**Introduction to Intellectual property and information technology**

This section deals with the due diligence enquiries that should be made relating to intellectual property rights and information technology in corporate transactions.

**Introduction to Intellectual Property rights**

A right in intellectual property (**‘IP’**) is a right to prevent others from using assets or ideas that have been created by a person or company, without the creator, or owner’s permission. IP can be essential to a company’s business as it might relate to branding, specialist know-how or key product.

Importantly, whilst some IP rights will be owned by the target, there may be some IP rights that are not owned but are merely used by the target under **licences granted by third parties**. These licensed IP rights may be very important to the target’s business activities.

IP rights may be registered or unregistered

**Registered IP rights**: Companies tend to keep more accurate records about registered IP rights. It is also possible to conduct searches on public registers (such as the UK Intellectual Property Office).

**Unregistered IP rights**: are much more difficult to research because there are no public registers to search.

The definition of IP in the acquisition agreement will usually refer to all IP owned by the target worldwide. Where **other jurisdictions** are relevant / important, local legal advice should be obtained to ensure that the target has all the IP rights it needs to carry on its activities in those jurisdictions.

**Common types of IP rights**

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| **IP Right** | **Description** | **Registered or Unregistered** |
| Patent | A patent is a monopoly right to use and exploit an invention for a limited period. | Registered |
| Trademark | A trademark is a sign capable of distinguishing goods or services of one undertaking from those of another, for example a logo. | Registered |
| Design right | A 'design' can be registered for ‘the appearance of the whole or a part of a product resulting from the features of the lines, colours, shape, texture or materials of the product or its ornamentation’. | Unregistered |
| Copyright | Copyright in a work allows its owner to prevent others from copying the work, provided the work is ‘original’. | Unregistered |
| Know-how | Trade secrets and confidential information. | Unregistered |
| Database rights | This right recognises the investment that is made in compiling a database and protects the contents of that database. | Unregistered |

**IP due diligence**

**Key action points in relation to registered IP rights:**

1. Seek confirmation that all registrations and applications for registration are in the right name and that key brands and patents are registered in the relevant markets by carrying out searches of the appropriate intellectual property registers.
2. Check when IP rights will expire and confirm that any and all renewal fees have been paid.
3. Seek confirmation that the validity of the IP rights has not been challenged by third parties and that the seller is not aware that any such rights have been infringed by third parties. Check whether there are any claims or disputes with third parties concerning any of the IP rights.

**Key action points in relation to unregistered IP rights**:

1. Try to identify all important copyright works owned and used by the target.
2. If an unregistered trademark is considered especially important, the buyer may ask the seller to apply for registration of the trademark prior to the acquisition.
3. Review the employment contracts and any consultancy agreements to establish who owns the copyright in any works created by staff. Copyright in any work created by an employee in the course of their employment is owned by the employer unless the contract of employment states otherwise. Copyright in any work created by a consultant will usually belong to the consultant unless otherwise agreed in the relevant consultancy agreement.
4. Enquire about the target’s documentation and record-keeping procedures; such information is vital to establishing not only the existence and ownership of any unregistered rights but it will also indicate the likely ease of asserting or defending such rights.

**IP due diligence: IP licences**

**Key action points in relation to IP licences granted by third parties:**

1. Obtain copies and check terms to determine:
   1. when the licences expire;
   2. any unusual or particularly onerous terms;
   3. If the transaction is an asset sale: are there any restrictions on assignment? Would the sale trigger termination of the licence?;
   4. If the transaction is a share sale: does the licence contain a change of control clause and, if so, what will the consequences be?

**Key action points in relation to IP licences granted to third parties:**

1. If any licences have been granted to third parties to use IP rights:
   1. seek confirmation that the target actually owns these rights;
   2. what are the terms of these licences? Will the terms prevent the target from using the IP rights?
2. If the target has been indiscriminate in allowing third parties to use its IP rights, this may affect the value or even the validity of those rights.

**IP rights used by other companies in the seller’s group**

If the target requires use of IP rights after completion which are also used by companies in the seller’s group, this will have to be negotiated with the seller.

* A **brand name** may be used to identify all the products sold within the seller’s group and this may be the trading name of the seller's retained businesses after completion.   
  If the target wants to continue to use this, the seller may grant the target a short-term licence agreement.
* Separating out the IT systems and software to transfer to the target can be difficult. So, it may be necessary to purchase **duplicate IT systems and software** for the target’s ongoing use.
* Trade marks may be used by the target and by companies in the seller’s group. If these group companies are using the trade marks on unrelated goods, it may be possible to **assign the trade marks** to the target so that it can use the trade marks for certain classes of goods whilst use by the group companies is restricted to other classes of goods.   
  Alternatively, a licence agreement  may be used.

**IT due diligence**

IP is closely linked with the ‘soft’ side of IT. Copyright subsists, for example, in the source code of software, in the HTML code for websites and in network diagrams. Domain names are often also brought under the IP umbrella (although they are not, strictly speaking, IP).

In addition, enquiries will need to be made regarding the computers, servers and other hardware that make up the target company’s IT systems themselves (to verify ownership, condition etc.). Equally, it will be necessary to examine the terms of any applicable maintenance contracts and any lease agreements.

IT is often a critical component of most businesses. Specialist IT lawyers or consultants will be responsible for conducting the due diligence on IT related matters.

**IT due diligence: Software**

* **Key action points in relation to software:**  
  Confirm who owns the copyright in any important software. Ownership can be determined by reviewing the relevant contracts. Have the relevant contracts been disclosed by the seller? Identify what open source software is used by the target, where it originates from and the terms of the open source software licences.
* Confirm how much of the software is licensed from third parties. If any software is licensed, find out the fees payable by the licensees, review the termination provisions of the licences and establish whether such licences can be assigned or novated (for an asset sale) or whether they may be affected by a change of control (for a share sale). Seek confirmation, also, that the target’s use of any licensed software is compliant with the terms of the licence.
* If software is licensed, confirm the target’s access rights to the source code in order to update the software and any rights it has if the licensor enters into an insolvency procedure or does not comply with its obligations under the licence.
* Under what circumstances and on what notice may the licence be terminated?

**IT due diligence: Website design and domain names**

**Key action points in relation to website design and development:**Seek confirmation regarding ownership in the copyright in the design and development of the website.

**Key action points in relation to domain names:**

* Seek confirmation that the target owns the key domain names that correspond with the important brand names of the business. All registrations should be confirmed and/or checked to ensure they are up to date and that they are not subject to any dispute.
* Enquiries should be made of relevant registries. For example: ‘Nominet’ is the registry for all .co.uk domain names.

**IT due diligence: Disaster recovery and maintenance**

**Key action points in relation to disaster recovery, maintenance and data protection:**

* Enquire whether the target has any disaster recovery systems in place.  Most businesses will have some kind of back-up plan to provide for business continuity if there is an unexpected failure of any of its systems (from software solutions through to full-service back up centres).
* Enquire whether any third party provides maintenance for the systems and, if so, seek confirmation of its fees and that all fees are paid up to date.
* Confirm that the target is complying with data protection legislation and that the buyer will be able to use personal data in the way it wishes going forward. The issue is of special importance for consumer businesses where much value may depend on the ability to process customers’ personal data in particular ways. See the element on Data Protection for more information.

**Summary**

* As a corporate solicitor working for a buyer in a transaction, you need to be aware of the types of IP rights that the target is likely to be using.
* IP rights can be registered or unregistered. The target is more likely to have documentation and records for registered IP rights than for unregistered rights.
* Where the target owns IP rights in other jurisdictions, local legal advice may be required to establish the rights that the target has.
* It is common for companies to hold licences to use IP rights that they do not own. Particular care must be taken to establish the terms of these licences (including what the termination provisions are).
* IT is an integral part of most businesses and therefore detailed enquiries must be made to establish what IT systems the target uses in its business and what IT it will require following completion.