STATE OF NEW YORK
SUPREME COURT COUNTY OF MONROE

WILLIAM H. THOMPSON and
WALTER TOOMBS,

Plaintiff,

DECISION AND ORDER

v.

Index #2007/07194

MICHAEL P. McQUEENY,
MICHAEL SERVENTI,
DOUGLAS M. VANOORT, JENNIFER
CHALMERS BALBACH, 331 HOLDING, INC.,
SUMMER STREET CAPITAL FUND I, LP,
SUMMER STREET CAPITAL NYS FUND, LP,
RAND CAPITAL SBIC, LP, RAND CAPITAL
CORPORATION and ONONDAGA VENTURE
CAPITAL FUND, INC.,

Defendant.

Defendants, Michael P. McQueeney, Michael Serventi, Douglas M. Vanoort, Jennifer Chalmers Balbach, 331 Holding, Inc., Summer Street Capital NYS Fund, LP, Rand Capital SBIC, LP, Rand Capital Corporation and Onondaga Venture Capital Fund, Inc., move by order to show cause for the following relief: (1) pursuant to CPLR 5519(a)(4), an order designating an officer of the court to take custody of US Patent Nos. 7,027,431 and 6,108,331 to abide the direction of the Appellate Division, Fourth Department upon defendants' appeal of the court's November 6, 2006 order; or, in the alternative, (2) pursuant to CPLR 5519(c), a stay of the proceedings to enforce the November 6, 2007 order pending the appeal. The order to show cause did not contain a temporary

restraining order.

Plaintiffs, William H. Thompson and Walter F. Toombs, filed a cross motion requesting either a denial of defendants' motion for a stay or, in the alternative, requiring defendants to promptly perfect their appeal and requiring defendants to post a bond or undertaking with adequate sureties in an amount not less than $10,000,000, to allow for recovery of damages which plaintiffs may sustain by reason of the stay granted in the event the court's November 6, 2007 decision and order is affirmed.

Plaintiffs commenced this action on June 8, 2007. After issue was joined, plaintiffs moved for partial summary judgment on the first, second, and fifth causes of action specifically enforcing the terms of the Letter Agreement, i.e., to cause the formation of a 331 Holding, Inc. subsidiary, to elect plaintiffs as the sole directors and officers of that company, to place ownership of the subject patents in that company, to distribute the new company's equity out to its shareholders (to defendants' exclusion), and to enjoin and restrain defendants from selling or otherwise transferring ownership of the '331 patent to anyone other than the new company. Defendants opposed plaintiffs' motion and also cross moved for an order permitting them to amend their answer and counterclaims to assert affirmative defenses and counterclaims for rescission and reformation of the Letter Agreement based upon allegations of mutual mistake.

By Decision and Order dated November 6, 2007, the court granted plaintiffs' motion for partial summary judgment and denied defendants' cross motion. It was ordered that defendant 331 Holding, Inc. must consummate the transactions contemplated by the Letter Agreement. The court further granted plaintiffs a permanent injunction retraining and enjoining defendants from selling, transferring, or otherwise disposing of the '331 Patent in violation of the terms of the Letter Agreement. Defendants' cross motion was also denied.

Thereafter, defendants appealed the court's ruling and presently seek an order designating an officer of the court to take custody of the patents to perfect defendants' claimed right to an automatic stay pursuant to CPLR 5519(a)(4). In the alternative, defendants seek a stay pursuant to CPLR 5519(c).

The relevant CPLR provisions at issue herein state:

> (a) **Stay without court order.** Service upon the adverse party of a notice of appeal or an affidavit of intention to move for permission to appeal stays all proceedings to enforce the judgment or order appealed from pending the appeal or determination on the motion for permission to appeal where: . . .
>
> 4. the judgment or order directs the assignment or delivery of personal property, and the property is placed in the custody of an officer designated by the court of original instance to abide the direction of the court to which the appeal is taken, or an undertaking in a sum fixed by the court of original instance is given that the appellant or moving party will obey the direction of the court to which the appeal is taken. . .

> (c) **Stay and limitation of stay by court order.** The court from or to which an appeal is taken or the court of original instance may stay all proceedings to enforce the judgment or order appealed from pending an appeal or determination on a motion for permission to appeal in a case not provided for in subdivision (a) or subdivision (b), or may grant a limited stay or may vacate, limit or modify any stay imposed by subdivision (a), subdivision (b) or this subdivision, except that only the court to which an appeal is taken may vacate, limit or modify a stay imposed by paragraph one of subdivision (a).

CPLR 5519(a)(4) is designed to prevent "an appellant from suffering an irreparable loss as a result of the appellant's having delivered personal property to the plaintiff as directed by the order of the trial court and then being unable to recover that property from the plaintiff if the trial court's determination is reversed on appeal." Wynyard v. Beiny, 4 Misc.3d 904, 907 (Surr. Ct. Bronx Co. 2004). The statutory scheme of CPLR 5519 provides, however, that even if a court finds that CPLR 5519(a)(4) applies, as argued by defendants herein, the court may exercise its discretion to limit or vacate the automatic stay pursuant to CPLR 5519(c). It is a matter of discretion for the court to determine whether to modify, limit, or vacate a stay under CPLR 5519(a). See Wechsler v. Wechsler, 8 Misc.3d 328, 329 (Sup. Ct. N.Y. Co. 2005).

The court agrees with defendants that the court's order, requiring the transfer of the patents to plaintiffs, falls within the ambit of CPLR 5519(a)(4) covering personal property. See 35

U.S.C. §261; COR Marketing & Sales v. Greyhawk Corp., 994 F.Supp. 437, 443 (W.D.N.Y. 1998); N.Y. Gen. Constr. Law §39. See also, In re Bronson, 150 N.Y. 1, 16 (1896). Defendants are entitled to an automatic stay of that part of the decision and order directing a transfer of the patents pursuant to CPLR 5519(a)(4).

The court must turn its attention to whether the circumstances warrant an exercise of discretion limiting, modifying, or vacating the stay imposed by virtue of CPLR 5519(a)(4), under CPLR 5519(c). Plaintiffs contend that the effect of the stay is that they are denied possession and use of the patents for the duration of an appeal. Plaintiffs contend that there is a danger that they would both incur lost revenue (which plaintiffs estimate at over $10,000,000) and associated profits. Plaintiffs further allege that the delay would prevent NewCo from starting up its manufacturing business and could render the technology of the patents, invented by plaintiff Thompson, obsolete as new technologies are constantly entering the marketplace. Plaintiffs caution that the "quickly moving 'window of opportunity'" in the technology industry will likely not be there if there is a delay. See Plaintiff's Memorandum of Law, 6.

Consideration of whether to vacate or modify an automatic stay, and whether conditions should be imposed on a stay of other aspects of the court's decision and order, invokes a multifactor

discretionary analysis of "any relevant factor[s], including the presumptive merits of the appeal and any emergency or hardship confronting any party." CPLR 5519, Practice Commentary C5519:4, Book 7B McKinneys Cons. Law of N.Y., at 227 (1995). See Da Silva v. Musso, 76 N.Y.2d 436, 443 n.4 (1990)("court considering the stay application may consider the merits of the appeal").

Defendants' demonstration of a meritorious appeal hinges on their interpretation of the literal language of the Letter Agreement as requiring an immediate separation of ownership as between the two patents by virtue of the provision that NewCo be immediately formed, capitalized, and receive an assignment of ownership in the '431 Patent. The reading of the literal language is, defendants contend, compelled by that aspect of the Letter Agreement which required a transfer of the '331 Patent to NewCo, if at all, only by December 31, 2007. Defendants contend that immediate transfer of the '431 Patent to NewCo in February 2007, when the LaGrand closing occurred, would have rendered the '431 Patent worthless by virtue of the Terminal Disclaimer because 331 Holding (USTEC's successor) would retain ownership of the '331 Patent until it could effect a sale thereof without impairing the '431 Patent (an impossibility under the Terminal Disclaimer) or until December 31, 2007. "Therefore, defendants respectfully submit that because the Letter Agreement by its explicit terms calls for the immediate separation of the Patents

- - thereby rendering the '431 unenforceable - - it cannot be construed literally, and resort must be had to extrinsic evidence," thereby rendering summary judgment inappropriate. Defendants Memorandum of Law (12-06-07), at 7.

That reading of the Letter Agreement is not plausible, however, because a separation of ownership of the two patents in February as between '331 Holding and NewCo, given the conditions attached to defendants' ('331 Holding's) retention of the '331 Patent, i.e., that no sale could occur which would impair the '431, and a conveyance of the '331 by the end of the year which would restore common ownership in NewCo, would not render the '431 unenforceable for all time. Under the former regulations, defendants' argument might have more merit, but the 1971 amendments to 37 C.F.R. §1.321, eff. April 30, 1971, "changed this requirement [i.e., expiration of patent immediately if the two patents ceased to be commonly owned] to provide that disclaimers need state only that the patent be unenforceable during the period it is not commonly owned with the other patents recited in the disclaimers." Merck & Co., Inc. v. U.S. Inter. Trade Comm., 774 F.2d 483, 486 (Fed. Cir. 1985). See 31 C.F.R. §1.321(c)(3)("shall be enforceable only for and during such period that said patent is commonly owned")(emphasis supplied). Accordingly, by the terms of the Letter Agreement, separate ownership would last only until December 31, 2007, or such sooner

time as defendants found that they could not effect a sale without encumbering the '431 (see, below), and NewCo would have fully enforceable patents in both the '331 and '431 as of the first of the year or that sooner time.[1]

Plaintiff raises the issue, in a post-argument letter

---

[1] Some background of the terminal disclaimer process, not contained in the court's Decision and Order, is in order:

> The patent statute by 35 U.S.C. § 101 (1988) precludes a patentee from obtaining more than one patent on the same invention. In re Longi, 759 F.2d 887, 892, 225 USPQ 645, 648 (Fed.Cir. 1985). By interpretation, this prohibition has been extended to preclude a second patent on an invention which "would have been obvious from the subject matter of the claims in the first patent, in light of the prior art." Id. at 893, 225 USPQ at 648. A second issued patent may not improperly extend the term of protection for an earlier patented invention. In re Braat, 937 F.2d 589, 592, 19 USPQ2d 1289, 1291-92 (Fed.Cir. 1991). These concepts are encompassed within the rubric of "double patenting." See In re Braithwaite, 379 F.2d 594, 601, 54 CCPA 1589, 154 USPQ 29, 34 (1967). . . . Unlike "same-invention" double patenting, obviousness-type double patenting can be overcome by filing a terminal disclaimer. As stated in section 1490 of the Manual of Patent Examining Procedure:
>
>> A disclaimer is a statement filed by an owner ... of a patent or of a patent to be granted, in which said owner relinquishes certain legal rights to the patent.... [A] terminal disclaimer under 37 CFR 1.321(a) and (b) [is] used to disclaim or dedicate a portion or the entire term of all of the claims of a patent.
>
> By disclaiming that portion of the second patent which would extend beyond the expiration of the first, the patentee gives up any extension of patent protection that might have resulted. Braithwaite, 379 F.2d at 601, 154 USPQ at 35.

Ortho Pharmaceutical Corp. v. Smith, 959 F.2d 936 (Fed. Cir. 1992). See also, Agrizap, Inc. v. Woodstream Corp., 431 F.Supp.2d 518, 536-37 (E.D.Pa. 2006).

submission, made upon agreement of the parties, that there is an unsettled question whether, once a separation of ownership occurs of patents subject to a terminal disclaimer, rights of third party users of the inventions during the time of ownership separation will acquire a priority of right to continue the claimed invention even after subsequent restoration of common ownership. The parties appear to acknowledge that the federal courts have not settled this question. But defendants, who have not advanced this point, have not raised an issue of fact that an entering of the public domain could occur unless a separate sale of the '331 was achieved, a transaction now known to be prohibited by the Letter Agreement. Nor has it been shown the doctrine of intervening rights applicable in the context of a recapture of patent rights by virtue of a reissue which broadens the originally lapsed patent right, 35 U.S.C. §252; Seattle Box Co., Inc. v. Industrial Crating and Packing, Inc. 756 F.2d 1574, 1579 (Fed. Cir. 1985), is at all applicable to the restoration of common ownership of patents subject to a terminal disclaimer.

The recapture rule "prevents an applicant from recapturing through reissue [subject] matter surrendered to overcome a rejection based on prior art." In re Doyle, 293 F.3d 1355, 1358 (Fed.Cir. 2002). Pannu v. Storz Instruments, Inc., 258 F.3d 1366, 1370-71 (Fed.Cir. 2001)("Reissued claims that are broader than the original patent's claims in a manner directly pertinent

to the subject matter surrendered during prosecution are impermissible."). In the case of restoration of common ownership of patents subject to a terminable disclaimer, there is no broadening of the original patent right allowed by the terminal disclaimer which would require the intervention of equity to protect putative intervening infringers claiming to practice what was left in the public domain, and no evidence of Congress' intention to similarly treat the two situations has been provided to this court. Cf., In re Doyle, 293 F.3d 1355, 1363 (fed Cir. 2002)("Congress has weighed the benefits and burdens of allowing corrections of this sort of error by reissue, and has decided to allow broadening reissues, subject, of course, to certain safeguards: the two-year time limitation and intervening rights.")

Contrary to defendants' argument, the enforceability of the '431 would not be impaired by an immediate assignment to NewCo when the LaGrand transaction closed if the parties employed the simple expedient of not recording the NewCo assignment until the unsettled question of a separate sale of the '331 was resolved. See 35 U.S.C. § 261 ("An assignment, grant or conveyance shall be void as against any subsequent purchaser or mortgagee for a valuable consideration, without notice, unless it is recorded in the Patent and Trademark Office within three months from its date or prior to the date of such subsequent purchase or mortgage.");

Heywood-Wakefield Co. v. Small, 96 F.2d 496, 499, 37 USPQ 363 (1st Cir. 1938) (unless an assignment is recorded with the PTO, title to the patent does not vest in the assignee); see also Group One, Ltd. v. Hallmark Cards, Inc., 407 F.3d 1297, 1307, 74 USPQ2d 1759 (Fed. Cir. 2005) (in the absence of a recorded assignment, inventor remains "owner of record," capable of taking actions to prosecute and maintain patent). In other words, without recording the assignment to NewCo before the parties ascertained the viability of the contingency Thompson demanded be included in the last sentence of ¶4(a), an immediate assignment to Newco as called for under the Letter Agreement could be made without impairing the enforceability of the patent.

In short, defendants, in only one aspect of a multifaceted transaction, and while both sides were uncertain about separate marketability of the '331, bargained for an uncertain right to sell the '331, failed to investigate the viability of their bargained for right to sell before concluding the transaction, Decision and Order, at 18-19, and now cannot be heard to complain that only a portion of the entire transaction be undone because they belatedly realized the effect of the Terminal Disclaimer.

The court's conclusions are only fortified by the fact that the December 31, 2007, deadline was only that, a deadline. Once it became clear to defendants that they could not market the '331 Patent under any circumstances without impairing the '431 Patent,

I would think they thereupon had a duty under the Letter Agreement, of good faith and fair dealing, to immediately convey the '331 Patent to NewCo and not delay its conveyance until the arrival of the deadline. Indeed, plaintiffs asked just for that result in their notice of motion, albeit not referencing defendants' duty of good faith and fair dealing, which would be the only source of a duty to convey the '331 Patent sooner than the deadline set forth in the Letter Agreement. Accordingly, the court's reference to the "fullness of time" in contemplation of the end of year deadline perhaps unnecessarily gave slavish deference to the deadline set forth in the Letter Agreement. But that reference cannot support this new claim of ambiguity, drawn from the Letter Agreement's call for immediate assignment of the '431, which was first raised in connection with defendants' current motion for an order giving effect to the automatic stay.

On the original motion, defendants focused on the "terminal disclaimer [as] creat[ing] an internal inconsistency in the Letter Agreement that can be reconciled only by way of reformation or rescission," Brydges Affirmation (10-29-07), at ¶6, and that this inconsistency related, not to the problem created by an immediate assignment of the '431 to NewCo as now claimed by defendants, but to the effect the disclaimer had on defendants' claimed inviolate right, but which in reality (as I found) manifestly was only an uncertain right (by the terms of

the Letter Agreement), to separately sell the '331. Id.

In fact, defendants' patent counsel took a position on the original motion, not ultimately embraced by defendants themselves except for the first time on this motion, that '331 Holding could, without NewCo's acceptance or cooperation, transfer the '431 Patent to NewCo "in full compliance with the literal terms of the Letter Agreement" and at the same time destroy plaintiffs' bargained for right to prevent a separate sale of the '331 that interferes with plaintiff's rights in the '431. Counsel reasoned that, because a mere unilateral assignment of the '431 to NewCo would destroy its viability, this would leave defendants free to transfer the '331 without having any residual effect on the enforceability of the '431. Michaels Affidavit, at ¶33. Thus, defendants' position on this motion is entirely new, inconsistent with the position they took on the original motion, which did not embrace patent counsel's concept, and does not demonstrate the merit of their appeal. Indeed, defendants admit this when they claim "irony" in that they "now are paying the price for *refusing* to render the '431 Patent unenforceable by transferring it to NewCo back in [February] 2007." Brydges Reply Affirmation (12-18-07), at ¶2 (italics in original; bracketed material supplied). As shown above, the '431 would be enforceable unless the transfer was recorded by NewCo, the timing of which NewCo could control, and even upon recording the period of unenforceability would only

last until the inevitable conveyance to NewCo of the '331 Patent.

A court is not obliged to give an agreement's literal terms an absurd meaning in the guise of finding ambiguity sufficient to preclude summary judgment. "[W]here a particular interpretation would lead to an absurd result, the courts can reject such a construction in favor of one which would better accord with the reasonable expectations of the parties." Reape v. New York News, Inc., 122 A.D.2d 29, 30 (2d Dept. 1986). Contrary to defendants' argument, the court's interpretation of the Letter Agreement

> would not constitute an improper rewriting of the agreement because "courts may as a matter of interpretation carry out the intention of a contract by transposing, rejecting, or supplying words to make the meaning of the contract more clear" (Matter of Wallace v. 600 Partners Co., 86 N.Y.2d 543, 547; see Castellano v. State of New York, 43 N.Y.2d 909, 911; Hickman v. Saunders, 228 A.D.2d 559, 560; Reape v. New York News, 122 A.D.2d 29, 30). In construing the meaning of an agreement, courts must accord words their "fair and reasonable meaning," rather than their mere literal meaning (Sutton v. East Riv. Sav. Bank, 55 N.Y.2d 550, 555 [citation omitted]; see Brown Bros Elec. Contrs. v. Beam Constr. Corp., 41 N.Y.2d 397, 400).

Essex Ins. Co. v. Pingley, 41 A.D.3d 774, 776-77 (2d Dept. 2007). See also, Castellano v. State of New York, 43 N.Y.2d 909, 911-12 (1978)(affirming that, when "words may be transposed, rejected, or supplied, to make its meaning more clear," this is "a question of interpretation," instead of "a reformation"). Reading the language of the agreement to provide for an inviolate right to

sell the '331, as defendants argued on the original motion, or as providing for a unilateral right to transfer of the '431 in a manner which immediately destroys its viability such that defendants would have been free to convey the '331 with impunity despite the last sentence of ¶4(a), as defendants now appear to contend that my decision and the Letter Agreement requires, would produce just such an absurd result at variance with the evident intentions of the parties to the Letter Agreement. I decline to indulge it for the purpose of weighing the merit of the appeal factor in the CPLR 5519(c) analysis.

Turning to the balance of exigency or hardship factors confronting the parties, I find that the plaintiff's projections of potential lost profits are, for the reasons stated in the Brydges Reply Affirmation (12-18-07), not established for purposes of this motion with reasonable enough certainty to warrant a finding that an undertaking should be ordered in the amount of $10 million as plaintiff contends. See Kenford Co., Inc. v. County of Erie, 67 N.Y.2d 257, 261-62 (1986); Awards.com v. Kinkos, Inc., 42 A.D.3d 178 (1st Dept. 2007)("no profit record to serve is at basis for projecting millions of dollars in future profits"). On the other hand, defendants claimed on the original motion that they had a $2 million offer for the '331 Patent, and thus that gives guidance of some note on the valuation issue. There will be at minimum a 6 month delay if defendants' 45 day

appeal perfection deadline results in a scheduling of the appeal by the June term, and a delay considerably in excess of that if scheduling during the Fall terms of court occurs. During this time, plaintiffs will have no ability to exploit either patent in the possession of an officer of the court pursuant to CPLR 5519(a)(4) without a suitable license arrangement which neither party has, curiously, addressed on this motion.

Although there is some hardship to the defendants in posting an undertaking, the stay undoubtedly impairs completely plaintiffs' rights to the patents as the court has found them, and creates, if Thompson's assessment of the current market is credited, a potential for substantial spoilation of the property as technology progresses. Therefore, the first objective of any undertaking set in this case must be to protect against any possible spoilation of this asset. Put another way, the undertaking must be sufficient to compensate plaintiffs to the extent of any damages that they may suffer if the value of the asset is diminished in any way or destroyed while the appeal is pending. Therefore, that undertaking must bear a fair proportion to the value of the asset which is to be transferred. The purpose of a bond under CPLR 5519(c) is to protect against all damages that might-occur by reason of the delay caused by the stay pending appeal. See Genet v. Delaware & H. Canal Co., 113 N.Y. 472; Essa v. Weiner, 178 Misc.2d 149. "An undertaking is 'a

sum fixed by the court' (CPLR 5519[a][4]) which the parties are required to 'file[ ] with the clerk of the court' (CPLR 2505 [emphasis supplied])." Du Jack v. Du Jack, 243 A.D.2d 908 (3d Dept. 1997). Contrary to defendants' argument that they are able to make any required payment, they cannot act as their own surety. See Nichols v. MacLean, 98 N.Y. 458, 1885 WL 10576 (1885); Alex v.. Grande, 29 A.D.2d 616 (3d Dept. 1967), Morgan v. Morgan, 2 Misc.3d 1011(A), 784 N.Y.S.2d 921 (Table), 2004 WL 834379, 2004 N.Y. Slip Op. 50285(U) (Sup. Ct. Kings Co. 2004); Ellenville Nat. Bank v. Nat Kagan Meat & Poultry, Inc., 84 Misc. 2d 815 (Sup. Ct. 1976).

Accordingly, the automatic stay is modified on plaintiffs' cross motion to provide for an undertaking. A hearing shall be conducted Friday, January 4, 2008, at 1:30pm, to aid the court in arriving at a suitable figure, and to determine whether an officer of the court might be found at reasonable cost, and to determine whether such officer might feasibly enter into a licence arrangement permitting some immediate exploitation of the patents by plaintiff during pendency of the appeal in a manner which protects defendants in the event they are successful.

SO ORDERED.

_____
KENNETH R. FISHER
JUSTICE SUPREME COURT

DATED: January 2, 2008
Rochester, New York