The enemy within

Exploring the ongoing Oculus legal actions, **Richard S Eisert**, **Marc J Rachman** and **Josh J Gordon** explain that companies developing or acquiring new tech must take precautions to limit lawsuit perils

The ongoing, expanding litigation involving Zenimax Media and id Software on the one hand, and Oculus VR, owned by Facebook, on the other hand, over technology critical to the development of the Oculus virtual reality (VR) headset, is a costly example of the numerous litigation risks faced by any development or production company in the virtual reality or other emerging technology space.

The seemingly endless saga now involves at least three separate actions:

- The recent appeal of a February decision by a federal jury in Dallas, Texas, to award $500m to the plaintiffs Zenimax and id Software against Oculus and two of Oculus' founders, Palmer Luckey and John Carmack in a case involving VR technology – despite the jury's conclusion that the defendants had not misappropriated any of the plaintiffs' trade secrets.
- A new filing by Zenimax seeking a permanent injunction against Oculus to halt their sale or use of any product containing infringed materials.
- An April suit by Carmack against his former employer Zenimax for withholding $22.5m on payment tied to the earlier acquisition of id Software by Zenimax.

The primary VR litigation

As plaintiffs in the VR case, Zenimax and id Software sued Oculus for approximately $3bn in total. The plaintiffs also sued Oculus' founder (Palmer Luckey), chief technology officer (Carmack, who previously worked for Zenimax), and former chief executive officer (Brendan Iribe) individually.

The allegations included claims that defendants had misappropriated VR-related trade secrets (including developments central to the creation of a state-of-the-art VR experience such as distortion correction technology, chromatic aberration correction method, gravity orientation and sensor drift correction technology, and time warping methodology), had infringed the copyrights in some key computer code, and that defendants (Luckey and Oculus) had violated a binding non-disclosure agreement (NDA) they had with the plaintiffs.

The plaintiffs also asserted that:

- Facebook had tortiously interfered with the NDA and that Oculus and Facebook had engaged in unfair competition with respect to their contracts, trademarks, copyrights, and/or trade secrets.
- Carmack had "converted" their property by copying files to a USB storage device and taking them with him.
- Oculus, Luckey, and Iribe had infringed their trademarks, including the names of popular video games "*DOOM*" and "*SKYRIM*".

The plaintiffs sought $2bn in damages, a royalty, and billions more in punitive damages.

The jury verdict

After a three-week trial, the jury rejected a number of the plaintiffs' claims, including their claim for misappropriation of trade secrets – which was the main emphasis of their case.

Nevertheless, the jury decided that Oculus (but not any of the other defendants) had directly infringed the plaintiffs' copyrights and that Oculus had breached the NDA. The jury awarded damages of $50m and $200m for those respective claims.

The jury also agreed with the plaintiffs that Carmack converted their property, that Oculus and Iribe infringed ZeniMax's trademarks, and held Oculus, Luckey, and Iribe liable for "false designation" of the origin of their trademarks. Although the jury did not award damages on the trademark infringement and conversion claims, the jury found that Oculus should pay \$50m, Luckey should pay \$50m, and Iribe should pay \$150m for false designation.

Oculus, Iribe, Carmack and Luckey have jointly appealed the entire verdict.They claim that there was not sufficient evidence to prove the copyright infringement or false designation of origin claims, and that the breach of contract claims related to the NDAs were barred by the statute of limitations.

The injunction and Carmack's suit

While each side continues to file motions related to the award of money damages, Zenimax has simultaneously taken the perhaps more significant step of seeking an injunction against Oculus. The company requests that Oculus be "permanently enjoined, on a worldwide basis, from using, marketing, selling, distributing, modifying, servicing, copying, or offering for sale or license any products, in whole or in part, that utilise in any form or for any purpose any of the copyrighted materials, including but not limited to (i) system software for Oculus PC…; (ii) system software for Oculus Mobile" and software required to integrate Oculus with multiple graphical interfaces. If granted, this injunction would likely prohibit Oculus from selling its VR headset as currently created and manufactured.

And, seemingly in direct response to the jury verdict against him, Carmack has filed suit alleging that Zenimax owes him \$22.5m in unpaid income related to Zenimax's previous acquisition of id Software.

Lessons

For companies newly involved in VR or in other emerging technologies, or seeking to expand their business in these areas, the Oculus actions have a number of important lessons.

First, the most important point: an injunction granted against a VR company (or any other company in emerging technologies) prohibiting the use of infringing intellectual property that is central to a main product is an existential threat. It is critical that founders and executives are confident that the base of their critical technology is non-infringing, since most companies in VR or other emerging technologies would not be able to recover from a court order that they must cease monetising their main product.

In a situation such as this, where a number of hardware manufacturers are all striving to create similar technology at once and have employees that have moved between the companies, there is increased risk that one party will, either accidentally or purposefully, infringe on another's intellectual property or other rights. Therefore, it is imperative that all companies do proper diligence on the intellectual property that they want to create or acquire, and any related contractual restrictions, including NDAs and restrictive covenants.

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As related to money damages, the \$500m total jury award fell short of the billions of dollars the plaintiffs sought to recover but it is, of course, still a significant amount of damages for most defendants to have to pay. It is also important to keep in mind that a damages award in these circumstances is only part of the cost of litigation. Preparing and going to trial, the amount of executive time involved in a lawsuit of this nature (Facebook's chief executive officer, Mark Zuckerberg, testified in person in court for several hours in the Oculus case), and the accompanying publicity all weigh heavily on defendants.

Secondly, the risk of litigation in the VR space is real. There is a great deal of money involved and entrepreneurs, inventors, and business people will seek to protect their inventions and investments by going to court, if they deem that necessary. In an emerging market with a potentially significant first-mover advantage, litigation is one tool for getting, and staying, out in front of the competition. Thus, as developers and other businesses of all kinds seek to capitalise on the growing VR market, they need to carefully analyse the positions and motivations of their competitors to assess their risk profile. And the numerous lawsuits filed even after the initial jury verdict should serve as a reminder that litigation has a tendency to expand, not shrink, when the stakes are at their highest.

Finally, this case illustrates the care that must be taken when hiring a former employee of a competitor who is bound by an NDA. The jury found Oculus must pay \$200m for its failure to comply with the NDA initially signed between Zenimax and Luckey, the obligations of which Oculus took on, according to the jury award, by manifesting its acceptance of the NDA when Luckey began working for Oculus. When hiring from a competitor, be wary of more than just intellectual property risks; your company may face exposure from related contractual rights and other potential wrongdoing. Perhaps paradoxically, the very reason a former employee of a competitor is valuable – that is, his or her proprietary knowledge – is the same reason the legal risk is elevated.

The bottom line

Companies developing – or seeking to acquire – new technology must take every precaution to limit their risks before litigation is on the horizon. The full extent and scope of those risks is often not clear without careful analysis.

The most critical step is ensuring that the company is not at risk of an injunction prohibiting the sale of any product containing vital intellectual property – and that is only the first hurdle. Working with counsel every step of the way can help to uncover potential liabilities and limit exposure.

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