

Buyer and Seller, Beware

The issues involved in identifying and transferring IP rights when purchasing product lines or companies

By Mark D. Hansing

As a buyer, you have identified a product line or company you want to purchase. You negotiate an agreeable price. You and the seller sign a purchase agreement. How do you know if any intellectual property (IP) rights come with the deal? How do you know if the right steps have been taken to transfer them?

Purchase of a product line or company normally includes all related IP rights. However, it is not always easy to identify which of the conventional forms of IP (patents, trademarks, copyrights and trade secrets) are involved. Each form has differences in what it covers and how those rights are transferred. Sometimes conventional purchase agreements do not contain unambiguous or required language for full and legal transfer. Sometimes purchase agreements do not cover IP assets.

By setting up an appropriate due diligence procedure, one can try to avoid overlooking valuable IP assets or creating issues that will require additional resources to remedy, if that is even possible after the fact.

A.) Due Diligence for Commercial Transactions

The first step is to identify the potential universe of IP that could be involved with the transaction.

1.) Ask the Seller - The obvious starting place is to ask for a comprehensive list of relevant IP from the seller. There is no

standard way to ask for this information; however, IP counsel can prepare a questionnaire tailored to the particular deal. The questionnaire would also ask for documents that support the identified IP. The main types of IP are:

- a.) Patents - issued and pending applications (in any country or patent office of the world);
- b.) Trademarks - issued registrations by state, federal or foreign offices and any unregistered brand names or trademarks the seller has used relevant to the business or product line intended to be purchased;
- c.) Copyrights - registered and unregistered potentially copyrightable subject matter related to the deal;
- d.) Trade secrets - the basic subject matter of everything the seller treats as a trade secret, or believes could be one;
- e.) Internet domain names, including those not in use.

2.) Independently Investigate - A seller's listing is a good starting point. While a buyer could decide simply to rely on the seller's list, it is usually in the buyer's best interest to conduct at least some of its own independent due diligence investigation and searching for IP relevant to the transaction. This not only is a double-check of the seller's information, but could uncover additional unknown valuable IP and/or could expose potential concerns or issues about the scope or validity of the IP.

3.) Personal Interviews - Most IP identification due diligence techniques ask for permission for the buyer to interview key employees of the seller. This can be a good source for trying to corroborate whether the seller's list is comprehensive. However, such permission may not be granted. It also involves quite a bit of work and skill, and it can never be assumed to be comprehensive or totally reliable.

B.) Evaluate the Identified IP

Once the due diligence identification steps have been completed and catalogued, the information normally should be evaluated in at least the following respects.

1.) Title - An evaluation should be made whether the seller has a legal title. Normally, the seller is required to provide conclusive legal documentation such as certificates of recordation of title with the USPTO, if applicable.

2.) Scope - An evaluation of the scope of the intellectual property should be conducted. For example, patents have written claims that define what the patent covers. Sometimes patents have drawings and written examples that are broad but the claims allowed by the USPTO are very narrow. The prospective buyer needs to know whether the patent has commercially valuable scope.

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For trademarks, the seller should supply verifiable documentation about where the mark has been used and on what products or services. If a mark has only been used in a small geographic area and/or for a single product, it may not cover use of that trademark outside that area or for different products or services.

The buyer needs to see an exact and complete copy of any claimed copyrighted works. A computer program, for example, which uses a specific programming language and sequence of programming steps, may not cover a competitor that uses a different programming language and sequence of coding steps. Buyer needs to be able to evaluate the scope of copyright protection that is being purchased.

With respect to trade secrets, some written description and documentation of the scope should be given to the buyer along with a list of security steps that have been taken to protect the trade secret. An independent evaluation should be made by the buyer about whether the claimed trade secret is likely protectable and of any commercial value. Just because the seller says they have a trade secret manufacturing process may not mean it is protectable or valuable.

3.) **Validity** - The buyer should make a business decision as to how extensive the validity of the claimed IP should be. For example, an independent opinion can be obtained from IP counsel as to whether an issued patent is likely to be found enforceable. Similar opinions can be obtained regarding trademarks, copyright and trade secrets.

4.) **Encumbrances** - The seller needs to be asked about any encumbrances related to the IP they list. For example, patents, trademarks, copyrights and trade secrets are normally considered as “personal property”. These IP “assets” have attributes like other property a company or individual holds (e.g. real estate, company securities). They can be bought, sold, aggregated, sub-divided, securitized, licensed, etc. Therefore, the seller should be asked, and ideally there should be independent due diligence by the buyer, for such things as liens, security interests, licenses, covenants not to sue, settlement contracts restricting IP rights, and indemnification obligations.

5.) **Valuation** - At least some attempt at putting a monetary value on the IP should be made. This is a difficult endeavor. There have been numerous books written about it. A number of economic theories exist, such as cost approach, market approach, and income approach. This is outside the scope of this article. However, it can be important to get a feel for

economic value when considering purchase of IP.

6.) **Potential Risk** - Other risks can exist. One class of a potential risk is some pre-deal trigger that prevents full transfer of IP rights. For example, if the seller had purchased the IP from a previous owner, that prior agreement may include a provision that terminates ownership if any attempt is made to transfer the IP. The next buyer could end up with nothing except a potential breach of contract claim against the seller. Some agreements prevent transfer, or cause ownership to revert to the prior owner, if there is any change in control of the seller. Thus, a buyer might purchase a business and find out the IP does not come with it. The buyer should request and obtain any documentation from any prior party that had or claimed rights in any of the IP.

Another potential risk is that practicing the IP could infringe intellectual property rights of third parties. The classic “chair versus rocking chair” hypothetical example can illustrate this problem. If a buyer purchases a patent that covers the idea of a chair on rockers, but a third party obtained an earlier patent on just the chair, the buyer could not sell rocking chairs without paying the owner of the chair patent. The buyer may purchase a valid patent in the transaction but may not be able to commercialize it in the marketplace.

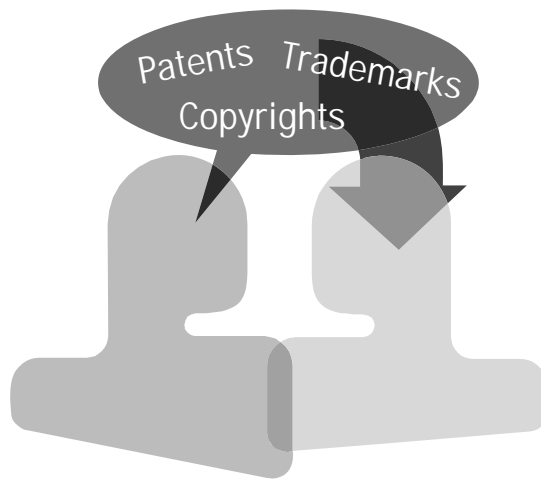
7.) **Renewals and Maintenance** - The seller needs to provide proof that any IP requiring renewal or maintenance has been kept up-to-date. For example, patents require payment of maintenance fees approximately every four years after issuance. If seller failed to meet a maintenance fee deadline in the past, a patent is technically expired. Registered trademarks require similar maintenance or renewal every 10 years. Copyrights have one term but it is important to evaluate the projected life of the copyright.

C.) Conclusion

This article is not comprehensive and is not intended to be. It is intended to raise some issues that should be at least considered when business transactions are conducted that may include IP.

As mentioned, a number of levels of diligence can be pursued. Business judgments have to be made as to how much expense and time is justifiable.

It is advised that the buyer engage IP legal counsel prior to any such activities and work with the buyer’s business counsel to make sure the purchase agreement meets the buyer’s needs, and any additional actions related to IP occur to fully and completely make the transfers. IP counsel can work with business counsel to take actions to try to remedy or repair any defects, or to enhance the IP prior to closing the business deal.



Splenda Leaves a Bitter Taste in Competitors' Mouths

By *Janaé Lehman Bell*

In 2004, Merisant Company, the makers of Equal® brand sweetener (the sweetener in the little blue packet) filed a lawsuit against McNeil Nutritionals LLC, the makers of Splenda® brand sweetener (the sweetener in the little yellow packet). The core concern – what is fair in marketing and branding.



Merisant alleges that the advertising and packaging of Splenda® highlighted by the phrase “Made from sugar, so it tastes like sugar” are false and misleading descriptions of the nature, characteristics, and qualities of Splenda®.

Therefore, Merisant argues that the sale of these goods in interstate commerce are in violation of federal trademark law (Lanham Act § 43(a)(1)(B), 15 U.S.C. § 1125.) Merisant alleges that the advertising and packaging of Splenda® sweetener lead consumers to believe that the product is natural and contains actual sugar, rather than sucralose – a sucrose molecule with three chlorine atoms substituted for three hydrogen-oxygen groups. Merisant asserts that sucralose can be made from starting materials other than sugar. It can be created by using a compound found in beans and onions and consequently, the sweet taste of Splenda® brand sweetener is not dependent upon using sugar as a starting material.

Additionally, Merisant asserts that the advertising campaign by McNeil actively seeks to enhance the false association between Splenda® and sugar in the mind of the consumer by substituting

the word “Splenda” for “sugar” in common phrases. For example, McNeil uses the slogan, “Roses are red, violets are blue, Splenda is sweet and so are you” to imply that Splenda® contains sugar.

In its complaint, Merisant further alleges that there is actual confusion among consumers including health professionals, who have arrived at the conclusion that Splenda® is a natural product. Merisant also speculates due to a trend in our society towards the consumption of organic or chemical free products that consumers undoubtedly purchase Splenda® brand sweetener thinking it is natural or that it contains sugar. Merisant alleges that advertising with the phrase “made from sugar” was key in consumer purchasing decisions; that it caused confusion and continues to cause consumer confusion and damage to Merisant in violation of Pennsylvania law of unfair competition.

Merisant is asking the court for compensatory damages including damages for diverted sales and loss of goodwill and reputation, and is requesting a court order for McNeil to institute a corrective advertising campaign to clarify that Splenda® is not natural or sugar.

Merisant’s Equal® brand sweetener, aspartame, contains the amino acids phenylalanine and aspartic acid combined with methanol. Products containing Equal® are required to carry a label informing consumers that it contains phenylalanine to warn individuals with phenylketonuria, a genetic disease where the individual lacks the enzyme to metabolize phenylalanine.

Splenda®, since its entry into the market in 2000, dominates the sales for sugar substitutes, having a 68 percent share in its class, compared to 15 percent for Equal®. Unlike its competitors, Splenda® is heat stable so it can be used in baking.

Managing Your Budget with Contingency Litigation

By *R. Scott Johnson*

At a recent CLE course in Chicago, I went to lunch with a lawyer who serves as in-house counsel for a pharmaceutical company. The company had several patents which were “allegedly” being infringed upon by its competitors. I asked if he was planning on filing suit and the response I got startled me. The company was waiting to see if its patent lawyer would take the case on contingency.

Usually, contingency cases are associated with personal injury actions where the client cannot afford the legal fees, but the chance of recovery is better than average. When a contingency case is filed, the client bears the costs of travel, experts, filing, etc. and the lawyer agrees not to charge any attorney fees in exchange for a share of the recovery. More and more, small businesses are using the contingency fee arrangements in the context of patent litigation to control their budgets and minimize the upfront expense of patent litigation.

Besides controlling the upfront expenditures and helping to minimize budgetary concerns, contingency litigation can offer some other benefits as well. For example, the in-house lawyer at the pharmaceutical company was pursuing contingency arrangements because it meant his company and its lawyer both had a stake in the litigation and both had to more thoroughly evaluate the potential risks and potential rewards before a case was ever filed. This meant not only an investigation into whether or not infringing activity was occurring, but also a more detailed assessment of what that infringer’s sales were, what the potential royalties and/or lost profits were, and what the potential for obtaining an injunction was. Then, he was in a better position to help his company and his patent attorney decide on whether they should all take the calculated bet on their shared success.

Contingency arrangements are just one of the many types of fee arrangements available. While contingency fee arrangements present many potential benefits, sometimes they are not right for either the client or the lawyer. There simply is no “one size fits all” type of fee and you should discuss any fee arrangement thoroughly with your lawyer prior to initiating any type of litigation activity. For more information on how we can help you manage the costs of litigation, contact one of the attorneys at MVS.

USPTO Releases Strategic Plan for 2007-2012

By John D. Goodhue

The U.S. Patent and Trademark Office (USPTO) recently released its Strategic Plan for 2007-2012. The full-text of the Strategic Plan is available at the Patent Office web site.

The USPTO's plan identifies four major goals:

- (1) optimize patent quality and timeliness;
- (2) optimize trademark quality and timeliness;
- (3) improve intellectual property protection and enforcement domestically and abroad; and
- (4) achieve organizational excellence.

In addition to setting these goals, the plan identifies more specific objectives associated with each of these goals and performance measures to be used to determine progress towards achieving the goals.

The strategic plan indicates: "This strategic plan proposes consideration of substantial changes of patents, trademarks, and management that will better position the USPTO and its users for future growth and complexity." Yet, the strategic plan provides little explanation of what changes will be implemented and how they may affect Applicants. One hopes that changes made to better position the USPTO do not adversely impact applicants.

The plan provides the USPTO's perspective as to what problems exist and some guidance as to how they expect to address these problems. Following are a few observations regarding the plan.

√ **Emphasis on intellectual property enforcement** - The strategic plan places more emphasis on intellectual property enforcement than one might expect given that the USPTO is not charged with the duty of enforcing intellectual property protection. It appears that the USPTO intends to increase their involvement in activities related to intellectual property enforcement, at least through educational efforts and input on policy making.

√ **"Patent quality" definition** - The strategic plan offers the following definition: "Quality means accurate and consistent results in examination. It presumes improved inputs, better-focused examination, improved review processes, and consistent examination results." The concerning aspect of this definition is the presumption of "improved inputs." The strategic plan is silent as to what exactly this may mean, but it is suspected that it will result in a shifting of additional burdens to applicants, whether through the post-grant review procedure or new procedures for submission of prior art.

√ **Patent quality measurement** - Certainly, the goal of optimizing patent quality is an important goal. One concern about the strategic plan is the use of metrics in monitoring process towards the goal of improved patent quality. The strategic plan cites to a falling percentage of patent applications approved for issuance as indicative of improved quality. Although perhaps that provides a convenient measure, there are obvious flaws in that logic. In particular, fewer patents approved does not mean the quality of those approved is necessarily better. A higher rate of patent applications not being approved may just as easily be indicative of a less than optimal patent examination process which does not recognize applications which should be approved.

√ **Timely examination** - The USPTO is placing an emphasis on timely examination of patent and trademark applications and is attacking this issue in several ways. Various initiatives include recruiting new examiners and accommodating examiners through telework. Other initiatives provide for improving electronic file management capabilities. Given the variety of approaches suggested it seems clear that issues regarding timely examination are not likely to go away in the near future.

DEFINITIONS

Examiner's Amendment

A written confirmation of an amendment made to an application. The examining attorney assigned to the application will make the amendment after consulting with the applicant or the applicant's attorney. The amendment is merely a written confirmation of the agreement between the examiner and the applicant. The applicant need not respond to the examiner's amendment unless the applicant wishes to make further changes to the application.

Information Disclosure Statement

A list of patents, publications, US applications, or other information known to the applicant or applicant's attorney that is submitted along with a non-provisional patent application to the USPTO. Providing this list is required and applicants must comply by being forthcoming with any information that is material to patentability of the invention claimed in the non-provisional application.