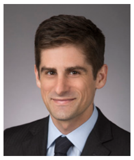
STARTING UP IP: PRIORITIES FOR EARLY-STAGE COMPANIES

BY VICTORIA R. M. WEBB AND BENNETT A. INGVOLDSTAD

This article gives a general overview of intellectual property (IP) for companies that are just beginning to recognize and capture the value of the IP they generate. Although early-stage companies have limited resources and time, awareness of some basic issues can help with prioritization and make the first meeting with an IP attorney more productive and less costly.

IDENTIFYING TYPES OF POTENTIAL INTELLECTUAL PROPERTY

Every business generates some type of IP, although not every business recognizes its IP or captures its value. The IP created by early-stage companies, especially those seeking venture capital funding, can often form the company's most valuable assets.[1] The United States, like most countries, provides several legal mechanisms for protecting IP. Trademark and trade dress rights protect the company's ***brand*** — the recognition and goodwill in the minds of its consumers through brand identifiers like logos, trade names, and product configurations. Patents protect a company's ***inventions*** — improvements to the state of the art developed by its employees — in exchange for the company disclosing those inventions to the public. Alternately, a company can keep its inventions secret and rely on trade secret law. Copyright prevents copying of the company's ***authored works*** — anything from code to images to the company website. Each type of IP has pros and cons, and multiple types may be useful in a given situation. Although an attorney can often most effectively identify and evaluate IP, a company short on resources can begin by compiling a list of potential IP before meeting with an attorney.

ELIMINATING QUESTIONS ABOUT OWNERSHIP

Once a company identifies its IP, it must ensure that it owns the IP. Generally, the more successful a business becomes, the more parties will come out of the woodwork with some kind of IP ownership claim.[2] The consequences of a company not actually owning its IP range from inability to enforce its rights against competitors to having to pay significant sums to later acquire the IP. Therefore, getting ownership issues worked out in writing upfront is an essential first step, and often the first time an early-stage company may engage an IP attorney.

For early-stage companies, ownership pitfalls arise at different points in time. First, founders and early collaborators often create IP before a company is incorporated, and that IP is owned by those individuals, not the company. Therefore, an early-stage company should verify that incorporation documents or a separate written agreement transfer ownership of any pre-incorporation IP to the company itself. Additionally, founders may not be employees of the company, so any future IP developed by the founders in connection with the company should be covered by an assignment agreement. Second, as early-stage companies expand, employment agreements should contain IP assignment clauses that effectively transfer ownership of IP developed by company employees. Third, early-stage companies will inevitably contract with third parties (vendors, consultants, or other contractors). To ensure that ownership of any IP developed for the company by the third parties transfers to the company, the company should include assignment clauses in contracts with the third parties or otherwise acquire the IP rights.

PROTECTING THE BRAND: TRADEMARK, TRADE DRESS, COPYRIGHTS, AND OTHER RIGHTS

A company's brand, as established by brand identifiers and customer-facing materials, may be as important as the products or technology it sells. Brand identifiers such as names, logos, and slogans can be protected using trademarks, trade dress, and domain names. Customer-facing materials (e.g., brochures, websites, advertising, etc.) can be protected using copyright. Although copyrights are created automatically, a company needs to take some steps to establish rights in brand identifiers.

Before investing in a brand identifier (or "mark"), a company should engage a trademark attorney to conduct a full clearance search — a search of federal trademark records, state records, and the Internet to determine availability of the mark. The goal of a clearance search is to evaluate not only whether a trademark application has a good chance of registering, but also whether the business is at risk of future legal troubles from other companies with existing rights in the same or similar marks. Considering the cost of potential litigation (or worse, having to abandon a brand the company has invested in), the cost of a clearance search is relatively minor. Sometimes even a quick do-it-yourself search on the Internet and of federal trademark records[3] before contacting an attorney for a more exhaustive search can reveal potential problems and save resources.

Once a company determines it can use a brand identifier, it can begin creating trademark rights via common law rights and federal trademark registrations. A company can begin to establish common law rights by simply adding a trademark (™) symbol after any mark on the company website, product literature, or other company materials. Although common law rights are cheaper and easier than registering a trademark, they afford fewer protections and make enforcement more difficult. Accordingly, companies should also consider registering their marks with the U.S. Patent and Trademark Office (USPTO). Advantages to registration over common law rights include presumptive ownership of the mark, nationwide protection of the mark, statutory damages for infringement, and benefits for filing internationally. These benefits are especially helpful if the company ever decides to enforce its mark through litigation. A trademark application should be filed as soon as possible, and can be filed even before the mark is being used. An early filing date is important, so if the company becomes aware of any similar mark in use by a competitor in any remotely similar field, a trademark attorney should be contacted immediately. Notwithstanding the added cost of applying for a registration, most businesses will greatly benefit from registering their trademarks.

In addition to filing trademark applications, desired domain names associated with the brand should be purchased. While many companies purchase .com domains early on, companies should also consider specialty domains (.blog, .store, .coupon, etc.) and foreign domain names, especially if the company envisions using these in the future for specialized marketing or for expanding the brand internationally. Once an early-stage company begins generating press attention,

MORE ▸

[STARTING UP IP, FROM PAGE 21]

there is a high risk that cybersquatters will purchase and try to ransom domain names in countries or spaces that the growing company will likely target in the future.

When resources are available, similar steps should be taken to protect all a company's brand identifiers, including product names, logos, slogans, advertising materials, and other branding. In most cases, early-stage companies must prioritize the marks or branding elements that are most critical to the company's overall brand and invest in protecting those marks first.

PROTECTING TECHNOLOGY: PATENTS, TRADE SECRETS, AND OPEN SOURCE ISSUES

In addition to building and protecting its brand, an early-stage company must make smart, strategic, and early choices to protect its investment into the inventions and technology it generates. Inventions and technology can be protected via patents or simply by keeping the inventions secret.

The first option is relying on trade secrets (e.g., the Coca-Cola formula). The default strategy is always to keep technical or inventive information secret, and even companies that rely on patents will choose this strategy while preparing their patent applications. To obtain trade secret protection, a company must take certain steps and use "reasonable efforts" to protect the information from disclosure and theft.[4] However, for some technologies, reverse engineering or re-implementation by competitors may be possible, which destroys the value of the trade secret.

If the company plans to publicly disclose an aspect of its technology, or if the technology is susceptible to reverse engineering or re-implementation, strong consideration should be given to filing a patent application. The patent application ideally should be filed before any public disclosure, and as early as possible once the technology is sufficiently developed. Costs can be minimized by filing cheaper provisional patent applications (a placeholder type of application), but a patent attorney should be involved; do-it-yourself patent applications of any type are usually worth very little.

Some early-stage companies forget that public disclosure includes talks with venture capitalists (VCs), potential partners, potential employees, and anyone not under a contractual obligation to keep information secret.[5] Most companies cannot avoid at least occasional public disclosures, but they can take steps to mitigate the impact on potential patent rights when patent applications have not yet been filed. Accordingly, companies should omit unnecessary detail during unprotected discussions with third parties, including VCs. Avoiding technical descriptions can preserve the company's ability to later patent those aspects. Although United States patent law does allow a one-year grace period for filing a patent application after public disclosure, it comes with significant risk of others taking the invention, modifying it, and patenting the modifications themselves. Additionally, other countries' patent systems do not allow any disclosure before filing patent applications, so if foreign patents are important, a patent application should be filed before any disclosure.

Once an early-stage company has decided to invest in filing patents on its technologies and products, a first meeting with a patent attorney will be most productive if the company has already thought deeply about the business case for filing a patent. A company should consider what aspect of its technology it needs to protect, what distinguishes the product or technology from its competitors, and what aspect the company believes is novel. The company should further consider which aspects, if protected, would allow it to block competitors in the future. While patent attorneys can determine the legal issues around filing a patent application, a business is in the best position to evaluate the value of a patent in the marketplace. A patent attorney should be able to provide some sense of what aspect of the technology can potentially be patented, and how much protection the business can potentially obtain. However, the scope of any patent (and even whether it will be granted) can be highly uncertain. Ultimately, it is the company's responsibility to manage this uncertainty and decide whether filing a patent is worthwhile.

In addition to carefully considering what to focus on in a patent application prior to meeting with a patent attorney, a company can also cut expenses by preparing detailed descriptions of its inventions before meeting with the patent attorney. Flowcharts, diagrams, and descriptions with as much detail as possible can reduce the time spent on discussions with the patent attorney. In addition, they can aid in development of initial figures or charts for the patent application.

Finally, software-focused companies should also take care when leveraging open source software. Inappropriate use of open source software can taint an entire code base, resulting in a company's valuable secrets becoming open sourced. Software-focused companies should carefully manage and catalog any usage of open source software to avoid accidentally open-sourcing company technology. Particularly, use of GNU General Public License (GPL) code and libraries without consulting an open source expert should be avoided. Keeping detailed records of open source packages, how they are used, and the license they contain will reduce headaches during due diligence (e.g., during a funding round or acquisition).

CONCLUSION

Every business needs to prioritize its IP, and early-stage companies are no exception. Early-stage companies have unique challenges because they rapidly generate IP, and often lack adequate legal representation due to juggling multiple priorities with minimal resources. However, the long-term success of a business can often hinge on whether it took appropriate early steps to protect its IP.

An early-stage company should first ensure its contracts effectively grant ownership of IP to the company itself. Next, a company should take steps to finalize and protect its branding by securing trademark and other rights and registering domains. Finally, an early-stage company should control its technology by filing patents on key aspects before they are disclosed to the public, and take care to avoid conflicts with open source licenses. Qualified attorneys should always be engaged to advise and secure the value of a company's IP. ■

1. IP additionally remains important throughout the lifecycle of a business. One study estimates that intangible assets, of which IP forms a significant part, make up 87 percent of the value of S&P 500 companies. See http://www.oceantomo.com/2015/03/04/2015-intangible-asset-market-value-study/.
2. A famous example involving a claim of partial ownership of Facebook was dramatized in the 2010 film "The Social Network." See CONNECTU LLC v. Zuckerberg, 522 F.3d 82 (1st Cir. 2008).
3. A basic trademark search can be run at tmsearch.uspto.gov. In the search results, a trademark is currently in force if it has a registration number and is marked "Live."
4. In practice, this often means taking security measures to limit access to the information to key employees.
5. Such contractual obligations often come in the form of nondisclosure agreements (NDAs). Although a company should try to obtain an NDA before any third party disclosure, many potential business partners (including nearly all VCs) will refuse to sign NDAs before hearing a pitch.