IN THE UNITED STATES DISTRICT COURT

FOR THE WESTERN DISTRICT OF WISCONSIN

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ERAGEN BIOSCIENCES, INC.,
a Delaware corporation,

Plaintiff,

v.

NUCLEIC ACIDS LICENSING, LLC,
a Florida limited liability company and
STEVEN BENNER, an individual,

Defendants.

OPINION and ORDER

06-C-305-C

- -

In this patent licensing dispute, plaintiff Eragen Biosciences, Inc. and defendants Nucleic Acids Licensing, LLC and Steven Benner each contend that the opposing side has breached the terms of their AEGIS agreement. Plaintiff seeks a declaration that the agreement is valid; defendants seek a declaration that the agreement is invalid. In addition, both sides plead common law claims of "money had and received" and unjust enrichment. Jurisdiction is present under 28 U.S.C. § 1332.

The case is before the court on the parties' cross-motions for summary judgment, dkt. ##25 and 46. Because defendants' interpretation of § 3.7 of the AEGIS agreement is the right one, defendants do not owe plaintiff any refund. Instead, plaintiff owes defendant an additional $3,416 in royalties. Although plaintiff underpaid these royalties and may have failed to make timely payments on past due maintenance fees, defendants waived their objection to the improper and untimely payments by engaging in a course of conduct that reasonably led plaintiff to believe the AEGIS agreement remained in force. Therefore, I will grant plaintiff's motion for declaratory judgment that the agreement is valid. Defendants' cross-motion for declaratory judgment will be denied. Finally, although both parties have erred in various ways with respect to their compliance with the AEGIS agreement and its enforcement, neither breached its duty of good faith and fair dealing with respect to the AEGIS agreement, the only agreement that is enforceable in this lawsuit.

From the parties' proposed findings of fact and from authenticated copies of the AEGIS agreement (which both parties have submitted in connection with their summary judgment materials), I find the following facts to be material and undisputed.

UNDISPUTED FACTS

A. Parties

Plaintiff Eragen Biosciences, Inc. is a Delaware corporation with its principal place of business in Madison, Wisconsin. Plaintiff is a biotechnology company that employs 42 people.

Defendant Nucleic Acids Licensing, LLC is a limited liability corporation incorporated in the State of Florida, with its principal place of business in Gainesville, Florida. Defendant Steven Benner is a citizen of Florida. He is the sole member and manager of defendant Nucleic Acids Licensing.

B. Past Dealings between the Parties

1. Background

Defendant Benner is the named inventor in many patents in the fields of nucleic acid chemistry, combinatorial chemistry, bioinformatics and "DNA analogs containing modified backbones." Defendant Benner invented each of his "technologies" when he was a professor at the Swiss Federal Institute of Technology. He is now a professor at the University of Florida, where he runs a laboratory.

In 1994, defendant Benner formed Sulfonics, Inc. as a joint corporate-academic venture for the purpose of developing and marketing the technologies he had patented. In 1999, Sulfonics merged with plaintiff. That same year, plaintiff entered into four licensing agreements with defendant Benner: the "Expanded Genetic Alphabet License Agreement," "Receptor Assisted Combinatorial Chemistry License Agreement," "Bioinformatics License Agreement," and the "Backbone Modified DNA License Agreement." Under these agreements, plaintiff was obliged to develop the licensed technology; pay all maintenance fees for the licensed patents; provide compositions to defendant Benner and his research group; provide defendant Benner and his colleagues with current versions of software that incorporated any of the licensed technology; and engage in research collaborations leading to joint publications.

From 1999 until 2003, defendant Benner served on plaintiff's board of directors. During his time on the board, defendant Benner was provided with copies of plaintiff's audited financial reports and interim financial statements. Defendant was and is aware that plaintiff practices accrual based accounting in accordance with generally accepted accounting principles (known in the accounting world as GAAP).[1]

Over time, numerous disagreements arose between plaintiff and defendant Benner regarding the 1999 licensing agreements and the direction of the company. Specifically, defendant Benner accused plaintiff of failing to develop his licensed technologies and to abide by the joint publication provisions of the parties' licensing agreements. In addition,

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[1]Although no party proposes it as fact, it is clear from the briefs that the parties agree on the definition of accrual based accounting, as described by Justice O'Connor in her dissent in Shalala v. Guernsey Memorial Hospital, 514 U.S. 87, 104 (1995): "Under the accrual basis of accounting, revenue is reported in the period when it is earned, regardless of when it is collected, and expenses are reported in the period in which they are incurred, regardless of when they are paid. This definition of "accrual basis" simply incorporates the dictionary understanding of the term, thereby distinguishing the method required of cost providers from "cash basis" accounting (under which revenue is reported only when it is actually received and expenses are reported only when they are actually paid)."

on multiple occasions, plaintiff made untimely royalty and licensing payments. In 2003, defendant Benner resigned from plaintiff's board of directors.

In an attempt to resolve the disputes that had arisen with respect to the 1999 agreements, the parties began negotiating new licensing agreements. The negotiation process was contentious, with threats of litigation abounding. On April 27, 2005, plaintiff and defendant Benner entered into three new licensing agreements: the Artificially Expanded Genetic Information System (AEGIS) agreement (which covers United States Patents Nos. 5,432,272, 6,001,983, 6,037,120, 6,140,496, 5,965,364, 6,617,106 and 6,627,456), the RACS agreement (which covers United States Patents No. 5,958,702) and the Bioinformatics agreement (which covers United States Patent Nos. 5,958,784 and 6,377,893) . Under the terms of the new agreements, plaintiff was relieved of liability for its past breaches of the 1999 agreements.

2. <u>The AEGIS agreement</u>

The AEGIS agreement is the only agreement at issue in this lawsuit. Ninety-five percent of plaintiff's revenue is derived from the technologies licensed under the AEGIS agreement. The AEGIS contains a number of provisions relevant to the parties' present dispute.

Section 3.4 governs plaintiff's sublicense royalties. In relevant part, it provides that plaintiff shall pay defendant Benner:

> twenty-five percent (25%) of sublicense fees and royalties and other consideration received by EraGen and its affiliates from the Existing Sublicenses and successor sublicenses specifically listed in Section 3.4(a), and specifically including the [Bayer Agreement]. . . .

Under section 3.7 of the agreement, titled "Calculation Date," royalties are to be paid

> . . . at the rates specified under this Agreement for all revenues accruing from Net Sales or sublicensing or grants on or after February 15, 2005. Royalties owed by EraGen to Benner for all revenues prior to February 15 [are to] be at the terms specified in and payable on the dates provided in the Expanded Genetic Alphabet Agreement.

(An earlier draft of § 3.7 would have required plaintiff to pay the rates specified in the Agreement "for all transactions on or after February 15, 2005." However, defendant Benner's lawyer replaced that language with the phrase "revenues accruing from Net Sales or sublicensing or grants on or after February 15, 2005.") In the final agreement, the word "accruing" is not defined.

The agreement provides that sublicensing royalties are to be paid biannually, on September 1 and March 1 of each year. Late payments are subject to a compound interest charge of 8% annually. Each royalty payment is to be accompanied by a report specifying "each item of income for which a royalty payment [wa]s made, the payer, the title of the grant, contractor sublicense associated with the item of income, the gross amount received, and any amounts deducted" in accordance with other terms of the agreement.

Section 3.12 outlines the parties' audit rights. In full, it states:

Each party shall maintain complete, clear, and accurate books and records to support the performance of its obligations and those of its Affiliates under this Section 3 for at least three (3) years following the end of the calendar year to which they pertain. Such books and records will be open to inspection during such three (3) year period by an independent auditor chosen by the receiving party, and reasonably acceptable to the paying party. All representatives of such auditor involved in the inspection and audit shall be required to sign reasonable nondisclosure agreements and to abide by reasonable site security requirements when carrying out the inspection and audit. Such on-site inspections may be made no more than once each calendar year, at reasonable times and on reasonable notice, provided that an additional inspection can be made if material underpayment is found during the first inspection. Inspections conducted under Section 3.12 shall be at the expense of the receiving party, unless an underpayment of at least five percent (5%) is found during such audit, in which case the paying party shall pay the costs of such an audit. The parties will endeavor to minimize disruption of the paying party's normal business activities to the extent reasonably practicable. Such audit shall take place during regular business hours during the term of this Agreement and for two (2) years following the expiration of this Agreement.

Section 4.2 governs termination of the agreement by defendant Benner. It states:

Benner may terminate this Agreement upon written notice to EraGen upon:

A. non-payment of the payments due Benner under Sections 3.1, 3.2, 3.3 and 3.4, and 5.3, provided that EraGen or its designees shall have the right to cure such breach within sixty (60) days of EraGen receiving written notice from Benner;
B. failure of EraGen to pay federal or state taxes;
C. violation of the terms of the releases granted by EraGen under Section 6.5; or
D. breach of Section 6.4.

Upon termination of this Agreement pursuant to Section 4.2, all of the rights in the Licensed Patents and Licensed Know How will revert to Benner, subject only to Benner's obligations to sublicensees as provided in Section 2.3.

Section 5.3, referred to in section 4.2(A), above, relates to the payment of patent maintenance fees. It states:

> EraGen shall pay all maintenance fees for issued patents within the Licensed Patents, and Benner shall execute any documents required for such action by EraGen within fifteen (15) days of written request. To the extent it has not already done so, EraGen will take the actions required by the United States Patent and Trademark Office to reflect a change in status from small entity to large entity for purposes of determining maintenance and other applicable fees payable to the United States Patent and Trademark Office for the Licensed Patents, at its own expense, including any retroactive payments that might be required to remedy inaccuracies in the maintenance fees paid prior to the Effective Date for the Licensed Patents. EraGen will pay any maintenance fees that are required for the Licensed Patents within two (2) months of the date on which such fees first become payable, and failure to make these payments within this time period will be treated in the same way as a failure to make other payments under Section 4.2(A), with any payment made by EraGen after notice by Benner under Section 4.2(A) being made directly to the United States Patent and Trademark Office to cure such breach. In the event that EraGen fails to pay the maintenance fees, Benner shall have the right to step in and make such payments (including payments where insufficient maintenance fees have been paid) and shall be promptly reimbursed by EraGen upon receipt of an invoice from Benner. Within fifteen days of the Effective Date, EraGen will reimburse Benner for all patent maintenance costs incurred by Benner for the Licensed Patents on or after January 1, 1999 and prior to the Effectice Date, in the total amount of $4,015 or such higher amount as shown in invoices from Benner. Failure to reimburse Benner for such prior or future maintenance payments shall be treated in the same way as failure to make other payments under Section 4.2(A).

Section 9.2 of the agreement specifies that the agreement "supercedes and replaces the Expanded Genetic Alphabet Agreement and [that] each party agrees to waive any and all failures by the other party to comply with any and all provisions of the Expanded Genetic Alphabet Agreement which occurred prior to the execution of this Agreement, with the exception of payment terms."

Section 9.5 governs notice, and reads as follows:

> Any required notices hereunder shall be given in writing by certified mail or overnight express delivery service at the address of each party below, or to such other address as either party may substitute by written notice. . .

Section 9.5 provides further that all notices sent to plaintiff must be mailed to its President and Executive Chief Officer and to its Corporate Counsel.

Finally, the agreement contains the following choice of law provision:

> This Agreement and all disputes arising out of or related to this Agreement, or the performance, enforcement, breach or termination hereof, and any remedies relating thereto, shall be construed, governed, interpreted and applied in accordance with the laws of the State of Florida, U.S.A., without regard to conflict of law principles, except that questions affecting the construction and effect of any patent shall be determined by the law of the country in which the patent shall have been granted.

3. Assignment

Before the parties entered into the AEGIS agreement, plaintiff had sublicensed the technology covered by the agreement to Bayer, which has obtained approval from the Food and Drug Administration to use the technology in a DNA diagnostic product used to manage the medical care of people infected with certain viral infections. On August 11, 2005, after the AEGIS agreement was signed, defendant Benner assigned the agreement and its related patents to defendant Nucleic Acids Licensing.

C. Royalty Payments

On August 31, 2005, plaintiff sent defendant Benner a check in the amount of $139,093 for "agreement fees" due under the AEGIS, RACS and Bioinformatics agreements. The payment was not accompanied by a royalty report detailing the amounts paid under each separate agreement. On September 1, 2005, defendant Benner received and deposited the payment.

Because no royalty report accompanied the payment, defendant Benner tried to determine how much plaintiff owed under each agreement. He did this by studying a profit and loss statement to plaintiff's shareholders for the month of November 2004, royalty reports from plaintiff for the "previous two semesters," plaintiff's "Dear Shareholders" letter dated June 2005, federal government websites reporting grant activity to plaintiff, general information concerning the sale of Bayer products and the full text of the Alantos sublicense agreement. Using information from those sources, defendant Benner estimated that defendant Nucleic Acids Licensing was due approximately $165,523 in royalty payments from plaintiff under the AEGIS Agreement. Defendant Benner estimated that plaintiff owed approximately $4185 under the Bioinformatics License Agreement, $53,846 under the

RACS Agreement and $1,333 in outstanding fees due under old agreements.

On September 2, 2005, defendant Benner sent plaintiff a letter titled "Notice of Termination." It contained the following language:

> **Whereas:**
> To the best of his knowledge and belief, Benner (hereinafter designated the Licensor) is due to be paid by EraGen Biosciences an Amount of c[irc]a:
>
> $224,887.00
>
> in royalties and other payments under Articles 3 & 5 of the Agreements, for the period beginning:
>
> January 1, 2005
>
> and ending
>
> June 30, 2005
>
> on or before the end of: September 1, 2005.
>
> **And whereas:**
> Payments in this Amount were not received by the Licensor as of this date.
>
> **Therefore:**
> EraGen has breached the Agreements.
>
> **Further therefore:**
> The Licensor hereby exercises his right under the Agreements to terminate the Agreements immediately, with final termination to occur on November 1, 2005, sixty days following this notice.

On September 7, 2005, plaintiff sent a letter to defendant Benner, enclosing the overdue license and royalty reports. In the letter, plaintiff asserted that it had miscalculated the amount due under the AEGIS agreement. According to plaintiff, although it had underpaid royalties on several of its sublicenses, it had overpaid the royalties due under the Bayer agreement by calculating payments using the wrong royalty rate. Plaintiff asserted that the net effect of these errors was that it had overpaid defendants in the amount of roughly $40,000.

From September 2005 through October 2005, the parties exchanged a flurry of letters and emails regarding the amount of royalties due to defendant Benner on September 1, 2005. It soon became clear that much of their disagreement resulted from their interpretation of § 3.7 of the AEGIS agreement.

Under the terms of the AEGIS agreement, plaintiff was obligated to pay defendant Benner 25% for sublicense fees and royalties it and its affiliates received from a number of its existing sublicenses, the primary one of which was the Bayer sublicense. Previously, plaintiff had paid only 10% of the sublicense fees and royalties generated from those sublicenses to defendant Benner. Under § 3.7, plaintiff was required to reimburse defendant Benner at the 25% rate "for all revenues accruing from . . . sublicensing . . . on or after February 15, 2005."

As defendant Benner explained in an email message dated October 3, 2005, he took the position that under § 3.7 of the AEGIS agreement,

> the relevant date [for calculating the new royalty rate] is the date that the

> income was "received by EraGen," not the date that the sublicensee might have generated income upon which payments to EraGen might be based.

Plaintiff disagreed. On October 10, 2005, plaintiff asserted:

> As detailed in Section 3.7 of the Agreement, the 25% rate was to be effective "for all revenues accruing from NetSales or sublicensing or grants on or after February 15, 2005. Royalties owed by EraGen to Benner for all revenues prior to February 15, 2005, shall be at the terms specified in and payable on the dates provided in the Expanded Genetic Alphabet Agreement." Therefore, the Bayer royalty revenues that [were] accrued (but not necessarily received) prior to February 15, 2005, are subject to the 10% rate.

On October 24, 2004, defendant Benner sent plaintiff two letters. In one of these, he alleged that plaintiff EraGen "ha[d] failed to make payments due under Sections 3.1, 3.2, 3.3 and 3.4, and 5.3 of the Agreement." Dkt. #30, exh. F, at 1. He asserted that plaintiff had failed to file complete reports, had inaccurately reported accounting information regarding its royalty payments and had underpaid its royalty obligations. Defendant Benner concluded the letter by stating, "Under Article 4.2 of the Agreement, failure to make these payments is sufficient grounds for termination. Therefore, the Notice of Termination, dated September 2, 2005, stands." Id. at 2.

Plaintiff responded to this letter on October 31, 2005. Plaintiff set forth the reasons why it believed it had overpaid defendant Benner and requested a refund of $41,599. Plaintiff's letter ended with the following statement: "To summarize, EraGen is in compliance with all reporting and payment obligations, and as such, will assume that your

Notice of Termination is null and void. If you disagree, please have your attorney send the reason pursuant to our Agreement, for final resolution." Dkt. #30, exh. G.

From November 2005 through February 2006, defendants made no mention of the royalty dispute. Then, on February 21, 2006, the parties picked up where they had left off. This time, defendant Benner's lawyer wrote to plaintiff, again asserting that the phrase "revenues accruing" in § 3.7 should be read as a synonym for "revenues received." The February 21 letter made no mention of the AEGIS agreement being terminated.

On March 1, 2006, defendant Benner received and cashed plaintiff's semi-annual AEGIS royalty payment, which covered royalties for the period from July 2005 through December 2005.

On March 6, 2006, plaintiff's lawyer responded to defendants' February 21 letter, reiterating plaintiff's interpretation of § 3.7. Defendants' lawyer replied on March 27, 2006, stating:

> Frankly, we find your analysis of the term "accruing" in Section 3.7 with respect to the term "received" in Section 3.4 C to be inconsistent. However, we also believe that this matter can be resolved if Eragen will provide us with a copy of the Bayer Agreement and copies of the relevant royalty reports from Bayer to EraGen. Please therefore send me copies of these documents at your earliest convenience . . . . I would appreciate an early reply to this letter indicating when we can expect receipt of those documents.

On April 6, 2006, EraGen's lawyer sent defendant Benner's lawyer the financial documents he had requested.

On May 18, 2006, defendant Nucleic Acids Licensing filed suit against plaintiff in the United States District Court for the Northern District of Florida, seeking a declaratory judgment that the AEGIS agreement was terminated in 2005.

If plaintiff's reading of § 3.7 is correct, plaintiff overpaid defendant Benner roughly $49,000. (Defendants quibble with the details, but appear to concede that the amount of overpayment would fall somewhere in this vicinity.) If defendant Benner's reading is the correct one, plaintiff owes defendant Benner $3,416.

D. Maintenance Fees

Section 5.3 of the AEGIS agreement makes plaintiff responsible for changing the status of the maintenance fees due to the United States Patent and Trademark Office (PTO) from small entity status to large entity status, including making past due payments related to the change. This requirement refers to the fact that the PTO permits "small entities" with fewer than 500 employees to pay reduced patent maintenance fees. Because plaintiff employs only 42 people, it qualified for small entity status at the time the licensed technology was first assigned to it. However, if a small entity enters into a sublicense with a "large entity," the maintenance fees increase.

At the time the '272, '364, '983, '120, '496, '456 and '106 patents were registered with the PTO, plaintiff was entitled to claim small entity status with respect to each of them.

However, on July 1, 2000, plaintiff entered into a sublicense with Bayer. Bayer employs more than 500 people, so all fee payments plaintiff made to the PTO after July 2000 should have been paid at the large entity rate. They were not.

When the parties entered the AEGIS agreement, incorrect fee payments had been made with respect to the '364, '983, '106 and '456 patents. Section 5.3 of the AEGIS agreement required plaintiff to fix this problem "to the extent it ha[d] not already done so" by changing the status of the licensed patents with the PTO, so that each reflected plaintiff's large entity status. In addition, plaintiff was required to pay all overdue fees associated with the error. The AEGIS agreement does not provide any explicit timeframe within which plaintiff was required to act.

On November 9, 2005, plaintiff wrote to defendant Benner, asking him to complete forms changing the power of attorney and correspondence addresses for the relevant patents in order to allow plaintiff to communicate directly with the PTO regarding the past due payments and entity status changes plaintiff was required to make under § 5.3. Although plaintiff knew that it was possible to pay the required fees and update the entity status for each relevant patent without having defendant Benner execute a power of attorney or change of correspondence address form, when plaintiff's letter was returned to it unopened, plaintiff sent it to defendant Benner a second time.

On November 27, 2005, defendant Benner responded via email, stating in relevant part: "EraGen need not be designated as the correspondence addressee for it to meet its obligations with respect to maintenance fees, which should have been done in any case in March, 2005."

On November 29, 2005, plaintiff responded to defendant's email by explaining:

> First, since EraGen is responsible for notifying the PTO of the loss of entitlement to small entity status, it is more efficient that the PTO respond directly with [sic] EraGen. . . . In any event, it is advantageous for the PTO to have a direct-line of communication with the individual entity (or in PTO parlance, the "customer") that is submitting the paperwork (and vice-versa). That is why Form 123 was included.
>
> Second, with respect to maintenance fees, the PTO will eventually send to EraGen the Maintenance Fee Statement which will confirm whether payment was timely received. If there are any errors on the statement, EraGen will make the necessary corrections in a timely manner without having to first contact you and then waiting for a copy. This is why Form 47 was included.
>
> I have no intention of keeping any paperwork or correspondence from your review—my request simply makes it easier for EraGen to comply with its obligations under the agreement . . . . Please let me know if this makes sense and whether you will be sending to me the requested forms.

Dkt. #32, Exh. D. Receiving no response to this message, plaintiff sent a follow-up email on December 2, 2005, asking defendant Benner whether he would "be following up and sending those forms" or whether it was his "intent to not do so." Defendant Benner did not respond and plaintiff took no further action to resolve the matter of the entity status and past due maintenance fees.

Then, in his February 21, 2006 letter to plaintiff regarding licensing fees and other matters, defendants' lawyer wrote:

> . . . I have checked the maintenance fee records for all five of the licensed patents for which a maintenance fee would have been due prior to the current time; copies of the printout for each of those patents is attached. As you will see from a review of this information, the maintenance fees paid by EraGen after the January 1, 1999 license agreement were all based on a "small entity" status. While that status would have been appropriate for payments by Dr. Benner prior to licensing, any license to an entity such as Bayer would necessarily require payment of a large entity fee . . . . On behalf of Dr. Benner, I request that EraGen's patent counsel take steps to immediately correct these deficiencies if not already done. If done, please provide Dr. Benner with the relevant documents. Of course, Dr. Benner will cooperate as necessary to achieve these objectives. I cannot emphasize enough the necessity for resolving these deficiencies as failure to do so timely may adversely impact the enforceability of these patents and constitutes a serious breach of the AEGIS agreement.

On March 2, 2006 and March 6, 2006, plaintiff's lawyer filed all paperwork required to correct the deficiencies in the past due maintenance fees and change the status of the patents that had been designated incorrectly. The PTO accepted plaintiff's withdrawal of it small entity status with respect to each of the patents and accepted the deficiency payments.

On March 4, 2006, defendant Benner wrote to plaintiff directly, asserting that the AEGIS agreement had been terminated under § 5.3 because of plaintiff's failure to resolve the entity status and make the payments required under that section. In his letter, defendant Benner contended that by citing § 5.3 in his October 24 letter to plaintiff regarding royalty disputes between the parties, plaintiff had been given notice that the agreement could be terminated within 60 days as a result of plaintiff's failure to take corrective action with respect to the entity status of the '272, '364, '983, '120, '496, '456 and '106 patents.

On May 30, 2006, two weeks after filing suit in the Florida district court, defendants' lawyer sent plaintiff the following letter:

> I turn first to the letter regarding maintenance fee payments, which for the first time confirms that EraGen had materially breached the License Agreement as of Dr. Benner's letter of October 24, 2005, and which breach was not cured within the 60 days specified in a reading together of Sections 4.2A and 5.3 of the April 27, 2005 agreement. Accordingly, I take this opportunity to again state unequivocally that Nucleic Acids Licensing, LLC deems the License properly terminated.
>
> * * *
>
> As stated above, it is NAL's position that the April 27, 2005 License Agreement is terminated. However, we understand that EraGen does not acquiesce in that position. Therefore, NAL has filed a declaratory judgment action in the United States District Court for the Northern District of Florida, Gainesville Division.

Dkt. #31, exh. G.

OPINION

A. <u>Choice of Law</u>

First things first. Before turning to the claims, it is necessary to establish what law governs them. In a lawsuit based upon diversity, such as this one, a federal court applies the choice of law principles of the jurisdiction in which it sits to determine the substantive law that will govern the case. Klaxon Co. v. Stentor Electric Manufacturing Co., 313 U.S. 487 (1941). In this court, Wisconsin's choice of law principles apply.

Wisconsin law recognizes that parties with equal bargaining power are free to "expressly agree that the law of a particular jurisdiction shall control their contractual relations," so long as the agreement does not come "at the expense of important public policies of a state whose law would be applicable if the parties choice of law provision were disregarded." Bush v. National School Studios, Inc., 139 Wis. 2d 635, 642, 407 N.W.2d 883, 886 (1987). Section 9.14 of the AEGIS agreement provided expressly that "all disputes arising out of or related to th[e] Agreement, or the performance, enforcement, breach or termination" of the agreement were to be "construed, governed, interpreted and applied in accordance with the laws of the State of Florida." Dkt. #15, exh. A, at 15. All of the claims raised in plaintiff's complaint and in defendant Nucleic Acids Licensing's counterclaim relate to or arise out of the AEGIS agreement. The parties suggest no reason why the choice of law provision in the AEGIS agreement might be unenforceable; therefore, Florida law governs each of the parties' claims in this lawsuit.

B. Validity of the AEGIS Agreement

At the heart of this suit lie the parties' cross-motions for declaratory judgment. Under § 4.2 of the AEGIS agreement, defendant Benner has the right to terminate the AEGIS agreement under certain enumerated circumstances. At issue is whether defendant Benner was entitled to, and in fact did, terminate the agreement as a result of plaintiff's alleged underpayment of royalties due under §§ 3.4 and 3.7 and failure to make timely payment of retroactive maintenance fees as required by § 5.3.

Section 4.2(A) of the AEGIS agreement provides that defendant Benner (or defendant Nucleic Acids Licensing, as Benner's assignee) is entitled to terminate the AEGIS agreement upon "non-payment of the payments due [him] under Sections 3.1, 3.2, 3.3 and 3.4, and 5.3, provided that [plaintiff] shall have the right to cure such breach within sixty . . . days of . . . receiving written notice." In order to determine which party is entitled to declaratory judgment regarding the validity of the agreement, three questions must be answered: (1) Did plaintiff engage in "non-payment of the payments due" to defendant Benner under §§ 3.4 or 5.3?; (2) Did defendant Benner provide plaintiff with adequate notice of his intent to terminate?; and (3) If notice was properly provided, did plaintiff cure the breach within 60 days of notification? Not surprisingly, the parties dispute the answers to all three questions.

Because much of the disagreement in this lawsuit stems from the parties' conflicting interpretations of the AEGIS agreement, specifically, §§ 3.7 and 5.3, the next step is to interpret the agreement's provisions governing the payment of royalties and maintenance fees. Therefore, I turn to the language of the AEGIS agreement.

1. Meaning of the provisions

a. Sections 3.4 and 3.7

The parties' dispute with respect to royalties due under §§ 3.4 and 3.7 of the AEGIS agreement boils down to the meaning of a single word: accruing. Both parties insist that the contract "is unambiguous and compels the rendering of judgment in their favor," University of Miami v. Frank, 920 So. 2d 81, 85 (Fla. Dist. Ct. App. 2006), all the while "ascrib[ing] a different meaning to the 'unambiguous' language of the contract," Miller v. Kase, 789 So. 2d 1095, 1098 (Fla. Dist. Ct. App. 2001).

"When a contract is susceptible to two different interpretations, each one of which is reasonably inferred from the terms of the contract, the agreement is ambiguous." Id.; see also Torwest, Inc. v. Killilea, 942 So. 2d 1019, 1020 (Fla. Dist. Ct. App. 2006). If ambiguous, the words of the contract should be given their plain and ordinary meaning, Leisure Resorts, Inc. v. City of West Palm Beach, 864 So. 2d 1163, 1166 (Fla. Dist. Ct. App. 2003). When exploring the meaning of an ambiguous term, "to determine its true meaning, the court must review the entire contract without fragmenting any segment or portion." Torwest, 942 So. 2d at 1020; J.C. Penney Co. v. Koff, 345 So. 2d 732, 735 (Fla. Dist. Ct.

App. 1977). The court "should try to place itself in the situation of the parties, including the surrounding circumstances, to determine the meaning and intent of the language used." Miller, 789 So. 2d at 1098 (citing Underwood v. Underwood, 64 So. 2d 281, 288 (Fla. 1953)).

Before the parties entered into the AEGIS agreement, plaintiff paid defendant Benner 10% in royalties on the money it earned from its sublicenses. Under the terms of § 3.4 of the AEGIS agreement, plaintiff continues to owe 10% on some sublicensing revenues, but is required to pay defendant Benner 25% of its revenue from other sublicenses, including the Bayer Agreement. Section 3.7 governs the date and manner in which plaintiff was required to begin paying the higher rate. According to that section, plaintiff must pay defendant Benner at the 25% rate for "all revenues accruing from . . . sublicensing . . . on or after February 15, 2005."

Plaintiff understands the phrase "revenues accruing" to be a term of art that refers to the accrual method of accounting, which plaintiff practices and of which defendant Benner was aware from the years he had spent on plaintiff's board of directors. When plaintiff calculated its September 1, 2005 royalty payment, it intended to apply a 10% rate to all revenue it accrued from its sublicenses before February 15, 2005, and a 25% rate to revenue accrued on designated sublicense agreements on or after that date. Unfortunately, it erred, and applied the 25% to some revenue from the Bayer license agreement that had been received on or after February 15, 2005, but that had accrued at an earlier date. Therefore, by plaintiff's calculation, it overpaid defendant somewhere in the range of $40,000-50,000. (Plaintiff initially contended that it had overpaid defendant by $41,883. It now alleges that its damages were $49,383.)

Defendants disagree vehemently with plaintiff's interpretation of "accruing." Defendants contend that although the word may have different meanings in other contexts, when read in the context of the AEGIS licensing agreement, it is merely a synonym for "received." If defendants are correct, then plaintiff *under*paid them by $3,416.

According to plaintiff, there are two reasons to think that the word "accruing" should be understood as a reference to accrual based accounting, under which revenues are recorded as they are earned by the sublicensee, rather than at the time they are received by the sublicensor. First, it is undisputed that plaintiff practices accrual based accounting and that defendant Benner was aware of this fact at the time the AEGIS agreement was drafted. Second, plaintiff asserts that the phrase "revenues accruing" is unambiguously a technical phrase, used to refer to the method by which it records income under its accounting system.

Courts must give the words of the contract their plain and ordinary meaning, whenever possible. Leisure Resorts, Inc., 864 So. 2d at 1166; Beans v. Chohonis, 740 So. 2d 65, 67 (Fla. Dist. Ct. App. 1999). In this case, however, the word "accrue" has several possible meanings, neither one more plausible than the other. The New Oxford American

Dictionary 11 (2001), favors plaintiff's reading, defining "accrue" to mean:

> trans. (of sums of money or benefits) be received by someone in regular or increasing amounts over time: *financial benefits will accrue from restructuring* [as adj.] (accrued) *the accrued interest*;
>
> intrans. accumulate or receive at the end of a financial period for work that has been done but not yet invoiced.

However, the American Heritage Dictionary 12 (4th ed. 2000), ascribes a much less technical meaning to "accrue,"defining it as:

> —intrans. 1. To come to one as a gain, addition, or increment: *interest accruing in my savings account.*
>
> 2. To increase, accumulate, or come about as a result of growth: *common sense that accrues with experience.*
>
> * * *
>
> —tr. To accumulate over time: *I have accrued 15 days of sick leave.*

Because accrue has several "plain meanings," the dictionary does not resolve the parties' dispute about the word's definition in the context of the AEGIS agreement.

Where to look next? Plaintiff turns to case law, and cites a 1935 decision from the Supreme Court of Florida, in which the Court held that evidence of one party's accounting practices was relevant to determine what the parties intended when they included the phrase "accrued profits" in their contract. Orlando Orange Groves Co. v. Hale, 161 So. 284, 294-95 (Fla. 1935). Although that case involved a contract that made reference to accrual, it was otherwise wholly distinguishable from this one. In Orlando Orange Groves, the Florida Supreme Court had before it considerable evidence not only of the plaintiff's accounting practices, but of the parties' long-term course of dealing under the relevant contract. It was the parties' "practical construction placed [on the contract] by the board of directors, over a considerable period of years" upon which the court's holding rested—not on the plaintiff's accounting practices. Id. at 295. Although defendant Benner's knowledge of plaintiff's accounting system is relevant to understanding what the parties meant by the phrase "revenues accruing" in § 3.7 of the AEGIS agreement, it is not dispositive.

When interpreting a contract, it is axiomatic that courts review the contract as a whole and give effect to all its language. Leisure Resorts, Inc., 864 So. 2d at 1166. Defendants contend that the parties' use of the word "received" in § 3.4 and § 3.10 should be read as a clarification (and not a contradiction) of the meaning of "accruing" as it is used in § 3.7. Section § 3.4 states clearly that royalty payments must be made on all "sublicense fees and royalties and other consideration *received* . . . from the Existing Sublicenses and successor sublicenses." From this, defendants extrapolate the parties' intent that the higher rate be paid for all money received beginning on February 15, 2005. In a similar vein, defendants cite § 3.10 of the agreement, which sets forth the information that must be included in each royalty report. According to § 3.10, royalty reports must accompany all royalty payments, and must "specify, for each item of income for which a royalty payment

[wa]s made, the payer, the title of the grant, contractor sublicense associated with the item of income, the *gross amount received*, and any amounts deducted" in accordance with other terms of the agreement. (Emphasis added.)

Equally important is what the contract does not say. Defendants emphasize that the AEGIS agreement does not define the term "accrue" in any specialized way, does not refer to accrual based accounting or to GAAP, and does not utilize the word anywhere else in the agreement. Moreover, although accrual accounting relies on estimated income that must later be verified and balanced, the contract contains no provisions for the filing of updated royalty reports, or the payment of additional royalties or refund of overpayment (when estimates turn out to be have been wrong).

Although neither side's reading of § 3.7 is implausible, when viewing the contract in the context of the entire AEGIS agreement, the balance tilts strongly in favor of defendants' reading of the agreement. Could the parties have drafted § 3.7 in a way that would have said more clearly how they intended to calculate the date for increased royalty payments under § 3.4? Absolutely. Nevertheless, I conclude that defendants' reading is the better one. The practical conclusion to be drawn from that interpretation is that plaintiff was obligated to pay the 25% royalty rate specified in § 3.4 for all revenue it received from the specified sublicensing agreements as of February 15, 2005. Because it is undisputed that plaintiff did not do so, the next question will be what effect, if any, its breach had on the validity of the agreement. (More on that in §§ B.2 and B.3, below.)

b. Section 5.3

Section 5.3 imposes on plaintiff the obligation to:

> pay all maintenance fees for issued patents within the Licensed Patents . . . within fifteen (15) days of written request. To the extent it has not already done so, EraGen will take the actions required by the United States Patent and Trademark Office to reflect a change in status from small entity to large entity for purposes of determining maintenance and other applicable fees payable to the United States Patent and Trademark Office for the Licensed Patents, at its own expense, including any retroactive payments that might be required to remedy inaccuracies in the maintenance fees paid prior to the Effective Date for the Licensed Patents. EraGen will pay any maintenance fees that are required for the Licensed Patents within two (2) months of the date on which such fees first become payable, and failure to make these payments within this time period will be treated in the same way as a failure to make other payments under Section 4.2(A) . . . . In the event that EraGen fails to pay the maintenance fees, Benner shall have the right to step in and make such payments (including payments where insufficient maintenance fees have been paid) and shall be promptly reimbursed by EraGen upon receipt of an invoice from Benner. Within fifteen days of the Effective Date, EraGen will reimburse Benner for all patent maintenance costs incurred by Benner for the Licensed Patents on or after January 1, 1999 and prior to the Effective Date, in the total amount of $4,015 or such higher amount as shown in invoices from Benner. Failure to reimburse Benner for such prior or future maintenance payments shall be treated in the same way as failure to make other payments under Section 4.2(A).

It is the second of these obligations, plaintiff's duty to work with the PTO to correct the entity status of the relevant patents, that is the subject of the parties' dispute in this case.

Plaintiff reads § 5.3 as imposing four obligations on it. First, it requires plaintiff to "pay all maintenance fees for issued patents within the Licensed Patents." Second, plaintiff must "take the actions required by the United States Patent and Trademark Office to reflect a change in status from small entity to large entity . . . including any retroactive payments that might be required to remedy inaccuracies in the maintenance fees . . . ." Third, plaintiff is obligated to "pay any maintenance fees that are required for the Licensed Patents within two . . . months of the date on which [the] fees first become payable." Finally, plaintiff must "reimburse Benner for all patent maintenance costs incurred by Benner for the Licensed Patents on or after January 1, 1999" and for any discretionary payments he may make in the future to correct non-payment or untimely payment by plaintiff. As plaintiff sees things, the provision authorizes defendant Benner to terminate the AEGIS agreement if plaintiff does not pay maintenance fees within two months of the date they become due or reimburse defendant Benner for past maintenance payments within 15 days of the AEGIS agreement's effective date or promptly after his invoicing plaintiff for future maintenance payments. According to plaintiff's reading of § 5.3, defendant Benner may not terminate the agreement for failing to take the "actions required by the United States Patent and Trademark Office to reflect a change in status from small entity to large entity" of the relevant patents.

Defendants see things differently. They agree that § 5.3 requires plaintiff to take all of the actions mentioned above, but believe that failure to complete any one of them is ground for termination. The crux of the parties' disagreement lies in the following sentence from § 5.3:

> EraGen will pay any maintenance fees that are required for the Licensed Patents within two (2) months of the date on which such fees first become payable, and failure to make these payments within this time period will be treated in the same way as a failure to make other payments under Section 4.2(A).

Plaintiff contends that this sentence cannot refer to its obligations regarding the entity status of the relevant patents because the fees for those patents "became payable" in the past. Plaintiff asserts that if it failed to meet its obligations with regard to correcting the entity status of the relevant patents, defendant Benner's remedy was not termination. Instead, plaintiff contends, defendant Benner should have invoked his right under § 5.3 of the AEGIS agreement to correct the entity status himself, and then to seek reimbursement of his costs from plaintiff.

Defendants disagree. As they read the provision, plaintiff's obligation to pay the past-due maintenance fees should be measured from the effective date of the AEGIS agreement, meaning that plaintiff had two months from the date the agreement was executed to work with the PTO to correct the entity status of the wrongly-designated patents and to make any retroactive payments due as a result of the error. Defendants point out that § 4.2(A) authorizes defendant Benner to terminate the AEGIS agreement for non-payment of the payments due Benner under "Sections 3.1, 3.2, 3.3 and 3.4, and *5.3.*" (Emphasis added.) That the provision does not distinguish between the obligations imposed on plaintiff by §

5.3, authorizing termination only for some of them, is strong evidence that § 4.2(A) means what it says: non-payment under any portion of § 5.3 is grounds for termination.

Neither side's proposed reading is entirely satisfactory. If, as plaintiff, asserts, not all of the obligations imposed on it by § 5.3 are grounds for termination under § 4.2(A), then it makes no sense for § 4.2(A) not to say just that. Alternately, defendants' reading fails to account for the fact that the patent maintenance fees for the wrongly designated patents "became payable" long before the parties entered the AEGIS agreement. Simply put, neither reading is plausible.

Fortunately, there is no need to resolve the meaning of the entity provisions of § 5.3 It is undisputed that plaintiff made all necessary corrections in March 2006, and that the PTO has accepted all retroactive payments and has updated the entity status of each relevant patent. Therefore, if the AEGIS agreement remains in effect, the entity provision will not need to be used in the future.

Moreover, the question whether plaintiff breached the provision is irrelevant to the outcome of the parties' cross-claims for declaratory judgment. As discussed in section B.2.b., below, even if I were to find that plaintiff breached its obligations under § 5.3 and that the breach could result in termination under § 4.2, defendants failed to provide adequate notice of that breach and therefore may not seek to terminate the agreement on that ground.

2. <u>Adequacy of notice</u>

Having established that plaintiff breached its obligation to pay royalties on money received after February 15, 2005 at a 25% royalty rate for designated sublicenses, and leaving open the possibility that plaintiff may have breached its obligation to correct the entity status of certain patents with the PTO, I turn to the next question, which is whether defendants put plaintiff on notice that its failure to cure each breach within 60 days would result in termination of the AEGIS agreement. I conclude that although defendants provided adequate notice to plaintiff of the breach of § 3.4, they provided no notice at all regarding the putative breach of § 5.3.

a. Breach of § 3.4

Under § 4.2, in order to terminate the AEGIS agreement for non-payment, defendant Benner was required to give plaintiff written notice and an opportunity to cure. Section 9.5 specified that notice was to be sent to plaintiff's chief executive officer and president and to its corporate counsel by certified or overnight mail. Defendant Benner sent plaintiff a letter on September 2, 2005 (one day after the royalty payments and report were due), notifying plaintiff that if it did not correct its underpayment of royalty fees by November 2, 2005, the AEGIS agreement would terminate.

Plaintiff contends that the termination notice was improper for a number of reasons, none of which is convincing. First, plaintiff asserts that defendant should have waited for its untimely royalty report to arrive before sending a notice of termination. However, when a party has failed to fulfill its contractual obligations, an opposing party cannot be required to sit by idly, waiting for some action that may never come before it may act to protect its own interests. In hindsight, it may have been diplomatic for defendant Benner to wait an additional week to receive the royalty report, but there was no way for him to know at the time it would be sent at all. He waited until the fees were due before sending his notice of termination. By doing so, he complied with AEGIS agreement.

Next, plaintiff contends that defendant Benner erred by treating its failure to account for all of the royalties as a "non-payment" under § 4.2. After all, plaintiff asserts, in the great scheme of things, defendant was underpaid by less than $3,500. Plaintiff's check was for more than $100,000. Again, in hindsight all that may be true, but it must be remembered that the royalty check was not accompanied by any documentation that would permit defendant Benner to determine with any real precision how much plaintiff owed him under the AEGIS agreement. Plaintiff's reading of defendants' rights under § 4.2 is overly restrictive, for by plaintiff's logic, it need only have paid defendant Benner a pittance in order to ward off any adverse action. Such a result would defy common sense and the parties' reasonable expectations. (It is, after all, undisputed that the AEGIS agreement was a result of the parties' earlier failed agreement, under which plaintiff routinely submitted incomplete and untimely royalty payments.)

Finally, plaintiff contends that even if defendant Benner believed rightly that plaintiff had failed to pay the royalties due under § 3.4, his remedy was to invoke the audit provisions of § 3.12, not to terminate the agreement under § 3.4. Although the contract authorizes either party to conduct an audit of the other's relevant financial records, it does not require either party to conduct an audit before taking steps to terminate the agreement. Moreover, as defendants are quick to point out, an audit would have done nothing to resolve the parties' dispute about the meaning of "accruing" in § 3.7. It is not the math that is the problem here; it is the theory behind the calculations.

In the September 2, 2005 letter, defendant Benner stated clearly that he was invoking his right to terminate the agreement under § 4.2 as a result of plaintiff's failure to pay royalties. Over the following two months, the parties exchanged emails and letters, but were unable to reach a mutual agreement regarding the proper interpretation of § 3.7. On October 24, 2004, defendant Benner sent plaintiff a letter in which he stated unequivocally that, "Under Article 4.2 of the Agreement, failure to make [royalty] payments is sufficient grounds for termination. Therefore, the Notice of Termination, dated September 2, 2005, stands."

Plaintiff sent a follow-up letter on October 31, 2005, two days before expiration of the "cure period," reiterating its interpretation of § 3.7 (which defendant Benner had rejected numerous times previously) and requesting that defendant Benner's lawyer contact plaintiff if defendant Benner continued to disagree with plaintiff's interpretation of the agreement. Plaintiff makes much of the fact that defendant Benner did not respond to this letter, but his failure to do so is irrelevant to the question whether plaintiff was given adequate notice of defendant Benner's intent to terminate the agreement on November 2, 2005 unless plaintiff paid the additional royalties. There can be no question that plaintiff received adequate notice of defendant Benner's intent.

b. Breach of § 5.3

When it comes to plaintiff's breach of its obligations under § 5.3, defendants propose two theories of notice. First, defendants contend that the AEGIS agreement itself put plaintiff on notice that its failure to make appropriate retroactive payments within 60 days of the agreement's effective date would result in termination of the agreement, an argument so contrary to the terms of the agreement itself that it borders on the absurd. I have found already that under § 5.3, plaintiff had 60 days to work with the PTO to correct the entity status of the relevant patents. After that time, under the terms of § 4.2, plaintiff would have been entitled to notice and 60 days to cure its breach before defendant Benner would have a right to terminate.

Defendants' second argument is that defendant Benner's October 24, 2005 letter provided notice to plaintiff that Benner intended to terminate the agreement not only for plaintiff's failure to pay royalties under § 3.4, but also for failure to pay maintenance fees under § 5.3. That, too, is a meritless contention. Although defendant Benner's letter contained a brief citation to § 5.3, it made no mention at all of maintenance fees or of plaintiff's failure to contact the PTO to correct the entity status of the relevant patents. Nor is there any reason to think he meant to do so. The first mention defendants made of their intent to terminate the AEGIS agreement because of plaintiff's failure to correct the entity status of the relevant patents came in a letter dated May 31, 2006— several weeks after defendants had filed suit in the Northern District of Florida, and long after plaintiff had, at defendants' request, fulfilled its obligations to update the entity status and make all retroactive payments due, as required under § 5.3.

Defendants did not provide plaintiff with proper notice of their intent to terminate the agreement as a result of plaintiff's failure to meet its obligations under § 5.3 with respect to updating the PTO entity status of several patents. Because defendants did not provide the required notice of plaintiff's breach of § 5.3 of the AEGIS agreement, they may not seek to invalidate the agreement on that ground.

3. <u>Validity of the AEGIS agreement</u>

On September 1, 2005, plaintiff breached its obligations under § 3.4 by underpaying defendant Benner the amount of royalties he was due. Defendant Benner provided plaintiff with adequate notice of his intent to terminate the agreement because if this breach, and plaintiff did not cure its error by remitting the overdue payment within 60 days of receiving notice. Therefore, only one question remains with respect to the cross-motions for declaratory judgment: After having properly notified plaintiff of its breach under § 3.4, did defendants' subsequent actions waive their right to terminate the agreement effective November 2, 2005?

Neither side has clearly set forth the Florida law governing waiver of a contractual breach. Defendants cite mainly to cases regarding unconscionability, but unconscionability is relevant only when a party alleges that a contract term in unenforceable. No one contends that the termination provisions of § 4.2 are not enforceable; the question is whether defendants waived their right to enforce the otherwise-enforceable provisions of § 4.2 by their post-November 2, 2005 conduct. Waiver is a different doctrine:

> Generally, one may waive a breach of contract by the other party by words or conduct. Statements or conduct indicating that the other party's performance is not required, or a willingness to continue honoring the contract, despite knowledge that the other party has failed to perform, may constitute a waiver. The continued recognition of the contract as binding after the other party's alleged breach acts as a waiver of that breach. Thus, anything that induces the other party to perform an agreement after a default, or which shows that the agreement subsists after a default, amounts to a waiver . . . The acceptance of a benefit under a contract with knowledge of a breach ordinarily constitutes a waiver.

17A Am. Jur. 2d Contracts § 714; see also 23 Samuel Williston & Richard A. Lord, A Treatise on the Law of Contracts § 63:9 (4th ed. 1993) ("[T]he general rule is that where a contracting party, with knowledge of a breach by the other party, receives and accepts payment or other performance of the contract, he or she will be held to have waived the breach.").

Florida courts define waiver as "the voluntary and intentional relinquishment of a known right or conduct which implies the voluntary and intentional relinquishment of a known right." Raymond James Financial Services, Inc. v. Saldukas, 896 So. 2d 707, 711 (Fla. 2005). Defendants contend that they did not "voluntarily and intentionally" relinquish their right to terminate the agreement on November 2, 2005, and that their conduct did not imply such a relinquishment. Although the relevant interactions between the parties are detailed above, a timeline may help to place those interactions in context with respect to plaintiff's breach of § 3.4 of AEGIS agreement:

- ♦ 9/1/05 Defendant Benner receives and cashes check from plaintiff for $139,093 for royalties due under several agreements (including the AEGIS agreement); no royalty reports filed.
- ♦ 9/2/05 Defendant Benner sends plaintiff Notice of Termination demanding total payment of $224,887.00 in royalties.
- ♦ 9/7/05 Plaintiff sends royalty reports; asserts overpayment of $41,883.
- ♦ 10/24/05 Defendants send plaintiff letter regarding royalties, citing § 5.3 as one of many several grounds for termination and reiterating Notice sent on 9/2/05.
- ♦ 10/31/05 Plaintiff sends letter reiterating its position with respect to § 3.7, asking defendants'

lawyer to provide additional information if defendants insist that the agreement will be terminated; defendants do not respond.

- ♦ 2/21/06 Defendants' lawyer sends letter asserting again that plaintiff underpaid the 9/05 royalties by misinterpreting § 3.7. No mention is made of termination.
- ♦ 3/1/06 Defendants receive and cash plaintiff's royalty payment for the period 7/05-12/05.
- ♦ 3/7/06 Plaintiff responds to the 2/21 letter reiterating its position with respect to the interpretation of § 3.7.
- ♦ 3/27/06 Defendants' lawyer write to plaintiff continuing to dispute the proper interpretation of § 3.7, but stating that he thinks the matter can be resolved if plaintiff submits financial documents.
- ♦ 4/6/06 Plaintiff submits the requested financial documents.
- ♦ 5/18/06 Defendant Nucleic Acids Licensing files suit in United States District Court for the Northern District of Florida seeking declaratory judgment that the agreement is invalid.
- ♦ 6/5/06 Plaintiff files suit in this court seeking declaratory judgment that the agreement is valid.
- ♦ 9/1/06 Defendants receive and cash plaintiff's royalty payment for the period 1/06-6/06.

Because November 2, 2005 is the date on which the AEGIS agreement purportedly terminated, the relevant events with respect to plaintiff's waiver argument are those that occur after that date. No activity of any importance occurred between November 2005 and late February 2006 and nothing may be inferred from defendants' inaction during this period. It is the events that occur between February and May that provide strong evidence of waiver. Beginning February 21, 2006, defendants' lawyer reopened the discussion of royalties due under § 3.4. Although defendants continued to assert that their reading was the right one, they made no mention of termination. More important is the fact that when plaintiff submitted its royalty report and payment on March 1, 2006, defendants accepted and cashed the payment, with no mention of termination. Defendants contends now that by cashing the payment they were merely trying to recoup some of their lost profits under the AEGIS agreement, which rightfully belonged to them beginning on November 2, 2005. Even if that is so, by failing to inform plaintiff what they were doing, defendants purposefully misled plaintiff into believing that the royalty payment was being accepted for what it was, and that any earlier breach had been excused.

Throughout the month of March, defendants continued to engage in conduct that suggested the AEGIS agreement remained in force. Defendants' lawyer wrote plaintiff a letter that stated in relevant part, "Frankly, we find your analysis of the term "accruing" in Section 3.7 with respect to the term "received" in Section 3.4 to be inconsistent. However, we also believe that this matter can be resolved if EraGen will provide us with a copy of the Bayer Agreement and copies of the relevant royalty reports from Bayer to EraGen." In response, plaintiff submitted financial papers, reasonably believing that doing so would foster conciliation. Several weeks later, defendants filed suit, contending as they do here, that the agreement was terminated as a result of plaintiff's breach under § 3.4 on November 2, 2005.

"Where a party fails to declare a breach of contract, and continues to perform under the contract after learning of the breach, it may be deemed to have acquiesced in an alteration of the terms of the contract, thereby barring its enforcement." Acosta v. District Board of Trustees of Miami-Dade Community College, 905 So. 2d 226, 229 (Fla. Dist. Ct. App. 2005). That is exactly what defendants did in this case. After invoking their rights under § 4.2, they proceeded to interact with plaintiff in ways that would reasonably have led plaintiff to only one conclusion: the AEGIS agreement remained in force and the parties were ironing out their disagreements to their mutual satisfaction. Because defendants have waived their right to terminate the agreement based upon the notice defendant Benner sent to plaintiff September 2, 2005, plaintiff's motion for declaratory judgment will be granted; defendant's cross-motion will be denied.

I note that defendants' waiver of plaintiff's past breach does not obligate it to tolerate future breaches. Should plaintiff fail to comply with its obligations under §§ 3.1, 3.2, 3.3 3.4, or 5.3, defendants retain the right to provide plaintiff with written notice of their intent to terminate. If, after 60 days, plaintiff fails to cure the breach and defendant takes no action to suggest that it has waived its right to terminate, under § 4.2 "all of the rights in the Licensed Patents and Licensed Know How will revert to Benner, subject only to Benner's obligations to sublicensees as provided in Section 2.3" of the AEGIS agreement.

C. Breach of the Implied Duty of Good Faith and Fair Dealing

Aside from the question whether plaintiff breached the written terms of the agreement, each side contends that the other breached its duty of good faith and fair dealing by purposefully misinterpreting the "true meaning" of the agreement and by acting in bad faith in myriad ways. Although the parties' briefs are laden with allegations of wrongdoing, they are light on law. The parties appear to believe that any wrongdoing or even mistake by the opposing party is grounds for a claim of breach of the duty of good faith. That is simply not true.

Although the parties have pleaded their claims and counterclaims for breach of the duty of good faith and fair dealing as separate counts, "no independent cause of action exists under Florida law for breach of the implied covenant of good faith and fair dealing." Burger King Corp. v. Weaver, 169 F.3d 1310, 1317-18 (11th Cir. 1999). Rather, "a party's good-faith cooperation is an implied condition precedent to performance of a contract; where that cooperation is unreasonably withheld, the recalcitrant party is estopped from availing himself of his own wrong doing." Id. at 1315 (citing Bowers v. Medina, 418 So. 2d 1068, 1069 (Fla. Dist. Ct. App.1982).

The purpose of the implied covenant is to protect the reasonable expectations of the contracting parties; however, its reach is restricted in several respects:

> First, the implied covenant is not an independent term within the parties' contract. Thus, it cannot override an express contractual provision. Because the implied covenant is not a stated contractual term, to operate it attaches to the performance of a specific or express contractual provision. There can be no cause of action for a breach of the implied covenant absent an allegation that

> an express term of the contract has been breached . . . . Thus, the duty of good faith performance does not exist until a plaintiff can establish a term of the contract the other party was obligated to perform and did not.

Snow v. Ruden, McClosky, Smith, Schuster & Russell, P.A., 896 So. 2d 787, 791-92 (Fla. Dist. Ct. App. 2005). In short, "the 'covenant' is not an independent contract term. It is a doctrine that modifies the meaning of all explicit terms in a contract, preventing a breach of those explicit terms de facto when performance is maintained de jure." Burger King Corp., 169 F.3d at 1316-17. Put another way, the covenant "is a gap-filling default rule . . . usually raised when a question is not resolved by the terms of the contract or when one party has the power to make a discretionary decision without defined standards. Publix Super Markets, Inc. v. Wilder Corp. of Delaware, 876 So. 2d 652, 654-55 (Fla. Dist. Ct. App. 2004); Sepe v. City of Safety Harbor, 761 So. 2d 1182, 1185 (Fla. Dist. Ct. App. 2000) ("where contract afforded party 'substantial discretion to promote that party's self-interest,' [the] duty of good faith . . . applied").

1. Plaintiff's claim for breach of the implied duty of good faith and fair dealing

In the amended complaint, plaintiff asserted that defendants had breached their implied duty of good faith and fair dealing with respect to the AEGIS agreement by

> Benner's decision to send out the September 2, 2005 termination notice without any factual basis for doing so, Benner's failure to provide EraGen with adequate written notice of the basis for the September 2, 2005

> termination notice, Benner's and NAL's contention that the September 2, 2005 termination notice was based on EraGen's failure to timely provide a royalty report . . . , Benner's and NAL's failure to provide any written termination notice with respect to the alleged violation of Section 5.3 (relating to the payment of patent maintenance fees), Benner's and NAL's attempt to mischaracterize the October 24, 2005 letter as a termination notice, Benner's and NAL's failure to employ the procedures set out in the 2005 Agreement . . . to clarify whether the royalty payments were accurate, before seeking termination of the 2005 Agreement, and Benner's and NAL's assertion of additional alleged grounds for termination of the 2005 Agreement in Benner's March 4, 2006 letter.

Dkt. #15, ¶42.

Having concluded that defendant Benner was well within his rights to send plaintiff a notice of termination on September 2, 2005, I find that plaintiff's claims relating to defendant Benner's September 2 letter fail from the start. Similarly, having concluded that defendants were under no obligation to employ the audit procedures set forth in § 3.12, I find that plaintiff's claim regarding defendants' failure to invoke those procedures fails as well.

Plaintiff's claim that defendants mischaracterized their October 24, 2005 letter as providing notice of termination under § 5.3 fails to implicate a breach of any contractual provision. Although the claim relates tangentially to § 4.2 of the AEGIS agreement, that section authorizes defendants to sent notice of breaches under § 5.3; it does not forbid them from doing so, even when their alleged notices are deficient.

Finally, plaintiff has not developed its claim that defendants "assert[ed] additional alleged grounds for termination of the 2005 Agreement in Benner's March 4, 2006 letter" sufficiently to permit the court to assess it in any meaningful way. Because plaintiff has failed to adduce evidence in support of its claim that defendants breached their duty of good faith and fair dealing, plaintiff's motion for summary judgment will be denied with respect to these claims; defendants' cross-motion with respect to these claims will be granted.

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2. Defendant Nucleic Acids Licensing's counterclaim for breach of the implied duty of good faith and fair dealing

In its counterclaim, defendant Nucleic Acids Licensing contended that plaintiff had breached its duty of good faith and fair dealing, stating that plaintiff

> engaged in a series of conduct resulting in breaches of the 2005 License, a pattern consistent with its conduct throughout the contractual relationship of the parties in both the 2005 License, the 1999 License and various other predecessor agreements involving the licensing of the Benner patents. EraGen's conduct relative to the 2005 License, including but not limited to, breaches of its semi-annual royalty accounting obligations, the failure to keep NAL reasonably apprised of the prosecution and maintenance of the licensed patents, including the payment of patent maintenance fees, the renegotiation by EraGen of a sublicense agreement to deprive the licensor of the receipt of additional promised royalty income and EraGen's consistent, historical pattern of requiring NAL to issue breach notices in order to receive royalty accounting information that NAL is entitled to under the agreement and then only after the near expiration of a cure period, all violate the 2005 License and the implied covenant of good faith and fair dealing.

Dkt. #16, ¶ 27.

To the extent that defendant Nucleic Acids Licensing is contending that plaintiff breached its duty of good faith and fair dealing in connection with agreements other than the AEGIS agreement, its claim fails for two reasons. First, the counterclaim for breach of the duty of good faith and fair dealing relates to actions plaintiff allegedly took with respect to the Expanded Genetic Alphabet License Agreement, an agreement not before this court and to which defendant Nucleic Acids Licensing was not party. Second, under the terms of the AEGIS agreement, defendant Benner (and, by virtue of assignment, defendant Nucleic Acids Licensing) waived his ability to bring an action regarding "any and all failures by the other party to comply with any and all provisions of the Expanded Genetic Alphabet Agreement which occurred prior to the execution" of the AEGIS agreement. AEGIS Agreement, dkt. #48, exh. 5, § 9.2. Defendant Nucleic Acids Licensing's claims that plaintiff violated its duty of good faith and fair dealing by engaging in a "pattern consistent with [plaintiff's] conduct throughout the contractual relationship of the parties" and a "historical pattern of requiring NAL to issue breach notices in order to receive royalty accounting information" are nothing more than an attempt to do what defendant Benner bargained not to do: sue for past breaches of the Expanded Genetic Alphabet Agreement. Consequently, plaintiff's motion for summary judgment on these claims will be granted; defendants' cross-motion will be denied.

In defendants' consolidated summary judgment brief, they contend that plaintiff breached its duty of good faith and fair dealing additionally by underpaying its September 2005 royalties; "fail[ing] to keep NAL reasonably apprised of the prosecution and maintenance of the licensed patents," and renegotiating a sublicense agreement "to deprive [defendant Benner] of the receipt of additional promised royalty income." Summary judgment is proper with respect to each of these claims. First, there is no evidence that plaintiff's failure to pay defendant Benner was evidence of bad faith. As discussed at length above, the meaning of § 3.7 was far from clear, and plaintiff's understanding of the provision, although incorrect, was not unreasonable. Second, defendants have adduced no evidence in support of their contention that plaintiff failed to keep them apprised of the prosecution and maintenance of any patents. Finally, to the extent that defendants complain that plaintiff failed to tell them about a sublicense plaintiff was in the process of renegotiating, defendants fail to connect plaintiff's alleged bad faith to a breach of any provision of the AEGIS contract. Consequently, plaintiff's motion for summary judgment on this claim will be granted; defendants' cross-motion will be denied.

D. Quasi-Contractual Claims for Repayment

Although plaintiff and defendant Nucleic Acids Licensing have pleaded "money had and received" and unjust enrichment as separate claims, Florida law treats both causes of action identically. Hall v. Humana Hospital Daytona Beach, 686 So. 2d 653, 656 (Fla. Dist.

Ct. App. 1996); Moore Handley, Inc. v. Major Realty Corp., 340 So. 2d 1238 (Fla. Dist. Ct. App. 1976). The theory behind both is this:

> Under a principle of ancient and honorable lineage, an improper taking of goods or money which actually belongs to another and which may in itself constitute a tort, also gives rise to an implied contractual obligation to return that property. As Prosser says:
>
> > [T]here has developed the doctrine that where the commission of a tort results in the unjust enrichment of the defendant at the plaintiff's expense the plaintiff may disregard, or "waive" the tort action, and sue instead on a theoretical and fictitious contract of restitution of the benefits which the defendant has so received.
> >
> > * * *
> >
> > Thus where the defendant has appropriated the plaintiff's money, or has taken his property and sold it, a quasi-contract count will lie for money had and received to the plaintiff's use, through the fiction of an implied promise to repay.

Barbouti v. Lysandrou, 559 So. 2d 648, 650 (Fla. Dist. Ct. App. 1990) (quoting W. Prosser & W. Keeton, The Law of Torts § 94, at 672-73); see also Marshall-Shaw v. Ford, 755 So. 2d 162, 165 (Fla. Dist. Ct. App. 2000). An "action for money had and received, or the more modern action for unjust enrichment, is an equitable remedy requiring proof that money had been paid due to fraud, misrepresentation, imposition, duress, undue influence, mistake, or as a result of some other grounds appropriate for intervention by a court of equity." Hall, 686 So.2d at 656.

Defendants' claim for unjust enrichment and money had and received was grounded in its contention that plaintiff had "received and retained substantial sums of money from sublicenses" and other sources *after the AEGIS agreement terminated*. Dkt. #16, at 7. Because I have found already that the AEGIS agreement remains in force, the money plaintiff collected under the agreement was collected legitimately; therefore, plaintiff's motion for summary judgment will be granted with respect to defendant Nucleic Acids Licensing's claims of unjust enrichment and money had and received.

Plaintiff's claim for unjust enrichment and "money had and received" stems from its alleged overpayment of $49,383 beyond the amount it was required to pay in royalties on income it earned from the Bayer sublicense. Having established above that defendants' interpretation of § 3.7 was the right one, it appears undisputed that plaintiff did not overpay defendants and is therefore owed no refund. Consequently, defendants' motion for summary judgment will be granted with respect to plaintiff's claims for unjust enrichment and money had and received.

ORDER

IT IS ORDERED that

1. The motion for summary judgment of plaintiff Eragen Biosciences, Inc. is

    a) GRANTED with respect to

        i. its request for a declaration that the AEGIS agreement is valid;

ii. defendant Nucleic Acids Licensing's claim for money had and received;

iii. defendant Nucleic Acids Licensing's claim for unjust enrichment; and

iv. defendant Nucleic Acids Licensing's claim that plaintiff breached its duty of good faith and fair dealing under the AEGIS agreement.

b) DENIED with respect to

i. its claim that defendants breached their duty of good faith and fair dealing under the AEGIS agreement; and

ii. its claims for money had and received and unjust enrichment.

2. The motion for summary judgment of defendants Steven Benner and Nucleic Acids Licensing, LLC is

a) GRANTED with respect to

i. plaintiff's claims for money had and received and unjust enrichment; and

ii. plaintiff's claim that defendants breached their duty of good faith and fair dealing under the AEGIS agreement.

b) DENIED with respect to

i. its claim for a declaration that the AEGIS agreement is invalid;

ii. its claim that plaintiff breached its duty of good faith and fair dealing under the AEGIS agreement; and

iii. its claims for unjust enrichment and money had and received.

Entered this 26th day of February, 2007.

BY THE COURT:
/s/
BARBARA B. CRABB
District Judge