Intellectual Property Audits in Intellectual Asset Management

by Yvonne Pah - y.pah@tamimi.com -

July 2011

Intellectual assets not only encompass registered intellectual property (IP) rights, such as: patents, trademarks, and design rights; but also include rights that are unregistered, such as confidential information, trade secrets, technical information, circuit layouts, know-how, copyrights (registration whereof is optional), human capital, industry knowledge, contractual relationships, innovations and goodwill.

Intellectual assets not only encompass registered intellectual property (IP) rights, such as: patents, trademarks, and design rights; but also include rights that are unregistered, such as confidential information, trade secrets, technical information, circuit layouts, know-how, copyrights (registration whereof is optional), human capital, industry knowledge, contractual relationships, innovations and goodwill. These subject matters often provide a particular organisation its competitive edge in the market.

'Intellectual asset management' is the phrase that is used to describe the process for capturing and managing knowledge to exploit for commercial gain. In a global and knowledge driven society, there exists a high degree of recognition that the assets of business now extend largely to intangible and intellectual assets. These intellectual assets, if managed and treated appropriately, enable organisations to maximise their value, minimise risk of infringement and third party abuse thereof.

Traditionally, inventory of physical assets of an organisation used to be carried out for the purposes of accounting and taxation. The inventory also allows an organisation to assess whether the physical assets are in usable order, need replacement, are not threatened with extinction or damage, or are redundant. In managing intellectual assets, the same principle is applied when we speak about intellectual property audits ('IP audits'). IP audits list any information pertaining to the origins, maintenance, and use of IP rights, in turn providing management with guidance on how returns may be generated from such rights. IP audits are not limited to registered rights but also any other intangible creative output of value to the business as highlighted above.

In conducting an IP audit, the driving factor should be whether the organisation is extracting the maximum value from its IP assets. Matters that typically arise in such an exercise include factors such as whether royalty payments that are being paid or received reasonably reflect the value of use of the subject matter, whether there are any risks associated with use of certain IP rights that may outweigh the value from their use, and whether there are any redundancies in terms of maintenance of IP rights. In terms of translating the value of IP assets onto the balance sheet, there are several accepted principles of valuation adopted by accountants that address as to what is and what could be the value of such rights.

IP audits can be conducted as a matter of good practice or upon the occurrence of certain events such as the incorporation of a new company; a corporate change such as a merger, acquisition or listing; a potential joint venture; an investment into another company purporting to have the know-how for certain innovations; or a sale of part of the business that includes assignment or transfer of rights.

A preliminary step in conducting an IP audit is to identify the IP assets. The identification process is likely to be more straightforward in terms of registered rights, such as patents and trademarks, but may require further inquiry with regard to others assets such as know-how and enterprise knowledge.

Once the IP assets have been identified, the next stage of the inquiry will turn to its origins and creation. This will lead to questions relating to the nature and extent of ownership of the IP assets. Documents that may be relevant at this stage include employee and consultant agreements, lab notebooks, marketing material and publications. This stage is also likely to include discussions with personnel from research and development, branding or marketing and the design team. In the course of collating data relating to the foregoing, it is good practice to simultaneously create an internal IP register, if this is not already in existence. Subsequent audits can then be limited to updating such a register.

Further issues that will need to be considered include the cost of protecting the IP assets and the extent to which they have been or will be commercialised or used. The costs and revenue associated with both (commercialisation and use) will be assessed during the commercial decisions made for the organisation.

Apart from the focus on the organisation's own IP assets, an IP audit will also consider the contractual arrangements it has with other parties regarding the right to use third parties' rights. Agreements in relation to matters, such as licensing, assignments, technical assistance, technology transfer, know-how, franchise, and marketing activities; are likely to be relevant during this stage.

Another inquiry to be made regarding third parties' rights is the potential risk of infringement of such third party IP rights. By way of illustration, there are instances where the research and development team may not be aware of certain existing technologies in another part of the world whilst developing a similar technology. The potential risk that could arise here is that the technology being developed may infringe the rights subsisting in existing technology elsewhere. The same may also apply to a brand that could be identical or similar to a prior registered trademark in a particular jurisdiction. Such conflicts can sometime arise due to the fact that national level IP protection regimes operate independent of each other, and afford statutory protection to the party who is first in time to seek such protection through registration.

Ownership of IP assets is another matter to be considered in an IP audit. IP assets are typically created by the employees of the organisation, a third party commissioned by the organisation, or in collaboration with another organisation. Inquiries then are made to ascertain whether or not clear documentation exists as to which organisation(s) own the IP assets and, if not, whether that was intended to be the case.

In order for organisations to determine if additional revenue streams are available from innovations supported by it, an IP audit must be carried out. As this article illustrates, where this is carried out, there will also be inquiries made on other associated factors, which can include risk and cost management issues surrounding use and protection of the IP assets.