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Federal Circuit Holds Ambiguity in License Terms Precludes Dismissal on the Pleadings

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By: Rachel J. Elsby

This case arose out of an infringement suit between Fraunhofer-Gesellschaft ("Fraunhofer") and Sirius XM Radio ("Sirius"). Fraunhofer, a German research organization, entered into a license in 1998 with Worldspace for a "worldwide, exclusive, irrevocable license with rights to sublicense" for technology used to stream data over multiple carrier data streams, such as with satellites. Worldspace then sublicensed it rights to Sirius, and by amendment, the parties made the sublicense irrevocable.

Worldspace later experienced financial difficulties, and in 2008 petitioned for bankruptcy. That petition was converted to Chapter 7 bankruptcy in 2012, where Worldspace rejected its agreement with Fraunhofer. Because the terms of the Fraunhofer/Worldspace license declared Worldspace's bankruptcy a rejection or breach of the agreement, Fraunhofer obtained the right to terminate. Fraunhofer, however, did not immediately terminate the license. Then, in 2015, following resolution of Worldspace's bankruptcy, Fraunhofer sent Sirius a letter alleging that Sirius was infringing four patents covered by both licenses. Fraunhofer also sent Worldspace a letter declaring their license terminated, and sued Sirius for infringement.

Sirius moved to dismiss Fraunhofer's complaint, arguing that its sublicense with Worldspace was a complete defense to infringement. The district court granted Sirius's motion. On appeal, the Federal Circuit considered whether (1) Fraunhofer terminated its license with Worldspace and (2) if so, whether that termination also effected termination of the Sirius sublicense.

On the issue of termination, Fraunhofer presented four theories for why the Fraunhofer/Worldspace license was properly terminated. The court rejected the first, that Worldspace's rejection of the license in bankruptcy unilaterally terminated it, outright. As to the three remaining "plausible" theories, which all concerned whether circumstances surrounding Worldspace's bankruptcy and the terms of the license gave Fraunhofer the right to terminate, the court held that it could not, on the record, determine whether Fraunhofer had the right to terminate *and* whether it properly exercised that right. Because neither of those issues were decided by the district court, the Federal Circuit declined to address them.

Next, the court turned to the question of whether, assuming the Fraunhofer/Worldspace contract was terminated, the Sirius sublicense survived. There, the court reversed the district court's determination, and held that such a determination requires interpretation of the specific license at issue. It does not survive, as the district court found, by operation of law, especially where, as here, the language of the licenses involved was ambiguous as to a sublicensee's survival rights. Thus, the court reversed and remanded the case to the district court to enable the parties to develop an appropriate record and for the district court to make the necessary factual findings.

Fraunhofer-Gesellschaft zur Förderung der angewandten Forschung e.V. v. Sirius XM Radio Inc., No. 2018-2400 (Fed. Cir. Oct. 17, 2019)

Practice Tip: Parties entering a licensing agreement should expressly address survival of sublicense rights in the event the license is terminated by one or more parties. And where a license is subject to bankruptcy proceedings, parties should attempt to obtain certainty regarding the effect on sublicenses prior to engaging in litigation.