

PRACTICAL CONSIDERATIONS FOR INTELLECTUAL PROPERTY DUE DILIGENCE IN TRANSACTIONS

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for Association of Corporate
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Ann M. LaFeir is a Senior Intellectual Property Attorney for USAA, a financial services company serving the military. Ann has been practicing in all areas of IP law since 2002, but her current responsibilities include conducting IP due diligence, freedom to operate research and analysis, and competitive intelligence in the banking and insurance industries. Previous to her law career, Ann was an aerospace engineer for several years working on space and avionic systems for Allied Signal. Outside of work, Ann is a wife, a mother to two teenage boys, a professional bodybuilder, and enjoys life on six acres outside of San Antonio with two horses, several chickens, and way too many goats.



Kevin Tamm is a senior intellectual property associate at Bracewell LLP where he focuses his practice on transactional intellectual property issues and IP due diligence for large and mid-size corporate clients.

Representation includes patent prosecution in the chemical and mechanical arts; post-grant reviews, including *inter partes* reviews; addressing IP issues in mergers and acquisitions, licensing and freedom to operate. Kevin counsels and represents clients in the areas of patentability and intellectual property asset management in the fields of energy, oil and gas, petrochemicals, specialty and organic chemicals, control systems, medical devices and small molecules.



DUE DILIGENCE TOPICS FOR DISCUSSION

- Identify the IP Portfolio
- Verify Ownership, Status, and Chain of Title
- Evaluate Proposed Use and Scope of IP
- Review Agreements for IP-Related Issues
- Consider IP Protection and Enforcement Strategy
- Analyze Foreign Assets
- Research Litigation and Administrative Challenges

WHY CONDUCT IP DUE DILIGENCE?

- Great value in deals is placed on the value of Intellectual Property Assets, along with IP necessary for conduct of the “Business”
 - 1998 → Volkswagen purchased the assets of Rolls Royce and Bentley automobiles for about \$900 million
 - Volkswagen did not realize until after close that the IP assets did not include the right to use the Rolls Royce trademark
 - The trademark was owned by BMW based on a prior agreement
 - Volkswagen later settles to give over the mark and production to BMW after costly deal
 - Volkswagen had acquired rights necessary to manufacture the cars, but did not have the right to brand as a Rolls Royce

IDENTIFY THE IP PORTFOLIO

- Consider the transaction type
 - Asset or stock purchase
 - Licensing in or out
 - Buying or selling assets in bankruptcy
 - Other mergers or acquisitions
 - IP portfolio sale or purchase
 - Joint Ventures, Financing, IPO

“There is no IP involved in this deal”

“The Company owns no IP”

- Each will have unique IP considerations regarding ownership, use, enforcement, representations, warranties, and indemnities

IDENTIFY THE IP PORTFOLIO

- **“Intellectual Property”** means any and all rights in, arising out of, or associated with any of the following in any jurisdiction throughout the world: (i) **patents**, patent applications (whether provisional or non-provisional), utility models, design registrations and applications, and certificates of invention and other governmental grants for the protection of inventions or industrial designs (including all related continuations, continuations-in-part, divisionals, reissues and reexaminations of any of the foregoing); (ii) **Copyrightable Works**, including copyrights, designs, and database rights, and registrations and applications for registration thereof, including moral rights of authors; (iii) **inventions**, invention disclosures, conceptions, statutory invention registrations, whether patentable or non-patentable, whether copyrightable or non-copyrightable and whether or not reduced to practice; (iv) **trademarks**, service marks, brands, certification marks, logos, trade dress, trade names, and other similar indicia of source or origin, together with the goodwill connected with the use of and symbolized by, and all registrations, applications for registration, and renewals of, any of the foregoing; (v) **internet domain names, social media accounts**, and user names (including “handles”), all associated web addresses, URLs, **websites and web pages**, and all content and data thereon or relating thereto; (vi) **trade secrets**, know-how, discoveries, improvements, technology, business and technical information, tools, drawings, methods, processes, techniques, and other confidential and proprietary information and all rights therein; (vii) **Computer Software**; and (viii) other proprietary rights relating to any of the foregoing (including remedies against infringement thereof and rights of protection of interest therein under the laws of all jurisdictions throughout the world).

VERIFY OWNERSHIP, STATUS, AND CHAIN OF TITLE

- Patents and Applications

*Watch for Joint
Development Agreements*

- Pending application or registration status
 - Country-by-country right
- Inventor assignments → company entity(ies)
 - “I do hereby assign” versus “I agree to assign” or “I will assign”
- Renewal, annuity, and/or maintenance fees to maintain active status
- Outstanding security interests?
- **Status of patent applications and registrations provides no information on “freedom to operate”
 - Separate consideration, more detailed diligence
- For published applications and registered patents, certain information publicly available
 - Detailed diligence would compare patent prosecution between countries for disclosure and consistency

VERIFY OWNERSHIP, STATUS, AND CHAIN OF TITLE

- Trademarks/service marks and applications
 - In the U.S., federal, state, and common law marks
 - Country-by-country rights
 - Consider “intent to use” applications, versus actual use in commerce
 - In the U.S., continuous use for 5 years can lead to “incontestable” status
 - **But, watch for maintenance, renewals, and annuities
 - In U.S., failure to file Section 8 Declaration leads to cancelation
 - Verify field of use restrictions or co-existence agreements
 - Volkswagen should have considered BMW trademark ownership of Rolls Royce
- Watch for confusingly similar marks in similar markets
 - Trademark “squatting” is prevalent in Asia
 - With large foreign portfolios local searchers and firms can help

VERIFY OWNERSHIP, STATUS, AND CHAIN OF TITLE

- Trade Secrets
 - Commercially valuable proprietary information where reasonable means are taken to keep it secret
- In the U.S., strong state and federal protection
 - State adoption of “Uniform Trade Secrets Act” and more recent federal Defend Trade Secrets Act “DTSA”, not mutually exclusive
- Foreign protection generally not as strong
- How will these be identified and defined in diligence and transaction?
 - Schedules with description or no schedules? NDA’s?
- How are company employees tasked with keeping the trade secrets?
 - Employment, termination, and confidentiality agreements, training/policies

VERIFY OWNERSHIP, STATUS, AND CHAIN OF TITLE

- Copyright and Software
 - In the U.S., copyrights generally exist at creation of a “work”
 - Federal registration not necessary, but helps in enforcement
- From a company standpoint, ensure “works made for hire” belong to company via written agreement from employee or independent contractor
- For copyrighted works, what rights have been licensed in or out?
 - Reproduce
 - Create derivative works
 - Distribute
 - Public display/performance
- Consider, copyright protects “form” not “function”

Software: patent, copyright, or both?

VERIFY OWNERSHIP, STATUS, AND CHAIN OF TITLE

- Open Source Software (“OSS”)
 - Can impose obligations on licensees
 - Licensee may need to make derivative works available to 3Ps
 - Notices and legal disclaimers may be required
- Code scans and software experts/vendors can detect certain OSS
 - Depends on importance to business and integration into business software
- Cost versus deal efficiency, consider amount of OSS and in-house expertise

EVALUATE PROPOSED USE AND SCOPE OF IP

- Patents

- Value found in licensing out, enforcement against competitors, employee recruitment, employee motivation, stock value, IPO?
- Portfolio size, cost to maintain and grow versus income from licensing or realization from enforcement/increase in market value
 - **Freedom to operate on technologies is a separate consideration, patents generally provide a “negative right” against others
- Country-by-country analysis on use of patents and technology (years later, “why did we file here”?)

- Trademarks

- Consider markets → regional, state, country(ies)
- Recognizable marks can have great value, depending on market



EVALUATE PROPOSED USE AND SCOPE OF IP

- Trade secrets
 - Consider geographical location and practicality of keeping a trade secret
 - Review and consider employee agreements in place over preceding years
 - What precautions have been taken to maintain trade secrets?
- Copyrights
 - Consider software created by employees or independent contractors and associated agreements
 - Consider licensed in and licensed out software and what is critical for day-to-day function of the business
 - Are employees using copyrighted software and data according to licenses?

REVIEW AGREEMENTS FOR IP-RELATED ISSUES

- Employee offer, acceptance, employment, and termination agreements
- IP Assignments (watch for earlier agreements, JDA, field of use, etc.)
 - Volkswagen could have considered BMW trademark ownership of Rolls Royce
- Consider executive/founder intellectual property obligations to company and rights
- Independent contractor agreements
- Non-disclosure and confidentiality agreements (do they exist?)
 - Would new NDA's be required during diligence?

REVIEW AGREEMENTS FOR IP-RELATED ISSUES

- Testing agreements
- Licenses in and out
 - Consider if assignable/transferable
 - What rights have been licensed, for how long, for what fees?
 - Consider bankruptcy section 365(n) as licensor or licensee
 - Licensees can elect to retain IP license from bankrupt licensor, but where is “IP”? Now includes trademarks
 - Check for Escrow and accessibility
 - Check for reverse licenses in IP sale agreements
- Verify if licenses or other agreements have extensive warranty (non-infringement) or indemnity obligations

CONSIDER IP PROTECTION AND ENFORCEMENT STRATEGY

- In mergers, acquisitions, joint ventures, licenses, what party has the right and/or obligation to obtain and maintain intellectual property assets?
- Consider what entity will pay for and manage intellectual property portfolios after close of a transaction
- Separate entities may have different uses for IP, enforcement versus licensing versus recruiting

CONSIDER IP PROTECTION AND ENFORCEMENT STRATEGY

- In mergers, acquisitions, joint ventures, licenses, who has the right and/or obligation to enforce?
- Consider what entity will pay for and conduct or participate in litigation and enforcement
- Generally only “exclusive” licensees have the right to enforce patents against others in the U.S.

FOREIGN ASSETS

- Can be of great importance, depending on applicable markets
- Country-by-country analysis on patents, trademarks, etc.
 - Prevent competitors from making/using/selling/importing in a country
 - Or license country-by-country or by region
 - Freedom to operate in a country separate consideration
- Recognizable trademarks can vary greatly based on countries' languages
 - Watch for trademark squatting for popular and profitable products
 - First-to-file systems versus U.S. generally first-to-use
 - 2016 → Michael Jordan wins a long legal battle against Qiaodan Sports, a multi-million dollar Chinese sportswear company using the Chinese transliteration of Jordan's name as its registered trademark

FOREIGN ASSETS

- Software
 - Protectability via patent varies greatly country-by-country
 - “Abstract idea”
 - Consider copyright protection, but generally protects form and not substance or function
- Trade Secrets
 - Foreign protection and enforceability generally weaker than in the U.S.
 - Consider practicality of keeping valuable technology a “secret” in other countries
 - Difficulty of reverse engineering, importance of employee agreements

LITIGATION AND CHALLENGES

- Patents

- Verify if patent assets have been enforced against others in litigation
 - Past versus present and timeline of reps/warranties
- Verify if issued patents have been administratively challenged by a 3P
 - *Ex parte* re-examination
 - *Inter partes* re-examination
 - Post-grant review
 - Covered “business method” challenge
 - » Similar foreign administrative challenges outside of U.S.
- Verify if competitor patents have been challenged administratively
- Now administrative procedures at the Patent Trial and Appeal Board (PTAB) have long-lasting and broad estoppel effects in federal litigation

LITIGATION AND CHALLENGES

- Licenses
 - Do licenses in or out prevent challenges to validity of intellectual property assets?
 - What venue/choice of law/escalation procedures are required?
- Trademark
 - Verify if registered state/federal marks have been involved in state/federal litigation
 - Watch for earlier users in the U.S. who may have regional common law rights
 - Again, watch for foreign squatting

LITIGATION AND CHALLENGES

- Copyright and Software

- Federal damages for copyright infringement can be extremely expensive
- Consider employee actions with respect to licensed-in copyrighted materials
 - Reproduce
 - Create derivative works
 - Distribute
 - Public display/performance
- Data libraries and requirements to “return or destroy” data

LITIGATION AND CHALLENGES

- Consider social media and websites
 - Are these controlled and monitored?
 - What employees have had access to accounts and programs?
 - Have take-down notices been filed for copyright violations against others?
 - Are others using marks in negative way to criticize an entity?
 - Watch for “negative” accounts mirroring important company brands

IP DUE DILIGENCE TAKEAWAYS

- Identify the IP Portfolio
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QUESTIONS AND COMMENTS

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- ACC Article
 - <https://www.acc.com/resource-library/top-ten-considerations-performing-intellectual-property-due-diligence-united#>