

It's Time For A Spring Cleaning: Why You Should Undertake An Intellectual Property Audit

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“Spring cleaning” gives one an opportunity to review what one has, discard the old, refurbish the not so old, separate out the new, determine what else one might need and judge if the budget will allow it. Like a “spring cleaning,” an intellectual property audit helps one put the intellectual property assets of one’s business in order.

Today, audits are particularly important. Officers and directors of corporations who have not exercised due care and diligence to ensure that a corporation’s intellectual property assets are in order may be held liable to shareholders for mismanagement of intellectual property assets. Mismanagement can be either active or passive. The general lack of awareness of the importance of intellectual property assets to the business of a company can be a breach of the duty of care and diligence, as can be failure to take action against the infringement of intellectual property assets by third parties. Similarly, protecting a company from infringement liability to others is an important duty that falls squarely on the shoulders of corporate officers and directors. The failure to exploit company assets—by licensing, for example—can also be considered a violation of the duty or even be deemed “corporate waste.”

An intellectual property audit should result in an understanding of the scope and breath of a company’s assets, and from such an understanding, officers and directors are put in a position from which they can make reasoned decisions about how best to deploy the assets. Assets can include patents, trademarks copyrights, trade-secrets, domain names, and even know-how and license agreements. Would it surprise you to learn that Honeywell Corporation, for example, recovered more than \$127 million dollars as damages for infringement of patents that it owned, even though the technology covered by those patents was never even commercialized by Honeywell itself?

An intellectual property audit allows you

to determine what you own and what you license and evaluate what you may want to license out and what you may need to license in. An audit allows you to consider what you need to protect, and what extent you exploit intellectual property rights. Most significantly, an audit allows you to manage your risks—to shareholders as well as to third parties, whose rights you might be infringing. The audit can result in a stronger intellectual property portfolio, as it may allow you to make decisions regarding ensuring that more invention disclosures make it to patent application stage. If patents, trademarks, etc., have no value, it may behoove management to expressly abandon the rights so as not to continue paying unnecessary maintenance fees, annuities, renewal fees, etc. Perhaps market considerations will dictate that certain intellectual property be donated. IBM, for example, reportedly donated more than 500 patents, resulting in tax savings as well as maintenance fee savings. The benefits of an audit are limitless.

An intellectual property audit is normally conducted by an intellectual property attorney in cooperation with valuation experts, as well as technical and market savvy company personnel. The attorney will identify intellectual property, guide the scope of the audit, and ultimately develop the intellectual property strategy in collaboration with company personnel. While an attorney can evaluate the breath and strength of your intellectual property rights, an evaluation of the financial strength of a portfolio should obviously be done in coordination with intellectual property evaluation experts such as auditors and other valuation experts. For example, credit enhancement firms conduct evaluations when companies want to raise capital because they take security interests in intellectual property in exchange for guarantees given to traditional lenders who lend capital (in collateralization transactions) to intellectual property holders. Some considerations that should be made during an intellectual property audit involve a review of what is happening in the market place so that both offensive and defensive intellectual property strategies can be adopted. That’s where

market savvy internal personal contribute to the analysis.

A good audit will also consider what agreements you have in place with employees and what agreements are needed. Non-disclosure agreements, confidentiality agreements and non-compete agreements should be reviewed, and the relevant portions of employment manuals should be looked at, to be sure that there are no “misplaced ducks.” Depending on the nature of the business, you might need to consider intellectual property provisions in joint-venture agreements and other joint cooperation agreements.

Although the benefits of an intellectual property audit should by now be apparent, recent legislation (that may or may not effect your business), in particular the Sarbanes-Oxley Act (“SOX”) and changes in the accounting rules, may effectively mandate that “audits” be conducted to comply with the disclosures and certifications required by SOX. SOX, among other things, requires that certain intellectual property assets be shown on company balance sheets. Thus, over and above the benefits discussed above, that you would obtain in conducting an audit, compliance with SOX is certainly an important benefit, to say the least.

In sum, the identification and management of your intellectual property will significantly benefit your company. The return of the investment you have made in intellectual property is best captured if you have knowledge of the assets that you have and you use that knowledge to manage the assets. An audit will accomplish that.

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