

TITLE: Top-10 Most Common Intellectual Property Rights Mistakes During Venture Capital Due Diligence

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1. TOO LATE TO START FILING US AND INTERNATIONAL PATENT APPLICATIONS.

Unfortunately for many good technology companies, it may be too late to file for patent protection. The current U.S. rule generally provides applicants with a 1-year grace period during which a patent application must be filed after certain public or private disclosure of the invention. Such disclosure may arise, for example, from a mere "offer for sale" of the technology, even if the product has not yet been built or prototyped. In comparison, the foreign rule, which applies to many industrialized jurisdictions, such as Japan and various European countries, do not give applicants the benefit of any grace period after a public disclosure has occurred. Thus, it is legally compelling for applicants to consider filing for patent protection sooner than later. Although in some situations, there may be some special exception which still allows for late filings; it is not advisable for applicants to count on those exceptions.

2. TOO NARROW LEGAL SCOPE OF CLAIMING PATENTABLE INVENTIONS.

Many issued patents are not commercially valuable because the scope of their submitted claims are particularly narrow, and can be relatively easily avoided by determined competitors. Thus when submitting new patent claim language, applicants should broadly define novel concepts that include potential design-arounds by other parties. Although this legal blocking strategy sounds easy enough to state as an objective, in fact, the serious exercise of analyzing future competitive and industry directions can be an extremely difficult task, particularly because the analysis often requires sophisticated market understanding, as well as technical and engineering vision.

3. INTERNALLY MISMANAGED PATENT INFRINGEMENT "WILFULNESS" EXPOSURE.

Under U.S. patent law, one's awareness or willful state-of-mind about the existence and infringement of a competitor's issued patent may significantly affect subsequent legal liability. Thus if a party is proven to be a willful infringer of a known patent, then for punitive policy reasons, economic damages may be awarded to the patent owner up to three times normal recovery amount. This treble-damage exposure is so substantial, that company management should be careful to avoid creating evidence of internal communications such as emails that may be construed later to indicate such willfulness state-of-mind. Additionally in many cases, it may be appropriate for companies as a matter of policy to discourage looking at issued patents owned by other entities. And

when a suspect patent is already known, management must take careful steps to refer the matter to competent patent counsel for appropriate analysis and opinion.

#### 4. RELYING SOLELY ON COPYRIGHTS FOR SOFTWARE PROTECTION.

Copyright protection in the U.S. and many other countries arises instantly and at virtually no cost to protect software technologies, such as computer programs, electronic databases, and graphical display screens and related media. In fact, copyright protection is often quite a suitable means to secure much digital media such as video and audio creative works, often even without compliance with copyright registration and notice requirements. Copyright protection, however, is legally vulnerable to reverse-engineering efforts by competitors, during which no copyright infringement may arise when the reverse engineering results does not result in literal copying of the original code, but merely an understanding of the underlying ideas and functions. In this vulnerable scenario, perhaps patent protection may be more appropriate to secure any novel algorithm, methods, and computing apparatus.

#### 5. INADVERTANTLY TAINTING I.P.R. WITH 3RD-PARTY CO-OWNERSHIP RIGHTS.

During the course typically of joint-development engineering projects, ideas may originate from many sources, such as advisors, consultant, employees, and even customers. This collaborative scenario sets the stage for creating intellectual property rights that may be co-owned by multiple parties. And unless the rights of such joint owners are specified up-front, for example by contract terms, then there is a problematic possibility that certain parties later may assert not just their partial ownership interest, but actually endeavor to offer licensing rights to other 3rd parties or even competitors.

#### 6. IGNORING THE IMPACT OF NEW "FESTO" U.S. SUPREME COURT RULING RE PATENT AMENDMENTS.

On May 28, 2002, the U.S. Supreme Court (*Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co., Ltd*) substantially changed the legal effect of amending patent claims, particularly upon the effective scope of amended claims. This judicial change cannot be ignored without possibly impairing commercial value of many issued U.S. patents, especially where applicants introduce explicit argument that distinguish various prior-art cited by the Patent Examiner. Without getting into the subtle legal and policy complexities associated with the so-called "Doctrine of Equivalents," the Festo decision and related subsequent federal cases clearly narrow many patent claims scope whenever applicants propose routine amendments to distinguish the claimed invention against cited prior-art references.

#### 7. UNDERESTIMATING THE IMPORTANCE OF TRADE SECRETS AND CONFIDENTIALITY.

Since patent protection may not arise for many years until after filing patent

applications, and copyright protection may not be applicable to protect functional aspects of various technologies, trade secret protection may serve realistically as a solid backstop against competitive piracy or other misappropriation of company know-how. Thus the importance of diligent use of Non-Disclosure Agreements (NDA) and in-house policies and systems to secure confidential and proprietary information rises to a more significant level of management priority. Additionally early disclosures, for example through customer marketing presentations, may irreparably hurt company rights to file domestic or international patent applications.

#### 8. OVERLOOKING LEGITIMATE OPPORTUNITY TO SET-UP OFFSHORE LICENSING TAX SHELTERS.

Often neglected by early-stage startup companies and entrepreneurs are offshore strategies for mitigating federal tax exposure. Such international tax strategies are especially relevant when foreign licensees of intellectual property rights are contemplated possibly in the company business plan. In many cases in fact, it is particularly beneficial to deploy one or more corporate entities offshore much sooner, rather than after licensees are identified, in order to minimize certain taxable valuation exposure associated with transferring such licensed rights.

#### 9. RESPONDING SLOWLY TO U.S.P.T.O. OFFICE ACTIONS.

Because the U.S. patent rules now provide 20 years of enforcement patent protection, after the U.S. filing date, it is important to expedite the claim amendment and application prosecution process; otherwise applicant's enforcement period is effectively eroded by unnecessary delays in the process. Accordingly, applicants should endeavor to respond in timely fashion, expediting all office action responses and facilitating communications with patent counsel whenever possible. Additionally, the new patent rules actually apply a time penalty to deduct enforcement period against issued U.S. patents in certain situations where applicants contribute to delays during patent prosecution.

#### 10. OVER/UNDER-SPENDING ON LEGAL FEES TO PROSECUTE PATENT APPLICATIONS.

In the realistic context of the current economic recession especially in Silicon Valley, startup companies and entrepreneurs who are strapped for cash may negotiate for substantial fee discounts from patent counsel to prepare and file patent applications. However, patent applicants should be careful to ensure that most qualified legal counsel in terms of technical and business experience are selected and engaged to work on critical company inventions, perhaps with bottom-line pricing being just one of a number of significant factors to consider.