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STUDENT COMMENTS

PACKAGE LICENSING AND POST-EXPIRATION ROYALTIES: THE RISK OF MISUSE

In order to survive, the system of free enterprise has required constant limitations of private concentrations of economic power. To foster the system of free competition the antitrust laws generally prohibit monopolistic forms of enterprise. The Constitution, however, declares, "The Congress shall have 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. . . ."¹ In furtherance of the design stated in the Constitution, the patent and copyright laws have authorized monopoly or restraint of trade in limited instances. A patent confers upon the patentee the exclusive right to prevent others from making, using or selling the invention covered by the patent for a term of 17 years.² This right to the invention becomes public when the 17-year period expires. Thus, the patent laws constitute an exception to the broad public policy of free competition. The patent is a privilege "conditioned by a public purpose"³—the encouragement of invention. The patent system, furthermore, has a built-in ambivalence in that the policy of rewarding the inventor by grant of an exclusive right is both limited and inhibited by a fundamental policy opposing any restriction on free competition. Accordingly, in most of its decisions since 1937 the Supreme Court has been influenced more by its fear of extending the patent monopoly than by a desire to reward the inventor.⁴

The "public policy which includes inventions within the granted monopoly excludes from it all that is not embraced in the invention."⁵ As a result of attempts by patent holders to secure monopolies broader than those lawfully granted by the Patent Office, the doctrine of patent misuse developed. The misuse doctrine denies relief to patent holders who attempt to extend the patent beyond the scope of the lawful grant. For example, a patentee bringing an infringement action may fail to gain any judicial relief because "courts, and especially courts of equity, may appropriately withhold their aid where the plaintiff is using the right asserted contrary to the public interest."⁶ Cessation of the misuse restores the right to injunctive relief and

¹ U.S. Const. art. I, § 8.

² Patent Code of 1952, § 154, 35 U.S.C. § 154 (1964).

³ *Mercoird Corp. v. Mid-Continent Inv. Co.*, 320 U.S. 661, 666 (1944).

⁴ See Williams, *Conflicting Landmark Decisions on Restrictive Patent Licenses; Package Patent Licensing and Acquisitions*, 10 *Antitrust Bull.* 295, 307, (1965).

⁵ *Morton Salt Co. v. G.S. Suppiger Co.*, 314 U.S. 488, 492 (1942).

⁶ *Id.* at 492. The equitable defense of "unclean hands" is normally applied to situations where the plaintiff has acted unjustly in the transaction of which he complains. The misuse doctrine is broader in that it may be applicable regardless of whether the particular defendant has suffered from the patent misuse. If the plaintiff's conduct has harmed the public interest (and even if it does not amount to a violation of the antitrust laws), this is sufficient basis to establish the affirmative defense of misuse. See 314 U.S. 488 at 492-94

damages for infringement occurring after the plaintiff has purged himself of the misuse.⁷

Agreements involving package licensing or post-expiration royalties, two types of patent business practice to be discussed in this comment, often give rise to the use of a patent misuse defense. It is the purpose of this comment to define the misuse doctrine in the interrelated areas of package licensing and post-expiration royalties by attempting to clarify the existing case law. Once the case law is understood, those practices which will create the risk of misuse become apparent.

I. PACKAGE LICENSING OF PATENTS

The patentee may grant to others the right to make, use and sell under his patent.⁸ Such grants are effected through licensing agreements which exact royalties for the rights transferred. Licensors often choose to include more than one patent in agreements. This practice, known as package licensing, characteristically involves the licensing of a group of patents for a specific period of time in consideration for payment of a uniform or non-diminishing royalty independent of the number of patents actually used or remaining unexpired. Package licensing agreements are desirable in that they often avoid "troublesome questions of infringement, complex bookkeeping, the difficulty of determining which patents cover the present and future needs of the licensee, cost differences, and similar practical considerations."⁹

This practice obviously lends itself to the potential misuse of forcing a licensee to accept unwanted patents in order to get a desired patent or patents. Conditioning the sale or lease of one commodity on the sale or lease of another, a practice known as a tying agreement or a tie-in, is considered a trade restraining device.¹⁰ Tying clauses in patent licenses generally compel the licensee to purchase unpatented or patented articles not within the scope of the licensed patent.

Since 1917 it has been established by the courts that tying the sale of a second product to a patented product is illegal.¹¹ The theory is that the tying is harmful because it creates a new monopoly wholly outside that granted by the patent. The tie-in, in addition, involves a direct restraint of trade in that it limits the choice of the licensee in his use and purchase of

(1942). See also *United States Gypsum Co. v. Nat'l Gypsum Co.*, 352 U.S. 457, 465 (1957); *Keystone Driller Co. v. General Excavator Co.*, 290 U.S. 240, 245 (1933).

⁷ For a comprehensive discussion of the misuse doctrine see Nicoson, *Misuse of the Misuse Doctrine in Infringement Suits*, 9 U.C.L.A.L. Rev. 76 (1962).

⁸ See *Adams v. Burke*, 84 U.S. 453 (1873).

⁹ Report of the Attorney General's National Committee to Study the Antitrust Laws (March 31, 1955) (hereinafter cited as Committee Report) at 239.

¹⁰ See Clayton Act § 3, 15 U.S.C. § 14 (1964) prohibiting such agreements where the effect "may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

¹¹ *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502 (1917); see also *Mercoid Corp. v. Mid-Continent Inv. Co.*, 320 U.S. 661 (1944); *Morton Salt Co. v. G.S. Suppiger Co.*, 314 U.S. 488 (1942); *Carbice Corp. v. American Patents Dev. Corp.*, 283 U.S. 27 (1931); *Bowman, Tying Arrangements and the Leverage Problem*, 67 Yale L.J. 19 (1957).

the other products and gives the patentee an unfair advantage over his competitors. In the 1948 case of *United States v. Paramount Pictures, Inc.*¹² the Supreme Court extended its general disapproval of tying arrangements to the "block-booking" of copyrighted films, *i.e.*, the requirement that along with the desired films the buyer purchase other films. By analogy to the patent area, the Report of the Attorney General's National Committee to Study the Antitrust Laws (hereinafter referred to as the Committee Report) relied on this copyright case to condemn mandatory (or coerced) package licensing of patents,¹³ which is the practice of refusing to license less than a complete package. Though the Supreme Court has not yet addressed itself to the legality of this practice the law as to mandatory package licensing, a species of tying arrangement, seems relatively clear. A refusal to license less than a complete package transforms package licensing into a misuse, because the licensor is then tying his patents to each other. Where, however, the licensee *voluntarily* accepts a package, no misuse occurs.

The leading Supreme Court decision on package licensing is *Automatic Radio Mfg. Co. v. Hazeltine Research, Inc.*¹⁴ Since the *Hazeltine* case, voluntary package licensing "has stood on a relatively sound legal footing. . . ."¹⁵ Hazeltine Research, a corporation which is not a manufacturer but which derives its income from licensing patents, entered into a ten year licensing agreement with Automatic Radio. Under the agreement the licensee was to pay royalties for the use of 570 patents, 200 applications, and any future patents acquired by Hazeltine. The royalties were based on a percentage of sales by Automatic Radio of complete radio broadcasting receivers. The licensee did not have to use any of Hazeltine's patents in the manufacture of its products but it was required to pay the royalty whether it used them or not. When Automatic Radio refused to pay the royalties, Hazeltine sued for the amount due. As an affirmative defense Automatic Radio claimed that the agreement involved a patent misuse. The Court held that it is not per se a misuse of patents to require the licensee to pay royalties based on a percentage of its sales even though none of the patents is used:

We cannot say that payment of royalties according to an agreed percentage of the licensee's sales is unreasonable. Sound business judgment could indicate that such payment represents the most convenient method of fixing the business value of the privileges granted by the licensing agreement.¹⁶

According to the Court, the royalty provision created no restraint of

¹² 334 U.S. 131 (1948). In 1962 the Supreme Court held that the block booking of copyrighted feature motion pictures for television exhibition is prohibited under § 1 of the Sherman Act. The Court stated that the economic power required to make the practice a restraint of trade is presumed when the tying product is patented or copyrighted. *United States v. Loew's Inc.*, 371 U.S. 38 (1962).

¹³ Committee Report at 239-40.

¹⁴ 339 U.S. 827 (1950).

¹⁵ Ansell, "Flat-Rate" Package Licenses and the Post-Expiration Royalty—Worlds in Collision, 26 Fed. B.J. 206 (1966).

¹⁶ 339 U.S. at 834; see *Plastic Contact Lens Co. v. Butterfield*, 366 F.2d (9th Cir. 1966).

competition beyond the legitimate grant of the patent and, therefore, was not unreasonable. In rejecting Automatic Radio's attempt to apply tie-in cases, the Court noted that there was no requirement for the purchase of goods in the agreement and that Hazeltine did not manufacture or sell goods.¹⁷ Instead the Court viewed the licensing agreement as essentially a grant by the licensor of a privilege to use any of its patents in consideration for payment of royalties unrelated to actual use. It is important to note that some but not all of the patents had expired, a point which the opinion did not discuss but which became significant in later cases. Furthermore, as counsel for the licensee in *Hazeltine* failed to press the argument of misuse by mandatory package licensing,¹⁸ the Court assumed that the package was voluntarily taken.

The Committee Report, in approving of *Hazeltine*, attempted to establish some guidelines by which to determine when package licensing is misused:

Package licensing should be prohibited only where there is refusal, after a request, to license less than a complete package. Additionally, the licensor should not be required to justify on any proportional basis the royalty rate for less than the complete package, so long as the rate set is not so disproportionate as to amount to a refusal to license less than the complete package. For example, where a substantial group of patents are offered at a flat royalty rate, the deletion of one or several specified patents need not affect the rate. . . . Moreover, where several "per piece" licenses are requested and offered, the mere fact that the sum of the "per piece" license royalties exceeds the package royalty rate should not of itself be considered a condition that all or no patents be taken, again, so long as the "per piece" rate is not so disproportionate as to amount to a refusal to license less than the complete package.¹⁹

The position taken in the Committee Report is in accord with that taken in *American Securit Co. v. Shatterproof Glass Corp.*,²⁰ the most authoritative statement concerning the question of mandatory package licensing. In that case the Third Circuit, affirming a decision by the District Court for the District of Delaware,²¹ held that the policy of the patentee to refuse to grant

¹⁷ 339 U.S. at 831. In an amicus curiae brief the Government had argued that a tie was present.

¹⁸ *Id.* In a strong and rather convincing dissenting opinion Justice Douglas, who was joined by Justice Black, stated, "The inevitable result [of the licensing agreement] is that the patentee received royalties on unpatented products as part of the price for the use of the patents.

"The patent owner has therefore used the patents to bludgeon his way into a partnership with this licensee, collecting royalties on unpatented as well as patented articles.

"A plainer extension of a patent by unlawful means would be hard to imagine." *Id.* at 838.

¹⁹ Committee Report at 39-40.

²⁰ 268 F.2d 769 (3d Cir.), cert. denied, 361 U.S. 902 (1959). The facts of the case were similar to those in *Hazeltine*, except that *American Securit* involved an issue of coercion.

²¹ 154 F. Supp. 890 (D. Del. 1957).

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a license under one or more of its patents unless a license was taken under all for a fixed royalty constituted unlawful coercion and an unlawful use of the patent monopoly. Because of such misuse, plaintiff was barred from enforcing its patents in an infringement action:

Mandatory package licensing is no more than the exercise of the power created by a particular patent monopoly to condition the licensing of that patent upon the acceptance of another patent, but that is too much.

Whatever may be the asserted reason or justification of the patent owner, if he compels a licensee to accept a package of patents or none at all, he employs one patent as a lever to compel the acceptance of a license under another. Equity will not countenance such a result.²²

Thus, according to the Third Circuit, mandatory package licensing is per se a patent misuse under the same principle applied in the "tie-in" cases.

Insofar as they approve of package licensing except where it is mandatory, the Committee Report and *American Securit* establish a sound rule. The general objections to forbidden tying arrangements being directly applicable to mandatory package licensing, that practice is clearly a misuse. Unfortunately, neither the Committee Report nor *American Securit* definitively states the degree of coercion that must be present in order to make a package license compulsory. In trying to establish a suitable rule, a decision by the Seventh Circuit has somewhat confused the area.

*Apex Elec. Mfg. Co. v. Altorfer Bros. Co.*²³ held, *inter alia*, that where there was no refusal to license less than all of three patents in the package,²⁴ it was no misuse for the patent owner to insist that exactly the same royalty be paid whether under one, two, or three of the patents. *Apex* thus states that it is not illegal coercion for a patentee to offer to license individual patents or less than the full package for the same royalty as would be charged for the full package. An argument in favor of such a position can be made, based on the well-established doctrine of patent law that a licensee is estopped from challenging the validity of the patent.²⁵ By accepting the package, the licensee would be estopped from contesting the validity of every patent in the entire package, including those not desired by him. On the other hand, by paying the same royalty for a single patent, the licensee is at least free to contest the validity of those patents he refused to accept. In other words, although the licensee pays the same royalty for a single patent he receives more than if he had accepted the full package at the same price. Arguably he then has a genuine alternative when he is

²² 268 F.2d at 777.

²³ 238 F.2d 867 (7th Cir. 1956).

²⁴ *Id.* at 871. "Plaintiffs at first charged a minimum royalty of fifty cents which was later increased to sixty cents and for this royalty they were always willing to grant a license under one, two or three patents." *Id.* at 872.

²⁵ *United States v. Harvey Steel Co.*, 196 U.S. 310 (1905); see the dissenting opinion of Justice Frankfurter in *MacGregor v. Westinghouse Elec. & Mfg. Co.*, 329 U.S. 402, 408 (1947).

offered a choice between one patent and a package at the same rate. This being so, theoretically there is no coercion.²⁶

It is highly improbable that the Supreme Court would take the position enunciated in *Apex*. It seems clear that refusal to reduce a flat royalty rate as fewer patents are licensed amounts to coercing the licensee into acceptance of the full package. Such a practice entails a "per piece" rate "so disproportionate as to amount to a refusal to license less than the complete package,"²⁷ and thus offends the standard established by the Committee Report. The freedom from being estopped as to those patents not accepted by the licensee would appear to be of such speculative value that it would not, in a real sense, offer the licensee a genuine choice. Indeed, it would be a rare licensee who would be willing to license one patent when he could license a package of patents for the same price.

II. POST-EXPIRATION ROYALTIES

The problem of post-expiration royalties, though it may arise independently, often arises within the context of package licensing so that the two areas are often inextricably linked. Following the expiration of the statutory 17-year monopoly granted to the patentee,²⁸ the patent becomes public property. Thus, a license agreement providing for royalty payments which extend beyond the expiration date of the patent may constitute a patent misuse. This is clearly the case when only one patent, rather than a package of patents, is involved, as in *Ar-Tik Systems, Inc. v. Dairy Queen, Inc.*²⁹

In that case a patent owner brought suit against a sub-licensee for royalties due after lapse of the patent. The licensing contract stated that the royalty would continue regardless of the expiration of the patent. The Third Circuit declared that this practice of charging post-expiration royalties constituted a misuse. The court relied to a degree on the Supreme Court case of *Scott Paper Co. v. Marcalus Mfg. Co.*,³⁰ which expressed a basic policy of patent law. That policy is that the patent laws do not contemplate that anyone by contract or by any form of private arrangement may withhold

²⁶ See 11 Vill. L. Rev. 382, 390 (1966).

²⁷ See text at note 19 supra. See also *International Mfg. Co. v. Landon, Inc.*, 336 F.2d 723 (9th Cir. 1964), cert. denied, 379 U.S. 988 (1965), wherein mandatory package licensing of 2 patents was permitted. It was known that no one could produce a product under one of the patents without infringing the other. Such patents are called "blocking" patents as distinguished from competing patents. Since tying arrangements require 2 or more distinct products and blocking patents are not distinct from each other, the anti-competitive effects inherent in mandatory package licensing are not found when the patents are blocking.

²⁸ See note 2 supra.

²⁹ 302 F.2d 496 (3d Cir. 1962).

³⁰ 326 U.S. 249 (1945). In *Scott Paper* an inventor assigned the patent to his employer. When he left the employment to start his own business, he allegedly infringed the patent. In a suit brought by his employer he defended on the ground that the patent which he had assigned had been copied from an expired patent. The employer, on the other hand, claimed that the defendant was estopped from asserting the invalidity of the patent because he had assigned it for value. The Court held that the assignor was not estopped from denying its validity where the device involved is that of an expired patent.

from the public the use of an invention for which the public has paid by the grant of a monopoly in the patented invention for a limited time.³¹

In dictum of *American Securit* the Third Circuit had gone far beyond its position in the later *Ar-Tik* case. In *American Securit*, which condemned mandatory package licensing, the court stated that the requirement that the agreement shall continue in full force and effect to the expiration of the last to expire of any of the patents "constitutes a patent misuse for it extends the payment of royalties of patents under patents which may expire to the expiration date of that patent most recently granted to Securit."³² This statement, which was unnecessary to the holding, put the Third Circuit on record as being completely opposed to the practice of licensing a package of patents at a flat or non-diminishing rate which is paid until the *last* patent in the package expires.

In 1964 the Supreme Court decided what is now the leading case in the area of post-expiration royalties, *Brulotte v. Thys Co.*³³ The Thys Company, which owned patents for hop-picking machinery, sold its machines to farmers for a flat sum and issued a license charging an annual royalty for use. The agreement in question licensed the defendants to use 12 patents relating to the machine, though only 7 were actually incorporated in the machine. All 7 of these patents had expired by 1957, and thereafter 2 licensees refused to pay royalties which had accrued under the licensing agreement both before and after the expiration date of the patents. Thys Company sued for royalties due, and the defendants claimed that the plaintiff had misused its patents by charging royalties after the patents had expired. The Supreme Court of Washington affirmed the judgment of the lower court and held that the period during which royalties were required was a reasonable amount of time over which to spread payments for use of the patent.³⁴

The Supreme Court reversed, stating that the contract did not involve payments for use during the pre-expiration period that were deferred until later but, rather, that the royalty payments were by their terms³⁵ for use during the post-expiration period. Recalling the broad condemnatory language of Justice Stone in *Scott Paper*,³⁶ the Court concluded that a patentee's use of a royalty agreement that projects beyond the expiration date of the patent is unlawful per se.³⁷ The decision also stated that the arrangement

³¹ Id. at 256-57.

³² 268 F.2d at 777.

³³ 379 U.S. 29 (1964); see 1965 Duke L.J. 836; The Supreme Court, 1964 Term, 79 Harv. L. Rev. 56, 199 (1965); see generally 3 A.L.R. 3d 770 (1965).

³⁴ *Thys Co. v. Brulotte*, 62 Wash. 2d 284, 291, 382 P.2d 271, 275 (1963).

³⁵ The Court did not clearly state what type of terms will make an agreement one involving post-expiration royalties. See note 37 *infra*.

³⁶ "[A]ny attempted reservation or continuation in the patentee or those claiming under him of the patent monopoly, after the patent expires, whatever the legal device employed, runs counter to the policy and purpose of the patent laws." 326 U.S. at 256, quoted in *Brulotte*, 379 U.S. at 31.

³⁷ 379 U.S. 29, 32 (1964). In his dissenting opinion, Justice Harlan raised the objection, among others, that courts will not be able to distinguish legal deferred purchase price payments from unlawful exaction of royalties after the patent expires. Skillful contract draftsmen will merely draft the contract in the form of a deferred purchase price payments contract; form, not substance, will govern, and the decision of the majority,

was analogous to forbidden tying arrangements.³⁸ The Court expressly distinguished *Hazeltine* on the basis that all of the patents in that case had not expired, while in *Brulotte* all 7 of the patents incorporated in the machine had expired prior to the termination date for the payment of royalties.³⁹ By choosing to distinguish *Hazeltine*, the Court, in effect, refused to go as far as did the Third Circuit dictum in *American Securit* which totally opposed the practice of licensing a package of patents with a flat royalty rate paid until expiration of the last patent in the package. Since the dictum in *American Securit* is contrary to the legality of the arrangement in *Hazeltine*, insofar as some of the patents in the *Hazeltine* package had expired,⁴⁰ the Supreme Court in *Brulotte* did not prohibit package licensing in which a non-diminishing rate is exacted until all the patents expire. Although *Brulotte* did involve more than one patent, the fact that 7 patents incorporated into the machine had all expired renders the holding of the case only a slight extension of the doctrine enunciated by the Third Circuit in *Ar-Tik*.⁴¹

In refusing to go as far as the Third Circuit did in its *American Securit*, dictum, the Court in *Brulotte* left unanswered several rather important questions:

(1) In a package licensing situation, are flat-rate royalties forbidden *only* where *all* of the licensed patents have expired?

(2) If not, under what circumstances will a non-diminishing royalty rate on a package license constitute a misuse? For example, will the courts permit a minor patent that is the last to expire to extend a uniform royalty rate from the inception of the license to the expiration of the last patent? In attempting to answer these questions, the cases since *Brulotte* have created

Justice Harlan believes, will become ineffectual. It would appear that since the Court is not clear as to what terms will render a licensing agreement a misuse, draftsmen will probably try to avoid any question of post-expiration royalties misuse by requiring that all payments be made before expiration of the last patent in the package. Thus, Justice Harlan's criticism may be only a theoretical point. Justice Harlan also distinguishes restriction of use of the machine from restrictions on use of the patented idea, which is illegal once the idea has fallen into the public domain. *Id.* at 34-39.

³⁸ "A patent empowers the owner to exact royalties as high as he can negotiate with the leverage of that monopoly. But to use that leverage to project those royalty payments beyond the life of the patent is analogous to an effort to enlarge the monopoly of the patent by tying the sale or use of the patented article to the purchase or use of unpatented ones." *Id.* at 33.

For a criticism of the analogy between tying and projecting royalties into unpatentable years, see 79 *Harv. L. Rev.* 56, *supra* note 33, at 200 n.6. See also 65 *Colum. L. Rev.* 1256 (1965). This article also suggests that the *per se* rule of *Brulotte* is too harsh. The writer suggests that the patent holder should be given a chance to show that no unfair use of patent leverage was involved by adoption of a rule establishing only a presumption that post-expiration payments are actually for post-expiration use. *Id.* at 1270-71.

³⁹ "Automatic Radio Co. v. Hazeltine . . . is not in point. While some of the patents under that license apparently had expired, the royalties claimed were not for a period when all of them had expired." 379 U.S. at 33.

⁴⁰ The *Hazeltine* decision, 339 U.S. 827 (1950), did not concern itself with the post-expiration royalty question, although the facts indicated that not all of the patents had expired. See 379 U.S. at 33, n.5.

⁴¹ The Court expressly agreed with *Ar-Tik*, 379 U.S. at 33-34. The fact that only 4 of the 5 other patents, which were not incorporated in the machine, had expired, apparently was not considered significant by the Court. See *Id.* at 30, n.2.

some confusion. It is therefore necessary to analyze them in light of the *Brulotte* precedent in order to see if they can be reconciled with that case.

III. CASES SINCE *Brulotte*

The first significant case which attempted to deal with some of the problems left unsolved by *Brulotte* was *McCullough Tool Co. v. Well Surveys, Inc.*⁴² The case involved a package licensing agreement similar to the one found in *Hazeltine*. Well Surveys, Inc. (WSI), the licensor, charged its licensee a flat rate of the receipts from using WSI's method of logging oil wells, regardless of whether any or all of the patents in the package were used. The licensee, McCullough, as one of its defenses to an infringement suit by WSI, claimed that WSI had misused its patents because some of those in the package had expired.

The Tenth Circuit held that the package licensing agreement was not made unlawful by the fact that the royalties were payable at a flat rate based upon the licensee's overall operations, even though some of the patents in the package had expired or would expire during the period of the agreement. The court distinguished *Brulotte* by noting that there was no attempt by WSI to extend the period for paying royalties beyond the date of expiration of the *last* of the patents covered by the agreement.⁴³ In upholding the post-expiration aspects of the agreement, the court relied chiefly on the factual similarity to *Hazeltine*:

The validity of such an agreement was upheld by the Supreme Court in *Automatic Radio Mfg. Co. v. Hazeltine Research, Inc.*, 339 U.S. 827 The facts in that case are almost identical with the facts in this case

The package licenses were offered for a flat percentage of the licensee's operations, whether or not any of the patents were used. There, as here, some but not all of the patents had expired before the license agreement in question was executed and more of them would expire during the effective period of the agreement.⁴⁴

Insofar as the decision held that there was no misuse in licensing a group of patents at a flat rate which continued unchanged after expiration of some of the patents, it is clearly justified under existing case law. The case falls squarely within the protection of *Hazeltine* wherein only some of the patents had expired, as was noted by the Supreme Court in *Brulotte*. Certiorari was denied in *McCullough*.⁴⁵

⁴² 343 F.2d 381 (10th Cir. 1965), cert. denied 383 U.S. 933 (1966).

⁴³ The license agreement in *Brulotte* "attempted to extend the period for paying royalties beyond the date of expiration of the last of the patents covered by the agreement. That is not the case here or in *Hazeltine*." *Id.* at 410.

⁴⁴ *Id.* at 409.

⁴⁵ 383 U.S. 933 (1966).

McCullough also held that the patentee did not engage in mandatory package licensing and therefore did not violate the prohibition established by *American Securit*. No misuse was shown in patentee's package licensing agreements since the evidence established that WSI had been willing to grant licenses on its patents individually or collectively upon reasonable terms. The Tenth Circuit thus reaffirmed the reasoning of the Third Circuit in

McCullough thus did not actually answer question (1) above. It did not go so far as to indicate that in a package licensing situation flat-rate royalties are forbidden only where all of the licensed patents have expired. On the contrary, the case merely holds that non-diminishing royalty rates are not necessarily forbidden simply because some of the licensed patents in the package have expired. Both questions (1) and (2), however, are explored in *Rocform Corp. v. Acitelli-Standard Concrete Wall, Inc.*⁴⁶ Rocform corporation held patents relating to the process of pouring concrete. It licensed the patents in a package as the "Rocform System," charging a flat price for use of the patents up to termination of the last necessary patent. When Rocform brought an infringement action, the licensee, as an equitable defense, claimed that the licensor had misused its patents. The trial court dismissed the case for want of equity,⁴⁷ and the Sixth Circuit affirmed on the basis that Rocform misused its patents in failing to reduce the royalty after the *most important* patent in the package had expired. The court considered the licensor's agreement to be the equivalent of the practice of using a royalty agreement that projects beyond the expiration date of the patent.

Rocform, of course, claimed that its licensing agreement was legal under *Brulotte*, which only went so far as to disapprove of a package license which continued to charge royalties after all the patents had expired. The Sixth Circuit, however, distinguished *Brulotte* by noting that the Rocform agreement was a "licensing arrangement where one important patent (about to expire) is grouped with others of longer duration for 'leverage,'" rather than a "sale of a piece of machinery which incorporated a number of patents"⁴⁸ as in *Brulotte*.

The *Rocform* decision, in finding a post-expiration royalties agreement to be illegal, adds a necessary corollary to the broad condemnation in *Brulotte* of royalties charged after all of the patents expire. In other words it answers question (1) above negatively by holding that in a package licensing agreement, flat-rate royalties are not forbidden only where all of the licensed patents have expired. It also answers question (2) in part by showing one condition under which non-diminishing package royalties constitute a misuse even though all patents in the package have not yet expired. A license agreement, when it contains no diminution of the license fee at the expiration of a patent of principal importance, constitutes an effort to continue to collect royalties on an expired patent.

It is submitted that the answers found in *Rocform* are correct. Ad-

American Securit by indicating that an element of coercion, such as a refusal by the licensor of a request to license less than all of the patents, is necessary to establish the misuse defense of mandatory package licensing. 343 F.2d at 408. The court did find the misuse of a tying arrangement in that WSI did not give the licensee the express right to manufacture its own instruments and in effect compelled him to buy the necessary instruments from WSI. *Id.* at 407. For a recent patent case involving a tying arrangement and a concise discussion of the misuse doctrine, see *Columbus Automotive Corp. v. Oldberg Mfg. Co.*, 264 F. Supp. 779 (D. Colo. 1967).

⁴⁶ 367 F.2d 678 (6th Cir. 1966).

⁴⁷ 237 F. Supp. 34 (E.D. Mich. 1964).

⁴⁸ 367 F.2d at 681. Having found a misuse, the court refrained from granting relief until plaintiff purged itself of the prohibited practice.

PACKAGE LICENSING

mittedly the facts are in form distinguishable from those in *Brulotte* because all of the patents in the *Rocform* package had not expired. However, when all of the "important" patents in the package have expired the licensing agreement is in substance the same as the one prohibited by *Brulotte*. *Rocform* merely extends *Brulotte* so as to prevent licensors from extending royalty payments for a patent which is about to expire by grouping it with others of little importance.

Hopefully it will be feasible for triers of fact to determine when a patent is "important." In making this determination the courts should limit the prohibition in *Rocform* to cases where the "important" patents are known to be important when licensed. The words used by the court to distinguish *Brulotte* suggest that the court intended such a limited holding. It would seem unfair to allow a licensee who has taken a package of patents of unknown value to refuse to pay the royalty originally agreed upon when one patent turns out to be very valuable but is about to expire. This would be to rob the licensor of the benefit of his original bargain.

As did *McCullough*, *Rocform* also dealt with the issue of mandatory package licensing. The dissenting opinion by Judge O'Sullivan argued that coercion is essential to a finding of misuse and that none was present in *Rocform's* agreement because, when requested to sign the patentee's contract, the defendant refused without suggesting any other agreement which would be acceptable and without requesting that it be given a license limited to one patent. The majority appears to be totally correct in rejecting this argument by observing that a demand for the desired patents as separate items is not "essential to a defense of misuse when the patentholder seeks equitable relief from infringement while still pursuing the illegal practice."⁴⁹ That is to say, the practice of charging post-expiration royalties is in itself a misuse establishing a defense separate from and independent of the misuse defense of mandatory package licensing.⁵⁰ The majority did find an element of coercion in that the agreement contained neither a termination provision that would have enabled the licensee to cancel upon expiration of the first patent nor a provision for reduced royalties upon such expiration.⁵¹ This finding, however, indicated an effort to collect royalties on an expired patent rather than illegal mandatory package licensing.

A recent decision by the Tenth Circuit in *Well Surveys, Inc. v. Perfo-Log, Inc.*⁵² appears to be in conflict with the Sixth Circuit's holding in *Rocform*. *Perfo-Log* involved a package license with one "important" patent, the Swift patent, which expired in 1968, and the less important Peterson patent which will not expire until 1978. When WSI brought an infringement action, the defendant claimed misuse. The court at the trial level granted summary judgment for the defendant, holding, among other things, that

⁴⁹ Id at 681.

⁵⁰ In *Rocform*, the plaintiff argued that, even if it had engaged in mandatory package licensing, that practice is not a misuse where interlocking patents are involved. Id. at 679. See discussion of *International Mfg. Co. v. Landon, Inc.*, 336 F.2d 723 (9th Cir. 1964), cert. denied, 379 U.S. 988 (1965), note 27 supra.

⁵¹ 367 F.2d at 680.

⁵² 396 F.2d 15 (10th Cir. 1968), cert denied, 37 U.S.L.W. 3185 (Nov. 18, 1968).

"[a] license agreement when it contains no diminution of license fee at the expiration of the most important patent and contains no termination clause at the will of the licensee constitutes in effect an effort to continue to collect royalties on an expired patent."⁵³ To support this conclusion of law the court cited *Rocform*.⁵⁴ What gives the lower court decision an added significance is the fact that the judge stated a conclusion of law much too broad to be supported by existing case law. That conclusion of law reads: "A package license agreement which provides that that agreement shall continue in full force and effect until the expiration date of the last patent to expire under which the license is granted constitutes patent misuse because it extends the payment of royalties under patents which will expire to the expiration date of patents which will expire later."⁵⁵ This statement is nothing more than the broad dictum of *American Securit*,⁵⁶ which case the district court cited for support. As was stated before, this type of broad statement would render illegal the agreement in *Hazeltine*, insofar as some of the patents in the *Hazeltine* package agreement had expired. The statement also disregards *Brulotte*, where the Supreme Court distinguished *Hazeltine* as a decision in which some but not all of the patents had expired.

The Court of Appeals for the Tenth Circuit, taking a much less restrictive view of the practice of package licensing, reversed and remanded the case for judgment on the merits on the broad ground that package licensing is not a misuse in the absence of coercion.⁵⁷ The court construed the language of the royalty provision as requiring payment only for operations which infringed a patent right of WSI. Since the Swift patent had expired at the time of the decision, it could not be infringed;⁵⁸ therefore, the court concluded that the agreement did not exact a royalty on an expired patent. Accordingly, the court stated that no royalty was payable unless the Peterson patent was used. The question, said the court, was whether the licensee was forced to enter the package agreement.⁵⁹ Since the defendant offered no evidence on this point, while the plaintiff's affidavits claimed that there was no coercion, the court assumed for the purpose of deciding defendant's motion for summary judgment that there was no coercion.

Perfo-Log argued that *Rocform* governed the case. The court did not agree:

In its statement of facts the Sixth Circuit said that *Rocform* offered to license only under its standard package agreement. In the case at bar, the affidavits submitted by WSI show a willingness to license any or all patents under reasonable, negotiated terms. If the Roc-

⁵³ 1967 Trade Cas. ¶ 72,187, p. 82,272. The court also stated that the patentee attempted to recapture part of the expired "important" patent. "Recapture" seems to imply that the patentee knew the patent was important when he licensed it.

⁵⁴ *Id.* The district court also found mandatory package licensing.

⁵⁵ *Id.*

⁵⁶ See text at note 32 supra.

⁵⁷ 396 F.2d at 17-18.

⁵⁸ *Id.* at 17. The trial court could not come to such a conclusion since at the time of its decision the Swift patent had not expired.

⁵⁹ *Id.*

form decision is taken as holding that a package license, including both important and unimportant patents, is misuse per se when there is no diminution in royalty, or provision for termination, after the expiration of an important patent, we respectfully disagree and adhere to our decision in the first *McCullough* case. The relative importance of patents has no significance if a licensee is given the choice to take a patent alone or in combination on reasonable terms. Freedom of choice is the controlling question.⁶⁰

In his dissenting opinion in *Rocform*, Judge O'Sullivan stated, "I read the majority opinion as holding that, without reference to coercion, the *Rocform* contract was illegal per se because, as viewed by them, *Rocform* was attempting to extend the life of one of its patents."⁶¹ This seems to be a correct interpretation of the holding in *Rocform*. If so, *Rocform* and *Perfo-Log* are conflicting decisions.

The position taken by the Tenth Circuit in *Perfo-Log* closely resembles that taken in the *Rocform* dissenting opinion by Judge O'Sullivan, who argued that coercion is essential to a finding of misuse. As was stated before, this argument is flawed; for, if coercion is present, the misuse is that of mandatory package licensing and the court need not even consider the issue of post-expiration royalties. Nevertheless, *Perfo-Log* does raise troublesome questions. If a licensee voluntarily enters into a package licensing agreement, one would expect that he would be bound to it even though the licensor would continue to receive the same royalty after an important patent expired. The very fact that the licensee voluntarily agreed to such a contract would appear indicative of his belief that the patents in the package, other than the one about to expire, were of sufficient value or "importance" to merit the royalty upon which the parties agreed.

If the Tenth Circuit is saying that licensing agreements that in substance charge post-expiration royalties by extending the life of an important patent are lawful so long as they are freely negotiated, the court is disregarding the principles articulated in the *Ar-Tik* and *Brulotte* cases. The Tenth Circuit's decision in *Perfo-Log*, however, may be interpreted as holding that, until all patents in the package expire, a freely contracted package license is not assailable on the basis that it exacts post-expiration royalties. The reasoning is that the parties themselves have determined by voluntary agreement that no patent is of singular importance. Such an interpretation is suggested by the court's statement that "[t]he relative importance of patents has no significance if a licensee is given the choice to take a patent alone or in combination on reasonable terms."⁶² In other words, the court appears to reject the whole *Rocform* concept of the "important" patent in a voluntary package license.

The Supreme Court denied certiorari in *Perfo-Log*.⁶³ Hopefully the Court

⁶⁰ *Id.* at 18. The court interpreted its decision in the *McCullough* case as requiring coercion for a misuse. *Id.* at 17.

⁶¹ 367 F.2d at 684.

⁶² 396 F.2d at 18.

⁶³ 37 U.S.L.W. 3185 (Nov. 18, 1968).

will solve this problem in the future. The Court's limited decision in *Brulotte* made necessary the additional rule found in *Rocform*. Future clarifying rules will be needed to handle situations similar to *Rocform* where all the patents have not expired, but in substance all "important" patents have expired or are about to expire. The Supreme Court may conclude that it will not be feasible for trial courts to decide, as was done by the district court in *Perfo-Log*, when a patent is of singular importance. If so, the Court might adopt a position which does not restrict the practice of package licensing. Such a position would forbid the use of flat-rate royalty provisions in package licenses only after *all* of the licensed patents have expired. Thus question (1) would be answered in the affirmative and consequently question (2) would not be reached.

CONCLUSION

Apart from the question of post-expiration royalties, the law as to package licensing is relatively clear. Voluntary package licensing is permissible under the *Hazeltine* decision. Although the Supreme Court has not ruled on the issue, it is safe to say that mandatory package licensing is a misuse since it is merely a species of tying arrangement. The practice is especially objectionable because it limits the freedom of the licensee to take only those patents which he wants. Such use of a patent to extend the monopoly granted by the Patent Office should not and will not be tolerated by the courts.

When package licensing is used, projecting royalties into years beyond the expiration date of a patent is not so obviously objectionable as mandatory package licensing. Both practices may extend the benefits accrued by the patentee to encompass an element not within his original grant, but post-expiration royalties involve no direct restraint of trade in the sense of limiting the freedom of the licensee or giving the licensor an unfair advantage over potential competitors. Therefore, in the area of post-expiration package royalties the courts will likely give favorable consideration to the policy of rewarding the inventor and not look only to the countervailing policy of restricting the legal monopoly granted by the patent. It is also possible, however, that the latter policy will eventually dominate. Thus the Supreme Court may decide to go further than it did in *Brulotte* by adopting the position represented by the dictum in *American Securit* which was repeated by the district court in *Perfo-Log*.⁶⁴ Such a decision would transform into a misuse all package licensing agreements which maintain a flat royalty until all patents in the package expire. Future licensing agreements would then have to contain provisions for proportional diminution of license fees as each patent in the package expired, or a clause providing for termination at the will of the licensee as certain patents expired. Requiring these provisions would appear to negate the practical business considerations for which package licensing is maintained.⁶⁵ For instance, great problems would arise in the situation where the licensee takes a package of patents which are all of

⁶⁴ See text at note 55 supra.

⁶⁵ See text at note 9 supra.

speculative value and agrees to pay a royalty based on a percentage of gross sales. One of the patents may become very valuable but expire after a few years while the remaining "unimportant" patents do not expire for several more years. A proportional reduction of license fees should then logically approach 100%, giving the licensee a windfall reduction while thoroughly discouraging package licensing. Provisions for proportional diminution of a package royalty rate as each patent expired would also entangle courts in the question of what constitutes a proportional reduction. This in turn would lead courts into the troublesome issues concerning the relative "importance" of patents. If, in the future, package licensing became impracticable because the Supreme Court adopted the *American Securit* dictum, patent holders, of course, could set up separate licensing agreements with individual royalty rates for each patent. Such separate licensing agreements have been called "commercially impracticable,"⁶⁶ and would entail the loss to businessmen of those advantages found in the practice of package licensing.

Pricing of a patent license presents quite a difficult task. Monetary return from a patent is rarely related to cost since there is no satisfactory or ascertainable correlation between research and development expenses and invention.⁶⁷ Industry norms, therefore, are generally the basis for establishing royalty rates.⁶⁸ If those norms based on package licensing rates were lost, disruptive difficulties in pricing might arise. The complex pricing, accounting and other business problems involved in proportional reductions of package licensing agreements, or in individual licensing, and the widespread use by patent holders of package licensing for reasons of business practicality suggest that package licensing should not be excessively curtailed by the courts.

The courts have been struggling to strike a balance between the conflicting policies of rewarding the inventor and of restricting private concentrations of economic power. As yet, they show little inclination to accept the broad dictum in *American Securit*. Accordingly, licensing agreements need not contain provisions for proportional diminution of royalty rates as each patent in the package expires. Contrary to the belief of some commentators,⁶⁹

⁶⁶ Herbster, Suggestion for a Package Licensing Program, 10 *Idea* 519, 532 (1966). This commentator has suggested that this type of royalty scheme, in addition to being "commercially impracticable," may be suspect under the decision of *American Photocopy Equip. Co. v. Rovico, Inc.*, 359 F.2d 745 (7th Cir. 1966), wherein the Circuit Court of Appeals held that exorbitant royalty rates involving the bulk of the industry can be so high as to amount to a method of price-fixing. That high royalty rates will become unlawful seems unlikely since on remand the trial court held that the royalties charged were reasonably within the reward which the patentee was entitled to secure. The Seventh Circuit affirmed this decision, 384 F.2d 813 (7th Cir. 1967). Also, Justice Douglas, by way of dictum, stated in *Brulotte*, "[A] patent empowers the owner to exact royalties as high as he can negotiate with the leverage of that monopoly." 379 U.S. at 33.

⁶⁷ Adams, The Legality of Compulsory Package Licensing of Patents, 12 *Antitrust Bull.* 773, 794-95 (1967).

⁶⁸ *Id.*

⁶⁹ Ansell, *supra* note 15, at 221. Kennedy, Patent and Antitrust Policy: The Search for a Unitary Theory, 35 *Geo. Wash. L. Rev.* 512, 550 (1967); The Misuse Doctrine and Post-Expiration, Discriminatory and Exorbitant Patent Royalties, 43 *Ind. L.J.* 106, 111 (1967).

Hazeltine, Brulotte, McCullough and *Rocform* are reconcilable rather than conflicting decisions. Therefore, it is submitted that the licensor should feel free to charge a flat royalty rate until the last patent in the package has expired, so long as the method used is a good faith, convenient method of operation involving no patent of singular importance. If, however, it is commercially practicable to reduce proportionately the royalty rate as each patent or group of patents expires, the licensor may be wise to do so.⁷⁰

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⁷⁰ See McCarthy, *A Patent Licensing Policy for Minimizing Antitrust and Misuse Risks*, 46 J.P.O.S. 547, 566 (1964). Since the Supreme Court in the future might require package royalties to be reduced proportionately as patents expire (i.e., might adopt the dictum in *American Securit*), one commentator has suggested the obvious alternative of limiting the life of the license to the first patent to expire until someone else litigates the question. Williams, 10 *Antitrust Bull.* 295, 311 (1965).