November 2014

STARTUPSOURCE

Brought to you by Aird & Berlis LLP

STARTUPSOURCE.ca

Ten Common Intellectual Property Mistakes Startups Make

By Mathew Goldstein, Ken Clark and Tim Jones*

Succeeding in a disruptive tech business is a daily battle. A good, strong suit of protective armour can help you make it through unscathed. Your IP protection can be that armour – a sword against imitators and a shield against counter-attacks. Mistakes in your early-stage IP strategy could create headaches down the road and jeopardize your success. Here are 10 errors we commonly see startups make:

REGISTRATION ISSUES

1. Nobody else has the domain name, so you think nobody's registered the business name.

Commercially available name generators will check your proposed business name for conflicts with existing domain names. But not finding any conflicts does not mean the corporate name or trademark is available! A NUANS corporate name search and a federal trademark search are must-dos for any entrepreneur who wants to ensure that their intended identity doesn't infringe.

2. You were able to register a business name, so you think it must be safe from infringement.

Founders often think that Corporations Canada or other incorporating agencies would not allow them to register a given business name that infringes on an existing trademark. Wrong again. There is no substitute for the aforementioned searches.

3. You didn't trademark your identity.

A trademark provides protection over the reputation of your goods and services by ensuring that a given word, phrase or image (like a business name or logo) is associated with your company. Trademark protection is preventative and stops infringement by others. Registration is relatively inexpensive and grants Canada-wide protection.

4. You are planning to market your invention, but aren't planning in advance to patent it.

A patent is a monopoly right on an invention for a set period in a given jurisdiction. It prohibits others from making or exploiting the patented item. When you're ready to talk about your idea or product in public (i.e. when it's time to sell it or fundraise around it), it may be time for a patent. But be careful – if you disclose too much to the public, you could jeopardize the right to obtain a patent.

Patents are expensive, unwieldy and time consuming ($15,000-$20,000 per country on average and roughly two years, minimum, to obtain) but they are the best protection available for high-volume / value products and even some services. Start thinking about it early, before someone else exploits your concept.

EMPLOYEE AGREEMENT MISTAKES

5. Your employee has the moral rights to property you're selling.

Whereas copyright to employees' works is generally owned by the employer (including the right to economic exploitation of the work), the authoring employee will, by default, retain moral rights. Moral rights are the author's rights of association with a work. They protect the work's integrity, allowing rights-holders to, among other things, prevent any editing of the work. This is relevant for assets like code, logos or marketing plans. Moral rights cannot be assigned or transferred, only waived, so consider putting moral rights waivers in employment and other contracts. (Make sure you have one in the first place – perhaps the most common employment agreement mistake is not having one.)

6. Your graphic designer owns your logo and your web designer owns your website.

Logo and webpage design are often done by independent contractors. Generally, contractors own the copyright to their work unless that copyright is assigned in writing, just as authors own moral rights unless they are waived. Because of this, many companies don't realize they don't own the assets they use every day.

7. You're not sure if your programmer can patent the code he writes.

Most programmers and developers employed by a startup would be considered "hired to invent" under common law, and therefore could not own patent rights to their code. However, it is risky to rely on this without documents backing it up. A lack of clarity in this area can result in protracted arguments. If the employee thinks they own their coding or their new feature idea, it almost doesn't matter whether they're right or wrong under law – it's an expensive headache for the company either way. Further, the employee is under no duty to disclose new "inventions" made on company time unless this is contractually stipulated. Prudent managers clarify expectations and obligations up front in employee agreements.

8. You think non-disclosure agreements don't matter anymore.

You've heard people say that California has practically stopped enforcing non-disclosure agreements (NDAs). They say that no VC or angel would ever sign one. Some people say the NDA itself is an outmoded concept. Should you abandon them as a legal option? Absolutely not. Whether they are enforced or not, NDAs can have a strong deterrent effect on ex-employees. In this competitive, high-turnover sector, there is a real risk of software designers leaving for competitors, or sales staff taking customer lists. The threat of NDA enforcement can be persuasive. That said, simply having a NDA alone is not enough – NDAs are only part of an information protection strategy. Without other measures to protect disclosure of information (such as document management policies and special training), it may be tough to prove in court that the information was truly intended to be confidential.

9. You adapted a U.S. employee contract.

Many precedent employee agreements are available online, but it is essential that, if relied on, they are tailored to a startup's particular circumstances. This is especially the case if the precedent is non-Canadian. Google provides a wealth of information about U.S. intellectual property concepts like "work created for hire," but these concepts may not translate between legal systems. "Work created for hire" specifically does not apply in Canada in the same way it does in the U.S.

WHY IP MISTAKES MATTER

10. You can't raise money or sell your business because you've failed an IP audit.

Investors will conduct due diligence into your business before they put any money in. The scrutiny is even more intense when an outside party is considering an acquisition. They will find the loose ends. Part of their diligence process is an inventory of your intellectual property to ensure that everything associated with the business can, in fact, be purchased with the business.

If your intellectual property assets are registered to outdated or inappropriate entities (e.g. contractors, subsidiaries, holding companies, your former name, your old sole proprietorship), you may experience serious problems at the exit stage. Do your due diligence before the investor does, and make sure you tie up any loose ends to your intellectual property ownership.

Aird & Berlis LLP has experience assisting startups with intellectual property matters, including patents, trade-marks, copyright, industrial designs and trade secrets. For more information, click here.

**Tim Jones was a summer student at Aird & Berlis LLP.*

Mathew Goldstein
Associate

Mat is a member of the firm's Financial Services Group. Prior to joining A&B, Mat practised at a top-tier New York City law firm.

Mat practices in the areas of corporate/commercial, banking and bankruptcy law, with a focus on financing transactions and restructuring.

Additionally, Mat advises entrepreneurs as well as start-ups and emerging companies, including those in the media and technology sectors, with respect to corporate structure, governance, financing, technology licensing and commercialization.

Mat is a contributor and editor of startupsource.ca, a blog which features timely commentaries on the latest developments in Startup news, events and information on capital raising and planning for future growth.

E mgoldstein@airdberlis.com | T 416.865.4637