

# AVOIDING A STARTUP PATENT CATASTROPHE



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It is unfortunate that many startup ventures fail to conduct basic patent and intellectual property investigations that can avoid potentially catastrophic circumstances. Perhaps the best way to illustrate this understandably strong statement will be to provide the following hypothetical scenario.

Imagine two highly technically qualified inventors—tenured PhD professors at a major US university—who jointly conceive of a novel widget and method of manufacturing it. Over several months they consider and mull over what they honestly believe are revolutionary new concepts, and thereafter they borrow money from relatives and close friends to build a proof-of-concept pilot prototype at an unused laboratory in their university.

To the joy of these relatives and friends, the pilot prototype works extremely well and establishes without doubt that the inventions are viable. Everyone involved is pleased and excited at the commercial prospects of the inventors enjoying huge potential financial rewards.

The inventors, following their proof-of-concept success, set about seeking to improve on the efficiency of their concept in order to reduce the costs of production and implementation. This improvement effort extends over a 12-month period with additional successes. At that point, the inventors decide to protect their original concepts via patents, as well as the efficiency improvements achieved.

With further money from friends and relatives, they retain patent counsel with instructions to conduct a preliminary patentability search and, if the results are favourable, to file a provisional patent application covering their new widget and its unique method of manufacture.

Armed with a patent application, the inventors form a corporation under which to commercialise their product and seek and obtain enthusiastic equity investors who finance a production facility. A sizable inventory of widgets is produced and stockpiled.

A week after embarking on a major marketing programme and taking significant orders, they are served with a formal federal district court complaint for patent infringement seeking preliminary and permanent injunctive relief as well as triple damages and attorneys' fees. The plaintiff named in this lawsuit is a European professor, not known to either of the inventors, whose US patent is an offshoot of an earlier-filed pending European patent application.

## Ownership

The conduct of these two inventors is significant, more for what they didn't do than what they accomplished. Let us consider a few issues.

The fact that the inventors used their university's laboratory, even though it was unused at the time, opens the door to a theoretical university claim seeking ownership of rights to the subject inventions. Universities typically post online their policies on inventions made by faculty and students. Ownership or licensing rights can sometimes be worth billions. You can be sure that any prospective investor's due diligence counsel will examine this issue closely before giving its client a go-ahead signal.

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Another important issue resides in the fact that the hypothetical scenario makes no mention of a “right to use” analysis and opinion. The inventors did pursue a patentability search, but patentability and patent infringement are entirely different animals. While it may be possible for an unexpired potentially infringed patent to pop up during a patentability search, that is not normally the focus of the searcher—he/she is more interested in whether the invention(s) is entitled to patent protection.

Had the inventors authorised a right-to-use investigation, it is entirely possible that they would have uncovered the patent owned by the plaintiff in the lawsuit. This would at least have enabled them to attempt to either negotiate a patent purchase or licensing rights, or try to ‘design around’ the patent-in-suit. At this point, the inventors are entirely at the mercy of the plaintiff and will spend much more money that could have gone into a right-to-use investigation.

Other issues that must be considered include: (a) the rights and obligations of and between the inventors and an agreement between them; (b) whether the inventors waited too long to file their patent application under the new US ‘first-to-file’ system; and (c) whether there is any liability on the part of the inventors to their friends, relatives and/or investors. ■

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