

IPAA ADVANCED TRAINING COURSE:

M&A, INVESTMENT DEALS INTELLECTUAL PROPERTY DUE DILIGENCE



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Chair of IP @ NBA

(Director of the ILPO, Commissioner of Patents, Designs & Trademarks, 2011 – 2017)

Normative Framework

- Dealing in Good Faith
- Public Order
- Allocation of Risk



Caveat Emptor !

מה אומרת הפסיקה לגבי בדיקות נאותות?

- תובע שכשל בבדיקת הנאותות יתקשה לדרוש סעדים זמניים
- צד שכשל בבדיקת הנאותות עלול לפספס וויתורים על זכויות, אותן לא יוכל לאכוף בהמשך
- כשלים בבדיקת נאותות עשויים להיתפס כאשם תורם בתביעה שעניינה רשלנות של הצד המגלה
- כשלים בבדיקת נאותות עשויים להפחית את גובה הסעד/העונש בתביעה שעניינה מרמה של הצד המגלה.

[מעבר לשאלות של טעות בעובדה]

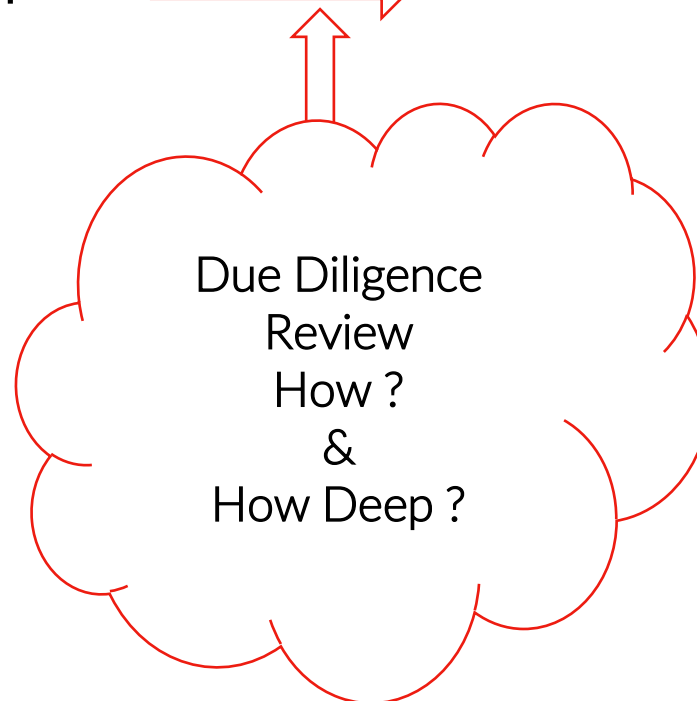
"... המנצל תמימותו של אדם כדי למכור לו במרמה מוצר שאין תוכו כבד, אינו יכול להיבנות מתמימותו של הקורבן כהגנה מהרשעה. נהפוך הוא, אפשר לומר כי מעשיו אף לוקים בחוסר מוסריות חריף יותר בשל כך. **אותו רציונל חל גם כאשר הקורבן הינו חברת הון סיכון. עם זאת, בסיטואציה שלפנינו, ה"תמימות" שהציגה אמיקום, אף שאינה מעלה שאלות בדבר עצם קיום המרמה, יכולה להעלות תהיות לגבי אופיו של הקשר הסיבתי בין מעשה המרמה לבין היקף ההשקעה.** האין זה אפשרי לומר, כי **העדר בדיקה מעמיקה מצד המשקיעים אודות האספקטים הטכנולוגיים המובהקים של צמ"מ ומוצריה, מעיד על כך שלא זה היה הגורם היחיד להשקעה?** האם לא ניתן לתהות שמא, אף לולא מצגי השווא, עדיין הייתה אמיקום משקיעה בצמ"מ – בהנחה שמוצריה עובדים – אך הייתה מעריכה את שוויה כפחות? האם אין יסוד לומר כי חלק מסכום ההשקעה בפועל אכן משקף יתרונות אמיתיים הגלומים במניותיה של צמ"מ?" (ע"פ 1242/06 ניסים צור נ' מדינת ישראל, סב(2) 271 (2007), סעיף 34 לפסק דינו של השופט חשין)

IP as Chattle?

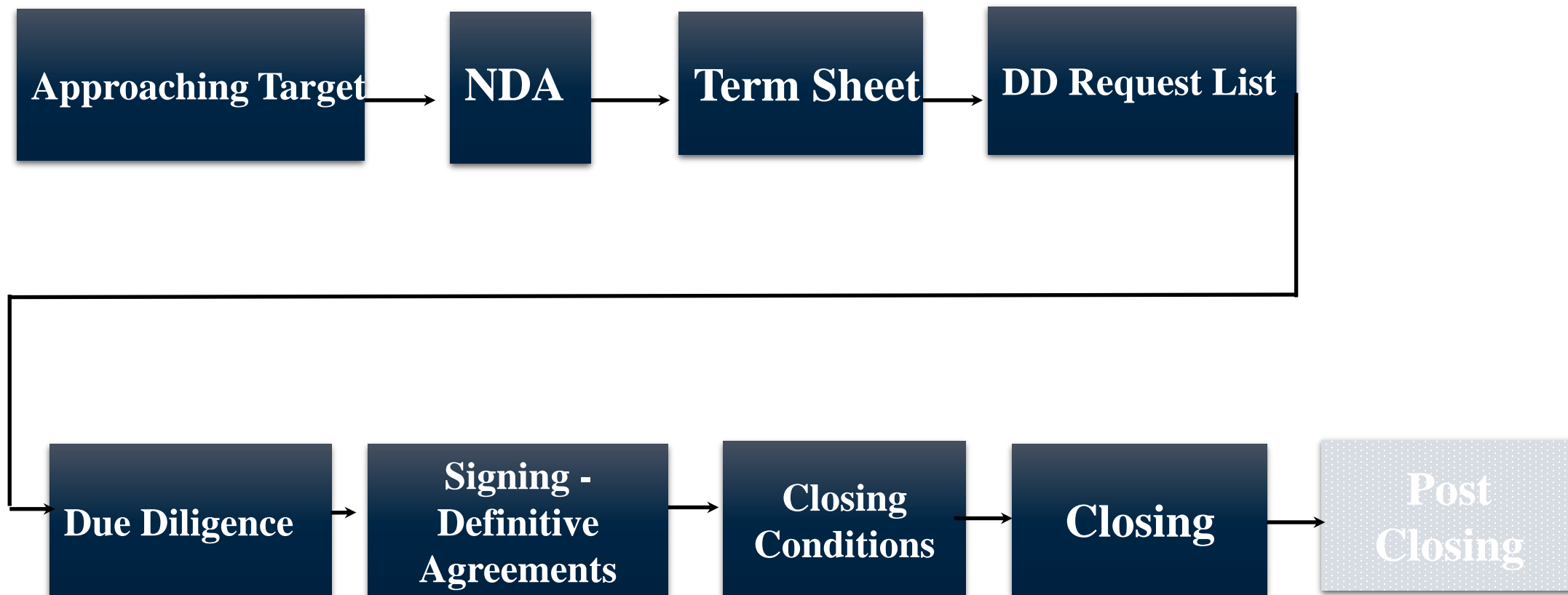
The Problem of verifying/checking IP



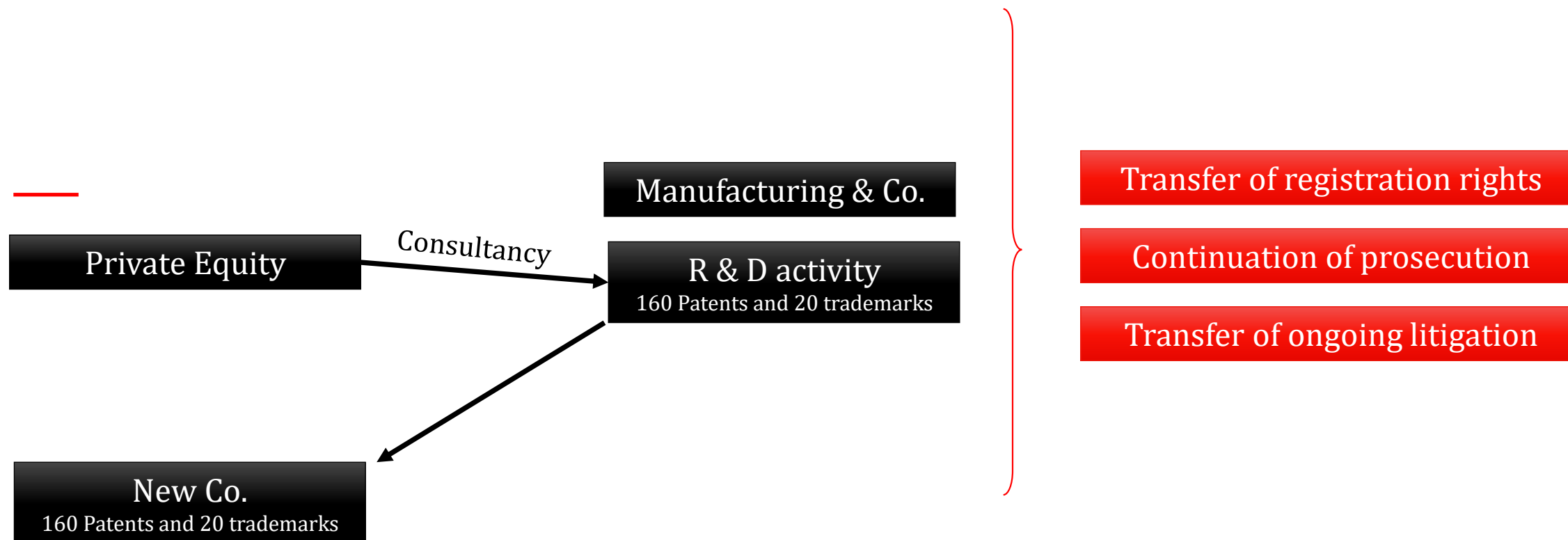
Warranties and Liabilities



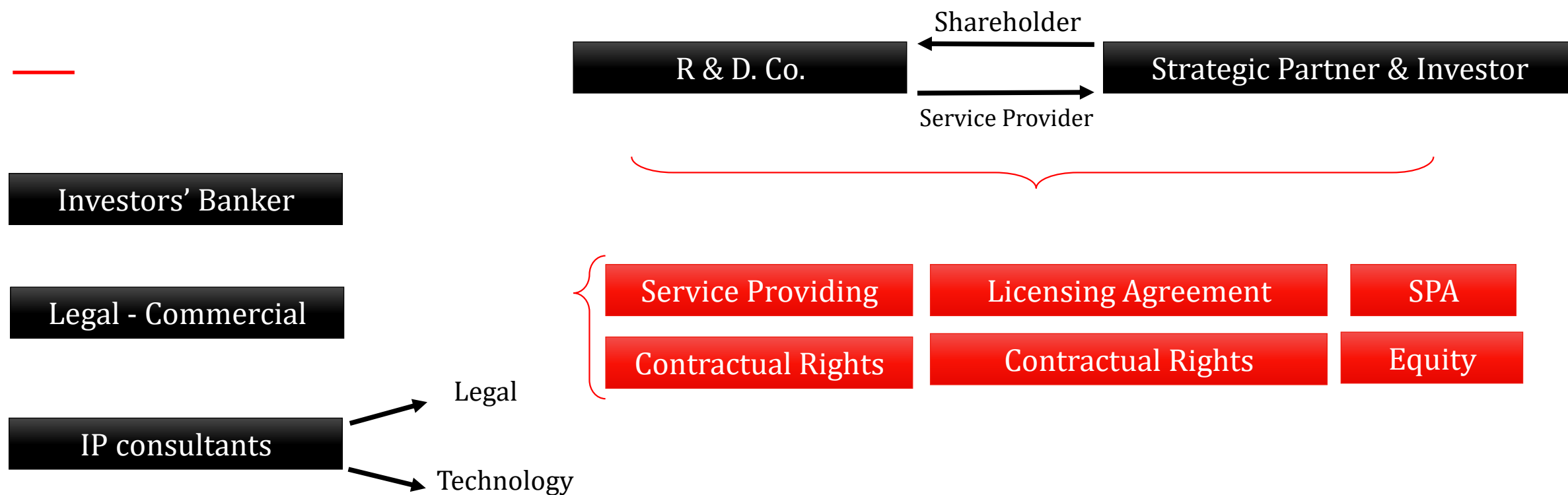
THE TRANSACTION – STEP BY STEP



Transactions aren't simple 1



Transactions aren't simple 2



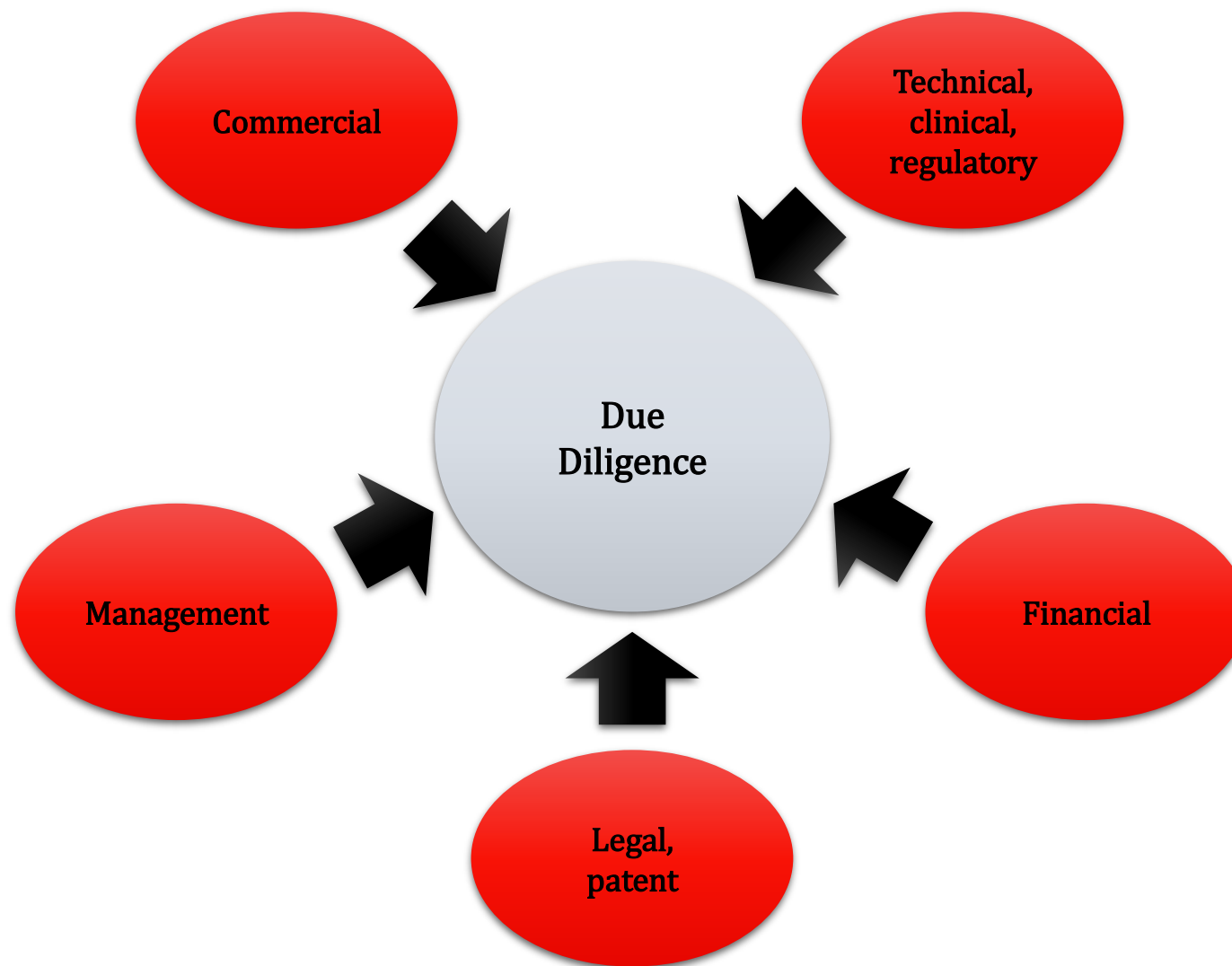
Types of Mergers and Acquisitions

Vertical	<ul style="list-style-type: none">▪ A vertical merger or acquisition is where the two companies operate at different stages of the supply chain. So this might involve one company purchasing its supplier, or the supplying company purchasing the firm it sells to.
Horizontal	<ul style="list-style-type: none">▪ A horizontal merger or acquisition is where the two joining companies operate in the same market, selling similar products
Conglomerate	<ul style="list-style-type: none">▪ A conglomerate merger or acquisition is where two companies from completely different industries join together
Concentric	<ul style="list-style-type: none">▪ A concentric merger or acquisition is where two companies operate in the same industry and have the same customer, but operate different products. These are generally complementary goods.

Imbalances

Differing Expectations	<ul style="list-style-type: none">▪ Different views of each company's value▪ Companies have unique informational asymmetries
Lack of Information	<ul style="list-style-type: none">▪ Product value is often uncertain▪ acquirer will not have full visibility into the licensed technology and may not be able to accurately predict its marketplace value<ul style="list-style-type: none">• Critical tacit information remains with out-licensor/seller• In-licensee/acquiror may not have experience with complexities of the licensed IP
Rush	<ul style="list-style-type: none">▪ Technology acquired as part of broader M&A transaction typically receives more deliberation

Due Diligence Players



THE PURPOSE

Investments/M&A transactions:

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- Part of a process – business, legal and accounting due diligence.
 - Factual inquiry – knowing the target.
 - Enhancing our client's ability to make a reasoned decision as to whether or not to pursue the transaction.
 - Helping the client understand and assess risks associated with the transaction.
 - Making structural or contractual accommodations to “work around” identified problems.

THE BASICS

- Understand the structure and terms of the transaction:
 - Read Term Sheet/LOI
 - Review (Fully) Available IP Status
 - Understand deal structure – VC investment, stock or asset purchase (assignment vs. change of control), merger (what type), venture lending, Licensing
 - Post closing – changes to business operations, planned divestitures
- Public Companies – review public information:
 - Stock Exchange Data
 - Company Reports
 - Target website – press releases
- Publicly Available IPR – PTOs / Search Engines
- Discuss with Client :
 - Client's concern for the transaction and what client believes are the main issues to focus on.

THE PROCESS

- Preparing the initial document request list:
 - Form due diligence request list – may change due to type of business.
 - Ask the company to send materials pursuant to index.
 - Company needs to specify materials missing on the list.
- Reviewing documents:
 - Keep in mind the transaction structure.
 - Review issues list for types of documents/agreements.
 - Keeping a list of all documents reviewed (name of document, parties, date).
- Preparing due diligence report – preliminary/on-going/final:
 - Identify discrepancy between state of affairs and client's perception.
 - Highlight anything that presents significant potential liabilities, affects the consummation of the transaction, interferes with client's business goals.

THE PROCESS

- Follow up questions/missing materials :
 - constantly evolving process (some areas will be of greater concern).
- Interview principals/relevant employees/IP Manager/IP Counsel ...
- Incorporating due diligence results into definitive agreements:
 - Representations and warranties, disclosure schedule consistent with due diligence findings.
 - Closing conditions (e.g., third party consents, executive employment agreements).
 - Indemnification, escrow.
 - Identify corporate “clean ups”.
 - Post closing covenants (e.g., directors and officers insurance, effectuating transfer of rights) .
- Review and comment on Disclosure Schedule.
- Due diligence process continues for the duration of the transaction – until signing.

REVIEWING DOCUMENTS – WHAT TO LOOK FOR

- Keep in mind the transaction structure.
 - Look for unusual terms – experience.
-
- **Determine Scope of Diligence – what is important for the transaction?**
 - Future revenues stream
 - New product launch expectations
 - ...

DISCLOSURE SCHEDULE

- Exceptions to representations and warranties.
- Information required by representations and warranties.
- Documents mentioned in the Disclosure Schedule and not reviewed – ask for them.
- Representations and warranties are heavily negotiated.
- Limit the scope of overly broad or vaguely worded disclosures.
- Limit cross-references.

IP DD LIST

- List of patents and patent applications, trademarks, (copyrights) by jurisdictions
- Search at PTOs
- List of infringement actions, disputes, threatened claims
- License Agreements:
 - In/Out Licensed intellectual property
 - Territory covered
 - Scope of grant – exclusive? Field-of-Use?
 - Sub-license rights
 - Payment/royalty terms
 - Indemnifications
 - Term and termination
 - Assignment; change of control
- Employee assignment/waiver
- Joint Owners
- Third Party Rights (Open Source, IIA, TTO ...)

Due Diligence in Licensing Transactions

- Diligence should go beyond confirmation of drug status and partner's financials
- Thorough diligence can alleviate information asymmetries
 - In-licensee can use diligence process to verify breadth and vulnerability of IP
 - Out-licensor can ensure that in-licensee has sufficient resources and expertise to develop and commercialize the product
- Brings thoroughness of M&A process to licensing transactions
 - Reduces risk of rush
 - Ensures transaction is thoughtfully structured
- With proper due diligence, parties are able to:
 - Provide the basis for a deal that will balance competing needs
 - Define future plans for the collaboration and avoid surprises at a later date
 - Have difficult conversations earlier in the relationship, rather than having issues surface later on

Deal-Specific Considerations

- **Data and Privacy law issues are increasingly prevalent**
 - Privacy rules under the CCPA (California Consumer Privacy Act) and/or GDPR (General Data Protection Regulation) may apply where personally identifiable information is involved
- **Software is becoming more prominent in all industries**
 - Emphasis on Copyright
 - Development “platforms” are highly software-driven
- **AI creating unique challenges**
 - Must consider rights of parties in data driving AI
 - Use of AI engines / AI services
- **SEPs**
- **Economic environment: pandemic (COVID-19) and trade-wars**
- **Entertainment Industry**
 - Clearance of rights

Deal-Specific Considerations (Cont'd)

- Academic technology transfer practices
 - They almost never sell IP, but only license
 - Mostly standard form but some leeway may be obtained
- Where collaboration raises joint ownership or cross-licensing issues, proprietary rights should be addressed
 - Where employees are involved, issues of service inventions according to the IL Patents Law should be mitigated
- Exclusive rights (in patents, designs and trademarks) require registration in order to be in force towards third parties
- Israel Innovation Authority (IIA) funding implications:
 - Collecting license fees for IIA-sponsored IP may warrant royalty payments to the IIA

Deal-Specific Considerations (cont'd)

Issue	Considerations	Options	Underlying Considerations <ul style="list-style-type: none"> • Current legal regime • Missing or conflicting licenses or legal rights
Data	<ul style="list-style-type: none"> • Sensitive data (e.g., PII, trade secrets) • Rights in data (ownership, use and access) • Storage of data (databank location) 	<ul style="list-style-type: none"> • Compliance with laws rep • Confidentiality rep • Specific privacy laws rep • PII rep • Extraterritorial covenants 	
Software	<ul style="list-style-type: none"> • Open source software • Escrow to third parties • IP embodied in the software • Security vulnerability • Bugs and design problems 	<ul style="list-style-type: none"> • Copy-left licenses rep • Escrow rep • Quality evaluation (review of code) • Access to employees maintaining the technology • Ongoing licensees and rights to updates 	
“Platform” Technologies	<ul style="list-style-type: none"> • Splitting assets (platform/candidates) • Hardware and software • Storage of source code and data 	<ul style="list-style-type: none"> • Red flag contract diligence of licensed IP • Maintenance covenant (IP and server upkeep) • Access rights 	
Artificial Intelligence	<ul style="list-style-type: none"> • Rights in data • Training data sets • Technical dependencies • Implicit bias 	<ul style="list-style-type: none"> • Control over data (past and future; physical control) • Access rights • Ownership rep (legal control) • Compliance with laws rep 	
Standard Essential Patents	<ul style="list-style-type: none"> • Identifying applicable patents and commitments • Relationships with licensors, licensees, SSOs, regulators • FRAND complexities 	<ul style="list-style-type: none"> • Deal structuring • Diligence 	
COVID-19	<ul style="list-style-type: none"> • Performance of the license • Enforcement issues • Compulsory licensing • Bayh-Dole compliance 	<ul style="list-style-type: none"> • MAE standard • Force majeure clause • Minimum royalty provision • Most favored licensee provision • IP enforcement provision • Compliance with laws rep 	

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THANK YOU!

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