

PATENT CONTINUATIONS – A POTENTIAL TRAP IN CROSS-BORDER TRANSACTIONS

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In a recent cross-border stock purchase, seller disclosed to buyer that the U.S. target company had received notice that it might be infringing a third party's U.S. patents. It was clear that if infringement was subsequently proved, the target company would incur post-closing liability. The seller agreed to indemnify the buyer for this post-closing liability. At issue was the scope of the indemnification.

Under U.S. patent law, a patent owner may file "continuation" applications directed to related inventions fully disclosed in the originally asserted patents. The patent owner may also file "continuation-in-part" applications directed to newly disclosed improvements over the subject matter of the originally asserted patents. These applications are sometimes called "child" applications. A patent that issues under a child applications receives the same registration date as the original patent. This means that the target company's pre-closing business activities could infringe a patent that issues post-closing. Child applications may also provide basis for further grandchild applications filed in the future. In fact, well-funded patent trolls often file a series of continuations so that the U.S. patent rights can be strengthened at any time to better target specific infringers.

In talking to Canadian IP counsel, we understand that there is no direct equivalent to a patent "continuation" or "continuation-in-part" under Canadian law. The closest thing under Canadian patent law is a divisional application which is only available under very limited circumstances – when there is more than one invention under the original patent application.

Canadian companies buying U.S. targets must undertake due diligence that identifies so called "patent children" and, when necessary, request broadly drafted indemnification provisions. Ideally, the buyer will be indemnified for all claims arising from the patents specified under any infringement notice received by the target company and all patents arising from related continuation and continuation-in-part applications whether filed before or after closing.

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