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IMPLIED TERMS IN LICENCE AGREEMENTS AND LIMITATIONS ON CONFIDENTIALITY

28 February 2018

The Court of Appeal (the "**Court**") in the *Kason Kek-Gardner Ltd v Process Components Ltd [2017] EWCA Civ 2132* (the "**Kason Case")** assessed and made a decision regarding the business efficacy test for implying a term in the context of an alleged breach of confidentiality provisions in an intellectual property licence.

IMPLIED TERMS

Implied terms are terms that have not been expressly agreed by the parties, but are implied into the contract by the Court. The Court can imply a term based on several factors including:

- usage;
- the parties' previous course of dealings;
- the intention of the parties;
- common law; and/or
- statute.

As set out in *Marks and Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd [2015] UKSC 72,* the test for implying terms in commercial contracts is that:

- the term must be necessary to give the contract business efficacy; or
- it must be so obvious that it goes without saying.

FACTS OF KASON CASE

The Kason Case was concerned with Kemutec Powder Technologies Ltd ("**KPTL**") who owned certain intellectual property rights ("**IP**") relating to its businesses, including the rights related to the assembly and sale of certain industrial machines and the use of trade names associated with them.

KPTL went into administration and its administrators entered into an asset sale agreement ("**A1**") with Process Components Ltd (the **"Claimant**") for certain parts of KPTL's business. The administrators entered into a second asset sale agreement ("**A2")** with Kason Kek-Gardner Ltd (the **"Defendant**") for the remaining parts of the business. Each asset sale agreement included the sale of IP used in the 'Business', but the agreements failed to clarify what this meant.

The Claimant entered into a licence agreement with the Defendant whereby the Claimant licenced the use of IP relating to the machines to the Defendant. The Defendant was subsequently acquired by a competitor of the Claimant, and the Defendant disclosed the licence agreement to the competitor during the due diligence process. This resulted in the Claimant terminating the licence agreement.

The Claimant claimed that they were able to terminate the licence because:

- the Defendant had breached confidentiality; and as a result
- the Defendant no longer had the right to use the IP under the licence.

The Defendant responded that:

- it did not need the licence to use the IP as it had already acquired the IP through the A2 agreement with KPTL's administrators; and
- the confidentiality clause in the licence agreement was subject to an implied term.

BUSINESS EFFICACY TEST FOR IMPLIED TERM

The Defendant argued that the confidentiality clause in the licence agreement was subject to an implied term that the Defendant was permitted to disclose the licence agreement 'for reasonable business purposes', which included disclosure to a prospective purchaser. Lewison LJ held that this implied term did not fulfil the business efficacy test, as the business purpose of the licence agreement was to enable the Defendant to operate its parts of the business. Therefore, a sale of the Defendant's shares by its shareholders was not a necessary business purpose of the licence. This case serves as a reminder that a contracting party's wider business purpose is not relevant to a consideration of whether a term should be implied to give business efficacy to a contract.

DRAFTING CONSIDERATIONS

When drafting confidentiality clauses or non-disclosure agreements ("**NDAs"**), care should be taken to ensure that all disclosure purposes a firm may need are covered. To prevent a potential breach of confidentiality, parties should negotiate and include the circumstances in which they would need to disclose confidential information to third parties in the ordinary course of business. Whether this is effective in preventing a breach depends on how well the NDA covers all situations where the company will need to disclose.

NEXT STEPS

For more information, and any guidance or advice on the enforceability of your contracts and confidentiality clauses, Cleveland & Co External in-house counsel, your specialist outsourced legal team, are here to help.

DISCLAIMER

WHY WE'RE DIFFERENT

Cleveland & Co are specialists in financial services, investment management and commercial contracts and related courses. Our team's in-house experience means we understand client challenges and we work alongside you to create solutions. We can provide insight on real vs hypothetical risks and help your team evolve.

WE OFFER

Cleveland & Co offer you fixed fees and retainer structures that provide you with certainty of cost and we offer industry experience that cuts through common legal complexity.

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