IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

NOVOZYMES A/S,	)	
	)	
Plaintiff,	)	
	)	
v.	)	C.A. No. 373-N
	)	
CODEXIS, INC. and MAXYGEN, INC.,	)	
	)	
Defendants.	)	

MEMORANDUM OPINION AND ORDER

Submitted: March 2, 2005
Decided: May 26, 2005

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LAMB, Vice Chancellor.

I.

In 1997, the plaintiff and one of the defendants signed an agreement to cross-license related bio-technology to each other on an exclusive basis. Although the licenses are similar, they differ in one key aspect: the defendant's license is royalty-free, whereas the plaintiff's license is contingent on the payment of royalties. If the plaintiff made all required payments, its license would remain exclusive in perpetuity. If, however, the plaintiff failed to pay one type of required payment, the minimum royalty, its license would become nonexclusive.

At issue here is the third and final minimum royalty payment, which the plaintiff failed to make within the express time period of the contract. The plaintiff claims that although the payment was late, it was made within a reasonable time and therefore maintains exclusivity under the contract. The defendants claim that because the plaintiff missed the payment deadline, the license has become nonexclusive.

The defendants move for summary judgment, arguing that there is no dispute regarding the language of the contract or the facts about the late payment. For the reasons discussed below, the defendants' motion for summary judgment is denied.

II.

A. Background

In 1997, Novo Nordisk A/S and Maxygen, Inc. (the predecessors in interest to the parties to this action) signed a five-year agreement ("License Agreement") to cross-license technology related to the DNA manipulation of enzymes.[1] Notwithstanding its five-year term, the License Agreement expressly states that the licenses "granted hereunder shall continue in force under the terms and conditions herein."[2] The basic structure of the agreement is that Novo Nordisk and Maxygen exchanged irrevocable worldwide exclusive licenses in their respective technologies.[3] Although the agreement appears to be reciprocal, the licenses have one crucial difference: Maxygen's license is royalty-free, but Novo Nordisk's license is contingent on the payment of royalties. In order to maintain its exclusive license of Maxygen's technology, Novo Nordisk was required to make three types of royalty payments: (i) an annual payment of $500,000, due in quarterly installments;[4] (ii) a percentage payment of net proceeds of actual sales; and (iii) a series of minimum royalty payments in the fourth, fifth, and sixth years.

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[1] The parties that negotiated and signed the licensing agreement are Novo Nordisk A/S and Maxygen, Inc. They later assigned their contract rights to Novozymes A/S and Codexis, Inc., respectively, which are the plaintiff and the defendant in this case.
[2] License Agreement § 9.1.
[3] *Id.* § 2.1.
[4] *Id.* § 8.5. Novo Nordisk could reduce its annual obligation up to 50% beginning in the third year of the contract. *Id.* § 9.1.

The minimum royalty payments differ from the other types of payments in two ways. First, untimely payments of the minimum royalty would cause Novo Nordisk's license of Maxygen's technology to be converted from exclusive to nonexclusive. The relevant language of section 3.5(c) is as follows:

> If NOVO NORDISK does not timely pay to MAXYGEN the stated Minimum Royalty Level under either subparagraph (a) or subparagraph (b) above by the end of sixty (60) days after the end of the applicable year, the licenses granted to NOVO NORDISK by MAXYGEN shall become nonexclusive within the NOVO NORDISK Field and/or the NOVO NORDISK Preferred Areas, as appropriate.

Second, the minimum royalty payments were structured in "hockey stick" fashion, meaning that the initial payment was low and subsequent payments quickly rose to much higher levels. In section 3.5(a), the payments are described as follows:

> If the royalties otherwise payable hereunder by NOVO NORDISK in any year beginning with the fourth year from the Effective Date are less than the Minimum Royalty Levels set forth below, NOVO NORDISK shall pay to MAXYGEN one hundred (100) percent of the difference between the Minimum Royalty Level for such year as stated below and the total royalties otherwise payable hereunder including, but not limited to, royalties attributable to MAXYGEN Know-How:

Year	Minimum Royalty Level
2001	350,000 (USD)
2002	700,000 (USD)
2003	1,000,000 (USD)

The final minimum royalty payment was almost as much as the first two payments combined. In addition, it represented a large percentage of the overall payments that Novo Nordisk was required to make over six years if it wanted to maintain its exclusive license from Maxygen.[5]

The two other provisions that relate to the timeliness of the final minimum royalty payment are section 4.2, which specifies the time period for royalty payments,[6] and section 9.2, which contains a time period for a party to cure a breach.[7]

B. The Dispute

Under section 3.5(c) of the License Agreement, Novozymes's minimum royalty payment for 2003 was due on or before February 29, 2004, 60 days after the end of the year. It is undisputed that Codexis sent an invoice for the payment

[5] Pl.'s Reply Br. at 4 (describing Novozymes's actual total royalty payments under section 3.5(a) as $2,050,000).

[6] Section 4.2 states:

> All royalty payments under this Agreement shall become due and payable sixty (60) days after the last day of the calendar quarter in which the corresponding sales of Licensed Products were made. Payment shall be accompanied by a report, on a country-by-country basis, showing the Net Sales in each segment of the Field as listed on Exhibit D used in the computation of the royalties payable. Any Minimum Royalty shall become due and payable sixty (60) days after the end of the applicable year.

[7] Section 9.2 states in relevant part:

> If a Party to this Agreement commits a material breach of any provision of this Agreement and fails to remedy such breach within thirty (30) days after written notice thereof from the other Party stating the intent to terminate the Party not in default may, at its option, terminate this Agreement by giving fifteen (15) days prior written notice to the Party in default.

in January 2004 and that Novozymes did not make the minimum royalty payment until March 2, 2004.[8] The issue between the parties is whether Novozymes's failure to make the payment on or before February 29, 2004 caused its license to become nonexclusive.

Codexis argues that Novozymes must strictly comply with the 60-day time limit based on the plain language of section 3.5(c). When a provision with an express time requirement is negotiated and agreed to by sophisticated parties, Codexis contends, the court should enforce the provision as written. Codexis also argues that section 3.5 of the License Agreement is an option and therefore the inclusion of the phrase "time is of the essence" in section 3.5(c) is not necessary to make the time limit strictly enforceable.

Novozymes responds by claiming it was not required to make the minimum royalty payment within the 60-day time limit of section 3.5(c) for three reasons. First, Novozymes claims it had a reasonable time beyond the 60 days in which to make the payment because section 3.5(c) allows for "timely" payment and does not contain the phrase "time is of the essence." Second, Novozymes claims that the words "shall become nonexclusive" in section 3.5(c) need to be modified by other language, such as the word "automatically." Novozymes argues that without the

[8] Although Svend Petersen, Novozymes's 30(b)(6) witness, was responsible for complying with the License Agreement and for signing off on the payments to Codexis, he was traveling from the middle of February until March 2 and caused Novozymes to be late sending the payment by being out of the office. Tr. at 10; Tr. at 17-18.

word “automatically,” which was in several drafts but not in the final version of the License Agreement, section 3.5(c) cannot function to terminate Novozymes’s right to exclusivity by March 2. Finally, Novozymes argues that the course of performance under the License Agreement eliminates any claim Codexis could make for enforcing strict time provisions. Novozymes argues that it made late payments on several occasions and Codexis did not object or attempt to enforce its rights.[9] Therefore, it contends, a payment that was a few days late cannot cause its license to become nonexclusive.

C. The Complaint

On April 12, 2004, Novozymes filed this action, claiming breach of contract and anticipatory repudiation. It requests injunctive relief that grants it the right to continue using Codexis’s technology exclusively. On July 26, 2004, Codexis filed a counterclaim for damages, alleging that Novozymes breached its contractual covenant of good faith and tortiously interfered with Codexis’s prospective economic relations.[10] Codexis filed a motion for summary judgment on February 1, 2005 and this court heard oral arguments on March 2, 2005.

[9] Only one of the late payments that Novozymes refers to is a minimum royalty payment, which was for 2002. Pl.’s Reply Br. at 7. The other late payments were four of the quarterly installments of the annual payments. *Id.*

[10] Codexis argues the counterclaim is not ripe until the contractual matter is resolved. Defs.’ Opening Br. at 13.

III.

Summary judgment shall be granted when there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law.[11] In deciding whether to grant summary judgment, a court must view the facts in the light most favorable to the nonmoving party and the moving party has the burden of demonstrating that there is no material question of fact.[12]

"A party opposing summary judgment, however, may not merely deny the factual allegations adduced by the movant."[13] "If the movant puts in the record facts which, if undenied, entitle him to summary judgment, the burden shifts to the defending party to dispute the facts by affidavit or proof of similar weight."[14]

IV.

A. <u>Is The License Agreement Ambiguous?</u>

The License Agreement is governed by New York law.[15] Under New York law, "a written agreement that is complete, clear and unambiguous on its face must be enforced according to the plain meaning of its terms."[16] "A contract is unambiguous if the language it uses has a definite and precise meaning."[17] When a

[11] Ct. Ch. R. 56(c); *see also Williams v. Geier*, 671 A.2d 1368, 1375 (Del. 1996).
[12] *Tanzer v. Int'l Gen. Indus., Inc.*, 402 A.2d 382, 385 (Del. Ch. 1979) (citing *Judah v. Delaware Trust Co.*, 378 A.2d 624, 632 (Del. 1977)).
[13] *Tanzer*, 402 A.2d at 385.
[14] *Id.*
[15] License Agreement § 19.
[16] *Greenfield v. Philles Records*, 780 N.E.2d 166, 170 (N.Y. 2002).
[17] *Id.*

contract is susceptible to more than one reasonable interpretation, it is ambiguous.[18] "[A]mbiguity is an issue of law for the courts."[19] "[In] a case involving a contractual obligation governed by ordinary contractual principles . . . , the fact that an agreement is ambiguous does not result in a grant of summary judgment in either party's favor."[20]

1. <u>The Time Requirement Of Section 3.5(c)</u>

The first disagreement between the parties relates to the express language of section 3.5(c) of the License Agreement, which governs the timing of the minimum royalty payments. "Where, as here, a contract of sale does not contain a specific declaration that time is of the essence, the law permits the parties a reasonable time in which to tender performance, regardless of whether the contract designates a specific date on which such performance is to be tendered."[21]

Codexis argues that the first sentence of section 3.5(c) is a strict time requirement that obligates Novozymes to make the minimum royalty payments within 60 days of the end of the year. Codexis relies on the plain language of section 3.5(c) that the payment must be made "by the end of sixty (60) days after the end of the applicable year." Novozymes counters that the absence of the phrase "time is of the essence" indicates that the 60-day time period was not an absolute

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[18] *Evans v. Famous Music Corp.*, 807 N.E.2d 869, 872 (N.Y. 2004).
[19] *Excess Ins. Co. v. Factory Mut. Ins. Co.*, 822 N.E.2d 768, 777 (N.Y. 2004).
[20] *Gray v. Pashkow*, 591 N.E.2d 1171, 1171 (N.Y. 1992).
[21] *Marchak v. Hallihan*, 2003 WL 22519405, at *1 (N.Y. App. Term. Oct. 2, 2003).

deadline. Instead, it asserts that it could make a minimum royalty payment beyond 60 days that would still be "timely" under section 3.5(c).

The court finds that both of these interpretations are reasonable. Section 3.5(c) does appear to dictate strict compliance with the 60-day time limit. This interpretation is supported by the express statement of the number of days in which the payment is due. The word "timely" at the beginning of section 3.5(c), however, indicates that perhaps the parties intended a time period beyond the 60 days in which Novozymes could cure a late payment.

This latter interpretation is consistent with section 4.2, which details the timing requirements for all payments in the License Agreement. Under section 4.2, nonminimum royalty payments "shall become due and payable sixty (60) days after the last day of the calendar quarter." Clearly, nonminimum royalty payments within 60 days of the end of the calendar quarter would be a breach of the License Agreement by Novozymes. Under section 9.2 of the License Agreement, Novozymes would then have 30 days in which to cure the breach. Codexis does not dispute this interpretation of section 4.2 as it applies to nonminimum royalty payments.

Section 4.2 further specifies that "[a]ny Minimum Royalty shall become due and payable sixty (60) days after the end of the applicable year." A reasonable interpretation of this sentence is that failure to pay the minimum royalty payment within 60 days of the calendar year is also a breach under section 4.2 that could be cured by section 9.2. However, this interpretation conflicts with Codexis's interpretation that section 3.5(c) converts Novozymes's license to nonexclusive immediately upon failure to pay within 60 days.

Codexis fails to explain how its purportedly unambiguous interpretation of section 3.5(c) can be reconciled with the last sentence of section 4.2. Both parties' interpretations of section 3.5 are reasonable given the facts before the court. Therefore, the License Agreement, as it applies to the required time period for minimum royalty payments, is ambiguous.

2. The Minimum Royalty Payments Of Section 3.5(a)

The next disagreement between the parties relates to whether the minimum royalty payments can be properly characterized as a series of options. "An option contract is an agreement to hold an offer open; it confers upon the optionee, for consideration paid, the right to purchase at a later date."[22] An option "binds the optionee to do nothing, but grants him the right to accept or reject the offer in accordance with its terms within the time and in the manner specified in the option."[23] As a New York court has previously held, an option can be contained within a contract.[24]

[22] *Kaplan v. Lippman*, 75 N.Y.2d 320, 324552 N.E.2d 151, 153 (N.Y. 1990).
[23] 1 WILLISTON ON CONTRACTS § 5:16 at 717-18 (4th ed. 1990).
[24] *T.I.P. Holding No. 2 Corp. v. Wicks*, 63 A.D.2d 263, 269 (N.Y. App. Div. 1978) (finding that a document contained both an option and a contract to purchase).

Codexis claims that the minimum royalty payments are options within the overall contract of the License Agreement. It argues that section 3.5(c), which potentially transforms Novozymes's license from exclusive to nonexclusive, acts to make the payments under section 3.5(a) optional. Codexis maintains that Novozymes had the right to do nothing, i.e. not make the payment, but if it chose not to pay, its license would become nonexclusive. These features of section 3.5, Codexis contends, indicate that the minimum royalty payments are options.

Novozymes asserts that Codexis is "just wrong" because Novozymes "chose and paid for exclusivity" in 1997.[25] But this assertion is directly contradicted by the language of section 3.5(c), which states that if the payment is not made, the license "shall become nonexclusive." In addition, Novozymes' brief *in the next sentence* contradicts its assertion of payment. After claiming that it "paid" for exclusivity in 1997, Novozymes states that it "has continued paying for that exclusivity."[26] Nowhere does Novozymes attempt to explain the obvious contradiction between claiming that it *has paid* for something and that it *continued paying* for that same thing. The answer is that the annual payments could be viewed as paying, in part, for three options to extend exclusivity through minimum royalty payments. This interpretation is supported by the wording of section 9.1, the termination provision which refers to "the licenses *and options* exchanged

[25] Pl.'s Reply Br. at 4.
[26] *Id.*

hereunder."[27] Novozymes fails to explain why the word "options" is in section 9.1 if, as it contends, the License Agreement had no options.

Although section 3.5(c) appears to transform the minimum royalty payments into options, section 3.5(a) contains an incompatible mandatory requirement that Novozymes make the payments. As section 3.5(a) expressly states, "NOVO NORDISK *shall pay* to MAXYGEN [the minimum royalty payments]."[28] This language suggests that Novozymes had the same obligation to pay the minimum royalty payments that it had to pay the annual payments or percentage royalty payments. Codexis is unable to explain the obvious conflict between the option language of section 3.5(c) and the mandatory language of section 3.5(a).

Therefore, the License Agreement is ambiguous as to whether the minimum royalty payments are options.

3. <u>The Effect Of The Word "Shall"</u>

The third disagreement between the parties relates to the meaning of the word "shall" in section 3.5(c). Codexis argues that "shall" means mandatory. Thus, it contends, if Novozymes does not pay within the 60-day time frame, its license is immediately converted to a nonexclusive license. Novozymes counters that, without the term "automatically," section 3.5(c) conflicts with the 30-day cure provision in section 9.2. Novozymes maintains that Codexis reads section 3.5(c) in

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[27] License Agreement § 9.1 (emphasis added).
[28] *Id.* § 3.5(a) (emphasis added).

isolation and does not give meaning to the related provisions of the License Agreement.

As New York law recognizes, "courts must interpret a contract so as to give meaning to all its terms."[29] Codexis's interpretation of the word "shall" in section 3.5(c) directly conflicts with the last sentence of section 4.2. Section 3.5(c) indicates that the license conversion to nonexclusive is immediate. But section 4.2 suggests that minimum royalty payments beyond 60 days of the end of the year are breaches curable within 30 days under section 9.2. Both section 3.5(c) and section 4.2 use the word "shall," yet Codexis interprets one section as being instantly mandatory and one as not. Therefore, the License Agreement is ambiguous as to when Novozymes's license would become nonexclusive.

B. Evidence Before The Court

The court's finding that the License Agreement is ambiguous is supported by evidence from both parties. The strongest evidence that the License Agreement is subject to more than one reasonable interpretation comes from the pre-hearing legal positions of the parties in which, strangely, the parties' original positions support the opposing parties' current position.

Codexis originally claimed that the minimum royalty payments were required payments and not options. In its invoice to Novozymes on January 30,

[29] *Greater N.Y. Mut. Ins. Co. v. Mut. Marine Office, Inc.*, 3 A.D.3d 44, 50 (N.Y. App. Div. 2003).

2004, Codexis refers to the 2003 minimum royalty payment as "due."[30] Nowhere does the invoice mention that the payment was an option or that Novozymes was not required to pay Codexis. Moreover, Codexis's claim is reinforced in its March 5, 2004 letter to Novozymes, in which it states that "[p]ursuant to section 3.5 . . . , Novozymes is required to make a minimum royalty payment of $1,000,000 for the 2003 calendar year."[31] Clearly, before this litigation, Codexis viewed the minimum royalty payments as required and not options. If Codexis's interpretation is correct, it supports Novozymes's position that nonpayment would be a breach curable in 30 days under section 9.2.

Novozymes has similar problems with its prior legal position. Svend Petersen, Novozymes's Rule 30(b)(6) witness, testified to an understanding of the License Agreement that appears almost entirely consistent with Codexis's arguments. First, Petersen testified that section 3.5(c) of the License Agreement made the minimum royalty payments of section 3.5(a) into a series of options.[32] His answers clearly show that Novozymes treated section 3.5(c) as granting it a

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[30] Defs.' Opening Br. Ex. 13.
[31] *Id.*
[32] Petersen Dep. at 57:

Q: Is it fair to say that the provision in 3.5(c) was originally conceived by Novozymes as a provision that would give it an option during each of the applicable years as to whether it wanted to continue with an exclusive license or not?

A: Yes.

Q: And it was entirely Novozymes' decision whether to exercise that option or not?

A: Yes.

series of options to extend exclusivity. Petersen was in charge of making the payments under section 3.5(c) and therefore his understanding of the effect of the payments is most relevant. During repeated questioning on the topic, Petersen never wavered from his position that (i) the minimum royalty payments of section 3.5 were a series of options; (ii) Novozymes had unilateral decision-making authority whether to make the minimum royalty payments; and (iii) if Novozymes decided not to make a minimum royalty payment, the license would become nonexclusive but there would be no breach of contract.

In an effort to counteract the damaging testimony of Petersen, Novozymes points to the August 20, 1997 negotiation notes of Russell Howard, then President of Maxygen and the signator to the License Agreement for Maxygen. Howard's notes about section 3.5(c) state "Go to non-exclusive license without minimum if the royalty / AMF not paid."[33] Novozymes argues that this statement shows Maxygen (i.e. Codexis) understood that only a nonpayment of the minimum royalty would convert the license to nonexclusive, not late payments. This argument is not persuasive. In the context of option contracts, late payments are equivalent to nonpayments. If Petersen were correct that the minimum royalty payments were options, it is irrelevant whether Howard's notes said "not paid" or

[33] Pl.'s Answering Br. Ex C.

"paid late." Both late payments and nonpayments prevent an option from being exercised.

Second, Petersen testified that nonpayment of the minimum royalty payments would not be a breach of the License Agreement.[34] Again, Petersen's testimony supports Codexis's position. If the nonpayment were not a breach, as Petersen contends, then Novozymes would not have the benefit of the 30-day cure period.

In their submissions to the court, the parties have now straightened out their legal arguments to support their respective positions. Presumably, more in-depth legal analysis clarified what should have been obvious if the License Agreement were unambiguous, as Codexis argues. Looking at the facts in the light most favorable to the nonmoving party, the court finds that there is a genuine issue as to whether the minimum royalty payment was due within 60 days of the end of the year or whether a timely payment beyond the 60 days would be effective to maintain Novozymes's rights.[35] Codexis has not met its burden of proving otherwise.

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[34] Petersen Dep. at 52:

Q: Does that mean Novozymes had a choice about whether to pay the minimum royalty or not?

A: Yes.

Q: And if Novozymes did not pay the minimum royalty, it would not be a breach of the contract?

A: No.

[35] Since the court finds that the License Agreement is ambiguous, it need not analyze the parties' contentions regarding course of performance and course of dealing.

H. <u>The 2003 Minimum Royalty Payment</u>

The court now turns to the issue of possession of the disputed 2003 minimum royalty payment. Codexis treated the payment like any other payment it received under the License Agreement. It did not set up a separate escrow account for the payment and it did not offer to repay the money to Novozymes.[36] Instead it has kept the money while arguing that Novozymes should not get the benefit of its payment because of the two-day delay.

Until the court determines the proper interpretation of the License Agreement, neither party should have the benefit of the disputed minimum royalty payment. Codexis is ordered to deposit $974, 279.78[37] into escrow with the Register in Chancery within 30 days.

V.

For the foregoing reasons, the motion for summary judgment is DENIED.[38]

IT IS SO ORDERED.

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[36] Tr. at 49.

[37] This amount was the amount due per Codexis's invoice dated January 30, 2004. According to the invoice, Novozymes was entitled to setoff its quarterly percentage royalty payments from the $1,000,000 minimum royalty payment due at the end of the year. Defs.' Opening Br. Ex. 13.

[38] The court notes that this opinion makes no ruling on the counterclaims alleged by Codexis. Although Novozymes argues that those claims should be dismissed with prejudice, it has not moved for dismissal. Accordingly, Codexis may continue to prosecute its claims.