

The Intellectual Property Auditⁱ

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The Intellectual Property Audit Measures an Organization's Intellectual Assets

With the advent of easy and ever-less-expensive computer access throughout the industrialized world, we live more and more in an economy based not on agrarian activities or industrial strength but on knowledge and the management of knowledge. Managing this new economy requires different tools than did agrarian or industrial economies. The agrarian economy demanded farming skill from the workers, and transportation and storage for crops. The industrial economy demanded manufacturing skills from the workers, transportation and a consumer market for manufactured items. Our new knowledge economy demands that organizations have in place the tools to manage the knowledge contained within them: some examples of this knowledge are contracts with employees, contractors, strategic partners, and consumers to protect the organization's knowledge base, patents to protect inventions, trademarks and service marks to protect organizational goodwill, copyright to protect publications, and a well-designed licensing program to allow the organization to commercialize and capitalize on its intellectual property.

This knowledge — the collective intellectual understanding of everyone who works for the organization — contained within an organization is the organization's intellectual capital. Intellectual capital makes up approximately 80% of the value of the S&P Fortune 500 companies.ⁱⁱⁱ Probably the best-known example of an organization's intellectual capital is the Coca-Cola logo, which is valued at approximately U.S. \$10 billion.^{iv} However, the books of these organizations do not reflect these assets; they are "hidden resources."^v "Book values of publicly traded companies mainly reflect the value of tangible and capital assets of the organization.... This is hardly an accurate reflection of the intangible assets as [good will] is created to balance the books following an acquisition. The market value of a

organization reflects the value of a hidden resource that is recognized and valued by the market....”^{vi}

Clearly, if an organization fails to account for 80% of its assets on its ledger books, that organization cannot provide an accurate valuation figure for investors, partners or consumers. Therefore, an organization must account for those intangible assets that do not appear on the ledger books but which make up so much of the organization’s market worth. It does so through an intellectual property audit.

The Intellectual Property Audit

One traditional definition of an intellectual property audit is “a cataloging of a organization's intellectual property assets.”^{vii} It is required for an organization to meet its due-diligence requirements for mergers, acquisitions, or other transfers. Today, organizations see an intellectual property audit not only as a balance sheet for intangible assets but also, more importantly, as a self-evaluation that the organization constantly and consistently engages in to determine the value of its own assets, determine how to best capitalize on those assets, and keep abreast of the changing values of its assets in the face of the ever-changing economic and legal ecosphere.

Who Should Conduct an Intellectual Property Audit?

“Intellectual property audit” is perhaps something of a misnomer. It indicates that the audit is a mere counting up of assets, and the person conducting the audit merely adds up the intellectual property found in the organization and reports the value. Nothing could be further from the truth. An intellectual property audit is an inherently legal undertaking^{viii}, and should therefore be performed by a team consisting of at least an attorney with expertise in the law of intellectual property, either in-house or outside counsel, or by the in-house personnel of the organization, if they have sufficient knowledge of the organization’s intellectual property to perform the activities required for an intellectual property audit of the organization. An intellectual property audit is not an accounting function. The intellectual property audit is an assessment of the legal status and value of an organization’s intellectual property, especially targeting those areas where the marketing and management goals of the organization and the existing protection of the organization’s intellectual property are somehow not well suited to each other. The attorney or attorneys and other team members (the team might consist of the intellectual property attorney and at least one representative from each of the management, marketing and technology areas^{ix}; because of the inherent legal

significance of the intellectual property audit, at least one member of the team must be an intellectual property attorney) selected to perform the audit should therefore have some expertise with the organization’s technology, the marketing and management goals of the organization, and have some familiarity with what is involved in intellectual property protection: prosecution of the registration application, maintenance of the property, and on through defense of the intellectual property through litigation and the appellate process.

When to Conduct an Intellectual Property Audit

When should an organization consider conducting an intellectual property audit? Attorney Leslie J. Lott has identified several appropriate times in the life of an organization for intellectual property audits^x; in this subsection, I borrow heavily from her listing and commentary.

New Intellectual Property Management

If the organization has new intellectual property management, the new intellectual property manager should have a thorough intellectual property audit performed to become familiar with the status of the portfolio.

Merger, Acquisition, Significant Stock Purchase

A significant corporate change (merger, acquisition, significant stock purchase) can impact intellectual property ownership; this is another signal for an intellectual property audit.

Transfer or Assignment of Interest in Intellectual Property

A transfer or assignment of intellectual property from one organization to another calls for an intellectual property audit of both organizations’ intellectual property. Here, the intellectual property audit allows the organizations to be sure the transfer or assignment meets the interests of both by ensuring that the intellectual property is properly protected and enhances the acquiring organization’s existing intellectual property interests, and that the intellectual property does not leave any unplanned vulnerabilities for the organization transferring the interests.

Licensing Program

An intellectual property audit should be performed when an organization sets up an intellectual property license or licensing program, and on a regular basis thereafter. This is important whether the organization is the licensor or the licensee. If the organization licenses its intellectual property to others, it must of course

actually own the intellectual property that it is licensing. Also, there must be no existing licenses that would interfere with the proposed new license.

If the organization is the licensee, obtaining the intellectual property rights of another, the audit determines that the scope and extent of the license to be obtained is adequate for its purposes.

Significant Change in Law

A significant change in case or statutory law may require an organization to re-evaluate its intellectual property.

One such change in statutory law occurred when Congress passed the federal anti-dilution statute. This change in the law significantly impacts the analysis of the potential liability of an organization for infringement of the trademarks of others and also affects the analysis of whether or not others are infringing the organization's rights.

Three examples of case law which arouse the need for an intellectual property audit are the *Qualitex* case (which deals with the protection of color as a trademark), the *Sony* case (which deals with the question of whether a device that can be used for copyright infringement is itself an infringement of copyright), and the *Festo* case (which deals with the Doctrine of Equivalents in patent prosecution).

Financial Transactions Involving Intellectual Property

Financial transactions involving intellectual property might include loans, public offerings, private placements, or any other transaction which directly involves an organization's intellectual property, or in which the intellectual property of the organization is or could be significant.

New Client Program or Policy

An organization should conduct an intellectual property audit in connection with new programs or policies, such as an aggressive foreign filing program, new marketing approach or direction, expansion of a product line or services, corporate reorganization, or any other corporate change that could affect the interaction between the organization's intellectual property and the marketplace.

Focus of an Intellectual Property Audit

Each intellectual property audit should focus on four key areas. First, the attorney performing the audit needs to *identify all the intellectual property assets* within the organization being audited. Second, the attorney must *identify any problems* that

exist with the intellectual property ownership. Third, the attorney must *identify any defects in title* or enforceability of the organization’s intellectual property. Finally, the attorney must *identify any unprotected intellectual property assets*.

Identification of Intellectual Property Assets

In identifying all of the intellectual property assets of a organization, an attorney focuses on “...identifying the intellectual property subject matter, how it works, and how it is manifested in the organization.”^{xi} Different types of organizations stress different types of intellectual property, depending on the organization’s purpose. An artistically based organization should have copyright protection in place, but may have very few, if any, patentable inventions or trade secrets. A technology-based or manufacturing organization, on the other hand, should rely heavily on patent and trade secret protection and less on copyright protection. Most organizations are likely to have logos and other trademark items.

Identification of Intellectual Property Problems

To identify any problems that may exist with the organization’s intellectual property ownership, the attorney performing the intellectual property audit attempts to trace the chain of ownership of intellectual property back to its creation. The attorney looks for assignment agreements from employees, former employees, contractors, strategic partners, acquired companies, and others who may have rights in the intellectual property if not assigned. This is especially true for patents, where, in the United States, the inventor owns all rights to “... exclude others from making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States, and, if the invention is a process, of the right to exclude others from using, offering for sale or selling throughout the United States, or importing into the United States, products made by that process, referring to the specification for the particulars thereof.”^{xii} It is possible in some other countries for an organization to be named as the inventor on a patent; in the United States, the inventor must be one or more human beings^{xiii} who may then assign rights in the patent to an organization.^{xiv} It is also true in copyrights, where independent contractors and consultants retain copyright to materials fixed in a tangible medium unless otherwise agreed.

The attorney performing the intellectual property audit also looks at the agreements that exist between the organization’s employees and the employees’ former employers. New hires can present a problem with intellectual property

ownership if they would violate a previous employer’s noncompete/ nondisclosure contracts by assigning the rights to any new inventions to their current employer. Hence, the intellectual property attorney must investigate the employees’ prior noncompete/nondisclosure agreements.

Identification of Defect in Intellectual Property Title or Protection

The attorney performing the intellectual property audit should identify any asset that is entitled to more protection than the asset currently enjoys. In some cases, such as in patents, key protection can be lost forever if the organization postpones the decision to pursue the registration for too long. This is often a problem in that the invention, while it should be perfectly patentable, has hit the statutory bar in the patent law because the inventor disclosed or used the invention in public more than one year before the organization applied for the patent. Or, an inventor may regard her invention as perfectly obvious when it is actually patentable. The attorney can also identify valuable trade secrets that the organization should protect more carefully than it does.

Identification of Unprotected Intellectual Property Assets

Often, copyright and trademark protection may be based only on common law because the owner fails to register the intellectual property with the appropriate agency. Or, an inventor may invoke a statutory bar of the patent law inadvertently and render his invention unpatentable. This can cause problems down the road for the organization when it tries to enforce its intellectual property rights because certain intellectual property rights (patent rights especially) are unenforceable unless the asset is registered with the proper governmental agency or agencies. Ultimately, lack of registration of a piece of intellectual property can lessen the value of the intellectual property itself. The attorney must identify any of these problems and bring them to the organization’s attention. The organization then may wish to remedy a problem if it can (in the case of patent registration, the organization may be unable to obtain registration due to the one-year statutory bar). The attorney should also identify any issues with recording of licensing or change in ownership of intellectual property. An organization’s failure to record such changes can result in a second licensee taking priority over the organization as first licensee if the organization fails to provide notice via registration. In US patent law, this notice has a 90-day look-back period. Proper registration also ensures that full remedies are available for infringement.

Intellectual Property Audit Breakdown

An intellectual property audit breaks down into nine areas that the intellectual property attorney should examine: patents, contracts with independent contractors, employment contracts, trademarks, licenses, trade secrets, copyrights including organization handbooks, training, and inventions.^{xv} Each area has its own requirements that must be monitored through an audit.

The attorney should first notify everyone who may be involved that the audit is about to take place. She then interviews the technical, legal, managerial, and human resources people to collect information on “...licenses, research and development reports, employee and contractor confidentiality and assignment agreements, and employee invention disclosure statements.”^{xvi} Based on the information thus obtained, she then documents the status of the organization’s intellectual property.

Inventions

Inventions are the first step in the development of potentially very valuable intellectual property. The attorney performing the audit should determine whether the organization is even aware of all the inventive activity carried out within its walls. Does the organization “harvest” its inventions (i.e., require disclosure of inventions and review disclosed inventions for patentability)? Is there an inventor incentive program in place? Does the organization monitor its employees’ inventive activity in other ways, such as having the in-house counsel “manage by meandering,” that is, walk through the laboratories and other workspaces of the potential inventors and talk with them? The attorney performing the intellectual property audit should identify any weaknesses in the organization’s “harvesting” of inventions and bring them to the attention of management at a level where they can be addressed.

Patents

Once an invention is disclosed, the organization must determine whether to obtain a patent on it, and in which country or countries a patent would be most valuable to the organization. Obtaining patent protection requires that the organization be aware of new innovations that occur in the research and development process.^{xvii}

In the United States, the patent law is set forth in Section 35 of the United States Code. That law provides that an invention must be of patentable subject matter, original, novel and nonobvious to be eligible for patent protection.^{xviii}

“Patentable subject matter” is defined in the code as “processes, machines, manufactures, and compositions of matter.”^{xxix}

The attorney determines whether the organization’s R&D staff maintains proper records of new developments that are reviewed and witnessed at regular and frequent intervals, thereby providing documentation for patentability determinations, and whether the organization observes the statutory time limits for patenting new inventions. If, for example, the invention is made public more than one year before the organization applies for a patent, the organization is barred from obtaining a patent on the invention.^{xx}

The attorney also examines the organization’s treatment of others’ patent rights: does the organization monitor itself in the light of others’ patents to reduce the potential for infringing activity? Does the organization routinely seek a patent opinion when there is the potential for infringing another’s patent before they begin any potentially infringing activity?

Contracts in General^{xxi}

Each contract that an organization enters into with regard to its intellectual capital must contain many elements, and parts of each contract must be individually negotiated.

Contracts, however, are expressed in language, and language is inherently prone to uncertainty in its interpretation, especially in cases where the contract’s drafter had little or no part in the negotiation of the agreement. The drafter’s job is to “...record exactly the transaction that the parties wish to undertake.”^{xxii} However, the probability of achieving absolute certainty in drafting any agreement is essentially zero; it cannot be done. Definitions of terms in the contract invariably use undefined terms, and those undefined terms are often not definable.^{xxiii} Therefore, even in the best scenario where a contract contains definitions for all its terms, the parties must still look to the judge for the reading of the contract, and then must interpret the judge’s reading, and the judge cannot consider all of the evidence surrounding the contract under the parol evidence rule. Even precise contracts are therefore remarkably imprecise.

However, even under the parol evidence rule, “[a] dispute over [an] alleged conversation that resulted in the oral license [cannot be offered into evidence under the parol evidence rule but] may be resolved by proof of partial performance.... Absent other complicating facts or application of the Statute of Frauds, a court could infer from such partial performance the scope of the license,...the consideration,...and the term....”^{xxiv}

The auditing attorney may examine the license agreements and strategic alliances between the client and another organization to be sure that the agreements cover trade

secrecy for the client, appropriately license any trademarks or patents, and are to the client’s advantage (or at least not to the client’s disadvantage).

Employment Contracts

Independent Contractors

By definition, independent contractors pose a conflict for protecting an organization’s intellectual assets. Independent contractors are generally experts in a particular area, and they market their expertise to many organizations. If one (or more) of those organizations has intellectual capital in something that an independent contractor has provided to them, the contractor should not be able to provide that same intellectual capital to other organizations, especially competing organizations. However, that expert still needs to make a living, and she does so by marketing her expertise.

This conflict is resolved best by having a clear contract with the independent contractor from the outset of the business arrangement, specifying who owns the expert’s work product, and who owns the contractor’s notes and ideas gotten while the contractor works for the organization.

One way to resolve the conflict is for the contractor and organization to agree to a shop right for the organization, wherein the contractor owns the intellectual capital, but the organization has a royalty-free license thereupon for the life of the information. This is very contractor-friendly because it allows the contractor to freely market the information to any other organization that she might contract with, but the organization can suffer from this arrangement because it cannot keep the information the contractor developed as trade secret (if the contractor assigns any invention then the organization can of course hold that patent), and therefore cannot properly commercialize any product that is derived from that information.

Another way to resolve the conflict is to “flip the coin” and give the organization full ownership of the intellectual capital that the contractor develops but allow the contractor access to all the non-trade-secret information he developed for the organization. This is excellent for the organization, but may deny to the contractor some or all of his area of expertise to market to other potential clients. Many ways exist to resolve this apparent conflict between the organization and the independent contractor. Outright purchase of information, royalties for access to information, grantbacks, agreements that change with time, sublicenses, assignments, use licenses can all be used individually or in combination to reach a mutually satisfactory agreement between the parties.

Clearly, each contract with each independent contractor needs to be negotiated individually. The contract will be based on the needs of each party at the time and in the foreseeable future, and these needs change with the parties and over time.

Employees

Agreements between an organization and its employees are used routinely to protect an organization’s intellectual property assets. They usually cover an organization’s trade secrets, inventions and works of authorship, and are generally signed both on an employee’s entrance to an organization and exit from the organization.

Employment contracts are part of the intellectual property of the organization; they delineate the protection of the organization’s intellectual assets both during and after the employee’s tenure. Each organization must be careful to ask each employee in an entrance interview whether she signed a non-disclosure agreement with any former employer that would be violated by the current organization’s employment agreement; if she did, the current employer must modify that employee’s agreement so as not to violate the former agreement.

Some employment agreements cover all trade secrets, inventions and works of authorship, whether or not related to the job the employee was hired to perform; others cover only those works created specifically for the organization while employed there; still others cover those works that the employee creates for the organization and those works that would compete directly or indirectly with any goal of the organization.^{xxv}

The last of the above examples may be the most commonly used paradigm. The first (all trade secrets inventions and works of authorship while employed) is too broad; for example, this type of agreement could have given the valuable HARRY POTTER^{TMxxvi} franchise to an employer had author J.K. Rowling signed it while writing the novels, whether or not the employer contributed anything (such as time, equipment, artistic support, etc.) to the work. This, of course, would have led to the employer’s enrichment at the employee’s expense, which is not a fair outcome for the employee. The second (only those works specifically created for the organization while employed at the organization) is not broad enough to properly protect the organization; an employee who must only protect an organization’s intellectual property while employed by the organization is free to leave and use the intellectual property she developed for the organization for a subsequent employer, possibly a

competitor. The last example (works created for the organization and works that would compete with the goals of the organization) generally avoids assigning an employee’s off-hours noncompeting but potentially valuable work to an employer, while protecting the trade secrets and other intellectual capital of the organization. It may therefore be most likely to be advantageous for both the employer and the employee.

The intellectual property audit can ensure that the proper protection for the organization’s intellectual property is in place with the employment and independent contractor agreements. In doing so, the attorney verifies that those agreements are neither overbroad nor too narrow. If the employment agreement or the independent contractor agreement is either too broad or too narrow, the attorney can recommend changes to be made in the contract, and perhaps provide means for employees and independent contractors who signed the insufficient agreement and later left the organization to be brought under the umbrella of the new, more appropriate agreement.

The auditing attorney should examine the contracts for both independent contractors and employees to ensure that the proper protections are in place: trade secrets are not to be revealed to others without authorization, patents and copyrights are to be assigned to the organization,

Trademarks

An organization should record each assignment of a trademark with the US Patent and Trademark Office (USPTO) in language that includes the goodwill and not the trademark alone with the assignment. The attorney performing the intellectual property audit can ensure that the proper assignment is made and recorded for each mark.

It is possible for an organization to lose its rights in a trademark or service mark through abandonment of the mark, or through failure to timely file the proper documentation with the USPTO. The auditing attorney must confirm that the organization filed the required registration and maintenance documents with the USPTO and that it has used the mark continuously in interstate commerce.

It is also possible for an organization to lose its rights in a trademark or service mark through improper licensing and improper policing of its mark. If a mark has, through improper policing, become a generic descriptor for the goods, the mark is lost. “Escalator” and “cellophane” are two examples of marks that became generic and therefore lost to their owners; more current examples of marks that remain

marks but are endangered are Kleenex® (how often do we grab a “kleenex” from the box of another brand of tissue?) and Xerox® (have you ever “xeroxed” a page?). The auditing attorney must ensure that any danger of becoming generic is addressed promptly and vigorously. Xerox Corp. and Kimberly-Clark (the makers of Xerox-brand photocopiers and Kleenex-brand tissues, respectively) spend millions of dollars annually to protect their marks.

The current registrations must cover the organization’s current trademarks, logos, slogans, and brands. By examining the packaging of the goods, the attorney can determine whether the currently registered marks match the currently used marks. The attorney should bring any discrepancy to the attention of the client.

Licenses

Licensing of intellectual property is one of the most efficient ways to capitalize on an intellectual asset. This means that the intellectual asset must be well protected by a license agreement. The full extent of a licensing agreement is beyond the scope of this work; it is a complex contract that should be negotiated on an individual basis.

The intellectual property attorney should make to make the following determinations with respect to the license contract.

- Is this an express license?

Licenses may be express or implied. An express license is a statement by the licensor that the licensee has certain rights to use intellectual property owned by the licensor. If the statement is written down and signed by both parties, then that writing provides strong evidence of the existence of a contract.

An implied license may arise from any one of a number of situations. They may be imposed by the courts based on the actions of the parties, or the parties may create the implied license without taking the matter to court by simply continuing to act as though a license exists. The intellectual property attorney might find an implied license by interviewing research personnel to see if they use technology from any source other than from within the organization, then tracing the ownership of any intellectual property that they use. The attorney might also find an implied license through a court’s ruling in litigation involving the technology in question.

- Is there a writing?
As with all contracts, a writing is not absolutely required for a valid, enforceable bargain. In the knowledge-driven economy today, of course, most contracts are reduced to writing and signed, but an oral contract can be equally binding as a written one. Clearly a writing is far preferred in any contract situation, including an intellectual property audit, because the attorney conducting the intellectual property audit has the words of the agreement before her on the printed page.
- Is a license exclusive? Is the organization that is undergoing the intellectual property audit the licensor or licensee?
A license can be exclusive (perhaps even denying the intellectual property owner the right to use the property) or non-exclusive. An exclusive license must be careful to look to the future and leave an opening in case the license proves unsatisfactory for any reason to either party.
- Does each license contain a granting clause?
Each license must contain a granting clause specifying the scope of the license and the licensee’s powers with the license.
- Has the owner of the property reserved any rights?
An intellectual property owner may choose to reserve, or keep back, some of the rights to the property (an example of this is the granting of a non-exclusive license).
- Does the license agreement specify who owns technology improvements?
A license should specify who owns any improvements that the licensee makes in the licensed technology.
- Does the license specify royalties, payment schedules and accompanying reports?
A license should specify all royalties and payment schedules, and the accompanying reports.

- Does the license agreement contain the standard contract clauses?
A license agreement should contain the standard contract clauses, such as term of the agreement, how the agreement can be terminated or modified, who defends the licensed technology in the event of litigation, whether the parties agree to arbitration before or instead of litigation, an integration clause, and so forth as needed.

Trade Secrets

Any valuable patent is contained in an envelope of undisclosed information. This envelope is the trade secret know-how that an organization develops around the use of its patented technology. It is not described in the specification of the patent because the knowledge was developed after the patent application was filed, and the patent law requires only that the best mode as of the date of filing be disclosed.

Trade secrets are protected by contracts between the organization and its employees, between the organization and its independent contractors, between the organization and its business or technology partners. The intellectual property attorney who performs the intellectual property audit should evaluate how well these agreements protect the valuable trade secrets.

Copyrights, Including Organization Handbooks

An organization's copyrights may be its most valuable asset. If the organization is based in the arts, then copyright becomes the foremost protection for its intellectual property.

Any material that is fixed and perceivable, directly or indirectly, in a tangible medium is copyrighted under the current U.S. copyright law.^{xxvii} It is copyrighted from the moment of creation,^{xxviii} but full protection is not available unless the work is registered in the Copyright Office at the Library of Congress.^{xxix} The intellectual property attorney must check the status of the registration of the organization's written materials to ensure that the courts can enforce the copyright laws of the United States if those written materials are infringed.

Training

Once the intellectual property audit is complete and the recommendations made, the organization should implement a training program for all employees to ensure that the recommendations that emerged from the audit are followed. Training should take place for all levels of the organization. The organization must

identify those areas in which employees need training, and the level at which they need it. It then must design and deliver the appropriate training courses and materials, and design and deliver the appropriate follow-up ongoing support.

An Overview of How an Intellectual Property Audit Works

The first step in performing an intellectual property audit is to develop a plan for the audit. An audit committee (usually consisting of an intellectual property attorney, a representative from management, marketing, and technology or research and development) defines the areas of inquiry and establishes the time schedule which the audit will follow. They outline the responsibilities of each member of the audit team. They then define the preliminary documents for review and decide which members of the organization — present and past — to interview.^{xxx}

The attorney develops an intellectual property database which contains, at a minimum, “...owner of the intellectual property asset, class of asset, the inventors or authors, when the asset was created or acquired, the asset's status (e.g., pending or issued patent, registered copyright, trademarks, domain names), on-going maintenance issues (e.g., payment of maintenance fees for patents, collection or payment of licensing fees), and the expiration or renewal date of the asset.”^{xxxxi} This database enables the organization to determine exactly what its intellectual property assets are and also to determine the status of each asset.

After the database has been developed, the attorney and the audit committee within the organization analyze the intellectual property and determine what action to take as to each piece of intellectual property. The committee and the attorney also identify mechanisms that the organization should use to identify and protect each new piece of intellectual property that the organization develops or otherwise acquires.

The audit team then documents the audit results and presents them to the organization, with recommendations as to where, if at all, intellectual property protection is inappropriately thin and where, if at all, protection can be reduced.

Benefits of an Intellectual Property Audit

An intellectual property audit benefits intellectual property buyers, owners and investors.

Intellectual Property Owners

Intellectual property owners benefit from an intellectual property audit when they depend on that property as a component of the organization's value (the greater the dependency, the greater the value of the intellectual property audit), when they license the property out, when there is a question that may involve litigation over the property, when they sell their stock or corporate assets, or when they engage in commerce involving the property.

Intellectual Property Buyers

If an intellectual property buyer is acquiring the stock or assets of a company, she should insist that an intellectual property audit be performed to determine the scope and level of protection in place and needed to make the investment worthwhile. This buyer should look at any licensing or distribution rights that are already in place in the company, and those that the company may be contemplating putting in place. The buyer is interested in determining what protections are available for the property, whether the property is adequately protected against any potential third-party claims to ownership (such as if it was developed by consultants, whether the consultant has properly assigned the property to the organization), whether the property is security guaranteeing a debt, whether needed federal and state registrations are in place and properly maintained, and, if any part was licensed or purchased from third parties, what rights to the third-party intellectual property the organization has purchased.

An intellectual property buyer may also be interested in simply acquiring rights to the intellectual property itself, without acquiring any part of the stock or assets of the organization that developed it. This buyer should look at what licenses exist already, whether trade secrets are available to increase the value of the property, whether any third party has any rights in the intellectual property that comprises any part of the property of interest, and, if so, what rights does the organization own, whether the property is in any way related to a government-sponsored activity.

Intellectual Property Investors

An intellectual property investor should demand an intellectual property audit when they consider funding a start-up company or financing an existing business. Often, the intellectual property is the sole asset of a start-up company, and it often forms a major part of the value of an existing company. Due diligence requires that the investor ensure that the property is fully protected. Investors also

would find the information gleaned through an audit to be useful in a debtor/creditor situation where the investor accepts an intangible asset as security on a loan.

Conclusion

The intellectual property audit is a necessary and important management tool in today’s knowledge economy. Indeed, it is the only way to assess the true value of an organization, and it is the only way for an organization to maintain and grow its intangible assets. Gone are the days when the corporation was valued at the price of its real and personal property. Today, managers and investors need to have a good understanding of the intangible side of the business as well as the tangible side. The intellectual property audit is the way for them to get a grip on reality.

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ⁱⁱⁱ Nermien Al-Ali, *Comprehensive Intellectual Capital Management*, John Wiley & Sons, ISBN 0-471-27506-9, ©2003, quoting Karl Erik Sveiby, *The New Organizational Wealth: Managing and Measuring Intangible Resources*, Berrett-Koehler Publishers, 1997, pp. 6-7.

^{iv} *Id.*; also, class notes, “Intellectual Property Management” course, Spring 2003, Professor Karl Jorda, Franklin Pierce Law Center.

^v *Id.*

^{vi} *Id.*

^{vii} Ron Corbett, *Symposium: Exploring Emerging Issues: New Intellectual Property, Information Technology, And Security In Borderline Commerce: Intellectual Property Strategies For Start-up E-commerce Organizations In The Post-dot-bomb Era*, 8 Tex. Wesleyan L. Rev. 643, 645 (2002).

^{viii} John K. Halvey and Barbara Murphy Melby, “Checklists for Performing Intellectual Property Audits,” *The Intellectual Property Strategist*, January 1995.

^{ix} <http://www.lawplusplus.com/column17.htm>

^x Leslie J. Lott: “Taking Stock of an Intellectual Property Inventory: How to Conduct an Intellectual Property Audit” <http://www.patentfla.com/articles/ipaudit.htm>. 1998, Lott & Friedland, P.A., Miami, FL.

^{xi} Corbett at 652.

^{xii} 35 U.S.C. 154. See also Herbert F. Schwartz, *Patent Law and Practice*, 3d Ed., at 39-40. BNA Books, ISBN 1-57018-240-X. ©2001.

^{xiii} 35 U.S.C. 102(f), 116, 256.

^{xiv} 35 U.S.C. 261.

^{xv} <http://agtalawyers.com/resources/ipaudit.html>.

^{xvi} Corbett at 656.

^{xvii} Robert C. Scheinfeld: “The New Wave: The Intellectual Property Audit.” *Brumbaugh Report*, Vol. 1 No. 3, Autumn 1991 at 1.

^{xviii} 35 U.S.C. 101.

^{xix} 35 U.S.C. 101.

^{xx} 35 U.S.C. 102(b), 35 U.S.C. 102(d).

^{xxi} Brian G. Brunsvold and Dennis P. O’Reilley: *Drafting Patent License Agreements*, 4th Ed. ©1971, 1984, 1991, 1998, BNA Books. ISBN 1-57018-129-2 (hardcover).

^{xxii} *Id.* at 42.

^{xxiii} *Id.* at 42.

^{xxiv} *Id.* at 13.

^{xxv} *Id.* at 321ff for an example of an employment agreement.

^{xxvi} HARRY POTTER is a trademark or registered trademark of AOL-Time-Warner.

^{xxvii} 17 U.S.C. 102(a).

^{xxviii} *Id.*

^{xxix} 17 U.S.C. 411(a).

^{xxx} John K. Halvey and Barbara Murphy Melby, “Checklists for Performing Intellectual Property Audits”, *The Intellectual Property Strategist*, January 1985, pages 2-4.

^{xxxi} Corbett at 656-657.