

## Social Media and Digital Assets in M&A Transactions

**W**ait! Don't skip these articles thinking that social media doesn't affect you. Social media has invaded our lives, with only a Rip

Van Winkle being immune (maybe). Some may scoff and others may cringe. The well initiated may laugh that the social media landscape, like its progeny "Big Data," is changing too rapidly to provide definitive advice—true, but we still have to deal with this powerful medium as it currently stands.



By Regina M. Joseph

### BACKGROUND

**What is Social Media?** For those who have been trying their hardest to avoid it, what is social media? To define it by example, it includes the well-known giants Facebook, LinkedIn, Twitter,

YouTube, Pinterest, Instagram, Google+, Reddit, and Tumblr (each for our purposes, an "Owner"). Special interest sites, such as Goodreads (purchased by

Amazon), exist for targeted markets, and new niche sites try to emulate Facebook (e.g., MARSocial for artists, Rich Ideas for entrepreneurs, and Foxwordy for lawyers). Since Facebook and Twitter have by far the greatest number of users, much of the discussion will focus on their operations.

**How Does Social Media Work (Big Picture)?** The Owner places little or no proprietary content on its site, differentiating it from content sites such as AOL, MSN and Yahoo, as well as sales conduit sites such as Amazon, eBay and Etsy. As essentially an empty shell, a social media site is populated with user content. By users interacting with other users, the site expands and becomes more valuable to its Owner. Interaction occurs through the users' written communications, which frequently are accompanied by photographs, artwork, and videos to enliven the commentary. Such works may be user-created, such as wedding and birthday photos, for which viewers may express approval by pressing a "LIKE" or "g+1" button, or by retweeting, favoriting or inserting a comment, depending on the site. Alternatively, a user might share someone else's work on his/her page. Do third parties object if their content is shared? Quite the contrary. When an item is shared, the new posting credits the original source. The original post thereby reaches many more viewers than were on the original circulation list.



**Monetization.** Social media sites frequently have no membership fee, at least as of this writing. Social media giants, having become public companies, make frequent changes to monetize their information streams. For example, Facebook frequently adjusts updates from users (its "Newsfeed") to force paid promotions. Twitter makes money by selling its analyses of social trends—when a product is free, *you* are the product. Facebook and Twitter are two of the major forces fueling the era of "Big Data" also known as "Social Data," which provide minute insights into fast developing customer trends (see, e.g., "The Social Data That Business Should Use," The Wall Street Journal, R4, Feb. 11, 2014;



and “Real Time Marketing in a Real-Time World,” *The Wall Street Journal*, R3, Mar. 24, 2014). A commonly quoted example about using mined social data is a restaurant sending a coupon to a nearby person who is selected because of his/her dining habits or those of his/her friends. These and other purchasing trends are being mined regularly (see, e.g., [http://www.thinkwithgoogle.com/tools/customer-journey-to-online-purchase.html#utm\\_campaign=ph1&utm\\_source=twitter&utm\\_medium=cpc&utm\\_content=L1](http://www.thinkwithgoogle.com/tools/customer-journey-to-online-purchase.html#utm_campaign=ph1&utm_source=twitter&utm_medium=cpc&utm_content=L1)).

**Owner’s Terms of Service.** Social media usage is subject to the site owner’s Terms of Service (“TOS”). The TOS are subject to change at any time in any manner without notice. In a recent decision, a California court upheld Instagram’s right to make material TOS changes,

including granting itself a right to sublicense a user’s posted content (*Rodriguez v. Instagram*, CGC-13-532875 (San Francisco Sup. Ct. Feb 28, 2014)). If the Owner determines that the user has violated its TOS, it may suspend, even terminate, the user’s account without notice or, in most cases, right of appeal. With the growing dependence of small business on social media, the ability to reach customers flows through these gatekeepers.

**How Does Social Media Work (More Detail)?** On almost all sites, a user sets up his/her profile page. A distinct username and password is chosen, and notifications are delivered to the creator’s e-mail address. Facebook encourages the use of real names, but Twitter less so. A social media account in and of itself gives the user very little. To create value, the user must invite “friends” or “followers” who will view or provide postings. Over time, a person’s Facebook page might serve the role of an extensive diary memorializing friendships, thoughts, opinions, and events ranging from the significant—weddings, births, birthdays, vacations, awards, accomplishments—to more the more mundane—favorite recipes, artwork, photos, music, books, commentary on current events, and so on. On Facebook’s tenth anniversary, it made available to users a collage of their photos. On Facebook’s seventieth and eightieth anniversaries, how much information about individual lives, even subsequent generations, will it possess?

**Business Use.** Social media is not limited to personal interactions. A user may also establish a “Page” to promote his/her business, brand, club, or cause. The usage rules vary by the site.

Facebook considers it a violation of its TOS for a personal account to represent something other than the user, such as the user’s business (Facebook Help Center). According to the present

Facebook TOS, a business Page must be a subset of an individual user’s profile page. This has not always been the case, and businesses that joined in the earliest years might have a direct account. Also, since public companies such as Ford and Chrysler have Facebook pages, there must be unpublished TOS for large users. In the published TOS, however, a business must be linked to the profile page. For the Page, the user must designate one or more administrators who are permitted to revise Page information and to respond to private messages. He/she may post advertisements or commentary on the Page to increase customer loyalty, and viewers may “write on the timeline.” When viewers “like” or follow the Page, new postings on the Page appear in the viewer’s Newsfeed, although Facebook determines how prominently the postings are displayed. Facebook has been steadily reducing the reach of the page in order to boost its revenues (see, e.g., <http://time.com/#34025/the-free-marketing-gravy-train-is-over-on-facebook/>). Postings can be boosted by paying a fee. A small business might well assign various employees to serve as administrators to engage in these marketing activities.

On Twitter, having a large number of followers to receive “tweets” is highly prized. Although Facebook places limitations on the number of LIKES and friends, Twitter and Google+ have fewer size limitations. Some bloggers, “influencers,” and small businesses have hundreds of thousands of followers. Engaging this many potential customers without a substantial expenditure obviously has value. Of course, this engagement is a bit of an art that varies by social media site, and there are a plethora of social media consultants advising as to how one should engage potential customers.

LinkedIn, in keeping with its reputation as being the premier site for professionals and executives, has a greater number of rules for a user to build his/her network, and there are limitations about viewing the user's network without paying a subscription fee.

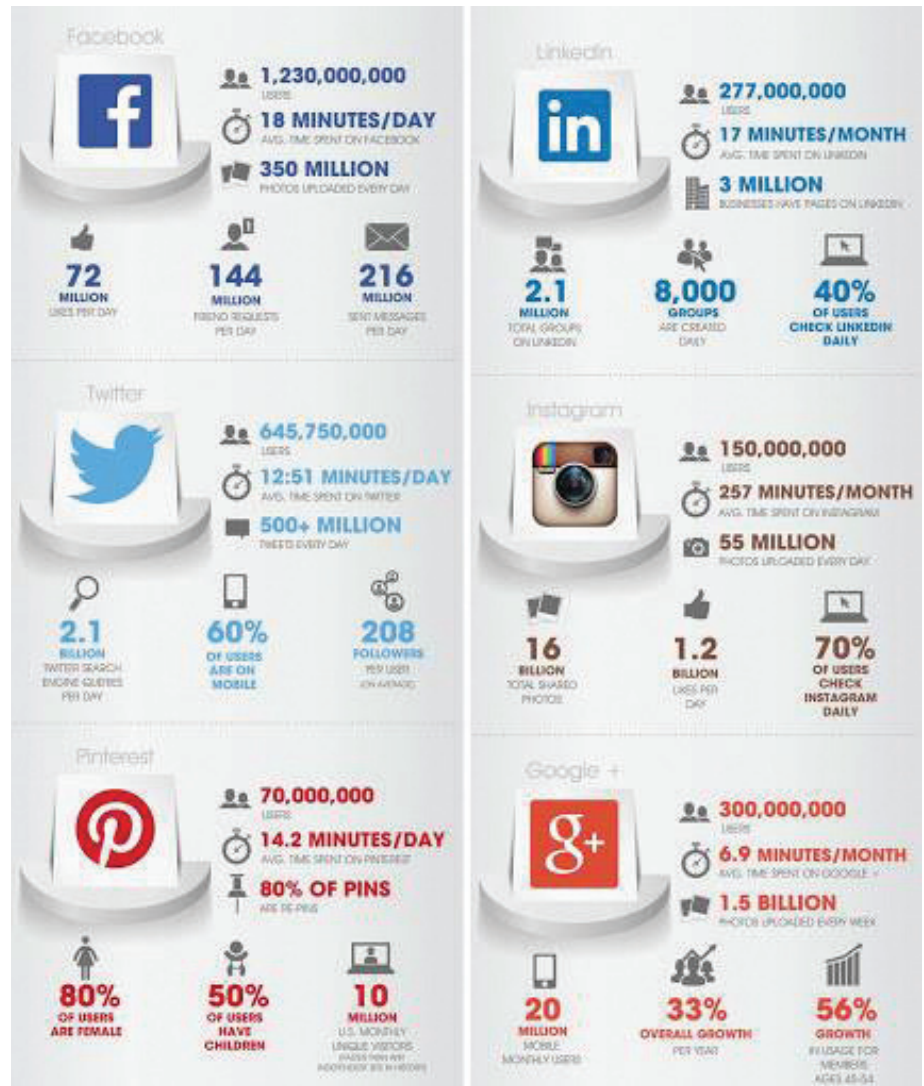
**Blurring of Business and Personal Use.** Social media encourages users to be personal, which might be through linked blogs or inviting on-site engagement. Increasingly, linked blogs are becoming revenue generation sites. For example, a blogger may review products, post product links, and enter into an affiliate program to receive revenue for sales through the site. The advertising tweets and Facebook posts appear on the blog's webpage. For small business, blogs present an increasingly common advertising avenue, and they may lead to highly-prized customer e-mail lists.

**Linkage.** A small marketer may feel overwhelmed by the need to update many social media sites. Some services, like Buffer and Zapier, link sites so that a post to one covers multiple media. Alternatively, some sites might permit the user to sign in via another social media site, so that a distinct registration is not required. However, a wise user will have a distinct set of user names and passwords for each site for security purposes.

The point of the foregoing exposition is that all these matters need to be addressed if social media accounts are to be effectively transferred. These "digital assets" have value, even if valuation is difficult.

## ACQUISITION OF DIGITAL ASSETS

Cottage industries have blossomed with the availability of relatively free exposure and direct sales reach. Examples are independent authors, painters, photographers, musicians,



jewelry makers, specialty clothing makers, artisans in a variety of media, and so on, as well as consultants and others who provide support services. The proliferation of affordable 3D printing devices, if they live up to their promises, will further accelerate this trend, as innovators will be able to manufacture items with minimal facilities and capital investment. Participation is not limited to cottage industries, of course. Many privately and publicly held companies have

Facebook, Twitter and other media accounts. That is where the customers are.

Although much of the goodwill of cottage industries may be personal to the promoter, there are probably transferable copyrights, licensing arrangements, ancillary sales (tee shirts, key chains, mugs, etc.), affiliate sales arrangements (*i.e.*, sites that reimburse a linked site when a customer buys a product after arriving from that site), and sales accounts through sites such

as Amazon and eBay. Of course, the business might also have tangible assets, such as inventory and computer equipment.

**What are the assets?** As in any acquisition, the acquirer must identify all desired property and contractual rights and arrange for the transfer of valid legal title at closing. If the target conducts substantial marketing through social media, the acquirer must procure rights to all digital assets and secure the related income and payment streams upon which the purchase price is based. This can be tricky. Although the target's website, domain names, trademarks, copyrights and other intellectual property are property rights capable of being reliably transferred by general and/or specific assignment documents, social media accounts are not. Under present law, the right to access social media accounts is a contractual one. As such, the rights and the transfer thereof is governed by the pertinent Owner's TOS, and Owners frequently change their TOS, sometimes in substantial ways. Thus, all pertinent rules should be reviewed in connection with each transaction.

Content posted on Facebook and Twitter belongs to the registered user (Facebook Statement of Rights and Responsibilities/Twitter TOS 5). The TOS also grant each such Owner a non-exclusive, transferable, sub-licensable, royalty-free, worldwide license to use that posted content (Facebook Statement of Rights and Responsibilities 2.1/Twitter TOS 5). Although a registered Facebook user has the right to download his/her data, the download will come as a single file, without distinguishing between the personal profile and the business page(s) (Facebook Help/ Accessing Your Facebook Data). The Twitter website also contains the ability to download an archive with the user's complete history (Twitter Settings).

Downloading and closing the account, however, would deprive the acquirer of the benefits of the user's goodwill. Instead, an acquirer would want to transfer the accounts or, on Facebook, the business page.

Although transfer prohibitions are most likely not a factor if the target is an entity and the acquirer buys its equity securities (at least the TOS do not state that a change in control constitutes a transfer), few acquisitions are so structured, since liabilities would be assumed with the assets. And, this does not help with accounts held in a personal name. Most private company acquisitions, even in the middle market, are asset acquisitions wherein assets must be properly assigned for the acquirer to have legal ownership. Large acquisitions usually involve a merger component that might be deemed to be an assignment depending on relevant state law.

**Transfer is problematic.** Under the Facebook Statement of Rights and Responsibilities 4.9, the user is prohibited from transferring his/her account (including any Page he/she administers) without obtaining Facebook's advance written permission. Facebook does not promise that the permission will not be unreasonably withheld or delayed, and it provides no contact information for requesting consent. The Twitter Rules incorporated in its TOS flatly state, "You may not buy or sell Twitter usernames." A Google+ unique url may not be transferred under a warning appearing at its creation.

If it is possible for the various social media accounts to be owned by an entity having no other assets, the acquirer could purchase the equity interests and leave the entity intact as a wholly-owned subsidiary; the assumed liabilities would be limited to the digital

assets. Inventory and other assets could be purchased through an asset purchase agreement.

If the target's market value was created through accounts in the personal name of the principal or employees, transfer might be impractical unless such individuals agree to work for the acquirer. If the business content was originally created by employees, the acquirer should determine if employee agreements adequately assign rights capable of assignment by the target to the acquirer.

Another means of accomplishing the account transfers might be by taking over all the seller's log-in information, security questions, and linkages. The acquirer may then change the passwords and manage the account. Even if the account has not technically been assigned, there is a rule against password disclosure and impersonation. As noted above, such actions probably violate the TOS. Also, depending on the service, it might not be possible to change the account name. Transferring the account by simply taking over passwords bears risks, therefore, unless advance consent is obtained. Is this risk high, given so many users? An Owner might discover it through the acquirer's public disclosure or the User's monitoring of usage patterns. Of course, a disgruntled seller or employee might notify the Owner. If discovered, the Owner could suspend or terminate the account without notice as permitted by its TOS. Losing the account means losing access to the contact base, unless the acquirer copied the ever-changing lists. Since the Owner controls access, the acquirer cannot view its acquisition of social media contacts with the same security as buying a proprietary "customer list." More value is created, of course, if the seller has turned the social media contacts into a direct e-mail list.

The purchaser doubtlessly does not want to build its future goodwill in the name of seller or its principal. The seller, on the other hand, would not want the acquirer's social media usage in its/his/her name to result in an infringement or libel action (known as "twibel" with respect to increasingly common Twitter actions), even with an indemnification agreement. People tend to tweet without thinking about the content or the potential reach; a post may become "viral" by being resent repeatedly. Acquisition of a social media account brings with it any claims that a third-party could have against the user, such as infringement, misappropriation of intellectual property, abuse, and so forth. The acquirer should seek indemnification if such a claim is made for content posted prior to closing.

Of course, if the principal maintains a post-closing relationship with the acquirer—either on an employment basis or being appointed an agent—and she continues the tweeting methodology (tweeting is like a garden that will wither and die if left unattended) perhaps the documentation will require her to assign the goodwill to the purchaser and to disclose all current log-in information and give notice of all changes. This plan, however, risks the acquirer having a dispute with the principal wherein she notifies the Owner of the TOS breach. However, if the relationship goes smoothly, the parties may create a post-acquisition plan to migrate the account names and followers to the acquirer with the Owner's consent. If they cannot be migrated, the documents could provide for a purchase price adjustment, assuming that these accounts represent a minimal segment of the target's business.

The acquirer also needs to capture the payment stream. Many items sold

through the sites promoted through social media receive purchase and royalty payments that are routinely transferred to a PayPal account or bank account deposit. Since asset acquisition agreements usually exclude the seller's bank accounts, the diligence process should ascertain if any automatic payment streams need to be redirected.

A business operating primarily in social media has been, somewhat derisively, called a "lifestyle business" due to the difficulty of creating marketable assets, even though the creator may derive substantial income. As more businesses develop substantial value through these accounts, pressure will undoubtedly be brought to bear on the Owners to solve these transfer problems. Of course, technology itself might solve the transfer difficulties if P2P platforms such as Twister (<http://twister.net.co/>) permit users to connect directly, thereby bypassing the current social media giants.

## CONCLUSION

Given the uncertainties surrounding the transfer of digital assets, an acquirer might choose to value the associated income streams differently than streams from traditional sales channels. In some respects, it's the old "Buyer Beware." However, social media revenue streams should not be disregarded. A small target might exclusively market through social media and have certifiable profits over several years from these efforts. If that target or its principals reach, for example, 500,000+ Twitter followers on a daily basis, there is arguably value (disregarding whether some of those followers are "zombies," *i.e.*, purchased from entities that create dead accounts for the mere purpose of selling blocks of Twitter followers). In *PhoneDog v. Kravitz*, Case No. C 11-03474 (N.D. Cal.), the plaintiff argued for a purported "industry standard" value of \$2.50 per Twitter

account in an action claiming an account was misappropriated by an employee who went to work for a competing employer. That number was unsubstantiated, but does show an effort at valuation that will become important in the future. Until that time, valuation is no easy matter and will need to be ascertained on a case by case basis.

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