

Trademarks in Transactions - Part II: Rap about Reps & Warranties

Kluwer Trademark Blog

March 15, 2018

Kai Schmidt-Hern (Lubberger Lehment) and Benjamin Koch (Lubberger Lehment)

Please refer to this post as: Kai Schmidt-Hern and Benjamin Koch, 'Trademarks in Transactions - Part II: Rap about Reps & Warranties', Kluwer Trademark Blog, March 15 2018, <http://trademarkblog.kluweriplaw.com/2018/03/15/trademarks-transactions-part-ii-rap-reps-warranties/>

This post is the sequel to the post 'Trademarks in Transactions - Part I: Due Diligence' which dealt with trademark issues which regularly arise during the due diligence phase of an M&A transaction.

Once the due diligence phase is over, and often already during the due diligence phase, the parties of an M&A transaction will start negotiating the seller's representations and warranties in relation to the company and its assets, including its trademarks. The buyer will ensure that the findings of the due diligence, in particular red flag issues, are adequately addressed and covered in the reps & warranties and indemnification clauses. This second part of "Trademarks in Transactions" deals with the issues surrounding the trademark reps & warranties that are typically discussed and negotiated with regard to a Share Purchase Agreement or an Asset Purchase Agreement.

Unrestricted Ownership

The typical starting point of the reps & warranties catalogue is the seller's representation that the schedules contain a correct and complete list of all (registered) trademarks owned by the target company (in the case of a share deal) or the seller (in the case of an asset deal). Buyers will reasonably expect the seller to further represent that it/the company is the unrestricted legal and beneficial owner of such trademarks, is free to dispose of them, and that the trademarks are

free of encumbrances. It is advisable to clarify that the term “encumbrances” only includes pledges, usufructs, and other security interests and liens, but not licenses granted to third parties (as licenses are usually dealt with separately).

Granted Licenses

Buyers insist in general on a representation that no licenses under the company’s/seller’s trademarks have been granted to third parties (other than those disclosed in the schedules). Such a representation is important, considering that under most jurisdictions licenses continue to be valid (and potentially devalue the trademark), even after a change in ownership of the company (in the case of a share deal) or an assignment of the trademarks to the buyer (in the case of an asset deal). In some cases, however, it may be necessary to narrow down the clause in order to avoid misrepresentations: For instance, many distribution contracts concluded between a trademark owner and resellers of the branded goods contain a right of the reseller to use the trademarks in advertising and at the point of sale. As many of these clauses go beyond the fair use right resellers enjoy under the applicable law, they qualify, strictly speaking, as a license agreement and therefore are excluded from the representation in most cases. Another example is intra-group licenses which are, in many groups, granted for all IP rights owned by the group companies. The seller may have a legitimate interest not to disclose all such intra-group licenses, at least as long as the seller warrants that those licenses will terminate as of the closing date of the transaction.

Obtained Licenses

If the company has obtained trademark licenses which are significant for the company’s business, the buyer (in the case of a share deal) will want to make sure that the licenses are in force and will continue even after the transaction has been closed. A standard representation would be that the licenses have been validly granted and have not been terminated, and that to the seller’s best knowledge the respective licenses cannot be terminated by the respective licensors for cause. This would be a customary rep at least if limited to the situation which exists at the signing date or closing date. That representation typically excludes the question as to whether the licenses can be terminated by the licensors because of the contemplated transaction under change of control clauses. It is the buyer’s homework during the due diligence phase to review the agreements for change of control clauses. The seller may under certain circumstances agree to refund part of

the purchase price or rescind the transaction if important license agreements are terminated, but the seller should not give a warranty that the license agreement cannot be terminated if they include change of control clauses. In asset deals, if a trademark license forms part of the assets sold and assigned, a similar issue arises in relation to the assignability of the license.

No Infringements

The buyer's preference will always be to obtain a hard representation that the company, or respectively the company's trademarks, are not infringing any third party's trademarks, and that no third parties are infringing company's trademarks. But for the seller this is difficult to accept, particularly considering that the similarity between trademarks is hardly a clear-cut assessment and that court and office decisions are difficult to predict. Usually, it is a good compromise to focus representations on any litigation threatened or pending within a certain time frame before the signing date, and on the seller's best knowledge in relation to other (potential) infringements.

Valid and Enforceable Trademarks

A rep & warranty that all of a company's trademarks are valid and enforceable sounds reasonable, but in fact is hardly acceptable for seller: In many cases trademarks are registered for goods and services for which they are not used. They may be at least partly vulnerable to cancellation on non-use grounds (after the grace period has expired, dependent on the applicable law). Furthermore, unless a company's trademarks have already been used for many years, it will be difficult to exclude the existence of third party trademarks which could be asserted against any of that company's trademarks. Representing that the trademarks exist validly at the signing date, have been properly maintained and that the seller has no knowledge of any third party trademarks which could be asserted against the validity usually sounds like an acceptable compromise.

Indemnifications

If the buyer has come across red flag issues during the due diligence it may decide to request an indemnification - at least in more severe cases such as trademark disputes with a higher potential of damage claims or rebranding costs. Negotiating indemnification clauses and conditions can be burdensome, given that both parties talk about the sharing of risks and the liabilities in worst case scenarios. A focus in

such negotiations usually lies in the period for which the indemnification is granted, the definition of claims and damages subject to indemnification (direct/indirect damages, loss of profits etc.) and formal and procedural aspects (e.g. notification periods and requirements, determination of the party having control over defense and settlements, and the obligations of the parties to assist each other). Negotiating indemnities in many transactions is one of the last major issues, and if the parties have agreed on them, they will all usually hope that the dark scenarios they have discussed for days and nights, will never occur in practice.