual property asset is granted to an individual party (e.g., joint venturer or the JV entity), with appropriate licenses to other parties as needed. It is also important to plan in advance for possible dissolution of the JV, so that ownership and rights to use the JV’s intellectual property assets are appropriately distributed among the former joint venturers.

Endnotes

1. Ron Ben-Yehuda, “Joint Ventures,” in *Structuring, Negotiating & Implementing Strategic Alliances*. (Practising Law Institute, 2001), 247, 249.
2. Thomas H. Kennedy, “Joint Ventures,” “Joint Ventures,” in *Structuring, Negotiating & Implementing Strategic Alliances*. (Practising Law Institute, 2001), 215, 217–218.
3. “Partnership” in the business sense and not necessarily in the strict legal sense.
4. Ben-Yehuda, N. 1 *supra*, 252.
5. Kennedy, “Joint Ventures,” 219–220.
6. Ben-Yehuda, “Joint Ventures,” 250.
7. *Universal Studios, Inc. v. Viacom, Inc.*, 705 A.2d 579, 593-95 (Del. Ch. 1997) (holding that joint venturers owe fiduciary duties to one another and that the successor party to the original joint venturer assumed and subsequently breached the fiduciary duties owed to the plaintiff second joint venturer by retaining its preexisting cable networks in contravention of the non-compete provision in the joint venture agreement.)
8. Kennedy, “Joint Ventures,” 220.
9. *Ibid.*
10. *Ibid.*
11. *Ibid.*, 221.
12. 35 U.S.C. § 262 (1996).
13. In *Ethicon, Inc. v. United States Surgical Corp.* Although both inventors, Yoon and Choi, contributed to some or all of the claims in the patent at issue, only Yoon was named as an inventor. Ethicon, the assignee of Yoon, sued U.S. Surgical for infringement under the patent. U.S. Surgical identified Choi as unnamed joint inventor and negotiated a license from him. Ethicon subsequently challenged the validity of U.S.

Surgical's license; however, the Court of Appeals for the Federal Circuit upheld its validity because Choi, as a joint inventor, was a joint owner of the patent and could freely license his rights to a third party. 135 F.3d 1456, 1466 (Fed. Cir. 1998). This case highlights the risk that a contributor to any claim of a patent is a joint owner of the entire patent and can lawfully license that patent to third parties.

14. 35 U.S.C. § 262.
15. *Shapiro, Bernstein & Co. v. Jerry Vogel Music Co.*, 221 F.2d 569, 571 (2d Cir. 1955).
16. See, e.g., *Willingham v. Star Cutter Co.*, 555 F.2d 1340, 1344 (6th Cir. 1977).
17. *Schering Corp. v. Zeneca, Inc.*, 104 F.3d 341 (Fed. Cir. 1997).
18. *Ibid.*, 345.
19. *Ethicon, Inc. v. United States Surgical Corp.*, 135 F.3d 1456.
20. Information courtesy of U.K. attorney Alastair Breward, Esq., of Taylor Wessing.
21. Information courtesy of Japanese attorney Yoshikazu Tani, Esq., of Tani and Abe.
22. 11 U.S.C. § 365(f).

ABOUT THE AUTHOR

RON LAURIE is the Managing Director for Inflexion Point Strategy, an intellectual property investment bank that provides clients with a seamless integration of domain expertise in business, technology, and intellectual property rights. Mr. Laurie has worked in Silicon Valley for more than 40 years, first as a software engineer and then as one of the nation's top intellectual property lawyers. As an attorney, he has advised computer, communications, semiconductor, media, and financial services companies on intellectual property strategy—a subject he taught at Stanford and University of California at Berkeley Law Schools—with a focus on the strategic use of intellectual property assets in complex business transactions. He was a founding partner of the Silicon Valley offices of Skadden Arps and Weil Gotshal and led intellectual property teams in some of the largest technology deals in history, worth over U.S. \$50 billion. He has been listed in virtually every peer review survey of leading intellectual property lawyers, including Top 25 California IP Lawyers, Best Lawyers in America, America's Leading Business Lawyers, Global Counsel 3000, and International Who's Who of Business Lawyers.