

## IP Due Diligence: The Five Questions You Must Ask in Corporate Transactions

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*Q: When would a company undergo intellectual property due diligence?*

*Konstantin Linnik:* Any corporate transaction involving IP assets necessitates diligence: merger, acquisition, IPO, investment (such as a venture capital financing), in-license, partnering, co-development, or distribution agreements. The buyer who is evaluating the Target could be a licensee, business partner, investor, banker, or underwriter.

IP due diligence analyzes patent issues, trade secrets, trademarks, copyrights, freedom to operate, IP litigation, licensing, reps, warranties, disclosures, and even employment agreements. The process will examine the Target's IP, such as how well the existing and potential IP protects the Target, what projected revenues will be based on the exclusivity period and geographic scope, and the current and projected expenses, including prosecution, maintenance, royalties, and enforcement. Because the diligence is expensive and is typically charged off as the overall transactional cost, the diligence is conducted as close to pre-closing as possible.

*Q: What are the must-ask questions in the diligence process?*

*KL:* There are five essential questions that must be asked at the outset. The first is to identify all owned and/or licensed patents and applications, along with their status and correspondence to products. Second, is the Target aware of any information that can make them unpatentable, invalid, or unenforceable? Third, ask to provide documentation that the Target owns these patents or has licensed rights. Fourth, is the Target aware of any third party patents or applications that may be infringed, has the Target received a notice from a third-party, or obtained a formal or informal opinion from counsel in the past? Finally, has the Target been involved in or anticipates any IP-related dispute? Independent verification follows.

*Q: How can IP due diligence affect a transaction?*

*KL:* The impact can be tremendous. If diligence uncovers fraud, infringement, or no documented ownership of intellectual property, then the deal may be called off. Lesser potential consequences include price and term adjustments, special indemnities for breach of reps and warranties, M&A or patent infringement insurance, or deal earn-outs.

*Q: What is the significance of indemnifications, reps, and warranties?*

*KL:* All too often, these provisions are viewed as “boilerplate” and their distinctions are overlooked – be careful not to fall into that trap. These provisions are critical because they allocate risks, force the Target to focus on issues, and, most importantly, warranties are fact-specific. A warranty is a promise that a proposition of fact is true and therefore presumed to be material. A representation is a presentation of fact made to induce someone to act. Indemnity is a duty to make good on any loss, damage, or liability incurred by another.

*Q: How can problems that are uncovered during IP due diligence be fixed?*

*KL:* There are several steps to undertake in the remediation process: execute and record assignments, amend licenses, file claim amendments, and pursue continuations, reissues, and re-exams if necessary. These actions may occur post-closing or be a condition of closing. Changing your IP counsel is often a necessity to move forward not only with correcting deficiencies, but also to develop and implement fresh IP strategy.

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