

KEY TERMS OF A LICENSING AGREEMENT

Topic 6 (a) subject matter
Topic 6 (b) Scope
Topic 6 (d) Forms of Payment

WIPO - HEPTECH WORKSHOP

“Advanced TTO s Meet Early - Stage TTO s”

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I. Intellectual Property (IP) Licensing

- A license is a consent by the owner (Licensor) to the use of IP by other party (Licensee) in exchange for money or some other value (cross – license).
- **COMMISSION REGULATION (EC) No 772/2004** – “Technology transfer agreements concern the licensing of technology. Such agreements will usually improve economic efficiency and be pro-competitive as they can reduce duplication of research and development, strengthen the incentive for the initial research and development, spur incremental innovation, facilitate diffusion and generate product market competition”

I. Intellectual Property (IP) Licensing

- IP licensing only occurs when one of the parties **owns** valuable intangible assets know as **Intellectual Property (IP)**.
- IP ownership gives a legal right to the owner of IP to exclude or prevent others from using that IP for commercial purposes.
- Intellectual Property (registered or non registered) is the **subject matter** of the licensing agreement.
- Different kinds of IP Licenses
 - Pure IP License
 - Product or Technology License
 - Standard License

I. IP Licensing

- Technology Licensing often occurs as a consequence or in the context of other relationships (research or business) in which other agreements are very important. In that case licensing agreement is interrelated to these other agreements.
 - Joint Venture Agreement
 - Merger of Businesses
 - Research Collaboration Agreement
 - Sponsored Research Agreement
 - Material Transfer Agreement
 - Research Service Agreement (IP ownership of the developed research results may be assigned in advance)

I. IP Licensing and Technology Transfer

Licensing Agreements

- Most frequently used mean for technology transfer, in particular in university-industry relations,
- Advantage - gives variety of options for business relations with different partners by using the same portfolio of IP,
- “Win – win “ solutions,
- Possibility for licensing partners to share the risk through royalty rates;
- Potentially provides significant return on investment and incentives for creativity and innovation;
- Very important business tool for new “collaborative innovation” or “open innovation”.

■ II. Key Terms of a Licensing Agreement



The key terms of a licensing agreement - are the vital elements in the structure of the licensing agreement.

Key Terms

The Four Clusters

- I. Subject Matter: What is licensed?
- II. Scope: What can you do with it?
- III. Financial: What value is it?
- IV. Upgrades and maintenance: What will happen with it in the future?

Key Terms and Business Objectives

- Key Terms are Inter - Related with Business Objectives of the Negotiating Parties.
- What do you want to achieve with the licensing agreement will influence your options related to key terms!
- What is essential for you?

Key Terms and Business Objectives

What is the **business reason** for the license?



What must you gain in order for this agreement to be **worthwhile**?

- What is the **best result** that can be obtained?
- What outcome do you want to **avoid**?
- From a business perspective, is the best result a license to IP rights only (“**pure IP license**”) or a broader set of related agreements (“**business partnership**”)?
- In what specific ways will this license **make money** for your business?

Chapter III: Cluster 1

The Subject Matter

Subject Matter: What is Licensed?

- Subject matter of a licensing agreement is always an intellectual property right;
- It can be registered IP:
 - Patent – formula for medical treatment;
 - Copyright – software;
 - Trademark – “coca – cola”, franchising – “McDonalds”
 - Industrial design – car design;
- Important subject matter of a technology transfer agreement is trade secret and know - how – non registered IP.

Subject Matter of the Imaginative “Smart Turbine” Licensing Agreement

Ind.
design

Patent 1 (Turbine)	Patent 2 (Integration System)	Patent 3 (Thin Film)
1. Claim	1. Claim	1. Claim
2. Claim	2. Claim	2. Claim
3. Claim	3. Claim	3. Claim
4. Claim	4. Claim	4. Claim
5. Claim	5. Claim	5. Claim
6. Claim	6. Claim	6. Claim
7. Claim	7. Claim	7. Claim
Copyright (Software, Schematics, Documentation)		
Trade Secrets Know-how		
Trademark		

II. What the Licensor Want to License OUT

Patent 1 (Turbine)	Patent 2 (Integration System)	Patent 3 (Thin Film)
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5. Claim	5. Claim	5. Claim
6. Claim	6. Claim	6. Claim
7. Claim	7. Claim	7. Claim

Ind.
design

Copyright
(Technical Documentation)

Know-how

Trademark

I. What the Licensee Wants to License IN

Patent 2 (Integration System)
1. Claim
2. Claim
3. Claim
4. Claim
5. Claim
6. Claim
7. Claim

Patent 3 (Thin Film)
1. Claim
2. Claim
3. Claim
4. Claim
5. Claim
6. Claim
7. Claim

Copyright
(Software, Schematics, Documentation)

Trade Secrets
Know-how

The Subject Matter

What are You Licensing? Define and Include Relevant Documentation

- Patent No. _____
- The trademark _____
- A protocol
- All rights necessarily infringed by the X Standard
- The X technology

- Formula (to be completed....?)
- The Product
- The Licensed Material
- Documentation
- Schematics
- As set forth in Appendix A...

Common Problems



- Who owns the IP?
- Unfinished development
- Patents not issued
- Multiple parties
- Pending claims
- MOUs or Letters of Intent
- Best efforts, good faith

How Can You Clarify the Subject Matter?



- Confidentiality agreements
- Prototype agreements
- Feasibility studies
- Interim agreements (addressing cost)
- Consultations with lawyers, experts
- Study of documentation, databases
- Study competing products

Chapter III: Cluster 2

The Scope of the Rights

Scope of Rights



- What and how broad rights your business model require?
- Make, have made, use, sell, import, transfer, make improvements?
- Copy, display, modify, make derivative works, distribute, transfer?
- Conduct research and product development?

Scope of Rights



- Very important element in a licensing agreement, as it gives both parties various options to negotiate and to adjust to their own business interest – “win-win”.
- Options mainly relates to:
 - Exclusivity of the rights
 - Field of use of IP and technology
 - Territory
 - Timelines
 - Sublicensing

Scope: Exclusive rights?



- A necessary risk (for Licensor)?
- What arguments can Licensee make for obtaining exclusivity of the rights?
- What arguments can Licensor make against?
- Possible means of protection against a lazy, dishonest, or ineffective licensee:
 - Minimum Royalties
 - Time Limitation of Exclusivity
 - Inefficiency as a Trigger for Contract Termination

Common Problems in Cluster 2



- Scope too broad
- Scope too vague
- Scope too restricted (e.g. no right to sell)
- Exclusivity granted without protections
- Unclear how sublicenses are administered
- Grant backs that prevent the licensee from creating advantage

Chapter III: Cluster 3

Financial Terms in Licensing
Agreements

Cluster 3: Financial Terms in License Agreements

- Value: Total value of the licensed IP in context of the other key terms; and
- Form of payment: How the payments will be made.

What is IP Valuation?

- Benefit
- Risk

Valuation: The process of identifying and measuring financial benefit and risk from an asset.

The value of IP depends on the context !!

Formes of Payment

- Royalties
- Lump sum
- Initial fee or licensing fee
- Installment payments
- Combinations

What is a Royalty?

- A form of payment in which Licensee pays value to Licensor over a negotiated period of time, in return for Licensor's consent to use IP.
- Royalties are based on volume (per unit) or a percentage revenues of products using the IP.

Why Royalties are Used

- A way of distributing payment of value to Licensor so as to:
 - Permit sharing of benefit,
 - Share risk that the technology will not succeed (because of technology defect or market failure),
 - Avoid immediate high cost to Licensee,
 - Ensure mutual motivation to make technology succeed.

Royalty Variations

- Minimum Royalties - Important for licensor in exclusive licenses as security in case of failure of licensee to exploit the technology
- Capped Royalties
- Ramping (Increasing) Royalties
- Declining Royalties
- Premium for high performance (bonus)
- Advances against royalties (where licensor needs up front cash to fund operations)

Royalty Variations

- Ramping (increasing) royalties
 - Declining unit sales >> higher royalty rate to keep income to licensor constant.
- Declining royalties
 - the reverse of above;
 - where value of technology is declining.

Royalty Variations

- Capped royalties
 - Cap royalties over term of agreement to a fixed amount/avoids windfall
 - Licensor does not like as it limits upside
- Premium for high performance (bonus)
- Advances against royalties (where licensor needs up front cash to fund operations)

Minimum Royalties

- Important for licensor in exclusive licenses as security in case of failure of licensee to exploit the technology;
- Absolute payment obligations? Risky for the licensee--can run it into insolvency if the technology is not successful or if the minimum is too high;
- Trigger for option to terminate or modify contract.

Important !

- Separate royalties for patents and know how (e.g. trade secrets) or other IP in case patent is invalidated;
- Do not confuse royalties with initial license fees, development installment payments, consulting payments, etc.

Comparable Royalties

Royalty Rates for In-Licensing by Industry							
Industry	0-2%	2-5%	5-10%	10-15%	15-20%	20-25%	>25%
Aerospace	50.0%	50.0%					
Automotive	52.5%	45.0%	2.5%				
Chemical	16.5%	58.1%	24.3%	0.8%	0.4%		
Computer	62.5%	31.3%	6.2%				
Electronics		50.0%	25.0%	25.0%			
Energy	33.3%	66.7%					
Food/Consumer		100%					
General Mfg.	45.0%	28.6%	12.1%	14.3%			
Government/University	25.0%	25.0%	50.0%				
Health Care	3.3%	51.7%	45.0%				
Pharmaceuticals	23.6%	32.1%	29.3%	12.5%	1.1%	0.7%	0.7%
Telecommunications	40.0%	37.4%	23.6%				

Dan McGavock, IPC Group, Chicago, Illinois (based on survey)

Financial Terms: Warranties & Indemnities

- Product warranty--who will assume liability if a customer or purchaser sues for product defects or failure to perform to specification (e.g. pharmaceuticals, software)?
- Indemnification--who bears risk of third party claims for infringement?
- This is negotiated and is a financial term.

Financial Terms: Warranties & Indemnities

- Generally non-profit and public institutions do not agree to indemnify because they have a public trust.
- Indemnity by small party not worth much so as a practical matter consider the assets of the party you are negotiating with.
- Often indemnity is capped at a fixed sum or at total amount of royalties paid.



Thank you !

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