

Keywords: Settlement agreement, release, license contract interpretation

General: Settlement agreements, like other contracts, are interpreted under state law. In this case, the state law of California governed interpretation of a settlement agreement with respect to whether the benefit of a release of a claim of patent infringement was intended to apply to an after-acquiring parent company. The court held that the acquiring company could not benefit from the release because the settlement agreement did not evidence that the clear intent of the parties was for an after-acquiring company to benefit.

Unova Inc. v. Acer Inc.
70 U.S.P.Q.2d 1464 (Fed. Cir. 2004)
Decided March 31, 2004

I. Facts

Unova owned several patents relating to “smart battery” management technology for notebook computers. In 2001 (prior to HP’s acquisition of Compaq), Unova was engaged in discussions to license the smart battery patents to Compaq. In May 2001, Unova and Compaq signed a settlement agreement.

In the settlement agreement, Compaq and its “parents” were released from liability for past infringement of the smart battery patents. The agreement also granted Compaq and its parents a covenant not to sue and a license for “Compaq Products.” At the time of execution of the agreement, Compaq did not have a parent company.

On May 3, 2002, HP acquired all of Compaq’s stock and became Compaq’s parent company. Subsequently, Unova filed a patent infringement lawsuit against HP alleging infringement of the smart battery patents. Unova and HP filed cross motions for summary judgment on the issue of whether the Unova-Compaq settlement agreement released HP from liability for past infringement. In November 2002, the District Court granted HP’s motion on the release issue. Unova filed this appeal to the Federal Circuit.

II. Issues

- A. Did the District Court err in granting summary judgment to HP on the issue of release from liability for past infringement?
- B. Did the District Court err in failing to grant summary judgment to Unova on the issue of release from liability for past infringement?

III. Discussion

- A. Yes. From a starting point that interpretation of contracts is typically a state law question, the Federal Circuit quickly concluded that California law governs interpretation of the Unova-Compaq settlement agreement. Under California law, a key issue is whether the written settlement agreement expresses a clear intent to benefit a third-party beneficiary such as HP.

The court carefully examined the settlement agreement to determine the intent of the parties. In the present case, the release portion of the settlement agreement was expressly applicable to Compaq's "parents." While finding that the release provision was clearly intended to cover past activity, the court concluded that HP was not a clearly intended beneficiary of the release because HP was not Compaq's parent as of the effective date of the agreement. HP countered that the use of the term "parents" in the settlement agreement expressed an intent to release companies that might become Compaq's parent in the future. The court noted that other places in the agreement clearly refer to future events and people, and that failure to specifically refer to future parents was counter to a clear intent for HP to benefit from the release.

Another factor that influenced the court's decision was that the remaining portions of the settlement agreement (the covenant not to sue and license provisions) were expressly limited to "Compaq Products." The court reasoned that the parties would not intend a broad release for acts of past infringement with respect to other products and then refer specifically to Compaq Products in the covenant not to sue and license. The court also noted that the agreement specifically referred to the possibility of a separate settlement of a different lawsuit between Unova and HP. Thus, the court concluded that the contract did not manifest a clear intent to benefit HP as an after-acquiring parent of Compaq.

The court went on to note that consideration of extrinsic evidence was inappropriate in cases such as this one in which the contract is clear on its face. Accordingly, the court concluded that consideration of extrinsic evidence that HP was intended to benefit from the Unova-Compaq settlement agreement was not appropriate.

- B. Yes. Based on its conclusion that the contract was clear on the issue of release, the court granted summary judgment to Unova on that issue. In other words, the court decided the issue of release in favor of Unova without remanding to the lower court for further consideration based on the presence of a genuine issue of material fact.

IV. Conclusion

This case illustrates the need for clear drafting of license agreements. Here, litigation resulted from the failure to employ consistent language between the release, covenant not to sue, and license provisions. The reference to "parents" when none existed also created a problem.

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