

IP Due Diligence Critical in Nanotechnology Transactions

BY PHILIP BRAGINSKY, SCULLY, SCOTT, MURPHY & PRESSER

It's a good thing for investors when an investment has real assets. While much has been said about the similarities in the emergence of nanotech and the Internet bubble, and much has been written about nanotech patents, the content and status of the intellectual property between the two is dramatically different. Nanotech IP is for real and will be around for a long time - and that's a good thing.

Today, the business of nanotech is more about intellectual capital than anything else. This capital is captured in the human resources (the brilliant people involved in nanotech from researchers to entrepreneurs), and the intellectual property (mostly in the form of patents and trade secrets). As always, a transactor is well served by knowing the details of this intellectual capital prior to making any transactions. Understanding human resources is a difficult and complex problem. Yet judging management and technical aptitude has become a good VC's *métier* and the management and engineers can usually be supplemented or replaced by a strategic investor or acquiror.

The intellectual property of a transaction target is far easier to understand than an entrepreneur's personality, but it is typically less understood by the transactor. Whether you are acquiring a company, making a strategic investment or spinning off a division, treatment of the IP may define the success of the transaction. This expertise is seldom a central part of the transaction team and still, in nanotechnology, the IP assets will surely be central to the success of the business. It is essential to bring this expertise in and ensure that a few buzz words have not persuaded you to consummate a deal you shouldn't have. Patents are sexy and inveigle many a deep-pocketed beholder, but caution here is counseled.

In nanotechnology transactions the IP assets are critical. Frequently, these transactions are motivated purely by the

technology. Yet it is typical for a venture investor to take at face value, without any further investigation, statements made in a business plan regarding a patent portfolio or proprietary technology. Indeed, many early stage investments "fail" due to fundamental misunderstandings regarding IP. It is also typical in an acquisition to neglect many important IP aspects, leading to reported cases where certain patents were not transferred or trade secrets were made public.

The nature and scope of a due diligence investigation depends on several issues including transaction type, the business models involved, and the maturity of the businesses. A competent due diligence must survey and inventory the IP assets involved in the transaction. A more sophisticated due diligence will verify chains of title, secure licenses, determine infringement issues and investigate adequacy of protection and scope of protection relative to the business and the competition. Of course, all of this must be done while evaluating privileges, and maintaining secure and accurate records. Particular concerns for nanotech transactions include technology ownership, the identification and maintenance of trade secrets, and the quality of patent examinations worldwide.

An expert due diligence will lend an understanding to these investigations that delivers value to a client. Value will be a function of managing time, timeliness, content and costs. Value therefore requires an understanding of what is more or less critical, what is more or less costly and what is more or less a priority to the particular client. Only with this understating can value be delivered from the due diligence investigation.

The diligence team must understand the industry, the technology, the transaction, and their role. An IP due diligence team should have a standing framework that can be rapidly applied and deployed to

any due diligence review. This framework consists of forms and procedures for cutting directly to the intellectual property assets and issues. Both the assets and issues must be inventoried first. Afterward, the inventory must be prioritized as to value and time constraints. For example, a threatened infringement litigation must be investigated prior to the use of generic trademarks.

To derive an accurate inventory, a well developed and easily understood due diligence request must be communicated. The request should include particulars such as identifying key business and technical personnel, identifying outside IP counsel, identifying scientific and technical publications, identifying invention disclosures and notebooks, and describing patent marking procedures. The team should also gather all public records, including patent office files and court filings. This includes ordering patent file histories, performing foreign counterparts and litigation searches, and conducting an inventor search and ranking.

Sometimes the response from such a request will produce an avalanche of material, sometimes a snowflake. This response must be immediately and critically reviewed to determine what is missing - and the missing material must be accounted for.

Additionally, constant reporting must be done concerning the investigation's progress. A final report delivered at the end of a transaction is of little help. In most cases, by the end of a transaction momentum to close is too strong to break. Real time updates and hot issues lists must be continuously communicated and processed.

Nanotech success will rely heavily on IP. To be on the right side of that ledger, eliminate as many risks as possible from your transactions. A proper due diligence investigation will help.