HUGOTAVOCATS
M&A in FOSS

A Practical Approach
OVERVIEW

- Intellectual Property: main value when acquiring a software or an internet company (along with the people)

- Purchaser wants to have the best price with the lowest risk

- Risk management from a legal standpoint:
  - Due Diligence
  - Representations and Warranties
OVERVIEW: DEAL SCHEDULE

- Negotiations between the parties (main structure of the deal and price)
- Drafting and negotiation of a term sheet
  - outline the deal
  - Set forth an exclusivity period
- Due Diligence
OVERVIEW: DEAL SCHEDULE

• Negotiating the long form agreements (during or after the due diligence):
  – Shares purchase agreement
  – Warranty deed
  – Disclosure letter
  – Corporate documentation
DUE DILIGENCE: BASIC PRINCIPLES

• Purchaser requests as much information as possible in various field (corporate, tax, labor, IP, etc.)

• Information could be divided into two categories:
  – Specific information
    • E.g. « list of all open source software »
  – Catch all information
    • E.g. « any information that could materially affect the value of the operation »
DUE DILIGENCE: BASIC PRINCIPLES

• Seller is solely responsible for providing complete, truthful, accurate, clear, non-misleading information
  – M&A is the perfect information world (from the Purchaser’s perspective)

• Rationale: information provided by Seller must confirm the valuation agreed upon or more generally the deal itself

• Bottom line: M&A are based on the assumption that no information is lacking, even though such information is not identified
REPRESENTATIONS & WARRANTIES

• Seller will be asked to make various representations, i.e. basically state that everything is in order, everything has been done lawfully since the incorporation of the company, etc.

• Seller will be asked to warrant said representations are truthful and accurate and will be liable (i.e. payment) for any damages arising out of said representations.
REPRESENTATIONS & WARRANTIES: WAY OUT

• Disclosure letter: a way for Seller to avoid (or limit) its liability is to disclose (i.e. inform the Purchaser) anything that is not in line with the broad representations requested by Purchaser

• Good for both parties:
  – Purchaser knows what it is buying;
  – Seller limits its liabilities
INTERMEDIATE SUMMARY

• Due Diligence: identify possible issues

• Representations & warranties: state that everything is in order

• Disclosure: limit Seller’s liability (based upon the due diligence)
APPLICATION TO FOSS: GENERAL COMMENTS

• Many legal documents are not adapted to FOSS but only to proprietary software (although less and less the case)
  – Many lawyers are not either!

• Paramount for the Seller to understand, identify, disclose FOSS

• Paramount for the Seller to adapt the legal documentation
DUE DILIGENCE & FOSS

• Two main categories
  – Software licensed to the Seller;
    • E.g. Development software, operating systems, etc.
  – Software licensed by the Seller
    • E.g. the product actually « sold » by the Seller

• Purchaser usually requires that Seller (FOSS and non-FOSS):
  – List all software used by the Company
  – Provide the corresponding licenses
• Analyzing FOSS and non-FOSS licenses is different:
  
  – Non-FOSS: mainly verify if the fees are paid and if the use is conform with the license (e.g. number of copies used, on site / off site restrictions, etc.)
  
  – FOSS: fees are not an issue! But need to verify the type of licenses, the use made, and the compatibility, etc.
DUE DILIGENCE & FOSS

- My recommendation: Seller must make its own FOSS list and analysis:
  - Seller must know its code *(what is used and how it is used)*
  - It should be requested by Purchaser (not always the case)
  - It will have consequences on the representations and warranties (and any disclaimer)
DUE DILIGENCE & FOSS

- For each FOSS, proposed list of data:

  - Name and version of software
  - Name and version of license(s) (and URL)
  - Author(s) and project website
  - Type of user interaction (internally used, SaaS, installed on client premises, etc.)
  - Software programs with which it interacts
  - Type of modifications to the Software
DUE DILIGENCE & FOSS

• Purpose:
  – Ensure that the common basic requirements are met for all FOSS programs (no warranty, access to code & license)
  – Identify which software is copyleft
  – What triggers the copyleft clause (mere interaction or distribution)
  – How strong is the copyleft (extent only to the covered program or to any derivative / linked program)
• In other words: identify any license violation
  – usually, there are violations!
SELLER’S REPRESENTATIONS & FOSS

• Sometimes still see broad representation clauses such as:
  – « Seller warrants that it owns all intellectual property rights in software programs used by Seller »

• Or worst clauses:
  – « Seller warrants it does use any free or open-source software program »
SELLER’S REPRESENTATIONS & FOSS

• Such clause are bad for two reasons:
  – They make no sense at all in today’s world;
  – They may have a vicious effect:
    • Purchaser might be happy to have the widest representations as possible, but
    • This does not compel the parties to identify any violation of a free or open-source license (and incidentally, Seller gives a representation that is not true)

• M&A are the last chance for the Seller to identify any FOSS issue (should have been done before though)
REPRESENTATIONS & FOSS: WHAT TO WRITE

• Always write something that is truthful
  – Well done due diligence is the key

• What the Seller can state is that:
  – « FOSS (including derivative works) are used pursuant to their respective licenses »

  – « There are no incompatibilities between FOSS programs as used by Seller »
FIXING VIOLATIONS

• Once a violation has been identified:
  – The Seller must disclose it
  – The Seller (usually in accordance with the Purchaser) must fix it

• How to fix it depends on the license, in all events:
  – Immediately stop any non-compliant use
  – Pay for the commercial license (if available)
  – Contact the project manager / author
TO CONCLUDE: A FEW PERSONAL THOUGHTS

• If you own a software company: don’t wait for due diligence to identify violations:
  – Set up the appropriate open source governance (be sure it is way cheaper to do so than to fix violations)
  – Ensure the developers know what can / cannot be done
  – Ensure all relevant information flows between the members of your team
  – Involve your lawyer / legal team in your compliance process
TO CONCLUDE: A FEW PERSONAL THOUGHTS

- Cost of being compliant is much lower than the cost of developing the corresponding free software
- Don’t be scared, FOSS is good: it is an opportunity, not a liability

BE FAIR WITH THE AUTHORS
DON’T HIDE IT, FIX IT!
THANK YOU FOR YOUR ATTENTION

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