



REUTERS/Tim Wimbourne

Drafting and Negotiating IP/IT Provisions in M&A Transactions

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Agenda

- Structure of Common M&A Transactions
- M&A Transaction Documents
- IP/IT Provisions
 - Definitions
 - Representations and Warranties
 - Other IP/IT Provisions

Hypothetical Scenario

Buyer seeks to acquire from Seller a subsidiary (“Target”) that provides, or partners with another party to provide, SaaS and server-based software offerings

Common M&A Transaction Forms

Forward Subsidiary Merger



Reverse Subsidiary Merger



Asset Sale



Stock Sale



M&A Transaction Documents

- The IP/IT issues in the transaction agreement will differ based on the form of the transaction
 - Stock Purchase Agreement
 - IP/IT representations and warranties, interim operating covenants, closing conditions
 - Disclosure schedules
 - Change of control issues
 - Merger Agreement
 - Same as Stock Purchase Agreement, plus potential anti-assignment issues
 - Asset Purchase Agreement
 - Similar to Merger Agreement, plus:
 - Appropriate definitions of transferred intellectual property and licenses
 - IP assignment agreements
 - Ancillary license agreements

Purchase Agreement: Definitions

- “Intellectual Property” means patents, trademarks (and domain names), copyrights, and trade secrets
- In an asset sale, the definition is more important as it likely defines the assets being purchased/retained
 - For example, “Patents” means patents and patent applications, including reissues, divisions, continuations, continuations-in-part, extensions, and re-examinations thereof, all inventions disclosed therein and improvements thereto, all rights therein provided by international treaties and conventions, and all rights to sue and recover damages for past, present, and future infringement, misappropriation, or other violation of any of the foregoing.

Purchase Agreement: Key IP/IT Representations & Warranties

- Sufficiency of Assets / Ownership / Right to Use
- Non-infringement
- Protection Measures / Trade Secrets
- Employee / Contractor Agreements
- Effect on Buyer
- Open Source Software
- Privacy
- Validity / Enforceability
- IT Assets

Use of Qualifiers in Representations & Warranties

- Common Qualifiers
 - Knowledge
 - Actual knowledge of specified persons (for example, CEO, CFO, CTO)?
 - Due inquiry?
 - Material Adverse Effect (MAE)
 - Materiality
 - Schedule of exceptions
- Use of qualifiers depends on relative bargaining power of the parties, the importance of the representation/warranty and the type of deal
 - For example, representations and warranties in public M&A deals are more often qualified by MAE and/or knowledge

Sufficiency / Ownership / Right to Use

- Ownership and right to use IP and IT rights
- The IP being purchased includes all of the IP used in the Business
 - Buyer will be concerned about the right to use the IP after Closing
 - Particularly important in asset sales and in carve-out transactions
- In asset sales, sufficiency representation is commonly based on some or all of the following:
 - Purchased Assets
 - IP/IT licensed to Target pursuant to Transferred Target IP/IT Agreements
 - Ancillary license agreements between Buyer and Seller
 - Transition Services Agreement between Buyer and Seller
- Seller should ensure no inconsistency with general sufficiency of assets rep

Sufficiency / Ownership / Right to Use

To the Knowledge of the Company, the Company has rights to use the material Intellectual Property necessary for the operation of the Company Business as currently conducted. The Company owns all right, title and interest in and to all material Owned Intellectual Property, free of all Liens (other than Permitted Liens). The Company has a right to use the Licensed Intellectual Property in connection with the operation of the Company Business as currently conducted, subject only to the terms of the Company IP Agreements governing such Licensed Intellectual Property.

Sufficiency / Ownership / Right to Use

~~To the Knowledge of the Company, the~~ The Company has sufficient rights to use the ~~material~~ Company Intellectual Property necessary for and Company IT Assets in connection with the operation of the Company Business ~~as currently conducted~~, and all of those rights will survive unchanged the consummation of the Transactions. The Company Intellectual Property includes all Intellectual Property used or held for use in connection with the operation of the Company Business, and there is no other Intellectual Property that is material to or necessary for the operation of the Company Business or for the continued operation of the Company Business after the Closing in substantially the same manner as operated prior to the Closing. The Company exclusively owns all right, title and interest in and to all ~~material~~ Owned Intellectual Property, free of all Liens ~~(other than Permitted Liens).~~ The Company has a right, exclusive licenses, non-exclusive licenses not granted in the ordinary course of business consistent with past practice, and obligations to grant any of the foregoing. The Company has a valid license to use the Licensed Intellectual Property in connection with the operation of the Company Business ~~as currently conducted~~, subject only to the terms of the Company IP Agreements ~~governing such Licensed Intellectual Property.~~

Non-Infringement

- Non-infringement of third-party IP by the Target
- Non-infringement of Company IP by third parties
- Should this representation and warranty “look back,” and if so, for how many years?
- Pending or asserted claims and active litigations
- Cease & desist letters and offers to license

Non-Infringement: Allocating Risk

Who bears the risk of unasserted third-party infringement claims?

- Buyer's position
 - Seller is in better position to identify, assess and mitigate
 - Buyer may be a more attractive target
 - Deeper pockets?
 - Relationship to potential claimants?
 - Address both threatened claims (cease and desist letters) and "invitations to license," which may be precursors to claims

Non-Infringement: Allocating Risk

- Seller's position
 - Risk of doing business
 - "Impossible" to assess infringement risk with 100% certainty
 - Avoid "back door" non-infringement warranties
 - *In re Paragon Trade Brands*, 324 B.R. 797 (Bankr. N.D.Ga. 2002)
 - “The representations and warranties set forth in this Section are the only representations and warranties made by Seller in this Agreement with respect to any activity that constitutes, or otherwise concerning, infringement, misappropriation or other violation of Intellectual Property.”
 - Avoid breaches based on complaints not yet served
 - Knowledge-qualify for claims for which process or other comparable notice has not been served on or delivered to Seller
 - Consider insuring against breach of representations

Non-Infringement

To the Knowledge of the Company, the use of the Owned Intellectual Property by the Company in connection with the operation of the Company Business as currently conducted, does not infringe any other Person's material Intellectual Property in any material respect. To the Knowledge of the Company, no Person is engaging in any activity that infringes any Owned Intellectual Property, except with respect to any infringement of Registered Owned Intellectual Property that may arise out of any Person's registration of Internet domain names or use of keywords on the Internet. The Purchaser acknowledges that the representations and warranties set forth in this Section are the only representations and warranties the Company makes in this Agreement with respect to any activity that constitutes, or otherwise with respect to, infringement, misappropriation or other violation of Intellectual Property.

Non-Infringement

~~To the Knowledge~~ The Company, its products, processes and services, and the operation of the Company, ~~the~~ Business and use of the ~~Owned~~ Company Intellectual Property ~~by the~~ Company IT Assets and Company Products in connection ~~with the operation of the Company Business as currently conducted, does therewith, do~~ not infringe, misappropriate or otherwise violate or conflict with any other Person's ~~material~~ Intellectual Property ~~in any material respect.~~ ~~To the Knowledge of the Company, no~~, and has not done so in the past six (6) years. No Person is engaging, or has engaged in the past six (6) years, in any activity that infringes ~~any Owned Intellectual Property, except with respect to any infringement of Registered Owned Intellectual Property that may arise out of any Person's registration of Internet domain names or use of keywords on the Internet. The Purchaser acknowledges that the representations and warranties set forth in this Section are the only representations and warranties the Company makes in this Agreement with respect to any activity that constitutes, or otherwise with respect to, infringement, misappropriation or other violation of,~~ misappropriates or otherwise violates or conflicts with any Company Intellectual Property.

Protection Measures / Trade Secrets

- To qualify as a trade secret, information must be the subject of efforts that are reasonable under the circumstances to maintain its secrecy
- A representation/warranty is heavily relied on because it is difficult to diligence trade secrets
- Level/quality of protective measures
- Unauthorized disclosure or use of confidential information or trade secrets
- Use of confidentiality agreements and non-disclosure agreements

Protection Measures / Trade Secrets

To the Knowledge of the Company, the Company has taken measures to maintain the confidentiality and value of all material confidential information necessary for the operation of the Company Business as currently conducted. To the Knowledge of the Company, no material confidential information has been disclosed by the Company to any Person except pursuant to non-disclosure agreements that obligate that Person to maintain the confidentiality of the confidential information and confidential Company Intellectual Property.

Protection Measures / Trade Secrets

~~To the Knowledge of the Company, the Company has taken measures to maintain the confidentiality and value of all material confidential information necessary for the operation of the Company Business as currently conducted. To the Knowledge of the Company, no material confidential information has been disclosed by the Company to any Person except pursuant to non-disclosure agreements that obligate that Person~~The Company has taken all reasonable measures consistent with industry best practices to maintain the confidentiality of the confidential information and value of all confidential information used or held for use in the operation of the Company Business, including all source code that is Company Software and other confidential Company Intellectual Property. No confidential information or confidential Company Intellectual Property have been disclosed by the Company to or discovered by any Person except pursuant to non-disclosure agreements that (i) obligate that Person to maintain the confidentiality of the confidential information and confidential Company Intellectual Property, (ii) impose perpetual confidentiality obligations with respect to trade secrets and personally identifiable information, and (iii) are valid, subsisting, in full force and effect and binding on the parties thereto, and with respect to which no party thereto is in material default thereunder and no condition exists that with notice or the lapse of time or both could constitute a material default thereunder.

Employee and Contractor Agreements

- Status and validity of existing agreements
 - Not only current agreements with the Target, but also agreements with previous employers
- Ownership of employee- and contractor-developed IP
 - Consider default rules of IP ownership and the types of IP that are important to the Target
 - Employee-developed IP
 - Copyrights: work made for hire
 - Patents: employed-to-invent, “shop right”
 - Contractor-developed IP
 - Typically requires written assignment
 - Agreements to assign versus present assignment of future right

Employee and Contractor Agreements

To the Knowledge of the Company, no employee of the Company is in default or breach of any employment agreement, non-disclosure agreement, assignment of invention agreement or similar agreement relating to the protection, ownership, development, use or transfer of any Intellectual Property. To the Knowledge of the Company, the Company is a party to agreements with all current employees that have been engaged by the Company to develop Intellectual Property, pursuant to which agreements the Owned Intellectual Property is owned by the Company and/or vests in the Company by operation of Law.

Employee and Contractor Agreements

~~To the Knowledge of the Company, no~~ No employee, contractor or agent of the Company is in default or breach of any employment agreement, non-disclosure agreement, assignment of invention agreement or similar agreement relating to the protection, ownership, development, use or transfer of ~~any~~ Company Intellectual Property or, to the Company's Knowledge, any other Intellectual Property. ~~To the Knowledge of the Company, the.~~ The Company is a party to valid and enforceable written agreements with all ~~current~~ employees Persons that have ~~been engaged by the Company to develop~~ conceived, developed, acquired or created Intellectual Property for the Company, pursuant to which agreements the ~~Owned~~ entire and unencumbered right, title and interest in and to that Intellectual Property is ~~owned by~~ assigned to the Company and/or vests in the Company by operation of Law.

Effect on Buyer

- Representation/warranty primarily addresses the risk of:
 - Licenses and other encumbrances that do not mature until Target is sold
 - Broad out-licenses or other obligations of Target that bind Target “and its affiliates”
 - After Closing, Buyer and its affiliates typically become Target’s affiliates
 - Change of control or assignment fees / increased royalties

Effect on Buyer

To the Knowledge of the Company, the consummation of the Transactions will not, pursuant to the terms of any Material Contract, result in the creation of any Lien (other than Permitted Liens) on, any material Owned Intellectual Property.

Effect on Buyer

~~To the Knowledge of the Company,~~ Neither the consummation of the Transactions ~~will not,~~ nor the negotiation, execution, delivery or performance of the Transaction Documents will result in any of the following pursuant to the terms of any ~~Material Contract, result in~~ Contract to which Company is a party or by which its properties or assets are bound: (i) the grant, license or assignment to any Person of any interest in or to, the modification or loss of any rights with respect to, or the creation of any Lien ~~(other than Permitted Liens) on, any material Owned Intellectual Property~~ on, any Company Intellectual Property or any Intellectual Property owned by or licensed to Purchaser or its Affiliates prior to Closing, or (ii) Purchaser or its Affiliates, or the Company, being (A) bound by or subject to any non-compete or licensing obligation, covenant not to sue, or other restriction on or modification of the current or contemplated operation or scope of its business, which that Person was not bound by or subject to prior to Closing, or (B) obligated to (1) pay any royalties, honoraria, fees or other payments to any Person in excess of those payable prior to Closing, or (2) provide or offer any discounts or other reduced payment obligations to any Person in excess of those provided to that Person prior to Closing.

Free / Open Source Software

- Buyer's concern:
 - Do Target's proprietary software products incorporate open source code in a manner that could jeopardize proprietary status of Target's software before and/or after Closing?
- Schedule of open source software
- Compliance with open source software licenses
- Representation/warranty regarding legal ramifications of that use

Open Source Software

To the Knowledge of the Company, the Company has complied in all material respects with the terms of all Contracts governing the use or distribution of the Public Software. To the Knowledge of the Company, the Company has not received any request from any Person to license, disclose or distribute the source code for any Company Product pursuant to a license governing Public Software.

Open Source Software

~~To the Knowledge of the Company,~~ Except as set forth in the Disclosure Schedule, no Public Software is, forms part of, has been used in connection with the development of, is incorporated into or is required to use, or has been distributed with, in whole or in part, any Owned Software or Company Product. With respect to the disclosed items, (i) the Disclosure Schedule identifies the applicable Public Software, the Company IP Agreement governing the use of the Public Software, the particular Owned Software and/or Company Product in or with which the Public Software is used, the general nature of any modifications to the Public Software in the Owned Software and/or Company Products, and whether those modifications were made by the Company, or by another Person, (ii) the Company has complied ~~in at~~ all ~~material respects~~ times with the terms of all Contracts governing the use or distribution of the Public Software. ~~To the Knowledge of the Company, the,~~ and (iii) no use of or activities with respect to the Public Software by the Company, or its contractors, customers, licensees or end users, (A) requires the licensing, disclosure or distribution of any Software (other than the Public Software) or Company Intellectual Property to any other Person, or (B) prohibits or limits the (1) receipt of consideration in connection with licensing or otherwise distributing any Company Products, or (2) imposition of contractual restrictions on the rights of licensees or other recipients to decompile, disassemble or otherwise reverse-engineer any Company Software. The Company has not received any request from any Person to license, disclose or distribute the source code for any Company Product pursuant to a license governing Public Software.

Privacy Matters

- Concerns the collection and protection of personal information
- Broad compliance with law representation/warranty may be difficult for certain Sellers to give
 - State laws vary
 - EU data protection directive
- Compliance with stated data protection policies and website privacy policies
- Compliance with Payment Card Industry Data Security Standard (PCI DSS)
- Has the Company received complaints and/or notices from the Government or other third parties?

Privacy Matters

To the Knowledge of the Company, the operation of the Company Website by the Company, and the use, collection, storage and dissemination of personally identifiable information, customer and user data, and other data and content (“Data”) in connection therewith or otherwise in connection with the Company Business as presently conducted do not violate any applicable US Laws (collectively, “Privacy Laws”). The Company has (i) posted a privacy policy, or a link thereto, governing its use of Data (“Privacy Policy”) on all user-facing pages on the Company Websites, and (ii) to the Knowledge of the Company, complied in all material respects times with the Privacy Policy. To the Knowledge of the Company, there is no material action or claim pending, asserted or threatened in writing by or against the Company alleging any violation of any Privacy Laws. The consummation of the Transactions will not cause a violation of, or require the consent, waiver or authorization of or declaration, filing or notification to any Person under the Privacy Policy. To the Knowledge of the Company, the Company has taken measures to protect material Data collected or accessed in the operation of the Company Business as currently conducted.

Privacy Matters

~~To the Knowledge of the Company, the~~ The operation of the Company ~~Website by~~ IT Assets ~~by or on behalf of~~ the Company, and the use, collection, storage and dissemination of personally identifiable information, customer and user data, and other data and content (“Data”) in connection therewith or otherwise in connection with the Company Business ~~as presently conducted, have not violated, and~~ do not violate, any applicable ~~US~~ Laws ~~or any Person’s privacy, publicity or confidentiality rights~~ (collectively, “Privacy Laws”). The Company has (i) posted a privacy policy, or a link thereto, governing and disclaiming liability for its use of Data (“Privacy Policy”) in a clear and conspicuous location on all user-facing pages on the Company Websites, and (ii) ~~to the Knowledge of the Company,~~ complied in ~~at~~ all ~~material respects~~ times with the Privacy Policy. ~~To the Knowledge of the Company, there is no material~~ and all other rules, policies and procedures the Company has established concerning Data (all of the foregoing, the “Privacy Rules”). There is no action or claim pending, asserted or threatened ~~in writing~~ by or against the Company alleging any violation of any Privacy Laws. ~~The~~ or Privacy Rules. Neither the consummation of the Transactions nor the negotiation, execution, delivery or performance of the Transaction Documents will ~~not~~ cause a violation of, or require the consent, waiver or authorization of or declaration, filing or notification to any Person under ~~the, any~~ Privacy Policy. ~~To the Knowledge of the Company, the~~ Laws or Privacy Rules. The Company has at all times taken reasonable measures ~~to protect material~~ consistent with industry best practices to ensure that all Data collected or accessed in the operation of the Company Business ~~as currently conducted is~~ protected against unauthorized access, use, modification, disclosure or other loss, and no such loss has occurred.

Validity / Enforceability

- Valid and enforceable vs. adjudged invalid or unenforceable
 - Patent / trademark / copyright marking
 - Exercise of quality control for trademarks
- In good standing with government or other IP registrar
 - Compliance with IP office rules
- Subject of any order, judgment, or settlement

Validity / Enforceability

To the Knowledge of the Company, the Owned Intellectual Property is (i) valid, subsisting and enforceable, and (ii) not subject to any order, judgment, injunction, decree, ruling or agreement that would materially adversely affect the validity or enforceability of, or the Company's use of or rights to, the Owned Intellectual Property.

Validity / Enforceability

~~To the Knowledge of the~~ The Company, ~~the Owned~~ Intellectual Property is (i) valid, subsisting and enforceable, ~~and (ii)~~ (ii) currently in compliance with all legal requirements necessary to maintain the Company Intellectual Property as valid, enforceable and in good standing, and (iii) not subject to any order, judgment, injunction, decree, ruling or agreement that would ~~materially~~ adversely affect the validity or enforceability of, or the Company's use of or rights to, the Company Intellectual Property. The Registered Owned Intellectual Property is currently in compliance with all legal requirements necessary to record and perfect the Company's interest in, and the chain of title of, that Intellectual Property. The Company has (A) enforced and currently enforces quality control measures adequate to maintain the validity and enforceability of all Trademarks it has licensed or otherwise permitted any other Person to use, and (B) made no material misrepresentations in, and has complied with the duty of candor and disclosure to the United States Patent and Trademark Office and all other applicable Governmental Authorities with respect to, all applications for registration included in the Registered Owned Intellectual Property.

Quality of IT Assets

- What are Company IT Assets?
 - Software, systems, servers, computers, hardware, firmware, middleware, networks, data communications lines, routers, hubs, switches and all other information technology equipment, and all associated documentation owned or used by the Target
- Sufficiency and adequacy of the Company IT Assets
- Backup, security and disaster recovery measures
- Unauthorized access and material failures
- Bugs, defects and viruses

Quality of IT Assets

To the Knowledge of the Company, the material software owned by the Company is adequate for the operation of the Company Business as currently conducted. To the Knowledge of the Company, the software owned by the Company is free from material bugs and other material defects, and have not materially malfunctioned or failed within the past twelve months in a manner that materially adversely affected the Company Business. The Company has implemented backup, security and disaster recovery measures and technology consistent and, to the Knowledge of the Company, no Person has obtained unauthorized access to any material Company IT Assets.

Quality of IT Assets

~~To the Knowledge of the Company, the material software owned by the Company is adequate for~~The Company IT Assets are adequate for, and operate and perform in all material respects in accordance with their documentation and functional specifications and otherwise as required in connection with, the operation of the Company Business ~~as currently conducted. To the Knowledge of the.~~ The Company, ~~the software owned by the Company is~~ IT Assets are free from material bugs and other ~~material~~ defects, ~~and~~ have not materially malfunctioned or failed within the past ~~twelve months in a manner that materially adversely affected the Company Business~~three years, and do not contain any Viruses. The Company has implemented backup, security and disaster recovery measures and technology consistent with industry best practices, and, ~~to the Knowledge of the Company,~~ no Person has obtained unauthorized access to any ~~material~~ Company IT Assets.

Other IP Provisions

- Absence of changes representation / warranty
- Interim operating covenants
- Transitional trademark license
- Closing conditions
- Ancillary agreements
 - Transition Services Agreement
 - IP License / Cross-License Agreements
 - Supply Agreements
 - Development Agreements

Interim Operating Covenants

- Seller will want leeway to continue operating the Business
- Buyer wants to protect basis of value
 - Protection and maintenance of IP
 - Restrictions on licenses not granted in the ordinary course of business
 - Restrictions on joint development work
 - Restrictions on disclosure of confidential information
 - Notification regarding IP-related claims

Interim Operating Covenants

The Company shall not:

(i) sell, assign or grant any security interest in, to or under any material Company Intellectual Property, (ii) grant to any Person any license with respect to any Company Intellectual Property or Company IT Asset, except in the ordinary course of business, (iii) disclose any material confidential information to any Person, other than in the ordinary course of business.

Interim Operating Covenants

The Company shall not:

(i) abandon, disclaim, dedicate to the public, sell, assign or grant any security interest in, to or under any ~~material~~ Company Intellectual Property, Company IT Asset or Company IP Agreement, including failing to perform or cause to be performed all applicable filings, recordings and other acts, or to pay or cause to be paid all required fees and Taxes, to maintain and protect its interest in the Company Intellectual Property, Company IT Assets, and Company IP Agreements, (ii) grant to any Person any license, or enter into any covenant not to sue, with respect to any Company Intellectual Property or Company IT Asset, except in the ordinary course of business; ~~(iii) disclose any material~~ consistent with past practice, (iii) develop, create or invent any Intellectual Property jointly with any Person, (iv) disclose or allow to be disclosed any confidential information or confidential Company Intellectual Property to any Person, other than in the ordinary course of business, to the Company's or the Subsidiaries' employees that are subject to confidentiality or non-disclosure covenants protecting against further disclosure, or (v) fail to notify Purchaser promptly of any infringement, misappropriation or other violation of or conflict with any Company Intellectual Property of which the Company or any Subsidiary becomes aware and to consult with Purchaser regarding the actions (if any) to take to protect such Company Intellectual Property.

Relevant Practical Law and Fried Frank Resources

- E-mail tech@friedfrank.com or visit us.practicallaw.com for copies of the following materials:
 - Intellectual Property: Stock Purchases and Mergers
 - Intellectual Property: Asset Purchases
 - Transitional Trademark License Clauses (Pro-buyer)
 - Transitional Trademark License Clauses (Pro-seller)
 - Data as IP and Data License Agreements
 - Webinar: Intellectual Property in M&A Transactions
 - Webinar: Data as Intellectual Property: Drafting and Negotiating Data Agreements
 - Webinar: Navigating the IP Deal: Technology License and Services Agreements for the Non-Specialist

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Questions