

Saskatchewan Telecommunications Holding Corporation



Main points	132
Introduction	133
Related companies and pension plan	133
Audit conclusions	133
Processes to manage intellectual property	134
Intellectual property at SaskTel	135
Assessing SaskTel's processes.....	135
Key findings (by criterion) and recommendations	136
Leadership and corporate support	136
Identification of intellectual property	138
Management of ownership.....	139
Monitoring and protection.....	141
Evaluation and reporting	142
SaskTel's governance of owned and controlled companies—a follow-up	143
Communicating governance expectations	145
Assessing board effectiveness of owned and controlled companies	145
Selected references for processes to manage intellectual property	146

Main points

Many of SaskTel's activities and services involve the use of intellectual property. Without appropriate rights to use—and protection of intellectual property—SaskTel would not be able to effectively carry on its businesses.

This chapter reports the results of our audit of how well SaskTel manages that intellectual property. SaskTel had adequate processes to manage intellectual property at November 30, 2006, except it should:

- ◆ develop a plan for managing intellectual property
- ◆ include intellectual property issues in its risk management framework
- ◆ consistently document intellectual property agreements with its subsidiaries
- ◆ establish centralized responsibility for maintaining original contracts
- ◆ implement a system to assist it to comply with the intellectual property rights it has acquired
- ◆ monitor its progress in achieving its plan for managing intellectual property

We also report the follow-up of our audit of SaskTel's governance of owned and controlled companies. SaskTel has addressed our recommendations.

Also, for the year ended December 31, 2006, SaskTel and its related companies and pension plan had reliable financial statements, had adequate processes to safeguard public resources, and complied with authorities governing their activities.

Introduction

Saskatchewan Telecommunications Holding Corporation (SaskTel) provides telephone, cell phone, internet, and e-business services. SaskTel provides these and other services, such as telephone directories and home security, through its many different companies.

Related companies and pension plan

At December 31, 2006, SaskTel owned the following companies with active operations (percentage of SaskTel's ownership is set out in parenthesis):

- ◆ Saskatchewan Telecommunications (100%)
- ◆ Saskatchewan Telecommunications International, Inc. (100%)
- ◆ DirectWest Corporation (100%)
- ◆ DirectWest Canada, Inc. (100%)
- ◆ SecurTek Monitoring Solutions Inc. (100%)
- ◆ Hospitality Network Canada Inc. (100%)
- ◆ Saskatoon 2 Properties Limited Partnership (70%)
- ◆ The Phone Book Company Partnership (85%)

Also, SaskTel sponsors and administers the Saskatchewan Telecommunications Pension Plan.

For a full listing of the companies owned by SaskTel, refer to the notes to its audited financial statements. Each year, SaskTel gives its annual report including its audited consolidated financial statements and the audited financial statements of each of the above-listed companies and pension plan to the Legislative Assembly. For additional information on SaskTel and its companies, see SaskTel's website at www.sasktel.com.

Audit conclusions

Our Office worked with KPMG LLP, the appointed auditor, to carry out the audit of SaskTel and the above-listed companies and pension plan. We followed the framework in the *Report of the Task Force on Roles, Responsibilities and Duties of Auditors*.¹ KPMG LLP and our Office formed the following opinions.

¹ To view this report, see our website at www.auditor.sk.ca/rrd.html.

In our opinion, for the year ended December 31, 2006:

- ◆ **The financial statements of SaskTel and each of the above-listed companies and the Saskatchewan Telecommunications Pension Plan are reliable.**

- ◆ **SaskTel and each of the above-listed companies and the Saskatchewan Telecommunications Pension Plan (except for DirectWest Canada Inc.) had adequate rules and procedures to safeguard public resources.** Due to the recent start up of DirectWest Canada, Inc., we plan to form an opinion on its rules and procedures to safeguard public resources starting with the year ended December 31, 2007.

- ◆ **SaskTel and each of the above-listed companies and the Saskatchewan Telecommunications Pension Plan complied with authorities governing their activities relating to financial reporting, safeguarding public resources, revenue raising, spending, borrowing, and investing.**

In this chapter, we also include the results of our audit of SaskTel's processes to manage intellectual property and a follow-up of our audit of SaskTel's governance of owned and controlled companies.

Processes to manage intellectual property

To deliver services and achieve their objectives, agencies must effectively manage their assets. This includes not only their physical assets, but also intangible assets including intellectual property. Intellectual property refers to the creations of the mind, such as inventions, symbols, names, pictures and designs. Patents, trademarks, copyrights, and industrial designs are examples of specific rights regarding intellectual property.²

As we outlined in our earlier chapter on intellectual property (2006 Report – Volume 1), there is increasing recognition of the importance of intellectual property. Agencies, including those in the public sector, are increasingly taking steps to identify their intellectual property assets and to protect and exploit those assets.

² Canadian Intellectual Property Office, p.3.

Agencies also require effective processes to identify and manage risks related to their use of others' intellectual property. As demonstrated in high-profile claims and litigation, offending the intellectual property rights of others can damage the interests and reputation of an agency.

Intellectual property at SaskTel

Intellectual property is important to SaskTel. SaskTel uses intellectual property in many ways in carrying on its businesses: providing telephone, cell phone, internet, and television services, and providing telephone directories and home security to its customers.

SaskTel has its own intellectual property that it needs to manage. It does this, for example, by protecting those rights under the law or by deciding whether to exploit those rights by contracting with others. Examples of this intellectual property include software products such as Martens (a software program for managing facilities) and trademarks (protecting SaskTel's name and symbols).

SaskTel also uses the intellectual property of others. SaskTel must obtain rights to use the hardware and software that enable it to deliver services. For example, SaskTel purchases licenses to use software from other companies, such as Oracle and Microsoft. SaskTel also pays for the right to distribute television and movies to its customers and other distributors.

Many of SaskTel's activities and services involve the use of intellectual property. Without appropriate rights to use and protection of intellectual property, SaskTel would not be able to effectively carry on its businesses. This chapter reports the results of our examination of how well SaskTel manages that intellectual property.

Assessing SaskTel's processes

The objective of our audit was to assess whether SaskTel had adequate processes to manage intellectual property at November 30, 2006. While SaskTel owns or controls many agencies (subsidiaries), we focused our examination at the parent because most activities related to managing intellectual property take place there. Throughout our audit, we followed the *Standards for Assurance Engagements* established by The Canadian Institute of Chartered Accountants.

To assess the adequacy of SaskTel's processes to manage intellectual property, we used the criteria set out in Exhibit 1. SaskTel accepted the criteria as a reasonable standard for assessing its processes. We reported these criteria in our 2006 Report – Volume 1.

Exhibit 1

Adequate processes to manage intellectual property include:

- ◆ Leadership and corporate support
- ◆ Identification of intellectual property
- ◆ Management of ownership
- ◆ Monitoring and protection
- ◆ Evaluation and reporting

Primary source: Australian National Audit Office, *Intellectual Property Policies and Practices in Commonwealth Agencies*

We concluded that at November 30, 2006, SaskTel had adequate processes to manage intellectual property except for the matters described in the recommendations below.

Key findings (by criterion) and recommendations

We describe below what we expected (in italics) and key findings for our five criteria, together with our recommendations.

Leadership and corporate support

We expect agencies to be committed to managing intellectual property to ensure that it is protected and available for use.

Senior management is accountable for intellectual property held or used by the agency. An intellectual property policy helps define the importance of intellectual property to the agency. An agency should use its policy to align how it manages intellectual property with the agency's strategic objectives and the risks it faces. The agency's intellectual property policy should set out the principles and criteria by which intellectual property assessments are made and identify who is responsible for making them. The policy should set out who is responsible for developing, approving, and maintaining the agency's intellectual property plan.

The intellectual property plan should define the types of intellectual property that the agency will need to identify and actively manage. The plan should reflect the importance of particular intellectual property to the objectives of the agency. This helps determine the amount of active management needed for that intellectual property.

The plan should include appropriate training (i.e., awareness and education activities) on intellectual property issues. It should also allocate sufficient resources to manage the agency's intellectual property needs. The policy and the plan should be communicated throughout the agency.

SaskTel has policies and procedures that address intellectual property rights. In its policies and procedures, SaskTel asserts its right to intellectual property created by employees and contractors. It also makes clear its corporate position that it will respect the intellectual property rights of others. These principles guide corporate decisions on intellectual property.

SaskTel does not explicitly assign responsibility for managing intellectual property issues. SaskTel does not have a central plan for intellectual property. Absence of a central plan may mean risks and opportunities are not identified.

SaskTel has a formal risk management framework. The framework does not include explicit consideration of intellectual property-related risks. Consequently, SaskTel may not consider some of these risks. However, SaskTel also has controls that reduce intellectual property-related risks. These include the involvement and expertise of the legal department.

Generally, SaskTel makes employees aware of intellectual property issues through a number of corporate policies including a code of business conduct. SaskTel specifically draws these to the attention of employees when they are hired and during annual performance evaluations. SaskTel does not have other broadly-attended education activities on intellectual property. Some staff (e.g., corporate lawyers) receive training on intellectual property issues and gain relevant knowledge by attending conferences.

Resources for managing intellectual property assets are included generally in division budgets.

- 1. We recommend that SaskTel should develop a plan for managing intellectual property. The plan should:**
 - ◆ **identify intellectual property assets**
 - ◆ **be proportionate to importance of intellectual property assets to the objectives and risks of SaskTel**
 - ◆ **describe approach/activities to manage intellectual property assets and risks**
 - ◆ **include training and resource allocation**

SaskTel management told us it will prepare a plan for managing intellectual property for approval by the SaskTel Executive. Management said it will provide a copy of the plan to a committee of the Board for information purposes as part of the follow-up to the audit.

- 2. We recommend that SaskTel include intellectual property issues in its risk management framework.**

SaskTel management told us its risk management group will include questions on intellectual property risks and liabilities in risk reviews conducted in 2007. Management said that it provides the risk reviews to the SaskTel Board annually.

Identification of intellectual property

We expect agencies to identify and record significant intellectual property.

To manage intellectual property appropriately requires knowledge of the intellectual property used by the agency. Intellectual property may be obtained from external parties through purchase or licence agreements. Intellectual property may also be developed by the agency.

Agencies need to determine the significance of the identified intellectual property to the strategic objectives of the agency. Agencies need to record significant intellectual property centrally. This should include a description of the intellectual property and where, when, and by whom it was created/purchased, the details of ownership rights (e.g., owned, licensed), who holds the intellectual property, who is directly responsible for its management, and the status of any protection. Documenting this information centrally helps ensure that intellectual property is appropriately managed across operating areas.

To manage intellectual resources adequately to achieve objectives, appropriate staff need access to this information. This awareness and informed use of intellectual property helps avoid duplication.

SaskTel does not have a central record of intellectual property assets. Without centrally identifying significant intellectual property (describing where, when, and by whom it was created/purchased, the details of ownership, who holds the intellectual property, who is directly responsible for its management, and the status of any protection), SaskTel risks not appropriately managing intellectual property across operating areas. SaskTel's legal department keeps a list of trademarks and of patents.

SaskTel also has experienced employees who, over time, have built their knowledge of SaskTel's intellectual property. This knowledge assists SaskTel in managing intellectual property. But this corporate knowledge is vulnerable to loss as SaskTel faces the same succession and staffing challenges facing all businesses in the province.

Management of ownership

We expect agencies to determine the appropriate level of ownership of intellectual property and secure that level of ownership.

In its management of ownership decisions for intellectual property, an agency will likely require different levels of ownership (i.e., levels of rights and interests) for different intellectual property assets. The amount of control required over the intellectual property relates to the use of the property to further the objectives of the agency. Management decisions on ownership range from full ownership (e.g., develop, buy), to rights to use (e.g., license), to rights to use and modify (e.g., license then change property) to other combinations resulting in less than full ownership.

Intellectual property issues are best approached before the creation/purchase of specific intellectual property. Therefore, the agency should consider intellectual property ownership issues before property is acquired, contracts are signed, tenders are invited, or consultants are hired.

Intellectual property issues should be a standard part of the agency's processes. For example, ownership rights and clauses should be clearly

stated in contracts with outside parties and employees. These contracts should also include non-disclosure and confidentiality clauses where necessary.

To manage ownership of intellectual property, staff need to be aware of potential issues and receive appropriate training.

SaskTel has a wide range of intellectual property rights. Senior management told us that SaskTel's general approach has been to acquire the rights it needs from others, rather than focusing on developing its own solutions in-house. Senior managers were aware of this approach although it was not well documented. SaskTel does not have a systematic approach for identifying and exploiting intellectual property opportunities.

SaskTel addresses intellectual property issues and concerns in many of its processes. As noted, SaskTel has policies and corporate procedures that specifically consider intellectual property. SaskTel's code of business conduct specifies that employees should respect copyright laws. This is also reflected in a policy that sets out SaskTel's expectation that it will protect the rights of others and describes how it will do so. Both the code of business conduct and other corporate procedures also provide that intellectual property developed by employees will belong to SaskTel.

SaskTel's approach to intellectual property is also reflected in templates and model documents. For example, hiring forms and annual performance evaluation forms for employees have a sign-off for supervisors to record that they have reminded staff of their obligations. A corporate procedure sets out the requirement that employment contracts must address intellectual property issues.

SaskTel has other relevant management controls, including a due-diligence checklist that considers intellectual property when evaluating business acquisitions. SaskTel also has formal legal review and contract approval processes.

Contracts generally included some provisions relating to intellectual property. Senior managers told us that when they evaluate contracts, they consider whether they should contract for subsidiaries separately and, if dollar amounts are high, whether SaskTel should obtain rights to the

intellectual property beyond just the right to use the product. SaskTel has successfully negotiated for such rights.

SaskTel does not have a consistent approach regarding agreements between SaskTel and its subsidiaries for intellectual property. Such agreements help in managing intellectual property and also help protect rights. Also, SaskTel does not have a central repository for all contracts. Therefore, SaskTel has risk that it may lose or not be able to find certain contracts, including original contracts, when needed.

3. We recommend that SaskTel consistently document intellectual property agreements with its subsidiaries.

SaskTel management told us that it will consistently document intellectual property agreements with its subsidiaries on a go forward basis.

4. We recommend that SaskTel establish centralized responsibility for maintaining original contracts.

SaskTel management told us it will establish centralized responsibility for the contract repositories for all original contracts. Management told us that centralized responsibility will include annual reviews with the keepers of the repository to ensure that all contracts are being kept for safekeeping, ensure the contracts in question are kept secure and are properly managed whenever someone needs to view an original contract, and that the contracts are properly handled from a records retention perspective.

Monitoring and protection

We expect agencies to monitor and protect intellectual property.

Agencies need to monitor their use of intellectual property that they own or have secured rights to use. Agencies also need to monitor others' use of agency-owned intellectual property (i.e., that they have commercialized). Agencies must monitor potential infringement of intellectual property rights, by the agency or by others, and appropriately address any identified infringement issues.

An understanding of the issues and processes to seek advice and make decisions can help ensure intellectual property is appropriately protected. It can also significantly lower the risk of agency infringement of others' intellectual property rights.

To monitor its use of others' intellectual property, SaskTel needs to know what it has the right to use and what it is actually using. It does not have adequate processes to do this. While SaskTel does have a system intended to track software licenses, it does not consistently collect and record information in the system. Also, SaskTel does not systematically check the number of instances that licensed applications are in use. Unless it can determine whether it is complying with the rights that it has obtained, SaskTel cannot take steps to address any issues.

SaskTel has relatively few intellectual property assets that it has sought to sell or license to other agencies. SaskTel uses contracts to protect its right to monitor use of its intellectual property. For certain intellectual property, SaskTel has employed an agent to specifically identify use by others that infringes on SaskTel's rights.

5. We recommend that SaskTel implement a system to assist it to comply with the intellectual property rights it has acquired.

SaskTel management told us it intends to direct consistent use of the tracking system in place to enable it to adhere to the contractual commitments it has made with respect to the intellectual property rights it has acquired from third parties. SaskTel management told us that in this regard, SaskTel will also be considering in 2007 the purchase of a new system to aid in tracking and complying with these contractual commitments.

Evaluation and reporting

We expect agencies to evaluate and report on both the performance of their intellectual property assets and the effectiveness of their processes to protect and, if applicable, exploit those assets.

Agencies should assess the effectiveness of their intellectual property management processes. Key intellectual property assets should be managed with the same attention given to tangible assets. The processes

should reflect the relative importance of the intellectual property assets to the strategic objectives of the agency and the risks it faces.

Regular reporting can identify opportunities for improvement and the need for revised intellectual property management strategies. Failure to regularly report on an agency's intellectual property results in less agency control over and accountability for intellectual property and can reduce the effective protection and development of these assets.

As indicated above, SaskTel does not have a documented plan for intellectual property. Nor does it have a central record of intellectual property assets. As a result, it is not able to systematically monitor or evaluate the performance of these assets. SaskTel does have extensive processes for assessing the performance of its businesses.

SaskTel does not formally evaluate or report on the effectiveness of its intellectual property processes. Management advised us that it evaluates the effectiveness of its processes in part by assessing the extent to which SaskTel has been involved in related litigation.

Reporting on the performance of intellectual property (for example, in areas like development activities, cost and method of acquisition, revenue generation, commercialization activities, enforcement, awareness activities) would allow SaskTel to assess progress against plan. Reporting on the effectiveness of their intellectual property processes would allow SaskTel to know if related risks are adequately managed.

6. We recommend that SaskTel monitor its progress in achieving its plan for managing intellectual property.

SaskTel management told us that it intends to annually bring forward an item to the SaskTel Executive that will present to the Executive the progress that SaskTel is making with regard to its intellectual property plan.

SaskTel's governance of owned and controlled companies—a follow-up

SaskTel operates its businesses in a complicated organizational structure that involves many separate companies. In 2004, we examined whether

SaskTel had adequate processes to govern the companies it owned and controlled. We reported the results of the audit in our 2004 Report – Volume 1, Chapter 5. We made recommendations aimed at improving how SaskTel communicated governance expectations to the companies it owned and controlled, and how SaskTel assessed the effectiveness of the boards of these companies.

We followed up the audit in 2005 and reported the results of the follow-up in our 2005 Report – Volume 1, Chapter 13. We noted SaskTel had made improvements. However, some of our recommendations remained outstanding. In the area of communicating governance expectations, we continued to recommend that SaskTel:

- ◆ regularly highlight where its Board delegates to the President of SaskTel authority to name board members of SaskTel's companies
- ◆ ensure that companies it controls, or plans to control, are subject to shareholder agreements and articles of incorporation that reflect the governance expectations placed on SaskTel

In the area of assessing the effectiveness of the boards of owned or controlled companies, we continued to recommend that SaskTel:

- ◆ document the governance risks and identify levels of governance risk that are acceptable for each company
- ◆ require each company to provide the SaskTel Board with its evaluation of its board

The Legislative Assembly's Standing Committee on Crown and Central Agencies considered our recommendations in November 2006 and agreed with them.

In March 2007, we assessed SaskTel's actions to address our remaining recommendations. SaskTel has met our recommendations. We set out the results of our work below.

Communicating governance expectations

SaskTel has modified a report that it provides annually to SaskTel's Board. The report summarizes the compliance of SaskTel's companies with governance expectations set out by the Crown Investments Corporation of Saskatchewan. The report now explicitly highlights the extent to which the SaskTel Board has delegated to the President of SaskTel the authority to name board members of SaskTel's companies.

SaskTel uses a due diligence checklist in considering and carrying out businesses acquisitions. The checklist requires review of articles of incorporation and shareholder agreements. In addition, SaskTel told us that it will be modifying the base documents it uses to draft or modify shareholder agreements to alert its lawyers to the governance matters that need to be considered.

Assessing board effectiveness of owned and controlled companies

SaskTel regularly and formally considers risks including for the companies they own and control. SaskTel told us it plans to include governance-related risks as part of its review of legal risks.

SaskTel now requires the companies it owns and controls to provide board evaluations to the SaskTel Board. The Governance Committee of the SaskTel Board receives these evaluations.

Selected references for processes to manage intellectual property

- Audit Office of New South Wales. (2005). *Follow-up of Performance Audit: Management of Intellectual Property*.
http://www.audit.nsw.gov.au/publications/reports/performance/2005/followup_ip/followup-IP-contents.html. (April 2006).
- Audit Office of New South Wales. (2001). *Better practice guide: Management of intellectual property*.
http://www.audit.nsw.gov.au/publications/better_practice/2001/intellectual_property_bpg_oct_01.pdf. (April 2006).
- Australian National Audit Office. (2004) *Intellectual Property Policies and Practices in Commonwealth Agencies*. In Audit Report No.25 2003–04. Canberra: Author.
- Canadian Intellectual Property Office. (2004). *Stand out from your competitors: Make intellectual property your best business ally*. Ottawa: Industry Canada.
- Limpert, B., & Samiian, A. (2002). *Conducting an Intellectual Property Audit and IP Due Diligence*. Conference papers presented at the Infonex Intellectual Property Summit 2002.
- Sum, T.W., & Manson, M.D. (2001). *Intellectual property due diligence audits of high-tech companies*. Conference papers presented at the Canadian Corporate Counsel Association, 13th Annual Meeting.
- Survey: Patents and technology. A market for ideas. (2005, October 22). *The Economist*, special insert after 58, 3.
- Survey: Patents and technology. The arms race. (2005, October 22). *The Economist*, special insert after 58, 6.