

CONTRACTING FOR A RETURN TO THE USPTO: *INTER PARTES* REEXAMINATIONS AS THE EXCLUSIVE OUTLET FOR LICENSEE CHALLENGES TO PATENT VALIDITY

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ABSTRACT

Licensing of patents is an important route for socially valuable transfers of rights in intellectual property. The continuing value of patent licenses, however, has been called into doubt in view of the Supreme Court's recent *MedImmune, Inc. v. Genentech, Inc.* decision. That case held that licensees do not have to repudiate their licenses in order to have Article III standing to seek a declaratory judgment on the validity of licensed patents. *MedImmune* furthers the federal policy, announced in earlier Supreme Court cases such as *Lear, Inc. v. Adkins*, of helping licensees police the public domain by eliminating contractual and state-law restrictions on their ability to challenge patent validity. This Article seeks to reconcile the tension between societal interests in getting rid of "bad" patents on the one hand, and in promoting the practice of patent licensing on the other. It argues that licensing parties should contract for, and courts should enforce, clauses that require licensees seeking to challenge patent validity to pursue an *inter partes* reexamination in the U.S. Patent and Trademark Office. This procedure provides an adequate alternative to district court decla-

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ratory judgment actions because it retains adversarial features, but does not subject licensees and licensors to the high cost of litigation. The proposed solution is thus desirable as a matter of licensing policy because it would likely help reduce the costs of licensing. More importantly, reexamination-only clauses are probably enforceable in spite of *Lear* if they are tailored to allow validity challenges prohibited by the reexamination statute to proceed in district courts.

I. INTRODUCTION

Patents are federal grants of legal rights that have some “attributes of personal property.”¹ Although patent rights can be analyzed as grants of monopoly power rather than rights in tangible property, such as personal possessions,² the statutory³ and common-law⁴ bases for treating patents as property rights are also quite strong. The common law generally disfavors restraints on alienation of property,⁵ and patent law is no different. The Patent Act explicitly provides for the assignment and licensing of patents.⁶ Indeed, Adam Mossoff demon-

¹ 35 U.S.C. § 261 (2006).

² See generally Mark A. Lemley, *What’s Different About Intellectual Property?*, 83 TEX. L. REV. 1097 (2005); Mark A. Lemley, *Property, Intellectual Property, and Free Riding*, 83 TEX. L. REV. 1031 (2005).

³ See 35 U.S.C. § 261.

⁴ See, e.g., *Cont’l Paper Bag Co. v. E. Paper Bag Co.*, 210 U.S. 405, 423–24 (1908); *United States v. Am. Bell Tel. Co.*, 167 U.S. 224, 250 (1897) (“The inventor is one who has discovered something of value. It is his absolute property.”); *Consol. Fruit-Jar Co. v. Wright*, 94 U.S. 92, 96 (1876) (“A patent for an invention is as much property as a patent for land.”). But see *Brown v. Voss*, 715 P.2d 514, 517–18 (Wash. 1986) (demonstrating that a property right can sometimes be protected by a liability rule); see also *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 392–93 (2006) (holding that a finding of patent infringement does not automatically have to be followed by an injunction); Adam Mossoff, *Exclusion and Exclusive Use in Patent Law*, 22 HARV. J.L. & TECH. 321, 353–54 (2009).

⁵ See, e.g., *White v. Brown*, 559 S.W.2d 938, 940 (Tenn. 1977) (stating that “free alienation of property . . . [is] one of the most significant incidents of fee ownership”); see also Mossoff, *supra* note 4, at 350 (observing that the “familiar legal definition of property . . . is ‘the exclusive right of possessing, enjoying, and disposing of a thing’” (quoting *McKeon v. Bisbee*, 9 Cal. 137, 142 (1858))) (emphasis added).

⁶ 35 U.S.C. § 261 (“Applications for patent, patents, or any interest therein, shall be assignable in law by an instrument in writing.”); MANUAL OF PATENT EXAMINING PROCEDURE § 301 (8th ed. 7th rev. 2008) [hereinafter MPEP] (“As compared to assignment of patent rights, the licensing of a patent transfers a bundle of rights which is less than the entire ownership interest A patent license is, in effect, a contractual agreement that the patent owner will not sue the licensee for patent infringement . . .”).

strated in a recent article that free alienability of patent rights has been an essential feature of U.S. patent law from its beginnings.⁷ On the normative side, Scott Kieff argued that the law should encourage transfers of patent rights so as to facilitate commercialization of patented inventions,⁸ a result that can be accomplished with vigorous and unfettered licensing and assignment practice.

Of course, not all property rights enjoy unlimited alienability. In his famous dissent in *Moore v. Regents of University of California*,⁹ Justice Mosk provided examples of property rights that can, by law, be alienated by sale but not by gift (e.g., a bankrupt's property), by gift but not by sale (e.g., wild fish or game killed pursuant to a sportsman's license), and by neither gift nor sale (e.g., a prescription drug or a license to practice a profession).¹⁰ For each of Mosk's examples, strong policy reasons exist for the restraints on alienability. For example, society wants prescription drugs to be used by persons who need them for a specific medical condition, rather than by addicts or black-market resellers. In the same vein, the law limits gifts by a person contemplating bankruptcy because of high potential for fraudulent transfer.¹¹ To be sure, licensing does not entail complete disposition of property in that the licensor retains its ownership rights, but it is a form of property alienation nonetheless.¹² As with restrictions on transfer by sale or gift, one can imagine policy reasons for restraints on transfer of some types of property rights by licensing—say, my licensing to someone else my right to vote in a particular election.

Limitations on licensing and other forms of property alienation do not have to take the form of a direct prohibition. Sometimes, public policy dictates that a particularly structured contract involving a transfer of some property right

⁷ Mossoff, *supra* note 4, at 24 (explaining that, in nineteenth-century courts, "American patents . . . were 'defined as an incorporeal chattel, which the patent impresses with all the characteristics of personal estate' [and] '[p]atent interests [were] not distinguishable . . . from other kinds of property'" (quoting a note following *Belding v. Turner*, 3 F. Cas. 84, 85 (C.C.D. Conn. 1871) (No. 3662) and *Carr v. Rice*, 5 F. Cas. 140, 146 (C.C.S.D.N.Y. 1856) (No. 2440))).

⁸ Compare F. Scott Kieff, *Property Rights and Property Rules for Commercializing Inventions*, 85 MINN. L. REV. 697, 753 (2001) (advancing the commercialization theory of patent law), with Mark A. Lemley, Colloquium, *Ex Ante Versus Ex Post Justifications for Intellectual Property*, 71 U. CHI. L. REV. 129, 141 n.42, 144–45 (2004) (criticizing the commercialization theory in favor of the reward theory).

⁹ 793 P.2d 479 (Cal. 1990).

¹⁰ *Id.* at 510 nn.9–11 (Mosk, J., dissenting).

¹¹ See 11 U.S.C.A. § 548 (West 2011) (making voidable, under certain circumstances, transfers made by a debtor in the period within two years of filing a bankruptcy petition).

¹² See Richard A. Epstein, *The Disintegration of Intellectual Property? A Classical Liberal Response to a Premature Obituary*, 62 STAN. L. REV. 455, 499 (2010).

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should not be enforced. One example is the doctrine of unconscionability.¹³ In *Williams v. Walker-Thomas Furniture Co.*,¹⁴ the Court of Appeals for the District of Columbia held unenforceable a contractual clause that, in the event of nonpayment for an item bought on credit at a department store, allowed the store to repossess other items that a customer had purchased but did not yet completely pay for due to a “cross-collateral” securitization structure of the store’s credit sales.¹⁵ Cases like *Walker-Thomas* suggest that principles of private ordering through contract sometimes give way to policy concerns over, for example, disparities in bargaining power or knowledge between department stores and their customers. An indirect result of the unconscionability doctrine is that alienation of property is also impaired. For example, in the absence of the cross-collateralization clause, the store may have to raise its prices or the cost of credit,¹⁶ leading to depressed demand for its goods.¹⁷

Although the Patent Act does not incorporate any explicit restrictions on the transfer of patent rights, case law has developed its own limitations on the enforcement of certain types of patent licenses. In *Brulotte v. Thys Co.*,¹⁸ the Supreme Court held that an agreement calling for payment of royalties past the expiration date of a licensed patent was unenforceable under the doctrine of patent misuse. The Court sought to combat anti-competitive effects of extending the patentee’s monopoly power past the lawful patent term.¹⁹ *Brulotte* has been severely criticized because its rule, while relying on questionable economic justifications, hampers the contracting parties’ ability to finance licensing transactions on mutually desirable terms.²⁰ Nevertheless, the case, which essentially prohibits patent licenses that call for post-expiration royalty payments, remains good law.²¹ Five years after *Brulotte*, where the majority opinion clearly expressed the Supreme Court’s discomfort with licenses that appeared to in-

¹³ RESTATEMENT (SECOND) OF CONTRACTS § 208 (1981).

¹⁴ 350 F.2d 445 (D.C. Cir 1965).

¹⁵ *Id.* at 447–49.

¹⁶ MARVIN A. CHIRELSTEIN, CONCEPTS AND CASE ANALYSIS IN THE LAW OF CONTRACTS 91 (5th ed. 2006).

¹⁷ See Russell Korobkin, Symposium, A “Traditional” and “Behavioral” Law-and-Economics Analysis of *Williams v. Walker-Thomas Furniture Company*, 26 U. HAW. L. REV. 441, 449 (2004).

¹⁸ 379 U.S. 29 (1964).

¹⁹ *Id.* at 32.

²⁰ See, e.g., Michael Koenig, Note, *Patent Royalties Extending Beyond Expiration: An Illogical Ban from Brulotte to Schieber*, 2003 DUKE L. & TECH. REV. 5, 8.

²¹ See *Scheiber v. Dolby Labs., Inc.*, 293 F.3d 1014 (7th Cir. 2002), *cert. denied*, 537 U.S. 1109 (2003).

terfere with federal competition policy,²² the Court held in *Lear, Inc. v. Adkins*²³ that the danger of unfair monopolization, inherent in the patent grant, dictated that challenges to patent validity should not be restrained by license agreements.²⁴ *Lear* abrogated the state contract law doctrine of licensee estoppel, which had prevented licensees from initiating such challenges.²⁵ The *Lear* decision has been interpreted to mean that “licensees were free to challenge licensed patents even if they had agreed to refrain from doing so.”²⁶ Commentators have criticized the case on the grounds that facilitation of validity challenges by licensees may chill licensing activity by decreasing the value of patent licenses and, as a consequence, reducing incentives for the pursuit of inventive activities.²⁷

²² *Brulotte*, 379 U.S. at 32–33.

²³ 395 U.S. 653 (1969).

²⁴ *Id.* at 671; see also Christopher R. Leslie, *The Anticompetitive Effects of Unenforced Invalid Patents*, 91 MINN. L. REV. 101 (2006) (detailing the costs of improvidently granted patents to society).

²⁵ *Lear*, 395 U.S. at 671. The licensee estoppel doctrine was based in part on the maxim that “[g]eneral rules of contract law do not allow purchasers to repudiate their promises simply because they become dissatisfied with the deal, at least without compensating the other contracting party.” ROGER E. SCHECHTER & JOHN R. THOMAS, *PRINCIPLES OF PATENT LAW* 367 (2d ed. 2004). In this context, licensees’ challenges to patent validity can be viewed as a manifestation of their dissatisfaction with the license. One exception to the *Lear* doctrine involves licenses that were entered into as a consequence of litigation. See, e.g., *Flex-Foot, Inc. v. CRP, Inc.*, 238 F.3d 1362, 1368 (Fed. Cir. 2001); see also Michael Risch, *Patent Challenges and Royalty Inflation*, 85 IND. L.J. 1003, 1007 n.16 (2010) (“Postlitigation settlement agreements may be considered res judicata and in some cases cannot be challenged by the settling licensee.”). The Article focuses on those licenses that were not the result of litigation and are therefore subject to the *Lear* prohibition.

²⁶ SCHECHTER & THOMAS, *supra* note 25, at 434. The following language from *Lear*, endorsing a nineteenth century case that held contractual prohibitions of patent validity challenges to be unenforceable, helped Schechter and Thomas, and the lower courts, reach this conclusion:

[T]his Court found the doctrine of patent estoppel so inequitable that it refused to grant an injunction to enforce a licensee’s promise never to contest the validity of the underlying patent. ‘It is as important to the public that competition should not be repressed by worthless patents, as that the patentee of a really valuable invention should be protected in his monopoly’

Lear, 395 U.S. at 663–64 (quoting *Pope Mfg. Co. v. Gormully*, 144 U.S. 224, 234 (1892)) (alteration in original).

²⁷ See Rochelle Cooper Dreyfuss, *Dethroning Lear: Licensee Estoppel and the Incentive To Innovate*, 72 VA. L. REV. 677, 682 (1986); see also SCHECHTER & THOMAS, *supra* note 25, at 368 (observing that “[i]f the value of patent licenses has been decreased after [*Lear*], so has the value of patents, which in turn would reduce incentives to innovate”).

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Subsequent Supreme Court cases have lessened *Lear*'s impact,²⁸ particularly with regard to the validity of royalty payments for licenses based on inventions for which a patent never issued,²⁹ but the case's core holding of promoting the freedom of licensees to challenge patent validity has never been overruled.³⁰ Moreover, the Supreme Court's recent *MedImmune, Inc. v. Genentech, Inc.*³¹ decision arguably extended *Lear*'s reach by removing procedural hurdles in the way of licensees who wish to challenge the validity of patents under license agreements. In *MedImmune*, the Supreme Court held that declaratory judgment actions in district courts by patent licensees against licensor patent owners can meet the case or controversy requirement of Article III of the Constitution even when the licensee has not stopped paying royalties.³² Courts must now evaluate licensees' standing to sue for declaratory judgment by considering the totality of the circumstances.³³ After *MedImmune*, judges would have

²⁸ See *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257, 265 (1979); *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 484 (1974).

²⁹ *Aronson*, 440 U.S. at 261–62.

³⁰ Importantly, the lower courts did not interpret *Lear* as holding that no-challenge clauses, even if found unenforceable, render the *patent itself* unenforceable on the theory of patent misuse. See, e.g., *Wallace Clark & Co. v. Acheson Indus., Inc.*, 401 F. Supp. 637, 640 (S.D.N.Y. 1975) (“Even if it were assumed that the license agreement seeks to prevent plaintiff from challenging the patent’s validity [in violation of *Lear*], the inclusion therein of this unenforceable provision does not constitute patent misuse.”) (citing multiple cases).

³¹ 549 U.S. 118 (2007).

³² *Id.* at 137. Subject to the strictures of Article III, the Declaratory Judgment Act grants parties threatened with a potential lawsuit the right to initiate court action via a declaratory judgment suit. *Id.* at 130. In the patent infringement context, the potential infringer can sue for declaratory judgment of non-infringement, invalidity, or enforceability of the patent that the other party threatens to assert. See also *infra* note 161.

³³ *Id.* at 127 (holding that courts must determine whether “the facts alleged, *under all the circumstances*, show that there is a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment” (quoting *Maryland Casualty Co. v. Pacific Coal & Oil Co.*, 312 U.S. 270, 273 (1941))) (emphasis added). To be sure, the lower courts have had little opportunity to apply *MedImmune* in the factual context of licensee challenges to patent validity since very few such challenges have reached the courts since *MedImmune* was decided. See David I. Levine & Charles E. Belle, *Declaratory Relief After MedImmune*, 14 LEWIS & CLARK L. REV. 491, 524 (2010) (“[O]f the cases following *MedImmune* (including cases returning to court because of the *MedImmune* decision) the Federal Circuit has not addressed even one action for declaratory relief brought by a licensee.”). As a result, the “totality of the circumstances” test has been developed largely by cases where no license exists and declaratory judgment jurisdiction is based on a threat of a patent infringement lawsuit. See, e.g., *SanDisk Corp. v. STMicroelectronics, Inc.*, 480 F.3d 1372, 1377–83 (Fed. Cir. 2007); see also Edo Royker, Note, *Covenants Not To Sue Provide Less Immunity in a Post-MedImmune World*, 61 HASTINGS L.J. 473, 476–77 (2009) (explaining the Supreme Court’s “totality of the circum-

to decide whether sufficient threat of litigation by the licensor exists if the licensee who is paying royalties “under protest” (e.g., when it believes the patent to be invalid) were to cease making these contractually required payments.³⁴ Because a license suggests that the patent owner is serious about enforcing its patents and likely considers the licensee’s activities to constitute infringement absent the license, *MedImmune*’s test for granting declaratory judgment jurisdiction appears easy for licensees to satisfy.³⁵ In the words of one Federal Circuit opinion, “*MedImmune* may have lowered the bar for determining declaratory judgment jurisdiction in all patent cases; certainly it did so in the licensor-licensee context.”³⁶

According to many commentators, licensees’ new-found ability to bring declaratory judgment suits for invalidity of licensed patents while continuing to enjoy the benefits of a license radically altered the balance of power in their favor.³⁷ In turn, this rule is said to have significantly reduced patent owners’

tances test” in *MedImmune* as interpreted by the Federal Circuit in cases that do not involve licensee-licensor disputes).

³⁴ See also *infra* Part III.A. Again, given the dearth of lower court case law interpreting *MedImmune* in the context of licensee-licensor disputes, one can only speculate about what courts might actually do if faced with such a dispute under the facts that differ from those of *MedImmune* itself. See Levine & Belle, *supra* note 33, at 524; *infra* notes 164–66 and accompanying text. As the foregoing discussion suggests, however, courts and commentators appear to agree that it would generally be straightforward for licensees to attain declaratory judgment standing for challenging the validity of licensed patents.

³⁵ To be sure, declaratory judgment jurisdiction is not mandatory; district courts have the discretion to decline such jurisdiction. See *Wilton v. Seven Falls Co.*, 515 U.S. 277, 282 (1995); see also *infra* notes 160–61 and accompanying text. The key consequence of *MedImmune* is to lower the bar for attaining declaratory judgment standing and presumably to enable licensees to show standing in a greater percentage of cases, as the foregoing discussion suggests. As do some other commentators, this Article proposes that parties to a license can lawfully limit such standing by contract under certain circumstances. See *infra* notes 57–58 and accompanying text; *infra* Part III.B.2.

³⁶ *Hewlett-Packard Co. v. Acceleron LLC*, 587 F.3d 1358, 1361 (2009); see also *Micron Tech., Inc. v. MOSAID Techs., Inc.*, 518 F.3d 897, 902 (Fed. Cir. 2008) (“Whether intended or not, the now more lenient legal standard facilitates or enhances the availability of declaratory judgment jurisdiction in patent cases.”). A licensee may wish to continue paying royalties while challenging the patent’s validity to avoid a potential injunction, treble damages, and attorney’s fees if it were to lose a patent infringement lawsuit. See *infra* notes 146–51 and accompanying text.

³⁷ See, e.g., Rochelle Cooper Dreyfuss & Lawrence S. Pope, *Dethroning Lear? Incentives To Innovate After MedImmune*, 24 BERKELEY TECH. L.J. 971, 973 (2009) (“[*MedImmune*] effects a dramatic change in the rules of the licensing game by substantially enhancing the bargaining position of the licensee to the detriment of the patent holder. The licensee can now seek a new arrangement any time it can mount a credible contract dispute. Furthermore, it can do so without taking any real risk, for if the patent is upheld, the licensee can continue to

incentives to license their technology³⁸ and increased the costs of licensing.³⁹ Rochelle Dreyfuss and Lawrence Pope argued that the *MedImmune* decision can potentially spur creative licensing solutions that would restore some of the licensors' bargaining power. Among license terms that Dreyfuss and Pope have proposed are the requirement that the bulk of the royalty be paid upfront and a condition that provides for an automatic termination of the license upon a validity challenge.⁴⁰ Nevertheless, these authors ultimately conceded that the best outcome licensors can hope for in the wake of *MedImmune* is that "[t]he decision could lead courts to revisit *Lear* and *Brulotte*, and the other 1960s cases expressing distrust with state law that touches on innovation policy."⁴¹

The *Lear* Court used the tool of federal preemption⁴² to override the time-honored common-law rule that forbids rescission of a contract when a party "become[s] dissatisfied with the deal."⁴³ Preemption doctrine mandates that,

rely on the license."); Katherine A. Helm & Gene W. Lee, *Call It a Comeback: A Sweeping Change in the Law on Declaratory Judgment Actions Against Patent Owners*, 64 N.Y.U. ANN. SURV. AM. L. 231, 245 (2008) ("[The new rule] kicked open the courthouse door for both licensees and prospective licensees.").

³⁸ See, e.g., Andrew Beckerman-Rodau, F. Scott Kieff, Lawrence Sung & Thomas Woolston, *eBay v. MercExchange and Quanta Computer v. LG Electronics*, 4 J. BUS. & TECH. L. 5, 23–24 (2009); Peter Jay, Note, *Removing Incentives for Technology Transfer: MedImmune v. Genentech*, 5 BUFF. INTELL. PROP. L.J. 69, 70 (2007) ("The likely result [of the *MedImmune* rule] will be a chilling of licensing practices."); Royker, *supra* note 33, at 491–95.

³⁹ See generally Dreyfuss & Pope, *supra* note 37; Risch, *supra* note 25.

⁴⁰ Dreyfuss & Pope, *supra* note 37, at 992–96, 1003–06; see also Risch, *supra* note 25, at 1024–42 (explaining and critiquing post-*MedImmune* strategies such as fully paid-up royalties and termination-on-challenge clauses); *infra* Part III.B.

⁴¹ Dreyfuss & Pope, *supra* note 37, at 1006. Dreyfuss and Pope hope for the eventual overruling of those cases because of their adverse effects on licensing relationships and innovation generally: "*Lear* and *Brulotte* . . . are certainly out of step with current economic understanding and business practices. Rules that give licensing parties greater flexibility to structure their arrangements can make licensing more efficient, improve public access to new technologies, and enhance incentives to innovate." *Id.*

⁴² ERWIN CHERMERINSKY, CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES 392 (3d ed. 2006). Federal preemption can take many forms, and the Chemerinsky treatise provides useful background on which subsequent comments rely. *Id.* at 392–418.

⁴³ SCHECHTER & THOMAS, *supra* note 25, at 367; see also *supra* note 25 and accompanying text. In dicta, the *MedImmune* Court took note of this contract principle, stating that "[patentees] appeal to the common-law rule that a party to a contract cannot at one and the same time challenge its validity and continue to reap its benefits . . ." *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 135 (2007) (citations omitted). The Court went on to add, however, that the principle is inapplicable to the *jurisdictional* question presented:

Rather, [the licensee] is asserting that the contract, properly interpreted, does not prevent it from challenging the patents, and does not require the payment

“[i]f there is a conflict between federal and state law, the federal law controls and the state law is invalidated because federal law is supreme.”⁴⁴ In the absence of explicit statutory federal preemption⁴⁵ and the lack of implied preemption through federal occupation of the entire intellectual property field,⁴⁶ as seen in the continued vitality of state trade secret law in the wake of *Lear*,⁴⁷ the remaining route that the federal courts can use to override state common law is the doctrine of conflict preemption.⁴⁸ Cases invoking conflict preemption have held that, in addition to explicit preemption and field preemption, the Supremacy Clause of the Constitution⁴⁹ dictates that state law is preempted by federal law when the former becomes an obstacle to implementing federal laws or policies.⁵⁰ *Lear* clearly announced the state-federal conflict created by the state law doctrine of licensee estoppel: it became an obstacle to the public interest in free access to ideas in the public domain by “muzzling” licensees who were likely to have the financial resources and strong economic incentives to rid the country of bad patents.⁵¹ Later commentators confirmed what appeared to be an unstated assumption in *Lear*: the U.S. Patent and Trademark Office (“USPTO”) issues

of royalties because the patents do not cover its products and are invalid. Of course even if [the licensor] were correct that the licensing agreement or the common-law rule precludes this suit, the consequence would be that [the licensor] win[s] this case *on the merits*—not that the very genuine contract dispute disappears, so that Article III jurisdiction is somehow defeated.

Id. at 135–36 (emphasis in original).

⁴⁴ CHEMERINSKY, *supra* note 42, at 392.

⁴⁵ *Id.* at 396–97.

⁴⁶ *Id.* at 401–02.

⁴⁷ *See Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 484 (1974).

⁴⁸ CHEMERINSKY, *supra* note 42, at 412–16 (framing this issue in terms of invalidity of “state laws that impede achievement of federal objectives”). Another preemption doctrine, based on the impossibility of compliance with both state and federal law, is not applicable here. *Id.* at 409–12.

⁴⁹ U.S. CONST. art. VI, cl. 2; *see also Gade v. Nat’l Solid Waste Mgmt. Ass’n*, 505 U.S. 88, 108 (1992) (observing that the Supremacy Clause is the constitutional source of the preemption doctrine).

⁵⁰ For examples of Supreme Court cases other than *Lear* where federal patent law was held to preempt state intellectual property law regimes, *see Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 152 (1989); *Compcorp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234, 238 (1964); *Sears, Roebuck & Co. v. Stiffel Co.*, 376 U.S. 225, 229 (1964).

⁵¹ “Muzzled” was the word choice of the *Lear* court: “Licensees may often be the only individuals with enough economic incentive to challenge the patentability of an inventor’s discovery. If they are *muzzled*, the public may continually be required to pay tribute to would-be monopolists without need or justification.” *Lear, Inc. v. Adkins*, 395 U.S. 653, 670 (1969) (emphasis added).

too many patents of questionable quality.⁵² As a result, we as a society have no choice but to enlist the aid of the litigation process, in part by removing barriers that prevent licensees from going to court, to correct the USPTO's mistakes.⁵³ Licensees who challenge questionable patents, then, serve as "private attorneys general" who can vindicate the public interest by helping return the inventions protected by improvidently granted patents to the public domain.

A declaratory judgment action is not the only way to challenge patent validity, however. A licensee can always stop paying royalties and raise the defense of invalidity when it is sued for patent infringement. However, this route contemplates a passive role for the licensee. In contrast, the Patent Act provides for an active route for checking the work of the USPTO—the reexamination system.⁵⁴ In particular, the *inter partes* reexamination procedure allows any third party to bring prior art that can potentially render already issued patent claims anticipated or obvious to the attention of the USPTO.⁵⁵ If the examiner conducting the reexamination agrees with the theory of the party who brings the challenge rather than with the patent owner, he or she can pronounce the claims at issue unpatentable and invalid.⁵⁶ Importantly, this approach may raise an estoppel, as the third-party requester cannot relitigate the USPTO's determination of a claim's validity in a reexamination.⁵⁷ This Article argues that patent li-

⁵² See, e.g., Mark A. Lemley & Bhaven Sampat, Essay, *Is the Patent Office a Rubber Stamp?*, 58 EMORY L.J. 181, 181 (2008).

⁵³ Some commentators have proposed the adoption of a bounty system to actively encourage challenges to patent validity. See, e.g., Joseph Scott Miller, *Building a Better Bounty: Litigation-Stage Rewards for Defeating Patents*, 19 BERKELEY TECH. L.J. 667, 668 (2004); John R. Thomas, Symposium, *Collusion and Collective Action in the Patent System: A Proposal for Patent Bounties*, 2001 U. ILL. L. REV. 305, 307–08 (2001); see also *infra* note 257 and accompanying text.

⁵⁴ The reexamination system was not yet in place when *Lear* was decided. See *infra* Part III.C.1 for analysis of clues suggesting what the *Lear* Court would have thought of the reexamination system in the context of its goal of encouraging patent validity challenges.

⁵⁵ 35 U.S.C. §§ 302, 311–318 (2006).

⁵⁶ *Id.* § 316(a) (stating that other possible outcomes of an *inter partes* reexamination are amendments to previously issued claims or a cancellation of some or all old claims and issuance of new claims to replace them).

⁵⁷ *Id.* § 315(c) ("A third-party requester . . . is estopped from asserting at a later time, in any civil action arising in whole or in part under section 1338 of title 28, the invalidity of any claim finally determined to be valid and patentable on any ground which the third-party requester raised or could have raised during the *inter partes* reexamination proceedings."). But see Tun-Jen Chiang, *The Advantages of Inter Partes Reexamination*, 90 J. PAT. & TRADEMARK OFF. SOC'Y 579, 586 n.32 (2008) ("There is some ambiguity regarding the extent to which an accused infringer who loses in *inter partes* reexamination can re-litigate validity using references that were *not* considered by the PTO.") (emphasis in original). The

censes should include clauses that make *inter partes* reexamination the exclusive route for resolving licensee-licensor disputes over patent validity, and that courts should enforce such terms. Contracting for the reexamination-only route would continue to enable licensees to vindicate the federal interest of policing the public domain in a setting that reduces disruption of private ordering endangered by the threat of costly litigation.⁵⁸

Part II will discuss the reexamination statute, provide some reasons why it has not yet gained widespread use, and detail potential advantages that it offers over district court litigation for resolving patent disputes. Part III will describe the uncertainty in licensee-licensor relationships engendered by the *MedImmune* decision, address representative solutions proposed by other commentators, and consider objections to those solutions from the viewpoints of licensing policy and enforceability. The Article will then propose the use of reexamination-only clauses in license agreements and examine them in the context of *Lear*'s patent policy and preemption concerns, arguing that such terms preserve the licensees' ability to act as private attorneys general who challenge bad patents. Finally, the Article will advance and address several objections to the reexamination-only approach and propose a variation of the reexamination-only license term that is likely to be enforceable under *Lear*, as well as suitable to both licensees and licensors. Part IV will conclude the Article by describing the contribution of the reexamination-only approach to the problem of reducing the costs of the rules of *Lear* and *MedImmune*. Furthermore, it will summarize the reasons why the proposed solution can enable licensees to comply with these cases while also helping promote contract-driven transfers of patent rights and

ambiguity lies in meaning of the phrase "newly discovered prior art unavailable to the third-party requester and the Patent and Trademark Office at the time of the *inter partes* reexamination proceedings." 35 U.S.C. § 315(c). Chiang notes that "[i]t is not clear . . . whether 'unavailable' means 'not possible to discover,' 'not actually discovered,' or something in between." Chiang, *supra*, at 586 n.32.

⁵⁸ It is worth noting that *MedImmune* did not affect the ability of licensees to bring reexamination challenges, since the reexamination statute does not have a standing requirement. See 35 U.S.C. § 301 ("Any person at any time may cite to the Office in writing prior art consisting of patents or printed publications which that person believes to have a bearing on the patentability of any claim of a particular patent.") (emphasis added). Whether licensing parties can lawfully agree, under *Lear*, to prohibit only reexamination challenges to patent validity (while allowing district court challenges), is a question that courts, to my knowledge, have not had occasion to address.

fulfill licensing parties' expectations of certainty that contracts generally provide.⁵⁹

II. THE *INTER PARTES* REEXAMINATION AS A ROUTE FOR CHALLENGING PATENT VALIDITY: PROS AND CONS

A. *The Basics of the USPTO's Post-Grant Proceedings*

The Patent Act contemplates several types of USPTO-run post-grant proceedings, that is, actions by the USPTO that may modify a patent after it was allowed. One such proceeding is a reissue,⁶⁰ where the patentee asks the USPTO to consider amending some or all of the claims in an issued patent. Reissues can be broadening, where the patentee requests claims that are greater in scope than those originally granted in view of its reassessment of the boundaries set by prior art and the coverage of the patent's specification.⁶¹ In contrast, when the patentee finds prior art that may invalidate some of its patent's claims, or perhaps discovers a defect in the specification, it can request a narrowing reissue.⁶² This type of a reissue enables the patentee to anticipate a validity challenge by amending its claims in such a way as to save the claims from wholesale invalidation, albeit in a narrowed form. Thus, reissue proceedings essentially allow patentees to correct their own mistakes. When patent owners realize that they have improvidently asked for, and received, claims that were unnecessarily narrow or perilously broad (or otherwise defective), the reissue remedy enables the patent owners to ask the USPTO to reset the claims' boundaries.⁶³ Reissue proceedings involve a dialogue that occurs strictly between the owner of the issued patent and the USPTO, and third parties are not involved in determining the scope of newly amended claims.⁶⁴ Of course, claim amend-

⁵⁹ See generally Epstein, *supra* note 12; see also Lorelei Ritchie, *Reconciling Contract Doctrine with Intellectual Property Law: An Interdisciplinary Solution*, 25 SANTA CLARA COMPUTER & HIGH TECH. L.J. 105 (2008).

⁶⁰ 35 U.S.C. § 251 (2006).

⁶¹ A patent owner cannot request a broadening reissue after two years from the date of issuance of the patent. *See id.*

⁶² *See id.*

⁶³ This practice has been criticized, as many commentators believe that patent owners should bear the risk of their own mistakes. See, e.g., Tun-Jen Chiang, *Fixing Patent Boundaries*, 108 MICH. L. REV. 523, 554 (2010); see also Mark A. Lemley & Kimberly A. Moore, *Ending Abuse of Patent Continuations*, 84 B.U. L. REV. 63 (2004).

⁶⁴ This kind of a dialogue between a patent applicant and the USPTO also represents standard pre-grant patent prosecution practice.

ments can significantly affect third parties by empowering patentees, who can now wield broader claims, to pursue an infringement case that would not have been available before reissue,⁶⁵ or to forestall a validity challenge by narrowing claims. To be sure, claim amendments in reissue, as do claim amendments generally, may lead to prosecution history estoppel in litigation.⁶⁶ But third parties simply have no say about what happens in a reissue proceeding.

Reexamination proceedings differ from reissues by the critical fact that the former can be requested by third parties.⁶⁷ The Patent Act provides for two types of reexaminations, *ex parte*⁶⁸ and *inter partes*.⁶⁹ The amendment to the Patent Act authorizing *ex parte* reexaminations, which was passed into law in 1980, allows anyone (e.g., third parties, the Commissioner for Patents, or the patent owner, perhaps preemptively) to initiate the reexamination process by citing potentially invalidating prior art to the USPTO.⁷⁰ Cited prior art must be accompanied by an explanation of its relevance, a written request for a reexamination of an issued patent, and a fee.⁷¹ After the request, however, the third party remains only marginally involved in the proceedings.⁷² The argument over the bearing of the prior art on the patentability of already issued claims takes place primarily between the examiner and the patentee. In fact, the *ex parte* requester can maintain complete anonymity in this type of a reexamination pro-

⁶⁵ Nevertheless, third parties whose activities or products did not fall within the scope of the pre-reissue claims, but became infringing after the broadening reissue, have intervening rights. See 35 U.S.C. § 252 (“A reissued patent shall not abridge or affect the right of any person or that person’s successors in business who, prior to the grant of a reissue, made, purchased, offered to sell, or used within the United States, or imported into the United States, anything patented by the reissued patent . . .”). In addition, the statute allows for equitable intervening rights even in cases where the claims have been *narrowed* in reissue. See *id.* (“[T]he court may also provide for the continued practice of any process patented by the reissue that is practiced, or for the practice of which substantial preparation was made, before the grant of the reissue, to the extent and under such terms as the court deems equitable for the protection of investments made or business commenced before the grant of the reissue.”); see also SCHECHTER & THOMAS, *supra* note 25, at 251 (“Less intuitive is that intervening rights may also arise when the claims are narrowed during reissue.”).

⁶⁶ See, e.g., *Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co.*, 535 U.S. 722, 727 (2002).

⁶⁷ 35 U.S.C. § 301. Note that “broadening reexaminations” are also not allowed. *Id.* § 305 (“No proposed amended or new claim enlarging the scope of a claim of the patent will be permitted in a reexamination proceeding under this chapter.”).

⁶⁸ *Id.* §§ 301–07.

⁶⁹ *Id.* §§ 311–18.

⁷⁰ *Id.* § 301.

⁷¹ *Id.* § 302.

⁷² See generally MPEP § 2201.

ceeding.⁷³ After the *ex parte* reexamination filing is made in the Central Reexamination Unit (CRU), the USPTO Director determines whether the request that accompanies the cited prior art raises a “substantial new question” of patentability.⁷⁴ If the Director finds that it does, he or she orders a reexamination and the patent owner can then “file a statement on the new question of patentability, including any proposed amendments the patent owner wishes to make.”⁷⁵ The third-party requester is allowed to file a reply to this statement, and at this point its role in the reexamination ends.⁷⁶

In stark contrast, *inter partes* reexamination contemplates intimate involvement of third-party requesters in the USPTO’s proceedings.⁷⁷ This procedure became available fairly recently, initially adopted in 1999 and significantly amended in 2002, and has steadily increased in popularity over the past several years.⁷⁸ Under the statute, third parties can ask the USPTO to determine whether a substantial new question of patentability exists, make arguments challenging non-final office actions issued by the USPTO, and, crucially, comment on the patentee’s claim amendments made in response to the cited prior art. These responses may cause the patent examiner to issue additional office actions.⁷⁹ Moreover, third-party requesters have the right to appeal the examiner’s final office action in response to the reexamination request to the Board of Patent Appeals and Interferences (BPAI).⁸⁰ If that resolution is unsatisfactory, they may further appeal to the Court of Appeals for the Federal Circuit and finally to the Supreme Court.⁸¹ Third-party requesters also have the right to challenge any

⁷³ 35 U.S.C. § 301 (“At the written request of the person citing the prior art, his or her identity will be excluded from the patent file and kept confidential.”).

⁷⁴ *Id.* § 303(a). This standard for initiating a reexamination may change to “a reasonable likelihood that the petitioner will prevail with regard to at least one claim” if the Patent Reform Act of 2011 becomes law. See Kevin A. Noonan, *Post-Grant Review Provisions of S. 23*, PATENT DOCS (Mar. 16, 2011), <http://www.patentdocs.org/2011/03/post-grant-review-provisions-of-s-23.html>.

⁷⁵ MPEP § 2249.

⁷⁶ See *id.* § 2201.

⁷⁷ 35 U.S.C. § 311.

⁷⁸ See Robert A. Saltzberg & Mehran Arjomand, *Reexaminations Increase in Popularity*, MORRISON & FOERSTER LEGAL UPDATES (2007), available at <http://www.jdsupra.com/documents/49c9fcbe-8a6d-4fbf-8d72-892c19db8b9c.pdf>.

⁷⁹ 35 U.S.C. § 314. See generally MPEP § 2601.01.

⁸⁰ 35 U.S.C. §§ 134(c), 315(b)(1).

⁸¹ *Id.* § 315(b)(1). A third-party requester’s right to appeal to the Federal Circuit, or to participate in the patent owner’s Federal Circuit appeal, is available only for *inter partes* reexamination proceedings commenced on or after November 2, 2002. See MPEP § 2601. Only a few BPAI decisions on *inter partes* reexaminations have been published, and very few Fed-

appeals made by the patent owner by reply briefs.⁸² Thus, *inter partes* reexamination proceedings, though conducted by an agency of the Executive Branch, exhibit some features of full-scale litigation. As the Manual of Patent Examining Procedure notes, “[t]he optional *inter partes* alternative provides third party requesters with a greater opportunity to participate in reexamination proceedings, while maintaining most of the features which make reexamination a desirable alternative to litigation in the Federal Courts (e.g., low cost relative to Court proceedings, expedited procedure).”⁸³

B. Reasons for Limited Utilization of the Inter Partes Procedure

1. Barriers to Widespread Adoption of *Inter Partes* Reexamination

In spite of some apparent advantages of *inter partes* reexaminations over litigation, many law firms focused on patent litigation have been slow to incorporate the procedure into their practices.⁸⁴ Although, as mentioned above,⁸⁵ *inter partes* filings have been steadily increasing in frequency since the 2002 amendments, the absolute number of such requests is still quite small. Since the procedure became available in 1999 and until the end of 2010, only 1015 *inter partes* requests have been filed.⁸⁶ Fiscal year (“FY”) 2005 saw 59 filings, with the number increasing to 70 in FY 2006, 126 in FY 2007, and 168 in FY 2008.⁸⁷ In FY 2009, the USPTO received 258 *inter partes* filings and the number climbed to 281 in FY 2010, confirming the upward trend in the utilization of the

eral Circuit appeals of the BPAI’s dispositions on *inter partes* reexaminations have been pursued since the appellate process was changed in 2002. Personal Communication with Rahul Pathak, Partner, Squire Sanders, Palo Alto, Cal. office (Feb. 22, 2010); *see also infra* note 109.

⁸² *See* 35 U.S.C. § 315(b)(2).

⁸³ MPEP § 2601; *see also infra* notes 129–31 and accompanying text. Note, however, that while reexamination is generally less expensive than litigation, it is far from cheap to initiate an *inter partes* reexamination or to mount an opposition to an *inter partes* request. *See* Raymond A. Mercado, *The Use and Abuse of Patent Reexamination: Sham Petitioning Before the USPTO*, 12 COL. SCI. & TECH. L. REV. 93, 99–100 (2011).

⁸⁴ One preliminary reason for the limited utilization of *inter partes* reexaminations is that the procedure is not available at all for patents issuing from applications filed before November 29, 1999. *See* MPEP § 2601.

⁸⁵ *See* Saltzberg & Arjomand, *supra* note 78.

⁸⁶ United States Patent and Trademark Office, *Inter Partes Reexamination Filing Data* (Dec. 31, 2010), available at http://www.uspto.gov/patents/stats/IP_quarterly_report_Dec_2010.pdf.

⁸⁷ *Id.*

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procedure.⁸⁸ Even when one adds third-party *ex parte* filings into the mix,⁸⁹ however, these numbers pale in comparison with the volume of patent litigation in district courts, with the federal court system seeing, on average, about 2,600 patent lawsuits a year over the past several years.⁹⁰ Of course, the number of patent lawsuits cannot be directly compared with the number of reexaminations, as many accused or potentially accused patent infringers may not have a realistic validity challenge and must rely only on non-infringement defenses.⁹¹ Nevertheless, it is unquestionable that the patent bar did not exactly embrace the reexamination alternative to litigation. One article pithily stated that “many [patent practitioners] suggested that recommending *inter partes* reexamination to a client was tantamount to committing malpractice.”⁹²

What explains the unwillingness of patent litigators to pursue the *inter partes* reexamination route as a defensive strategy? One answer is litigation estoppel following the USPTO’s determinations of claim validity against the challenge of the third-party requester.⁹³ Indeed, if a reexamination challenge is brought during litigation, the case can sometimes be stayed pending the resolution of an *inter partes* request, with the outcome of the reexamination often resolving the litigation.⁹⁴ But estoppel cannot be the whole story, since district

⁸⁸ *Id.*

⁸⁹ Many *ex parte* filings are made by the patent owner. See United States Patent and Trademark Office, *Ex Parte Reexamination Filing Data* (Dec. 31, 2010), available at http://www.uspto.gov/patents/stats/EP_quarterly_report_Dec_2010.pdf (thirty-three percent of *inter partes* requests since the procedure was instituted in 1981 were made by patent owners). The data shows that there were 643 *ex parte* filings in FY 2007, 680 in FY 2008, 658 in FY 2009, and 780 in FY 2010.

⁹⁰ *Patent Litigation Costs: How Much Does It Cost To Protect a Patent?*, INVENTION STATISTICS/INVENTION DATA, http://www.inventionstatistics.com/Patent_Litigation_Costs.html (last visited Jan. 6, 2011). In addition, the comparison is complicated by the phenomenon of concurrent reexamination and litigation. See *Inter Partes Reexamination Filing Data*, *supra* note 86 (some seventy percent of patents that have undergone or are undergoing *inter partes* reexamination are also at issue in a litigated case). This fact, however, does not alter the conclusion that the reexamination system is used significantly less frequently than litigation to challenge the validity of issued patents.

⁹¹ See also *infra* note 134.

⁹² Stephen G. Kunin & Anton W. Fetting, Symposium, *The Metamorphosis of Inter Partes Reexamination*, 19 BERKELEY TECH. L.J. 971, 978 (2004).

⁹³ 35 U.S.C. § 315(c); see also *supra* note 57 and accompanying text. As noted above, however, the USPTO’s determinations in *inter partes* reexamination are ultimately appealable to the Federal Circuit. See *supra* note 81 and accompanying text.

⁹⁴ 35 U.S.C. § 318; see Chiang, *supra* note 57, at 583 (“District courts have liberally granted stays of litigation when *inter partes* reexamination has been ordered.”). Chiang also notes that reexamination practice can have an effect on settlements: “[b]oth sides can adjust their

court determinations of validity, like any judicial decision, have res judicata effect.⁹⁵ So the real question must be why the patent bar prefers the forum of the district courts to the forum of the USPTO. First, and most obvious, the reexamination procedure is simply not available for patents issued from applications filed before November 29, 1999,⁹⁶ further complicating direct comparisons between the number of reexaminations and patent lawsuits. A second obvious answer, already alluded to above, is that the reexamination statute limits the kinds of challenges that the third-party requester can bring in its attempt to invalidate the patent.⁹⁷ For example, the USPTO will not consider evidence of prior invention⁹⁸ or on-sale and public use statutory bars⁹⁹ to patentability in a reexamination proceeding; only “patents or printed publications” are acceptable as § 102 (novelty-defeating) or § 103 (non-obviousness-defeating) prior art.¹⁰⁰ Moreover, the requester cannot challenge the patent on the basis of § 112 defects.¹⁰¹ Thus, the third-party requester cannot argue that the claims, as issued,

settlement positions to account for the reduced uncertainty [due to a resolved reexamination challenge], making settlement more likely [and] reducing litigation costs.” *Id.*; see also MPEP § 2686.04; Robert Greene Sterne et al., *Reexamination Practice with Concurrent District Court Patent Litigation*, 9 SEDONA CONF. J. 53, 53 (2008).

⁹⁵ Note, however, that res judicata does not always bar subsequent reexamination challenges. That is, even after an adverse district court determination (i.e., affirmance of validity), a party challenging a patent may still be able to request *inter partes* reexamination, due to a more stringent standard of proof required to invalidate patent claims in district court challenges. See *infra* note 113 and accompanying text. For a discussion of this issue primarily in the *ex parte* reexamination context, see Betsy Johnson, Comment, *Plugging the Holes in the Ex Parte Reexamination Statute: Preventing a Second Bite at the Apple for a Patent Infringer*, 55 CATH. U.L. REV. 305, 305, 318 (2005) (arguing that an adjudicated infringer sometimes has “two bites at the apple” but noting that, specifically for *inter partes* challenges, the statute provides that “[the] infringer may not request [a] . . . reexamination to challenge a patent if the request is based on issues he raised or could have raised in a prior civil action” (citing 35 U.S.C. § 317(b)); see also Chiang, *supra* note 57, at 581 (“[The USPTO] may . . . invalidate a patent that has previously been upheld by a court.” (citing *Ethicon v. Quigg*, 849 F.2d 1422 (Fed. Cir. 1988))).

⁹⁶ See MPEP § 2601.

⁹⁷ See *supra* note 55 and accompanying text.

⁹⁸ 35 U.S.C. § 102(g)(2) (2006).

⁹⁹ *Id.* § 102(b).

¹⁰⁰ *Id.* § 301 (“Any person at any time may cite to the Office in writing *prior art consisting of patents or printed publications* which that person believes to have a bearing on the patentability of any claim of a particular patent.”) (emphasis added).

¹⁰¹ See *id.*; see also MPEP § 2258(II) (“Where new claims are presented or where any part of the disclosure is amended, the claims of the reexamination proceeding, are to be examined for compliance with 35 U.S.C. 112. Consideration of 35 U.S.C. 112 issues should, however, be limited to the amendatory (e.g., new language) matter. . . . To go further would be inconsis-

are invalid because the patent is not in compliance with enablement, written description, best mode, or definiteness requirements of § 112.¹⁰² In addition, reexamination challenges cannot be based on grounds such as incorrect inventorship, inequitable conduct, unpatentable subject matter, or lack of utility—indeed, any ground that does not involve citing “patents or printed publications” against the issued patent.¹⁰³ In this regard, *inter partes* reexaminations differ markedly from post-grant opposition proceedings in the European Union, where a third party can essentially inject itself into the patent prosecution process during a nine-month period following the grant of a patent, and challenge the patent under any statutory patentability provision of European Union law.¹⁰⁴

The third, and perhaps most important, systemic barrier to wide acceptance of the procedure is some patent litigators’ mistrust of the USPTO. The

tent with the statute to the extent that 35 U.S.C. 112 issues would be raised as to matter in the original patent claim.”). This exclusion, in addition to the prohibition of challenges based on § 102(b) statutory bars, is a serious drawback of the reexamination system from the viewpoint of patent validity challengers, as § 112 defects account for a significant percentage of patents invalidated in litigated patents. See John R. Allison & Mark A. Lemley, *Empirical Evidence on the Validity of Litigated Patents*, 26 AIPLA Q.J. 185, 208 (1998); see also *infra* note 238 and accompanying text.

¹⁰² See 35 U.S.C. § 112; *supra* note 101. Note that claim amendments resulting from the reexamination, however, can be challenged on § 112 grounds (as well as on any newly arising novelty or non-obviousness issues). See 37 C.F.R. § 1906(a) (2005); MATTHEW A. SMITH, *INTER PARTES* REEXAMINATION 76 (Ed. 1E, Jan. 31, 2009) (on file with author); see also MPEP § 2617.

¹⁰³ 35 U.S.C. § 301.

¹⁰⁴ EUROPEAN PATENT CONVENTION, Part V, art. 99. An amendment to the Patent Act that was recently under consideration contemplated introducing a similar provision into U.S. patent law. See Patent Reform Act of 2010, S. 515, 111th Cong. at 49–62, available at <http://judiciary.senate.gov/legislation/upload/PatentReformAmendment.pdf>. The 2011 version of the Patent Reform Act contains an analogous provision for an opposition proceeding that would be available for nine months after the allowance of a patent. See Dennis Crouch, *Patent Reform Act of 2011: An Overview*, PATENTLY-O (Feb. 10, 2011), <http://www.patentlyo.com/patent/2011/02/patent-reform-act-of-2011-an-overview.html>. If such a post-grant opposition procedure is adopted in the U.S., the proposal in Part III may be modified such that parties could contract for an opposition proceeding in addition to a traditional *inter partes* reexamination (which would still be available under the current proposal after the nine-month opposition period passes) in appropriate circumstances—i.e., when the license is for a patent application or a very recently issued patent. For arguments proposing a USPTO-run post-grant opposition procedure and an analogous administrative proceeding, respectively, and discussions the virtues of these proposals in the context of adjudicating patent validity disputes, see Kevin A. Meehan, *Shopping for Expedient, Inexpensive & Predictable Patent Litigation*, 2008 B.C. INTELL. PROP. & TECH. F. 102901; Jonathan S. Pope, Comment, *Declaratory Judgment Jurisdiction in Patent Disputes: A Rock and a Hard Place*, 9 J. MARSHALL. REV. INTELL. PROP. L. 583 (2010).

reasoning goes, if the patent office was wrong once and issued a bad patent, how do we know that patent examiners will not make the same mistake again?¹⁰⁵ This perception was perhaps justified in the early days of the reexamination system, when third-party challenges were evaluated by the same examiner who allowed the original claims.¹⁰⁶ By now, however, it is clear that the USPTO is taking self-correction through *inter partes* reexaminations seriously, perhaps overzealously so.¹⁰⁷ Greg Gardella and Emily Berger simply noted that “[the USPTO] is now much more likely, on its second review, to invalidate patents which do not represent significant advances over the previously developed technology.”¹⁰⁸ Thus, in spite of some recent high-profile cases in which the USPTO did not appear to make substantive concessions to third-party requesters,¹⁰⁹ it is difficult to argue that the agency exhibits a bias toward patent owners

¹⁰⁵ Discussion in this paragraph is based in part on a Personal Communication with Rahul Pathak, *supra* note 81.

¹⁰⁶ This is not the case today: “[i]t is the policy of the Office that the CRU will assign the reexamination request to an examiner different from the examiner(s) who examined the patent application.” MPEP § 2636.

¹⁰⁷ See *Inter Partes Reexamination Filing Data*, *supra* note 86 (for the 221 *inter partes* reexamination certificates issued since 1999, ten percent of challenged patents had all the claims confirmed, forty-seven percent had their all claims cancelled or disclaimed, and forty-three percent resulted in “claims changes”). Note that the combined percentage of patents invalidated or narrowed in *inter partes* reexaminations is significantly greater than the percentage of patents invalidated in district court litigation. See Michael Meehan, *Increasing Certainty and Harnessing Private Information in the U.S. Patent System: A Proposal for Reform*, 2010 STAN. TECH. L. REV. 1, 1 (noting that “[h]alf the patents are invalidated” in patent infringement actions (citing Allison & Lemley, *supra* note 101, at 205–07)); see also *infra* note 134.

¹⁰⁸ Greg H. Gardella & Emily A. Berger, *United States Reexamination Procedures: Recent Trends, Strategies and Impact on Patent Practice*, 8 J. MARSHALL REV. INTELL. PROP. L. 381, 381 (2009). More precisely, some claims are completely invalidated while others are narrowed by amendment. See *supra* note 107.

¹⁰⁹ See, for example, eBay’s challenge to MercExchange’s patents. Johnson, *supra* note 95, at 333 n.172 (several *ex parte* reexaminations). Reexamination challenges to stem cell patents belonging to the Wisconsin Alumni Research Foundation have also been viewed as generally unsuccessful. See *U.S. Office Upholds Embryonic Stem Cell Patents*, MILWAUKEE J. SENTINEL (June 28, 2008), available at <http://www.jsonline.com/business/29551579.html> (*ex parte* Reexamination Nos. 90/008,102 and 90/008,139, and *inter partes* Reexamination No. 95/000,154). Nevertheless, a recent BPAI decision reversed the disposition of the examiner in one of the three reexaminations (the *inter partes* one) and rejected all three claims of the patent at issue, U.S. Pat. No. 7,029,913 (issued Apr. 18, 2006), as obvious. See *Found. for Taxpayer & Consumer Rights v. Wisconsin Alumni Research Found.*, Appeal No. 2010-1854, 2010 WL 1734377 (B.P.A.I. Apr 28, 2010) (reversing examiner’s disposition in Reexamination No. 95/000,154). The patent owner has since reopened prosecution of the 7,029,913 patent. In contrast, by all accounts, various reexamination challenges to NTP’s patents that became famous in the *NTP, Inc. v. RIM* litigation over the Blackberry have ulti-

in *inter partes* proceedings. Perhaps a more subtle reason for the fact that the procedure has been slow to catch on is a cultural divide between patent litigators and prosecutors. Many attorneys who work in patent litigation simply do not have access to patent attorneys or agents, as patent prosecution groups are fairly uncommon in large general-practice or even litigation-focused firms. Also, litigators may lack familiarity with the seemingly byzantine rules of the USPTO.¹¹⁰ Indeed, it is no surprise that litigators generally feel more comfortable with the trial process and may prefer to take their chances with a jury or a judge rather than to combine forces with prosecutors, who must become involved because patent bar registration is required to practice before the USPTO. Moreover, reexaminations are specialized procedures that even many registered patent attorneys or agents are not fully comfortable with; the fact that *inter partes* reexaminations became available relatively recently does not help. In the meantime, the threat of litigation estoppel always lurks in the background,¹¹¹ putting a great deal of pressure on conducting the reexamination correctly. A protracted trial, where mistakes are perhaps more likely to be forgiven, might begin to look like a more attractive option.

2. Advantages of *Inter Partes* Reexamination

Although the *inter partes* procedure certainly has its drawbacks, such as limitations on the types of allowable grounds for challenging patent validity discussed above,¹¹² it also offers a number of advantages over litigation. Perhaps the most important advantage is the absence of the statutory presumption of validity accorded to the USPTO's initial allowance of a patent, which attaches in litigated cases.¹¹³ Given that the USPTO apparently grants a large number of questionable patents,¹¹⁴ commentators have called for abolishing the presump-

mately been quite successful, though a BPAI disposition on one of the reexaminations is currently on appeal to the Federal Circuit. See Scott A. McKeown, *NTP Patent Reexamination Appeals Heard Today at CAFC*, PATENTS POST-GRANT (Feb. 10, 2011), <http://www.patentspostgrant.com/lang/en/2011/02/ntp-patent-reexamination-appeals-heard-today-at-cafc>.

¹¹⁰ Personal Communication with Rahul Pathak, *supra* note 81.

¹¹¹ See *supra* note 93 and accompanying text.

¹¹² See *supra* note 100 and accompanying text.

¹¹³ See 35 U.S.C. § 282 (2006).

¹¹⁴ See generally Lemley & Sampat, *supra* note 52.

tion of validity.¹¹⁵ Nevertheless, the presumption, “which requires that a patent be proven invalid by ‘clear and convincing evidence,’”¹¹⁶ remains in force, though the Supreme Court has recently taken up a case that might hold that the “clear and convincing” standard is inapplicable under some circumstances.¹¹⁷ Those opposed to removing the presumption argue that the USPTO deserves judicial deference because it is an agency entrusted with issuing patents. Thus, it is argued that the problem of improvidently granted patents should be solved *ex ante* by giving more resources to the USPTO, rather than an *ex post* by making the USPTO’s decisions easy to overturn in court.¹¹⁸ In any case, there is no presumption of validity in reexamination proceedings.¹¹⁹ Moreover, “the patent office can [even] find an issued patent invalid on reexamination based on the same prior art it considered during the initial examination.”¹²⁰ Finally, the quantum of evidence required to overturn the original determination is merely a preponderance of the evidence.¹²¹

Furthermore, the “broadest reasonable interpretation” standard generally applied by the USPTO in its determinations of claim scope leaves patentees more vulnerable to § 102 and § 103 challenges in reexaminations than in ana-

¹¹⁵ See, e.g., Christopher R. Leslie, *Patents of Damocles*, 83 IND. L.J. 133, 140 (2008); Doug Lichtman & Mark A. Lemley, *Rethinking Patent Law’s Presumption of Validity*, 60 STAN. L. REV. 45, 51 (2007).

¹¹⁶ See Chiang, *supra* note 57, at 581 (referencing cases applying the “clear and convincing evidence” standard).

¹¹⁷ Not even the 2010 version of the patent reform bill, generally seen as adverse to patent holders, had a provision striking the presumption of validity, as only cosmetic changes to 35 U.S.C. § 282 were proposed. See Patent Reform Act of 2010, S. 515, 111th Cong. at 102, available at <http://judiciary.senate.gov/legislation/upload/PatentReformAmendment.pdf>. However, the Supreme Court recently granted *certiorari* in a case where the defendant has challenged the “clear and convincing” standard for invalidating patent claims where the allegedly invalidating prior art was not considered by the examiner during prosecution. See *Microsoft Corp. v. i4i Ltd. P’ship*, No. 10-290, 2010 WL 3392402, at *1 (U.S. Nov. 29, 2010). Even if the Supreme Court changes the standard of proof, however, the statutory presumption of validity would remain.

¹¹⁸ Discussion with Peter Detkin in IP: Commercial Law class at Stanford Law School (Jan. 25, 2010).

¹¹⁹ Chiang, *supra* note 57, at 579 (“[T]he accused infringer contests validity on equal ground—there is no presumption of validity.”).

¹²⁰ *Id.* at 581 (citing 35 U.S.C. § 312(a)). In contrast, even if the *Microsoft* case comes out against the “clear and convincing” standard for invalidating patent claims based on newly discovered prior art, that standard would remain in force for prior art that was already considered. See *supra* note 117 and accompanying text.

¹²¹ Chiang, *supra* note 57, at 581.

logous challenges under the same statutory provisions in litigated cases.¹²² The broader the claims are considered to be, the more likely they are to sweep in prior art and therefore fail on anticipation or obviousness grounds.¹²³ Additionally, commentators have noted that the USPTO is more likely than juries to apply correctly the legal standard for determining obviousness against patent owners.¹²⁴ At trial, it may be difficult to convince a lay jury that an infringing product “would have been obvious . . . to a person having ordinary skill in the art.”¹²⁵ Expert decision-makers of the USPTO, however, may be more inclined to apply the standard stringently, without sympathy or deference to the “wronged” patent owner.¹²⁶ Another advantage of the reexamination route is the absence of a requirement for discovery into the accused product.¹²⁷ As Tun-Jen Chiang further observed, “the only relevant materials in an *inter partes* reexamination are those pertaining to validity, such as prior art publications and patents. The functionality of the accused product is not at issue. . . . [T]he duty of candor applies only to the patent owner, not the accused infringer.”¹²⁸

¹²² *Id.* at 581–82. See also *In re Suitco Surface, Inc.*, 603 F.3d 1255, 1259 (Fed. Cir. 2010) (explaining the proper application of the broadest reasonable interpretation standard in a reexamination proceeding); Dawn-Marie Bey & Christopher A. Cotropia, *The Unreasonableness of the Patent Office’s “Broadest Reasonable Interpretation” Standard*, 37 AIPLA Q.J. 285, 294–97 (2009) (criticizing the standard as ambiguous and in conflict with the patent statutes). In district court cases, parties litigate disputed claim construction issues before the judge, as required under *Markman v. Westview Instruments, Inc.*, 52 F.3d 967 (Fed. Cir. 1995) (en banc), *aff’d*, 517 U.S. 370 (1996). See Bey & Cotropia, *supra*, at 303.

¹²³ Chiang, *supra* note 57, at 581. Note that *inter partes* reexaminations are often used precisely for this purpose: “[t]hird parties generally seek reexamination to remove the threat posed by a patent they believe to be demonstrably overbroad.” Gardella & Berger, *supra* note 108, at 387.

¹²⁴ Gardella and Berger, *supra* note 108, at 401 (noting that “an obviousness argument for invalidating a patent has traditionally had more success in the USPTO,” with the caveat that the recent Supreme Court decision in *KSR Int’l Co. v. Teleflex, Inc.*, 550 U.S. 398 (2007) may have changed this dynamic).

¹²⁵ 35 U.S.C. § 103.

¹²⁶ See Chiang, *supra* note 57, at 582–83; see also Gregory V. Novak, *Concurrent Reexaminations As a Patent Litigation Defense Tool*, in PATENT LITIGATION 2010, at 797, 805 (PLI Intellectual Prop., Course Handbook Series No. 24197, 2010), available at WL 1020 PLI/PAT 797 (“Obviousness issues are . . . frequently disfavored in litigation, but can be applied in reexamination without the same stigma attached.”).

¹²⁷ Chiang, *supra* note 57, at 582; Novak, *supra* note 126, at 805.

¹²⁸ Chiang, *supra* note 57, at 582 (citations omitted). Cf. *infra* note 207 (discussing whether the USPTO’s lack of power to order discovery makes the procedure inadequate for vindicating the policy of *Lear*).

Finally, although some commentators have decried the slow pace of *inter partes* reexamination proceedings,¹²⁹ they can often be faster, and are significantly less costly, than patent trials.¹³⁰ Strategically, of course, a party accused of patent infringement may sometimes prefer a protracted trial in order to bury the patent owner in litigation costs. As will be seen below in Part III, however, such strategic behavior, particularly in the patent licensing context, is undesirable from a policy perspective.¹³¹ Given that the amendment to the Patent Act including the *inter partes* reexamination provision was originally titled “Patent Litigation Reduction Act,”¹³² it stands to reason that the procedure can be a preferable, low-cost substitute for patent litigation.¹³³ There is no clear indication that the USPTO systematically favors patent owners in reexaminations,¹³⁴ which

¹²⁹ See, e.g., Scott M. Daniels & Kate Addison, *Why Wait for Oppositions?*, 47 IDEA 343, 358 (2007).

¹³⁰ See generally James Bessen & Michael J. Meurer, *Lessons for Patent Policy from Empirical Research on Patent Litigation*, 9 LEWIS & CLARK L. REV. 1, 2–6 (2005) (detailing the high costs of patent litigation); see also Chiang, *supra* note 57, at 579 (“Versus litigation, *inter partes* reexamination is a much less costly method of contesting validity.”); Novak, *supra* note 126, at 797 (“[S]ince the inception of the Central Reexamination Unit (CRU), reexamination proceedings are producing favorable results in a more timely manner.”).

¹³¹ See MPEP § 2686.04 (noting that “Congress desired that the creation of an *inter partes* reexamination option would lead to a reduction in expensive patent litigation”).

¹³² See Tremesha S. Willis, Note, *Patent Reexamination Post Litigation: It’s Time To Set the Rules Straight*, 12 J. INTEL. PROP. L. 597, 603 n.63 (2005) (“The object of the new law was to ‘reduce expensive patent litigation in U.S. district courts by giving third-party requesters, in addition to the existing *ex parte* reexamination in Chapter 30 of title 35, the option of *inter partes* reexamination proceedings in the PTO.’” (quoting 145 Cong. Rec. E1788, E1789–90 (1999))).

¹³³ See also Wayne B. Paugh, *The Betrayal of Patent Reexamination: An Alternative to Litigation, Not a Supplement*, 19 FED. CIRCUIT B.J. 177, 222 (2009) (“It is well-known that Congress and the patent community expected *inter partes* reexamination to be a more attractive alternative to litigation . . .” (citing Mark D. Janis, *Inter Partes Patent Reexamination*, 10 FORDHAM INTEL. PROP. MEDIA & ENT. L.J. 481, 498 (2000))).

¹³⁴ See *supra* notes 106–09 and accompanying text. To be sure, it is possible that the large number of patents invalidated or narrowed in reexamination proceedings may be due to a selection bias—challengers may not initiate *inter partes* proceedings unless they decide that they have a good chance of succeeding. Nevertheless, the significantly greater percentage of patents narrowed or invalidated in *inter partes* challenges versus that of patents invalidated in district court actions tends to support the inference of the lack of pro-patentee bias. See *supra* note 107. The comparison is complicated by the fact that most patent validity disputes occur in the course of infringement suits initiated by patent owners; as discussed above, many accused infringers may not have a colorable challenge to the validity of asserted patents. Though often caused by a threat of an infringement action, *inter partes* reexaminations must be initiated by third parties who presumably have a validity challenge worth bringing.

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suggests that the procedure is an acceptable route for vindicating the public interest of eliminating improvidently granted patents. Indeed, the preceding discussion indicates that, while *inter partes* reexaminations certainly have their drawbacks, they also offer significant advantages over validity challenges in district courts.¹³⁵

C. *A Preliminary Note on Federal Preemption*

The discussion so far lends credence to the proposition that *inter partes* reexaminations, like declaratory judgment actions challenging patent validity, provide an adequate avenue for attacking bad patents. Although the procedure has significant limitations (e.g., the “patents or printed publications” restriction and the litigation estoppel provision),¹³⁶ so does the litigation route (e.g., the presumption of validity and high costs). Because Congress adopted *inter partes* reexaminations to reduce the volume of patent litigation, it is difficult to argue that the use of this administrative remedy disserves the federal policy interest of facilitating challenges to patent validity, as seen through the lens of *Lear* and *MedImmune*. There is a wrinkle in the argument, however. As the Manual of Patent Examining Procedure notes, “[Congress] nonetheless also provided in the statute that a court validity challenge and *inter partes* reexamination of a patent may occur simultaneously.”¹³⁷ Does this provision, when combined with the holdings of *Lear* and *MedImmune*, render contractual restrictions that make *inter partes* reexamination the licensees’ exclusive route for attacking patent validity unenforceable as preempted by federal law? In Part III.C, I analyze the rationales behind the two aforementioned Supreme Court cases and argue that reexamination-only clauses do not violate the policies announced in their holdings. Therefore, such terms may be enforceable, at least if limited to challenges based on published prior art (i.e., “patents or printed publications”).¹³⁸ Before I reach the question of preemption of reexamination-only clauses, however, I begin Part III by discussing threats to licensing relationships created by unfettered patent challenges and evaluate several approaches to this problem pro-

See *supra* note 91 and accompanying text. *But see generally* Mercado, *supra* note 83 (detailing the problem of reexamination requests of questionable merit).

¹³⁵ Of course, this comparison assumes that the challenge that the licensee wishes to bring is allowed by the reexamination statute. See *infra* Part III.C.2 for a detailed analysis of how licensing parties can tackle the issue of validity challenges that cannot be brought in reexamination.

¹³⁶ 35 U.S.C. §§ 301, 302, 315(c).

¹³⁷ MPEP § 2686.04 (emphasis in original).

¹³⁸ 35 U.S.C. § 301; see also *infra* Part III.C.2.

posed by other commentators. I conclude Part III by arguing that reexamination-only clauses are a creative licensing solution that should be suitable to both licensees and licensors.

III. PATENT LICENSING AFTER *MEDIMMUNE*: PROBLEMS AND REEXAMINATION-ONLY CLAUSES AS AN ENFORCEABLE SOLUTION

A. *MedImmune As a Potential Threat to Licensing Relationships*

The *MedImmune* case arose out of a dispute over a license agreement involving the so-called “Cabilly II” patent belonging to Genentech.¹³⁹ The 1997 agreement covered both an existing Genentech patent and a “patent application relating to ‘the coexpression of immunoglobulin chains in recombinant host cells’”¹⁴⁰ that issued as the Cabilly II patent in 2001. Once the patent was granted, Genentech notified MedImmune that Synagis, a drug manufactured by MedImmune and “used to prevent respiratory tract disease in infants and young children,”¹⁴¹ was a “Licensed Product” covered by the 1997 agreement. MedImmune therefore owed royalties on sales of this very successful monoclonal antibody drug.¹⁴² MedImmune disagreed, “believing that the Cabilly II patent was invalid and unenforceable, and that its claims were in any event not infringed by Synagis.”¹⁴³ Nevertheless, MedImmune continued to make its royalty payments “under protest,” instead of ceasing the payments and “risk[ing] a potential injunction, treble damages, and attorney’s fees”¹⁴⁴ that might have resulted if Genentech successfully sued it for patent infringement and proved willfulness. Under prior Federal Circuit case law, no case or controversy within the meaning of Article III existed on these facts, since the presence of a license that was not yet breached removed the “reasonable apprehension of suit” required to

¹³⁹ See also Liza Vertinsky, *Reconsidering Patent Licensing in the Aftermath of MedImmune*, 45 HOU. L. REV. 1609, 1613–15 (analyzing the factual background of *MedImmune*).

¹⁴⁰ *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 121 (2007) (citing the Genentech-MedImmune license agreement).

¹⁴¹ *Id.*

¹⁴² Matthew Herper, *Is There a Hidden Value in MedImmune?*, FORBES.COM (Feb. 6, 2004), http://www.forbes.com/2004/02/06/cx_mh_0206medimmune.html (“In June 1998, MedImmune hit the biotech jackpot when the Food and Drug Administration approved Synagis. . . . Pediatricians have snapped up the drug. In 2003, Synagis sales totaled \$849 million, helping push MedImmune’s total revenue past \$1 billion for the first time.”).

¹⁴³ *MedImmune*, 549 U.S. at 121–22.

¹⁴⁴ Vertinsky, *supra* note 139, at 1614.

maintain a justiciable declaratory judgment action.¹⁴⁵ The Supreme Court, however, explicitly rejected the Federal Circuit's "reasonable apprehension" test¹⁴⁶ and held that a justiciable controversy existed because MedImmune's "threat-eliminating behavior" of acceding to a license "was effectively coerced"¹⁴⁷ by the threat of a patent infringement lawsuit. Justice Thomas, the lone dissenter, criticized what he viewed as the Court's overly capacious view of coercion in the context of "private contractual obligations."¹⁴⁸ The majority, however, made it clear that a patent license could not be an automatic bar to a declaratory judgment suit for invalidity or non-infringement.¹⁴⁹ Through reached in a different factual context,¹⁵⁰ an influential Federal Circuit case interpreting *MedImmune* acknowledged that the Supreme Court decision mandated replacing the "reasonable apprehension" test with a "totality of the circumstances" test for determining whether sufficient coercion was present between the parties to permit a declaratory judgment suit to go forward.¹⁵¹ As discussed in the Introduction, although there are very few post-*MedImmune* cases featuring the precise factual scenario of the licensee-licensor dispute,¹⁵² the Supreme Court's concerns about coercion and its exhortation of the lower courts to examine the totality of the circumstances in deciding whether to grant declaratory judgment standing in patent cases, as well the actual outcome of *MedImmune*, all point to the conclusion that, in most cases, licensees should be able to clear this hurdle fairly easily.¹⁵³

The patent licensing community¹⁵⁴ and many academic commentators have approached the *MedImmune* decision with a great deal of discomfort.

¹⁴⁵ See *Gen-Probe Inc. v. Vysis, Inc.*, 359 F.3d 1376, 1379–82 (Fed. Cir. 2004), *overruled by MedImmune*, 549 U.S. at 121.

¹⁴⁶ *MedImmune*, 549 U.S. at 132 n.11.

¹⁴⁷ *Id.* at 129.

¹⁴⁸ *Id.* at 145 (Thomas, J., dissenting); see also Levine & Belle, *supra* note 33, at 501–06 (criticizing the *MedImmune* majority's "coercion" rationale); Sean M. O'Connor, *Using Stock and Stock Options To Minimize Patent Royalty Payment Risks After MedImmune v. Genentech*, 3 N.Y.U. J. L. & Bus. 381, 439–45 (2007) (same).

¹⁴⁹ Levine & Belle, *supra* note 33, at 533–34.

¹⁵⁰ See *supra* notes 33–34 and accompanying text.

¹⁵¹ *SanDisk Corp. v. STMicroelectronics, Inc.*, 480 F.3d 1372, 1377–83 (Fed. Cir. 2007).

¹⁵² Levine and Belle found one such district court case in their study. See *Linzer Prods. Corp. v. Sekar*, 499 F. Supp. 2d 540 (S.D.N.Y. 2007) (cited in Levine & Belle, *supra* note 33, at 522 n.212).

¹⁵³ See *supra* notes 33–38 and accompanying text.

¹⁵⁴ See, e.g., Toshihiro Kuwahara & Warren G. Lavey, *Drafting Strategies for Licensing Agreements After MedImmune Decision*, in JOSEPH YANG & IRA J. LEVY, *ADVANCED LICENSING AGREEMENTS 2008*, at 141 (PLI Intellectual Prop., Course Handbook Series No. G-927,

Summarizing the literature on the subject, Paul LaVanway argued that *MedImmune* may significantly impair licensee-licensor relationships:

The *MedImmune* decision will undoubtedly change licensing behavior. Some practitioners suggest that putative patent infringers will strategically accept a “coerced” license to avoid the treble damages associated with willful patent infringement and preserve the right to bring a declaratory judgment action. Others believe that *MedImmune* will change the way patent licenses are drafted and may increase licensing costs by incorporating risk premiums into the license for potential legal costs if validity or enforceability is later challenged.¹⁵⁵

Post-*MedImmune*, the increased facility with which licensees can attain declaratory judgment standing to sue for patent invalidity introduces greater uncertainty in licenses. Alienability of patent rights may become severely impaired due to that uncertainty and the expected concomitant increase in the prices of licenses brought about by the higher risk of litigation.¹⁵⁶ In the extreme case, parties may refuse to contract altogether, though one would imagine that a patent owner would prefer a license on bad terms to no license at all if it has no other way of monetizing the patent. Capturing the fundamental conflict between contract law and the policy of allowing facile challenges to patent validity by licensees, Kieff lamented that “*MedImmune* . . . seems to allow the licensee to challenge the patent while simultaneously holding the patentee to the rest of the deal.”¹⁵⁷ This state of affairs can become intolerable for a patent owner who is contemplating granting a license because it may come to believe that the license is not worth the paper it is written on.¹⁵⁸ This result is highly undesirable,

2008), available at WL 927 PLI/Pat 141; John W. Schlicher, *Patent Licensing, What To Do After MedImmune v. Genentech*, 89 J. PAT. & TRADEMARK OFF. SOC'Y 364, 374 (2007); Paul Dennis Connuck, *Patent Licensing Law Developments: Learning To Live with MedImmune—License Drafting Strategies*, KRAMER LEVIN INTELL. PROP. ALERT (Feb. 2007), http://www.kramerlevin.com/files/Publication/90feb428-7a04-4b42-84c8-0ff6e31dd214/Presentation/PublicationAttachment/601d27fe-6661-4c9a-9065-13182e53beaa/IP Patent_Medim_v3.pdf.

¹⁵⁵ Paul J. LaVanway, Jr., Note, *Patent Licensing and Discretion: Reevaluating the Discretionary Prong of Declaratory Judgment Jurisdiction After MedImmune*, 92 MINN. L. REV. 1966, 1978 (2008).

¹⁵⁶ See generally Dreyfuss & Pope, *supra* note 37; Risch, *supra* note 25.

¹⁵⁷ Beckerman-Rodau et al., *supra* note 38, at 24 (referring to the part of the article written by Professor Kieff).

¹⁵⁸ *Id.* Although the *MedImmune* rule applies to existing licensee-licensor relationships, the main concern articulated by Kieff is its *ex ante* effect on patent owners who contemplate licensing their patents. Kieff added that “[i]f one side of the deal can always get out, it is not worth much to the other side to be in the deal. One way renegotiation means no contract.” *Id.*

since patent licensing “is often necessary to develop follow-on technologies that advantage the public.”¹⁵⁹ As a potential solution, LaVanway called for federal courts to make greater use of the discretionary aspect of the declaratory judgment inquiry by, for example, declining jurisdiction more readily when the patentee-licensor is a small firm, which may be harmed more severely by litigation than a large firm.¹⁶⁰ But lines between small and large firms are difficult to draw, so that by advocating for greater discretion, LaVanway’s proposal may not cure the uncertainty in licensing relationships brought about by *MedImmune*.¹⁶¹

Another commentator, Michael Risch, described the effect of *MedImmune* and *Lear* as a “patent-challenge tax” that leads to “inflated royalties” and “causes trickle-down costs to consumers,” not to mention “disincentives to create and license patented technology.”¹⁶² This tax represents “social costs that offset the social benefits created by encouraging patent challenges.”¹⁶³ Within this framework, post-*MedImmune* contractual solutions should be evaluated according to their effectiveness in reducing the patent-challenge tax. The subsequent discussion addresses various tax-reducing solutions, including the reexamination-only solution proposed in this Article. Before describing the solutions, however, it is worth noting that the magnitude of the *MedImmune* problem remains unclear. One study found that “there has been no torrent of declaratory relief actions”¹⁶⁴ and its authors concluded that “*MedImmune*’s lack of limiting factors [on what constitutes a justiciable controversy] is of theoretical

¹⁵⁹ LaVanway, *supra* note 155, at 1998; *see also* Christian Chadd Taylor, Note, *No-Challenge Termination Clauses: Incorporating Innovation Policy and Risk Allocation into Patent Licensing Law*, 69 IND. L.J. 215, 228 (1993) (stating that “the [Supreme] Court declared . . . that ‘the policy of stimulating invention that underlies the entire patent system runs no less deep’ than the policy of free competition” (quoting *Dawson Chem. Co. v. Rohm & Haas Co.*, 448 U.S. 176, 221 (1980))).

¹⁶⁰ *See* LaVanway, *supra* note 155, at 1997; *see also supra* note 35 and accompanying text.

¹⁶¹ Given that *MedImmune* appears to place the burden of uncertainty on patent owners, it is interesting to note that the Declaratory Judgment Act was enacted in part to reduce risks placed on parties who feared that they would be sued for infringement: “[t]he legislative history shows that Congress was primarily concerned with the plight of parties confronted with uncertainties in their legal and business relations, but who had no resort to the courts because the other party possessed the cause of action.” Lisa A. Dolak, *Declaratory Judgment Jurisdiction in Patent Cases: Restoring the Balance Between the Patentee and the Accused Infringer*, 38 B.C. L. REV. 903, 910 (1997).

¹⁶² Risch, *supra* note 25, at 1004.

¹⁶³ *Id.*

¹⁶⁴ Levine & Belle, *supra* note 33, at 534. These authors speculate that “licensors may have simply avoided litigation through negotiation or strategic decision-making.” *Id.* at 524.

interest but is not deeply problematic.”¹⁶⁵ Similarly, Risch observed that “there are no reports of widespread patent challenges” and provided possible explanations for why this might be the case, but ultimately concluded that it is probably simply too early to analyze the effects of *MedImmune* as “technology covered by post-*MedImmune* licenses may not be sufficiently developed to warrant challenges yet.”¹⁶⁶ If the influence of *MedImmune* on litigation is difficult to assess, one imagines that it must even more challenging to measure the case’s impact on incentives to innovate.¹⁶⁷ One thing is certain: licensees are concerned about *MedImmune* and some have already adjusted their licensing strategies to account for the new rule.¹⁶⁸ These reports suggest that *MedImmune* has had a tangible impact on the licensing community, so that additional approaches to managing the patent-challenge tax are worth exploring.¹⁶⁹

**B. Toward a Private Law Solution to the MedImmune Problem:
Termination and Arbitration**

1. Termination-on-Challenge Clauses

Dreyfuss and Pope suggested that problems created by *MedImmune* may be resolved by contracting parties themselves using creative licensing solutions.¹⁷⁰ One approach is a termination-on-challenge clause, which “entitl[es] the licensor to terminate the license agreement if the licensee challenges the

¹⁶⁵ *Id.* at 536.

¹⁶⁶ Risch, *supra* note 25, at 1019–20 n.90.

¹⁶⁷ See Vertinsky, *supra* note 139, at 1625–32, 1650–53 (building a model that takes account of the various factors that might impact incentives to innovate).

¹⁶⁸ See, e.g., *Stanford Adds New Clauses to License Agreements in Wake of MedImmune Case*, TECH TRANSFER BLOG (June 4, 2008), <http://www.technologytransfertactics.com/content/2008/06/04/stanford-adds-new-clauses-to-license-agreements-in-wake-of-medimmune-case> (cited in Dreyfuss & Pope, *supra* note 37, at 989 n.86).

¹⁶⁹ See also Victor DeGyarfas, *Patent Licensing and Declaratory Judgment Actions After MedImmune*, FOLEY & LARDNER PUBLICATIONS, at *1, *14 (2009), http://www.foley.com/files/tbl_s31Publications/FileUpload137/5026/deGyarfas-Paper.pdf (finding that “[s]ome patent licensing entities have felt the impact of *MedImmune* and appear to be engaging in a ‘sue first—ask questions later’ policy” and concluding that “an unintended consequence of *MedImmune* may be an increase in the number of patent infringement suits filed by licensing entities who seek to insure that if litigation ensues it will be in what is perceived to be a favorable forum”).

¹⁷⁰ See Dreyfuss & Pope, *supra* note 37, at 991–1006.

validity of a patent.”¹⁷¹ This solution “would fully restore the parties to the pre-*MedImmune* situation”¹⁷² in that licensees would no longer be able to take advantage of their contractual rights while challenging the subject matter of the contract. The question arises, however, whether a solution could be devised that would do a better job of fostering licensing relationships than the regime of facile license termination. As a general matter, public policy disfavors contract breakdown, as contracts are thought to increase overall social welfare by encouraging productive specialization and providing a private-ordering mechanism for transferring resources into the hands of those who value them most.¹⁷³ The doctrines of material breach¹⁷⁴ and substantial performance¹⁷⁵ reflect the strong norm that the law should not hand contracting parties a pretext for facile exit from their relationships or a ready excuse not to perform on the contract. Thus, a contracting party must be given an opportunity to cure its breach, and the breach itself must be material, before performance of the other party is excused.¹⁷⁶ Some cases have further held, controversially so, that completed performance that is not quite to the letter of the contract, but close enough,¹⁷⁷ does not always excuse the other party’s contractual obligations.¹⁷⁸

To be sure, licensees’ challenges to patent validity can seriously impair contract-based relationships. It is not clear, however, that terms allowing for

¹⁷¹ *MedImmune v. Genentech: A Dilemma Removed for Patent Licensees*, COOLEY LLP CLIENT ALERTS, (Feb. 15, 2007), <http://www.cooley.com/58416>. This alert states that it is not clear whether such clauses sufficiently encumber the *Lear* policy as to render the clauses unenforceable. *Id.*; see also Risch, *supra* note 25, at 1031 (“[termination] provision’s enforceability is unsettled” (citing Kuwahara & Lavey, *supra* note 154, at 159)).

¹⁷² Dreyfuss & Pope, *supra* note 37, at 1003. These authors maintained that, for maximum advantage to the licensee, the clause should be styled as an “option to terminate.” *Id.* at 1004.

¹⁷³ As noted in a classic treatise, there exists “a fairly strong sense that the law should do what it reasonably can to prevent or deter the break-down of contract relations.” CHIRELSTEIN, *supra* note 16, at 143.

¹⁷⁴ See *id.* at 143–49 (discussing the doctrine of material breach).

¹⁷⁵ See *id.* at 136–40 (discussing the doctrine of substantial performance).

¹⁷⁶ See RESTATEMENT (SECOND) OF CONTRACTS § 237 (stating that the absence of “uncured material failure” is a condition of performance) (emphasis added); CHIRELSTEIN, *supra* note 16, at 144 (“If the obligor’s failure to perform is not ‘material’ in character . . . the injured party is required to continue performance but may claim damages for whatever loss has been sustained.”).

¹⁷⁷ See, e.g., *Jacob & Youngs, Inc. v. Kent*, 129 N.E. 889, 891 (N.Y. 1921) (holding that the defendant’s contractual obligation to pay the plaintiff for work which did not perfectly comply with the contractual stipulations was not excused); *supra* note 175 and accompanying text.

¹⁷⁸ Contrast this approach with the perfect tender rule. See CHIRELSTEIN, *supra* note 16, at 140–43 (discussing the perfect tender rule).

immediate license termination upon challenge of validity are the right response, since the license can still have a great deal of value to both parties (and to the society as a whole) if the patent's validity is affirmed. Dicta from *MedImmune* appear to support the view that a validity challenge does not necessarily justify contract termination by the licensor:

[The licensee] is not repudiating or impugning the contract while continuing to reap its benefits Rather, it is asserting that the contract, properly interpreted, does not prevent it from challenging the patents, and does not require the payment of royalties because the patents . . . are invalid.¹⁷⁹

Of course, the story changes when a termination-on-challenge clause becomes a part of the contract, since such a term reflects the parties' *ex ante* determination that a validity challenge is a breach serious enough to justify the breakdown of the license. The termination right is now a part of the licensor's bundle of rights under the contract,¹⁸⁰ and the licensee must decide whether maintaining the license would be valuable even when serious doubts develop about validity of the licensed patents.¹⁸¹ Nevertheless, termination-on-challenge clauses may not be consonant with contract law doctrines driven by the goal of preserving contractual relationships.¹⁸² Given the private and social value of patent licenses, a solution that preserves such contracts even in the face of licensee attacks on the patent is preferable.¹⁸³ Furthermore, commentators have maintained that termination-on-challenge clauses may encumber the licensees' ability to challenge patent validity to such a degree¹⁸⁴ as to contravene the feder-

¹⁷⁹ *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 135 (2007) (citations omitted).

¹⁸⁰ See David M. Treadway, Comment, *Has the Supreme Court Forgotten the Patentee? Recent Patent Licensing Decisions Contradict Patent Policy, Harm Licensors, and Alter Negotiations*, 33 U. DAYTON L. REV. 303, 329 (2008) ("Parties are capable of defining various reasons for termination, and so long as they agree to them by contract, they are bound by those terms.").

¹⁸¹ For example, when the license is an exclusive one, it may not be advisable for licensees to attempt to invalidate the patent, since placing the invention in the public domain would increase competition. Moreover, "[a]s the value of the licensed product increases, the licensee's cost of termination increases." Risch, *supra* note 25, at 1030.

¹⁸² See *supra* notes 173–78 and accompanying text.

¹⁸³ Again, however, one must account for the counterargument that the existence of a termination-on-challenge clause can serve as a tool that helps deter contract breakdown in the first place. The author gratefully acknowledges Professor Dreyfuss for bringing up this point and agrees with it. The author maintains, however, that on balance such clauses are disfavored as a matter of public policy and contract doctrine for the reasons stated in this paragraph and the preceding one.

¹⁸⁴ See *supra* note 171 and accompanying text. *But see* Taylor, *supra* note 159, at 221–25 (arguing that termination-on-challenge clauses are enforceable in spite of *Lear*).

al policy of furthering “public interest in free access to technology in the public domain.”¹⁸⁵ Finally, license termination is likely to be followed by expensive patent infringement litigation—the very outcome that the contracting parties presumably sought to avoid when they agreed to a license.¹⁸⁶

2. Arbitration Clauses

Among the various responses to *MedImmune*, arbitration clauses, which help prevent rather than permit contract breakdown, fall on the end of the spectrum opposite termination-on-challenge clauses. Licenses that include arbitration terms, “instead of leaving the licensee free to challenge the patent in court as contemplated by *Lear* and *MedImmune* . . . would . . . [require the licensee] to arbitrate.”¹⁸⁷ A major advantage of arbitration is that it is significantly less costly than litigation.¹⁸⁸ From the point of view of the patent owner worried about invalidation of its patent, arbitral resolution of patent validity is desirable because the arbitrator’s decision does not have the force of collateral estoppel.¹⁸⁹ Since the Patent Act explicitly provides for voluntary arbitration as a permissible means of resolving patent disputes, arbitration clauses do not, on the surface, appear to contravene federal law. As Dreyfuss and Pope observed, however, it is difficult to reconcile contract provisions that restrict licensees to binding arbitration as the *exclusive* route for challenging patent validity with the holding of *Lear*: “*Lear*’s goal of putting advances that should not be patented into public domain will be frustrated.”¹⁹⁰ While arbitration-only terms are not so draconian

¹⁸⁵ J. William Dockrey, *Licensee Estoppel: Coping with the Licensee’s Dilemma*, USEBRINKS PUBLICATIONS AND ARTICLES (Dec. 2003), http://www.brinkshofer.com/resource_center/63-licensee-estoppel-coping-licensees-dilemma (explaining why the *Lear* Court abrogated the doctrine of licensee estoppel).

¹⁸⁶ M. Natalie Alfaro, Comment, *Barring Validity Challenges Through No-Challenge Clauses and Consent Judgments: MedImmune’s Revival of the Lear Progeny*, 45 HOUS. L. REV. 1277, 1305 (2008) (noting, after discussing termination-on-challenge clauses, that “[w]hatever the manner in which licensing parties choose to ‘contract around’ *MedImmune* and *Lear*, changes in drafting will inevitably result in an increase in litigation”). I argue that, with the aid of reexamination-only clauses, litigation is perhaps not inevitable.

¹⁸⁷ Dreyfuss & Pope, *supra* note 37, at 999.

¹⁸⁸ See David A. Allgeyer, *In Search of Lower Cost Resolution: Using Arbitration To Resolve Patent Disputes*, 12 CONFLICT MGMT. 9 (2007).

¹⁸⁹ See 35 U.S.C. § 294(c) (2006); *cf.* *Blonder-Tongue Labs., Inc. v. Univ. of Ill. Found.*, 402 U.S. 313, 350 (1971) (holding that a court’s final judgment of patent invalidity has the effect of collateral estoppel even in the absence of mutuality of the parties).

¹⁹⁰ Dreyfuss & Pope, *supra* note 37, at 1001. Note that the arbitration provision of the Patent Act allows for the possibility that arbitration clauses can be held unenforceable. 35 U.S.C.

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as to “muzzle” licensees completely, they do destroy the ability of licensees to act as private attorneys general to correct the USPTO’s mistakes for the benefit of the public. Furthermore, since arbitrators’ decisions are generally confidential¹⁹¹ and very difficult to overturn on appeal,¹⁹² other parties may not gain access to the information that spurred the arbitration proceeding. But perhaps the best argument against enforceability of contractual provisions that limit licensees to the arbitration route is that a specialized administrative procedure, reexamination by the USPTO, already exists for resolving validity disputes outside the federal courts. Canvassing arguments against arbitral resolution of patent disputes, Smith and co-authors noted:

[T]he laws of a state entrust a specific court or administrative agency with exclusive jurisdiction over certain types of patent disputes. Thus, if an arbitral award is given the effect of a court (or administrative) judgment, arbitration of infringement or validity issues derogates the exclusive jurisdiction of the state body entrusted with these issues.¹⁹³

While arbitration is certainly an allowable route under the Patent Act for resolving patent validity disputes between parties, two governmental entities—one judicial,¹⁹⁴ the other administrative¹⁹⁵—already have specific jurisdictional grants to adjudicate patent validity. A contract that completely forecloses both of these public federal fora in favor of arbitration not only conflicts with federal patent policy under *Lear*, but also seems to undermine the authority and effectiveness of the USPTO by eliminating the agency’s jurisdiction and preventing public review of its work in cases that end up in arbitration. In other contexts, the Supreme Court affirmed strong federal policy favoring arbitration¹⁹⁶ but cau-

§ 294(a) (“Any such provision or agreement shall be valid, irrevocable, and enforceable, except for any grounds that exist at law or in equity for revocation of a contract.”). Federal policy articulated in *Lear* can thus render arbitration provisions unenforceable in some cases.

¹⁹¹ Dreyfuss & Pope, *supra* note 37, at 999–1000.

¹⁹² *See Flex-Foot, Inc. v. CRP, Inc.*, 238 F.3d 1362, 1365 (Fed. Cir. 2001). This case notes that a district court generally may only vacate an arbitration award if there were “(1) fraud in procuring the award; (2) partiality on the part of the arbitrators; (3) gross misconduct by the arbitrators; and (4) the failure of the arbitrators to render a mutual, final, and definite decision.” *Id.* (citing 9 U.S.C. § 10 (1994)).

¹⁹³ M. A. Smith et al., *Arbitration of Patent Infringement and Validity Issues Worldwide*, 19 HARV. J.L. & TECH. 299, 306 (2006).

¹⁹⁴ The judicial entity consists of the federal district courts. 28 U.S.C. § 1338 (2006) (assigning original and exclusive jurisdiction to district courts in patent cases).

¹⁹⁵ The administrative agency is the USPTO. 35 U.S.C. §§ 302, 303 (assigning reexamination jurisdiction to the USPTO).

¹⁹⁶ *See, e.g., Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24–25 (1983).

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tioned that, as a general matter, private agreements to arbitrate do not completely preempt related agency action.¹⁹⁷ In view of these considerations, courts will likely find “arbitration-only” clauses in patent licenses to be unenforceable.¹⁹⁸

C. *The Reexamination-Only Solution: The Best of Both Worlds?*

1. **Reasons for Probable Enforceability of Reexamination-Only Clauses**

This Article proposes that reexamination-only clauses will help contracting parties reduce the costs of the rules announced in *MedImmune* and *Lear* without violating those rules, a result that would help alleviate the policy concerns detailed above in Part III.A.¹⁹⁹ Unlike termination-on-challenge clauses,²⁰⁰ reexamination-only provisions would enable licensees and licensors to maintain their contractual relationships and avoid costly litigation if the claims are challenged and adjudicated valid.²⁰¹ Indeed, reexamination procedures share the advantage of arbitrations in that they are cheaper than litigation,²⁰² but they also provide for public airing of licensee concerns over questionable patents. If the USPTO invalidates wrongly issued claims, the validity challenge would have the salutary effect of fostering “free competition in ideas which do not merit patent protection.”²⁰³ Similar to invalidity judgments in district courts, claim

¹⁹⁷ *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28–29 (1991).

¹⁹⁸ *See supra* note 190 and accompanying text. Fully paid-up royalty payments and other proposed post-*MedImmune* solutions, such as consent judgments, have their own drawbacks. *See, e.g.*, Dreyfuss & Pope, *supra* note 37, at 992–99; Risch, *supra* note 25, at 1024–42. For another interesting method to mitigate licensees’ risks, using stocks and stock options, *see O’Connor, supra* note 148.

¹⁹⁹ This Part primarily addresses enforceability of reexamination-only clauses under *Lear*. The Conclusion, Part IV, explains in more detail how this solution helps resolve utilitarian concerns discussed in Part III.A and meets common-law norms addressed in the Introduction. For now, it is assumed that reexamination-only clauses offer the same kinds of advantages to licensing parties as arbitration-only clauses, as noted in the text.

²⁰⁰ *See supra* Part III.B.1.

²⁰¹ The same result (continuation of the licensing relationship and likely avoidance of litigation) would obtain if the USPTO narrowed the claims but the licensee’s product would still clearly fall within their scope. For a more complicated scenario, where claims are narrowed and it is no longer clear whether the licensed product falls within their scope, *see infra* notes 262–63 and accompanying text. If the relevant claims are completely cancelled in reexamination, litigation is also avoided since the license is no longer enforceable, and the contractual relationship ends.

²⁰² *See supra* note 130 and accompanying text.

²⁰³ *Lear, Inc. v. Adkins*, 395 U.S. 653, 656 (1969).

cancellations or amendments in reexamination raise non-mutual collateral estoppel against the patent owner (i.e., the originally issued claims become ineffective not only as between the parties, but also as to the rest of the world).²⁰⁴ Listing various possible contractual clauses that may help licensors protect themselves after *MedImmune*, David Treadway contended that “[one] benefit of . . . [the reexamination] clause is that it would be hard to imagine a court deciding that it violates *Lear*. In fact, options like reexamination were not available when *Lear* was decided”²⁰⁵ Indeed, although the *Lear* Court sought to preserve the licensees’ right to challenge patent validity in district courts, language in the opinion nevertheless suggests that the Court would have been comfortable with the *inter partes* reexamination alternative:

A patent, in the last analysis, simply represents a legal conclusion reached by the Patent Office. Moreover, the legal conclusion is predicated on factors as to which reasonable men can differ widely. Yet the Patent Office is often obliged to reach its decision in an *ex parte* proceeding, without the aid of the arguments which could be advanced by parties interested in proving patent invalidity.²⁰⁶

In reaching its conclusion to abrogate licensee estoppel, the *Lear* Court was clearly troubled by the nature and dynamics of patent prosecution, as it is a system in which one interested party, the patent applicant, controls the flow and presentation of information to the USPTO. *Inter partes* reexaminations address these concerns by enabling third-party requesters to play an active role in the process of reviewing disputed patent claims.²⁰⁷ Crucially, requesters may challenge claim amendments upon issuance of non-final office actions and appeal examiners’ findings to other administrative and judicial tribunals.²⁰⁸ As with

²⁰⁴ See 35 U.S.C. § 307(b); see also *supra* note 189 and accompanying text.

²⁰⁵ Treadway, *supra* note 180, at 331. Of course, the Court could have objected to the reexamination procedure as insufficient to vindicate the public interest because of the limited grounds on which validity challenges can be brought. This objection is addressed in detail in Part III.C.2.

²⁰⁶ *Lear*, 395 U.S. at 670; see also Mark A. Lemley & Carl Shapiro, *Probabilistic Patents*, 19 J. ECON. PERSPECTIVES 75 (2005) (highlighting the uncertain nature of patent rights).

²⁰⁷ That said, the only forum actually blessed by the *Lear* court was that of the district court. Even putting the issue of limited grounds for challenging validity, which I address in Part III.C.2, to one side, one can still make a plausible argument that the USPTO is not an adequate forum for vindicating the public interest under the reasoning of *Lear*. For example, the USPTO lacks subpoena power and cannot order discovery. The author thanks Professor Chiang for these points. The discussion below, however, reflects the author’s view that there are also reasons to believe that *Lear* would have blessed the *inter partes* reexamination route had it been available in 1969.

²⁰⁸ See *supra* notes 79–82 and accompanying text.

patent prosecution generally, arguments made in reexaminations are available publicly and become a part of a patent's prosecution history, which can raise an estoppel in future litigation.²⁰⁹ The resulting buildup of public record helps encourage parties to make careful and accurate arguments, reducing the possibility that the USPTO will make incorrect validity determinations due to misleading or incomplete information.

Indeed, the *inter partes* proceeding has the advantage over standard patent prosecution in that the USPTO's validity determinations are made in a process that has unmistakably adversarial features; further, its relatively low costs may make it preferable to litigation from the viewpoint of public policy.²¹⁰ As extensive discussion above indicates, there is no reason to believe that *inter partes* reexaminations are somehow inadequate or deficient relative to judicial determinations of patent validity.²¹¹ As discussed above in Part II.B.2, *inter partes* reexaminations arguably subject the USPTO's initial findings to more stringent review than district court trials due to the absence of the presumption of validity and the USPTO's application of the broadest reasonable interpretation standard to the challenged claims. Barriers to widespread use of *inter partes* reexaminations may be largely cultural or psychological, given the relative novelty of the procedure and doubts that the USPTO can effectively correct its own errors.²¹² For licenses on patents issued on the basis of applications filed after November 29, 1999, for which *inter partes* procedures are available,

²⁰⁹ See, e.g., *Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co.*, 535 U.S. 722, 722 (2002).

²¹⁰ Farrell and Merges have argued that litigation might not in many cases produce correct decisions on patent validity because of financial disparities and asymmetric incentives of the litigating parties. See Joseph Farrell & Robert P. Merges, *Incentives To Challenge and Defend Patents: Why Litigation Won't Reliably Fix Patent Office Errors and Why Administrative Review Might Help*, 19 BERKELEY TECH. L.J. 943, 948–960 (2004). In the cheaper reexamination setting, these authors' concern that money will affect legal outcomes becomes less salient. Although Farrell and Merges did not believe that the *inter partes* reexamination system was sufficiently attractive for challengers to replace litigation, *id.* at 967, it is worth noting that the article was published in 2004, only two years after the most recently amended reexamination statutes became law and at a time when reexaminations were still viewed with extreme suspicion. See also *supra* Part II.B.

²¹¹ In spite of all of these reasons, it is not doubted that, in some cases, reexamination-only clauses would force licensees to go to the UPSTO even though they might come to believe that a district court would be a better forum for challenging the validity of a particular patent on the basis of a patent or a printed publication. The discussion proceeds on the assumption that this scenario (i.e., licensee had first agreed to bind itself to the *inter partes* route, but later decided that it prefers a district court) does not describe a case where the licensee's right to challenge the patent is so burdened as to make the reexamination-only clause unenforceable under *Lear*.

²¹² See *supra* Part II.B.

clauses making such reexaminations the exclusive route for resolving doubts about patent validity may be a workable solution.²¹³ Subject to certain possible refinements, such clauses have a chance of being enforceable under *Lear* because *inter partes* validity challenges by licensees may police the public domain as effectively, if not more so, than challenges in district courts.²¹⁴

As noted above, the reexamination statute explicitly allows for concurrent reexamination and litigation in district courts.²¹⁵ Consequently, it is valid to ask whether reexamination-only clauses would frustrate the federal policy of allowing both of these routes to attack potentially invalid patents. Indeed, litigation and *inter partes* reexamination where the third-party requester is one of the litigants often take place simultaneously.²¹⁶ Can licensing parties really contract themselves out of this scheme, “opt[ing] out of the distribution of rights established by patent law”?²¹⁷ Mark Lemley argued that “the law of preemption is a mess”²¹⁸ and “[t]he result is that it is difficult to predict the precise contours of federal patent preemption.”²¹⁹ Even under a strong preemption theory, however, it is difficult to see how reexamination-only clauses could be rendered unenforceable due to a conflict with federal patent policy.²²⁰ After all, an expert federal decision-making body—the USPTO—remains in the game, empowered to make determinations of claim validity and to fashion precise responses to third-party challenges by allowing amended claims.²²¹ The reexamination statute itself provides for stays of litigation pending reexamination proceedings, suggesting a great degree of deference to the USPTO in the statutory scheme.²²² This deference is consistent with the Supreme Court’s view that Executive Branch agencies are generally adequate for resolving issues that may otherwise be litigated in Article III courts,²²³ provided that (1) utilization of the administrative deci-

²¹³ Of course, reexaminations can be a good compromise only so long as the reexamination statute allows the specific challenge to patent validity that the licensee wishes to bring. See *infra* Part III.C.2.

²¹⁴ See *supra* Part II.B.2.

²¹⁵ See *supra* Part II.C.

²¹⁶ See generally Sterne et al., *supra* note 94.

²¹⁷ Mark A. Lemley, *Beyond Preemption: The Law and Policy of Intellectual Property Licensing*, 87 CAL. L. REV. 111, 137 (1999).

²¹⁸ *Id.* at 115.

²¹⁹ *Id.* at 139.

²²⁰ See *supra* notes 48–50 and accompanying text.

²²¹ See *supra* note 195 and accompanying text.

²²² See 35 U.S.C. § 318.

²²³ See, e.g., *Commodity Futures Trading Comm’n v. Schor*, 478 U.S. 833, 833 (1986).

sion-maker is justified by efficiency considerations, and (2) its determinations can be appealed to an Article III forum (here, it is the Court of Appeals for the Federal Circuit, which takes appeals from the BPAI).²²⁴ In the patent licensing context, the value of an administrative resolution is at its height, since the parties have entered into a license agreement presumably to avoid costly litigation.²²⁵ Enforcement of reexamination-only clauses would honor the parties' apparent wishes to stay out of court, while preserving the federal forum of the USPTO for resolving questions of patent validity. The availability of such a forum militates against the conclusion that these contractual clauses are in conflict with, and are unenforceable, due to federal preemption.²²⁶ Indeed, the reexamination statute does not mandate but simply allows concurrent litigation and reexamination.²²⁷

Finally, *MedImmune* explicitly left open the possibility that licensees and licensors may contract for a prohibition of certain types of validity challenges. In buttressing its conclusion that a license, by itself, does not constitute a promise never to challenge patent validity, and thus cannot immunize the licensor from a declaratory judgment action, the Court simply said that "it is not

²²⁴ See 35 U.S.C. § 315.

²²⁵ Notably, commentators have argued that high litigation costs may prevent that the *Lear* policy from being vindicated:

Litigation costs to invalidate . . . unwarranted patents also exacerbate welfare losses due to imperfect or asymmetric information. A patentee, holding a patent that could be invalidated in post-issuance litigation, may decide to set a license fee that is lower than the cost of litigation (*i.e.*, a sub-litigation cost license fee). A potential infringer, not wishing to bear the risk and costs of litigation, may pay the license fee for an unenforceable patent. As long as the costs of litigation and information acquisition for other infringers are significant, a patentee may continue to collect several small license fees. . . . [O]ne of the determinants of the probability that a patent will be challenged is the size of the stakes, which corresponds to the license fee. High license fees will make the costs of litigation and prior art retrieval worthwhile for potential infringers. Low license fees, in contrast, allow the patentee to escape invalidation by discouraging attempts to invalidate a patent.

Jay P. Kesan & Marc Banik, *Patents As Incomplete Contracts: Aligning Incentives for R&D Investment with Incentives To Disclose Prior Art*, 2 WASH. U. J.L. & POL'Y 23, 32–33 (2000). Lemley and Shapiro have also suggested that high litigation costs contribute to the problem of undersupplied patent challenges. Lemley & Shapiro, *supra* note 206, at 98; see also *supra* note 210 and accompanying text; *infra* note 257 and accompanying text.

²²⁶ See *supra* notes 44–53 and accompanying text. Cf. *Monsanto Co. v. McFarling*, 302 F.3d 1291, 1294–95 (Fed. Cir. 2002) (upholding a forum selection clause in a technology transfer agreement).

²²⁷ See 35 U.S.C. § 318.

clear where [in the Genentech-MedImmune license agreement] the prohibition against challenging the validity of the patents is to be found.”²²⁸ While this statement cannot imply that a patent license may include a *blanket* prohibition against validity challenges (such a term would be in direct conflict with the holdings of *Gormully*²²⁹ and *Lear*,²³⁰ neither of which could have been overruled by *MedImmune*’s jurisdictional holding),²³¹ the *MedImmune* Court appears to suggest that licensing parties may lawfully agree to place some restrictions on such challenges. Particularly if reexamination-only clauses are circumscribed as described below,²³² courts may view them as innocuous forum-selection provisions²³³ that channel validity determinations toward the USPTO. Therefore, enforceability of reexamination-only clauses is consistent with both the *MedImmune* and *Gormully-Lear* lines of cases, comporting with these two seemingly inconsistent doctrinal strands.

2. Objections to the Reexamination-Only Solution: Questions About Enforceability and Wishes of Licensing Parties

Three objections to the reexamination-only solution are readily apparent. The first objection I discuss deals generally with enforceability of reexamination-only terms; the second addresses why such terms might be undesirable from the patent owner’s perspective and considers enforceability of an addition-

²²⁸ *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 135 (2007).

²²⁹ *Pope Mfg. Co. v. Gormully*, 144 U.S. 224, 234 (1892).

²³⁰ *Lear, Inc. v. Adkins*, 395 U.S. 653, 656 (1969).

²³¹ Dreyfuss and Pope disputed this conclusion, suggesting that, “while *Lear* is understood as prohibiting the enforcement of any contract provision that reduces the licensee’s incentive to challenge validity, *MedImmune* can be interpreted as permitting patent holders to bargain for such restrictions.” Dreyfuss & Pope, *supra* note 37, at 976. Nevertheless, another commentator countered that “*MedImmune*’s dicta will likely not change well-settled law [that prohibits no-challenge clauses] in the near future.” Risch, *supra* note 25, at 1012. The author agrees that Dreyfuss and Pope’s reading of *MedImmune* is plausible, but sides ultimately with Risch since the *MedImmune* Court mentioned *Lear* in several instances without explicitly disapproving or modifying the holding of that case. *MedImmune*, 549 U.S. at 124, 125, 135.

²³² See *infra* Part III.C.2.

²³³ See Risch, *supra* note 25, at 1006, 1042 (arguing that a “venue selection” clause is “surely legal” as a “reasonably negotiated license term”); see also *supra* notes 225–27 and accompanying text.

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al clause that might make the reexamination-only solution more palatable to licensors; the third considers again why *licensees* might resist such terms.²³⁴

The first objection is based on the “patents or printed publications” limitation of the reexamination statute.²³⁵ If the licensee seeks to invalidate the patent via the on-sale bar,²³⁶ for example, advantages of the *inter partes* procedure over litigation²³⁷ will not do the challenger much good. By all accounts, patent challenges not permitted by the reexamination statute, such as § 102(b) public use and on-sale bars and § 112 defects, are brought quite frequently, and often successfully, by accused infringers.²³⁸ Therefore, courts that interpret licenses with reexamination-only clauses may find that such clauses result in sufficient “muzzling” within the meaning of *Lear* as to jeopardize the public interest in purifying the patent system.²³⁹ In view of this potential problem with enforceability of reexamination-only terms, parties may modify the clause to provide that challenges based on published prior art must go through the reexamination system, while all other challenges could be brought in a district court.²⁴⁰ If the licensee wishes to attack the patent on multiple grounds, some of which are permitted to be advanced in reexamination and others which are not, the clause may provide that the licensee must first bring its § 102 and § 103 “patents or printed publications”²⁴¹ challenges via *inter partes* reexamination.²⁴² This mod-

²³⁴ See also Part II.B.1.

²³⁵ See also *supra* note 103 and accompanying text. Even if the Patent Reform Act of 2011 becomes law and a post-grant opposition procedure is adopted, the prior art limitation will remain an issue because, after the nine-month period passes, only traditional reexamination will be available for those wishing to challenge patent validity through the USPTO. See *supra* note 104.

²³⁶ See 35 U.S.C. § 102(b).

²³⁷ See *supra* Part II.B.2 for a discussion of some advantages of *inter partes* reexamination over litigation for patent challengers.

²³⁸ See, e.g., Allison & Lemley, *supra* note 101, at 210 (“The five most popular grounds of invalidity that defendants asserted, as measured by those issues actually decided by the courts, are obviousness (asserted in 160 out of 300 cases), section 102 prior art (asserted in 91 out of 300 cases), section 102 non-prior art (71 out of 300 cases), best mode (45 out of 300 cases), and enablement/written description (36 out of 300 cases).”). Interestingly, § 102 prior art challenges were particularly successful, resulting in invalidity determinations in 60.6% of the cases in which they were brought; for best mode, the success rate was 34.8%, and for enablement/written description, 36.1%. *Id.* at 209. While this data set is fairly dated by now, it likely remains true that challenges outside the purview of the reexamination statute continue to account for a substantial fraction of district court invalidity holdings.

²³⁹ See also *supra* note 51 and accompanying text.

²⁴⁰ The author gratefully acknowledges participants in Stanford’s Center for Law and the Biosciences journal club for this suggestion.

²⁴¹ 35 U.S.C. § 301.

ified reexamination-only clause, which avoids a complete bar of § 112 challenges and novelty and non-obviousness challenges not based on a patent or a printed publication (as well as challenges on other grounds such as § 101 or inequitable conduct),²⁴³ would likely be enforceable under *Lear* given that licensee “muzzling” is now minimized.²⁴⁴

The second objection has to do with the central problem for licensors created by the *Lear* and *MedImmune* cases—patent owners may be unwilling to give licensees a contractual “free shot” at invalidating the patent without suffering any adverse consequences.²⁴⁵ One answer is that, for better or worse, the Supreme Court sought to achieve exactly this result when it spoke of permitting unfettered challenges to patents.²⁴⁶ Another, more involved response entails combining the reexamination-only term with a clause that mandates upward adjustment of the royalty rate in the event that challenged claims are upheld in reexamination. Other commentators have proposed such “royalty escalation”²⁴⁷ clauses as a general approach to “increas[ing] the risk to the licensee, thus putting it on equal footing with the patent holder.”²⁴⁸ One further refinement of

²⁴² Of course, a counterargument can be made that this approach creates judicial inefficiencies, though invalidation of asserted claims on the basis of a prior art patent or a printed publication in an *inter partes* reexamination would moot challenges on other grounds in a district court.

²⁴³ See also *supra* notes 100–03 and accompanying text.

²⁴⁴ Likewise, reexamination-only clauses would not, by definition, bar non-infringement challenges, which arise when the licensee maintains that its “licensed” products are actually not covered by the patents under license. Cf. Risch, *supra* note 25, at 1005 n.8 (framing the act of “challenging the patent” as “any challenge to the requirement of paying royalties under the patent,” including both non-infringement and invalidity challenges). Notably, the *MedImmune* case itself included both a non-infringement and an invalidity challenge. See *supra* note 143 and accompanying text. Reexamination-only clauses would therefore not provide the desired litigation cost savings in cases when licensees bring only non-infringement challenges. When both types of challenges are brought, however, the clause may require that validity challenges be resolved first through the reexamination system, mooting the controversy in the event the claims are invalidated. If the claims are upheld by the USPTO and non-infringement litigation then follows, however, reexamination-only clauses might lead to inefficient results. Perhaps, then, reexamination-only clauses are most useful when infringement issues are clearly not in controversy, a scenario that may hold true for a sizable subset of patent licenses. (*MedImmune*, one recalls, involved a dispute over a license entered into for a patent application, so that it might have been difficult to predict the precise coverage of the patent that would issue from it.) See *supra* Part III.A; see also *infra* note 262 and accompanying text.

²⁴⁵ See *supra* Part III.A. See generally Dreyfuss & Pope, *supra* note 37.

²⁴⁶ See generally *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969).

²⁴⁷ Risch, *supra* note 25, at 1036–39.

²⁴⁸ Dreyfuss & Pope, *supra* note 37, at 1001.

this solution involves increasing the royalty rate during the pendency of a patent challenge, followed by “an even higher royalty if the challenge is not successful.”²⁴⁹ Several commentators contended that such clauses should be enforceable because they do not eliminate the licensees’ incentives to challenge patents; indeed, a successful challenge would be a major victory for a licensee because it would no longer owe any royalties.²⁵⁰ Similarly, royalty escalation clauses that are not overly punitive²⁵¹ can be built into licenses that also contain reexamination-only clauses. Perhaps, with the reexamination-only solution already in place, it is difficult to justify also increasing royalties during the pendency of the challenge, since compensating the patentee for the costs of defending patent validity in litigation may be the primary reason for such a term.²⁵² A clause that provides for, say, doubling of the royalty rate upon a finding of validity of challenged claims in *inter partes* reexamination, however, would be likely enforceable as non-punitive and not overly burdensome to the patentee’s right to challenge the patent within the meaning of *Lear*.²⁵³ As Dreyfuss and Pope noted, “patents that have survived a challenge are generally perceived by the business community as more valuable than untested patents. Accordingly, the higher rate should be regarded as reflecting the economics of the relationship, rather than as a penalty for challenging the patent.”²⁵⁴

Yet a third objection to the reexamination-only solution builds on the general concern about litigation estoppel following the USPTO’s determinations in a reexamination.²⁵⁵ Licensees might worry that, if the examiner were to uphold the claims or narrow them but in such a way that the licensed products

²⁴⁹ *Id.* at 1001 n.122 (“In fact, Stanford University has already announced that it will use this approach.”).

²⁵⁰ *Id.* at 1002; Risch, *supra* note 25, at 1036–37.

²⁵¹ Risch warns that excessive royalty escalation provisions might run afoul of the prohibition of penalty liquidated damages. *Id.* at 1037.

²⁵² Dreyfuss & Pope, *supra* note 37, at 1002 (“Imposing an increased royalty during the period of [a declaratory judgment] challenge defrays the additional economic burden defending such a challenge imposes on the patent holder.”). Nevertheless, defending a reexamination challenge is far from costless, making a clause that provides for modest royalty increase during the pendency of *inter partes* reexamination reasonable after all. See generally Mercado, *supra* note 83.

²⁵³ Such a clause would also provide for the royalty rate to double if the claims are narrowed in reexamination, but continue to cover the licensed products. Of course, if the licensing parties then disagree on the issue of claim scope (i.e., whether the licensee would actually infringe the amended claims if the license were terminated), they may opt for litigating the issue of infringement. See the following paragraph for further discussion of this scenario.

²⁵⁴ Dreyfuss & Pope, *supra* note 37, at 1002.

²⁵⁵ See *supra* Part II.B.1.

continued to be covered, licensees would get nothing for their efforts and might even end up with a higher royalty if the license includes a royalty escalation clause discussed above, while the licensor would now hold a stronger patent.²⁵⁶ While the result of getting the claim scope precisely right might be socially desirable,²⁵⁷ it does the licensee no good if its products still infringe the claims after the reexamination.²⁵⁸ The fear of this Pyrrhic victory scenario is surely justified. The right decision, instead, might be to go for all the marbles in district court to at least have a chance to invalidate the claims in question completely, the presumption of validity hurdle notwithstanding.²⁵⁹ The possibility of an unfavorable reexamination outcome, however, should incentivize the licensee to do its due diligence before bringing a challenge; after all, the very purpose of post-*MedImmune* licensing solutions is “to allocate back to the licensee some of the risk of patent invalidation.”²⁶⁰ Moreover, if the examiner gets the claim scope right after a reexamination and the licensed patents continue to cover the licensee’s products or activities, the licensee is getting exactly what it bargained for²⁶¹—immunity from a meritorious suit for patent infringement that may well result in a large award of damages or an injunction if not for the license. If it is unclear whether the product infringes the reexamined claims, the licensee can sue for a declaratory judgment of non-infringement in a district court, which is an action that reexamination-only clauses cannot bar.²⁶² Again,

²⁵⁶ The increased strength of the patent would become important if the licensing parties later end up in litigation, after all. The author thanks colleagues at Wilson Sonsini Goodrich & Rosati for advancing this objection. *See also supra* note 254 and accompanying text.

²⁵⁷ *See supra* notes 221–23 and accompanying text. *Cf.* Dreyfuss & Pope, *supra* note 37, at 1001 n.121 (noting that non-mutuality of collateral estoppel, *see supra* note 189, discourages patent challenges); Farrell & Merges, *supra* note 210, at 952–53 (arguing that patent challenges will be undersupplied because they are a public good); Lemley & Shapiro, *supra* note 206, at 90 (same); Risch, *supra* note 25, at 1022 (same); *see also supra* note 53 (citing proposals to rectify this problem by paying bounties in order to encourage patent validity challenges).

²⁵⁸ As mentioned *supra* in note 107, forty-seven percent of patents that were challenged in reexamination and reached a final disposition had their all claims cancelled or disclaimed, but forty-three percent resulted in “claims changes,” i.e., amendments.

²⁵⁹ *See supra* notes 113–17 and accompanying text.

²⁶⁰ Dreyfuss & Pope, *supra* note 37, at 991.

²⁶¹ *See supra* note 25 and accompanying text.

²⁶² Alternatively, after the reexamination challenge and the resulting narrowing of claims, the licensee can argue that it no longer owes royalties because the “contract, properly interpreted, does not prevent it from challenging the patents, and does not require the payment of royalties because the patents do not cover its products.” *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 135 (2007). This approach frames the issue as a contractual dispute, but the fun-

to avoid this undesirable and costly scenario, the licensee would be well-advised to conduct a detailed analysis of the likely effect on the scope of the claims of the prior art it plans to cite against the patent in reexamination.²⁶³ The reexamination-only solution does not completely tie the licensee's hands, but rather encourages well thought-out challenges pursued after a thorough consideration of the risks of an unfavorable reexamination outcome. Of course, licensees who believe that reexamination-only clauses are extremely unfavorable or risky for potential challengers of patent validity can simply refuse to allow their inclusion in the license. As a result, however, such licensees would likely end up paying higher royalties to compensate patent owners who are wary of litigation costs.

IV. CONCLUSION: LOWERING THE COSTS OF LICENSING AFTER *MEDIMMUNE* WITH REEXAMINATION-ONLY CLAUSES

This Article began with the well-established proposition that patent licensing can be viewed as a form of property alienation, with the license as a contract mechanism by which the patent owner promises, in exchange for a royalty, to forbear from using its right to exclude the other party from making and using the subject matter of the patent.²⁶⁴ In discussing licensing of intellectual property, Richard Epstein argued that “the state should not impose restrictions on this right of alienation unless these can be strictly justified to protect the interests of other individuals. . . . [T]he normal rule is, and should be, one of freedom of contract.”²⁶⁵ In *Lear*, the Supreme Court identified the injuries inflicted by bad patents upon the public (i.e., unwarranted monopoly and restrictions on the use of ideas that belong in the public domain) as externalities that justified interference with the freedom of contract.²⁶⁶ As Risch noted, however, while “licensees just might be society's best hope for invalidating patents, . . . this is not a costless proposition.”²⁶⁷ Some social costs of the *Lear-MedImmune*

damental underlying issue is still non-infringement or lack of coverage of “licensed” products by the new claims.

²⁶³ Another scenario that would defeat the cost-savings advantage of the reexamination-only solution involves subsequent appeals of the USPTO's determination in the *inter partes* reexamination to the BPAI and then to the Federal Circuit, as provided by 35 U.S.C. §§ 315(b), (c). One can imagine, however, that in the majority of cases parties will not pursue appeals past the stage of the BPAI, leading to the result that reexamination-only clauses would enable litigation cost reduction in the average case.

²⁶⁴ See *supra* Part I.

²⁶⁵ Epstein, *supra* note 12, at 498.

²⁶⁶ *Lear, Inc. v. Adkins*, 395 U.S. 653, 670–71 (1969).

²⁶⁷ Risch, *supra* note 25, at 1044.

rule may include higher royalty rates that end up being passed through to consumers,²⁶⁸ reduced licensing activity,²⁶⁹ and a “decrease in incentives to invent.”²⁷⁰ Moreover, if licensees choose to take advantage of the relaxed jurisdictional requirements and mount too many poorly thought-out challenges against good patents, the fundamental policy of *Lear* would not be served and these costs would be generated without a good justification.²⁷¹

The *inter partes* reexamination solution pays heed to both the norms of contract law and the public interest by allowing contracting parties to agree in advance on *how* the licensee would go about challenging patent validity if that should become desirable.²⁷² Reexamination-only clauses would help restore some degree of certainty to patent licenses that was impaired by *MedImmune*, as patent owners would no longer have to view every license as a declaratory judgment suit waiting to happen, no matter what the possible grounds for invalidity might be.²⁷³ Arguing that *MedImmune* may have undermined the alienability of patent rights, Epstein lamented that its holding created an “open question [as to] whether any two parties could ever settle a patent dispute with a license agreement that the licensee could not seek thereafter to upset by another round of litigation.”²⁷⁴ Building reexamination-only clauses into licenses can thus help licensees and licensors “secure the stability of expectations such that people can plan today the distribution of rights that they wish to enjoy tomor-

²⁶⁸ See Farrell & Merges, *supra* note 210, at 953–54; Risch, *supra* note 25, at 1004; see also *id.* at 1019 (enumerating the sources of the costs of patent challenges to the licensor as “potential attorneys’ fees and other litigation costs, potential loss of royalties, and interference with other licenses if the patent is invalidated”).

²⁶⁹ See Risch, *supra* note 25, at 1021–22, 1022 n.102 and references therein.

²⁷⁰ Dreyfuss & Pope, *supra* note 37, at 974; see also *supra* Part III.A.

²⁷¹ The evidence so far, however, is that challenges to licensed patents have not become widespread, though perhaps it is too early to assess the effect of *MedImmune*. See *supra* notes 164–66 and accompanying text; see also Risch, *supra* note 25, at 1018 (“Some licensees . . . prefer peace to litigation even if they believe the patent might be invalid. Other licensees may believe that the patent is valid, and want to avoid the risk of treble damages and attorneys’ fees if the matter were litigated.”) (footnotes omitted).

²⁷² This is particularly true if the clause restricts only “patents or printed publications” challenges to the *inter partes* reexamination route, but allows other challenges to proceed in a district court. See *supra* Part III.C.2. In this form, reexamination-only clauses would serve as forum-selection provisions tending to lower the price of the license, and therefore encouraging more licensing activity without significantly compromising the public interest. See also *supra* notes 225–26, 233 and accompanying text.

²⁷³ See *supra* Part III.A.

²⁷⁴ Epstein, *supra* note 12, at 502.

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row.”²⁷⁵ Knowing that a well-defined, bargained-for, and relatively low-cost resolution to some conflicts over patent validity is available would encourage prospective licensees and licensors to contract more freely.²⁷⁶ As a result, the indirect restraints on alienability of patent rights created by the *Lear-MedImmune* regime would be loosened. The availability of reexamination-only clauses may then lead to the socially beneficial outcome of more vigorous licensing activity, which in turn would be expected to help licensors “wring the last unit of value out of the underlying [patent] asset.”²⁷⁷

To be sure, reexamination-only clauses will not solve all of the problems that *Lear* and *MedImmune* have created for licensors, including risks of “potential loss of royalties . . . and interference with other licenses if the patent is invalidated,”²⁷⁸ the latter if the license is nonexclusive. It is clear, however, that the “patent-challenge tax” cannot be eliminated completely,²⁷⁹ just reduced with private-law measures subject to the courts’ scrutiny in the wake of *Lear*. Reexamination-only clauses accomplish this result by lowering litigation costs in some types of licensee-licensor disputes,²⁸⁰ and are likely to be enforceable as forum-selection clauses if they explicitly allow district court validity challenges on the grounds that are barred by the reexamination statute.²⁸¹ Risch contended that “[t]he terms that are most likely to be effective [in lowering the patent-challenge tax]—other than the explicit promise to challenge which is now unenforceable—are those that most increase the cost to the licensee in case of chal-

²⁷⁵ *Id.*

²⁷⁶ Cf. Risch, *supra* note 25, at 1025 (“[U]ncertainty about the legality of any provision will likely prevent complete elimination of the [patent-challenge] tax.”).

²⁷⁷ Epstein, *supra* note 12, at 499.

²⁷⁸ Risch, *supra* note 25, at 1019.

²⁷⁹ *Id.* at 1024–25.

²⁸⁰ One reexamination expert argued that, given the reasoning of a case recently decided by the Federal Circuit, the reexamination route may generally be the preferred, low-cost approach for accused infringers wishing to challenge patent validity on § 103 grounds. See Scott Daniels, *Was Reexamination the Answer in Tokai v. Easton?*, REEXAMINATION ALERT (Feb. 6, 2011), <http://www.whda.com/blog/2011/02/was-reexamination-the-answer-in-tokai-v-easton> (“The majority’s analysis reads very much like the affirmances of obviousness rejections that issue daily from the PTO Board of Appeals. It is hard to imagine the Board, presented with the undisputed facts of this case, reaching a different conclusion. . . . None of what is said here is meant to criticize any of the parties, but merely to suggest that *there are some issues that may be less expensively resolved by reexamination at the PTO.*”) (emphasis added). This blog posting discusses the case of *Tokai Corp. v. Easton Enters., Inc.*, Nos. 2010-1057 and 2010-1116, 2011 WL 308370 (Fed. Cir. Jan. 31, 2011).

²⁸¹ See also *supra* note 272 and accompanying text.

lenge.”²⁸² Similarly, a license term that reduces the cost of the challenge to the patent owner—particularly, the cost of litigation—can also be effective in lowering the tax.²⁸³ The reexamination-only solution would tend to reduce the prices of patent licenses and, in turn, help alleviate the social costs of *MedImmune* and *Lear*.²⁸⁴

While the market for patent licenses has its pathologies²⁸⁵ and the patent system in general is surely not a perfect means for promoting the commercialization of inventions,²⁸⁶ licensing practice represents an important avenue for monetizing patents and for acquiring know-how useful for developing new technologies.²⁸⁷ Given the great economic and social value of patent licenses, uncertainty surrounding legal rights of parties who contract to transfer patent rights is not desirable. Nevertheless, the *MedImmune* decision arguably injected a great degree of uncertainty into licensee-licensor relationships and cast doubt on the continuing value of patent licenses, as it granted licensees the ability to challenge patents without terminating their licenses.

²⁸² Risch, *supra* note 25, at 1044.

²⁸³ See Schlicher, *supra* note 154, at 374 (noting that “[i]f a patent owner does not believe that *Lear* and *MedImmune* problems may be avoided by contract terms,” one rational outcome would be increasing the royalty by “an amount approximating validity litigation costs”); see also Risch, *supra* note 25, at 1020, 1053 (developing a model showing that increased costs of validity challenge to the licensee increase the patent-challenge tax); *id.* at 1040–42 (proposing a fee-shifting clause to address the problem with the cost of patent challenge and concluding that “[n]egating litigation costs by both reducing the chance and costs of challenge can have a much larger percentage effect on the tax”).

²⁸⁴ See *supra* notes 268–70 and accompanying text. One added cost of the reexamination-only solution that must be considered is the burden of increased reexamination activity on the USPTO. Cf. Katharine M. Zandy, Note, *Too Much, Too Little, or Just Right? A Goldilocks Approach to Patent Reexamination Reform*, 61 N.Y.U. ANN. SURV. AM. L. 865, 891–92 (2006) (expressing concern about “overwhelming PTO’s resources” in the context of reexamination reform proposals). The solution proposed in this Article is certainly meant to channel some patent challenges from the district courts to the USPTO. It is unclear, however, whether the number of such challenges would be so high as to overwhelm the USPTO. See *supra* notes 164–69 and accompanying text.

²⁸⁵ See Lemley, *supra* note 8, at 148–49; see also Mark A. Lemley, *The Economics of Improvement in Intellectual Property Law*, 75 U. TEX. L. REV. 989, 1048–65 (1997).

²⁸⁶ See generally Ted Sichelman, *Commercializing Patents*, 62 STAN. L. REV. 341 (2010) (arguing that the patent system is inadequate for promoting commercialization of inventions and proposing a new “commercialization patent” system).

²⁸⁷ See KEVIN G. RIVETTE & DAVID KLINE, REMBRANDTS IN THE ATTIC: UNLOCKING THE HIDDEN VALUE OF PATENTS 119–44 (2000); see also Kieff, *supra* note 8; Edmund W. Kitch, *The Nature and Function of the Patent System*, 20 J.L. & ECON. 265, 277 (1977) (“[A] patent system lowers the cost for the owner of technological information of contracting with other firms possessing complementary information and resources.”).

Adding to the dialogue between federal patent policy concerns and private law responses that seek to establish stable licensing relationships, this Article offers a contractual resolution to the tension between the need to invalidate bad patents on the one hand, and the goal of promoting active licensing practice on the other. The solution for those involved in patent licensing is to contract for the use of *inter partes* reexamination, a recently established post-grant patent review procedure that is beginning to gain traction in the patent community but has not yet received its full acceptance, to challenge the validity of licensed patents. The Article argues that the procedure is a desirable, low-cost alternative to litigation that gives the USPTO a fair, workable opportunity to correct its own mistakes in an adversarial setting. Moreover, the Article shows that clauses limiting licensees to *inter partes* validity challenges, at least when such clauses allow challenges that are not permitted in reexaminations to proceed in district courts, likely do not violate *Lear*'s strictures against the "muzzling" of licensees' capability to police the public domain, and should therefore be enforceable. In so doing, this Article provides a roadmap for reconciling federal patent policy interests with fundamental common-law tenets of freedom of contract and freedom from restraints of alienation of property.