

IP monitor

Buyer beware: IP is not just another asset

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There is no doubt that trade-marks, brands, and other trade indicia and intellectual property (“IP”) can be one of a company’s most valuable assets. That does not mean that trade-marks and other IP can be treated like any other asset in the context of an acquisition. The dangers and potential consequences of failing to appropriately and specifically consider trade-marks, goodwill, and other intangibles when purchasing a business were illustrated in the recent Federal Court of Canada decision *1429539 Ontario Limited v. Café Mirage Inc.*, 2011 FC 1290, (“*Mirage*”).

Facts and findings in *Mirage*

The Plaintiff in *Mirage* operated a franchise known as “The Symposium Café”. At its peak, the franchise comprised five restaurants before encountering financial difficulties. As part of a debt settlement, the Plaintiff sold two of the restaurants to a creditor who then sold them to the Defendants on an “as is” basis.

The new owners declined to join the Symposium franchise system and operated the restaurants under the name Café Mirage while retaining the appearance, trade dress, trade-marks and menus of the Symposium Café.

The Plaintiff, the original franchisor, brought an action against the Defendants for infringement of trade-marks, copyright, and related IP associated with the franchise.

Although it was not explicitly set out in the agreements of purchase and sale, the Defendants argued that by acquiring the business of the two restaurants they also acquired the right to use the trade-marks, and other IP associated therewith.

On the issue of trade-marks, the Court found that the assets of the business did not include a right to use the trade-marks associated with those assets outside of the franchise system.

The Plaintiff also claimed that the Defendants’ new menus, which were based on those acquired from the Plaintiff as part of the deal, infringed the Plaintiff’s copyright. The Court found that while the asset transfer included an implied license to use the menus that were the subject of the asset sale, “*copyright does not transfer with the physical assets such as menus.*” Therefore, notwithstanding the asset sale, the Defendants had no right to produce an updated menu that was a substantial copy of the Plaintiff’s.

In the result, the Court issued an injunction preventing the Defendants from using a number of trade-marks that formed part of their business. The Court also awarded damages for infringement of the Plaintiff’s copyright.

Considerations in an acquisition

As the *Mirage* case demonstrates, proper IP due diligence is essential in order to determine exactly what rights are owned by the seller, what rights are included in the sale, and what rights are required in order to take full advantage of the assets being acquired.

Once the IP landscape is properly understood, parties to a transaction should ensure that IP rights are specifically addressed in the relevant agreement. In the *Mirage* case, had the IP issues been addressed up front, it is unlikely that the parties would have found themselves litigating the IP rights before the Courts.

Considerations in a licensing arrangement

The responsibility to carefully consider the implications of a transaction involving IP falls on both the buyer and seller. The seller and trade-mark owner should particularly consider the value and any licensing associated with the trade-mark.

The distinctiveness and non-use risks in trade-mark licensing

A trade-mark, by definition, is a word or design that is capable of distinguishing one trader's wares or services from those of another. In a licensing scenario, where a trade-mark is used in association with the wares and/or services of the licensor as well as one or more licensees, the simultaneous uses, if not appropriately monitored and controlled, may weaken the trade-mark's ability to distinguish the wares or services of the true trade-mark owner (licensor). This may prejudice the trade-mark owner's ability to enforce its rights.

Another consideration in licensing scenarios is potential exposure to a non use challenge. The *Trade-marks Act* allows a third party to challenge a registration on the basis of non-use. Faced with such a challenge, the registered owner must show evidence that it has used the trade-mark in the preceding three years. In situations where the mark is only being used by licensees, the licensees' use will only accrue to the benefit of the registered owner (licensor) if the owner (licensor) retains control of the character or quality of the wares or services to which the trade-mark is applied. Failing to demonstrate use can result in the expungement of the trade-mark from the register.

In order to ensure that a licensor's trade-mark rights are secure, certain terms should be included in trade-mark license agreements. First, the licensor should have the ability to inspect and control the character and quality of the wares to which the trade-mark will be applied. Further, the licensee should be required to indicate on its wares or advertisements that the trade-mark is being used under license from the licensor. Also, the registered owner (licensor) should limit the licensees' ability to deviate from the trade-mark as registered. Depending on the circumstances of any given situation, other considerations may apply.

Conclusion

Parties to commercial transactions should take care and pay attention to the rights and value of any associated IP. From a buyer's perspective, a failure to properly address intangible assets can give rise to uncertainty and costly litigation, as was the case in *Mirage*. From a seller or licensor's point of view, a failure to include certain provisions in an agreement can severely undermine existing rights and could also result in costly litigation.

Assessing a transaction's IP landscape and ensuring that the necessary terms are included in any agreement is a better means of providing predictability and confidence.

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