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FORMAL BUT FORGIVING: A NEW APPROACH TO PATENT ASSIGNMENTS

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ABSTRACT

This Article contributes to an emerging literature and jurisprudence regarding what role other legal regimes should play in the development of patent law. Some scholars argue that common law systems should be purged from patent law, while others argue that patent law is already too specialized and devoid of generalist law. Further, the Supreme Court has recently struggled deciding patent cases that require consideration or application of other legal regimes, such as contract law, the Bayh-Dole Act, and antitrust law.

This Article argues that scholars and courts have not yet appreciated the interrelatedness of the tension between defining the scope of patent law and the Federal Circuit's adjudicative rule formalism. The Federal Circuit's bright-line, rigid rules are designed to promote certainty, but when those rules are paired with a movement away from a generalist approach to law that is not supported by all of the judges sitting on the Federal Circuit, the result is the opposite of certainty. These interrelated concerns within patent law are perhaps most apparent when contract law and patent law combine to create patent licensing law. The Federal

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Circuit has created its own contract law so that it does not need to consider state contract law, but it is applying this law inconsistently.

This Article demonstrates that state contract law teaches it is both possible and beneficial to have a more nuanced approach to formalism than is currently employed by the Federal Circuit. It further provides a framework for the interpretation of patent assignments, showing how patent licensing law can better allow for differences in the sophistication of both the parties and the assignment itself. This new understanding of formalism will promote sharing of technology and collaboration among inventors and companies, and, overall, greater certainty in patent licensing law.

INTRODUCTION	300
I. OLD PROBLEM, NEW CONTEXT.....	305
A. The Common Law Approach	309
B. The Federal Circuit Approach.....	314
1. The <i>FilmTec</i> Rule: Legal Ownership	314
2. The <i>Arachnid</i> Rule: Equitable Ownership	317
3. The Aftermath of <i>FilmTec</i> and <i>Arachnid</i>	319
4. The Uneasiness of the Supreme Court and Expansion	321
II. LEVELS OF FORMALITY IN CONTRACT LAW.....	327
A. Mechanical Jurisprudence and Lon Fuller	328
B. Formalism in the U.C.C.	332
III. A TAILORED APPROACH TO FORMALITY IN PATENT ASSIGNMENTS	339
A. Identifying the Purpose and Then Tailoring Formality ...	339
B. A Formal But Forgiving Approach for Expectant Interests.....	344
C. A Formal Approach for Transfer of Existing Patents	349
CONCLUSION.....	352

INTRODUCTION

Patent law is complex. Its foundation consists of science that is both formal and abstract and law that is predominately statutory, but that also calls on aspects of the common law systems of property, tort, and contract.¹ This unique combination of science and law produces an intricate system with a challenging objective: finding the balance between the rights and remedies of patent holders that will

1. See Orin S. Kerr, *Rethinking Patent Law in the Administrative State*, 42 WM. & MARY L. REV. 127, 129 (2000); Peter Lee, *Patent Law and the Two Cultures*, 120 YALE L.J. 2, 2 (2011); Ted Sichelman, *Purging Patent Law of "Private Law" Remedies*, 92 TEX. L. REV. 517, 519-20 (2014).

result in the optimal level of innovation.

Congress recognized the difficulty of melding science and different sources of law, and in 1982 created the U.S. Court of Appeals for the Federal Circuit (“Federal Circuit”).² With the proclaimed goal of consistency, the Federal Circuit established a highly formalistic approach to patent doctrine by creating bright-line rules unique to patent law that are both rigid and abstract.³

At first, the Federal Circuit was applauded.⁴ But as years have passed and the reversal rate continues to climb, so has the displeasure with the Federal Circuit.⁵ The Supreme Court continues to strike down the Federal Circuit’s rigid rules in favor of a more balanced, factor-based approach,⁶ and scholars have argued that the Federal Circuit’s formalism impairs innovation and fails to create

2. Federal Courts Improvement Act of 1982, Pub. L. No. 97-164, 96 Stat. 25 (codified as amended in scattered sections of 28 U.S.C.).

3. See S. REP. NO. 97-275, at 5 (1981), *reprinted in* 1982 U.S.C.C.A.N. 11 (“The creation of the Court of Appeals for the Federal Circuit will produce desirable uniformity in . . . [patent] law.”); see also John R. Thomas, *Formalism at the Federal Circuit*, 52 AM. U. L. REV. 771, 774, 793 (2003) (explaining that the “mission” is to “provid[e] more consistent guidance to innovative industry, the Patent Office, and others impacted by the patent system” and that “the Federal Circuit has embraced an increasingly formal jurisprudence” (footnotes omitted)).

4. See, e.g., Rochelle Cooper Dreyfuss, *The Federal Circuit: A Case Study in Specialized Courts*, 64 N.Y.U. L. REV. 1, 74 (1989) (finding that “[o]n the whole, the [Federal Circuit] experiment has worked well for patent law, which is now more uniform, easier to apply, and more responsive to national interests”).

5. See, e.g., Kimberly A. Moore, *Markman Eight Years Later: Is Claim Construction More Predictable?*, 9 LEWIS & CLARK L. REV. 231, 246–47 (2005) (“With judicial claim construction now nearing its adolescence . . . there should be more predictability. The reversal rate ought to be going down, not up.”); Gideon Parchomovsky & R. Polk Wagner, *Patent Portfolios*, 154 U. PA. L. REV. 1, 40–41 (2005) (highlighting claim construction methodology, among others, as “key areas of expanding uncertainty”); Thomas, *supra* note 3, at 795 (noting that district court judges are outspoken regarding “the Federal Circuit’s high reversal rate”).

6. See, e.g., *KSR Int’l Co. v. Teleflex Inc.*, 550 U.S. 398, 415 (2007) (“rejecting the rigid approach of the Court of Appeals”); *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 132, 137 (2007) (holding that the Federal Circuit applied too rigid of a standard for Article III case or controversy requirements); *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 394 (2006) (overturning the Federal Circuit’s presumption for issuing injunctions and mandating it apply the traditional four factors in determining whether to grant a permanent injunction). One notable scholarly contribution in response to the Supreme Court’s recent flurry of activity in patent law is John Golden’s article titled *The Supreme Court as “Prime Percolator”: A Prescription for Appellate Review of Questions in Patent Law*. 56 UCLA L. REV. 657 (2009). In his article, Golden argues that the Supreme Court should “view[] its role with respect to substantive patent law as that of ‘prime percolator,’ rather than ‘final law sayer.’” *Id.* at 662 (footnote omitted). And, further, that in this new role “the Supreme Court should be reluctant to review patent law issues where Federal Circuit judges are already engaged in active debate or recognize significant room for legal development.” *Id.* at 663.

more certainty.⁷

Like Congress, scholars have also recognized that “lawyers and science don’t mix.”⁸ For example, leading scholars in the field have argued that patent law should not be tied to or supported by common law systems.⁹ The crux of this argument is that patent law is now sufficiently robust to stand on its own.¹⁰ On the other hand, there is a growing jurisprudence on the value of other legal regimes in patent law, with much focus on common law systems.¹¹ The growth in this area of scholarship is due in large part to the Supreme Court recently deciding several patent cases that required application, or at least consideration, of other legal regimes.¹²

In this Article, I engage these two concerns—the Federal Circuit’s penchant for rigid rules and the integration of different sources of common law into patent law—and argue that they are best understood as interrelated. I demonstrate so by focusing on the central interaction between the common law system of contract and patent law, which occurs when parties are drafting, and courts interpreting, the licensing of patented technology or assignment of patents.¹³

The licensing and assigning of patents is one of the most important, though under-the-radar, parts of the patent system. In

7. See, e.g., Arti K. Rai, *Engaging Facts and Policy: A Multi-Institutional Approach to Patent System Reform*, 103 COLUM. L. REV. 1035, 1037-39 (2003) (finding the Federal Circuit’s bright lines “suspect” in that they “are insensitive both to technological fact and to related issues of innovation policy”); see also Craig Allen Nard & John F. Duffy, *Rethinking Patent Law’s Uniformity Principle*, 101 Nw. U. L. REV. 1619, 1660, 1629-35 (2007) (highlighting criticisms of the Federal Circuit and arguing that the centralization of appeals decreases opportunities for judges to be innovative when interpreting and analyzing the law, as well opportunities to compete with each other over the production of noteworthy opinions).

8. Lee, *supra* note 1, at 4.

9. See, e.g., Mark A. Lemley, *Property, Intellectual Property, and Free Riding*, 83 TEX. L. REV. 1031, 1075 (2005) (arguing that intellectual property “no longer needs to turn to some broader area of legal theory to seek legitimacy”); Sichelman, *supra* note 1 (arguing for the removal of tort law remedies in patent law).

10. See Lemley, *supra* note 9, at 1075; Sichelman, *supra* note 1.

11. See Jennifer E. Rothman, *Copyright, Custom and Lessons from the Common Law*, in INTELLECTUAL PROPERTY AND THE COMMON LAW 230 (Shyamkrishna Balganesh ed., 2013).

12. See Golden, *supra* note 6, at 667-68, 723-24 (separating and categorizing cases involving “the interaction between patent law and another legal regime” and cases involving “substantive patent law”); see also *Federal Trade Commission v. Actavis, Inc.*, 133 S. Ct. 2223, 2237 (2013) (holding that patent holders must take antitrust law into consideration when settling their disputes).

13. There is arguably another interaction of contract law and patent law, and that is when determining when a commercial offer for sale has occurred, triggering the first of two steps of the on-sale bar. See *Pfaff v. Wells Elec., Inc.* 525 U.S. 55, 67-68 (1998). Orin Kerr has also likened the patent system generally to that of contract law. See Kerr, *supra* note 1, at 135-36.

2009, for example, the Patent Office recorded that “of the 167,349 utility patents granted . . . only 19,894 (11.9%) were issued to individual inventors”; the remaining patents were issued to companies.¹⁴ The general rule in patent law is that the individual inventor (whether an employee or contractor) owns what s/he creates.¹⁵ The high number of patents issued to companies illustrates just how many assignments take place between inventor and company prior to the grant of a patent.¹⁶

The role of contract law in patent law and the most desirable level of formality in patent assignments have not yet been viewed simultaneously. In this Article, I seek to fill that gap in the literature and make two contributions. First, I demonstrate why contract law should not be removed from patent law. Second, I introduce a new framework of formality for the Federal Circuit to use when interpreting patent assignments.

The Federal Circuit has created rigid rules—magic words in the form of “mother may I”—that parties must use when drafting their patent assignments. The Federal Circuit has also determined just recently that only “Federal Circuit contract law” applies to the interpretation of patent assignments.¹⁷ This by itself is perhaps disconcerting, but I find it is most problematic that the Federal Circuit inconsistently applies its own rules. This has resulted in particularly unforgiving and unpredictable interpretations of patent assignments. When the Federal Circuit enforces its patent assignment rules—and, again, it does not do so consistently—the difference in ownership in these cases rests on just a few words: “will assign” or “shall assign” versus “hereby assign.”¹⁸ I find that the Federal Circuit does not apply these bright-line rules consistently because there is disagreement among the judges about the role common law contract should have in the development of patent law.¹⁹

14. See Brief for Alexander M. Shukh, Ph.D. as Amicus Curiae in Support of Petitioner at *9, *Bd. of Trs. of Leland Stanford Junior Univ. v. Roche Molecular Sys., Inc.*, 131 S. Ct. 2188 (2011) (No. 09-1159), 2010 WL 5312673, at *8-10 (employing these statistics to demonstrate the impact of the Federal Circuit’s *FilmTec* and *Arachnid* dichotomy in this area of patent licensing); see also *U.S. Patent Activity Calendar Years 1790 to the Present*, U.S. PATENT & TRADEMARK OFFICE, www.uspto.gov/web/offices/ac/ido/oeip/taf/h_counts.htm (last updated Mar. 26, 2014) [hereinafter, *U.S. Patent Activity*].

15. See *Bd. of Trs. of Leland Stanford Junior Univ. v. Roche Molecular Sys., Inc.*, 131 S. Ct. 2188, 2195 (2011) (“Our precedents confirm the general rule that rights in an invention belong to the inventor.”).

16. See *U.S. Patent Activity*, *supra* note 14.

17. *Abraxis Bioscience, Inc. v. Navinta L.L.C.*, 672 F.3d 1239, 1241 (Fed. Cir. 2011) (O’Malley, J., dissenting).

18. See *infra* Part I.

19. Shubha Ghosh has carefully analyzed the law of assignments, providing details and statistics of the Federal Circuit’s contract jurisprudence, which highlight the

The resulting uncertainty of the Federal Circuit's contract law affects patent holders, companies, and even universities. If the wrong language is used, it may result in a loss of valuable patented technology. Most recently, in *Board of Trustees of Leland Stanford Junior University v. Roche Molecular Systems, Inc.*, a 2011 Supreme Court decision, Stanford University lost all rights to what it reasonably thought was its HIV testing kit patented technology.²⁰ Stanford may have avoided this loss if it had known it needed to use very precise wording, a rule based on uncertain Federal Circuit contract law (as opposed to California contract law).²¹

This Article provides a pragmatic solution to the uncertainty of the law when patent assignments must be interpreted and potentially enforced. Ultimately, formal jurisprudence is good for patent law.²² However, recognition of different levels of formality is needed so that the Federal Circuit can tailor its bright-line rules to achieve predictable and fair results.²³

This Article proceeds in three parts. Part I introduces the tension between the common law system of contract and the Federal Circuit's contract law. The tension began in 1991 when the Federal Circuit first encountered "expectant interests" in patent assignment agreements.²⁴ Part I traces the Federal Circuit's inconsistent treatment of expectant interests in patent assignments, and its recent inconsistent treatment of patent assignments.

Part II discusses how "formalism" is generally used in contract law and patent law, namely, as mechanical jurisprudence. It then draws on Lon Fuller's definition of formalism in contract law to impart a different understanding of formalism. I use Article 2 and Article 9 of the Uniform Commercial Code ("U.C.C.") to illustrate the

"deep rifts" between the Federal Circuit judges. *Short-Circuiting Contract Law: The Federal Circuit's Contract Law Jurisprudence and IP Federalism*, 5, 11 (Feb. 12, 2014) (Working Paper, University of Wisconsin Legal Studies Research Paper 1247 (available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2390214)).

20. 131 S. Ct. 2188 (2011).

21. See *id.* at 2202-04 (Breyer, J., dissenting); see also Ghosh, *supra* note 19, at 4, 23-24; Sean M. O'Connor, *The Aftermath of Stanford v. Roche: Which Law of Assignments Governs?*, 24 INTELL. PROP. J. 29, 29 (2011) (providing a thorough discussion and analysis of the *Stanford* decision and explaining that the Supreme Court did not rule on the Federal Circuit's law on assignment because it limited itself to the first question presented focusing on the interpretation of the Bayh-Dole Act).

22. Peter Lee explains that formal rules allow generalist judges to engage less with technical, scientific issues, which in turn helps to delimit and simplify potentially expansive and unproductive inquiries into patented inventions. See Lee, *supra* note 1, at 7; see also Thomas, *supra* note 3, at 774.

23. See Thomas, *supra* note 3, at 774-75.

24. See *FilmTec. Corp. v. Allied-Signal Inc.*, 939 F.2d 1568 (Fed. Cir. 1991). An expectant interest arises when a party has an interest in the future to some right or property, but at the present moment that right or property is not yet identified or in existence. See *infra*, Part I.

varying levels of formalism in contract law. Article 2 represents the anti-formalist (or “realist”) approach, with Article 9 representing the most formal approach in the U.C.C.

Part III analyzes these levels of formality in Article 2 and Article 9 by identifying the purpose of the law and then deciding the best level of formality to use given that purpose. I then apply that framework to patent licensing law and propose a normative argument for how the Federal Circuit can promote clearer and more predictable interpretation of patent assignments. As done in Article 9, the Federal Circuit should adopt two separate levels of formality: a formal, forgiving level for when courts are faced with interpreting expectant interest clauses, and a formal, unforgiving level of formality for patent assignments that transfer already-existing patents.

I. OLD PROBLEM, NEW CONTEXT

In its simplest form, a patent assignment sells and conveys the ownership of a patent to another.²⁵ It is on this basis—that a patent assignment is a contract—that the Federal Circuit has historically applied state contract law when faced with an issue involving a patent assignment.²⁶ In particular, the Federal Circuit has stated that determining who owns the patent rights and on what terms is a matter for state courts.²⁷ This deference to state law also aligns with Supreme Court jurisprudence, which has long held that state law governs contracts even when federally created rights are involved.²⁸

However, in recent years, the Federal Circuit has held multiple times that federal law, or what one Federal Circuit judge termed “Federal Circuit contract law,” is the proper law to apply when analyzing patent assignments for ownership rights.²⁹ Determining

25. See generally 35 U.S.C. § 261 (2012) (outlining ownership and assignment qualities of patents).

26. For example, the Federal Circuit found in *Euclid Chemical Co. v. Vector Corrosion Technologies, Inc.* that “[c]onstruction of patent assignment agreements is a matter of state contract law.” 561 F.3d 1340, 1343 (Fed. Cir. 2009) (quoting *Mars, Inc. v. Coin Acceptors, Inc.*, 527 F.3d 1359, 1370 (Fed. Cir. 2008)). Similarly, the Federal Circuit applied California contract law in *Alfred E. Mann Foundation for Scientific Research v. Cochlear Corp.* in determining whether or not an exclusive license should be treated the same as an assignment for standing purposes. 604 F.3d 1354, 1359 (Fed. Cir. 2010).

27. See *Jim Arnold Corp. v. Hydrotech Sys.*, 109 F.3d 1567, 1572 (Fed. Cir. 1997) (“[T]he question of who owns the patent rights and on what terms typically is a question exclusively for state courts.”); *Tri-Star Elecs. Int’l, Inc. v. Preci-Dip Durtal SA*, 619 F.3d 1364, 1367 (Fed. Cir. 2010) (“An assignment of a patent is interpreted in accordance with statutory and common law of contract.”).

28. The courts have applied this reasoning and defer to state law even when the contracts involve federally created rights. See, e.g., *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257, 262 (1979).

29. *Abraxis Bioscience, Inc. v. Navinta L.L.C.*, 672 F.3d 1239, 1241 (Fed. Cir. 2011)

whether a party has legal ownership of a patent is crucial in the determination of which cause of action is available—patent infringement or breach of contract³⁰—and that, in turn, dictates the applicable remedy structure.³¹

Jurisdiction over patents is exclusively saved for federal courts, and, likewise, standing to sue in patent cases is a matter of federal law.³² If the plaintiff does not have legal title to the asserted patent, then she also does not have standing to file an infringement action under that patent.³³ The party bringing the suit does not only want access to a breach of contract action; the party wants access to patent damages.³⁴

Patent damages are frequently in the news because of the high dollar amounts; recently, for example, the *Apple v. Samsung* litigation resulted in a stunning damage award of more than one billion dollars.³⁵ Patent damages have the potential to be much more lucrative than contract damages.³⁶ This is because the patent holder in a patent infringement suit elects to receive either “lost profits or a reasonable royalty.”³⁷ The lost profits category allows a patent holder to receive the profits it would have made but for the defendant’s infringement.³⁸ The reasonable royalty compensates the patent holder for the value of the use that the infringer received from the patented invention.³⁹

(O’Malley, J., dissenting).

30. *See* *Crown Die & Tool Co. v. Nye Tool & Mach. Works*, 261 U.S. 24, 33-34 (1923).

31. *Id.*

32. *DDB Techs., L.L.C. v. MLB Advanced Media, L.P.*, 517 F.3d 1284, 1290 (Fed. Cir. 2008) (citations omitted).

33. *Crown Die & Tool Co.*, 261 U.S. at 40 (citation omitted) (internal quotation marks omitted) (stating that the plaintiff in a patent infringement action must have “legal title to the patent . . . at the time of infringement,” which is at least the time of the filing of the lawsuit); *see also* *Arachnid, Inc. v. Merit Indus. Inc.*, 939 F.2d 1574, 1579 (Fed. Cir. 1991) (“The general rule is that one seeking to recover money damages for infringement of a United States patent (an action ‘at law’) must have held the legal title to the patent during the time of the infringement.”) (emphasis omitted).

34. *See* Nick Wingfield, *Jury Awards \$1 Billion to Apple in Samsung Patent Case*, N.Y. TIMES (Aug. 24, 2012), http://www.nytimes.com/2012/08/25/technology/jury-reaches-decision-in-apple-samsung-patent-trial.html?_r=0 (“[The jurors] found that Samsung infringed on a series of Apple’s patents on mobile devices, awarding Apple more than \$1 billion in damages.”).

35. *See id.*

36. *See id.* (“Because Samsung was found to have willfully infringed Apple patents, the judge . . . could grant . . . triple the damages . . .”).

37. David W. Opderbeck, *Patent Damages Reform and the Shape of Patent Law*, 89 B.U. L. REV. 127, 132 (2009) (footnote omitted).

38. *Id.* at 132-33 (“In all cases, the patentee must prove causation connecting the infringement and the lost profits.” (footnote omitted)).

39. *See* Mark A. Lemley, *Distinguishing Lost Profits from Reasonable Royalties*, 51 WM. & MARY L. REV. 655, 661 (2009).

Unlike in contract law, a successful patent holder is also eligible for extracompensatory damages.⁴⁰ In cases of willful infringement, the Patent Act grants courts the discretion to enhance “damages up to three times the amount” of the base or compensatory award.⁴¹ Further, after a patent holder receives base monetary damages and potentially enhanced damages, the patent holder may also request a permanent injunction and for the defendant to pay its costs and attorney’s fees.⁴²

Again, in order to have access to these damages, the party bringing the patent infringement suit bears the burden of establishing that it had the requisite ownership interest prior to filing the lawsuit.⁴³ Since 1790, the general rule in patent law is that all rights to an invention belong to the inventor.⁴⁴ However, the party bringing the suit here may be one that is not the inventor, but a successor in title, an assignee, or an exclusive licensee with all substantial rights.⁴⁵ If the party is an assignor or exclusive licensee, it must have this transfer of ownership in writing.⁴⁶

Federal courts are faced with ownership challenges (and therefore standing challenges) in patent infringement suits when the party bringing the action is an exclusive licensee or assignee of the patent.⁴⁷ Frequently, this challenge occurs when there is an assignment of future rights to intellectual property that is

40. See *Graco, Inc. v. Binks Mfg. Co.*, 60 F.3d 785, 792 (Fed. Cir. 1995) (“Willfulness of the infringement is the sole basis for the court’s exercise of its discretion to enhance damages under 35 U.S.C. § 284 (1988).”); see also *In re Seagate Tech., L.L.C.*, 497 F.3d 1360, 1371 (Fed. Cir. 2007) (holding “that proof of willful infringement permitting enhanced damages requires at least a showing of objective recklessness”).

41. 35 U.S.C. § 284 (2012); see, e.g., *In re Seagate Tech., L.L.C.*, 497 F.3d 1360, 1368 (Fed. Cir. 2007).

42. See 35 U.S.C. §§ 283, 285.

43. See *Crown Die & Tool Co. v. Nye Tool & Mach. Works*, 261 U.S. 24, 39-40 (1923). Just like in other non-patent contexts, the plaintiff must present “competent proof,” supported by a preponderance of the evidence that standing exists. See *Sicom Sys., Ltd. v. Agilent Techs. Inc.*, 427 F.3d 971, 975-77 (Fed. Cir. 2005).

44. See *Bd. of Trs. of Leland Stanford Junior Univ. v. Roche Molecular Sys., Inc.*, 131 S. Ct. 2188, 2192 (2011).

45. The Patent Act provides that “[a] patentee shall have remedy by civil action for infringement of his patent.” 35 U.S.C. § 281. The term “patentee” may either be the party to whom the patent was originally issued, or a successor in title to that party. *Id.* § 100. The successor in title, the assignee, may also be an exclusive licensee that was granted all the substantial rights to the patent. *Propat Int’l Corp. v. Rpost, Inc.*, 473 F.3d 1187, 1193 (Fed. Cir. 2007). Non-exclusive licensees do not have standing to sue for patent infringement. See *id.* at 1193.

46. 35 U.S.C. § 261 (“Applications for patent, patents, or any interest therein, shall be assignable in law by an instrument in writing.”).

47. See *Propat Int’l Corp.*, 473 F.3d at 1193.

nonexistent at the time of the contract.⁴⁸ A hypothetical will help illustrate.

Let us say that Jordan, a recent graduate, joins the research staff at Atkinson Acre Technology Company (AATC). On Jordan's first day of work, AATC and Jordan execute an employment contract stating that AATC will own any intellectual property that Jordan creates during employment. At the time of signing the agreement, Jordan's first day of work, no invention or intellectual property exists. Certainly, therefore, at this point no patentable interest exists. It may exist in the future, but it does not exist in the present. This is termed an "expectant interest" in patent law.⁴⁹ But just a few months later at work, Jordan conceives a great idea for new, potentially patentable technology. What, if anything, is needed to ensure that ownership of this idea is legally transferred from Jordan to AATC? Oftentimes, the pivotal issue here is whether the patentable idea transfers to AATC automatically, that is, without a need for any further act of conveyance by either AATC or Jordan, or whether Jordan must do something else to convey ownership to AATC. This conveyance may be shortly after Jordan conceives of the idea, or perhaps down the road after the patent is applied for and/or obtained.

The growing confusion here is not just concerning which law to apply to the expectant interest clause in Jordan's contract (state contract law versus Federal Circuit), but whether particular language needs to be used in order to obtain a particular result. Currently, the Federal Circuit requires very specific language for parties like AATC to ensure that AATC does not need any further act or conveyance from Jordan to obtain legal title to the patentable interest.⁵⁰

The Federal Circuit's approach is rigid, and quite unforgiving, if the parties do not use the necessary magic words; however, under state contract law, courts generally look at the entire picture, both the words and the intent of the parties.⁵¹ There is not one particular word or phrase that is given more weight than others. These so-called "magic words" serve as the dividing line in the Federal Circuit between being declared a legal owner or merely an equitable owner of

48. See G. Sage Lyons, *The Sale of Future Goods*, 11 ALA. L. REV. 320, 322 (1958).

49. E.g., *FilmTec Corp. v. Allied-Signal Inc.*, 939 F.2d 1568, 1572 (Fed. Cir. 1991) ("If an assignment of rights in an invention is made prior to the existence of the invention, this may be viewed as an assignment of an expectant interest.").

50. See *id.*; *Bd. of Trs. of Leland Stanford Junior Univ. v. Roche Molecular Sys., Inc.*, 131 S. Ct. 2188, 2194-200 (2011); *Propat Int'l Corp.*, 473 F.3d at 1191-94.

51. See *In re G.D.H.*, 366 S.W.3d 766, 769 (Tex. App. 2012), *reh'g overruled* (Apr. 30, 2012); *Auto Glass Exp., Inc. v. Hanover Ins. Co.*, 975 A.2d 1266, 1271-72 (Conn. 2009); *City of Grosse Pointe Park v. Michigan Mun. Liab. & Prop. Pool*, 702 N.W.2d 106, 112-13 (Mich. 2005).

the patent.⁵² Of course, this assumes that the Federal Circuit applies this “magic word” approach. If it does not, then the analysis much more closely mirrors that of state courts.

From the example above, if AATC is the *legal* owner of a patent conceived of by Jordan, and a company, let’s name it “Blackacre Technology” (“BT”), infringes this patent, AATC may file a patent infringement suit and have access to the lucrative patent remedy structure. But if AATC is only the *equitable* owner, as opposed to legal owner, caused most likely because some further act of conveyance was necessary to perfect its ownership of what Jordan conceived of while employed, then AATC will not have standing to bring a patent infringement suit. Consequently, the landscape of patent damages detailed above is not available. At best AATC may be left with a breach of contract action against Jordan with no recourse against BT until it gains legal ownership of the patent.

Many of these patent standing cases are further complicated when Jordan, the inventor, works for another company at the same time she works at AATC or claims that she conceived of the invention after her employment ended at AATC. Accordingly, there would also need to be litigation to determine when precisely the invention was conceptualized and which party at that moment had the trump card of the employment agreement.

The Federal Circuit did not encounter its first expectant interest case until 1991.⁵³ And although the Federal Circuit cited common law cases and leading law review articles relating to expectant interests, there was little discussion of this law or whether state law should play a role in the interpretation of the contract.⁵⁴ Furthermore, the Federal Circuit did not follow the rules of the common law system contained in the early cases cited, nor those that were explained by Samuel Williston in his seminal 1906 article *Transfers of After-Acquired Personal Property*.⁵⁵

A. *The Common Law Approach*

Similar to an expectant interest in patent law, a “future good” is personal property that at the time of contracting is either unidentified or nonexistent.⁵⁶ Historically, a contract to sell or other transfer of a future good conveyed only “an equitable lien [on] the

52. See *Bd. of Trs. of Leland Stanford Junior Univ.*, 131 S. Ct. at 2203-05.

53. *FilmTec Corp.*, 939 F.2d at 1572-73 (addressing expectant interest for the first time).

54. See *id.*

55. Samuel Williston, *Transfers of After-Acquired Personal Property*, 19 HARV. L. REV. 557, 557-69 (1906); see also Lyons, *supra* note 48, at 320 (“Future goods are goods not in existence at the time of the making of the contract of sale or those to be subsequently acquired or manufactured by the seller.”).

56. Williston, *supra* note 55, at 557.

property.”⁵⁷ It did not matter what form the contract was in or what words were used; a contract to sell a good not yet existing resulted in a lesser right than a legal lien or actual legal title to the property.⁵⁸ Although it is not quite clear in common law what the distinction was between legal and equitable title, Williston reported that equitable title did not convey full legal rights to the property.⁵⁹

During this time of equitable ownership, only a bona fide purchaser for value without notice would trump the rights of the entitlement holder.⁶⁰ It was not until the moment that the property was identified or possession gained that the entitlement holder could obtain legal title to the property.⁶¹ Generally, in order to make the transition from equitable title to legal title, a further conveyance or “act of performance by the seller” was needed.⁶²

A notable exception to this general bar against transferring legal title to goods not yet possessed or in existence is “the doctrine of potential possession.”⁶³ This doctrine, as explained by the English case *Grantham v. Hawley*, allows the transfer of legal title of certain future goods without any further act of conveyance.⁶⁴ The *Grantham* court found that “crops of specified land, the wool to be clipped in the future from specified sheep or the future young of specified animals, can be bargained and sold at law, because the seller has ‘potential possession.’”⁶⁵ Following this reasoning, at least with future crops

57. *Id.*

58. *See id.*

59. *See, e.g.,* Samuel Williston, *Is the Right of an Assignee of a Chose in Action Legal or Equitable?*, 30 HARV. L. REV. 97, 106-07 (1916) [hereinafter Williston, *Right of an Assignee*] (arguing that an assignee of a chose of action only obtained an equitable interest); *cf.* Grant Gilmore, *The Assignee of Contract Rights and His Precarious Security*, 74 YALE L.J. 217, 221 (1964) (making the assumption that “choses in action” can be legally transferred and stating that he does not know what a “merely equitable interest” meant or currently means). Access to court and monetary damages, for example, might be more limited if legal title was not possessed. *See* Schmid v. Baum's Home of Flowers, 37 S.W.2d 105, 111 (Tenn. 1931) (holding that the scope of enforceability of equitable interests of a receiver “depend[ed] upon the terms of the deeds of trust under which he claim[ed], as well as upon the equities asserted in the proceeding in which the receivership was ordered”).

60. *See* Williston, *supra* note 55, at 558-63 (emphasis omitted).

61. *See id.* at 559, 578.

62. *See* Lyons, *supra* note 48, at 321-22.

63. *Id.* at 322.

64. *See* *Grantham v. Hawley*, (1792) 80 Eng. Rep. 281 (K.B.) 281-82 (holding that a lessor with potential but not actual possession of goods could transfer its interest).

65. Williston, *supra* note 55, at 558; *see* *Grantham*, 80 Eng. Rep. at 282 (“[L]and is the mother and root of all fruits. Therefore he that hath it may grant all fruits that may arise upon it after, and the property shall pass as soon as the fruits are extant.”); *see also* Lyons, *supra* note 48, at 323 (explaining that a good is in “potential existence” if it is already planted or there is an expected increase of a crop or offspring of goods that are already in existence and owned by the seller).

and offspring of a seller's animals, early courts were willing to impose a legal fiction that the seller already had possession of the goods and could therefore transfer legal title.⁶⁶ As soon as the crops grew and matured or the lamb was born, legal title would transfer automatically to the buyer.⁶⁷ This transfer was effective back to the original contract execution date.⁶⁸

The doctrine of potential possession was likewise adopted in the United States.⁶⁹ This doctrine was used in situations other than in those of future crops and unborn animals, most notably for the transfer of oil interests.⁷⁰ Some states even adopted a specific statute recognizing the doctrine of potential possession.⁷¹

When faced with interpreting the parties' agreements and determining whether the parties meant to convey legal title or just equitable title with some further act of conveyance to complete the transfer, early American courts looked to both the contractual language used in the agreement and the intent of the parties.⁷² Courts seemed to emphasize particular language such as "assigns, transfers and conveys"⁷³ or "absolute sale."⁷⁴ They also gathered information regarding the structure of the companies and their business transactions to determine what the parties likely intended to accomplish with their respective agreements.⁷⁵

66. Williston, *supra* note 55, at 558.

67. *See* Lyons, *supra* note 48, at 322-23.

68. *Id.* at 323.

69. This doctrine has been met with some resistance. *See, e.g.*, *Cole v. Kerr*, 26 N.W. 598, 599 (Neb. 1886) (declining to follow *Grantham* because "it cannot be said that the mere ownership or possession of the soil carries with it the production of crops potentially. Soil alone does not produce crops of corn in this degenerate age, if it ever did. It now requires, in addition to soil, seed and labor, both of man and beast . . .").

70. *See, e.g.*, *Black v. Solano Co.*, 299 P. 843, 845 (Cal. Ct. App. 1931); *Merrill v. Cal. Petrol. Corp.*, 288 P. 721, 723 (Cal. Ct. App. 1930).

71. *See, e.g.*, OKLA. STAT. tit. 42, § 8 (1951).

72. *See, e.g.*, *W. Oil & Ref. Co. v. Venago Oil Corp.*, 24 P.2d 971 (Cal. 1933); *Hogue-Kellogg Co. v. Baker*, 190 P. 493 (Cal. 1920).

73. *See, e.g.*, *Western Oil*, 24 P.2d at 973.

74. *See, e.g.*, *Hogue-Kellogg Co.*, 190 P. at 494 (contract stated "this contract is understood by both parties to pass title and constitute an absolute sale"); *Hamilton v. Klinke*, 183 P. 675, 678 (Cal. 1919) (contract stated "[i]t is mutually understood and agreed that this contract . . . constitutes an absolute sale").

75. *See Western Oil*, 24 P.2d at 972-73 (analyzing the corporate structure of the company and how it was sold with the accompanying agreement to help determine the intent of the parties in transferring rights to potential oil). The doctrine of potential possession—the exception to the general rule of future goods in common law—is nonexistent in Article 2 of the U.C.C. Article 2 states that where the parties purport to effect a present "sale of future goods," the agreement "operates as a contract to sell" the goods. U.C.C. § 2-105 (2) (2013). Article 2 also explains that "[g]oods must be both existing and identified before any interest in them can pass. Goods which are not both existing and identified are 'future' goods." *Id.* Accordingly, under Article 2 there must be some further conveyance or act of performance by the seller to effectuate the

The law of future goods and the distinction between a contract to sell and a present sale was settled much earlier than the law of choses in action.⁷⁶ The transfer of potential legal rights and intangibles, including patents,⁷⁷ is currently a dominating part of secured financing, and different rules have surfaced as the law in this area has developed. Similar to the sale of goods where there is a distinction between a present sale and a promise to sell, common law courts at first made a distinction between a present interest in payments due (which when transferred created a legal interest) and an expectant interest in payments due (which only transferred an equitable lien).⁷⁸

Early sources found that “[i]t has been said to be a rule rather of logic than of law that a man cannot transfer title to property he does not own or, as the Latin tag has it: *Qui non habet, ille non dat.*”⁷⁹ Like with the sale of future goods, this transfer of future rights was “only an imperfect or ‘equitable’ interest.”⁸⁰ However, the former dissenting position starting gaining traction,⁸¹ and now this once minority viewpoint is largely in line with current doctrine of assignments of future intangibles.

Article 9 of the U.C.C. addresses whether expectant interests, termed “after-acquired property” in this context, need a further act of conveyance once they come into existence.⁸² In exchange for a loan, a borrower (debtor) generally identifies specified collateral owned by

transfer to the buyer.

76. See Williston, *supra* note 55, at 562-63 (documenting that the law in 1906 did not generally allow existing choses in action to be transferred).

77. See *Contract Rights as Commercial Security: Present and Future Intangibles*, 67 YALE L.J. 847, 847 n.1 (1958) [hereinafter *Contract Rights as Commercial Security*] (“The term intangible includes both choses in action, *i.e.*, claims based on legal rights . . . [and] [s]ome types of intangible property . . . [such as] patents, copyrights, leases, licenses and secret processes.”); see also U.C.C. § 9-102 (a)(42) (“‘General intangibles’ means any personal property, including things in action, other than accounts, chattel paper, commercial tort claims, deposit accounts, documents, goods, instruments . . . [and] money . . .”).

78. See, *e.g.*, *Rockmore v. Lehman*, 128 F.2d 564, 566-67 (2d Cir. 1942) (originally holding that, at best, the assignment created an equitable lien), *rev’d on rehearing*, 129 F.2d 892 (2d Cir. 1942).

79. GRANT GILMORE, *SECURITY INTERESTS IN PERSONAL PROPERTY* 228-29 (1965).

80. *Id.* at 229; see also *Contract Rights as Commercial Security*, *supra* note 77, at 851 (explaining that “to be fully effective, an assignment must be legal not equitable and involve present rather than future property”).

81. *Rockmore*, 128 F.2d at 567 (Clark, J., dissenting). As one dissent explained (which was later adopted on rehearing), “I do not believe the decisions require so ancient a theory as that an assignment of definite contract rights, future only in the sense that they are conditioned upon the performance which the promisee has promised, is only a promise to pay out of future funds and not a present transfer.” *Id.*

82. See U.C.C. § 9-204 (2010).

her that the lender (creditor) may take if she defaults on the loan.⁸³ This collateral may already exist—such as tools in a shop—or it can be an expectant interest—such as rights to accounts that one will acquire in the future.⁸⁴

The Article 9 provision covering after-acquired property is sometimes referred to as the “floating lien” or “floating security interest” provision.⁸⁵ This provision states that obligations covered by the security agreement may be secured by after-acquired collateral, and, further, that the obligations may include future advances as described by the security agreement.⁸⁶ The second official comment of the floating-lien provision states:

a security interest arising by virtue of an after-acquired property clause is no less valid than a security interest in collateral in which the debtor has rights at the time value is given. A security interest in after-acquired property is not merely an “equitable” interest; no further action by the secured party—such as a supplemental agreement covering the new collateral—is required.⁸⁷

Accordingly, much like the doctrine of potential possession, under Article 9 expectant interests in security agreements are automatically converted into legal interests once the property is identified or comes into existence.⁸⁸

The next part will look at how the Federal Circuit handles expectant interests in patent assignments. Instead of having one fixed rule like Article 2 (cannot convey future goods without further conveyance)⁸⁹ or Article 9 (can use after-acquired property as current collateral),⁹⁰ the Federal Circuit has two rules and focuses on the particular words used to convey the expectant patentable interest to determine which rule to apply in its interpretation of the assignment.⁹¹

83. *See Id.* § 9-102(a)(28).

84. *See Id.* § 9-102(a)(12).

85. *Id.* § 9-204; *see also* Knox v. Phoenix Leasing Inc., 35 Cal. Rptr. 2d 141, 148 (Ct. App. 1994) (“One of the notable features of article 9 is its approval of the concept of the so-called ‘floating lien’ generated by security interests extending to after-acquired debtor property.”).

86. *See* U.C.C. § 9-204 (stating that “a security agreement may provide that” any or all obligations covered by the security agreement are to be secured by after-acquired collateral and that obligations covered by a security agreement may include “future advances or other value, whether or not the advances or value are given pursuant to commitment”).

87. *Id.* cmt. 2 (emphasis added).

88. *Id.*; *see also* Grantham v. Hawley, (1792) 80 Eng Rep. 281 (K.B.).

89. U.C.C. § 2-202.

90. *Id.* § 9-204.

91. *See* discussion *infra* Part II.B.

B. The Federal Circuit Approach

The Federal Circuit directly confronted expectant interest clauses in *FilmTec Corp., v. Allied-Signal Inc.*,⁹² published just days before its sister opinion, *Arachnid, Inc. v. Merit Industries, Inc.*⁹³ With these two cases, the Federal Circuit created extremely rigid rules unique to patent law, and at first, these rules seemed to apply only in situations similar to the Jordan and AATC hypothetical—contracts that involved expectant interest clauses.⁹⁴

But recently, the Federal Circuit has extended these rules to patent assignments, that purport to transfer already existing patents.⁹⁵ In lieu of using state contract law to interpret when title was passed and what happens when there is a gap in possession and transfer of the title as it has historically done, the Federal Circuit is now applying the *FilmTec* and *Arachnid* rules.⁹⁶ The following discussion will explain the *FilmTec* and *Arachnid* rules and explore how the Federal Circuit and district courts are applying these rules.

1. The *FilmTec* Rule: Legal Ownership

The inventor in *FilmTec Corp. v. Allied-Signal, Inc.*, John Cadotte, filed a patent application claiming a reverse osmosis membrane.⁹⁷ Such a membrane may be commercially useful in purifying salt-containing solutions and desalinizing seawater.⁹⁸ Shortly after filing this application, Cadotte assigned his rights to the patent application and any subsequently issued patent to FilmTec.⁹⁹ Cadotte, along with three others, founded FilmTec.¹⁰⁰ Thereafter, FilmTec sued Allied for infringement of Cadotte's (now allegedly FilmTec's) reverse osmosis membrane patent.

On appeal to the Federal Circuit, Defendant Allied pointed to a contract between North Star Division of Midwest Research Institute

92. 939 F.2d 1568 (Fed. Cir. 1991).

93. 939 F.2d 1574 (Fed. Cir. 1991).

94. *Id.* at 1581-82; *FilmTec Corp.*, 939 F.2d at 1572-73; *see supra* Part I.A.

95. *See infra* text accompanying notes 138-48.

96. *See infra* text accompanying notes 138-48.

97. 939 F.2d at 1569-70. The patent also claimed a corresponding method employing "the membrane to reduce the concentration of solute molecules and ions in solution." *Id.*

98. *Id.* at 1570 n.1.

99. This assignment was recorded with the United States Patent and Trademark Office ("USPTO"). *Id.* at 1570. This matters with regard to subsequent purchasers, but the recording does not offer any weight to, or a presumption of, the assignment's validity. *See* 35 U.S.C. § 261 (2012) ("An assignment, grant or conveyance shall be void as against any subsequent purchaser or mortgagee for a valuable consideration, without notice, unless it is recorded in the Patent and Trademark Office within three months from its date or prior to the date of such subsequent purchase or mortgage.").

100. 939 F.2d at 1570.

(“MRI”) and the United States (“the Government”) that Allied argued could defeat FilmTec’s standing to bring the patent infringement suit.¹⁰¹ One clause in this contract stated that MRI “*agrees to grant and does hereby grant* to the Government the full and entire domestic right, title and interest in [any invention, discovery, improvement or development (whether or not patentable) made in the course of or under this contract or any subcontract (of any tier) thereunder].”¹⁰²

The significance, Allied argued, is that this expectant interest clause shows that anything conceived while MRI was working with the Government is owned by the Government.¹⁰³ Allied made this connection because prior to founding FilmTec, Cadotte and his other cofounders worked at MRI.¹⁰⁴ At this time, MRI did much of its research for the Government in the field of reverse osmosis membranes, and Allied pointed to lab notebooks showing that Cadotte conceived of the patented technology while employed with MRI.¹⁰⁵ Consequently, Allied argued that Cadotte did not own legal title to the patent application and therefore could not assign any resulting patent to FilmTec.¹⁰⁶ If this were true, then FilmTec would not legally own the patent and, therefore, the patent infringement suit against Allied would be dismissed based on lack of standing.¹⁰⁷

The Federal Circuit saw this as an expectant interest issue because of the agreement between MRI and the Government that “agrees to grant and does hereby grant” ownership of all discoveries

101. *Id.* at 1570-71.

102. *Id.* at 1570. (emphasis added).

103. *Id.* at 1571.

104. *Id.* at 1570-71.

105. *Id.* at 1570. The district court did not make a final ruling on whether the invention was in fact conceptualized during Cadotte’s employment with MRI. *Id.* It did not do so because at most, the district court stated that the Government would only have equitable rights to the patented invention. *Id.* The district court came to this conclusion after analyzing the language of the agreement between MRI and the Government, and then granted a preliminary injunction to FilmTec against Allied’s use of the patented infringement. *Id.* at 1570, 1573.

106. *Id.* at 1571. A missing piece here is a similar agreement between Cadotte and MRI. Without this agreement, it is not clear that anything Cadotte created automatically belongs to MRI. At most, it seems like MRI would only have shop rights in the patent. These rights would allow MRI to use the patented invention at no cost, but would not transfer any ownership interest to MRI. Paul M. Rivard, *Protection of Business Investments in Human Capital: Shop Right and Related Doctrines*, 79 J. PAT & TRADEMARK OFF. SOC’Y 753, 757 (1997). Nevertheless, the Federal Circuit continued in its analysis.

107. *Filmtec*, 939 F.2d at 1571. Upon review, the Federal Circuit stated that the district court did not address whether an employment agreement existed between Cadotte and MRI. *Id.* The Federal Circuit noted that this gap in the record created a hurdle in analyzing ownership of the patent. *Id.* at 1571-72. Nevertheless, it continued its analysis.

made by MRI to the Government.¹⁰⁸ The Federal Circuit explained that an expectant interest is a conveyance that is made prior to the existence of the interest or entitlement.¹⁰⁹

It then created the *FilmTec* rule,¹¹⁰ which provides that no further act is needed to convey legal title when the words “does hereby grant” are used.¹¹¹ The *FilmTec* court created this rule after finding that the contract between MRI and the government was an assignment for “future goods,” and, further, that this assignment initially only conveyed equitable title.¹¹² However, the Federal Circuit found that, once the property comes into existence, “no further act would be required” and that “the transfer of title would occur by operation of law.”¹¹³ Consequently, as soon as MRI conceived of an invention, the ownership of such invention was automatically granted to the government.

Overall, the Federal Circuit focused on the “does hereby grant” words and although it cited the common law regarding goods (where a further act of conveyance is needed to morph equitable title to legal title), it aligned with the exception to the general rule of future goods—that of potential possession—and what Article 9 allows for after-acquired property.¹¹⁴ In adopting the Article 9 rule for after-acquired property, the Federal Circuit seemed to adopt the “first in time, first in right” rule in Article 9.¹¹⁵

Here, Cadotte and the other inventors signed the agreement with MRI first, and then subsequently signed a conflicting agreement with FilmTec. The Federal Circuit’s holding gave priority to the first contract the inventors signed (the one with MRI). Perhaps the uncertainty of the law stemming from the *FilmTec* rule could have been avoided if the Federal Circuit explicitly agreed to a formal “first in time, first in right” rule. It did not do so, and as the discussion below demonstrates, the law of assignments only gets more uncertain after this case.

108. *Id.* at 1570, 1572.

109. *Id.* at 1572.

110. *Id.*

111. *Id.* at 1570, 1572.

112. *Id.* at 1572 n.8.

113. *Id.* at 1573.

114. *Id.* at 1570, 1572; *see also* O’Connor, *supra* note 21, at 6-7 (noting that the Federal Circuit “did not state whether it was basing its decision on an application of state law—which normally governs contract interpretation—or establishing a rule of federal common law”).

115. *See* Steven L. Schwarcz, *The Impact on Securitization of Revised UCC Article, 974 CHI-KENT L. REV. 947, 956* (explaining that Article 9 generally accords priority “to the first secured creditor to file or perfect[] under a rule usually referred to as ‘first in time, first in right’”). Many thanks to Shubha Ghosh for helping me appreciate this point of priority in the *FilmTec* rule.

2. The *Arachnid* Rule: Equitable Ownership

As mentioned above, the Federal Circuit published its decision in *Arachnid, Inc. v. Merit Industries, Inc.* just days after *FilmTec*.¹¹⁶ In this opinion, the *Arachnid* rule was created, which follows the common law position and current Article 2 position that a further act of conveyance is needed to transfer legal title.¹¹⁷

Like in *FilmTec*, the legal issue here was whether the plaintiff, Arachnid, Inc. (“Arachnid”) had legal title to the patented invention when it filed its patent infringement suit against Merit Industries, Inc. (“Merit”).¹¹⁸ In 1980 Arachnid entered into a consulting agreement with Industrial Design Electronic Associates (“IDEA”).¹¹⁹ Pursuant to this agreement, “IDEA was to provide consulting services [to Arachnid to] improve[] . . . the computerized scoring system of Arachnid’s [electronic] dart games.¹²⁰ The agreement stated that “[a]ny inventions conceived by IDEA or its employees . . . in the course of the project covered by this agreement, shall be the property of [] [Arachnid], and all rights thereto *will be assigned* by IDEA . . . to [Arachnid].”¹²¹

Several months after the agreement between IDEA and Arachnid was terminated, IDEA engineers filed a patent application claiming a “coin-operated electronic dart game that is . . . scored by two microprocessors.”¹²² The inventors, including IDEA’s president, assigned the patent application and any subsequently resulting patent to IDEA.¹²³ At this point Arachnid already had an existing lawsuit against IDEA claiming infringement of another patent, but it amended that complaint to include a demand for “an assignment of all rights, title, and interest, both legal and equitable” in the patent application (which subsequently resulted in an issued patent).¹²⁴

During the period of this litigation, specifically May 6, 1985, IDEA entered into a nonexclusive licensing agreement with Merit, the defendant in this action.¹²⁵ In the licensing agreement Merit was granted the right to practice the patented invention at issue here,

116. *Arachnid, Inc. v. Merit Indus., Inc.*, 939 F.2d 1574 (Fed. Cir. 1991).

117. *Id.* at 1577-82; *see also supra* Part I.A.

118. *Arachnid, Inc.*, 939 F.2d at 1576.

119. *Id.*

120. *Id.*

121. *Id.*

122. *Id.* at n.1. Instead of being controlled by one microprocessor as prior dart games were, the patent application claims an electronic game “controlled and scored by two microprocessors.” *Id.*

123. *Id.* at 1576.

124. *Id.* Arachnid included in this amendment claims for breach of the consulting agreement and unjust enrichment in relation to IDEA’s use of what Arachnid considered its technology. *See id.*

125. *Id.* at 1576-77.

and from December 1985 through June 1986 sold hundreds of infringing games.¹²⁶ It was for this infringement period that Arachnid sought damages.¹²⁷ Arachnid filed this lawsuit against Merit in 1986, and Merit filed a motion for partial dismissal based on its position that Arachnid did not own the patent at this time and therefore had no standing to sue.¹²⁸ At most, Merit argued, Arachnid owned equitable title.¹²⁹

Further complicating the lawsuit, in April of 1987, in the earlier lawsuit against IDEA, a jury decided that the patented invention was indeed “conceived while IDEA was under contract” with Arachnid.¹³⁰ As a result, on April 27, 1987 the judge issued a statement in his order finding that “plaintiff Arachnid, Inc. is hereby declared and decreed to *have been and to be* the lawful owner of all right, title, and interest in and to the invention.”¹³¹ It is on this decree of Arachnid’s ownership that Arachnid argued in the lawsuit against Merit that IDEA never owned any interest in the patent based on the 1980 consulting agreement, and, therefore, IDEA had nothing to grant to Merit.¹³² Again, it was this decree, however, that granted Arachnid retroactive ownership and, therefore, a possible right to the money damages for the time period when Merit sold hundreds of the electronic dart games.¹³³

The Federal Circuit rejected Arachnid’s “Back-to-the-Future” theory as well as the earlier judge’s order of retroactive patent ownership.¹³⁴ At most, the Federal Circuit stated, the judge’s order may have granted equitable title.¹³⁵ It “did not retroactively divest IDEA of legal title to the . . . patent during the 1985-86 timeframe and revest that legal title in Arachnid for standing purposes.”¹³⁶

In holding so, the Federal Circuit followed a Supreme Court opinion finding that only legal title during the time of the infringement gives a plaintiff an action at law.¹³⁷ Furthermore, it disagreed with Arachnid that the 1980 consulting agreement was

126. *Id.* at 1577.

127. *Id.*

128. *Id.*

129. *Id.* at 1578.

130. *Id.* at 1576.

131. *Id.* (internal quotation marks omitted).

132. *Id.* at 1578.

133. *Id.* at 1579 (holding that the “1987 order decreeing Arachnid ‘to have been’ the owner of the invention since its conception was legally ineffective to bestow standing upon Arachnid to retroactively seek patent infringement damages for the 1985-86 period”).

134. *Id.*

135. *Id.*

136. *Id.*

137. *Id.*

self-executing for future assignments—that is, that the agreement automatically divested from IDEA or vested to Arachnid inventions conceived of during the agreement time frame.¹³⁸

The Federal Circuit, like in *FilmTec*, focused on the language used in the agreement.¹³⁹ In particular, the Federal Circuit held that the words in the consulting agreement between Arachnid and IDEA stating that patentable inventions “will be assigned” was unlike the language used in *FilmTec* (“agrees to grant and does hereby grant”).¹⁴⁰ The “will be” language did not “rise to the level of a present assignment” unlike that in *FilmTec* and, consequently, the Federal Circuit found that the consulting agreement was “an agreement to assign, not an assignment.”¹⁴¹ Accordingly, the *Arachnid* Court did not follow the generalized first in time, first in right rule that is implicit in the *FilmTec* decision. Instead, the *Arachnid* rule seems to follow the early common law where one could not morph the equitable title into legal title without some further act of conveyance (unless it was for crops or animals under the doctrine of potential possession).¹⁴²

3. The Aftermath of *FilmTec* and *Arachnid*

In both *FilmTec* and *Arachnid*, the Federal Circuit’s ultimate conclusions focused on very specific language of the grant clause within the employment and consulting agreements. Moreover, the opinions are devoid of the previously employed recitation that “[c]onstruction of patent assignment agreements is a matter of state contract law.”¹⁴³

The *FilmTec* rule (“does hereby assign” conveys an immediate assignment) and the *Arachnid* rule (“will be assigned” conveys an agreement to assign) now appear in many recent Federal Circuit opinions. For example, in *Speedplay, Inc. v. Bebop, Inc.*, a 2000 opinion, the Federal Circuit reasoned that the contract language was similar to the language found in *Filmtec* and that upon such conception or development the ownership of the invention would automatically shift to Speedplay.¹⁴⁴ Specifically, the contract provided that any invention conceived or developed during the term of the contractual relationship “shall belong” to Speedplay and that

138. *Id.* at 1580.

139. *Id.* at 1580-81.

140. *Id.* at 1580; *FilmTec, Corp. v. Allied-Signal, Inc.*, 939 F.2d 1568, 1570 (Fed. Cir. 1991).

141. *Arachnid, Inc.*, 939 F.2d at 1580.

142. *See* *Grantham v. Hawley*, (1792) 80 Eng. Rep. 281, (K.B.) 281-82.

143. *Euclid Chem. Co. v. Vector Corrosion Techs.*, 561 F.3d 1340, 1343 (Fed. Cir. 2009) (quoting *Mars, Inc. v. Coin Acceptors, Inc.*, 527 F.3d 1359, 1370 (Fed. Cir. 2008)).

144. 211 F.3d 1245, 1253 (Fed. Cir. 2000).

the owner “hereby conveys, transfers and assigns,” any such invention.¹⁴⁵

The Federal Circuit has increasingly struggled, however, in expectant interest cases because of the remaining question of whether state common law should be applied or whether it is completely subsumed by the *FilmTec* and *Arachnid* rules. The clash of the common law system of contract and patent law first appeared in the 2007 Federal Circuit opinion, *IpVenture, Inc. v. ProStar Computer, Inc.*¹⁴⁶

The respective briefs of the parties in this case heavily relied on California law to interpret and govern the interpretation of the contract. This was because the district court’s opinion focused on California law and, in particular, how California law does not make a distinction between an agreement and an agreement to assign.¹⁴⁷ Rather, California law interprets this sort of “futures” contract as Article 9 does: no further act of conveyance is required to transfer legal title.¹⁴⁸ The Federal Circuit did not comment on the parties’ reliance on state law, nor did it cite any California case law.¹⁴⁹ It did, however, overrule the district court, finding that the language in the assignment—“I agree to disclose . . . assign . . . and [] execute all documents and cooperate with HP in all necessary activities”—is one that only conveyed equitable title.¹⁵⁰ The Federal Circuit reasoned that the words “I agree” are most similar to the “will be assigned” language in *Arachnid*.¹⁵¹

Just five months later, the Federal Circuit directly confronted the common law of contract versus Federal Circuit contract law

145. *Id.*

146. 503 F.3d 1324 (Fed. Cir. 2007).

147. *See id.* at 1327.

148. Compare U.C.C. § 9-203(b) (2010) (explaining the enforceability of security interests but not requiring specific triggering language), and *In re CFLC, Inc.*, 166 F.3d 1012, 1016 (9th Cir. 1999) (“No magic words . . . are necessary to create . . . a security interest . . .”) (quoting *In re Amex-Protein Dev. Corp.*, 504 F.2d 1056, 1058-59 (9th Cir. 1974)), with *IpVenture*, 503 F.3d at 1327 (noting that “California law does not distinguish between an assignment itself and an agreement to assign” and that an employment agreement is sufficient to trigger an “assignment of []Proprietary Developments”).

149. *See* Ian N. Feinberg et al., *Consequences of the Federal Circuit’s New Reliance on Federal Common Law to Interpret Patent Assignment Agreements*, 3 LANDSLIDE, Jan.-Feb. 2011, at 24, 25 (documenting that starting with “*Arachnid* in 1991, the Federal Circuit interpreted invention assignment clauses without deciding—or even discussing—whether state law or federal common law governed . . . [and that] [t]his trend continued through 2007 with the Federal Circuit’s opinion in *IpVenture*”).

150. *IpVenture Inc.*, 503 F.3d at 1326 (emphasis added).

151. *Id.* at 1327 (“The *FilmTec* usage ‘does hereby grant’ is not present; nor is the *Speedplay* usage ‘hereby . . . assigns.’ Instead, the . . . agreement says ‘agree to assign.’ . . . [Consequently] [w]hile that agreement is an agreement to assign, such interest in the [] patent must be implemented by written assignment.”).

issue.¹⁵² The Federal Circuit held in *DDB Technologies, L.L.C. v. MLB Advanced Media, L.P.* that the “question of whether a patent assignment clause creates an automatic assignment or merely an obligation to assign is [so] intimately bound up with the question of standing in patent cases . . . [that it is] treated . . . as a matter of federal law.”¹⁵³

In response, Judge Newman penned a strong dissent criticizing the majority opinion and arguing that the opinion is “grievous[ly] overreaching . . . [and] contrary to law and precedent.”¹⁵⁴ Furthermore, that “[s]tate statutory and common law have long been recognized as governing the ownership of patent property” and that “[t]here is no conflict between the creation of the patent as a creature of federal law[,] and ownership of patent property governed by state law.”¹⁵⁵

4. The Uneasiness of the Supreme Court and Expansion

The Supreme Court is similarly unsure about the Federal Circuit’s *FilmTec* and *Arachnid* rules in contracts that contain expectant interest clauses.¹⁵⁶ In *Stanford v. Roche*, the issue for the Supreme Court to decide was whether the Bayh-Dole Act automatically vests a university’s ownership in any potential or future patent rights when particular research done by the university (Stanford in this case) is federally funded.¹⁵⁷ In a footnote, the Supreme Court stated that “[b]ecause the Federal Circuit’s

152. See *DDB Techs., L.L.C. v. MLB Advanced Media, L.P.*, 517 F.3d 1284 (Fed. Cir. 2008).

153. *Id.* at 1290 (citation omitted). The Federal Circuit then analyzed the language in the assignment clause that stated “[e]mployee agrees to and does hereby grant and assign to Company or its nominee his entire right, title and interest in and to ideas, inventions and improvements.” *Id.* at 1287. It held that the specific wording “agrees to and does hereby grant” is an “express assignment of rights in future inventions” and that if the patents were in fact created during employment, then the patents would have automatically been assigned by operation of law and no further act is necessary to complete this transfer or legal title. *Id.* at 1290 (internal quotation marks omitted). This holding directly contradicts an earlier Federal Circuit opinion that explicitly stated that patent ownership is “a question exclusively for state courts.” *Jim Arnold Corp. v. Hydrotech Sys. Inc.*, 109 F.3d 1567, 1572 (Fed. Cir. 1997).

154. *DDB Techs.*, 517 F.3d at 1296 (Newman, J., dissenting).

155. *Id.* Interestingly, Judge Newman authored the majority opinion in *IpVenture*, and scholars have speculated that his dissent in *DDB* means that *IpVenture* was decided under California law even though there were no specific California cases cited in the opinion. See Feinberg et al., *supra* note 149, at 25.

156. See *Bd. of Trs. of Leland Stanford Junior Univ. v. Roche Molecular Sys.*, 131 S. Ct. 2188, 2199-2205 (2011).

157. *Id.* at 2192. The Bayh-Dole Act was passed by Congress “to ‘promote the utilization of inventions arising from federally supported research,’ ‘promote collaboration between commercial concerns and nonprofit organizations,’ and ‘ensure that the Government obtains sufficient rights in federally supported inventions.’” *Id.* at 2192-93 (quoting 35 U.S.C. § 200 (2012)).

interpretation of the relevant assignment agreements is not an issue on which we granted certiorari, we have no occasion to pass on the validity of the lower court's construction of those agreements."¹⁵⁸ This result is disappointing because it was a chance for the Supreme Court to directly address the relationship between contract law and patent law, but it does serve as an example of the Supreme Court faced with interpreting patent law in addition to another legal regime. In this case it was the Bayh-Dole Act, but perhaps sometime soon with another opportunity the Supreme Court will directly face the muddled patent assignment law.

That said, three Supreme Court justices did take the time to express concern with the application and principles of the *FilmTec* rule.¹⁵⁹ These justices focused on the problem that the difference between transferring automatic legal title and only equitable title is down to just a few words.¹⁶⁰ Specifically, Justice Breyer and Justice Ginsberg feel that "[g]iven what seem only slight linguistic differences in the contractual language, this reasoning seems to make too much of too little."¹⁶¹ Further, they find the distinction made in *FilmTec* troubling because it is "a technical drafting trap for the unwary," and that "[t]he Federal Circuit provided no explanation for what seems a significant change in the law."¹⁶² Justice Sotomayor also shares these concerns.¹⁶³

The Federal Circuit has recently expanded the *FilmTec* and *Arachnid* rules beyond cases involving expectant interest clauses.¹⁶⁴ Instead of the issue of standing resulting from an interpretation of whether the expectant interest morphs automatically into legal title or whether some further act of conveyance is needed, the standing issue arises here when there are potential gaps in the chain of title.¹⁶⁵ Prior to this expansion, the Federal Circuit applied state law in interpreting what to do when the chain of title is broken.¹⁶⁶

In *Abraxis Bioscience, Inc. v. Navinta L.L.C.*, the gap in title to

158. *Id.* at 2194 n.2.

159. *See id.* at 2199 (Sotomayor, J., concurring), 2203 (Breyer, J., dissenting).

160. *See id.* at 2203 (Breyer, J., dissenting).

161. *Id.* at 2202-03.

162. *Id.* at 2003.

163. *Id.* at 2199 (Sotomayor, J., concurring).

164. *See Abraxis Bioscience, Inc. v. Navinta L.L.C.*, 625 F.3d 1359 (Fed. Cir. 2010).

165. *See id.* at 1361, 1365-67.

166. *See, e.g., Tri-Star Elecs. Int'l v. Preci-Dip Durtal SA*, 619 F.3d 1364, 1367 (Fed. Cir. 2010). Judge Newman for the majority held that "[a]n assignment of a patent is interpreted in accordance with statutory and common law of contract." *Id.* Consequently, Judge Newman applied state law that required a focus on the parties' intent when entering the agreement. *Id.* Judge Newman also cited the Restatement (Second) of Contracts and two earlier Federal Circuit opinions highlighting the importance in contract law of contract interpretation in accordance to the parties' intentions. *Id.*

the at-issue patents arose because of sloppy assignments between companies.¹⁶⁷ The plaintiff, Abraxis, and AstraZeneca (“AZ-UK”), entered into an asset assignment agreement (“Agreement”) with an effective date of June 28, 2006.¹⁶⁸ This Agreement specified that New York law controls if a contract dispute arises.¹⁶⁹ The problem with this Agreement is that at the time of execution, AZ-UK (the one in privity with Abraxis) had not received legal title from two of its own subsidiaries, Astra Lakemodell Aktieboad (“Astra L”) and AstraZeneca AB (“AZ-AB”).¹⁷⁰

The Agreement stated that AZ-UK “*shall or shall cause one or more of its Affiliates to, Transfer to the Purchaser, and the Purchaser shall purchase and accept . . . all of the right, title and interests . . . [to] the asserted patents.*”¹⁷¹ Presumably recognizing this deficiency, Astra L and AZ-AB just prior to filing the lawsuit both executed assignment agreements of its respective patents to AZ-UK.¹⁷² They did not specifically assign the patents to Abraxis.¹⁷³ Both assignment agreements reference the June 2006 Agreement and state that these supplement assignment agreements are to “further convey” legal title of the patents to AZ-UK and then to Abraxis as intended under the Agreement.¹⁷⁴

Abraxis cited New York state law that allows parties to backdate agreements and argued that the assignments had *nunc pro tunc* effect based on the June 2006 Agreement.¹⁷⁵ The district court agreed with Abraxis that New York law controls, and, accordingly, Abraxis had legal title to the patents on the day of filing (and therefore had standing).¹⁷⁶ However, the Federal Circuit disagreed (in both the first review and en banc review), finding that though “state law governs the interpretation of contracts generally . . . the question of whether a patent assignment clause creates an automatic assignment or merely an obligation to assign is intimately bound up with the question of standing in patent cases.”¹⁷⁷ Moreover, because of this

167. 625 F.3d at 1361-62.

168. *Id.* at 1361.

169. *Id.* at 1368.

170. *Id.* at 1361-62.

171. *Id.* at 1361 (emphasis added) (citation omitted).

172. *Id.*

173. *Id.* at 1361-63.

174. *Id.*

175. See Brief of Plaintiff-Appellee at 48, *Abraxis Bioscience, Inc. v. Navinta L.L.C.*, 625 F.3d 1359 (Fed. Cir. 2010) (No. 09-1535), 2010 WL 804468, at *48.

176. See *Abraxis Bioscience, Inc.*, 625 F.3d at 1363.

177. *Id.* at 1364 (quoting *DDB Techs., L.L.C. v. MLB Advanced Media, L.P.*, 517 F.3d 1284, 1290 (Fed. Cir. 2008)); *Abraxis Bioscience, Inc. v. Navinta L.L.C. (Abraxis Petition)*, 672 F.3d 1239, 1240-41 (Fed. Cir. 2011) (denying per curiam petition for panel rehearing and rehearing en banc).

unique situation, this question of interpretation is based on federal law.¹⁷⁸ The Federal Circuit then reversed the district court, holding that Abraxis did not have legal title on the day of the suit because present language like “I hereby” was not used in the June 2006 agreement.¹⁷⁹

Judge O’Malley, in her first patent opinion for the Federal Circuit, dissented from the Ninth Circuit’s per curiam denial of Abraxis’ petition for rehearing en banc, arguing the *Abraxis* panel was wrong in creating special federal rules that govern the assignment of patent rights.¹⁸⁰ Judge O’Malley (joined by Judge Newman) stated that “by virtue of this decision, this court now requires the application of *Federal Circuit contract law* to transfers of existing patent rights, without regard for the state law jointly chosen by the contracting parties.”¹⁸¹ In addition, Judge O’Malley argued that the *Abraxis* opinion would disrupt expectations of parties and, further, that the choice of law provisions selected by parties would be rendered meaningless.¹⁸²

The last decade of Federal Circuit and United States Supreme Court patent assignment opinions have resulted in inconsistent precedent and contrasting views from judges on how patent assignment language should be interpreted.¹⁸³ There is tension over the role of the contract law when courts are reviewing patent licenses. It is not surprising then that district courts are struggling to apply this inconsistent precedent.

One district court took an extremely literal approach,¹⁸⁴ while another district court only hesitantly mentioned in passing the *Arachnid* rule.¹⁸⁵ Both ultimately decided to apply state law.

178. *Abraxis Bioscience, Inc.*, 625 F.3d at 1364.

179. *See id.* at 1364-65 (explaining that an agreement to assign does not convey title: assignments are considered automatic when they include terms like “hereby”).

180. *Abraxis Petition*, 672 F.3d at 1241-50 (O’Malley, J. dissenting).

181. *Id.* at 1241 (emphasis added).

182. *Id.*

183. *See supra* notes 146-182 and accompanying text.

184. *See Affymetrix, Inc. v. Illumina, Inc.*, 446 F. Supp. 2d 292 (D. Del. 2006). This is an expectant interest case with the at-issue grant clause in the consultant contract using the terms “shall be.” *Id.* at 296. The district court found all the Federal Circuit precedent was not on point because “[t]he agreement . . . contain[ed] neither the ‘will assign’ language of *Arachnid* nor the ‘does hereby grant’ language of *FilmTec*.” *Id.* Consequently, the district court cited a 1996 Federal Circuit opinion that did not involve a future goods question of law (but that said patent assignments are a matter of state law construction), and then applied California law. *Id.* (citing *Minco, Inc. v. Combustion Eng’g, Inc.*, 95 F.3d 1109, 1117 (Fed. Cir. 1996)).

185. *See Balsam Coffee Solutions Inc. v. Folgers Coffee Co.*, No. 6:09-CV-89, 2009 WL 3297292, at *3 (E.D. Tex. Oct. 14, 2009). The facts of this case involve a transfer of existing patents instead of expectant interest of patents, but this distinction was not discussed or noted. *Id.* at *1-2. The opinion concluded that the language in the at-issue agreement was unlike that in *Arachnid* because “the agreement here intended a

In still another opinion, the district court noted its confusion regarding whether to apply Federal Circuit contract law or its own state law.¹⁸⁶ The district court started its analysis of the patent assignment contained in a dissolution agreement by finding that “the Federal Circuit applies federal law to determine the validity and terms of an assignment for patent rights.”¹⁸⁷ It then referenced another Federal Circuit opinion that contradicted Federal Circuit precedent and held that “[c]onstruction of patent assignment agreements is a matter of state contract law.”¹⁸⁸

The dissolution agreement contained the following language: “Bios hereby conveys, assigns, transfers and delivers to [Agribiotics, Inc.] all of its right, title, estate and interest to all its property, assets, business and undertaking, both real and personal, movable and immovable.”¹⁸⁹ This agreement does not reference intellectual property specifically and certainly is very broad, but the district court found that there was no indication that the company’s patents were to be excluded.¹⁹⁰

Furthermore, the district court likened this language to that in *FilmTec* because of the seemingly present intention to assign the assets despite additional language in the dissolution agreement calling for Bios to provide any necessary documentation “for more effectively and completely vesting the property and assets conveyed . . . or for the purpose of registration or otherwise.”¹⁹¹

In another recent case, the district court of Maryland discussed the Federal Circuit line of cases and its application to the employment agreement at issue.¹⁹² After citing *FilmTec* and *Arachnid*, the district court found that “[d]istinguishing agreements that constitute actual, effective assignments from those that do not seems to hinge on fine semantic distinctions.”¹⁹³ The language in the agreement stated that “*without further consideration* to [the inventor] any inventions or improvements that [he] may conceive, make, invent or suggest during [his] employment by [C.R. Daniels or

present transfer of all legal and equitable rights.” *Id.* at *3. In coming to this conclusion, the district court decided to apply Texas state law that focuses on the intent of the parties. *Id.*

186. EMD Crop Bioscience Inc. v. Becker Underwood, Inc., 750 F. Supp. 2d 1004 (W.D. Wis. 2010).

187. *Id.* at 1012.

188. *Id.* (quoting *Euclid Chem. Co. v. Vector Corrosion Techs., Inc.*, 561 F.3d 1340, 1343 (Fed. Cir. 2009)).

189. *Id.* at 1013.

190. *Id.*

191. *Id.* at 1014.

192. C.R. Daniels, Inc. v. Naztec Int’l Grp, L.L.C., No. 11-01624, 2012 WL 1268623, at *7-15 (D. Md. Apr. 13, 2012).

193. *Id.* at *8.

Casto & Harris] . . . *shall become* the absolute property of [C.R. Daniels or Casto & Harris].”¹⁹⁴ The agreement also stated that the inventors agreed to “execute any patent papers covering such inventions or improvements as well as any papers that [the employer] may consider necessary or helpful in the prosecution of applications for patent thereon.”¹⁹⁵

Ultimately, the district court held that although the agreement lacked the “words of present conveyance” as contemplated by *FilmTec* and *Speedplay* (both containing the seemingly paramount word “hereby”), it was understandable because the parties in the employment agreement were addressing ownership of intellectual property that had not yet been created.¹⁹⁶ Most important to the district court was the “crucial consideration” regarding “whether assignment was ‘expressly undertake[n] . . . at the time of the agreement,’ or whether it was left ‘to some future date.’”¹⁹⁷

Overall, it found that the missing key words “hereby grant” were not necessary given the tenor of the entire agreement.¹⁹⁸ Consequently, the language in the employment agreement constituted a valid present assignment of any intellectual property that was to be created in the future during the relevant period of employment.¹⁹⁹ Although this district court opinion seems well reasoned and is perhaps the right result given the entire agreement, it is contrary to Federal Circuit precedent.²⁰⁰

As the foregoing discussion regarding the district court opinions citing and interpreting the *FilmTec* and *Arachnid* rules illustrates, there is much uncertainty and confusion among the district court judges.²⁰¹ Some courts are flat out not applying the rules, while other courts are doing their best to use them as the Federal Circuit has in

194. *Id.* at *11 (citation omitted).

195. *Id.* (citation omitted).

196. *Id.* (quoting *Freedom Wireless, Inc. v. Boston Commc'ns Grp., Inc.*, 220 F. Supp. 2d 16, 20 (D. Mass. 2002)) (stating that “because the parties were addressing the ownership of intellectual property that had not yet come into being, the use of some seemingly future-oriented language was understandable”).

197. *Id.* (citing *Gellman v. Tellular Corp.*, 449 F. App'x 941, 944 (Fed. Cir. 2011)) (omission in original).

198. *Id.* at *12 (“[T]o find dispositive the absence of words such as ‘hereby grant’ is to exalt form over substance, and to validate Justice Breyer’s criticism . . . in which he said that ‘the *FilmTec* rule’ was a ‘drafting trap for the unwary’ that ‘the cognoscenti may be able to meet . . . in future contracts simply by copying the precise words blessed by the Federal Circuit. . . .”) (quoting *Bd. of Trs. of Leland Stanford Junior Univ. v. Roche Molecular Sys.*, 131 S. Ct. 2188, 2203 (2011)).

199. *Id.* at *16.

200. *Cf. FilmTec Corp. v. Allied-Signal Inc.*, 939 F.2d 1568, 1572-73 (Fed. Cir. 1991).

201. *See C.R. Daniels*, 2012 WL 1268623, at *8-10 (discussing district court opinions).

their respective opinions.²⁰² District courts are going to continue to create their own inconsistent precedent when encountering expectant interest cases. After *Abraxis*,²⁰³ they will presumably do so anytime there is a potential gap in title.

The Federal Circuit is practiced at taking a so-called formalistic approach, but in those situations the rules are meant to be both abstract and formal so as to cover new arising technologies without district court judges needing to engage on a case-by-case basis.²⁰⁴ Further, these areas are central to patent law and fall directly in the Federal Circuit's specialty.

Here, this is a collision of patent law with the common law system of contracts as adopted by individual states.²⁰⁵ Moreover, the question arises whether the Federal Circuit's normal "formalism" can be directly applied to a different system of law.²⁰⁶ Arguably, the Federal Circuit assumes without exploration that there is only one way to create a formal, bright-line rule in patent licensing law.²⁰⁷ This is the genesis of much of the uncertainty and confusion in this area of law.²⁰⁸ The next part takes a step back to examine how the experts of contract law view formalism and learn how the drafters of the U.C.C. encapsulate different levels of formalism for its many different situations.

II. LEVELS OF FORMALITY IN CONTRACT LAW

The argument against the Federal Circuit's bright-line approach in drawing a distinction between one or two words is not the same argument often espoused in patent law against the Federal Circuit's "formalist" approach in central areas, such as claim construction and written description.²⁰⁹ The crux of this misunderstanding is that the term "formalism" is employed in a myriad of different situations, that has created an imprecise term with fuzzy boundaries.²¹⁰ In this Part, I will identify how contract law and patent law most often define "formalism," and I will then explore Lon Fuller's understanding of the function of formalism.

202. See *id.* (surveying the diversity of district court opinions).

203. See *Abraxis Bioscience, Inc. v. Navinta L.L.C.*, 625 F.3d 1359, 1364-65 (Fed. Cir. 2010).

204. See Rai, *supra* note 7, at 1110.

205. See *id.* at 1109.

206. See *id.* at 1103-06.

207. See *id.* at 1106.

208. See *id.* at 1107-08.

209. See Parchomovsky & Wagner, *supra* note 5, at 40-41.

210. See Thomas, *supra* note 3, at 775-77; see also Curtis Bridgeman, *Why Contracts Scholars Should Read Legal Philosophy: Positivism, Formalism, and the Specification of Rules in Contract Law*, 29 CARDOZO L. REV. 1443, 1450 (2008) (finding that many definitions of formalism "are in tension, if not outright conflict, with one another").

A. *Mechanical Jurisprudence and Lon Fuller*

Most often in contract law and patent law, the term formalism is employed in the classical view as “mechanical jurisprudence.”²¹¹ Though “formalism” remains imprecise in this context, most generally at the heart of this term is the idea that a rule is a rule, not because of its actual substantive content, but rather, because it is a rule.²¹² This notion of rules are rules, favoring form over substance, allows fact finders to divorce themselves from outside influences or factors (such as policy or morality) and focus on applying the law.²¹³

Mechanical jurisprudence is linked with contract law because Christopher Columbus Langdell and Samuel Williston, two influential contracts scholars, are credited as main proponents of this jurisprudence.²¹⁴ This is also how patent scholars most often define formalism, although patent scholars tend to use the phrase “according to rule”²¹⁵ or “adjudicative rule formalism.”²¹⁶ Perhaps the Federal Circuit also focuses a bit more (at least explicitly) than early mechanical jurisprudence did on the value of certainty that this type of adjudication can offer to judges and the law. The Federal Circuit

211. Bridgeman, *supra* note 210, at 1449.

212. *Id.* (explaining that “[d]efining ‘formalism’ is a tricky task,” but that “most fundamentally, formalism is the view that rules are legally binding because they are rules rather than because of any substantive justification for them”); *see also* Frederick Schauer, *Formalism*, 97 YALE L.J. 509, 510 (1988). Schauer explains in his seminal work on formalism that “[a]t the heart of the word ‘formalism,’ in many of its numerous uses, lies the concept of decisionmaking according to *rule*.” *Id.*

213. Brian H. Bix, A DICTIONARY OF LEGAL THEORY 69 (2004) (a decision-maker applying formalism moves “mechanically or automatically from category or concept to conclusion, without consideration of policy, morality, or practice”); *see also* Schauer, *supra* note 212, at 510 (“Formalism is the way in which rules achieve their ‘ruleness’ precisely by doing what is supposed to be the failing of formalism: screening off from a decisionmaker factors that a sensitive decisionmaker would otherwise take into account.”).

214. *See* Bridgeman, *supra* note 210, at 1449 (explaining that Langdell and Williston are “early alleged purveyors of this jurisprudence” and referring readers to Anthony J. Sebok, LEGAL POSITIVISM IN AMERICAN JURISPRUDENCE (1998), for clarification on the various misconceptions surrounding classical formalism). I use these names to explain who mechanical jurisprudence is often associated with in contract scholarship, but I do so with a bit of trepidation. The contentious debate in modern contract doctrine and scholarship of formalism vs. anti-formalism, or textualist vs. contextualist, which is often linked with the giants of contract law—Samuel Williston and Arthur Corbin—is one that I do not intend to engage with this article. I do think it helps frame how I use the term formalism, but that is the extent of my use of these terms and names.

215. *See, e.g.*, Peter Lee, *Antiformalism at the Federal Circuit: The Jurisprudence of Chief Judge Rader*, 7 WASH. J. L. TECH. & ARTS 405, 407 (2012) (stating that “by formalism, [Lee is] referring to the court’s emphasis on deciding cases ‘according to rule’”).

216. *See, e.g.*, Thomas, *supra* note 3, at 776 (recognizing that the Federal Circuit decision-making embraces “adjudicative rule formalism”).

has stated that it applies its own “law to patent issues in order to serve one of the principal purposes for the creation of this court: to promote uniformity in the law with regard to subject matter within our exclusive appellate jurisdiction.”²¹⁷

With this type of formalism, a common critique is that when rules are applied without sensitivity to the unique facts and policy inherent in each case, the resulting outcome is not as fair, reasonable, or favorable to the parties as it could have been if a more flexible rule of law were employed.²¹⁸ In patent law specifically, John Thomas has detailed the Federal Circuit’s embrace of formal rules and opined that this approach may impair innovation.²¹⁹ Similarly, Arti Rai has argued that the Federal Circuit’s bright-line rules are “suspect” in that they “are insensitive both to technological fact and to related issues of innovation policy.”²²⁰ Timothy Holbrook has also stated that “[t]he Federal Circuit increasingly has articulated rules of law to promote certainty, at the expense of fairness.”²²¹ And, further, that “[t]he root of this bias likely derives from the court’s Congressional mandate to promote uniformity and certainty in patent law.”²²²

This view of classical formalism as mechanical jurisprudence is just one understanding of formalism.²²³ Lon Fuller explores another understanding of formalism in his seminal article *Consideration and Form*.²²⁴ Instead of adjudicating “according to rule” without regard to substance, Fuller emphasizes that a rule is not enforced because it is a rule, but rather because of a deeper understanding that a particular form is desirable.²²⁵ He explains that in certain instances the law generally is greatly helped by requiring parties to perform in a particular manner.²²⁶

217. *Midwest Indus., Inc. v. Karavan Trailers, Inc.*, 175 F.3d 1356, 1359 (Fed. Cir. 1999).

218. *See* Bridgeman, *supra* note 210, at 1450-51. This is precisely why Karl Llewellyn, “a leader of the Legal Realist movement,” disagreed with mechanical or adjudicative-rule formalism. Gregory E. Maggs, *Karl Llewellyn’s Fading Imprint on the Jurisprudence of the Uniform Commercial Code*, 71 U. COLO. L. REV. 541, 542 (2000). Instead of encouraging fact finders to divorce or insulate themselves from having discretion in the law, Llewellyn and others “believed that statutes should seek to improve judicial decisions by recognizing that judges inevitably act with considerable discretion.” *Id.*

219. Thomas, *supra* note 3, at 774-75.

220. Rai, *supra* note 7, at 1037.

221. Timothy R. Holbrook, *The Supreme Court’s Complicity in Federal Circuit Formalism*, 20 SANTA CLARA COMPUTER & HIGH TECH. L.J. 1, 1 (2004).

222. *Id.*

223. *See* Bridgeman, *supra* note 210, at 1449.

224. Lon L. Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799, 799-800 (1941).

225. *See id.* at 801.

226. *Id.*

This may seem like a small distinction between definitions, yet there is a level of flexibility inherent in Fuller's understanding of formalism. It is not the form that is driving the style of adjudication; it is the reasoning behind desiring a certain form that matters most.²²⁷

The statute of frauds is one example.²²⁸ In order to enforce a promise conveying any interest in real property, the promise must be written.²²⁹ The form of the promise in these instances is crucial; if the parties want it enforceable in court they must make the promise in a particular manner: in a signed writing.²³⁰ The value in requiring parties to make these particular promises to convey real estate in a certain form is that this situation is often riddled with mistakes, perjured testimony, and lapses in memory.²³¹

That is, the law does not generally disfavor the substantive notion of parties making oral promises for land; rather, lawmakers recognize that in these instances there is a propensity for parties to either make these promises rashly or to simply lie about a promise made in the first instance.²³² The reasoning for wanting a form takes center stage, not the rule itself that requires a signed writing.²³³

Fuller explains in *Consideration and Form* that legal formalism in this context performs three important functions: the evidentiary function, cautionary function, and channeling function.²³⁴ By requiring all promises transferring an interest in real estate to be recorded in a writing, the writing is serving as *evidence* that the parties did in fact reach an agreement.²³⁵ Furthermore, having the parties reduce their agreement to a writing forces them to slow down, to be deliberate and *cautious* when exchanging their promises.²³⁶ Finally, and perhaps most importantly, requiring a writing serves as a simple and cheap cheat sheet—a *channeling* device—for both the

227. *See id.*

228. *See* U.C.C. § 2-201 (2010).

229. *Id.*

230. *See id.*

231. *See* Fuller, *supra* note 224, at 800.

232. *Id.* at 799 (explaining that promises with no consideration are denied enforcement because they are “gratuitous promises” that “are often made impulsively and without proper deliberation,” and, accordingly, the objection to enforcing these promises does not go “to the content and effect of the promise, but to the manner in which it is made”).

233. *See id.* at 799-800.

234. *Id.* at 800-03.

235. *Id.* at 800 (arguing that the most obvious function of a legal formality is to provide “evidence of the existence and purport of the contract, in case of controversy” (citations omitted) (internal quotation marks omitted)).

236. *Id.* (“The affixing and impressing of a wax wafer—symbol in the popular mind of legalism and weightiness—was an excellent device for inducing the circumspective frame of mind appropriate in one pledging his future.”).

parties and the courts.²³⁷ Simply, the parties know where they stand without the need for litigation.²³⁸

Beyond the statute of frauds, in classical contract law there are other examples where parties are required to make promises in a very particular way.²³⁹ These formal rules are not there with the understanding that a rule is a rule in this context and that form is valued over substance in efforts to be consistent and not to be swayed by morality or policy.²⁴⁰ Rather, the rules are there because of the high value of the functions that this formality provided for the promisor, promisee, the court, and potentially third parties.²⁴¹ However, classical contract law, law according to rule, did not always embrace Fuller's understanding of formalism.²⁴² Cases started cropping up with results that seemed to value form over function or form over the right result.²⁴³

Take for example the classical parol evidence rule.²⁴⁴ Once an agreement was reduced to writing, the parol evidence rule served as a formal bar to exclude all evidence not appearing in the four corners of the agreement.²⁴⁵ This seems like a good rule. If something matters to you as a party, it should be within the four corners of the contract. Fuller's three functions support this²⁴⁶: the agreement should be complete on its face to help both the parties and the court if there is disagreement down the road.

Nevertheless, when the law favors the rule because it is a rule, instead of sticking to it generally to encourage parties to help themselves and the courts, the result can be unfair and defeating. As evidenced by the casebook chestnut case, *Mitchill v. Lath*,²⁴⁷ with the parol evidence rule, this will likely occur when parties simply neglect or forget to put part of their agreement in their writing.²⁴⁸

In Ms. Mitchill's case there was evidence that the parties had intended that upon the purchase of real property from the Laths, the

237. *Id.* at 801-03.

238. *Id.* at 801. More properly stated: a writing will provide an "external test of enforceability" and facilitate "judicial diagnosis." *Id.* (citations omitted) (internal quotation marks omitted).

239. See Bridgeman, *supra* note 210, at 1444.

240. Fuller, *supra* note 224, at 805-06.

241. *Id.*

242. See, e.g., Bridgeman, *supra* note 210, at 1453.

243. See, e.g., *Mitchill v. Lath*, 160 N.E. 646 (N.Y. 1928).

244. See generally *id.* at 646 (citing *Glackin v. Bennett*, 115 N.E. 490 (Mass. 1917)) (defining "the parol evidence rule" as "a rule of law which defines the limits of the contracts to be construed").

245. *Id.* at 647.

246. See *supra* notes 234-38 and accompanying text.

247. 160 N.E. at 646.

248. See Bridgeman, *supra* note 210, at 1453.

Laths would also remove an ugly icehouse that was adjacent to the property.²⁴⁹ Apparently after the purchase the Laths decided they didn't want to actually go through this hassle, and perhaps after consulting with an attorney, the Laths decided the odds were in their favor under New York law that Ms. Mitchell could not force them to take the building down.²⁵⁰

This is because at the time of the opinion New York strictly adhered to the parol evidence rule.²⁵¹ Consequently, Ms. Mitchell's plea to introduce the evidence that the parties had in fact agreed for the removal of the building, despite this agreement not appearing in the contract, was denied.²⁵² In this instance, this legal rule actually prevented Ms. Mitchell from obtaining what would otherwise have been a fair and just outcome—making the Laths honor their promise to remove the icehouse.

Before litigation Ms. Mitchell was likely aware that the removal of the icehouse was not in the contract. She also likely knew (or at least her counsel knew) that the law of New York was that no parol evidence is allowed in the contract. The case was presumably pressed because of the unique facts and hope that New York law was starting to move away from rigid rules like the rest of the nation under the anti-formalist or “realist” movement, a movement that was picked up and largely adopted in Article 2 of the U.C.C., but not by Article 9 of the U.C.C.²⁵³

This next section will demonstrate the different levels of formality in the U.C.C. It is a model of what I believe Lon Fuller envisioned: a comprehensive system that is flexible and cares not about the rule, but about what level of formality is needed to get the best results for the parties and the court.

B. Formalism in the U.C.C.

Karl Llewellyn and what is largely considered to be his project, Article 2 of the U.C.C., governing the sale of goods, embraced the anti-formalist movement oftentimes called “Legal Realism.”²⁵⁴ Unlike

249. See *Mitchell*, 160 N.E. at 647.

250. See *id.* at 646-47.

251. *Id.*

252. *Id.* at 648.

253. See discussion *infra* Part II.B.

254. See Joseph H. Sommer, *Against Cyberlaw*, 15 BERKELEY TECH. L.J. 1145, 1187 (2000) (noting that Llewellyn's Article 2 “abandoned most formalisms of contract formation, and sought a contract wherever it could be found”); see, e.g., *Blesi-Evans Co. v. W. Mech. Serv., Inc.*, No. Civ. 07-5061-KES, 2010 WL 1492844, at *7 (D.S.D. Apr. 13, 2010) (holding Plaintiff's “formulation of the parol evidence rule, which applies to cases that do not fall within Article 2 of the UCC does not reflect the parol evidence rule under the UCC” and, consequently, that Plaintiff's argument—that evidence of “the parties' correspondence is inadmissible” because the language of Plaintiff's March 14, 2006 bid and Defendant's purchase order is unambiguous—is unavailing (internal

under mechanical jurisprudence where the fact finder is insulated from her own discretion by way of a formal rule to be applied in nearly every situation, Llewellyn wanted statutory law crafted with the understanding that fact finders will often act in their own discretion.²⁵⁵ Under Llewellyn's guidance, the U.C.C. avoids formal rules and embraces "open-ended standards."²⁵⁶ The parol evidence rule (section 2-202), for example, actually invites evidence of the parties' prior communications and of industry-specific norms and customs.²⁵⁷ The only time the parol evidence rule bars introduction of evidence under the U.C.C. is when the evidence is directly contradicted by the written terms.²⁵⁸ And even then, in practice, courts have frequently taken an extremely narrow view of "contradict."²⁵⁹

When the classical view of the parol evidence rule is compared with section 2-202, a very different level of formality appears. A formality spectrum can be constructed: Article 2 on the left side, representing the anti-formalist level of formality, and classical contract law on the right. The anti-formalist approach in Article 2 invites much more evidence from the parties in an attempt to understand the context of the parties' agreement instead of strictly interpreting and following a rule.²⁶⁰ The drafters of Article 2 were trying to prevent situations like *Mitchill v. Lath*, where the court was unforgiving of Ms. Mitchill's predicament of not putting the removal of the icehouse in the contract.²⁶¹

citations omitted).

255. See Maggs, *supra* note 218, at 542. The U.C.C. is sometimes called "Karl's Kode" or "Lex Llewellyn." *Id.* at 541-42.

256. *Id.* at 543.

257. See U.C.C. § 2-202 (2010); see, e.g., *A & A Mech., Inc. v. Thermal Equip. Sales, Inc.*, 998 S.W.2d 505, 510 (Ky. Ct. App. 1999) (explaining that "[p]arties wishing to disclaim UCC provisions may, to a limited extent, do so, but deviations from the Code and from the presumptions underlying it should be clearly expressed[, and] no such presumption is that, in the absence of a writing clearly intended to exclude it, a trial court may consider evidence of circumstances surrounding the agreement—particularly with respect to related writings, course of dealing, course of performance, and usage of trade—to explain and supplement . . . the agreement's written terms").

258. See U.C.C. § 2-202.

259. Another casebook chestnut, *Hunt Foods & Industries, Inc. v. Doliner*, is perhaps the best example of how courts have sometimes interpreted what it means to have something contradict the written agreement. 270 N.Y.S.2d 937 (App. Div. 1966). In this opinion, the court held that a written agreement whereby the plaintiff had a purchase option of the defendant's stock was not inconsistent or contradicted by an alleged oral agreement that the purchase option was in fact conditional because the written agreement did not specifically state it was free of any conditions. *Id.* at 939-40.

260. See Bridgeman, *supra* note 210, at 1445 ("The general strategy was not only to avoid absurd results, but also to incorporate the norms and practices from relevant industries and to pay special attention to the circumstances of the parties involved.").

261. See U.C.C. § 2-202; *Mitchill v. Lath*, 160 N.E. 646, 646-47 (N.Y. 1928).

Accordingly, Article 2 is meant to be flexible and to allow courts to engage the facts and unique composition of the case to find the fair or just result. And, in fact, one is hard-pressed to find a provision in Article 2 that does not include normative language.²⁶² The result of this flexible and informal approach to the sale of goods is the court oftentimes finds the result the parties truly intended, but it comes at a high cost.

Nowhere in Article 2 will you find an explicit direction on how to form a contract to achieve a particular result or how to ensure that there are no problems with an agreement down the road.²⁶³ And everywhere in Article 2 the parties can find a way to introduce evidence outside the four corners of the document.²⁶⁴ As Judge Kozinski stated in frustration,

even when the transaction is very sizeable, even if it involves only sophisticated parties, even if it was negotiated with the aid of counsel, even if it results in contract language that is devoid of ambiguity, costly and protracted litigation cannot be avoided if one party has a strong enough motive for challenging the contract. While this rule creates much business for lawyers and an occasional windfall to some clients, it leads only to frustration and delay for most litigants and clogs already overburdened courts.²⁶⁵

The decrease in clear rules and, consequently, the increase in litigation, is precisely the opposite approach of Article 9 of the U.C.C.²⁶⁶ Article 9 covers secured transactions and contains very specific categories, and rules within each category tell the debtor, creditor, or third party exactly how to and how to not structure the financing agreement to get a particular result.²⁶⁷ It is a rigid system of bright-lines rules, but there is a bit of flexibility when the issue only touches the debtor and creditor and not third parties.²⁶⁸ It is different than classical contract law in that the high level of

262. See, e.g., U.C.C. §§ 2-204, -206. See also Bridgeman, *supra* note 210, at 1445 (“[O]ne can hardly find a page of the text of the U.C.C. that does not include the term ‘reasonable,’ . . . ‘reasonable under the circumstances’ or something similar.”).

263. See U.C.C. §§ 2-201 to -210.

264. See, e.g., *id.* § 2-202 (providing circumstances under which parol or extrinsic evidence may be considered).

265. *Trident Ctr. v. Conn. Gen. Life Ins. Co.*, 847 F.2d 564, 569 (9th Cir. 1988).

266. Unlike section 2-207, for example, where Article 2 drafters tried to understand the nature of these form-exchanging transactions and then anticipate what outcomes would be fair given the terms within these transactions, Article 9 gives very clear rules on what is required of parties to reach certain objectives. See Jeffrey M. Lipshaw, *Models and Games: The Difference Between Explanation and Understanding for Lawyers and Ethicists*, 56 CLEV. ST. L. REV. 613, 626-27 (2008).

267. U.C.C. § 9-101; see Barkley Clark, *Revised Article 9 of the UCC: Scope, Perfection, Priorities, and Default*, 4 N.C. BANKING INST. 129, 129-36 (2000) (discussing broadened scope of revised Article 9).

268. See, e.g., Clark, *supra* note 267, at 173-74 (citing U.C.C. § 9-608(a)(3)).

formality is in the statutory rules themselves, and not just in the strict interpretation of a common law rule.²⁶⁹ If we were to put it on a formality spectrum, it would be much closer to classical contract law than Article 2.

Let us return to the AATC and Jordan hypothetical.²⁷⁰ Suppose that AATC wants to refurbish and update its office furniture. In order to do this, it will cost AATC \$50,000. AATC does not have this in cash, and therefore needs to borrow money. It contacts First Bank, and First Bank decides to loan this money if AATC can come up with collateral (sometimes referred to as “assets”) to secure this loan. Let us assume that AATC is going to use the furniture that it buys as part of the necessary collateral, but because of its depreciation value, AATC also is going to use one of its patents to secure this loan. If AATC defaults on the loan, First Bank wants to make sure that it can take the furniture and the patent and sell them to cover the money it loaned to AATC. In the event AATC defaults on the \$50,000 loan, under Article 9, First Bank will have one of three possible claims against AATC: an unsecured claim, a secured claim, or a purchase money security interest (“PMSI”) claim.²⁷¹ Let us focus on the first two.²⁷²

There are at least three advantages to becoming a secured creditor versus an unsecured creditor. First, in the event the debtor defaults on the loan or files bankruptcy, a secured creditor will have a “priority right” to the assets used to secure the loan.²⁷³ First Bank wants to be the first in line to get the furniture and patent described in the security agreement with AATC.²⁷⁴ Second, the secured creditor’s claim is also said to be “dilution-proof,” which means that no creditor who lends money after the secured creditor does is able to acquire an interest in the assets already used to secure a loan.²⁷⁵ This makes sense. First Bank does not want the value of the assets to be diluted by another creditor’s claim to those same assets. And, finally, a secured creditor has a property right to the collateral; First

269. *See id.*

270. *See supra* Part I.

271. *See* U.C.C. §§ 9-601(a), -103.

272. To be thorough, the third possible claim is a PMSI claim. *Id.* § 9-103(b). A PMSI takes priority over a previous secured creditor who has rights to after-acquired assets. *Id.* § 9-103 (e)(3)(B). A PMSI is a secured claim to goods that are purchased with the money loaned in which the claim secures. *Id.* § 9-103(a)-(b). Accordingly, First Bank will have a PMSI claim over the furniture, but not the patent. *See id.* This is because AATC did not use the proceeds of the loan to purchase the patent—it already had that and there is a risk that there might be a prior secured creditor who has first priority to that patent. *See id.*

273. *See* Richard Squire, *The Case for Symmetry in Creditors’ Rights*, 118 YALE L.J. 806, 846 (2009).

274. *See id.*

275. *Id.* at 846-47.

Bank is allowed to seize the assets itself if AATC defaults and is not in bankruptcy.²⁷⁶ It follows that First Bank unsurprisingly will want to be a secured creditor versus an unsecured creditor.²⁷⁷

Section 9-203 tells creditors like First Bank exactly how to become a secured creditor and create, attach, and perfect a security interest in the collateral that AATC uses to secure its \$50,000.²⁷⁸ There is a particular form here and, if AATC follows it to the letter, it can know where it stands without the need for litigation.²⁷⁹

Section 9-203 states that in order to create an enforceable security agreement—an agreement demonstrating intent between the creditor and debtor to create a security interest in the designated collateral—First Bank and AATC must take the following three steps.²⁸⁰ First Bank must give value to AATC (the \$50,000 in this instance), AATC must have rights in the collateral (the furniture and the patent), and, finally, AATC and First Bank must sign a security agreement that describes the collateral.²⁸¹ Once these three basic

276. See U.C.C. § 9-609(a), -609(b)(2) (giving a secured creditor the repossession right that permits the secured creditor to bypass the court's approval and seize the secured assets so long as the debtor is not in bankruptcy and doing so will not breach the peace); see also Squire, *supra* note 273, at 847 (explaining that "a secured creditor enjoys a property right in the secured assets, in the sense that he can seize those assets upon the debtor's default even if the debtor has conveyed them to a third party").

277. See U.C.C. § 9-609. The unsecured creditor is the one that merely makes a loan to the AATC and does nothing else. The unsecured creditor assumes that all will go right—AATC will pay its loan on time and completely with no problems. If anything does go wrong, there are no self-help options for the unsecured creditor. See *id.* § 9-609. This unsecured creditor cannot go to the offices of AATC and seize the new furniture that was purchased by the loan. Instead, it must file a suit, get a judgment, and then get the sheriff's office to seize this property in hopes that it can sell this furniture to recoup some of its loss. If AATC declares bankruptcy, the unsecured creditor will wait in line with all the other unsecured creditors of AATC for all AATC's assets to be sold, and the resulting money split between the creditors. Oftentimes, this result is little (if any) money for each unsecured creditor.

278. See *id.* § 9-203.

279. See *id.* § 9-609(b)(2).

280. *Id.* § 9-102(a)(74) (defining security agreement as "an agreement that creates or provides for a security interest"); see also *Barton v. Chem. Bank*, 577 F.2d 1329, 1334 (1979) (explaining under Georgia law that "for a valid security agreement the parties need merely agree to create a security interest in the collateral" and, accordingly, "an intent to create a security interest is the sole requisite for a security agreement").

281. Section 9-203(b) provides these first steps:

[A] security interest is enforceable against the debtor and third parties with respect to the collateral only if: (1) value has been given; (2) the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party; and (3) one of the following conditions is met: (A) the debtor has authenticated a security agreement that provides a description of the collateral and, if the security interest covers timber to be cut, a description of the land concerned

prerequisites are complete, then the security agreement is both created and attached; the security agreement is enforceable against the debtor, AATC.²⁸²

This security agreement that is created and then attached to the specified collateral is strictly between the debtor and creditor.²⁸³ Returning to Fuller's model, the security agreement serves both the evidentiary function and the cautionary function.²⁸⁴ The security agreement will show that there is an agreement between AATC and First Bank, and it also serves as a cautionary device to slow down First Bank's decision to loan the \$50,000 to AATC.²⁸⁵

Yet because all of these functions are of utility to just AATC and First Bank (and potentially a court down the line), there is a bit of flexibility built into section 9-203 with regard to the form that the security agreement takes. The drafters of Article 9 presumably would see the channeling function here slightly less important because no third parties' rights are involved.²⁸⁶ In particular, Article 9 does not require AATC and First Bank to contain any particular magic words to be enforceable.²⁸⁷ The parties must take the three steps as required under the statute;²⁸⁸ beyond that there is room for mistakes and different levels of formality within the agreement (most often depending on how big the loan is and the level of sophistication between the two parties).

This is in contrast to the last step for First Bank to perfect its interest in AATC's collateral. First Bank must file a financing statement in the state that AATC is located.²⁸⁹ This form only requires a limited amount of information.²⁹⁰ Section 9-502 informs First Bank that to be a sufficient filing to perfect its interest it must include in its initial financing statement the name and mailing address of the debtor (AATC); the name and mailing address of the secured party, or a representative of the secured party (First Bank); and a very general account of the attached collateral (furniture and patent).²⁹¹

U.C.C. § 9-203(b).

282. *Id.* § 9-203 cmt. 2.

283. *Id.* § 9-203 cmt. 2 (explaining when a security interest "becomes enforceable *between the parties*" (emphasis added)).

284. *See* Fuller, *supra* note 224, at 800 (discussing the evidentiary and cautionary functions, respectively, of legal formalities, such as security agreements).

285. *See id.*

286. *See id.* at 801-03.

287. *See* U.C.C. § 9-203(b) (discussing enforceability).

288. *See id.*

289. *See id.* § 9-301(1) (explaining that "while a debtor is located in a jurisdiction, the local law of that jurisdiction governs perfection").

290. *See id.* § 9-502(a) (discussing sufficiency of financing statement).

291. *See id.* §§ 9-502(a), -516(b)(4), -516(b)(5)(A). A possible fourth requirement is a

The purpose of this financing statement filed in the debtor's state is to place future creditors of AATC on notice that First Bank has first priority to this new furniture and the particular patent in the event of a default or bankruptcy filing.²⁹² Third parties that are considering a transaction with AATC concerning any personal property capable of being perfected by filing are aware that they need to first examine the filing records in AATC's home state for financing statements evidencing someone else's possible interest in AATC's personal property.²⁹³ The financing statement is a channeling device that places third parties on notice that AATC has a loan from First Bank and what collateral is used to secure that loan.²⁹⁴

Due to this different function of the financing statement versus the security agreement, which just concerns the debtor and creditor, Article 9 requires exact compliance with section 9-502.²⁹⁵ There is little forgiveness (if any) when a mistake is made.²⁹⁶ In particular, Article 9 mandates that "a filing office [shall] refuse[] to accept [a record]" for a host of listed reasons, such as a failure to provide a name and mailing address for the debtor or secured party or omission of a required description of the attached collateral.²⁹⁷ If a mistake is made regarding the debtor's name, Article 9 informs that this initial financing statement is insufficient and is not effective to perfect a security interest.²⁹⁸

This may seem like a lot of steps and statutory reading, but there is no guesswork here for the parties. First Bank knows exactly what it has to do in order to create and attach a security agreement and then perfect its interest. No litigation is necessary if parties follow the explicit rules of Article 9. The litigation that exists in regards to these rules is oftentimes because of the informal nature of the security agreement (remember, that is just between the debtor and creditor). These security agreements may be oral,²⁹⁹ and in some rare instances may not have been signed or ever officially created.³⁰⁰

real property description if the financing statement constitutes a fixture filing, as-extracted collateral, or timber to be cut. *See id.* § 9-502(b)(3).

292. *See Helms v. Certified Packaging Corp.*, 551 F.3d 675, 680 (7th Cir. 2008) ("The purpose of the financing statement is to place would-be subsequent creditors on notice that a creditor has a security interest in the debtor's property . . .").

293. *See U.C.C.* § 9-301(3).

294. *See Fuller*, *supra* note 224, at 801-03.

295. U.C.C. § 9-502.

296. *See id.*

297. *Id.* § 9-516(a)-(b).

298. *Id.* § 9-520(c). This is true even if the financing statement is filed and accepted by the state filing office. *See id.*

299. *See, e.g., Barton v. Chem. Bank*, 577 F.2d 1329, 1334-35 (5th Cir. 1978) (holding that the "liberal standards" of the creation of a security agreement were met through the oral agreement and ensuing conduct of the parties).

300. *See, e.g., In re Bollinger Corp.*, 614 F.2d 924, 925 (3rd Cir. 1980); *Casco Bank &*

These rules are rigid and equally applied. But they are not absolute, and with the exception of getting the debtor's name wrong, mistakes can be made and fixed.³⁰¹ The next section further explores the reasons why Article 2 and Article 9 have different levels of formality. It also places the current Federal Circuit's approach on the formalism spectrum and then identifies a better place for it to be on the spectrum in light of its objectives. Overall, I will argue that the Federal Circuit should adopt a new framework of formality similar to that of Article 9.

III. A TAILORED APPROACH TO FORMALITY IN PATENT ASSIGNMENTS

The purpose of a particular law or set of laws is crucial in the determination of what level of formality is necessary to effectuate that purpose. The identification of the purpose allows for the tailoring of the most desirable level of formality. As the foregoing demonstrated, Article 2 is informal and governed by a set of statutes offering guidance, whereas Article 9 is governed by a set of rules that vary in formality depending on whether the security agreement or financing statement is at issue. This variance in formality is a result of Article 2 and Article 9 having very different purposes. The first step for patent licensing law is to identify the overarching purpose, or objective, and then the formality tailored to best support that purpose.

A. Identifying the Purpose and Then Tailoring Formality

Article 2 governs the sale of goods between consumers and merchants alike.³⁰² Whether it is for the sale of cattle,³⁰³ rodent traps,³⁰⁴ a fall-protection system for employees working on Grand Central Terminal,³⁰⁵ or natural gas reserves,³⁰⁶ Article 2 applies. Because of the varied nature of transactions, Article 2 drafters used normative terms in the provisions so that these provisions could be interpreted in accordance with industry norms and the sophistication of the parties. What is "reasonable" in the cattle industry is different from what is "reasonable" in the oil and gas industry.

Trust Co. v. Cloutier, 398 A.2d 1224, 1228-29 (Me. 1979).

301. See, e.g., *In re Flagstaff Foodservice Corp.*, 56 B.R. 899, 902 (Bankr. S.D.N.Y. 1986) (holding filing effective despite filing officer's failure to index financing statement).

302. U.C.C. § 2-102.

303. See *Rudiger Charolais Ranches v. Van De Graaf Ranches*, 994 F.2d 670, 671-72 (9th Cir. 1993) (applying Article 2 of the Washington U.C.C.).

304. See *Ragus Co. v. City of Chicago*, 628 N.E.2d 999, 1001-02 (Ill. App. Ct. 1993) (applying Article 2 of the Illinois U.C.C.).

305. See *Sinco, Inc. v. Metro-North Commuter R.R. Co.*, 133 F. Supp. 2d 308, 311 (S.D.N.Y. 2001) (applying Article 2 of the New York U.C.C.).

306. See *Res. Inv. Corp. v. Enron Corp.*, 669 F. Supp. 1038, 1042 (D. Colo. 1987) (applying Article 2 of the Texas, Oklahoma, and Kansas U.C.C.).

There are very few directives in Article 2, only proposed roadmaps that parties may or may not follow to reach their end objective. This flexibility has aided parties when their agreements are unclear or missing important details because Article 2 invites courts to wade through long bouts of discovery and introduction of course of performance, course of dealing, and usage of trade.³⁰⁷ However, this may hurt parties who ultimately are not aware of the default rules that may come into the agreement if the court cannot find persuasive evidence that they did not want the default rule.³⁰⁸ Further, parties that do specifically dicker out every term may still be forced to litigate due to the normative language used in Article 2 that results in extreme flexibility and no bright-line rules.

Critical here, however, is that Article 2 generally just governs the sale of goods between a buyer and a seller.³⁰⁹ There are rarely third parties' rights at stake in Article 2.³¹⁰ The buyer and seller can make mistakes and choose to not use an attorney to help them draft their agreement. Ultimately, this may mean they have to litigate to determine their rights, duties, and remedy, but this is a cost they share just between themselves. Arguably, they have an almost unfettered right to contract as they please, and the flexible guidelines of Article 2 support this purpose of free exchange between two parties.³¹¹

Article 9 developed from a motivation to encourage lending practices.³¹² If the law could help reduce a lender's risk and cost, and thereby increase predictability and certainty, then a lender should be more willing to enter into transactions with debtors.³¹³ The drafters recognized that states needed a unified set of state laws to provide this cohesive and predictable structure for these financing transactions and further, that each state needed a place for parties to gather information about what financial transactions might affect them.³¹⁴

Their drafters' solution is Article 9 of the Uniform Commercial

307. See U.C.C. § 2-202.

308. See *id.*

309. See *id.* § 2-102.

310. An exception to the general notion that Article 2 only involves the relationship of the immediate buyer and seller is when title to the goods being passed to the buyer is at issue. For example, in section 2-403, a person with voidable title is able to transfer good title to a good faith purchase for value, whereas a person with void title does not have the same power to transfer good title. *Id.* § 2-403(1).

311. See *supra* Part II.B.

312. "The aim of this Article is to provide a simple and unified structure within which the immense variety of present-day secured financing transactions can go forward with less cost and with greater certainty." U.C.C. § 9-101 cmt. (1962).

313. See *id.*

314. See *id.*

Code, which explicitly repealed most prior statutes governing security devices.³¹⁵ The drafters recognized that they needed predictable and form-specific rules because of the high stakes and involvement of third parties.³¹⁶ But the drafters recognized a competing pull. With so many diverse transactions, sophistication of parties, and new financing methods, this cohesive and formal system must also be flexible.³¹⁷

As mentioned in the above section, in Article 9 there are two main documents, the security agreement and the financing agreement.³¹⁸ Each has a unique purpose and a corresponding different level of formalism.³¹⁹ With the security agreement, the parties need only to establish that there is a mutual intent to create a security agreement.³²⁰ The parties do not need any particular magic words or any formal wording such as “Article 9” or “security agreement.”³²¹ The mutual intent to create a security interest may be evidenced by a written document, oral language, or circumstances that include reference to course of performance, course of dealing, and usage of trade.³²² And although the security agreement does not need to identify with a high-level of particularity the personal property used as collateral, nor explicitly identify the type of transaction involved,³²³ it must generally describe the collateral.³²⁴

315. Richard C. Tinney, *Who is “Buyer in Ordinary Course of Business” Under Uniform Commercial Code*, 87 A.L.R.3d 11, §2[b] (1978) (explaining that “the purpose of Article 9 of the Uniform Commercial Code [is] to provide a single, unified concept of a secured transaction to replace the former many-faceted system of conditional sales, trust receipts, factor’s liens, chattel mortgages, crop mortgages, mortgages on railroad equipment, and assignment of accounts”).

316. *See id.*

317. U.C.C. § 9-101 cmt. (1962) (“The Article’s flexibility and simplified formalities should make it possible for new forms of secured financing, as they develop, to fit comfortably under its provisions . . .”).

318. *See supra* Part II.B.

319. *See supra* text accompanying notes 266-69, 295-301.

320. *See In re CFLC, Inc.* 166 F.3d 1012, 1016 (9th Cir. 1999).

321. *See id.* (“No magic words or precise form are necessary to create or provide for a security interest so long as the minimum formal requirements of the Code are met.” (quoting *In re Amex-Protein Dev. Corp.* 504 F.2d 1056, 1058-59 (9th Cir. 1974) (internal quotation marks omitted)); *see also In re Thompson*, 315 B.R. 94, 104 (Bankr. W.D. Mo. 2004) (finding that the parties stated in plain language in the installment sales agreement that if any payment was late by ten or more days that the personal property listed in the installment sales agreement became the property of the seller until the debt and incurred expenses were paid in full). But note that there must be this intent to create a security interest. Filing a financing statement alone is not sufficient. *See Allete, Inc. v. GEC Eng’g, Inc.*, 726 N.W.2d 520, 524 (Minn. Ct. App. 2007).

322. U.C.C. § 1-303 (2010).

323. *See WILLIAM H. LAWRENCE, WILLIAM H. HENNING & R. WILSON FREYERMUTH, UNDERSTANDING SECURED TRANSACTIONS* (LexisNexis, 5th ed. 2012) (explaining “[t]he parties need only to enter into a contractual relationship that falls within the scope of

The creation of a security agreement is similar to the formation of an agreement for the sale of goods under Article 2. This is because both the sale of goods and the security agreement are between just two parties, seller and buyer or creditor and debtor.³²⁵ Third parties are not looking to the security agreement for notice, at least not in the first instance.³²⁶ This creation and attachment of the collateral establishes the relationship between the creditor and debtor and provides the creditor with a property right in the personal property of the debtor in case of a default or bankruptcy.³²⁷ The security agreement performs an evidentiary function for the court and the parties, as well as a cautionary function for the parties.³²⁸ If the parties form and execute the security agreement correctly, the security interest is “attached.” The next step “perfects” this attachment.

The financing agreement serves an important purpose here: it puts third parties on notice where they would stand if they entered into a finance transaction with a particular debtor.³²⁹ Filing a financing statement and therein perfecting the attached security agreement does not affect the relationship between the creditor and debtor.³³⁰ Rather, perfection serves a pure channeling function; it is a cheap and fast way for third parties to assess the position of a debtor.³³¹

Because of this pure notice function, the financing statement does not need to be detailed, but it must be accurate.³³² If a mistake is made in the security agreement, it only hurts the two parties in privity with one another. If there is a mistake made in the financing statement, it affects all third parties that want to do business with a

Article 9 to have a security interest; they do not have to reference Article 9”).

324. See *Helms v. Certified Packaging Corp.*, 551 F.3d 675, 680-81 (7th Cir. 2008) (explaining the security agreement “is the primary source to which a creditor’s or potential creditor’s inquiry is directed and must be reasonably specific” (quoting *In re Laminated Veneers Co.*, 471 F.2d 1124, 1125 (2d Cir. 1973) (internal quotation marks omitted))).

325. See U.C.C. §§ 2-106, 9-102.

326. See *supra* notes 292-94 and accompanying text.

327. See *Squire*, *supra* note 273, at 847.

328. See *supra* notes 284-85 and accompanying text.

329. See *Helms*, 551 F.3d at 680 (“The purpose of the financing statement is to place would-be subsequent creditors on notice that a creditor has a security interest in the debtor’s property . . .”).

330. See *id.* at 680-81.

331. See JOHN O. HONNOLD ET AL., *THE LAW OF SALES AND SECURED FINANCING* 640 (7th ed. 2002) (“The filing system also *provides information to existing and prospective creditors generally*. . . . [T]he filing system reduces the costs of obtaining information.”).

332. *Id.* at 641-42 (explaining the notice function of financing statements and emphasizing the importance of accuracy).

particular debtor. Mistakes are vastly more costly in the financing statement than in the security agreement. Accordingly, drafters of the U.C.C. were flexible in how parties create and attach their security agreement, but they were strict as to what form must be followed in the financing statements.³³³ Again, this was to increase the accuracy of the financing statement because of its notice function.

Determining the most desirable level of formality poses more of a challenge in patent law than it does in the sale of goods or secured financing because of the many layers, interested parties, and conflict regarding the objectives of patent law. It is generally accepted that patent law rests on a utilitarian foundation whereby Congress has the power to create patent laws to “promote the Progress of Science and useful Arts.”³³⁴ And to further the objective of encouraging innovation Congress established the United States Patent and Trademark Office (“PTO”) to issue patents for the protection of inventions on behalf of the government.³³⁵

“The [PTO] is an agency of the U.S. Department of Commerce” that serves not just the government, but also “inventors and businesses with respect to their inventions . . . the President of the United States, the Secretary of Commerce, . . . the Department of Commerce, and other agencies of the government in . . . all domestic and global aspects of [patent law].”³³⁶ And of course Congress also established the Federal Circuit to hear all patent appeals.³³⁷ Accordingly, Congress, the PTO, and the Federal Circuit all have a hand in granting, enforcing, and defending patents. Lastly, inventors (whether individuals or companies) are the hamsters in this big wheel.

If patent law is about furthering and encouraging innovation, it seems to follow that the purpose of patent assignments is to likewise further and encourage innovation. However, there is a heavy and somewhat recent practice of using patent licenses (more so than patent assignments) as a way to increase royalties and avoid

333. See Clark, *supra* note 267, at 160-62.

334. U.S. CONST. art. I, § 8, cl. 8; see also Peter S. Menell, *Intellectual Property: General Theories*, in 2 ENCYCLOPEDIA OF LAW AND ECONOMICS: CIVIL LAW AND ECONOMICS 129, 130 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000) (“The United States Constitution expressly conditions the grant of power to Congress to create patent and copyright laws upon a utilitarian foundation . . .”).

335. See *General Information Concerning Patents*, U.S. PAT. & TRADEMARK OFF., (Nov. 2011), http://www.uspto.gov/patents/resources/general_info_concerning_patents.jsp#heading-7.

336. See *id.* (“Through the preservation, classification, and dissemination of patent information, the Office promotes the industrial and technological progress of the nation and strengthens the economy”).

337. See Rai, *supra* note 7, at 1037 n.2 (explaining that the Federal Circuit hears appeals from “a PTO denial of patentability” and appeals from all district courts).

lawsuits.³³⁸ In this Article, I chose to focus on the former purpose, and arguably the most beneficial use of patent assignments. If one party needs patented technology to advance its products or help build new technology, the patent system, through its assignment law, should encourage these transactions.

B. A Formal But Forgiving Approach for Expectant Interests

There are two separate times that parties assign patents: prior to the issuance of a patent³³⁹ and after the patent already exists.³⁴⁰ Let us start with the first: transferring ownership prior to the issuance of the patent. In this situation, there are a limited amount of possibilities and situations in pre-issuance patent assignments between an inventor and company.³⁴¹ Of course, I do not suggest that patent assignments are without variety. There are industries within patent law that have more differences than similarities, such as biotechnology, pharmaceuticals, semiconductors, and software.³⁴²

In every industry, however, an inventor creates new patentable technology. Oftentimes, the inventor claims it is her patentable technology while the company (or another company that the inventor was working for either at the same time or shortly before or after) claims title to the patentable interest.³⁴³ The scene is different, but the storyline remains the same. And the tool that is often used and litigated in these situations is the expectant interest clause.³⁴⁴

338. See Philip Mendes, *To License a Patent - or, to Assign it: Factors Influencing the Choice*, WORLD INTEL. PROP. ORG. 2 (http://www.wipo.int/export/sites/www/sme/en/documents/pdf/license_assign_patent.pdf (last visited May 19, 2014) (“If the revenue strategy sought is royalties, licensing is the most common, and most prudent commercialization pathway.”); see also Reiko Aoki & Jin-Li Hu, *Time Factors of Patent Litigation and Licensing*, 159 J. INSTITUTIONAL & THEORETICAL ECON. 280, 282 (2003) (“Firms may agree to license . . . *ex post* in order to avoid litigation.”).

339. See, e.g., Shannon H. Hedvat, Comment, *A New Age of Pre-Employer Rights: Are Automatic Assignments the Standard?*, 13 U. PA. J. BUS. L. 817, 828 (2011) (discussing employment contracts that assign patents for future inventions).

340. See Mendes, *supra* note 338, at 2 (discussing the assignment of patents after a patent exists).

341. In this Article, I use “company” rather broadly. The term includes any formally organized business, whether for profit or not-for-profit.

342. That is not to say that I advocate here for the same patent law to be applied to all industries within the patent system. Others have already pointed out the inherent tension that exists in patent law because the law as written is content-neutral, but when applied is often context-sensitive. See, e.g., Dan L. Burk & Mark A. Lemley, *Policy Levers in Patent Law*, 89 VA. L. REV. 1575, 1577 (2003) (“[D]espite the appearance of uniformity, patent law is actually as varied as the industries it seeks to foster.”).

343. See William P. Hovell, *Patent Ownership: An Employer’s Rights to His Employee’s Invention*, 58 NOTRE DAME L. REV. 863, 866-70 (1983) (describing conflicts that arise between employers and employees in various contexts of employment).

344. E.g., *FilmTec Corp., v. Allied-Signal Inc.*, 939 F.2d 1568, 1572 (Fed. Cir. 1991).

Generally, an inventor is either an employee of the company or a hired consultant for the company and then the issue is this: who owns the patentable technology, inventor or company?³⁴⁵ This is precisely the issue in both of the Federal Circuit cases discussed in detail previously, *FilmTec* and *Arachnid*.³⁴⁶ As we saw with security agreements under Article 9, the assignment agreement between an inventor and company can serve an important evidentiary function.³⁴⁷ The parties and, if litigated, the judge will want a written document evidencing that an agreement was made. Fortunately, the Patent Act already anticipated this and requires all assignments to be in writing.³⁴⁸

The written agreement between inventor and company also serves a cautionary function. The process of putting into writing the assignment of any patentable inventions during the course of employment, and the inventor's (hopefully thorough) reading of the agreement and subsequent signing ensure to some level that the parties slow down and think about what they are agreeing to in the patent assignment.³⁴⁹ However, in order for the patent assignment agreement to truly perform the cautionary function as intended by Fuller, this written agreement, like the security agreement in Article 9, needs to be written in a form and with language that clearly manifests the mutual agreement between the parties.³⁵⁰ This means the parties must understand and attach the same meaning to the words used to describe their agreement.

Inventors like Jordan and AATC, and even sophisticated parties like Stanford University, are likely unaware of what the Federal Circuit and the regional district courts require for an automatic and immediate transfer of ownership to occur upon the conception of the patentable invention. Or even if they did stay current with the Federal Circuit opinions, it remains difficult to know what is required because the Federal Circuit itself is inconsistent.³⁵¹ These two reasons—lack of patent licensing knowledge by the parties and

345. Patent law does not have a rule like copyright law does with regard to a distinction between “employee” and “independent contractor.” In copyright law, if the author is deemed an employee working within her scope of employment when creating the art, then the art is owned by the employer. If she is deemed to create the art outside the scope of her employment or is an independent contractor, and there is no agreement to the contrary, then the employee owns the art. *See Cmty. for Creative Non-Violence v. Reid*, 490 U.S. 730, 750-53 (U.S. 1989).

346. *FilmTec Corp.*, 939 F.2d at 1571; *Arachnid, Inc. v. Merit Indus. Inc.*, 939 F.2d 1574, 1577-82 (Fed. Cir. 1991).

347. *See* discussion *supra* Part II.

348. *See* 35 U.S.C. § 261 (2012) (“Applications for patent, patents, or any interest therein, shall be assignable in law by an instrument in writing.”).

349. Fuller, *supra* note 224, at 800.

350. *Id.* at 801-02.

351. *See* discussion *supra* Part I.

inconsistent patent licensing law—combined with the need to tailor the level of formality make it paramount that the common law of contract remains an important influence on patent licensing law.

The magic language created by the Federal Circuit is too formal and unforgiving for parties like Jordan and AATC, or like the parties in *FilmTec* and *Arachnid*.³⁵² For the Federal Circuit to require magic words in this instance is requiring a form of contracting that has little meaning to parties.³⁵³ What is occurring with the Federal Circuit's path since *FilmTec* and *Arachnid* is akin to the demise of the seal in the common law.³⁵⁴ If everyone knows and respects what the seal means—in common law that the contract is enforceable even if there is no recitation of consideration³⁵⁵—then it serves as a short cut for the parties and court.

But what happens when parties start using the seal when they do not know what it means, or they do not use the seal because they do not know that they are supposed to use it in their contracts? The function of the seal and the value of the seal is lost. At best, the parties end up with what they want and are happy that they saved the trouble of writing out the exact details of the agreement. But in many other instances, the parties later find themselves responsible for a particular form (the wax impression on the contract or the magic words to convey expectant interests)³⁵⁶ that they were unaware of and are now faced with arguing why their agreement does or does not meet the required form of the district court or Federal Circuit.

Overall, between an inventor and a company, there is little need for a channeling function, and, accordingly, a more forgiving approach should be used. With this information about the purpose of patent assignments occurring prior to the issuance of patent, we can add to the formality spectrum. This current high level of formality does not match what the patent assignment in this particular situation is used for—evidentiary and cautionary functions between an inventor and the employer or contractor.³⁵⁷ Instead, the level of formality here required is more similar to the security agreement in Article 9.³⁵⁸ There should still be clarity and certainty, but also

352. See *FilmTec Corp. v. Allied-Signal Inc.*, 939 F.2d 1568 (Fed. Cir. 1991); *Arachnid, Inc. v. Merit Indus. Inc.*, 939 F.2d 1574 (Fed. Cir. 1991).

353. See *FilmTec Corp.*, 939 F.2d at 1568; *Arachnid, Inc.*, 939 F.2d at 1574.

354. See Fuller, *supra* note 224, at 823 (suggesting “[d]oubt may legitimately be raised . . . whether there will be any phase in the future or what may be called the ‘blanket formality,’ the formality which, like the seal, suffices to make any kind of promise, not immoral or illegal, enforceable”).

355. See *id.* at 800-01.

356. See *supra* note 321.

357. See Tinney, *supra* note 315.

358. See *supra* Part II.B.

flexibility. I propose if we were to continue in the construction of a formality spectrum, that the current level of formality be shifted a bit towards the left—towards where Article 2 would be on the spectrum. Just a bit less formal, however, as accuracy is still best achieved in this situation by requiring parties to use clear and precise language. This decrease in formality can be achieved in several ways. The easiest way to implement this shift is for the Federal Circuit simply move away from the *FilmTec* and *Arachnid* rules, whether explicitly or in dicta, in its next expectant interest clause opinion.

If the Federal Circuit takes a step back from the high level of formality—that is, the magic words of “I hereby” versus “I will”—the parties can use their own language in the contract and demonstrate their intent through their conduct and past experiences. What does the written agreement say, who is paying to obtain the patent, and what has the company and that particular inventor, or other inventors employed by the company done in the past? It is appropriate and reasonable to pass down to the district courts because these are questions that generalist judges are ready to answer and ones that the parties themselves can ask prior to any litigation.

Moreover, this would allow district courts to use an intent-based approach. Regional district courts are filled with generalist judges.³⁵⁹ These judges know the contract law of their state and the judges know how to deduce the intent of parties through their written contracts, conduct, or the parties course of performance and dealing.

The district court in *Affymetix* demonstrates this point. The court was unsure how to apply Federal Circuit law to the facts it had before it.³⁶⁰ The expectant interest clause does not use the precise words that the Federal Circuit encountered in *FilmTec*, *Arachnid*,³⁶¹ or any other cases after that, and so the district court did what generalist judges do best.³⁶² The court relied on its own state law, and asked the parties to show using the law of their state (California in this case), what they meant and how California law interprets their agreement.³⁶³

In the end, the court found what it needed through deposition testimony.³⁶⁴ The inventor stated in his deposition, when asked about the contracts at issue, that “[t]he—the basic idea was we worked together, and we—Affymetrix owns everything, Affymax. That was—

359. See Edward K. Cheng, *The Myth of the Generalist Judge*, 61 STAN. L. REV. 519, 522, 534-39 figs. 1.1 - .12 (2008).

360. *Affymetrix, Inc. v. Illumina, Inc.*, 446 F. Supp. 2d 292, 294 (D. Del. 2006).

361. See *FilmTec Corp. v. Allied-Signal Inc.*, 939 F.2d 1568 (Fed. Cir. 1991); *Arachnid, Inc. v. Merit Indus. Inc.*, 939 F.2d 1574 (Fed. Cir. 1991).

362. *Affymetrix*, 446 F. Supp. 2d at 296.

363. *Id.* at 296-97.

364. *Id.*

that was sort of the quid for getting to play.”³⁶⁵ As a result of the testimony, the district court concluded Affymetrix owned the patents because the parties understood that all intellectual property conceived would immediately be owned by Affymetrix.³⁶⁶ In other words, the court found that the expectant interest in all future patents would immediately vest to Affymetrix when the ideas were conceived.

This method alone may seem costly and frustrating to parties and courts if all kinds of unlimited extrinsic evidence is allowed in to show what the parties intended by their language in the expectant interest clause. This is similar to the espoused frustration in the above section about Article 2.³⁶⁷ To combat the potential for increases in litigation, and to help make the currently murky area of law more predictable immediately, the Federal Circuit could also choose to adopt a default rule or, similarly, a presumption. Technically this is not for the Federal Circuit to do, yet it has been the practice of the Federal Circuit since 1982 to create law to fill in the statutory gaps.³⁶⁸

A default rule or presumption here would likely follow the *FilmTec* rule and Article 9, where the result is immediate ownership of legal title to the patent once the patentable interest can be identified—that is, once the inventor conceives of her patentable invention.³⁶⁹ This default rule or presumption of automatic transfer is to the benefit of companies, reflecting that, in many instances, the company is paying the inventor and providing them equipment and support to invent technology for the company. And, further, this default rule or presumption of automatic transfer of patented technology when an expectant interest clause is used is desirable to avoid a holdout situation, where, most simply, the inventor demands more money before signing over her invention to the company that has already paid her.³⁷⁰

Working through the potential presumption is harder than just instilling a default rule. I will work through how a presumption might look by applying it to the Jordan and AATC hypothetical.³⁷¹ In that situation, the expectant interest clause in their contract would be construed to give AATC legal title to any potentially patentable technology as soon as Jordan conceives of it. Jordan may overcome this presumption by showing evidence that the agreement between

365. *Id.* at 297 (alteration in original) (internal quotation marks omitted).

366. *Id.* at 296-96.

367. *See* discussion *supra* Part II.B.

368. *See supra* notes 3-5 and accompanying text.

369. *See supra* notes 112-14 and accompanying text.

370. *See* Janet Frelich, *A Nuisance Model for Patent Law*, 2011 U. ILL. J.L. TECH. & POL'Y 329, 335-38 (2011).

371. *See supra* Part I.

her and AATC was that some further act of conveyance on Jordan's part is necessary to transfer legal title of the patentable technology to AATC. Jordan must show sufficient proof supported by a preponderance of the evidence, a relatively low standard in the world of presumptions.

The preponderance of evidence standard is sufficient because there is little-to-no public notice function in the patent assignment between Jordan and AATC. This agreement does not concern third parties. Certainly down the road, it may serve a channeling function to third parties who look to acquire a company or at least some of its intellectual property, but, at that time, they can read these expectant interest clauses in the contracts that are kept on file, and determine for themselves what likely occurred between the inventors and the company it seeks to do business with.

Adopting a presumption or default rule that when an expectant interest clause is used it results in automatic transfer of legal title to patentable technology is simple and clear. Allowing a party to overcome this default rule or presumption by introducing evidence to the contrary is fair; perhaps cumbersome, but no worse than the current system that is unforgiving. And, finally, allowing an inventor and company to state in their own words, and, if necessary, demonstrating to a court through their conduct and previous course of performance or course of dealing, will create more uniform and consistent law within each state. This approach is flexible in that each written agreement may be worded differently, but formal in that parties must communicate this agreement in writing and with language that either means something to them or, if the more laborious method of downshifting formality is adopted, with the attached default rule or presumption of automatic transfer of legal title once the invention is conceived.

C. A Formal Approach for Transfer of Existing Patents

In the situation above, the issue is determining when the legal title was transferred, which is different than when one company is assigning an already existing patent to another company. There, the issue involves gaps in the chain of title of already existing patents. This is precisely the situation in both *Abraxis* and *Tri-Star Electronics*.

In *Abraxis*, the patents were transferred from inventors to various parties (one patent to Astra L and two patents to AB Astra) with no problems.³⁷² It was when a merger between AB Astra and AstraZeneca AB and then an asset purchase between *Abraxis* and

372. *Abraxis Bioscience, Inc. v. Navinta L.L.C.*, 625 F.3d 1359, 1360-61 (Fed. Cir. 2010).

AstraZeneca UK took place that the chain of title was broken.³⁷³ One patent was still with the original company (Astra L), and two were either with AB Astra, AstraZeneca AB, or Abraxis.³⁷⁴ None of the documents were precise in their grant clauses, even though upon evaluation of the record it is clear that Abraxis meant to own all of the patents through the merger documents, an asset purchase agreement, and an IP assignment agreement.³⁷⁵

However, this situation is different than a grant of an expectant interest prior to the issuance of a patent. Here, Abraxis and the other companies involved are sophisticated parties (each are involved in the pharmaceutical industry where they presumably are consistently going through the PTO to obtain pharmaceutical patents or other types of patents), but this transfer between companies was for the purpose of merging and understanding the liabilities, debts, and assets of the company.³⁷⁶ Although it is not exactly analogous to the financing statement of Article 9 that puts potential creditors on notice of the debtor's debts, the purpose is similar.

Abraxis and AstraZeneca UK were merging and the parties needed to know what debts and assets each had in order to know if they wanted to do business.³⁷⁷ The channeling function here is important—a cheap and fast short cut is needed to quickly evaluate the situation. The stakes are higher and the formality of the patent assignment needs to reflect that difference. When mistakes are made and gaps in title occur, the consequence is not just contained between two parties. A third party wanting to do business is often involved when the patent is used as collateral or when a patent is sold and then resold or licensed.

A clear and formal rule is needed due to the potential for mistakes and sloppiness in transferring assets. This is not too high of a price to ask considering that intellectual property often comprises a company's most valuable assets. The PTO recently published research showing that intangible assets, including intellectual property, “now comprise over 50% of the outputs of U.S. industry, and [that] intellectual property rights . . . provide a platform for intangibles to be transacted so that they can provide profits for innovators and move technologies to their most efficient uses in the economy.”³⁷⁸

This is when magic words are necessary. These words will put

373. *Id.* at 1361.

374. *Id.*

375. *See supra* Part I.B.IV for full case details.

376. *See Abraxis*, 625 F.3d at 1360-61.

377. *Id.* at 1360-63.

378. Request for Comments on Eliciting More Complete Patent Assignment Information, 76 Fed. Reg. 72,372 (proposed Nov. 23, 2011) (to be codified at 37 C.F.R. pt. 3).

third parties who are looking to merge or buy some portion of another company on clear notice that there is or is not clear title to the patented technology. The rules announced in *FilmTec* and *Arachnid* may be applied much more effectively here than with the expectant interest transfer from inventor to company. Accordingly, I propose that the appropriate level of formality in this instance is the same as what we saw above in the already-existing Federal Circuit expectant interest rules. If the parties use active and present language in their patent licensing agreements—similar language to that used in the common law of contracts dating back hundreds of years ago—parties would know at first glance who owned what patent.

Language such as “this agreement between Company A hereby assigns absolute and full legal title to Patent X, Patent Y, and Patent Z to Company B” or “Company A agrees to grant and does hereby grant to Company B the full and entire domestic right, title and interest in any and all inventions currently owned by Company A” would accomplish this channeling function.

One area of difficulty is that—unlike a financing statement that must be filed with the state office, which is necessary for the perfection of a security interest³⁷⁹—a patent assignment does not by law have to be recorded in the PTO to be effective. The PTO does, however, encourage parties to file these assignments with its office so that third parties may learn who owns what patent. In the same section where the Patent Act states that patent assignments “shall be assignable in law by an instrument in writing,” it also states that “[a]n assignment, grant or conveyance shall be void as against any subsequent purchaser or mortgagee for a valuable consideration, without notice, unless it is recorded in the [PTO] within *three months* from its date or prior to the date of such subsequent purchase or mortgage.”³⁸⁰ In other words, patent owners that fail to record patent assignments within three months of the patent filing or within three months of a further assignment of the patent risk losing their rights to a subsequent purchaser.³⁸¹

The PTO provides an easy fill-in-the-blank form for parties to either electronically file or mail to the PTO.³⁸² Even if parties decide to not file their patent assignments with the PTO, they can still look to this form for direction on how to effectively communicate what party is transferring what patent to whom.

While the PTO recognizes that this is an incomplete and

379. See *supra* text accompanying notes 289-301.

380. 35 U.S.C. § 261 (2012) (emphasis added).

381. See *id.*

382. See U.S. Patent and Trademark Office, Recordation Form Cover Sheet (PTO-1595) (2011), available at <http://www.uspto.gov/web/forms/pto1595.pdf>.

imperfect filing system, it did recently proposed new recording requirements and held a public roundtable to discuss these proposed changes.³⁸³ This roundtable was attended by many industry giants (for example, IBM, Google, and Hewlett-Packard), patent attorneys, representatives from trade associations such as the American Intellectual Property Law Association (AIPLA), regulators (for example, representatives from the Department of Justice Antitrust Division), and academics.³⁸⁴ Moreover, the roundtable shows the importance of a transparent patent recordation system but, until such a system is put in place, the Federal Circuit can mitigate confusion and increase certainty by adopting the standards proposed here.

CONCLUSION

Overall, the role of the common law system of contract should be both valued and increased. We learned from Lon Fuller that in the contract context, varying levels of formality are employed when there are varying purposes of the at-issue laws.³⁸⁵ When an inventor is assigning her expectant interest to patentable technology to a company, the Federal Circuit should embrace a formal, but forgiving approach. No magic words are necessary here, but the assignment does need to be in writing and should clearly communicate who is intended to own the patent and at what time.

This is different when an already existing patent is assigned from one company to another company. There, the Federal Circuit should embrace a formal approach. Companies should learn to effectively use the magic words created by the Federal Circuit in *FilmTec* and *Arachnid*.³⁸⁶ These magic words serve a channeling function—any user interested in the patented technology can review the patent assignments on file and quickly determine the ownership status of the patent.

383. See U.S. PATENT & TRADEMARK OFFICE, ROUNDTABLE ON REAL-PARTY-IN-INTEREST INFORMATION (2013), available at http://www.uspto.gov/ip/officechiefecon/roundtable_01-11-2013.jsp.

384. *Id.* at 2-3.

385. See *supra* notes 224-27 and accompanying text.

386. See *supra* Part I.B.