

FILED

APR 11 4 42 PM '83

WILLIAM L. WHITTAKER  
CLERK

U.S. DISTRICT COURT  
NO. DIST. OF CAL.

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

THE MAGNAVOX COMPANY, a corp., )  
and SANDERS ASSOCIATES, INC., )  
a corporation, )

Plaintiff, )

v. )

ACTIVISION, INC., a corporation, )

Defendant. )

NO. C 82-5270 TEH

ORDER DENYING DISQUALIFICATION MOTION

This cause came on for hearing on March 14, 1983 on plaintiffs' motion to disqualify defendant's counsel. The Court being fully apprised, and having considered the written and oral arguments of counsel for both sides, as well as the supporting affidavits filed by both sides, and good cause appearing, for the reasons hereinafter stated,

IT IS HEREBY ORDERED that plaintiffs' motion is denied.

FACTS

There are no disputed material facts relating to this motion. Plaintiff Sanders owns five patents concerning video-games: U.S. Patent Nos. 3,659,284; 3,659,285; 3,728,480; RE 28,507; and RE 28,598 [hereinafter "the Sanders patents"]. Sanders has granted an exclusive license in these patents to Magnavox.

1           In 1975, Magnavox and Sanders opposed Bally, Sears,  
2 Seeburg and Atari in four separate lawsuits which were consoli-  
3 dated in the Northern District of Illinois and came to be known  
4 as "the Chicago cases." Among the issues in the Chicago cases  
5 was the validity of the five Sanders patents.

6           Atari was represented in the Chicago cases by Thomas  
7 Herbert of Flehr, Hohbach, Test, Albritton & Herbert [hereinafter  
8 "the Flehr firm"], which had been representing Atari in most of  
9 its patent matters since 1972. Because the interests of both  
10 Atari and Bally at the time of the Chicago litigation would best  
11 have been served by a declaration that the Sanders patents were  
12 invalid, the Flehr firm joined forces with counsel for Bally and  
13 conducted extensive research into evidence supporting a claim  
14 that the concepts underlying the Sanders patents had already  
15 existed in "prior art." In conducting this research, the Flehr  
16 firm utilized technical employees of Atari to obtain "leads" as  
17 to where such evidence might be located. Information on the sub-  
18 ject of "prior art" was freely shared between counsel for Atari  
19 and counsel for Bally, and eventually led to the filing of a  
20 document entitled "Notice of Prior Art," which summarized the  
21 Atari-Bally research. No protective order was entered in the  
22 Chicago cases regarding the contents of this "Notice of Prior  
23 Art."

24           In June 1976, on the eve of trial, the Atari v. Magnavox  
25 and Sanders case settled. A consent judgment was entered against  
26 Atari, finding inter alia that RE 28, 507 was a valid patent and  
27 that Atari was an infringer of that patent. The settlement agree-  
28 ment included three important provisions. First, Magnavox and

1 Sanders covenanted not to sue Atari as an infringer of any of  
2 the five Sanders patents in the future. Second, Magnavox granted  
3 Atari a non-exclusive sublicense on the five Sanders patents,  
4 good for the duration of those patents, in exchange for Atari's  
5 covenant to pay Magnavox in specified installments a sublicen-  
6 see's fee, the last installment of which was due on January 31,  
7 1983. Third, and most importantly for purposes of this motion,  
8 the settlement included the following provision:

9           So long as the license agreement is in effect,  
10           ATARI or its counsel, will not actively parti-  
11           cipate in any further litigation relating to  
12           the [five Sanders patents] in which they are not  
13           a party or in which no game by or for ATARI is  
14           involved, and will not aid any person, other  
15           than a customer or supplier of ATARI if sued  
16           for violation of the aforementioned patents  
17           in connection with the sale of games made by  
18           ATARI, accused of infringement of said patents  
19           . . . by supplying any information concerning  
20           the validity of said patents . . . or any pos-  
21           sible argument or facts relating to a defense  
22           against a charge or possible charge of infringe-  
23           ment of said patents . . .

24 The crucial phrase "or its counsel" was not supplemented by any  
25 other language elsewhere in the settlement agreement which might  
26 have indicated whether the reference was intended to bind Atari's  
27 1976 counsel (the Flehr firm) independent of its representation  
28 of Atari or only insofar as it continued to represent Atari in  
future patent matters, but the Court notes that the agreement  
was signed on behalf of four entities: Magnavox, Sanders, Atari,  
and the Flehr firm. The firms representing Magnavox and Sanders  
did not sign the agreement.

          According to an unchallenged representation in open  
court by general counsel for Activision, Magnavox has in the  
course of the last decade entered into similar non-exclusive

1 sublicense agreements with "dozens" of its competitors. These  
2 agreements have regularly included provisions similar to the  
3 above-quoted provision, purporting to preclude both the sub-  
4 licensee and its counsel from challenging the validity of the  
5 Sanders patents except under certain very narrow circumstances.

6 In mid-1978, the firm of Townsend & Townsend took over  
7 the representation of Atari in all patent matters except a few  
8 minor bookkeeping matters which the Flehr firm continued to handle  
9 for Atari, none of which were or are related to videogames or  
10 the Sanders patents in any way. After Magnavox filed this motion  
11 in the case at bar, the Flehr firm ceased representing Atari  
12 altogether.

13 In 1980, Activision was formed, and it retained the  
14 Flehr firm to represent it in all patent matters. In Septem-  
15 ber 1982, Sanders and Magnavox sued Activision in this Court,  
16 seeking damages for alleged infringement of U.S. Patent Nos.  
17 3,659,284 and RE 28,507. Activision has counterclaimed for a  
18 declaratory judgment that both of these Sanders patents, as well  
19 as U.S. Patent No. 3,728,480, are invalid. Activision is still  
20 represented by the Flehr firm.

21 MOTION

22 Sanders and Magnavox have moved to disqualify the Flehr  
23 firm from representing Activision, because of the Flehr firm's  
24 previous representation of Atari. Specifically, plaintiffs argue  
25 that four independent bases exist for disqualification:

26 (1) the Flehr firm's representation of Activision will  
27 inevitably make use of information disclosed by Atari to the  
28 Flehr firm during the 1976 representation;

1 (2) the Flehr firm's representation of Activision is  
2 "adverse" to the interests of its former client Atari;

3 (3) the Flehr firm's representation of Activision fails  
4 to avoid the appearance of impropriety; and

5 (4) the terms of the 1976 settlement agreement signed  
6 by the Flehr firm prohibit the Flehr firm's representation of  
7 Activision in this case involving the Sanders patents.  
8 Activision and the Flehr firm contest all four of these arguments.

9 LEGAL STANDARDS AND THEIR APPLICATION

10 Under Rule 110-3 of the Local Rules of the Northern  
11 District of California, attorneys practicing before this Court  
12 are required to comply with the California State Bar Rules of  
13 Professional Conduct. Two of those rules are relevant to this  
14 case: Rule 4-101 ("Accepting Employment Adverse to a Client"),  
15 and Rule 5-102(B) ("Avoiding the Representation of Adverse In-  
16 terests").

17 Additionally, American Bar Association Canon 9 (con-  
18 cerning the need to avoid even the appearance of impropriety)  
19 sets a standard against which this Court will measure the Flehr  
20 firm's conduct.<sup>1/</sup> And finally, the terms of the 1976 settlement  
21

---

22  
23 <sup>1/</sup>The California Professional Conduct Rules contain no pro-  
24 vision requiring that attorneys avoid even the appearance of im-  
25 propriety, such as ABA Canon 9 provides. However, the adoption  
26 of the California Professional Conduct Rules by the Local Rules  
27 of the Northern District of California is not exclusive, and does  
28 not preclude application of the ABA Canons in addition to the  
California Rules in a disqualification motion. In Re Airport  
Car Rental Antitrust Litigation, 470 F. Supp. 495, 499-500 (N.D.  
Cal. 1979). Accordingly, this Court has measured the Flehr firm's  
conduct against ABA Canon 9.

//

1 agreement signed by the Flehr firm, in conjunction with Californi  
2 law regarding the validity of such agreements, provide a fourth  
3 standard against which the Flehr firm's conduct must be measured.

4 I. California Professional Conduct Rule 4-101.

5 Rule 4-101 provides in pertinent part:

6 [An attorney] shall not accept employment ad-  
7 verse to a client or former client, without  
8 the informed and written consent of the client  
9 or former client, relating to a matter in refer-  
ence to which he has obtained confidential in-  
formation . . . in the course of his employment  
[from] such client or former client.

10 The cases interpreting Rule 4-101 have identified two elements  
11 to a violation of this rule, both of which must be proved in  
12 order for disqualification to be appropriate. First, the present  
13 employment must be "adverse to a client or former client," which  
14 means both that the client or former client's interest must be  
15 at odds with the new client's interest, and that the client or  
16 former client must be presently a party on the opposite side of  
17 the litigation. <sup>2/</sup> Duncan v. Merrill Lynch, Pierce, Fenner &

18  
19 <sup>2/</sup> Certain very narrow exceptions to the 'opposite party'  
20 half of the adversity requirement have been carved out for "mani-  
21 fest and glaring conflicts," Empire Linotype School, Inc. v. Uni-  
22 ted States, 143 F.Supp. 627, 631 (S.D.N.Y. 1956); Porter v. Huber,  
23 68 F. Supp. 132 (W.D. Wash. 1946); see also Estates Theaters, Inc.  
v. Columbia Pictures, Inc., 345 F. Supp. 93, 98-99 (S.D.N.Y. 1972)  
and for disqualification motions made by alter egos of the former  
clients, Emle Industries, Inc. v. Patentex, Inc., 478 F.2d 562 (2d  
Cir. 1973). These exceptions do not apply to the case at bar.

24 Plaintiffs in this case argue that Trone v. Smith, 621 F.  
25 2d at 1001-02 indicates that the client or former client need not  
26 always be the 'opposite party' in a Rule 4 disqualification, but  
27 the citation is inapt. The former client was in fact the opposite  
28 party in the Trone case; and the language cited by plaintiffs in  
this case merely states that, once disqualified from representing  
a new client against a former client, a lawyer can also be dis-  
qualified from representing the new client against the former  
client's co-parties, even if those co-parties were not themselves  
former clients of the disqualified lawyer. Activision has no co-  
defendants in the case at bar.

1 Smith, 646 F.2d 1020, 1028 (5th Cir. 1981); Fred Weber, Inc.  
2 v. Shell Oil Co., 566 F.2d 602, 608 (8th Cir. 1977); In Re Yarn  
3 Processing Patent Validity Litigation, 530 F.2d 83, 88-90 (5th  
4 Cir. 1976); Fisher Studio v. Loew's, Inc., 232 F.2d 199, 204  
5 (2d Cir. 1956); Richardson v. Hamilton Int'l Corp., 333 F. Supp.  
6 1049, 1054-55 (E.D. Pa. 1971). Second, the subject matter of  
7 the present employment must be "substantially related" to the  
8 subject matter of the past employment. Trone v. Smith, 621 F.2d  
9 994, 998 (9th Cir. 1980); Westinghouse Electric Co. v. Gulf Oil  
10 Corp., 588 F.2d 221, 223 (7th Cir. 1978).

11           Although the language of Rule 4-101 speaks of "obtain  
12 [ing] confidential information," the Ninth Circuit follows the  
13 long line of cases holding that the moving party in a disqualifi-  
14 cation motion need not point to specific confidential information  
15 disclosed or likely to be disclosed; rather, the likelihood that  
16 confidential information has been or will be discussed is irrefut-  
17 ably presumed from the existence of the previous attorney-client  
18 relationship and from the substantial relationship between the  
19 past and present subject matters. Trone v. Smith, 621 F.2d at  
20 1001-01. However, the existence of this irrefutable presumption  
21 is the primary justification for the Rule 4 requirement that the  
22 injured client or former client must be the 'opposite party':  
23 permitting a third-party surrogate to use such a strong presump-  
24 tion for his own purposes would be fundamentally unfair. In Re  
25 Yarn, 530 F.2d at 90.

26           Applying these requirements to the case at bar, a "sub-  
27 stantial relationship" certainly exists between the subject mat-  
28 ter of the Flehr firm's past representation of Atari (i.e., the

1 five Sanders patents) and the subject matter of the Flehr firm's  
2 present representation of Activision (i.e., three of those five  
3 Sanders patents). But plaintiffs have failed to persuade the  
4 Court that the Flehr firm's representation of Activision is "ad-  
5 verse" to Atari, for two reasons.

6 First, since Atari is not an opposite party to Activi-  
7 sion in this litigation and since this case does not involve any  
8 "manifest and glaring" conflict that would warrant abandoning  
9 the opposite party requirement of Rule 4-101, plaintiffs lack  
10 standing to complain of the Flehr firm's representation of Activi-  
11 sion in this case. Plaintiffs argue that the standing defect  
12 is cured by their submission of an Affidavit from Charles S. Paul,  
13 General Counsel to Atari, indicating that Atari objects to the  
14 Flehr firm's representation of Activision; but the Court finds  
15 no support for this argument in the case law, and believes that  
16 permitting plaintiffs to avail themselves of the Rule 4 irrefut-  
17 able presumption of confidential disclosures in this case would  
18 be fundamentally unfair.

19 Second, even if plaintiffs did have standing to assert  
20 Atari's interest, the Court finds that Activision's interest is  
21 not in fact at odds with Atari's present interest, because Atari's  
22 present interest would be better served if the Sanders patents  
23 at issue are declared invalid (as Activision seeks) than if their  
24 validity is upheld. See, e.g., In Re Yarn, 530 F.2d at 88 (hold-  
25 ing a non-exclusive licensee's interest not adverse to an alleged  
26 infringer of the licensed patent, at least in the absence of some  
27 specific evidence of adversity or a statement from the licensee  
28 to that effect). To be sure, plaintiffs argue that this case



1 is distinguishable from In Re Yarn, because of their submission  
2 of the Affidavit from Mr. Paul, which states in conclusory lang-  
3 uage that Atari's interest is "adverse" to Activision's. How-  
4 ever, the Court is unpersuaded by the Paul affidavit, because  
5 neither Mr. Paul nor counsel for plaintiffs has explained precise-  
6 ly where the adversity lies. In the absence of such explanation,  
7 the Court follows the In Re Yarn Court in presuming that a non-  
8 exclusive licensee should have a greater interest in itself being  
9 free of the license restrictions than in seeing one potential  
10 competitor (i.e., Activision) prevented from trafficking in the  
11 patented technology, id., particularly where, as in this case,  
12 the non-exclusive licensee already has "dozens" of other competi-  
13 tors. Accordingly, the Court concludes that the Flehr firm has  
14 not violated Rule 4-101. <sup>3/</sup>

---

15  
16  
17  
18 <sup>3/</sup>The Court wishes to emphasize that its conclusion is not  
19 based on two spurious arguments advanced by Activision. First,  
20 Activision has argued that no material "confidences" of Atari  
21 are jeopardized by the Flehr Firm's representation of Activision,  
22 because the fruits of Atari's research leads on the "prior art"  
23 question were placed in a public record in the Chicago cases.  
24 However, 'publication' of a confidence is not a defense to an al-  
25 leged violation of Rule 4-101, because likely disclosure of con-  
26 fidential information is irrefutably presumed. In Re Airport Car  
27 Rental Litigation, 470 F. Supp. 495, 501 (N.D. Cal. 1979).  
28 Second, Activision has argued that Atari "waived" any right to  
the prior art research contained in its files, because it permit-  
ted the Flehr firm to examine and microfilm those files pertain-  
ing to the Sanders patents during the months immediately preced-  
ing the commencement of this lawsuit. However, Rule 4-101 states  
on its face that waiver is invalid unless "written." Accordingly,  
the Court has rejected both these arguments in reaching its con-  
clusion that the Flehr firm has not violated Rule 4-101.

//

1 II. California Professional Conduct Rule 5-102(B).

2 Rule 5-102(B) provides:

3 [An attorney] shall not represent conflicting  
4 interests, except with the written consent of  
all parties concerned.

5 The cases interpreting Rule 5-102(B) have identified two elements  
6 to a violation of this rule, both of which must be proved in  
7 order for disqualification to be appropriate. First, the lawyer  
8 must in fact be representing "conflicting interests." <sup>4/</sup> Unified  
9 Sewerage Agency, Etc. v. Jelco, Inc., 646 F.2d 1339, 1343 (9th  
10 Cir. 1981); Fred Weber, 566 F.2d at 608-09. Second, the lawyer  
11 must in fact presently be representing both of the conflicting  
12 interests. Jelco, 646 F.2d at 1344-45.

13 Applying these requirements to the case at bar, Magna-  
14 vox has failed to persuade the Court that either requirement is  
15 met. As noted above in the discussion of Rule 4-101, the Court  
16 finds that Atari's interest in the Sanders patents is not at odds  
17 with Activision's, and hence concludes that the Flehr firm is  
18 not representing "conflicting interests." Second, even if a con-  
19 flict did exist between the past representation of Atari regard-  
20 ing the Sanders patents and the present representation of Activi-  
21 sion, the Flehr firm's minor bookkeeping work for Atari in the  
22 years after 1978 on matters wholly unrelated to the Sanders  
23 patents does not warrant a finding that the Flehr firm has been  
24 simultaneously representing both parties. See Jelco, 646 F.2d

25  
26 <sup>4/</sup> Because Rule 5-102(B) does not import any strong presump-  
27 tion analogous to the irrefutable presumption of confidential dis-  
28 closure that accompanies Rule 4-101, the requirement in Rule 5-  
102(B) that there be "conflicting interests" does not include an  
'opposing party' requirement. See Fred Weber, 566 F.2d at 609.  
Inconsistency under Rule 5-102 can be shown merely by demonstrat-  
ing that the two clients' interests are at odds with one another.

1 at 1344-45. Accordingly, the Court concludes that the Flehr firm  
2 has not violated Rule 5-102(B).

3 III. ABA Canon 9.

4 ABA Canon 9 requires that lawyers avoid even the appear-  
5 ance of impropriety. The cases interpreting Canon 9 have identi-  
6 fied two elements which must be shown before a lawyer can be dis-  
7 qualified under this Canon. First, although actual wrong-doing  
8 need not be shown, the moving party must at least show a "reason-  
9 able possibility" that some specifically identifiable impropriety  
10 did occur or will occur. Fred Weber, 566 F.2d at 609, quoting  
11 Woods v. Covington County Bank, 537 F.2d 804, 813 (5th Cir. 1976).

12 Second, the "likelihood of public suspicion [of impropriety]"  
13 must outweigh "the social interest . . . served by a lawyer's  
14 continued participation." Woods, 537 F.2d at 812, 813 n. 12.

15 Applying these requirements to the case at bar, the  
16 Court notes that the Ninth Circuit has stressed that Canon 9  
17 should not be used to upset the "delicate balance" achieved by  
18 rules like Rule 5-102 between the profession's need to preserve  
19 the highest ethical standards and the parties' right to their  
20 own freely chosen counsel. Jelco, 646 F.2d at 1352; Trone v.  
21 Smith, 621 F.2d at 1002. Hence the classic Canon 9 case does  
22 not involve confidential disclosures or representation of con-  
23 flicting interests, which can best be considered under Canons  
24 4 and 5, but rather involves direct considerations of appearance,  
25 such as were at issue in the many cases considering the question  
26 of whether one lawyer's knowledge can be imputed to his or her  
27 entire firm. See, e.g., Westinghouse Electric Co. v. Kerr-McGee,  
28 580 F.2d 1311, 1318 (7th Cir.), cert. denied, 439 U.S. 955 (1978).

1           By contrast, the case at bar involves no direct con-  
2 siderations of appearance. Counsel for plaintiffs conceded in  
3 oral argument that the only Atari "confidences" at issue in this  
4 case were those concerning the "prior art" research into the  
5 Sanders patents, which research was placed in a public record  
6 in the Chicago cases. Hence this is not the sort of case likely  
7 to arouse "public suspicion [of impropriety]." Moreover, given  
8 the fairly limited number of patent attorneys available, and  
9 particularly given the zeal with which plaintiffs' counsel have  
10 induced "dozens" of patent attorneys to sign settlement agreements  
11 purportedly prohibiting those attorneys from participating in  
12 any litigation involving the Sanders patents at issue in this  
13 case, the Court concludes that Activision's right to their own  
14 freely chosen counsel clearly outweighs the profession's need  
15 to avoid chimerical hints of impropriety.

16 IV. The 1976 Settlement Agreement Signed by the Flehr firm.

17           Analytically, the settlement agreement signed by the  
18 Flehr firm in 1976 warrants their disqualification only if (1) the  
19 clause precluding participation in litigation relating to the  
20 five Sanders patents applies to the Flehr firm independent of  
21 its representation of Atari, and (2) that clause is valid. On  
22 the first issue, the Court is satisfied that the parties intended  
23 the clause precluding litigation relating to the Sanders patents  
24 to apply to the Flehr firm independent of its representation of  
25 Atari. To be sure, the language of the settlement agreement it-  
26 self is ambiguous, but the fact that the agreement was signed  
27 by three business entities yet only by one of the law firms in-  
28 volved provides sufficient objective evidence that the parties

1 intended the Flehr firm to be bound regardless of whether it re-  
2 presented Atari in future or not. See Brobeck, Phleger & Harrison  
3 v. Telex Corp., 602 F. 2d 866, 873-74 (9th Cir. 1979).

4           However, the Court is persuaded that the clause preclud-  
5 ing the Flehr firm from participating in any litigation relating  
6 to the five Sanders patents is clearly invalid and unenforceable  
7 under Cal. Bus. & Prof. Code § 16,600, because it restrains a  
8 law firm from engaging in a lawful profession and because none  
9 of the statutory exceptions applies to this case. Defendants  
10 contend that the Flehr firm is not precluded by the agreement  
11 from practicing law, but is merely precluded from practicing law  
12 against the five Sanders patents for the life of those patents.  
13 Defendants cite three cases in which non-compete agreements have  
14 been approved, Gordon v. Landau, 49 Cal. 2d 690, 694 (1958);  
15 Boughton v. Socony Mobil Oil Corp., 231 Cal. App. 2d 190, 191  
16 (1964); King v. Gerold, 104 Cal. App. 2d 316, 318 (1952), but  
17 the California courts in all three cases stressed that the non-  
18 compete agreements approved were between competitors in the same  
19 business or profession, and were of very short duration. By con-  
20 trast, Magnavox and Sanders here seek to enforce an agreement  
21 between videogame companies and a law firm, whose express dura-  
22 tion was in the neighborhood of twenty years. The important  
23 public policy considerations outlined in KGB, Inc. v. Giannoulas,  
24 104 Cal. App. 3d 844, 848-49 (1980) which justify the general  
25 statutory bar to non-compete agreements in California are parti-  
26 cularly affronted where, as here, two videogame companies attempt  
27 to buy out "dozens" of patent law firms by persuading their  
28 clients to settle, so that any remaining challengers to the