

Eli Lilly and Co. v. Genentech, Inc., Not Reported in F.Supp. (1990)

17 U.S.P.Q.2d 1531

1990 WL 305392
United States District Court, S.D. Indiana,
Indianapolis Division.

ELI LILLY AND COMPANY, Plaintiff,

v.

GENENTECH, INC., Defendant.

GENENTECH, INC., Plaintiff,

v.

ELI LILLY AND COMPANY, Defendant.

Nos. IP 87-219-C, IP 88-1463-C. | July 17, 1990.

Attorneys and Law Firms

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Inc.

Opinion

ENTRY

[DILLIN](#), District Judge.

*1 This cause is before the Court on the motions of Genentech, Inc. for partial summary judgment and Rule 11 sanctions, and the motion of Eli Lilly and Company for disqualification of Genentech's counsel. For the following reasons, these motions are denied.

Background:

On August 25, 1978, Plaintiff Genentech, Inc. (Genentech), a California corporation, and Defendant Eli

Lilly and Company (Lilly), an Indiana corporation, entered into a contract regarding the synthetic production of human insulin (the Insulin Agreement). The contract stated that Genentech had demonstrated an ability "to genetically engineer microorganisms capable of producing human polypeptide hormones and has acquired related patent rights". The contract further stated that Lilly had experience in the production of human insulin from animal pancreas glands. The contract provides that its terms shall be governed by California law. Dr. Walter E. Buting, then a Lilly patent lawyer, negotiated the Insulin Agreement on behalf of Lilly.

In essence, the Insulin Agreement gave Lilly access to Genentech biological material which Lilly in turn was to use in developing and marketing synthetically produced human insulin. Lilly agreed to pay Genentech a royalty fee in exchange. Under Article VI of the agreement, Genentech granted to Lilly an exclusive patent to use its biological material "for the limited purpose of manufacturing, selling and using Recombinant Insulin without regard to Genentech Patent Rights...." In its complaint in No. IP 88-1463 (the Contract Action), Genentech claims, *inter alia*, that Lilly's research and production exceeded the scope of this limited patent license. Specifically, Genentech contends that Lilly used the biological material referred to in the agreement to develop a human growth hormone (hGH) product in order to compete with Genentech's hGH product. Genentech asserts that such production beyond the scope of the license breach of the parties' contract.

Lilly and Genentech are also embroiled in a related patent infringement suit. In No. IP 87-219-C (the Patent Action), Lilly seeks a declaratory judgment that several Genentech patent for the synthetic expression and purification of hGH are invalid and not infringed by Lilly's hGH process. . . .

Discussion:

1. Motion for Partial Summary Judgment:

Summary judgment, pursuant to [Rule 56, F.R.Civ.P.](#), is proper only when there is no genuine issue of material fact. *Big O Tire Dealers, Inc. v. Big O Warehouse*, 741 F.2d 160, 163 (7th Cir.1984). The burden of establishing the lack of any genuine issue of material fact is upon the

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movant, and all doubts are to be resolved against him. *Yorger v. Pittsburgh Corning Corp.*, 733 F.2d 1215, 1218 (7th Cir.1984). As the United States Supreme Court has observed:

Neither do we suggest that the trial court should act other than with caution in granting summary judgment or that the trial court may not deny summary judgment in a case where there is reason to believe that the better course would be to proceed to a full trial.

Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 106 S.Ct. 2505, 91 L.Ed.2d 202, 216 (1986).

The motion for partial summary judgment is focused on Genentech's contention that Lilly used Genentech materials to develop products other than insulin. Genentech argues that this alleged practice by Lilly breaches the following section of the license agreement:

Article VI

GRANT OF RIGHTS TO LILLY

6.01 *Use of Recombinant Microorganisms and Know-how Free of Genentech Patent Rights.* Subject to the payments of royalty as provided in Article VIII and the fulfillment of the other terms and conditions of this Agreement, Genentech hereby grants to Lilly the exclusive, irrevocable world-wide right with the right to grant sublicenses, to use all Genentech Recombinant Microorganisms for the limited purpose of manufacturing, selling and using Recombinant Insulin without regard to Genentech Patent Rights, and in connection only with such production, sale and use, to use all technical information and know-how supplied by Genentech hereunder. Rights granted hereunder shall include the right to practice under any applicable Genentech Patent Right.

The license agreement also included an integration clause which stated that the written contract "constitutes the entire Agreement between the Parties ... supersedes all previous Agreements, whether written or oral," and can be modified only "in [a] writing ... signed by the Party against whom such modification or waiver is sought."

Genentech seeks judgment as a matter of law that § 6.01 of the Insulin Agreement includes a *covenant by Lilly* not to use Genentech Recombinant Microorganisms (G.R.M.s) for non-insulin purposes. In short, Genentech's motion for summary judgment must be denied because such a negative covenant cannot be implied as a matter of law.

*3 The United States Supreme Court approved the use of limited patent licenses in 1938, recognizing them as essentially a waiver of the patentee's right to sue. *General Talking Pictures Corp. v. Western Electric Co.*, 304 U.S. 175, 58 S.Ct. 849, 82 L.Ed. 1273 (1938) [*Talking Pictures*]. In *Talking Pictures*, the defendant-licensee was given the right to "manufacture ... and to sell [amplifiers] only for radio amateur reception and radio broadcast reception." *Id.* at 181, 58 S.Ct. 849, 82 L.Ed. at 1276. The Court observed that the patent license at issue "amount[ed] to no more than a mere waiver of the right to sue." *Id.* at 181, 58 S.Ct. 849, 82 L.Ed. at 1276. Thus, the Court reasoned that "[b]y knowingly making sales ... outside the scope of the license, the transformer company infringed the patents embodied in the amplifiers." *Id.* at 181-82, 58 S.Ct. 849, 82 L.Ed. at 1277.

Subsequent caselaw has followed *Talking Pictures* by interpreting limited licenses as waivers of the right to sue so that violation of the license restriction gives rise to a patent infringement suit. These subsequent cases have also reasoned that violation of the license restriction does not give rise to an action for breach of contract.

In *Lanova Corporation v. Atlas Imperial Diesel*, 75 U.S.P.Q. 225 (Del.Super.Ct.1947), the license granted to Atlas the right "to manufacture engines ... embodying the inventions of its patents, said license being limited to stationary, marine, industrial and automotive engines" having a limited piston displacement. *Id.* at 226. Atlas allegedly used the patented technology to manufacture engines which were larger than the license specified. Following the reasoning of *Talking Pictures* that a limited license is a mere waiver of a patent infringement suit, the court reasoned that the license did not prohibit Atlas from manufacturing larger engines:

[T]he only thing which the defendant has given up by signing the license is its promise to pay royalties for the use of the patents in making engines within the license limits. The contract itself does not *restrain* it from doing anything which it could not have done otherwise; in

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effect, the **license** merely binds the defendant to pay for a limited use without fear of being sued for **infringement**.

Id. at 228 (emphasis original). The court stated that Atlas' use of patented technology to produce larger engines

is not barred by the **license** itself; the contract merely does not give that right. If the defendant should use the **patents** over and above the limitation, the plaintiff would have no remedy under the contract but could sue for **infringement**."

Id. Accord *Florida Canada Corp. v. Union Carbide Corp.*, 280 F.2d 193 (6th Cir.1960) (No negative covenant should be implied as a matter of law in a limited **license** of **patents** and trade secrets, especially when the **license** includes an integration clause)).

*4 In *B & J Manufacturing Co. v. Hennessy Industries, Inc.*, 194 U.S.P.Q. 496 (N.D.Ill 1976), then District Judge Flaum further developed rules to apply when a licensee has allegedly produced goods beyond the scope of the limited **patent license**. Judge Flaum followed the rule set down in *Lanova* and *Florida Canada Corp.* that a negative covenant could not be implied as a matter of law in the following excerpt, which is closely analogous to the case at hand:

[T]he purpose of the [**license**] agreement is to grant Hennessy the limited use of plaintiff's **patents** in return for the payment of royalties. As long as defendant has paid the royalties the plaintiff is receiving the benefits of his bargain. Moreover, it is not as if the plaintiff will lose any rights by the court's failure to imply such a negative covenant since B & J can, as it has, sue for **patent infringement** on those items manufactured outside the **license** grant. Therefore, this court agrees with the position enunciated in *Florida Canada Corp. v. Union Carbide & Carbon Co.*, *supra*, that no such negative covenant should be implied as a matter of law, especially in the face of an express integration clause.

Id. at 499.

Judge Flaum also noted that a very high standard of proof must be met before a negative covenant could be implied under the facts of *B & J Manufacturing Co.*:

As a general rule, covenants may only be implied into an integrated agreement "when the implied term is not inconsistent with some express term of the contract and

where there arises from the language of the contract itself, and the circumstances under which it was entered into, an inference that it is absolutely necessary to introduce the term to effectuate the intention of the parties."

Id. (emphasis original) (citing S. Williston on Contracts, § 1295 at 34–36 (3d ed. 1968)). The court concluded that a negative covenant could not be implied under the facts in *B & J Manufacturing Co.* because the evidence showed that the subject of manufacturing items beyond the scope of the **license** was never considered by the parties. *Id.* Rather, the evidence indicated that the intent of the parties in drafting the **license** was "to delineate what Hennessy *could do under* the agreement and not what Hennessy was prohibited from doing." *Id.*

Based on the above cited law, the Court cannot imply a covenant by Lilly not to produce non-insulin products into its Insulin Agreement with Genentech as a matter of law. Unlike *B & J Manufacturing Co.*, however, disputed issues of fact remain regarding whether implying a covenant by Lilly prohibiting its non-insulin use of G.R.M.s into the Insulin Agreement is "absolutely necessary" to effectuate the intent of the parties. In *B & J Manufacturing Co.*, the evidence on summary judgment showed that the intent of the parties in drafting the licensing agreement was "to delineate what Hennessy could do under the agreement and not what Hennessy was prohibited from doing." *Id.* In this case, the parties have presented conflicting affidavits regarding their intent in drafting § 6.01 of the agreement. It is also clear that discovery regarding the negotiation of the Insulin Agreement is far from complete.

*5 For the above stated reasons, the Court cannot imply a negative covenant into the integrated Insulin Agreement as a matter of law. The Court is similarly unable to grant summary judgment because the facts regarding the parties' intent in drafting § 6.01 are in dispute and not yet fully developed. Thus, *Genentech's motion for partial summary judgment is denied*.

II. Motion to Disqualify Genentech's Counsel:

[was denied]

Conclusion:

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For the reasons stated above, Genentech's motion for partial summary judgment, Lilly's motion to disqualify Genentech's counsel and Genentech's motion for sanctions under [Rule 11](#) are denied.

Parallel Citations

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Footnotes

- ¹ Lilly has also filed a motion asking the Court to review *in camera* "confidential exhibits" submitted in support of its reply brief on the disqualification issue. Because most of these exhibits were not submitted to opposing counsel for their review and reply, the Court has not considered them in ruling on Lilly's disqualification motion. Accordingly, Lilly's motion for *in camera* review of *ex parte* exhibits and Genentech's motion to strike the same are both rendered moot. [Briscoe v. Kusper](#), 435 F.2d 1046, 1057 (7th Cir.1970) (Reliance upon *ex parte* evidence considered *in camera* is "fundamentally inimical to due process." Preventing copying and inspection of such documents "severely curtailed [the opposing party's] ability to ascertain the exact claims at issue and their opportunity to respond to those claims.") (Cummings, J.)).
- ² Lilly replies that the above cited caselaw does not apply because the parties in this case are not on the eve of trial. Lilly's rejoinder is not persuasive for two reasons. First, as Genentech correctly notes, proximity of the trial to the disqualification motion is only one of several factors taken into account in the above cited caselaw. Second, considering the fact that a trial date has not yet been set in the co-pending cases against Genentech would elevate form over substance because Genentech has already invested approximately \$5 million in its present counsel. [Central Milk Producers Co-op](#), 573 F.2d at 992 (A disqualification motion should not be allowed "to deprive [an] opponent of counsel of his choice after substantial preparation has been completed"); [Accord Jackson](#), 521 F.Supp. at 1034-35. Since disqualification motions sound in equity, the Court may weigh the hardship which would be imposed on Genentech if the motion were granted given the substantial preparation already completed by its counsel.

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