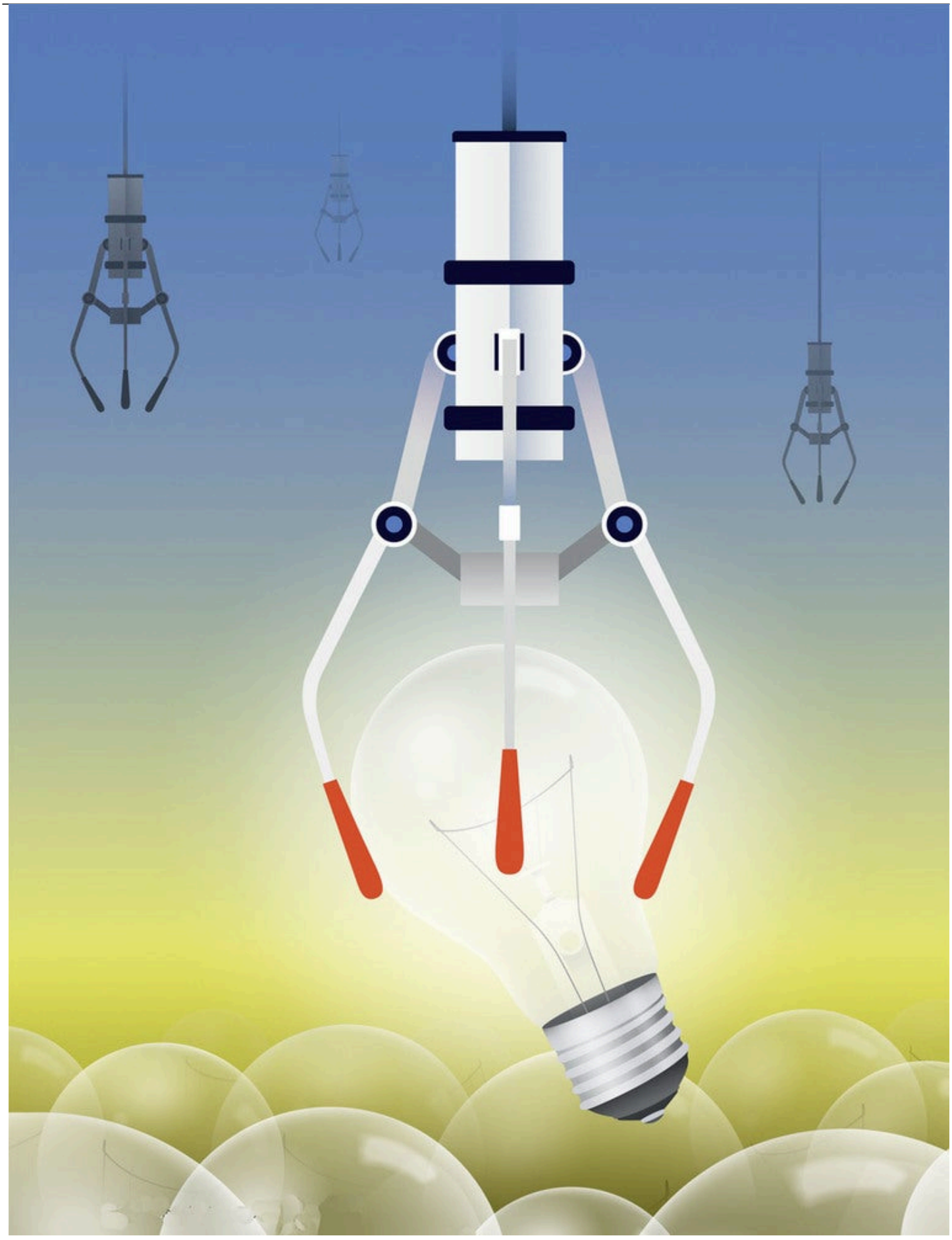
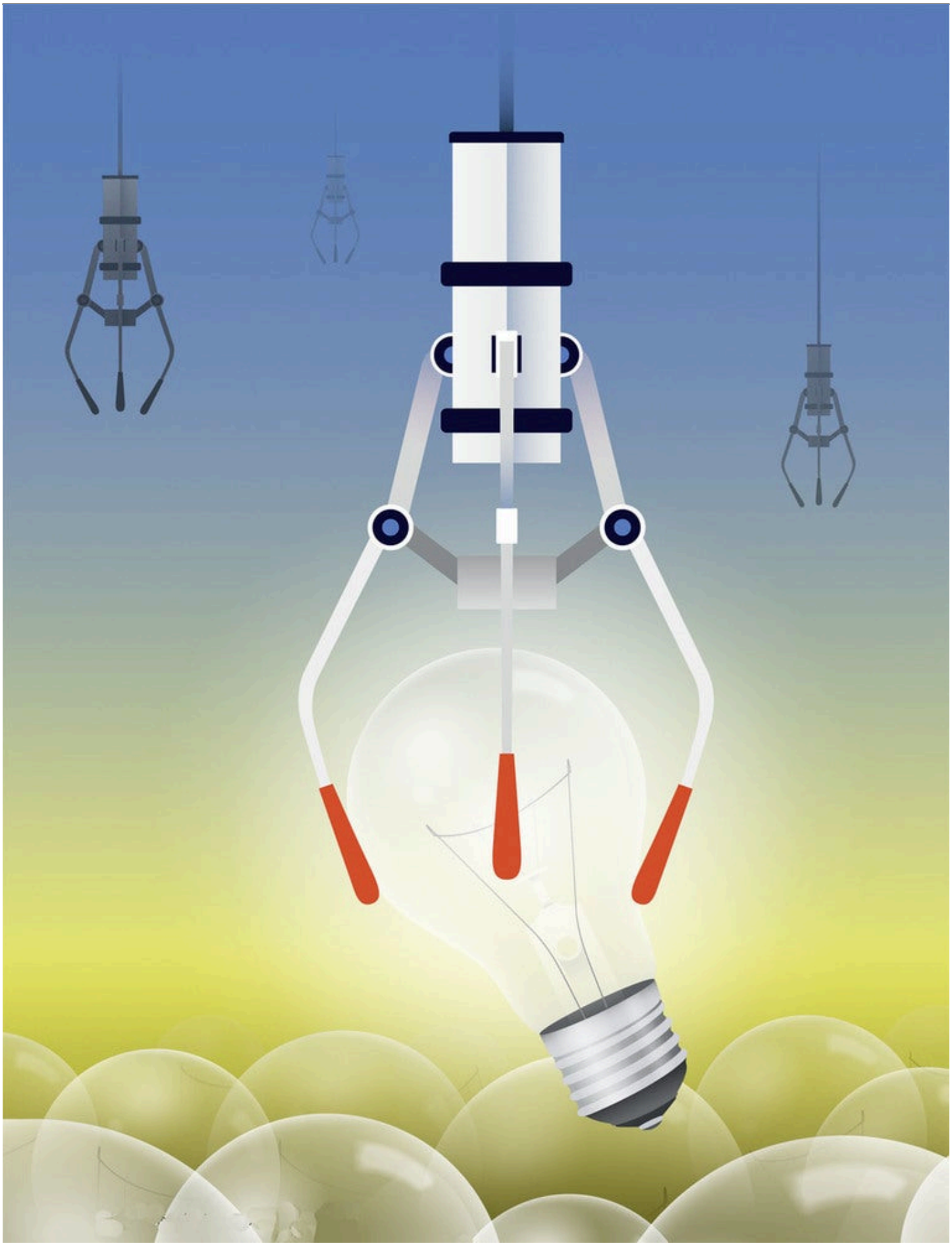


Maximizing Intellectual Property Portfolios in Challenging Times

Intellectual Property





CHEAT SHEET

- ***Don't cut IP.*** When there is financial pressure to cut costs, IP management is often reduced or eliminated. But a strategically constructed IP portfolio can add immense value.
- ***Create value.*** To increase the effectiveness of your company's IP strategy: (1) align your IP with the company's business purpose; (2) create revenue by commercially exploiting your IP; (3) proactively build your IP in line with the company's future plans; (4) strategically enforce your IP; (5) create IP that has a capital value; and (6) maintain your IP.
- ***Coming to fruition.*** The value you create in your company's IP portfolio will be most useful in these scenarios: (1) acquisition of the company; (2) acquisition by the company; (3) sales of the company's assets; (4) asset-based financing; and (5) going public.
- ***Avoid value leaks.*** Structure your business contracts with enough flexibility so that there is room for new opportunities if your IP is used differently in the future.

COVID-19 is highlighting companies' weaknesses and challenging their strengths. For companies with key intellectual property (IP) assets, those challenges take on a special level of concern for in-house counsel. "Crisis management" demands associated with COVID-19 make it increasingly difficult to focus on strategic and tactical decisions with long-term implications, particularly when cash flow becomes limited and unanticipated resource allocations become necessary.

> **IP assets in a portfolio should not be static, but rather track closely the development and movement in the underlying business to which they are tied.**

IP management involves costs — for creating, maintaining, exploiting, enforcing, and monetizing. For many companies, those costs make IP management a potential target of cost-cutting in times of financial stress, when there is inevitably an expectation that costs be reduced or eliminated. However, a strategically constructed IP portfolio can be a very valuable asset to your company in any economic climate, and may be an essential component of building value your company will need in order to achieve its ultimate goals. Fortunately, it is never too late to strategically realign your company's IP portfolio.

Value creation

The following six principles can help guide the value-adding effectiveness of your company's IP strategy: (1) align your IP with the company's business purpose; (2) create revenue by commercially exploiting your IP; (3) proactively build your IP in line with the company's future plans; (4) strategically enforce your IP; (5) create IP that has a capital value; and (6) maintain your IP. These principles will position your company for strength and cost-effectiveness in any economic climate and maximize the company's opportunity to realize the value of its IP portfolio when securing financing, procuring investment, or preparing for sale.

1. Alignment

IP assets are most valuable when aligned with your company's business purpose. This requires a careful crafting of different forms of legal protection and solid planning and communication within your company. Anticipation of where the business will go is informed prediction, so a step-by-step approach to balancing where the business is and where it might go — versus covering every possible country jurisdiction and protection in advance — is the key. What to avoid is simply "getting a trademark" on every idea without understanding the underlying business reason behind the request. In-house counsel play a critical role in ensuring that all such requests are enhancing the company's IP assets, and not creating unnecessary costs and burdens associated with filing, maintenance, and enforcement over time.

2. Create revenue

A company's IP assets ought to be designed with a mind toward prospective revenue. That can be revenue derived from your company's core business, or through licensing or sale to third parties. If an IP asset is not a revenue driver for your company, it may not be a necessary asset. With this in mind, a regular dialogue with your client following each request for new IP rights is fundamental to the strategy. The key to this principle is staying on top of the IP portfolio sufficiently to know when IP assets are "aligned," when there are gaps, and when IP assets are no longer creating revenue for the company. If revenue is the driver for your IP, assets in the last category should be identified and sold or otherwise eliminated. This allows for costs to be minimized at all stages in the process and related revenue maximized.

3. Proactively build IP

IP assets in a portfolio should not be static, but rather track closely the development and movement in the underlying business to which they are tied. Again, this takes close communication and strategic coordination within your company. If the company's business moves in new directions, trademark recitations may no longer cover those new areas of expansion or additional recitations may be needed. Patents may similarly no longer protect the means by which the business is being done, or reflect the company's latest product designs. This gap not only creates potential opportunities for third parties to compete, but may also introduce the risk of inadvertent infringement by your company. To build assets proactively, management of your company's IP portfolio needs to track where its business is today, and anticipate where it is likely to go in the future.

4. Enforce your IP

IP assets are fundamentally about rights to exclude others. Failure to enforce your company's exclusive rights can lead to constructive abandonment of its IP assets, or at least a significant diminution in the strength of those IP assets in excluding others and recovering prospective damages. What this means is that policing for infringement, putting infringers on written notice, and taking legal action where necessary to enforce rights are necessary components of effective IP portfolio management. Principle three above, "Proactively Building Assets," sets a perfect stage for the most efficient direction for policing and enforcement. If you are focused on the building and protection of strong, relevant IP assets for your company, you can more effectively allocate time, effort, and costs.

> **Your company's business, and the environment in which it operates, are in constant change. The recent COVID-19 crisis has highlighted as much, but constant change is a reality in any business circumstance.**

5. Create IP that has capital value

IP, like real property, can create a revenue stream from “rent,” or, in the case of IP, licensing or sales revenue as part of a company’s core business. This creates a value to the business as a going concern, and has a capital value. The value of IP is not necessarily connected to a single source of derived income. Brands are a key component of the goodwill value of a business. Patents may have massive value if they hold the rights to a limited monopoly of a product that is in great commercial demand. Being of statutorily fixed limited duration, the value of any one patent is diminished by time, however. Best practices in building capital value in an IP portfolio are ensuring that a company’s IP portfolio is kept strong and enforceable, is closely tied to the company’s current and future business direction, and accurately reflects the level and type of protections the company needs in the geographies in which it does business.

6. Maintain your IP

Your company’s business, and the environment in which it operates, are in constant change. The recent COVID-19 crisis has highlighted as much, but constant change is a reality in any business circumstance. Accordingly, regularly reviewing your company’s IP portfolio to ensure that it remains aligned with the company’s business goals — current and future — is critical. IP assets that cease to support those goals can be sold, licensed, abandoned, or held depending upon whatever path is of greatest commercial benefit. Absent such a regular review and realignment, a costly gap can exist between your company’s business goals and the IP assets that support those goals. The result can be a diminution in the company’s value. However, where properly aligned and maintained, a company’s IP portfolio can greatly increase the company’s value.

Given recent COVID-19 related events, and the uncertain duration of the current pandemic, growing strategically and making the best decisions for your company’s long-term future can be challenging. While there are certainly tactical moves that can be made to support and grow an IP portfolio at any time, it is consistency and implementation of a long-term strategy for raising capital and generating revenue from an IP portfolio that creates the most value. If IP is an important asset for your company, maximizing the value of that asset is critical, whether your company’s future goals include raising capital for growth, sale, or preparing for an IPO or other equity event.

Avoiding value leak is an important part of creating valuable IP

Think strategically about how the company’s IP might be used differently or more broadly in the future and ensure your business contracts provide flexibility to leave room for those opportunities.

By way of example, if your company’s IP includes copyrighted materials such as articles or short stories, you should aim to:

- License your IP on a non-exclusive basis whenever possible, or where exclusivity is necessary, grant it for a limited period to enable additional licensing of the same IP.
- License the use of your IP to specified categories and reserve everything else for the company as licensor. Is there interest in taking your short story and making a film of it? Grant only film rights and reserve for your company stage rights, television rights, and podcast rights, as well as everything else not explicitly granted. Unless you intend to sell your IP rights

completely, new and different prospective value for your IP should be for the company's benefit.
- For transactions that involve options to purchase IP (such as an article being considered for development into a book), provide for a reversion of rights if your licensee fails to use your IP for the purpose intended with a particular time. This will enable your company to place the IP with a third party that can better monetize the IP — the fruits of which your company would typically benefit from under the terms of the option agreement — if your initial counterparty fails to do so within a reasonable time.

Nascent businesses often make the mistake of granting broader rights than are necessary, or for longer than is necessary, limiting the company's ability to seize on profitable opportunities when they later arise.

Value realization

The value you strategically create in your company's IP portfolio will truly manifest its rewards in the following five scenarios: (1) acquisition of the company; (2) acquisition by the company; (3) sales of the company's assets; (4) asset-based financing; and (5) going public. An optimal strategy to maximize your IP portfolio value requires strategic tailoring. As a result, the considerations for the structure and composition of the IP portfolio to be constructed and managed by in-house counsel will differ slightly or more in each case. Accordingly, structuring your company's IP portfolio in a fashion consistent with the company's desired IP purpose and end goals is important for maximizing value in any of these scenarios.

1. Acquisition of the company

In this scenario, the key goal is to maximize total company value and to minimize the seller's warranty risk. To that end, an IP portfolio should have certainty around its assets. This includes a verifiable chain of title, government registrations, geographical applications of such government registrations, scope of protections to ensure that they cover the business that is being sold, and a successful history of policing and enforcement to ensure that a company's IP assets are not constructively abandoned or being infringed. To this end, patents should be carefully prosecuted to ensure that there is solid claim construction, adequate disclosure in the specifications to allow for continuations in whole or in part, or divisionals, depending upon circumstances and the jurisdictions where you are prosecuting. A stronger, more limited patent portfolio that is tailored to the business it supports can be more valuable in a sale than one that is ill-defined or sporadic in design. Similarly, brands and associated domain names should be strong and enforceable, and have an excellent history of policing and enforcement. Copyrights should be filed on websites, key publications, software as appropriate, and all advertising and marketing materials. A strong, well-documented, and effective system for trade secret protection in the company, with all employees and independent contractors having signed work-for-hire contracts in advance, is also key. Designing an IP portfolio with an eye toward having it acquired is about ensuring that the IP assets support and reflect the needs and goals of the company's business, and are well documented, fully legally protectable, prosecuted to create strong rights, and historically well-enforced. The company's officers, and perhaps shareholders, are going to have to make representations and warranties regarding the IP portfolio in any sale. The legal status of the portfolio itself needs to be ready to support such

contractual representations and warranties, and be strong enough to make an inadvertent breach of such representations unlikely.

2. Acquisition by the company

In this scenario, the above structural considerations are similarly applicable, with some important differences. If part of the acquisition strategy is to offer the target party equity in the company, then a more aggressive approach to IP asset creation could be warranted. A company might consider steps such as: taking more risks in expanding prospective rights to brands through intent-to-use applications; aggressive use of the doctrine of expansion in brand enforcement; selecting more suggestive (as opposed to fanciful) slogans and marks to support marketing campaigns; and taking an aggressive posture on enforcing domain name rights at ICANN, all of which can suggest that a company is “on the move up.” This posture could support the ability of a seller to value its assets more highly and, ultimately, the resulting value of the acquiring company. Similarly, a broad patent filing strategy to build a large potential patent asset “footprint” in a “hot” emerging area of technology, combined with Patent Cooperation Treaty (PCT) filings internationally to “stake a claim” in such markets, can also indicate that a company is willing to take risks to enhance market position. In this scenario, continuing to file copyrights aggressively — and having a strong trade secret system with carefully constructed employment and independent contractor contracts to ensure IP assets are owned by the company — remains critical. Here, where the company is unlikely to have to represent and warrant the legal position of its IP portfolio, more risk may be warranted where useful to establish an aggressive present and future IP position. Such a position may end up having to be circumscribed later, but a buyer may get credit in prospective asset valuation where there is a strong “go forward” story for future growth supported by an aggressive and well-articulated IP position.

> **Sloppy IP prosecution, lack of good and verifiable chains of title, poorly constructed IP portfolios, IP portfolios in early stages of prosecution and registration, or those portfolios that lack historical enforcement, are unlikely to be financeable.**

3. Asset sales

In this scenario, it is possible that every category of a company’s IP portfolio could be sold together or separately. Combinations of certain assets could also be selectively packaged for a sale, across different categories of legal protection (e.g., patents, brands, copyright, and trade secrets). While for every company such a scenario is possible, many companies make it a strategy. As various business units become more or less profitable, strategic direction shifts and certain business units may become more or less relevant to the company’s future strategy. When that happens, the value of IP investments that were made in anticipation of business opportunities that were not fully realized gets revisited and the possibility arises that the resulting IP assets may be more valuable to a third party than to the company. As a result, they may be sold off for their asset value to such third parties. Planning for this eventuality is challenging, as it is frequently not predictable. Charting a course for all eventualities is impossible. Accordingly, it really becomes about trying to spot such likely events as far in advance as possible and trying to strengthen the assets being sold as much as possible for a likely sale. Generally, the more legal certainty created around an IP portfolio being sold, the greater the potential value. That rule may be abrogated, however, in a very “hot” area of IP where the industry or base technology is still developing. For example, one of the authors was involved in a transaction in which some trade secrets and know-how rights limited to use in China were sold to a buyer in China for millions of dollars, in a nascent area of industry/technology. The in-house counsel helped create, protect, and legally frame trade secret and know-how rights in a pharmaceutical

company to maximize protection in different jurisdictions. These rights were then parsed geographically and monetized by country, well before patents were filed or granted. This provided early stage revenue for the company.

4. Asset-based financing

In this scenario, your company has a straightforward goal — to borrow money against an asset. The more value that can be ascribed to the asset being financed, the better. IP portfolio assets are no exception to this rule. The documentation for most general business loans or lines of credit today includes terms that "sweep" all IP assets up as part of the underlying security for the loan. This has two significant legal impacts that are often lost in the detail: First, a third party contractual legal obligation is created at that point to maintain and enforce the financed IP assets; and second, the IP assets of the company cease to be available for sale or additional financing absent a prior release from the lender. As a result, many companies are unknowingly in technical breach of their contractual lending covenants as a consequence of how they manage their IP portfolios. Accordingly, close scrutiny of loan documents in advance, and on an ongoing basis, is very important. There is also a growing market for IP-based asset lending. From discussions with such lenders, and two of the authors' personal experience, strong IP assets can form an independently valuable asset base on which loans can be secured. The same considerations and IP portfolio structural criteria identified in Paragraph 1 of this section are equally applicable here. A stronger, focused, more historically enforced IP asset is generally going to lead to a higher borrowing valuation. While an aggressive IP portfolio designed to maximize future growth and potential can also be of value, lenders tend to be highly conservative. The lawyers, accountants, consultants, and investment bankers they hire to advise them on such transactions will, as a result, generally be similarly conservative. Sloppy IP prosecution, lack of good and verifiable chains of title, poorly constructed IP portfolios, IP portfolios in early stages of prosecution and registration, or those portfolios that lack historical enforcement, are unlikely to be financeable.

5. Going public

In this last scenario, your company has a straightforward goal, similar to securing asset-based financing, but in this case, it is to maximize the legally and financially defensible asset value of the company and its underlying IP portfolio. As noted, due to the accounting treatment for goodwill, a substantial portion of the total financial value of the company will necessarily be inextricably connected to the company's brands and intangible assets. There simply must exist legally strong and defensible brands and intangible assets to serve as the associated repository of such goodwill. Accordingly, in a planned IPO scenario, attention must be placed on building and supporting a strong IP portfolio that is registered and strongly protected, particularly around key company brands. Additionally, the corporate officers taking the company public, as well as the professionals supporting that effort, can be legally and statutorily liable for any misstatements in the filing documents. This can include criminal sanctions for breach. In such a case, ensuring that any and all statements regarding an IP portfolio can be justified, and backed up by documentation and all necessary legal proofs, is essential. A failure to ensure IP asset quality in this case can have serious consequences that go beyond valuation impact or contract breach. Compliance with regulatory and other legal requirements is critical to ensure that the IP assets are legally protected and maintained. There is little room for error in this scenario — getting ahead of such processes in advance will be key to a company's success.

Failing to maximize the value of your company's IP while the opportunity exists may make it difficult or impossible to "make up for lost time" when an unexpected event like COVID-19 redirects in-house

counsel's attention. The resulting lost opportunity costs can prevent your company from having the ability to generate revenue it needs in the course of operating its business, or worse, can prevent an essential opportunity — such as a sale or capital raising effort — from being realized. Fortunately, in-house counsel are well positioned to take the lead in maximizing a company's IP value by adhering to the six principles outlined above. In doing so, in-house counsel can help ensure that the value of the company and its IP assets are maximized, which can make all the difference when the day comes for value realization. ACC

For more news on protecting trade secrets, read "Can Employees Be Convicted of a Crime for Unauthorized Use of Computer?" on ACC
Docket's website: accdocket.com/articles/computer-crime.cfm

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Loose Lips Sink IPs (March 2020)

Seeing Through the IP Haze (Sept. 2019)

Using Workforce Agreements to Protect Your IP and Prevent Termination Problems (Sept. 2019)

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