If you are fortunate, you work in a bustling legal environment filled with excellent mentors who are dedicated to developing your skills in the areas of intellectual property, corporate transactions, and due diligence. These mentors have many years of experience dedicated to these fields and spend focused time with each junior attorney. This environment also has procedures in place to train their attorneys on critical thinking and issue spotting in transactions. Their database is rich with well-developed checklists used to help conduct due diligence, memos highlighting key issues to look for in transactions, and regular meetings to discuss updates in the case law. Plenty of one-on-one instruction is offered to help junior attorneys learn how to conduct due diligence and address difficult questions. There are also resources dedicated to teaching project management, effective communication, and methods to streamline transactions.

This book is for the rest of us.

The contributors of this book have a combined total of hundreds of years’ experience in the field of intellectual property. Collectively, they have run individual deals ranging in value from the tens of thousands to billions of U.S. dollars. They come from technical backgrounds ranging from electrical and chemical engineering to software development and pharmaceutical technology. They work in large law firms, small law firms, in house, or as solo practitioners. Despite these diverse backgrounds, they are united in one thought: the field lacks a practical guide on how to train an attorney on conducting effective, cost-efficient due diligence in the areas of intellectual property and technology. This book is
intended to be a do-it-yourself, rigorous, comprehensive intellectual property due diligence guide.

To start, we must ask: What is intellectual property and technology due diligence?

The broad category of *intellectual property* includes patents, trademarks, copyrights, and trade secrets, and all of the information and materials that may be protected by any of these categories. Intellectual property is one of the most valuable commercial assets in modern times. In 2015, intangible assets represented an estimated 84 percent of the S&P 500 companies’ value, compared to only 20 percent of S&P 500 companies’ value in 1982.1 Intangible assets comprise a large portion of that value and are generally credited as being essential to growing economies in developed and developing countries across the world.2 In G8 countries, copyright-based industries and interdependent sectors alone account for approximately 4 percent to 11 percent of gross domestic product (GDP); in the United States alone, they account for 11.09 percent of GDP.3 Licensing of intellectual property and technology is also a growing and significant portion of the economy, and in 2011 it was estimated as accounting for $180 billion.4

As a result, intellectual property has an ever-increasing role in business transactions and often is the driver in the deal. It is now common for corporations to acquire or finance others’ business units for intellectual property licensed royalties and revenue streams, for patent sales and/or potential enforcement or licensing of related patents, and for market-based investment strategies.

---

3. Id.
Yet the field of intellectual property is rife with land mines. Foundational laws in intellectual property have been significantly affected by recent decisions at the Supreme Court, Federal Circuit, and District Court levels, complicating the evaluation and valuation of intellectual property assets. The continued globalization of companies also affects intellectual property and forces attorneys to take an international view of intellectual property portfolios, particularly in the rapidly changing legal environment of Europe, Asia, and emerging countries.

Due diligence itself is the reasonable study of materials and information to satisfy a legal requirement. In the context of intellectual property and technology, it is the study of an organization’s intangible assets to determine what intangible assets are present, the risks and benefits associated with those assets, and whether the assets, risks aside, satisfy the business purpose of a proposed business transaction. To put it in simpler terms,
the purpose of due diligence is to see if the assets are a good fit for the acquirer or funder.

Due diligence is traditionally performed or run by transactional lawyers and financial advisors and may use subject matter experts on discrete parts of the deal, such as employment attorneys, government contract attorneys, environmental attorneys, and the like. When the deal scope involves a large amount of intellectual property or technology, then intellectual property attorneys are required to correctly assess the veracity of the intellectual property and technology to ensure that the business needs are being met. Ideally, a transaction that involves copyrights will involve persons with copyright experience and an understanding of how technological innovations challenge the current copyright laws. A transaction involving patents would ideally involve patent attorneys with technical expertise in the same technological sector as the subject patents and products. Given the complexity and depth of each area of intellectual property, subject matter expertise in each discipline is strongly recommended.

As the due diligence counsel, one should never blindly take the word of another on the intellectual property strength, scope, or relevance to the underlying technology. Instead, counsel should review the known information, conduct a separate analysis, and make an independent judgment as to the veracity and relevance of the intellectual property. The results of this analysis should also be clearly communicated to the business leaders so that the deal team can decide how the due diligence results impact the transaction. For instance, if due diligence counsel finds unfavorable facts about the intellectual property and/or its relation to the involved technology, then the deal leaders can decide how to use this information strategically. For instance, if the due diligence reveals that a key patent has less term time than originally contemplated, or that the golden product of the company infringes a suite of competitor patents, then the unfavorable findings are leverage for the acquirer or funding source to use against the seller/fundee. Less frequently, the process will reveal unanticipated benefits, such as foreign registrations that were previously unknown or extended
registration terms. In such an instance, the target intellectual property portfolio would justify a higher price than originally contemplated.

The finding of an intellectual property due diligence may also dictate how a deal may or must be structured. For instance, one may find that one deal structure breaches important, valuable inbound licenses, whereas another deal structure doesn’t affect the licenses at all.

The due diligence findings can also impact the mechanics of a deal. Acquisition documents always state the property at the heart of the deal and the contractual obligations and rights that are attached to the property. Due diligence is used to help both parties develop and agree upon the assets to be transferred, or manage risk through scoping the representations and warranties in the transaction documents.

The due diligence information can also assist the parties after the deal is closed. For instance, an acquiring company may plan to spin off and sell an acquired product division and its intellectual property upon realizing the high value players in other markets may place on the portfolio. The acquiring company may decide to sell certain patents to nonpracticing entities, with a license back. Liens may be applied for solely based on the intellectual property. In addition, due diligence findings can be used to facilitate business ventures, or to facilitate and expedite the integration of two firms by allowing acquiring management to understand the other party’s resource. Good management teams often work in parallel during a transaction event and use the due diligence information for deal pricing, structuring, documentation, and future planning.

The technical information that is protected as intellectual property often indicates in detail how a company runs its business. For example, a company with a large patent portfolio means that it invests time and money to gain a limited monopoly on the market. It also means that the company is running against a deadline—a twenty-year patent term—and thus must continue to innovate often to keep ahead of its competitors. A company that mainly protects its intellectual property as a trade secret
may have equally (or more) valuable intellectual property than the company with the patent portfolio. The trade secret-protected company functions under the belief that its intellectual property is difficult to reverse engineer, and its value is best obtained from not disclosing the information to the public. In contrast, a company’s having many pending or recently granted patents indicates that new products or services are being introduced or have recently been introduced.

Although the mechanics of non-intellectual property due diligence is fairly straightforward and has not changed a great deal in recent years, intellectual property itself is complicated, constantly evolving, and highly technical. The constantly changing laws surrounding intellectual property further complicate this area of due diligence and often require subject matter experts to study the materials. This book is intended to assist the intellectual property attorney in conducting such a review.

A word about resources. Discussing legal tools without practical materials is fruitful and can be overwhelming. For this reason, we have compiled a list of resources for an attorney’s use in a transaction (see the appendix). These resources are intended to combine updated legal knowledge with sensible information and reasonable steps a practitioner can take to spot potential issues and address those concerns appropriately.