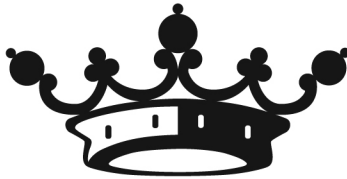


I N S I D E T H E M I N D S

Navigating Intellectual Property Disputes

*Leading Lawyers on Protecting IP Assets,
Preventing and Resolving Disputes, and
Understanding Recent Regulations*



ASPATORE

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Strategies for Avoiding and Navigating IP Disputes

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ASPATORE

Introduction

For almost twenty-five years, I have been engaged in the practice of intellectual property (IP) law, including overseeing the clearance, registration, and protection of trademarks and copyrights, as well as counseling in the areas of licensing, trade secrets, entertainment, the Internet, and related matters. My clients are in a multitude of industries, including, among other things, fashion, cosmetics, toys, real estate, finance, e-commerce, and the Internet and new media. They are both licensors and licensees, employers and employees, and talent and distribution.

I increasingly find, particularly in light of the current business climate, that clients want a business-oriented, pragmatic approach that weighs costs against anticipated benefits, and I strive to keep this balance in mind at all times. As a result, a central aspect of my approach to IP matters is my focus on the business perspective. I concentrate on what matters to the client and how to attain those results in the most efficient and economical way.

The purpose of this chapter is to outline current issues in the IP arena, best practices for avoiding disputes, and key considerations for successfully navigating disputes if they cannot be avoided.

Recent Trends in IP Disputes

There have been only two active areas of practice since the economic downturn: bankruptcy and litigation. Other disciplines—real estate, corporate, tax, etc.—have contracted or, at best, remained static. As a result, I am seeing two main trends:

1. **Substantial litigations.** The first seems, perhaps, counterintuitive. Active, substantial litigations are more difficult to settle than they have been in the past. Rather than being more efficient and frugal, it seems that the larger law firms are reluctant to let a case go before the last dollar has been wrung from it.
2. **Avoiding bankruptcy issues and IP ownership.** The second trend is directly related to my area of practice. Licensors and licensees are, by necessity, being more creative than they had been in the past. The value proposition for the deal may or may not be

there in the coming months. So, for example, a famous national and international brand, which has also been experiencing a cash crunch, recently entered into a license deal, as licensor, with a client of mine. My client, the licensee, paid the entire amount of the multi-year license fee up front. There are no royalties, and the price was, on its face, beneficial to the licensee. However, and these are significant “howevers,” by paying the entire sum due under the agreement, the licensor is incentivized to find a way to terminate the license so it can re-license the property to a third party for additional income, and since the license was for a series of trademarks, the licensee is exposed to a trustee rejecting the agreement in a bankruptcy, with its up-front payment becoming an unsecured claim. We found ways to minimize, but not eliminate, the risks.

Owners of IP are, if anything, more actively protecting it. While companies are disinclined to incur large legal expenses while riding out a recession, they are very protective of their IP rights. Clients are hunkering down and taking whatever steps they can to gain a competitive advantage. As part of that, they are going to great lengths to protect what is theirs. This has caused a spike in the number of demand letters (e.g., “That mark is mine. Stop using it.” or “You are now a former employee. Do not use our stuff.”) The efficacy of those assertions, however, is another matter entirely.

There are six categories of IP-related matters: patents, trademarks, copyrights, trade secrets, Internet and domain names, and contractual disputes (including licenses, work-for-hire agreements, non-competes, talent agreements, production and distribution agreements, and the like). All can be important in varying degrees depending on the specific matter, and understanding the manner in which they interrelate, or do not, is essential. For example, one logo may be protected by both trademark and copyright, but once a patent is filed, because it is public and no longer kept secret, you have given up trade secret coverage. This might be advantageous, but given that patents have a limited life span and trade secrets do not, it might also be something to consider. At a minimum, it is essential to understand the current issues in the relevant area.

Recent Activity in Patent Litigation

Patent litigation is very active, so much so that the Eastern District of Texas, which has been the preferred jurisdiction for commencing a patent infringement matter due to its local rules, expertise, plaintiff-friendly attitude, and rocket docket, has been overwhelmed and lost its sheen. In 2003, there were fourteen patent cases filed. In 2004, this number more than quadrupled, when fifty-nine patent cases were filed. In 2006, the number jumped to an estimated 236 cases. It was in this jurisdiction that Judge Leonard Davis recently ordered a permanent injunction that “prohibits Microsoft from selling or importing to the United States any Microsoft Word products that have the capability of opening .XML, .DOCX, or DOCM files (XML files) containing custom XML.”

The one action to be most aware of in the world of patents right now is *In re Bilski*, 543 F.3d, 943, 88 U.S.P.Q.2d 1385 (Fed Cir. 2008) *cert. granted*. This action, presently pending before the U.S. Supreme Court, questions the validity of a patent that covers a commodities trading method. Since software *per se* is not patentable because patent law does not allow the patent registration of algorithms (but does allow the patenting of a physical process that is controlled by an algorithm (see *Diamond v. Diehr*, 450 U.S. 175 (1981))), this is not all that surprising. However, it is likely that the case will set a significant precedent and have broad implications for the patentability of business methods and software. The U.S. Patent and Trademark Office recently issued guidance for the examining process in light of *Bilski*.

Until 1998, it was widely assumed that business methods were not patentable in the United States. Some inventions could be protected as trade secrets, but most could not practicably be kept confidential, and competitors were therefore free to copy them. The 1998 decision by the Court of Appeals for the Federal Circuit in *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*, 149 F.3d 1368 (1998) turned that standard on its head. The *State Street* decision upheld a patent on a software program that was used to make mutual fund asset allocation calculations. In the wake of that decision, companies have been seeking (and obtaining) business method patents at a furious pace.

The granting of patent protection to what may be viewed as questionable inventions has created the setting for litigation seeking to reverse that trend. *Bilski* will be the test.

Recent Activity in Trademark Litigation

There have also been important and substantive clarifications on the trademark side. Entities are protecting their marks, while the infringers simultaneously try to rebuff their efforts. Copyright disputes, which go hand in hand with trade secrets, arise with the question of who owns what and whether an employee is an independent contractor. Massive layoffs caused former employees to strike out on their own, and their employers are in many cases asserting that the competition is improper.

Illustrative Cases

Non-compete agreements or non-compete provisions of employment agreements can be a valuable and important tool for protecting a company's IP against use or misuse by former employees, suppliers, distributors, and others. However, you need to be very cognizant of the governing jurisdiction. In most, for example, the provision needs to be narrowly tailored and limited in geographic scope and duration. Two years is a good rule of thumb for the outer limit.

California, on the other hand, has effectively outlawed non-compete covenants. There was some dispute as to whether these covenants could be narrowly tailored and therefore upheld, but that has now been effectively shot down. In two recent cases, the courts made this clear.

FLIR Systems, Inc. v. Parrish

In *FLIR Systems Inc. v. Parrish*, ___ Cal. App. 4th ___, 2009 Cal. App. LEXIS 943 (2d Dist. June 15, 2009), the Court of Appeals for the Second District affirmed a judgment both denying an injunction and awarding the ex-employee defendants \$1,641,216.78 in attorneys' fees where their former employer/plaintiff was found to have sought an injunction in bad faith, since misappropriation was possible but not actually "threatened" within the meaning of California's Uniform Trade Secret Act (Civil Code s. 3426).

The important points to remember from *FLIR* are that the courts can and will award attorneys' fees as sanctions where a request for an injunction has been brought in bad faith. This occurs when a suit is brought prematurely against an ex-employee who possesses, but does not imminently threaten to use or misuse, trade secrets. Other factors that may show bad faith include: unreasonable settlement demands or ones that restrain trade, pursuit of injunctive relief broader than what is protectable by the trade secret, and the continued pursuit of claims on legal theories expressly rejected by California courts.

Edwards v. Arthur Anderson

In *Edwards v. Arthur Anderson*, 44 Cal. 4th 937 (Cal. 2008), the California Supreme Court confirmed California's bright-line prohibition against post-employment restrictions such as covenants not to compete. This summarized California law governing restraints of trade and covenants not to compete, such as California Business and Professions Code Section 166000, as well as numerous state court decisions, and concluded that these restraints unequivocally invalidate post-employment restraints. The court then went on to reject a line of cases developed in the Ninth Circuit holding that post-employment restraints in California can be lawful if they are only "narrow restraints." (The Ninth Circuit's interpretation—often referred to as the "rule of reasonableness"—is set forth in *Campbell v. Trustees of Leland Stanford Jr. Univ.*, 817 F.2d 499 (9th Cir. 1987).) In short, there is no way to properly draft or enforce such post-employment restraints in California. The only protection available against former employees is the same as what is generally available to use against any third party—trade secrets, trademarks, copyrights, and patents.

I am aware of no other jurisdictions that are as employee-protective as California. Regardless, California's law serves to highlight that all aspects of IP should work together to protect what is protectable. If that means taking a "belt and suspenders approach," so that you have one piece of IP protected by trademark and copyright and an employee non-compete, that is fine.

Strategies for Prevailing in IP Disputes

Strategies for prevailing in IP disputes are specific to the industry sector and facts of the IP involved, but clients and attorneys must in all circumstances pay close attention to four issues that will likely arise in any contested matter (and we are not concerned here with more general litigation issues such as jurisdiction and venue):

1. Does the claimant company have clear right and title to the pertinent IP?
2. Is the registration, if there is one, enforceable and is there supporting documentation for each aspect of the registration?
3. Have the jurisdictional prerequisites to institution of an action been satisfied?
4. What are the local rules and idiosyncrasies of the court and jurisdiction in which you intend to bring your action?

On the operational side of IP disputes, demand letters, IP ownership research, use of experts, financial impact, competitive forces, and dispute resolution are important considerations.

Determining Clear Right and Title to the Relevant IP

A critical preliminary step prior to taking any action to enforce or protect an IP claim is to identify the IP the claimant company owns. This is not necessarily as straightforward as it might sound. There might be a holding company that must be named as plaintiff, there might be a break in the chain of title, there might be approvals needed from licensors or licensees or financial institutions or parents or affiliates, or there might be issues with a registration (more on that below).

Start by asking the client questions. But verify the answers. Clients are not always aware of what they do or don't have. Track registrations and assignments on the U.S. Copyright Office and the U.S. Patent and Trademark Office Web sites, as well as the Web site of the applicable international jurisdiction, most of which are now online. For example, see www.copyright.gov/records and www.uspto.gov/main/trademarks.htm. These sites allow one to research (without cost) existing registrations, check

title and ownership, and verify assignments. Counsel should also perform an online search, check domain registrars such as www.register.com or search www.networksolutions.com/whois/index.jsp, and consult with external experts to perform a comprehensive search and obtain a copy of the entire application file history, known as the “file wrapper.”

You may also need to retain an expert. The manner in which experts are most efficiently and effectively used can vary widely:

1. **Private investigators.** At the beginning of the process, we may use private investigators to scrutinize the potential defendant’s size and activities, and obtain samples of the infringing materials.
2. **Patent experts.** You will almost always need an expert in a patent matter to obtain an opinion both that the patent is enforceable—since it must be reproved in each action—and that the competing technology infringes upon it. This will be essential for the *Markman* or claims construction hearing (a pre-trial hearing in a U.S. district court during which a judge examines evidence from all parties on the appropriate meanings of relevant keywords used in a patent claim, when patent infringement is alleged by a plaintiff, named for the U.S. Supreme Court case of *Markman v. Westview Instruments Inc.*, 517 U. S. 370 (1996)).
3. **Survey experts.** You may need a survey expert in a trademark infringement suit to prove likelihood of confusion or, if the claim is dilution, to prove you have a famous mark.
4. **Copyright experts.** You may need an expert in a copyright infringement action, depending on the nature of the work infringed. For instance, in music infringement suits, an expert is often required to compare the two works at issue.

Ensuring the Viability of the Pertinent Registrations

After you have clarified what it is your client wants to protect and identified the client’s objectives, you need to cross the t’s and dot the i’s on the pertinent registrations—be it trademark, patent, or copyright.

Unlike patents or copyrights, trademarks need not be registered in order to be enforced and protected. There are, nonetheless, many good reasons for doing so. These include: the registrant's rights are nationwide, as opposed to existing only in the geographic area in which the mark is used; a registration is an essential tool against cyber-squatters; it grants the registrant a presumption in court that the trademark is valid and is owned by the registrant; after five years of continuous use and registration it becomes incontestable, which forecloses certain of the grounds for cancellation; a registration provides the registrant with improved remedies in an infringement action, including the possibility of treble damages and attorneys' fees; and a registered trademark may be filed with U.S. Customs to prevent importation and allow seizure of counterfeit or infringing goods at the border.

Despite all of the advantages, clients need to be careful with registrations. A recent series of decisions, which began with a 2003 Trademark Trial and Appeal Board decision, *Medinol Ltd. v. Neuro Vasx Inc.*, 67 USPQ2d 1205 (TTAB 2003), and includes other unpublished cases, raises concerns that many applicants registering trademarks in the United States are committing fraud against the Patent and Trademark Office, regardless of any actual intent to do so. The Trademark Trial and Appeal Board adopted a bright-line rule of law under which the applicant is presumed guilty of fraud for including in the specification of goods or services on which the mark is not actually used, even if the error is completely inadvertent. The same rule applies to the intent required for an intent-to-use application, as well as to renewal applications and other maintenance of a mark, such as filings under Sections 8 and 15 of the Lanham Act. The rule has been that to cleanse the fraud, the entire registration must be canceled. The goods or services on which the mark is not actually used cannot simply be stricken.

The Trademark Trial and Appeal Board has very recently shown a modicum of leniency on this issue in *Zanella Ltd. v. Nordstrom Inc.*, 90 U.S.P.Q. 2d 1758 (T.T.A.B. 2008). Without going into great detail, the decision is significant because it may allow registrants to take proactive and timely steps to correct a registration by deleting goods and services inadvertently included in any statement of use or renewal, so long as it does so before a challenge to the registration is made on fraud grounds. If proactive steps are taken in a timely manner, challenges to registrations on

fraud grounds are now likely to be more difficult to establish, though not precluded. At best, the corrections may create a presumption that there was no intent to commit fraud.

For example, a famous clothing company (we'll call it XYZ Clothing) obtained a registration twenty years ago in International Class 25 for a wide array of clothing, including everything from shorts to bathrobes. However, despite the fact that the items were listed on the registration, XYZ Clothing never sold sweatshirts or bathing suits. That is considered fraud on the trademark office, and the entire registration is subject to invalidation. This extremely valuable asset could be wiped out if the problem is not timely corrected.

Therefore—prior to instituting any action—it is essential to conduct a complete trademark audit, ensure that a registration is accurate and current, and correct any errors found. It is also wise to file a new application in case the original is invalidated.

Ensure That Any Jurisdictional Prerequisites Have Been Satisfied

You cannot institute a patent suit unless and until a patent has been issued. Make sure the patent is current, the owner is correct, and the claims are supported. Though copyright protection technically exists the moment a work of authorship is set down in tangible form, the holder of the copyright cannot commence an action to protect and enforce it until a registration has been granted or denied, not simply filed.

A recent decision in New York, *Do Denim vs. Fried Denim*, No. 08Civ.10947, 2009 U.S. Dist. LEXIS 51512, at *7 (S.D.N.Y. June 17, 2009), highlights this point. The court dismissed the copyright claims of plaintiff jeans maker Do Denim against competitor manufacturer Fried Denim Inc., holding that merely filing the copyright applications, fees, and deposits did not satisfy the jurisdictional requirement that a copyright be registered before a lawsuit is initiated.

Ensure That Trade Secrets Are Secret

I have found that few clients understand what a trade secret is and what can be done with it, and even fewer take the appropriate steps to protect their trade secrets. There are two components to a trade secret: (1) it has to be something valuable that gives a company an advantage over its competitors, and (2) the company has to take steps to keep it confidential. For example, if a trade secret is sitting on an employee's desk and the company takes no action to assert its rights to that trade secret, the trade secret protection provided by law is compromised.

It is more often than not the case that the alleged trade secret can be shown to give the client some advantage over its competitors (after all, if the process or procedure did not do so, it is not likely anyone would bother fighting about it). Often, the more difficult showing is confidentiality. This is one of those times that you cannot put the genie back once it is out of the bottle, so counsel should advise clients to limit access to their trade secrets from inception. Have a written policy stating who can and cannot access the trade secret. If it is on a computer, have it password-protected with limited access, and if it is in hard copy, keep it in a locked file cabinet. Take whatever affirmative steps can be taken so you can demonstrate that your client has minimized access to the trade secret.

The Next Steps When a Dispute Is Unavoidable

Demand Letters

The demand letter, though never required, is a good and cost-effective initial step in asserting rights to IP. It serves multiple purposes. For one, it gives the infringer notice that the claimant has a grievance. Additionally, it wipes out any claim the infringer might make from that point forward that the infringement was unintentional or innocent (which is significant because willful infringement usually results in higher damages awards and can result in an award of attorneys' fees), and it usually initiates a dialogue between the claimant and the infringer that, more often than not, leads to an amicable resolution of the matter without the expense and disruption of litigation.

The letter identifies the client and counsel, asserts rights to the IP and the basis for that claim, annexes copies of the registration certificates, if any, sets forth a statement of how the IP is being adversely impacted by the infringer's actions, requests the immediate cessation of the infringing activity, and requests information such as the infringer's source, sales, and profit information. That raises the stakes on damages across the board. For example, for copyright infringement, the client can be awarded treble damages and attorneys' fees.

This is one potential pitfall of the demand letter of which you should be aware. If the infringer feels strongly about its position, it can file for a declaratory judgment or other relief in its home jurisdiction, thereby giving itself home field advantage and rendering the claimant a defendant and probably the counter-claimant in its own action. This is undesirable from the claimant's point of view, but there is a solution. I have—if the size of the issue and the client's interest and pocket warrants—filed a complaint and annexed that to the demand letter as an exhibit, not as a formal service but just as notice. Though the action is filed, it is not yet served, so it communicates to the defendant that you and your client are quite serious, it sets the clock running for a resolution or litigation, and it minimizes the risk that the defendant will file its own action. A less costly and less effective alternative to that, which can be useful when the initial demand is ignored but the client would rather avoid litigation, is to prepare a complaint and annex it to the demand letter, but not file it with a court. This also shows a level of seriousness, and that you are prepared to escalate the matter but have not yet done so. Of course, it leaves the infringer with the option of filing for the declaratory judgment, as discussed above.

Analyzing Financial Impact

The value and financial impact of trademarks and their related goodwill can be substantial, but litigations are often more about injunctive relief than monetary damages, which is by no means to say that money damages are not obtainable. The measure of damages in the copyrights context focuses on statutory damages or lost sales. In patent matters, goodwill and non-monetary losses are the focus, and the client is seeking injunctive relief: first, the other party is prevented from continuing to perform the damaging action, and then monetary damages are sought. In general, the issue is not

monetary damages *per se*, but measuring the strength of the trademark. Strong trademarks yield sustainable and satisfactory judgments from the courts. For example, if the trademark is famous, the court may determine that the defendant was diluting the trademark. Analysis of trademark strength includes the extent to which the trademark is famous, and the breadth of its use.

Competitive Forces

When undertaking an action, the preference (subject to the substantive governing law and jurisdiction) is to be in your home court. As a practical matter, if the opposing side is based elsewhere, it is more expensive to hire an attorney in your home jurisdiction and fly in witnesses, and therefore strategically better for you.

Above all else, it is important to be proactive to counter competitive threats. For example, say a client received reliable information that a competitor was going to be promoting a product at a trade show that we felt was a clear infringement. In that case, the best strategy is to shut down the offending act prior to, or during, the show, and make it a high-profile matter.

A current client has a product that is considered the hottest item in its category, and many of its competitors are infringing upon the item. These cases are like having a finger in the leaking dike. You do the best you can by getting the word out to the industry that your product is the original, and that you have exclusive rights. No matter how many holes you plug, five others will spring up.

Dispute Resolution in IP Matters

My preferred venue for IP litigation is federal court. Alternative dispute resolution is an option, but to the extent that your client needs injunctive relief, you must be in court. If you have an alternative dispute resolution clause in an agreement, always have a carve-out for equitable relief being heard by the courts.

Here is one example in which alternative dispute resolution was good for my client. I represented a world-famous fashion designer. She had numerous licensees, including one for shoes that were sold throughout the country. She also had eponymous retail stores. The quality of the shoes manufactured and sold by the shoe licensee dropped dramatically, to the point that while the designer was prepared to have the shoes sold at a low price point, she was unwilling to carry them in her stores. Instead, she sold shoes from other manufacturers that did not bear her mark or label. The licensee took offense, arguing that selling third-party shoes in the stores was akin to selling them under the designer's trademark and brand, thereby violating its exclusive trademark license. Not only did we obtain a defense verdict dismissing all claims, but we also obtained money damages and were awarded attorneys' fees. This would have taken a lot longer and cost more in court.

Preventing IP Disputes

Preventing IP disputes is preferable to reactive situations, because it is less costly and more predictable. Taking steps such as considering the internal IP audit discussed above; choosing a new trademark with care and properly clearing it; clarifying work-for-hire status of independent contractors; ensuring the employment agreements identify the employee's preexisting IP by listing it and excluding anything not expressly listed; protecting trade secrets; establishing an IP policy; and monitoring and auditing IP are all helpful.

Choose a Properly Cleared Trademark with Care

Trademarks can be strong or weak, and they are classified into one of five categories, which, from strongest to weakest, are:

1. **Fanciful (strong):** The strongest marks are words that are completely made up and have no meaning outside of the trademark context, such as Xerox.
2. **Arbitrary (strong):** The next strongest marks are words that have a common meaning but are used for a completely different purpose in the trademark context, such as Apple for computers.
3. **Suggestive (strong):** The next strongest marks are those that, when applied to the good or service, require imagination, thought,

or perception to understand the nature of the goods or services, such as Jaguar for cars. It takes an imaginative leap to understand that the cars are meant to be as fast and sleek as the animal.

4. **Descriptive (not strong):** The weakest category of mark is one that describes a quality, characteristic, feature, function, purpose, or use of the product or service. It is often tempting to choose such a mark because of the ease of recognition of the goods or services to which they apply. Such a mark is not protectable unless secondary meaning is established (i.e., a showing that consumers identify the descriptive mark as a source indicator of the goods or services, which is shown through use and advertisement over a period of time, such as “vision center” in connection with a business offering optical goods and services).
5. **Generic (unprotectable):** These are commonly used words or terms that cannot be owned by anyone. Examples of generic words that had once been trademarks are aspirin and escalator.

Obviously, the ideal is to create a fanciful mark so that your client obtains the strongest and broadest protection possible.

After the mark has been created or chosen, a trademark search should be conducted to ensure there are no confusingly similar marks in use or registered. Care needs to be taken, and experience is essential. This can be a trap. It is not merely identical marks that are of concern, but any mark that is confusingly similar (a concept well beyond the scope of this chapter). And do not forget to clear the domain name as well.

Clarify Work-for-Hire Status

The world of IP is often “pay now or pay later.” Establishing ownership of the IP up front is critically important. If the company uses independent contractors, it must use a work-for-hire agreement to prevent an individual from asserting personal ownership. Nothing highlights this better than work for hire in copyright.

The general rule is that the person who creates a work is the author of that work. But there is an exception to that: copyright law defines a category of works called “works made for hire.” If a work is “made for hire” by an

employee, the employer, and not the employee, is considered the author. It is sometimes tricky to determine whether an individual is an employee, but that is not even the surprising part.

You can hire an independent contractor to create a project, direct its development, pay for it in full, and yet not own the copyright. If the author is not your employee, you do not have a work-for-hire agreement, the work at issue does not fit within one of the nine categories specifically listed at Section 101 of the Copyright Act 17 USC 101, and you do not have a written agreement signed by the author and yourself in advance of creation of the work, the best you can get is an assignment of the work. Those nine categories are (1) a work specially ordered or commissioned for use as a contribution to a collective work, (2) as a part of a motion picture or other audiovisual work, (3) as a translation, (4) as a supplementary work, (5) as a compilation, (6) as an instructional text, (7) as a test, (8) as answer material for a test, or (9) as an atlas. See *Community for Creative Non-Violence v. Reid*, 490 U.S. 730 (1989). The practical import of the distinction is the length of the term of the copyright, and whether there will be take-back rights.

Protect Trade Secrets

Protection of trade secrets extends beyond establishing non-competes. The company should take all available measures, including placing the material in a password-protected file that provides limited access, ensuring that all trademarks are registered properly, and ensuring that all goods and services are protected by trademark. Registered trademarks are not necessary to assert ownership, but they create a rebuttal presumption and make the company's and attorney's lives easier. Judges and defendants are affected strongly by seeing a trademark registration. Doing the legwork up front can save time and money—especially if the company is under pressure to act.

Confidentiality agreements that prohibit contractors (and employees) from sharing details of their work with others also add to the protection. Ultimately, the goal is to own all of the IP and establish the protections at the beginning of the process.

Monitor and Audit IP

There are two types of IP audits: internal and external.

1. **Internal.** The documentation required to perform an internal audit is straightforward. The goal is to organize and check all of the IP owned by the company, which should produce copies of all the registrations with the applications. For example, copyright information should note who created it, while trademarks must be supported with proof of sales, advertising, promotion, and third-party promotions. The process and work product should be maintained by counsel in order to preserve privilege. The company may not want to produce some of the communications in response to a subpoena or document demand. For example, and this happens regularly, a client requests counsel to clear a trademark or some other piece of IP. The attorney responds that there is a problem with a third-party mark, but the client proceeds anyway. If that third party later makes a claim against the client, it would be greatly preferable to not have that “smoking gun” communication produced on privilege grounds.
2. **External.** The external audit can actually be an income source. In any situation in which the owner of IP has granted rights to another, such as in a license or distribution agreement, and receives periodic payments under the agreement based on sales, a royalty audit can be a very useful tool in ensuring that the owner is obtaining full realization of the asset. Such an audit requires utilizing an experienced expert, usually an accountant who specializes in audits and knows how and where income is hidden on the accounting books on an hourly or contingency basis. The process can be cost-effective if done properly, and it communicates to the licensee or other member of the agreement that they are being watched.

The benefits of a well-managed IP program are vast. Knowing what you own enables you to ensure coverage for the IP that is important to your business, and thereby to know what can be done to stop others from infringing upon your territory. Sometimes, most commonly in the patent context, this can even result in a “bet the company” action—that is, a

litigation that, if lost, can shut you down either because the damages award will be so great or because you will be enjoined from using someone else's IP, which may be critical to your business. Moreover, a valuation, placed on the goodwill associated with the IP, is often an undervalued and sellable asset that can put the company in an advantageous position.

Communicate with Research and Development Employees

The key to communications with research and development employees is to take an aggressive posture relative to ownership of IP. The employer should provide an invention document or employee agreement with a provision that states that the employer owns everything except for IP that the individual developed before employment started. If the work is not listed as previously created IP, there can be no dispute in the future: the IP is the company's. The provision places a huge burden on the employee, because he or she has to think of everything they created that they want to carve out. The employer must be clear about what is and is not a trade secret, who has access to the secrets, and what employees are allowed to do with these. For example, a general sales representative on the floor of a retail store should not have access to the supplier list. All of the agreements should be documented in writing and signed by all parties who are involved.

Conclusion

In my experience, there are two fundamental reasons IP practitioners love the discipline: its ever-growing breadth and scope, and because it addresses emerging technologies and is typically at the cutting edge. The challenge is keeping abreast of all there is to know.

From the Madrid Protocol, to the Digital Millennium Copyright Act, to the Berne Convention, to California's Proposition 65 and the Consumer Product Safety Improvement Act, to the outer limits of copyright fair use and the RealNetworks DVD decision (*RealNetworks Inc. et al v. Disney Enterprises Inc., et al.*, 3:08-cv-04548-MHP) in the U.S. District Court for the Northern District of California, a full discussion of all the area extends well beyond the scope of this chapter. Will the Second Circuit reverse Judge Sullivan's decision in *Tiffany (NJ) Inc. v. eBay Inc.*, 576 F. Supp. 2d 463 (S.D.N.Y. 2008), and find eBay secondarily liable for the sale of counterfeit

Tiffany merchandise sold on its site? Will the Supreme Court resolve the split in jurisdictions over the issue of whether metatags and keyword sales should be analyzed under trademark law? What about the blurring of the line between the real world and the virtual one? One of my clients recently received a request from a social networking site aimed at teenage girls to use the client's trademarks and clothing designs in the site's virtual stores. What if it had not asked permission?

There are numerous blogs and organizations, such as the International Trademark Association and the Copyright Society of the USA, that are important tools for keeping abreast of this rapidly changing area.

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