

December 2009— Accidental Copyright Infringement During Corporate Restructuring

In the recent case of *Cincom Systems, Inc. v. Novelis Corp.*, 581 F.3d 431 (6th Cir. 2009), companies learned a new fear when going through a corporate reorganization: The software on their computers can open a whole new realm of liability.

All of the software you purchase carries a license agreement. Copyright licenses are by default non-transferable. Even where it is explicitly listed in the license agreement, the designers usually add a non-assignability clause. If a party transfers a license to their software without permission, they have committed copyright infringement. The hidden danger is, according to *Cincom*, a corporate restructuring can now lead to infringement.

In *Cincom*, a company (Alcan) had two subsidiaries. Alcan merged the two subsidiaries into a new entity: Novelis. After the merger, Novelis continued to use the software, which stayed on the same computer, in the same office, but the office had a new name on the door. According to the Sixth Circuit in *Cincom*, Novelis infringed on *Cincom's* copyright by using the software without a license. The end result: almost half-a-million dollars in statutory damages against Novelis.

The reasoning is simple. A corporation (or an LLC, or other types of corporate entities) is a legally separate being. If a new legally separate being has the licenses after the restructuring, then those licenses have been transferred. If the licenses are transferred without permission, then copyright infringement has occurred.

Unlike most other areas of law, copyright infringement has the potential for statutory damages that are unconnected to the actual damage incurred. Each incident could lead to \$150,000 per incident, plus attorneys fees. This is true, no matter what the actual price of the software would be.

Cincom can be boiled down to one rule: If the owner of your software is a different legal entity at the end of the day, you may face liability. *Cincom* is also a warning.

It could affect businesses in any number of scenarios, including:

- Corporate Restructuring (including changing from an LP to an LLC, or other forms)
- Mergers
- Asset Purchases
- Single Purpose Entity Transactions
- Trusts



There are two ways to prevent liability under *Cincom*: (1) When purchasing software, negotiate an assignment clause in case of corporate restructuring; or (2) contact the software distributor during your due diligence period and negotiate an assignment. Otherwise, the costs of your restructuring could rise exponentially.

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