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PERSPECTIVES ON LAW

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WHAT'S INSIDE

President's Message

by Mark Cassanego

Technology Sector Leadership: Presenting a Different Face of Carr McClellan

This special edition of *Perspectives* focuses on our firm's expanding experience, knowledge and capabilities in representing technology companies and their investors. This knowledge base cuts across all practice areas of the firm, well beyond our corporate and intellectual property (IP) groups.

Litigation. Trade secrets. Licensing. Real estate. Taxation. Estate planning and wealth transfer. Over the years our lawyers have built broad experience in the technology industry across all these disciplines. Our firm has a long history of representing companies and their owners in their various business endeavors, spanning many industries and business models. That broad experience, which includes representation of many clients in the technology sector, forms the foundation of our growing technology practice.

Our corporate group has seen the most significant growth in the representation of technology industry clients. That growth includes representing entrepreneurs and their startups in all aspects of formation and early growth, as well as angel and other investors in all stages of equity financings. Ed Willig's article on the evolving funding marketplace for startups provides important context for newly formed technology companies, the entrepreneurs that lead them and the investors that fund them. Helen Christakos explains the new privacy guidelines for the mobile industry issued by Kamela Harris, the California Attorney General. Valerie Menager points out why the National Labor Relations Board (NLRB) is not irrelevant to a technology industry workforce that is growing again. And although he's a litigator, Scott Atkinson shows his versatility by parsing the salient provisions of important recent amendments to the Video Privacy Act.

Our litigators have deep expertise in a wide array of "soft IP" cases, including disputes involving trade secrets and licensing. Our real estate attorneys have represented both tech companies that lease space and landlords that lease facilities to tech companies, leading to valuable insights into a whole range of specialized, and often unique, business and legal issues. Sales tax issues regarding cloud-based software (often delivered as a service), and the shifting sales tax framework under various states' laws are the subjects of increasing focus by our tax department. And not to be left out, our estate planning and wealth transfer group has built a considerable body of experience in deploying complex planning techniques for the tax efficient transfer of wealth created in the technology industry.

Read on. The articles that follow represent a cross section of our lawyers, providing just a glimpse into the myriad of subject matters in which our firm has developed expertise and experience that provide value for our technology industry clients.

What to Ask Potential Investors Beyond "Is Your Money Green?"

by Ed Willig, Esq.

Overview

Investment into U.S. venture-backed companies dropped 20% to $6.6 billion in the fourth quarter of 2013 compared to a year earlier, according to Dow Jones VentureSource, and was down 15% to $29.7 billion for all of 2012. As the venture capital industry evolves, the funding landscape for startups has become more challenging. However, some different sources of funding are becoming more accessible to young companies that have endured the pure startup phase and show promise. Along with traditional venture capital funds, corporate investors, private equity firms and hedge funds are providing institutional investment. There are potential advantages and disadvantages to each of these financing sources. We've listed some of these advantages and disadvantages below.

Traditional Venture Capital Funds

Advantages:

- Many of these funds, through their experience and connections, can add value to a company that goes well beyond the amount of money invested. In addition to providing strategic guidance, well-known funds can open many doors to potential customers, investors, and other resources.

Disadvantages:

- These investors will typically want liquidity within a fixed time horizon.
- These investors may be reluctant to assign the higher valuations that some other categories of investors may assign (particularly hedge funds).
- Some of the "lower tier" funds have been unsuccessful; as a result, they are unable to invest in subsequent rounds or provide the non-financial support that has been a hallmark of traditional venture capital funds.

Corporate Venture Capital Investors

Many large corporations have established successful venture capital operations, using their investments to keep up on new developments and emerging talent in their industries.

Advantages:

- As with traditional venture capital funds, corporate investors can add value through their deep industry knowledge and contacts.
- A corporate investor's name alone may open doors to potential customers and other opportunities.
- Some of these investors do not have fixed time horizons, and unlike traditional venture capital funds they do not have to return funds to their limited partner investors. This can also make them more open to a range of investment structures and more unusual situations.

Disadvantages:

- Because these investors often sell products in, and invest in, a single industry, there may be conflicts of interest between the investor and the companies in which they invest, or between two or more companies in which they are invested.

Private Equity Funds and Hedge Funds

Having become aware of the high returns that some venture capital funds have earned in the past, a growing number of private equity funds, hedge funds, and similar investors have entered the venture capital game. This is not a new phenomenon, but it is starting to make an impact on startups.

> "With new institutional options, as well as crowd-sourcing options emerging, startups have more options than before, and more issues to consider."

Advantages:

- These investors often use higher valuations when making their investments, yielding higher investment proceeds or less dilution for existing investors than lower valuations would bring.
- These investors may have strong financial contacts which may be useful if the company will go public or seek other non-venture capital financing.
- Some of these investors are comfortable with a "buy and hold" strategy and may have a relatively long investment horizon.
- These investors may be more comfortable holding publicly traded securities than are traditional venture investors, so these investors may retain an investment in a company after a public offering, stabilizing the company's investor base.

Disadvantages:

- Some of these investors are not used to investing in emerging companies. When there are setbacks – as there often are at emerging companies – these investors may become unsupportive.
- The higher valuations some of these investors are paying can put increased pressure on a company to rapidly achieve a certain valuation or liquidity event, sometimes at the expense of the company's long-term development.

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California Attorney General Issues Mobile Industry Privacy Guidelines

by Helen Christakos, Esq.

Overview

In January, California Attorney General Kamala Harris further built on her high-profile 2012 campaign to improve privacy protection for consumers who use mobile devices by issuing a report titled "**Privacy on the Go**" ("Privacy Report") which lists recommended best practices for app developers, mobile advertising networks, operating systems developers, app platform providers, mobile carriers and others in the mobile industry. The Privacy Report is not legally binding, but it further highlights that consumer privacy is a top priority for California regulators. It also provides useful guidance on the regulators' key privacy concerns relating to the mobile industry, and it signals potential future regulatory actions.

Background

The Privacy Report's key premise is that mobile device users tend to ignore traditional app privacy notices, because they are complex documents that are difficult to review on small screens.

Harris encourages companies to: (1) consider privacy issues at the time they are designing products and services; (2) implement the Fair Information Practice Principles; and (3) adopt a "surprise minimization" approach to alert users about how their information is collected, used and disclosed and give them control over data practices not directly related to an app's functionality or that involve sensitive information.

Harris offers numerous industry-specific recommendations, including the following:

- Only collect data you need to operate the app (app developers/owners)
- Obtain prior consent from users before obtaining/accessing personal information (app developers/owners and ad networks)
- Create transparent privacy notices that accurately describe your collection, use and disclosure of consumers' personally identifiable data (app developers/owners and ad networks)
- Provide consumers with the opportunity to learn about privacy practices before downloading apps, and provide app users with tools to report non-compliant apps (app platform providers and ad networks)
- Move away from unchangeable, device-specific identifiers and transition to temporary device identifiers (ad networks)
- Securely transmit user data using encryption for permanent unique device identifiers and personal information (ad networks)

Impact on the mobile industry

Forewarned is forearmed. App developers, mobile advertising networks, operating systems developers, app platform providers and mobile carriers may want to consider implementing the Privacy Report suggestions now to stay ahead of the curve. Although the Privacy Report is not legally binding, it shows that privacy is high on the regulator radar. Mobile industry companies should take note. As indicated in the report, certain areas-such as collecting only the data needed, making privacy policies transparent and consistent across apps and devices and making data more secure-are key concerns. Companies in the mobile industry should voluntarily and quickly implement measures that comply with these guidelines. As part of your initiatives,

we encourage you to think like a consumer, and create simple, clear policies and promote these as features of your services. Additionally, companies that voluntarily comply with these guidelines should advise their customers and their peers of this. Leading today, rather than having measures imposed later on, is the right approach both from a risk management and customer relations perspective.

We can help you find innovative ways to stay ahead of the recommendations in this report.

If you have any questions about how to comply with state or federal privacy laws or whether to implement the best practice recommendations in the Privacy Report, please contact:

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Why Non-Unionized High Tech Companies Still Need to Pay Attention to the National Labor Relations Board

by Valerie Menager, Esq.

Overview

The National Labor Relations Board (NLRB) is the agency that administers the National Labor Relations Act (NLRA), which is the law that protects employee rights to unionize and collectively bargain with their employers. The NLRB's rulings had significant influence on employment law back in the mid 1950s, when a third of all workers in the U.S. were unionized. In recent times, this influence has been drastically reduced as the percentage of unionized employees in the private sector has shrunk to a tiny 6.6%, largely in manufacturing. Therefore, many employers, especially technology companies that predominately employ knowledge workers in the US, view the NLRB as a historical artifact with little actual power.

Starting in January 2012, this perception changed dramatically, when President Obama made three appointments to the NLRB panel of five judges during a recess of the Senate. With a quorum of judges, the NLRB, and its regional Administrative Law Judges, quickly issued a series of rulings holding that common employer policies on topics such as employment at will, social media usage in the workplace, internal investigations and arbitration agreements violated the NLRA.

Specifically, the NLRB and its Administrative Law Judges found that these standard policies could be interpreted to violate the employee's right to discuss or negotiate the terms and conditions of their employment. Such "concerted activity" during off duty work times is protected under Section 7 of the NLRA because it allows employees to form groups, such as unions, and to collectively negotiate with employers for better wages and working conditions.

In January 2013, just as employers began to determine how to redraft these standard employment policies to comply with these new NLRB rulings, the DC Circuit Court of Appeals vacated the holding of an NLRB case because it found that the three NLRB judges had been improperly appointed during the Senate recess. This raised the possibility that all of the rulings made by the NLRB starting in 2012 until the present time could be vacated.

Impact on technology companies

So you can go back to not worrying about the NLRB, right? Wrong. It is highly likely that the DC Circuit Court decision will be appealed, and the NLRB has announced that they are going to continue to rely on the NLRB's own case precedent and regulations to continue to enforce the rights of non-unionized employees to engage in concerted activity. This means that some of the technology sector's most basic HR policies could be found to be unenforceable by the NLRB.

What can you do to protect your company against unfair labor practice charges filed with the NLRB? Have your legal counsel review any policies that your company may have including social media, at will employment, arbitration, internal investigations or that concern any off duty conduct to make sure that they do not violate the NLRA.

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What to Ask Potential Investors...

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Impact on Startups Seeking Funding

A company seeking funding should explore alternatives from multiple sources, and get the advice of multiple advisors before deciding to accept any investment. There isn't a single type of investor that's best for every situation. In our experience, the type of investor that's best for a given company depends on many factors.

With new institutional options, as well as crowdsourcing options emerging due to changes in the regulation of angel investors — including the rise of sites like Kickstarter (the subject of a future article) — startups have more options than before, and more issues to consider.

Before deciding to move forward with an investor, you should get as much advice as you can from those with significant experience, and from a wide range of sources, including successful startups, serial entrepreneurs, business advisors and attorneys who have worked through many types of deals.

For support with your funding strategy and other corporate development needs, please contact:

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Finally — Video Privacy Protection Act Amended for the Internet Era

by Scott Atkinson, Esq.

Overview

On January 10, 2013, President Obama signed into law amendments to the 1988 Video Privacy Protection Act (VPPA) that facilitate social media sharing of video viewing preferences when users consent to disclosure of information via the Internet. The amendments have a number of practical implications for online video providers and their users. The VPPA Amendments permit video streaming services to add opt-in features that will make it much easier for consumers to share their video viewing habits on social media platforms. The VPPA Amendments, however, do not distinguish between social media sharing with friends and sharing with third party advertising or analytics companies. We recommend you get ahead of the curve and create clear distinctions in your data sharing opt-in agreements between sharing data socially versus sharing with third party advertisers and analytics companies.

Impacts of the Amendments on Video Service Providers and their Users

To comply with the amended VPPA, video streaming services must request consent for any personally identifiable data sharing in a separate agreement. In other words, video streaming services cannot obtain valid user consent under the VPPA Amendments via their standard User Agreement or Terms of Service.

Video streaming services must renew their consumers' consent at least bi-annually and create internal systems to suspend data sharing after the expiration of any advance consent period.

Video streaming services must also provide a conspicuous means for the consumer to withdraw consent either completely or on a case-by-case basis. That way, consumers who, for example, share the movies they are watching with their friends on Facebook can opt-out of sharing the fact that they viewed particular videos that might be personally or politically sensitive with their Facebook friends.

Under the new law, nothing stops a video streaming service from having a "one click fits all" approach where a "yes" click means a consumer is willing to share socially and with third parties, but such a policy should be clearly stated. For example, depending on a service's policy terms, a user's interest in *Abraham Lincoln: Vampire Hunter* or *Larry the Cable Guy: Health Inspector* can legally be shared not just with her Facebook friends, but advertisers *and* analytics companies, too. Because the statute provides that consumers must give their "informed, written consent" to sharing, video service providers can minimize the risk of violation by clearly and directly informing their users with whom information will be shared if they click "Yes." While providing users with separate consent options for social sharing vs. sharing with advertisers and analytics companies is not required by the VPPA Amendments, doing so may make users happy (and therefore make good business sense) by giving users a further measure of control over dissemination of their information. It could also protect against future legislation that may tighten restrictions.

Background

Under the old statute, a "**video tape service provider**" (which includes Internet video streaming services, like Hulu or Netflix) could disclose personally identifiable information regarding a customer's viewing habits to "any person with the informed, written consent of the consumer given at the time the disclosure is sought."

Under the Video Privacy Protection Act Amendments Act of 2012, the consumer's written consent can now be obtained through electronic means using the Internet, provided that the consent is in a "form separate and distinct from any form setting forth other legal or financial obligations of the consumer."

The VPPA Amendments also permit the consumer to choose between giving consent to disclosure either: (1) in advance for a set period of time, up to two years or until consent is withdrawn; or (2) each time disclosure is sought (like under the old statute).

Under the VPPA Amendments, the service provider must give the consumer "in a clear and conspicuous manner" the opportunity to withdraw consent either on a case-by-case basis or from ongoing disclosures, at the consumer's election.

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Navigating the Tax Storm Clouds on the Horizon

by Brendan Lund, Esq.

Overview

Seeking new revenues, states are starting to consider taxation of cloud-based services. For example, Washington enacted a statute which specifically taxes Software as a Service (SaaS) providers. Other states have issued letter rulings addressing specific fact scenarios. Missouri ruled that SaaS hosted on an out-of-state server are not subject to sales tax when accessed by an in-state user. In contrast, New York has concluded that it can impose a tax on software hosted on an out-of-state server and accessed by an in-state user. Rulings such as these can subject a provider to a state's sales and use tax regime.

Historically, states have imposed tax on the sale of tangible personal property. Businesses providing services have largely escaped taxation of these services. These principles were codified with traditional "bricks and mortar" businesses in mind.

But, in the past two decades, states have struggled to amend long-standing statutes to address the taxation of digital products. State legislatures have failed to develop a consistent method of taxing, for example, a digital download of software. Some states remain steadfast in only taxing tangible personal property provided to taxpayers in their state. Other states now impose tax on certain services provided within their state. Still others have adapted their statutes to now tax downloads of digital products or web-based software. Cloud computing is a further evolution that will stretch traditional state tax principles.

Impact on Cloud Service Providers and Users of Cloud Services

One of the biggest challenges the industry will face is how to define what providers and buyers of those services are actually buying or selling. SaaS models apply to distinct user groups, but all are predicated on borderless global networks. Will a state treat cloud-based products as tangible personal property or as a service? How do states tax these services, if at all? If a business is located in California, servers are located in Washington and the consumer is located in Arizona, which state's laws apply? California's because the business is headquartered there? Washington's because the servers are physically located there? Or, Arizona's because the end-user is located there? The answers to these questions can result in meaningful tax differences that will impact a business's bottom line.

States are also focused on end-users as a source of revenue. Some states have characterized the licensing of cloud-based services as a lease of tangible personal property. Property leased in a state could create income tax nexus for the user of cloud-based services. This could mean that a business that licensed, for example, SaaS products in another state, unwittingly expanded its income tax footprint, subjecting it to filing income tax returns in that state.

Service providers should act now to anticipate upcoming tax issues for their particular business model. Since states are adopting taxation laws with very different philosophies, and the laws evolve continually, your strategy will need to be revised frequently. Due to the nuances of how the laws are evolving, your entire corporate strategy may evolve.

States will continue to find ways to tax cloud-based services. Businesses, both providers and users of cloud-based services, need to understand this evolution. For help navigating the rapidly evolving cloud services taxation issues, please contact:

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The "Google Effect": How High-Tech Companies Are Impacting Building, Architecture and Design

by Jennifer Johnson, Esq. and Manroop Purewal, Esq.

Overview

Technology companies in the Bay Area have led the resurgence of the local commercial real estate sector. And these companies are also creating a new norm in campus design known as the Google Effect. Google may have been one of the first to create this type of "unique" work space, but more recent examples of this paradigm shift are everywhere and almost accepted as the new "norm." Take Facebook. Facebook is akin to a mini college campus. Employees enjoy three meals per day, serviced by cafes, a BBQ restaurant, pizza parlor, taqueria and ice cream shop. Additional amenities such as gyms, laundry services, medical and dental clinics and even day care are showing up, to the point of being expected perks by the Bay Area's in demand workforce.

You may think this "Google Effect" is about keeping employees at work longer, but that is only part of the story. Technology companies have hired architects and psychologists to critically analyze the concept of the work space prior to building. Thought is given to the culture of the company, promoting collaboration, stimulating imaginative thinking, enhancing random interaction, and much, much more. Consequently, this has turned the office space upside down. Many of these technology companies have "ubiquitous space" with few, if any, private offices. At Facebook, for example, there are no private offices—even for executives. Instead, employees are bunched together as part of teams, working together, elbow-to-elbow, with the goal of working collaboratively. The long term impact on facilities management, building costs, productivity, human resources and compliance are not understood, with positives and negatives likely to emerge.

Impact on Bay Area Companies

All this innovative design comes with its own set of issues. The most important issue you need to think about is density. The open floor plan has led to a rapid increase in employees per square foot not seen before in the traditional closed-door office layouts. Infrastructure such as mechanical systems, bathrooms, and adequate storage space for bikes and personal items must be in place to support the higher density demands, along with better acoustics and private space areas. Additionally, concerns about employee privacy, data security, and productivity need to be managed. These issues are easier to tackle when dealing with new construction, but present a bigger challenge when older buildings are modernized to accommodate the increased demand from technology companies. Either way, significant costs are incurred. This is just the tip of the iceberg in terms of challenges; other issues include load factors, security and access, confidentiality, and dealing with growth expectations.

With the projected increase in growth of the technology industry, the "Google Effect" on the Bay Area commercial real estate sector will likely be even more prevalent in the years to come. Stay tuned.

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Theft of Trade Secrets Clarification Act of 2012: A Powerful New Weapon for Businesses

by Robert Bleicher , Esq.

Overview

On December 28, 2012, President Obama signed the Theft of Trade Secrets Clarification Act of 2012, which significantly expands trade secret protection by extending criminal penalties to the theft of a wider class of trade secrets under the existing Economic Espionage Act (EEA). Now included are company "back office" information and processes, such as unique business methodologies, customer lists, internal market and customer research, and programs developed to create and utilize that information. These are now subject to the criminal penalties of the EEA. This knowledge now falls within the scope of Section 1832(a), even if it cannot be readily identified in a particular product or service.

Background

The Clarification Act amends the Economic Espionage Act of 1996, 18 U.S.C. §1832. Before amendment, the EEA protected a trade secret "that is related to or included in a product that is produced for or placed in interstate or foreign commerce." Section 1832(a) now includes a trade secret "that is related to a product or service that is used or intended for use in interstate or foreign commerce."

California Civil Code §3426.1(d) defines a trade secret as "information, including a formula, pattern, compilation, program, device, method, technique, or process that: (1) derives independent economic value, actual or potential, from not being generally known to the public or to other persons who can obtain value from its disclosure or use; and (2) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy."

Impact on businesses

The amended EEA should further encourage businesses to clearly identify their key foundational processes and data, determine whether that information is protectable as a trade secret, and then take steps to ensure that the information is being treated as a trade secret. By doing so, and therefore falling within the broadened protections of Section 1832(a), businesses gain a powerful new deterrent against the theft of their key intellectual property. For help revising your trade secret protection strategy, please contact:

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