

Licensing

A Researcher's Guide



Contents

Introduction	2
Section 1 How can IP be commercialised?	4
Section 2 Why License?	10
Section 3 How to License	16
Section 4 Types of Licence	21
Section 5 The Licence – The Basics	23
Section 6 Payment Provisions	34
Section 7 Other Licence Provisions	48
Section 8 Post-Signing Actions	54
Section 9 Snap-shot of Licensing-out	56
Section 10 Glossary of Terms	58
Section 11 Useful Links	60

Introduction

This Guide is intended to act as a practical reference booklet for use from time to time during your research career. Its goals are to increase your awareness of licensing as a possibility for transferring your intellectual property (IP) into a business/industrial context and to encourage you to be as engaged as much in the licensing process as is appropriate. It explains:

- what a licence of IP is and why you may want to license IP
- the different ways in which IP can be licensed
- what types of licence there are and what terms a licence should typically contain
- what you should be doing after a licence agreement has been signed.

As the IP originator you will be very motivated to participate at some level. You will certainly have a key interest in making sure the licensing is carried out professionally and with the best chance for success. This Guide will help you ensure that by your asking the right questions and checking appropriately on the process, its progress and the documentation, that the best quality outcome is likely and that there is real momentum throughout the process. If you are better acquainted with the activity, you are in a position to add value and form a productive partnership with those leading your licensing project on behalf of your research institution and with the professional advisers engaged to advise on the project. You will also come across as more credible to those to whom the IP is hopefully to be licensed.

Throughout this Guide we refer to “your IP” but this is to make the Guide personal. Legally any IP that you create almost certainly belongs to your research institution. However, in spirit, you, your institution and its IP commercialisation team will act as one. Your IP commercialisation organisation will be able to advise you further, however this Guide will act as a prompt for you in these relationships.

Remember that this is just a guide and not a substitute for you taking your own independent professional advice.

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The fundamental requirement before embarking upon any IP commercialisation activity is to protect it. Having done so, a number of options will be available to you. One effective way to commercialise (or exploit) IP is for you or more likely your institution (the licensor) to license it to someone else (the licensee) who will carry out the necessary further work, especially the marketing, distribution and sales activities.

There are two main ways in which you can commercialise IP, you can either:

- sell it (as you would sell a house or a car); or
- permit someone else to use it (as you would do if you rented out a flat).

Selling IP

Selling IP to a third party is technically known as an '**assignment**'. In the same way that you would not be able to continue to live in a house that you have sold to someone else, once IP has been assigned to someone else you will have no further rights to use that IP. This is important to remember because if you continue to use the IP after you have assigned it then, unless you have the permission of the new owner to do so, you will infringe the new owner's rights in the IP (which is illegal).

Say you have developed a pack of teaching materials for your meteorology students. You are contacted by Ms Bright from the local television weather department. Ms Bright is interested in using your materials for training her weather staff. Ms Bright offers a significant sum of money in return for an assignment of all IP in the training materials. This seems too good an offer to miss for the department and therefore it is decided to go ahead with the assignment.

The following September you continue to incorporate the same teaching materials in your first year and distance learning courses. You are contacted by Ms Bright who informs you that if you wish to continue to use the teaching materials, a licence fee of £220 per student must be paid by the Research Institution for use of the materials. Ms Bright is perfectly entitled to do this on the basis that the local TV station is the new owner of the materials. Clearly you should have thought about this before assigning your IP and got a licence back for use in teaching at the very least.

Licensing IP

Instead of assigning IP, it may be more appropriate to retain ownership of the IP and instead just allow someone else to use it. This is known as a **'licence out'**. On the other side of the coin, it may be that you need to use IP which is owned by someone else. You will need to request to be granted rights to use the IP. This is known as a **'licence in'**. When the licence is of copyright in artistic works, of design rights or of a trade mark, for reproduction on an article, it is called merchandising. For written or musical works the licence may be part of a Publishing Agreement. For any filmed material, it is likely to be part of a Production Agreement.

Let's look at a couple of examples:

Licensing Out	Licensing In
You have produced an on-line 'IP management' training package. You have been approached by a company which wishes to use this package. The package, including its constituent software and various training materials, can be licensed out to the company to use as it requires.	You have developed a novel form of radiator device. However, for this to be of any interest to the commercial market it needs to be specifically insulated. You know of a company which uses some technology to spray on insulating coating – this would be ideal. The company has a patent over this technology. To use the technology to insulate your radiator in preparation for commercialisation you need a licence from the company to use its 'spray coating' technology.

It is less likely that you will be involved in a situation where you need to 'license in' IP. This is more often used by spin-out companies. This Guide concentrates on the 'licensing out' of IP and will therefore tend to look at a licence from the perspective of the party which is licensing out.

When will I need to consider whether to sell or allow someone to use my IP?

Figure 1 illustrates some examples of when a licence or an assignment of your IP may be involved.

Figure 1

	If you write an article for a publisher, the publisher is likely to request you to either assign or license your copyright in the article to the publisher.
	If you want to allow someone to use and commercialise an invention that you have developed and patented, you will need to license that person the rights to use and commercialise the invention and the patent.
	If you are working on a collaborative project with another company or institution under which you intend to combine each others' intellectual property and develop it further – you will require a licence from the other party to use its IP for the purposes of the project. Likewise, the other party will require a licence from you to use your IP for the purposes of the project.
	If you have written a particular piece of software, you may want to license the object code for this software to end-users.
	When a spin out company is set up it will often require certain IP to be transferred to it. This will sometimes be in the form of an assignment as any investors who put money into the company may insist that the company owns the IP it requires. However, in some cases the spin-out may take a licence of the IP instead.

Assignment -v- Licence – which is the better option?

Well, basically this depends. The type of IP, its value, potential, your plans, the costs involved, competition and its relevance to other research areas are all factors which may need to be considered. Figure 2 contains a comparison of some of the advantages and disadvantages of assigning or licensing your IP.

Figure 2

Concern	Assignment	Licence
Future use	Once assigned, you will lose all your rights to the IP. This means that if you or any other research group needs to use the assigned IP or any part of it for future research and development, in most cases, the consent of the new owner of the IP will need to be obtained and you may even need to pay for such further use.	When you allow someone else to use your IP, you will still retain ownership. You can therefore limit the extent to which the IP can be used. Depending on the nature of the licence you may still be able to continue to use the IP or you may negotiate certain areas in which you need to continue to use it.
Tax	When you sell IP, you are deemed to make a disposal for capital gains tax (CGT) purposes and you will be liable to pay the tax. (If your research institution is assigning it may be a charitable institution and be exempt from CGT).	The grant of a licence does not automatically amount to an outright disposal of your IP, therefore capital gains tax will not be payable on any money you may receive pursuant to any licence you enter into (although corporation or income tax may be payable on such money). However, if an exclusive licence is granted of IP created prior to 31 March 2002, capital gains tax may be payable and advice should be sought.

Concern	Assignment	Licence
<p>Value</p>	<p>Often you know exactly how much you are going to get for your IP and you will make a quick return with no continuing obligations.</p> <p>However, selling your IP may provide you with the least return in the longer term, as IP tends to become more valuable as it is developed further and commercialised.</p> <p>Fixing the sale price for your IP may be difficult if you have not yet exploited your IP. As a result, you may be at risk of selling your IP at an undervalue.</p> <p>If you think that your IP is very high risk and it will be difficult to commercialise successfully – then this may be your best option as at least you will be getting something in return.</p>	<p>By allowing someone to use your IP, you minimise your capital investment and risk and maximise the return you will get on your IP by creating an income stream, whilst still retaining control over your IP and the parties you are allowing to use it.</p> <p>The percentage return you get on your IP, when you allow someone else to use it, will be less than if you were to commercialise your IP yourself, as the proceeds of commercialisation will be shared with the third party.</p> <p>You can also use licensing as a tool to enter into new markets and countries which you might not be able to reach without the assistance of a local licensee. Licensing is often the ideal middle way for you to adopt when you do not have the resources to exploit your IP, giving additional financial return on it.</p>

Concern	Assignment	Licence
Insolvency	If the new owner of the IP becomes insolvent it is very difficult to recover your rights in the IP. You would in effect have to buy it from the insolvency practitioner, such as a liquidator.	If the person/company you have allowed to use your IP becomes insolvent, you should be able to recover all the rights you granted to such person/company, as long as you provided for this in your licence agreement.
Maintenance/ Costs	If you assign registered rights, the new owner will assume responsibility for the maintenance and defence of the registered rights e.g. the payment of renewal fees and any legal costs.	If you license registered rights, unless otherwise provided for under the licence agreement, the owner will retain responsibility for the maintenance and defence of those rights. In some cases you may be in a position where the IP is simply not worth you continuing with these responsibilities. In these cases it may be simpler just to assign.

As you can see, in most cases it will be more beneficial for you to license your IP as opposed to assigning it. Licensing is not easy though. Unless you are very experienced in licensing you should get advice from your IP commercialisation organisation or a specialist IP lawyer.

Let's now look in more detail at some of the issues you should be considering when allowing someone to use your IP.

There are five main reasons why you might consider getting involved in licensing:

- financial gain for you and your institution
- resources to support your research interests
- the alternative to spin-out company commercialisation
- opportunities for case study material
- seeing your research translate into tangible products, processes or services.

These reasons are in no particular order, nor is any one mutually exclusive of the others. Your priority will depend upon the nature of the IP to be licensed, its stage of development, the degree of IP protection secured and your personal objectives and other commitments at the time.

It is almost certainly the case that your research institution's principal reason for supporting the licensing route of IP commercialisation (rather than forming a spin-out) is to extend its relationships with industrial and commercial companies and to see its reputation enhanced by its high quality research work being translated into economic benefit for society, especially if this is within its own local and national contexts.

Let's look at each reason in some detail.

Personal and institution financial gain

Your research institution will usually be willing to share with you the gains it makes from the licensing of its inventions, copyright, designs etc. The sharing proportion will differ from institution to institution, but it will generally mean sharing the net gains with you (which means the amount after any deductions for things such as patent costs, marketing expenses, proof-of-principle investments, certain taxes). You will be expected to pay tax on your gain, but this can be done by PAYE or sometimes by paying you the full amount due and for you to make your own tax arrangements. Your institution will expect to be indemnified by you, should you elect to make your own arrangements).

The income will usually flow to the institution as a series of payments (known as royalties) based upon a percentage of the sales value of the product or service of which the IP forms a part or (in exceptional cases) the whole. Sometimes an up-front payment can be paid (called a licence fee) to recognise the expertise and effort necessary in having created and in transferring the IP to the licensee (see Section 6 – Payment Provisions).

It will be motivating for you to be able to see that your institution and school/unit have benefited financially from the successful commercialisation of the IP that you originate. You are also at liberty to place some or all of the money due to you personally into further research, which many researchers do, in order to enhance their research outputs (and which in turn may help with increased opportunities for promotion and for reputation by, for example, generating more quality research papers).

Whilst for the “right” IP there are good chances to earn income from licensing, the returns may not start to flow regularly until a long time after the agreement to license has been signed. This is because the organisation to whom the licence is granted will most probably need to expend considerable resources in developing the IP that has been licensed before being able to commercialise it. Therefore not only will it be a while before royalties are due (probably several years), the share that your institution will receive from the licensed organisation (the royalty rate or level of royalties) is likely to be only a small percentage. So a typical arrangement could be:

■ Main agreement

The licensee agrees with the research institution to take a licence on agreed terms, e.g. 5% of net sales revenue. Of course, although often conforming to typical industry norms/ranges, the royalty rate varies from case-to-case and will be the outcome of a negotiation.

■ Secondary (internal) arrangement

The research organisation and the researcher have a standard policy of sharing, e.g. 50/50 of net income. Hence, after the deduction of patent costs, marketing costs etc. by the institution, the research institution and the researcher both receive 2.5% of the licensee’s net sales revenue. The returns to an individual researcher from a licence of research-based IP can be attractive, although in general they are modest.

There are examples of spectacular money-spinners but these are exceptional, so whilst it is perfectly acceptable to aim for big success, just don't bank on it turning out that way! More details and explanations of royalties and payment terms are set out later in Section 6.

Resources to support your research

Once a company has agreed to take a licence, it will often decide that the preliminary development work is best carried out in your research lab/department under your supervision, rather than at its premises, for example to create a refined prototype. The licensee may also wish to test the IP in different circumstances and environments. This will mean that the licensee could purchase extra equipment for you to undertake the work (which usually becomes a permanent loan to or is eventually owned by the research institution). It may also mean that you are allowed access to state-of-the-art resources at the licensee's premises, which your research institution may not have, to continue the research and development work. The licensee could also be willing to pay for the employment costs of a research assistant to support the work and will often agree to the results of the work being published (subject to it having the opportunity to patent before publication and to withdraw any commercially sensitive information).

There are a number of formal schemes and grants which will financially support knowledge transfer activities and collaborations (e.g. Knowledge Transfer Partnerships and Support For Innovation Funds) and, if needed, the licensee can qualify as the eligible commercial partner necessary to apply for such schemes. Some of the schemes are linked to academic award programmes (e.g. Masters by research) and so can be aligned with your mainstream interests and be mutually beneficial to the research institution and the licensee. More details about your local business link and the Department for Business, Innovation and Skills who can help with such support are available at www.bis.gov.uk

A close relationship between your research group and the licensee's research team can evolve during the initial IP transfer and development phase. There are many examples where licensees have become interested in other aspects of a licensor's research activities and as a result have

sponsored research in areas beyond the area in which it originally took an interest and the licence. It is also typical for a licensee to pay for your conference attendance fees, research seminars and symposia participation, if it is in the field in which it is seeking to promote the licensed IP.

An additional benefit of such on-going relationships is that you will be in an ideal position to know or to find out about the progress of the originally licensed IP (e.g. how much commitment is being made to its promotion, internally and externally).

Why license rather than spin-out?

The time required and the demands made of you to commercialise IP via a spin-out would probably be considerably greater than by licensing to an established company. An existing firm could include a spin-out which has previously been established for some time, either at your own research institute or at another one.

With licensing, following the initial effort needed in getting a firm interested in your IP and the time and effort required in transferring the IP, any continuing involvement by yourself is likely to diminish rapidly. In any event such on-going contact is likely to be self-regulating, in that it would be well controlled through a consultancy and/or research contract. This is a much more controlled interaction for you than with a spin-out, which tends to be a more fluid and dynamic experience and with many more interested parties involved e.g. entrepreneurial managers, private investors, venture capitalists etc., who are more like intermediaries rather than research collaborators – so they apply different goals/pressures.

Often your IP will require a large infrastructure to be developed and enhanced, which could be very expensive. There may already be complementary IP, products and services which are present in established firms. An established firm could include a spin-out which has previously been in existence for some time, either at your own research institute or at another one. In these circumstances it makes sense to seek to place your IP in that context, rather than try to raise capital via a spin-out company and ultimately to compete with established players.

A further consideration is market access. An established firm may already have its own marketing team and sales force, its own distribution channels and a well-respected brand and reputation. These will enable it to access the market for your product very effectively; by contrast commercialising the IP through a start-up company will require that company to create its access to the marketplace from scratch. It is possible to consider creating a company solely to attract some investment to develop your IP. This is more of a tactic as the founders of such companies are usually planning to license the developed IP, rather than planning to run a product or service-based company. Companies that are set-up for this purpose are usually called IP development start-ups or licensing start-ups (or spin-outs). They bring with them many of the attendant challenges of any spin-out and tend to conform to the usual process and steps involved.

Whilst it may be tempting to go down this route to raise some capital in order to retain a degree of independence of development/control, it would be worth thoroughly testing whether it is in practice necessary to do so and to try a licensing approach first.

If your IP is truly the “first-of-its-kind” and is likely to have a revolutionary impact in its field, there may not be an established player to whom you can license or, even if there is, that may not be the best way for you to derive the maximum value. Your commercialisation team will discuss such cases with you.

Case Study Material

Since licensing involves you directly taking part in an IP activity, it provides you with real experiences and will give you first-hand feedback from those people who are receiving the IP and then turning it into a commercial opportunity. This will often involve you in discussions about the financing, project management and the resourcing of the licence project, as well as introducing you to many people from other disciplines, such as product development and marketing. This enables you to develop “colourful” (but non-confidential) material which could be used in workshop discussions or research training programmes to enhance your research team’s understanding of the perspective of and the demands upon those people who are concerned with taking research outputs to market. If you also have teaching duties, this “live” material might be interesting for students.

Translation of ideas into society

It is fully understood that you have chosen a career in research because of your interests in analysis and curiosity-driven experimentation and not principally because of any strong interest, for example, in industrial applications or business management. Nevertheless, having come up with a new way of doing things, or having solved a problem or limitation, it is pleasing to researchers to see how ideas might benefit society. This is only likely to be achieved if the IP is converted into a useful product, process or service through another organisation and so licensing to an existing business is a good way to achieve this goal.

IN BRIEF

- Financial rewards from successful licensing are usually not immediate but can build up to respectable levels over the years
- Licensing can be about more than making money and can lead to other appropriate benefits
- In many cases it is the most relevant, practical and straightforward way to commercialise research institution generated IP
- Patience is a virtue and will definitely be needed if you engage in licensing.

The two main activities that are necessary to achieve a licence are:

- finding a company that is interested in the opportunity that your IP represents and convincing it of its merits; and
- agreeing the terms on which the IP will be licensed.

Both of these are taxing. Of course your institution's IP commercialisation organisation or a specialist agency will manage these tasks in partnership with you. Nevertheless, as the IP originator, you are essential to both activities; very actively in the first activity and in an advisory capacity in the second.

Gaining Interest

You are as likely as anyone to identify and obtain interest from the company that ultimately enters into the licence arrangement. A study by the Massachusetts Institute of Technology (MIT) shows that half of all its licensees has been identified by the IP originator. Similarly the Lambert Review of university/business interaction revealed that 50% of all licensing contracts by UK universities had been concluded where the researcher already had some form of relationship with the licensee company e.g. through a consulting assignment or applied research project. Therefore, you can be very helpful and important in this marketing exercise. Not only will you readily be able to think of one or two probable target companies, you will also have the opportunity to publicise licence opportunities by your presence and talks at conferences, seminars and exhibitions and also through writing in appropriate publications/articles.

It is also useful to produce a marketing flyer (ideally in conjunction with your IP commercialisation organisation) and have this displayed on your website as well as on the IP commercialisation organisation's website. However, experience shows that, to be useful, the flyer must be written in such a way that clearly shows the projected applications and benefits that the IP could deliver if developed. It should also attempt to give specific ideas of the economic benefits to particular products or firms. This can be quite difficult to construct but is worth spending time on, since a description about the IP itself is not usually what potential licensees are interested in reading. They will be much more captivated by "user" language than by a mini thesis on the idea/invention.

The majority of successful licence marketing exercises are where there have been highly targeted marketing techniques applied by the licensor and where there has been a high understanding by the licensor of the likely economic benefits of its licence offering to particular firms. The executives in firms are sometimes just so busy with their existing business issues and demands upon their time, that unless proposals are extremely relevant and “hit the mark”, they just will not get airtime.

Accordingly, the approach from the prospective licensor must quickly establish where the licence would fit in the licensee’s business e.g. the appropriate division or product range, and clarify the business benefits to the licensee. Where licensing is a particularly common and well-established means of acquiring technologies e.g. in the pharmaceutical industry, considerable knowledge of the licensee’s business, together with the correct identification of the individuals responsible for licensing in, will be expected. Although many licences arise from active prospecting by firms themselves (i.e. demand-led), this can be hit-and-miss from your point-of-view. Many large firms will usually concentrate their efforts and prospecting on research institutions where they already have other substantial relationships (e.g. strategic partnerships) or where they have had previous successful experience of licensing-in from those institutions. This is because even the largest international firms have limited resources when it comes to hunting for IP in every research institution. So they have to select and focus on some to a certain extent. Some companies do employ dedicated professionals whose main or only job it is to bring in new and exciting IP. You should ask your IP commercialisation team members (or the agency they may be using) to let you know which firms have these licensing-in executives.

Small and medium-sized enterprises (SMEs) are also ideal potential licensees because of their requirement to innovate frequently but these SMEs are difficult to identify in the first place and will not be as familiar with licensing as a way of developing their business, as much as the more well-known and larger firms. Hence an excellent network will be necessary to achieve a good short-list of both large companies and SMEs to be approached. Licensing-out can be affected by industry cycles. For example, when firms, who rely on a strong patent portfolio to protect their products/sales, find that their patents are soon to expire, they tend to be more active in prospecting for external IP and more open/receptive to licensing-in. It is good to be aware of this as it may coincide with your exploitation of your IP. Your IP commercialisation organisation will be able to give you an idea of these industry trends.

You will benefit from practising for effective presentations in the pre-deal phase. Your IP commercialisation team will be familiar with how to present in licence proposal situations and can both advise you, as well as rehearse with you as part of a co-ordinated team approach/presentation. This type of preparation is very important and will enhance credibility and therefore the chances of capturing serious interest and attention.

Agreeing terms

This will obviously be the result of a negotiation. In general, it is best to develop the discussion about the terms over time through a series of sessions, rather than in one or two formal bargaining events over the table. It is usually best to see the licence arrangement for what it is – which is a risk-sharing partnership, rather than a “them-and-us” situation.

Whether you are planning to license to a large firm or an SME, it is sure to be the case that the potential licensee will have a great deal of experience in the development and marketing of products and services and will have a good feel for the time and effort that it will have to put into taking your IP to market. In addition, it can also be a hugely costly affair to transform raw or even partially developed IP into goods, process improvements or services. Hence the potential licensee will need to debate with you the business case, in order to share with you its specific experience and inputs. Through such a process, it should become more apparent to you and the potential licensee what the cost-benefit parameters are of agreeing a deal.

Thus the “best” deals and licence contracts generated from research institution offerings, are those that arise out of a good relationship and understanding, not usually out of adopting a tough negotiating stance. It is a matter of finding the right balance between deriving fair reward for the actual contribution that your IP will eventually contribute to commercial success and the incentive and value to the licensee in spending the time and the risk on the IP.

Negotiation is definitely an art which does require a lot of experience so that all requests and discussions are credible. So this is where you should make use of and have a good understanding with your IP commercialisation

organisation, to ensure that you have an understanding of the terms which should be arrived at. Your IP commercialisation organisation will have been involved in many negotiations and probably be members of the Licensing Executives Society from where additional expertise and support data can be drawn. You will, therefore, benefit from their early involvement.

In general, the negotiation discussions will begin with a focus on business issues and will end by becoming largely legal. In between there may be one or more diversions into the underlying technology. Certainly at some point you should bring in legal advisers. The lawyers will take on an increasing role as discussions progress and the final details will be settled almost entirely by them, but it is important to recognise that you and/or your commercialisation organisation will be expected to take the lead on business issues (including most importantly the financial terms).

You do not want to undervalue your IP and there are a number of specialist IP transfer agencies and independent consultants who can assist.

These work in different ways, but by sharing the potential returns with them, they will be able to give an objective view of the value of the IP in use and also undertake the marketing and negotiations in partnership with you and your institution's IP team or on your institution's behalf.

A deal that is linked to the sales revenue of a firm is usually a good way to start, even if the IP relates to a process rather than a product or service, because that way each party shares when both parties are actually receiving income. The trick is to get the right formula and the right protections! Section 6 gives some suggestions and typical things to look for and benchmarks, and provides a few negotiating tips – all of which are aimed at making you more familiar with the terminology. It will also allow you to be more knowledgeable when you are involved in such discussions with your own IP commercialisation team, as well as when involved in their meetings with the potential licensee. It will also give you some idea of what you should be checking (areas that your IP advisers will be covering in discussions) and as a checklist when you see any draft agreements materialising.

There are a great many issues that need to be finalised when negotiating a licence (as you will see from the size of the final licence agreement!). The main issues to be resolved are:

- purpose
- territory
- field of use
- type of licence (exclusive, sole, non-exclusive).

These and other issues are discussed in detail later.

MUSIC TO A POTENTIAL LICENSEE'S EARS

- We have proprietary and registered IP of direct relevance to your firm.
- We have proved that the principle works in a number of environments/conditions.
- We have constructed a clear business case as to how the IP can benefit your firm.
- We are in a position to present and demonstrate the IP to you at your earliest convenience, including having a comprehensive confidential package of know-how and performance data to support it.
- We have an excellent track-record of licensing-out from our research institution and we engage professional IP advisers appropriately to relate directly to your own legal advisers.
- We can offer appropriate research support (for which we may be able to obtain grant funding) and consultancy until your firm has fully adopted the IP and for a relevant time following that.

There are three main types of licence which can be granted – an exclusive licence, a sole licence or a non-exclusive licence. Your decision as to which type of licence to grant will depend on the degree of freedom you want to offer and the rights of use you also want to retain.

Taking the example of the on-line ‘IP management’ training package referred to earlier. If you are looking to license this package to Company X, the different options are as follows:

Exclusive Licence	Sole Licence	Non-Exclusive Licence
If you grant Company X an exclusive licence to use the package, this means that only Company X can use the package. You would not be able to use the package (even for research), neither would you be able to license anyone else to use the package.	If you grant Company X a sole licence to use the package, this means that Company X can use the package and you would be able to use it, however, you would not be able to license anyone else to use the package.	If you grant Company X a non-exclusive licence to use the package, this would mean that you would be free to use the package yourself and you would also be free to license anyone else to use the package, in addition to Company X’s right to use.

Reasons why you may want to grant an exclusive licence?

- If you do not have the resources to commercialise your IP as you would wish to do, and other than the party to whom you wish to grant a licence, there are no other market players who have the capacity or that other party would not invest in commercialising the IP without exclusivity.
- You or your institution does not require use of the IP and you would be happy to lose a fair degree of control over the IP.
- You would like to maximise your return from that licensee.

Reasons why you may want to grant a sole licence?

- You do not have the capacity, be it financial or technical, to commercialise the IP alone, but you want to retain the ability to also use the IP. (This can also be done through an exclusive licence in which the exclusive licensee grants you back a non-exclusive licence).
- You still want to retain a certain level of control over the IP.
- There are no other market players who would be suitable to work with or the licensee would not invest in commercialising the IP if there were other licensees.

Reasons why you may want to grant a non-exclusive licence?

- There is more than one party capable of commercialising the IP.
- If you are unsure whether the first party to whom you are licensing is in fact the best option.
- You need complete freedom to grant licences to whomever you wish.
- If the IP does not need further development and is in a readily usable form, for example, a piece of software, a CD Rom or an on-line package.
- If you are unsure about the potential value of the IP and what can be done with it, you may want to offer the opportunity to a number of players to evaluate and work with the IP.

If you are granting an exclusive or sole licence you will definitely want some obligations on the licensee actually to commercialise the IP. Ideally this would be through some minimum sales provisions (see Section 6 – Payment Provisions). If you have granted an exclusive or sole licence, you might include a provision whereby if minimum sales figures have not been paid or targets are not reached then the licence becomes non-exclusive.

Q. Does a licence have to be in writing?

A. Whilst it is not essential for all types of licence to be in writing, it is always advisable to put them in writing so that the nature and extent of the rights which have been granted are clear. It is far easier to point to a provision which is written in black and white than rely on something you have said during a conversation. If there is ever a dispute in the future, it could end up with one word against another.

Let's now take a look in more detail at the specific provisions you would want your licence agreement to contain. Set out below is an example of the structure of a typical licence agreement. You may want to refer to this as to see how the provisions discussed below usually fit in sequence and to get some more tips. Your institution's commercialisation team will have template licence agreements, so you could also request a copy of one of those if you want more details.

Example of Licence Structure

PARTIES

- Ensure the Licensor(s) and Licensee are correctly identified, with company numbers, where companies.

BACKGROUND

- Set the scene of how the IP was created; how the IP is being licensed and for what purpose.

OPERATIVE PROVISIONS

1. DEFINITIONS

Insert definitions to make the contract more user friendly. In particular, ensure you properly define the Technology, Field of Use, Territory and Royalties!

2. GRANT OF LICENCE

- The Licensor grants to the Licensee a(n) [exclusive/sole/non-exclusive] licence of the IP.
- Ensure you draft the licence narrowly if it is only for one product, or in restricted fields or territory.
- Is it sub-licensable? You must grant the right to sub-license manufacture, if the Licensee is not manufacturing itself.

3. KNOW-HOW

- Include here how and when any know-how or technical information will be transferred to the Licensee.
- Include details of any training to be given, including costs.

4. IMPROVEMENTS

- How will improvements be disclosed?
- Will they form part of main licence or be subject to a separate licence?
- Licensee's improvements – assignment/licence to Licensor?

5. CONFIDENTIALITY

- You will be disclosing some information which is only protected by confidentiality. Ensure appropriate confidentiality provisions are in place.

6. PAYMENTS

Include:

- Upfront payment (recoupable or not against royalties)
- Royalties – net sales value or per service provided
- Ensure sub-licensees are caught by provisions
- Minimum royalties and what happens if not reached?
- When and how are royalties to be paid?
- Interest on late payment provisions.

7. ACCOUNTS

- Accounts of transactions relating to licensed technology to be kept.
- Statements to be delivered with royalty payment.
- Access to records for Licensor's accountants.

8. LICENSEE'S OBLIGATIONS

- Is it to maintain patents?
- Place patent/copyright notices on Products.
- Maintain quality of Products.
- Are there any marketing requirements?

9. INFRINGEMENT

- Who has right to take infringement action?
- Each party to assist the other where the other is taking/or defending the claim.
- Who has the right to claim damages?

10. TERM AND TERMINATION

- How long will agreement last?
- How can it be terminated?

11. CONSEQUENCES OF TERMINATION

- What happens to IP/Technology on termination e.g. return documents/tooling to Licensor?
- Any right to sell-off.

12. LIABILITY

Licensee should be liable for sale of its products/provision of services incorporating licensed IP. Include an indemnity from the Licensee for this.

13. MISCELLANEOUS

Cover here, which law governs the contract; how changes can be made; whether the contract is assignable.

14. SIGNATURES

Make sure it is signed by people AUTHORISED to sign and bind each party.

Specific Licence Provisions

Parties

Always make sure it is clear who is entering into the licence. Check the licence is between the right parties. There is no point in drafting a licence from yourself to another party when, in fact, it is your institution which owns the IP in question. Always fill out full names and addresses. In the case of a company, include the company's registration number and registered office. This can easily be found on Companies House website www.companieshouse.gov.uk, through the WebCheck facility.

Remember, the party which owns the IP and is permitting another to use it is referred to as the **Licensor**. The party to whom the licence is being granted is referred to as the **Licensee**.

LICENSOR → IP → LICENSEE

Run some checks?

You probably would not think about letting your house or flat out before meeting your tenant or at least running some checks to make sure they are likely to pay you and for example do not have a criminal record. Why should you treat your IP any differently? Try to make some preliminary investigations into your potential licensee. In particular, if you will be relying on your licensee to commercialise your IP – check their track record – are they good at it? What is their reputation like? Is it likely they will be able to pay you? Check whether your licensee has any winding up petitions filed against it. This is an indication they have had or are having financial problems.

Background

You may see a “Background” section at the beginning of a licence agreement. This is just a way of setting the scene and briefly describes the purpose of the licence. Try not to include any definitions or specific provisions in this section – these should be in the main body of the licence.

Scope

What rights am I licensing?

You must always specify exactly what you are permitting your licensee to use. If you are licensing the rights to use copyright, such as a piece of written work or software, it is common to refer to this as the “*Works*”. If you are licensing the rights to use a particular piece of technology, certain know-how, a piece of equipment or a model or prototype – this is often referred to as the “*Technology*” or the “*Licensed Technology*”.

In all cases it is important that you describe the IP which you are licensing in as much detail as possible. You can do this in a schedule to the licence agreement by describing the IP, referring to laboratory notebooks which contain the information, or even abstracts. Where you are licensing a registered patent, a design, or a trade mark, refer to the registration details or, if it has not yet been registered, the application details. For example:

Patent No.	Country	Priority Date	Registration Date	Title
5688384	UK	02/07/00	02/07/04	Remote sensor tracking device

Unlike a patent, for instance, you can divide copyright up and just license part of it. You can license one publisher in relation to digital rights and another for non-digital; one publisher for hardback rights and another for softback; one publisher for English language rights and another for French language rights.

There are several ways to license software. Often the licensor of the software may want to limit the licensee's use of the software. For example, the licence may only grant access to the object code and provide that the software must not be altered or modified without the licensor's consent. However, if you wish to ensure as wide a distribution as possible for your software and you wish to allow users greater freedom to contribute to the functionality of the software, an open source licence of the software may be appropriate.

Open source software (OSS) is provided under a licence which allows the source code to be copied, modified and redistributed. There are many different types of OSS licence. The most widely used is the General Public Licence (GPL) which is developed and maintained by the Free Software Foundation. Generally, the GPL allows a user to copy, modify and redistribute the program. However, if it is redistributed, the source code or an offer to provide the source code, must be distributed with the object code.

There are other licences which impose fewer conditions than the GPL. For example, the BSD licence is shorter and more flexible than the GPL and grants wide rights to redistribute and use the software. For more information visit www.opensource.org. As OSS licensing is complex, you should always seek specialist advice before entering into any such licence.

If you are only licensing the object code of software your licensee may ask you to enter into an Escrow Agreement. This is an agreement with a third party known as an Escrow Agent: there are several specialist companies which act as Escrow Agents. It means that you lodge a copy of your source code with the Escrow Agent on the basis that the source code will only be released to your licensee in specific circumstances e.g. if you or your institution becomes insolvent or fails to maintain the software.

What can the licensee do with the licensed IP?

You must clearly specify exactly what the licensee is permitted to do with the licensed IP. Be careful not to offer the licensee too much freedom if it is not in fact necessary. There are various ways you can limit the scope of the licence you are granting. These are illustrated in Figure 3.

Figure 3

“Purpose”	<p>You can limit the licence to a particular ‘purpose’. For example, if the licensee is only interested in using your technology for the purposes of manufacturing a certain Product – specify that the licence is granted “solely for the purposes of manufacturing Product X”.</p> <p>If the licensee wants to develop the IP further and also manufacture Product X – specify that the licence is granted “for the purposes of further research and the manufacture of Product X”.</p>
“Territory”	<p>If necessary you can also limit the licence to a specific territory. For example, if the licensee only needs to use the IP in the UK – specify this. This will mean that you could, if you wanted to, license the same IP to others for use in countries outside the UK. Do not use generic terms such as “Europe” as that will create a debate about whether countries, such as Turkey, are in or out of Europe. If you want to define your Territory as the European Union specify it is the EU as at the date of the licence – other countries may join subsequently.</p>
“Field of Use”	<p>It may be appropriate to limit the licence to a particular field of use. For example, if the licensee is using your IP only for research in the field of aeronautical research – specify that this is the case. Again, this will offer you the freedom, should you want to, to license the same IP to others in other fields of research, such as medical devices.</p>

Example:

By using these principles, you can tailor this very wide licence:

“The Licensor grants to the Licensee an exclusive licence to use the Licensed Technology”

to this more specific licence:

“The Licensor grants to the Licensee an exclusive licence to use the Licensed Technology solely within the Field of Use to manufacture the Licensed Products within the Territory”

Don't put all your eggs in one basket!

You do not have to limit yourself to one licensee for the same IP. You would be taking a risk if you totally rely on one single party to commercialise your IP successfully in all ways and in all markets. What if things go wrong? What if your licensee turns out not to be as experienced or committed as you had originally thought? Even if you are thinking of granting a third party an exclusive licence of your IP, you can see from the previous example that there are ways in which you can tailor the licence to only that which is needed. This will leave you with other options in respect of the same IP in different areas.

Dr. Genius has a patent for a process which can be used to enable self-analysis of blood glucose levels. Under cover of confidentiality agreements, he has been negotiating with two parties, Dial Drug Limited and Sugar Free plc with a view to licensing the patent to either of them. Through negotiation it has emerged that Dial Drug Limited wishes to use the patent to manufacture a product which will allow diabetics to carry out self-analysis of their blood glucose levels whereas Sugar Free Limited wishes to use the patent to manufacture and sell a product which can be used to monitor the sugar content in juice drinks for babies and toddlers.

As both interested parties will be operating in differing sectors (one in the medical sector and the other in the food sector), Dr. Genius could grant an exclusive licence to both parties in different fields of use. By doing this, Dr. Genius will have created a greater opportunity to maximise the money to be made from the IP and will not have to rely on the success of just one avenue of commercialisation. If it becomes apparent that the IP can be used for purposes other than those proposed by Dial Drug Limited and Sugar Free Limited, Dr. Genius could exploit these in the future.

Here are some tips on how to make the most of the rights you are licensing:

Scenario: Your licensee is keen to obtain an exclusive licence on a worldwide basis. You are not sure that your licensee has the capacity or the experience to commercialise on a worldwide basis.

Suggestion: You could provide your licensee with exclusive rights in a more limited territory where you are confident the licensee will be successful. As it is possible to offer both exclusive and non-exclusive rights in the same agreement you could then offer non-exclusive rights in a wider geographical area (although this would restrict you from offering exclusive rights to a third party in these territories). A further possibility would be to offer your licensee an option or right of first refusal in respect of additional territories, as and when the licensee is able to make a convincing business case to you that it has the capacity to enter into those further markets.

Scenario: Your licensee is keen to obtain an exclusive licence in a particular Field. You are not sure that your licensee has the capacity or the experience in that Field.

Suggestion: You could provide your licensee with a non-exclusive or a sole licence in that Field for a limited period of time. If your licensee is able to demonstrate to your satisfaction a certain level of achievement or commitment within the time allowed you could then convert the licence to exclusive terms.

Sub-licensing

A sub-licence is a licence which is subsequently granted by the licensee as opposed to the licensor. It is a bit like a tenant sub-letting your flat or house to someone else. You will need to specify in a licence whether or not the licensee is permitted to sub-licence the rights which it has been granted.

Why might I want my licensee to have the ability to sub-licence?

- If you think that your IP will become more valuable by your licensee appointing third parties to assist, you may want to consider allowing your licensee the right to sub-licence.
- If, for example, your licensee has a licence to use your IP to manufacture certain products – your licensee may need to sub-contract certain manufacturing tasks. The licensee will need to sub-licence its sub-contractor the right to use the IP for the manufacturing tasks.
- Your licensee may be part of a group of companies and want its group companies to assist it. They will need a sub-licence.
- If you are keen that only your licensee has the ability to use the IP and you would prefer to retain better control over your IP and be certain who is using it – you may prefer to prevent the ability to sub-licence.



TOP TIP

It is possible to include the ability to sub-license, but only on the basis that your licensee first notifies you and obtains your approval. You may also want to approve the terms of the sub-licence which is being offered. This way, at least you have the opportunity to 'vet' the party who will also be using your IP and you are kept fully in the loop.

If you do decide that your licensee can appoint its own licensees of your IP, you should ensure that the licensee remains liable to account for all payments, whether they accrue on the licensee's or its sub-licensees' commercialisation of your IP. You should make clear on what terms your licensee can sub-license – these would usually be terms which are identical to your licence (called the head licence) except for the right to sub-license.

Clearly an important aim of the licence is to see some money in return. It is therefore important to make sure you get the payment provisions right.

What happens if payment provisions are not included in the licence agreement?

Be aware that, if your licence agreement does not:

- fix a price; or
- specify a method of calculating the price; or
- the price cannot be determined by previous dealings between the parties, it may be implied that a “reasonable” charge was intended to be fixed.

You do not want to get into a position where you and your licensee are arguing about what a reasonable charge is, therefore it is best to include express payment provisions in the agreement. Avoid including provisions that state that the parties will agree the price at a later date. “Agreements to agree” are unenforceable under English law and in some other countries.

Payment Terms

What are the most common methods of payment found in a licence?

Royalties

The most common form of payment for licensed IP is a royalty. The term royalty tends to mean regular payments which typically may vary according to the number of products manufactured, used or sold, or the number of times a process is applied (depending on the type of rights you have licensed out). However, the term can also be used to describe payments which are more of a capital nature, for example “lump sum”, “up-front”, “stage” or “annual” payments.

It is illegal to fix the price at which your buyer sells its products. In the same way you must not fix the minimum price at which a licensee sells licensed products. Only the rate at which royalties will be charged, or the method of calculation for the royalties, can be specified. Specifying the price for selling the licensed goods may be deemed to be price fixing and this may cause you problems under competition law. Always check with your IP commercialisation organisation or specialist lawyers if you are at all unsure.

Up-Front Payments

In addition to or instead of a royalty you may want to ask for an “up-front” or “lump sum” payment upon signature of the licence. Up-front payments are commonly found in a licence of software. In Publishing Agreements they are called “Advances”. They are also useful if a licensor requires some immediate cash flow – perhaps to support further or reimburse past research costs. It may be more difficult to convince a licensee that an up-front payment should be paid when licensing other forms of IP, especially if the licensee is likely to have other initial investment costs and expenses. It is entirely appropriate to ask for this as an additional payment, although firms will often resist this or wish to set the sum against the early royalty payments (i.e. they will deduct it from those future payments which will be due to the institution). Let’s look at a couple of examples of circumstances in which you may be able to obtain an up-front payment.

Professor Smart has agreed to grant Paradox Limited an exclusive licence of patents and know-how for use in the manufacture and sale of a filtration tool in the United Kingdom. Professor Smart has previously granted a similar exclusive licence to Magnetix Limited (which has now expired). Magnetix had great success with the filtration tool and it is clear that there is a ready market for it, especially as there is no other tool like it on the market. Professor Smart may be able to demand an up-front payment and argue that this represents the price Paradox must pay for access to rights which have proven to be commercially successful and provide a competitive advantage.

Dr Dexter has patented a novel technique of protein analysis which is more straightforward and significantly quicker than any other. Dr Dexter is thinking of granting NewChem Limited a sole licence to use the patent in the EU (as configured at 1 Sept 2007) for the purposes of developing a product it is looking to take to market. Dr Dexter could argue that an up-front payment is justifiable on the basis that it reflects the considerable amount of R&D investment time and money NewChem Limited has saved.

Stage Payments/Milestone Payments

Another option you may wish to consider is requesting payments at certain stages. This is useful if your licensee is going to be carrying out further research and development or marketing under the licence, and the licensed rights are only going to reap benefits at certain stages. A payment can be triggered at each stage. It may be that during development certain regulatory milestones have to be met. A payment could be requested upon passing each milestone.

Mary has developed a novel, patentable technique for assessing levels of cholesterol. She has discussed this with ABC Limited under a confidentiality agreement and is going to grant ABC Limited a sole licence to use her technique to develop a cholesterol gauging product for the UK market. Mary has filed a UK patent application. Mary has demanded that payments under the licence be made in stages, with the payments rising when the patent application has moved into its international stage and in regular stages after that until the patent has been granted. As the patent proceeds to grant – the technology will increase in value. The payments will reflect the diminishing risk associated with the project for ABC Limited and the reward for Mary for the growing success of her technology.



Negotiation Tip

If you are in need of initial or stage payments to help cash flow, you may be able to persuade a licensee to make such payments more easily if they can be “set off” in some form against the royalties to be paid in the future based on sales. It is possible for royalties to be set off against all or only part of any initial or stage payment made.

How are royalties calculated?

Royalty Base

You must also consider the basis on which royalties will be charged. This will depend on the nature of the rights you are granting and the context in which your licensee will exercise those rights.

If your IP represents an identifiable product or is required to manufacture a product, it may be appropriate to charge a percentage of the price each product is sold for. If your IP represents a process or a technique, you may instead prefer to charge a fixed amount for each time that process or technique is used, although this may be difficult to monitor. In the case of a patent licence, a percentage of the sales price of any product which falls within a valid claim of the patent may be appropriate. If the licence relates solely to know-how – a percentage of the sales price of products, which incorporate or whose development has made use of the know-how, would be better.

With software, royalties can be charged on a 'per user' or 'per machine' basis. However, it is common for an annual fee to be charged or a mix of the two.

Colin has developed a chemical formula which can be used to manufacture, amongst other things, long-lasting, chip-proof nail varnish, a product for which there is much demand according to market research carried out by Hi Tech Make Up Limited. Colin has started to negotiate with Hi Tech and is going to grant Hi Tech a licence to use the formula to manufacture nail varnish products. As this is a straightforward case in which the licensed rights will produce a readily saleable product, a suitable royalty base would be an agreed percentage of the net sales value of each bottle of nail varnish which has been made with the formula.

The Calculation

Once you have worked out the basis on which royalties will be charged, it is advisable to set out the method you are going to use to calculate them. You may ask for a percentage of the "gross" sales price. This means that the percentage will be taken from the full sales price, before any value added tax has been deducted. A licensee is likely to resist this and will want tax deducted before any percentage is calculated. It is therefore more common to see "net sales" referred to in a licence. It is often tempting to define a royalty merely as a percentage of "net sales", however this often requires further definition. Figure 4 illustrates a series of questions you will need to bear in mind when drafting.

Figure 4

Question	Answer
<p>How should VAT or other sales tax or duties be factored into the price?</p>	<p>It is usual for the percentage royalty to be calculated from the sales price once VAT or other sales taxes or duties have been deducted.</p>
<p>How will the licensee’s costs for carriage, insurance, delivery, packing etc. be dealt with?</p>	<p>If your licensee has to pay for the costs associated with delivering products to its customers, insurance or other associated charges, it is likely that your licensee will want to first deduct these costs from the sales price before the percentage royalty is calculated. You should resist this. Sometimes these are stated only to be deductible if they are separately set out on your licensee’s sales invoice to its customer.</p> <p>Remember – the more deductions you allow your licensee to make – the less royalty you will receive.</p>
<p>What happens if the licensee never actually receives payment from its customer?</p>	<p>Ideally, as a licensor, you will want to specify that a royalty is payable on the amount which is invoiced by the licensee. This means that if the licensee is not paid by the customer you will still receive your percentage. Your licensee is likely to resist this provision and will want to only pay a percentage on the amounts it actually receives from its customer.</p>



Negotiation Tip If your licensee is resistant to calculation from amounts invoiced, you could argue that whether or not the licensee recovers payment from its customers is a matter for your licensee’s credit control. You should not have to rely on whether or not this process is adequate. Another option to help your cash flow is to give credit if there are bad debts but not just if the licensee’s customer is a slow payer.

What happens if the royalty is a percentage of a price and your licensee sells at a price lower than it should?

It is possible that your licensee may sell certain products to its group of companies or even contacts/friends within the industry at a price lower than the proper market price. If you are receiving a percentage royalty you will not want to lose out if this is the case.



Negotiation Tip It is possible to include a provision which states that – should any product be sold other than on arm's length terms, the true market value shall be substituted and used for the purposes of calculating the percentage royalty due back to the licensor.

You could also address this by getting a fixed sum on the sale of each product. Remember to get the right to increase this fixed sum by reference to an index if the licence is long.

What happens if the licensee has the right to sub-license?

If this is the case, make sure that it is clear that the royalty is on sales made by the licensee and also on sales made by its sub-licensees.

Make sure it is clear whether royalties on sales by any sub-licensee should be paid directly to you or via your licensee.

What if the IP being licensed is actually a process which will be used by the licensee?

In these cases it may be more appropriate to charge a fixed amount for every time the licensee uses the process. Alternatively, you can ask for a percentage royalty on every product which is sold by the licensee having used the process to manufacture that product, but think about how you will monitor this.

What happens if the licensee decides to hire/lease its products as opposed to selling them?

In these cases, you can include a provision which states that – should any product be leased or otherwise disposed of, the price that would have been charged if the product had been sold, will be used for the purposes of calculating the royalty.

How do I know what percentage royalty to ask for?

What percentage royalty is normal? Well, this is not that easy to answer as it will depend on a whole range of factors. In some of the media industries, such as music, rates are fairly standardised. More typically elsewhere, rates can have a very wide range. However, there are no hard and fast rules for determining an exact figure. One of the most common rules of thumb for patent licensing is the “25% Rule”. This says that the licensee pays a royalty equivalent to 25% of its expected profits for the product that incorporates the patent. It is only a rule of thumb!

The final figure will depend upon, amongst other things, the type of IP, its ‘shelf-life’, its value and – how much your licensee wants it! Figure 5 illustrates a list of the factors which may be taken into account when making a decision. This may also be useful should you ever need to argue why the rate you have requested is not too high!

Figure 5

Factor	Explanation
Anticipated commercial benefits of the licensed IP	If there is a strong chance your IP is likely to be successful and it is the only option your licensee really has – you should be in a fairly strong position to request a higher percentage.

Relevant industry norms	<p>Consider the type of IP you are licensing and what this has commonly been licensed for in the past. For example, the norm for the chemical and electronics industry tends to be a little higher than for consumer products. The pharmaceutical industry tends to be one of the highest. Your IP commercialisation office will have examples.</p> <p>If you ask for a percentage far higher than what you would expect based on the relevant industry norm – you may have to argue on what other basis the higher percentage has been requested.</p>
Degree of exclusivity granted	<p>If your licensee is obtaining an exclusive licence, this will be more attractive than a non-exclusive licence and a higher percentage will be justified.</p>
Strength of the licensed rights	<p>The stronger your IP (e.g. if your IP is registered or if your IP is particularly complex or has involved a high degree of development) the higher the percentage you may be able to justify.</p>
Amount of further investment required to bring the licensed product to the market	<p>It is quite common for the IP which you are licensing to be in a relatively early stage of development. If this is the case, it could take some time (often years) before your licensee is able to take it to market and see any financial return. Your licensee may still have to spend some considerable investment time and money on the IP in order to develop it fully to a marketable form. The more time and money your licensee is required to spend on the IP – the lower the percentage royalty your licensee is going to want to pay.</p>

Degree of competition/ availability of other technologies	<p>If your licensee has a number of options other than your IP, you will need to be careful not to charge a royalty which is too high and causes your licensee to go elsewhere for a cheaper option.</p> <p>On the other hand, if your licensee is restricted to your IP as its only or most preferred option – this will put you in a better position to ask for a higher royalty.</p>
Inherent risk	<p>You will need to consider the likelihood of any circumstances arising which could prevent or hinder the success of your IP. If, for example, there is a strong chance your patent may not proceed to grant, some regulatory approval e.g. for a pharmaceutical, may not be obtained, or there is a strong chance your IP will not be received well in the market, then it may be harder to justify a higher percentage.</p>

Should the percentage stay the same for the duration of the licence?

Indexation

It is a risky ploy going for a fixed royalty rate for the duration of the licence as this rate may only reflect the position of the market in the early stages of the licence or if it is a fixed amount it may be eroded by inflation. How do you take any inflationary factors into account? Well, to do this you can provide for an automatic review of the royalty rate by reference to a suitable index. This can take place at regular stages of the licence – usually annually. The General Index of Retail Prices is probably the most commonly used index in the UK, but may not be appropriate to all scenarios.

Royalty Reductions

Your licensee may want to include a provision in the licence which will ensure that the royalty reduces if the licence becomes less useful/attractive for some reason. Figure 6 gives some examples of the kind of circumstances where this might arise.

Figure 6

Why a reduction?

The licensed IP becomes outdated or is overtaken by another model or version on the market.

This is quite common in the context of software.

Clearly, in these cases the value of your IP will diminish if something else 'better' comes on the market. The licensee may want this reflected in the royalty if this does occur.

It is not possible to obtain protection for the licensed IP in a particular territory.

For example, if you are licensing a patent in a number of different countries and that patent fails to proceed to grant in one country. The strength of the IP will diminish in that country on the basis that, without the protection of the patent, a third party could develop and use the same technology to compete with your licensee in that country without risk of infringing, as you have no patent there. The licensee may want to reduce the royalty or pay no royalty for sales in that country, if this occurs.

The licensed IP has been infringed and it is not practical (for example, too expensive) to seek a legal resolution.

If there is someone else using your IP in the market and you are not in a position to stop them – they will then become competition for your licensee. The licensee may want to reduce the royalty or not pay a royalty on the basis of this unwanted competition.

The payment of the current royalties means that the product is not competitive in terms of price.

This may be relevant if you have charged a fixed royalty. If, for example, you have charged £2 per item sold by your licensee and interest in the market falls to such a degree that your licensee is only able to obtain £3 for each item – your licensee may want the opportunity to reduce the royalty to ensure it receives a fair level of profit from its sales.



Negotiation Tip

If your licensee is pushing to have this kind of provision in the licence you may want to ensure that the royalty will only be reduced if the drop in market interest is through no fault of your licensee.

Variable Royalties

You may want to include some form of sliding scale (increasing or decreasing) for royalties dependent on, for example, the quantities of products sold or the number of processes used. For instance, if sales reach certain relatively high levels, then the royalty rate payable reduces.

By doing this, you will provide an incentive to the licensee to maximise its sales or increase its initial investment.

If you are in a particularly strong bargaining position, you may want to impose a minimum royalty level. This means that if your licensee does not pay a certain amount of royalties in a period of time (usually one year) then the licensee would have to pay the difference between the royalties it has paid and the minimum level. It is also possible to include other consequences if the minimum level is not met – such as terminating the licence or substituting a non-exclusive licence for an exclusive licence.



Negotiation Tip

If you are struggling to obtain the royalty percentage you want – you may be able to negotiate a higher amount on the basis that a sliding scale is introduced and it will reduce upon achievement of certain volumes/milestones.

Royalty Stacking

In some cases your licensee may be selling a product, which not only incorporates the IP licensed from you, but also a number of other components licensed from others. If a particular product has so many licensed-in components, there may come a point at which the profit margin for the product is so eroded that it is no longer economically viable. It is common in these situations to see a maximum overall royalty level set which, when reached, triggers a reduction pro rata across all the royalty-bearing components.

Accounts and Records

Bank Details

Don't forget to put your bank details into the licence – the licensee needs to be clear when and to whom they are making the payments. Keep the flexibility for you to change it if you tell the licensee.

What if the licensee pays late?

You may want to include a provision which states that interest will be payable on late payments. A common percentage usually agreed upon is around 4% above the base rate of your bank or LIBOR (London Inter-Bank Offered Rate). Alternatively, you can rely on rights under the Late Payment of Commercial Debts (Interest) Act 1998 which is 8% above the base rate of the Bank of England at the time of writing. This should act as a deterrent to ensure that the licensee does not fall behind with royalty payments and, if it has any sub-licensees, that such sub-licensees will not make any late payments either. However, it must represent a fair assessment of your expected loss and not be a penalty.

Currency Conversion

Remember that licences will often be international in nature and may involve currencies other than the pound and the Euro. Where royalties are calculated in a currency other than that in which they are to be paid, the question arises as to which party bears the risk of loss in currency conversion. A licensee in a strong bargaining position may insist a licensor should be satisfied with whatever is the spot rate of exchange offered by a nominated bank on, for example, the last day of each royalty period or the date of actual payment.

Complications can arise where exchange control regulations in a particular country make it difficult or impossible for a licensee to pay the requisite royalties. Unless you can impose an alternative payment mechanism, or it is possible for the royalties to be paid from elsewhere, you should seriously consider whether you should be entering into the agreement at all.

Withholding Tax

There may also be legal obligations in the country where the licensee is based to withhold tax from royalties before they are paid to you or your institution. There are treaties dealing with what is known as double taxation and so advice should be sought on this.

Monitoring

When putting together the payment provisions for your licence, you must also think about how you would want to be able to check that your licensee is complying with them and actually paying what is due. Figure 7 illustrates some suggestions.

Figure 7

Tip	
	Include reporting obligations on the part of the licensee. Ensure the licensee is obliged to provide details of all sales it makes (and possibly products manufactured) using the IP and how the royalty has been calculated – including appropriate break-down sales figures. This is often sent at the same time payment is made. You can ask for this on a monthly, quarterly or even annual basis. You can also specify that the licensee should produce any figures you may require upon request.
	Ask for a copy of an annual statement of sales certified by auditors and a set of annual accounts from the licensee.
	Include a provision which permits either you or your nominated accountant to inspect the licensee's (and possibly any sub-licensees') records and accounts, with a right to enter the licensee's (and sub-licensees') premises if necessary in order to do this.
	If, following your check of any figures, it transpires that the royalties which have been paid by the licensee to you are not enough – include a provision under which the licensee must pay the difference plus interest and possibly your costs of checking.

Training

It is possible that your licensee may require a helping hand to use or understand the IP for which it has taken a licence. If so, they may require further information, assistance or training from you. If this is the case you will want to make it clear to what extent you would be prepared to offer that further information or assistance.

If the licensee requires you or other members of your research group to travel to its premises to assist, you may want to impose a maximum period of time during which this would be possible. Otherwise, this could impact upon your own work and other commitments. In some circumstances you may want to charge for additional services on a consultancy basis. Think also about ensuring your licensee pays for any travel or out-of-pocket expenses. You will need to get the relevant permissions from your manager and institution to do so. Ensure under the licence you are limited to transferring and helping them understand, the know-how or the way in which the technology works. Any research requirements should be dealt with separately under a research development agreement.

Where your licensee simply requires further information – only agree to provide this upon reasonable request and to the extent you believe it is necessary for the purposes of the licence. Furthermore, make sure your licensee is obliged to keep any additional information confidential.

Improvements

What happens if you or your licensee amends or modifies your IP? This is commonly referred to as an “improvement”. Whether you or your licensee owns the improvements made will need to be considered in the licence.

Here are the main provisions you may need to consider in relation to improvements:

Improvement Provisions

Obligations on either or both parties to disclose to each other any improvements they may develop.



TOP TIP

Your licensee may try to include a provision which states that any improvements you make to the IP will automatically form part of the IP your licensee is licensed to use (pipeline). You should try to avoid this. A research institution exists to create improvements and so, whilst this may be a common provision in licences from companies, it is not in licences from research institutions. Should you then make any improvements, you can try to license these separately and extend your income stream. If your research institution is a charitable institution, it may have an obligation to obtain further payment for such improvements. You should avoid creating a pipeline.

Whether or not your licensee will own its own improvements to the IP.

If your licensee develops any improvement which changes your IP to such a degree that your licensee could actually use its improvement without infringing your IP – this is known as a “severable improvement”. Generally, obliging your licensee to either assign to you or exclusively license to you any severable improvement that it develops, is something that is prohibited under competition law. Always check with your IP commercialisation organisation representative if you are looking to include a provision of this nature.

To avoid encountering any problems under competition law – you should only request a non-exclusive licence from your licensee to use any of its severable improvements.

Any improvements which your licensee may develop which are not severable are commonly referred to as “non-severable improvements”. If your licensee insists on owning its non-severable improvements, you may want to ask for a licence to use them. Alternatively you may be able to request an assignment of those non-severable improvements and offer the licensee a licence to use them in return, without infringing competition law. Again, check with your IP commercialisation organisation.

Remember – provisions surrounding improvements can sometimes get a little tricky. Always contact your IP commercialisation organisation. Ensure you have the definition “improvements” drafted tightly to ensure wider research in the area of the licensed IP is not caught.

Maintenance

Who will be responsible for the maintenance of the licensed IP?

If you rented out your flat or house, the chances are your tenant would expect you to deal and pay for the maintenance and upkeep of the property. This would probably be set out in the tenancy agreement. In the same way, you will need to decide whether you want to be responsible for maintaining your IP, for example, paying any relevant IP renewal fees, or whether you want the obligation to fall on your licensee. Details need to be set out in the licence.

Beware – if you decide that you want your licensee to take responsibility, bear in mind that if it fails, for example, to renew a key registration, whilst you would be able to pursue it for breach of the licence agreement, it is unlikely you would be able to re-instate that registration.

Infringements

What can I do to protect my position if a third party infringes my licensed IP?

You will need to decide with your licensee who will take responsibility for challenging any third party which could be infringing the licensed IP. On the other hand, if you or your licensee is challenged by a third party for using the licensed IP you will need to decide how any defence proceedings would be dealt with. The party taking responsibility will usually be able to call on the other party to provide all necessary assistance. Although this can be costly, it is often better to keep control of any actions, particularly if you have several licences. It may therefore be worth looking at taking out IP insurance, but, be warned, it is not cheap!

Liability

Can I limit my liability if things go wrong?

You should try to ensure that you limit your liability to the maximum extent possible in relation to your licensee's use of the licensed IP. Wherever possible, seek an indemnity from the licensee against any claims by third parties against you arising from the licensee's use of the licensed IP, in particular product liability claims.

Remember that liability is a contentious area. The extent to which you will be able to limit your liability may ultimately depend on the strength of your bargaining position and the extent to which you are able to insure against any losses. There are also technical legal rules in this area. You should speak to your IP commercialisation organisation.

Katie is negotiating a mixed patent and know-how licence with VenGen Limited. VenGen Limited are demanding that Katie provides them with a warranty, backed up with an indemnity, that she is the owner of the relevant IP and has the right to license it. What should Katie do?

Before Katie gives any sort of warranty, she must be sure that she does indeed own the rights that she is licensing out. She should try to qualify the warranty that she gives by warranting that, only so far as she is aware, does she own the relevant rights. This protects Katie to the extent that if it emerged that someone who had assisted her (e.g. as a sub-contractor) in relation to the IP which forms the subject matter of the licence had merely copied someone else's work, Katie would not be liable under the warranty if she did not know about this. VenGen Limited will probably try to resist the inclusion of awareness in the warranty as it limits its remedies, but remember, in doubt, you must be careful about the extent of the warranty you give.

Duration and Termination

For how long should the licence last?

This really depends. The licence should be sufficiently long to allow the licensee to recover its costs of commercialising the IP exploiting the invention. However, a licence should not normally run beyond the period of protection for the relevant IP. For example, the duration of a patent licence will be, at most, for the maximum term of the patent. Note that a licence of a patent which extends beyond the term of protection of the licensed rights could in any event fall foul of competition law.

In music publishing agreements the duration may be by reference to the number of albums. The publisher will often have an option to extend the licence to cover one or more additional albums.

Can I terminate the licence prior to expiry of the term?

Yes – If you include the right in your licence agreement. Typical reasons for termination:

- breach of the licence
- if your licensee is insolvent
- if there is a change in control of the licensee and this results in the identity of the licensee changing to an entity with whom you or your institution does not wish to do business
- if the licensee fails to commercialise the licensed IP fully
- if the licensee claims that the IP is not valid

After termination

What happens after the licence has ended? The licensee has no further rights to use the licensed IP. Sometimes exceptions are made if the licensee has been producing products and has some product in stock to sell off or outstanding orders to meet. If the licensee has had confidential information you will want it to be returned or destroyed.

Applicable Law

What law should apply to the licence?

It depends – you should remember that licences are often international in nature. You may want the law of the legal jurisdiction where you might have to litigate. For national rights such as patents, you may want to choose the law where the particular patent is registered. Sometimes you will have no choice. If you license in some countries, you have to use their law; it is a complex area on which you should seek advice.

It is all too easy to think that just because a licence has been signed, it can be put in a drawer and forgotten about. Think again! Here are just a few of the issues you should bear in mind following completion of your licence:



If you have licensed a UK patent, you should register the licence at the Intellectual Property Office as soon as possible, but in any event within 6 months, following execution of the document. Why should you do this? Well, if you do not, third parties will not be bound by the licence unless they knew of the transaction. Also, you will not be able to claim remedies for infringements of the patent occurring before the licence was registered. There are similar rules for other registered IP.



Where different jurisdictions are involved, make sure that you find out what their requirements are regarding registration of licences – you should preferably do this before entering into the agreement.



Check you are getting the money that is due to you. You need to ensure that royalty payments are being made on time and that all accounts and records provisions are being complied with. This can be done by writing to the licensee frequently, say, every 6 months to find out the level of sales activity.



Check whether there are any obligations or restrictions contained within the licence agreement which you will need to make other colleagues or members of your department aware of to ensure they are complied with.



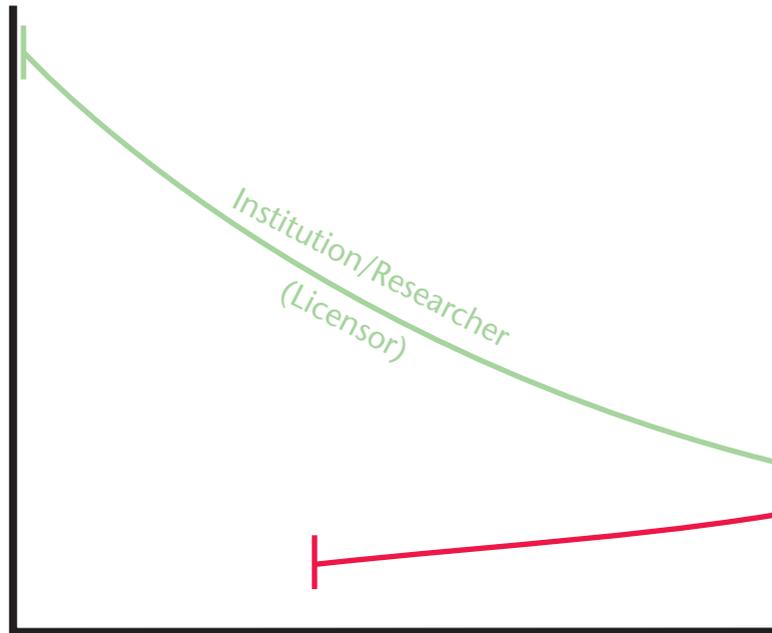
Keep a clear record of the IP which has been licensed out, particularly if on either an exclusive or sole basis. Remember – you cannot offer the same licence of this IP to anyone else.



TOP TIP

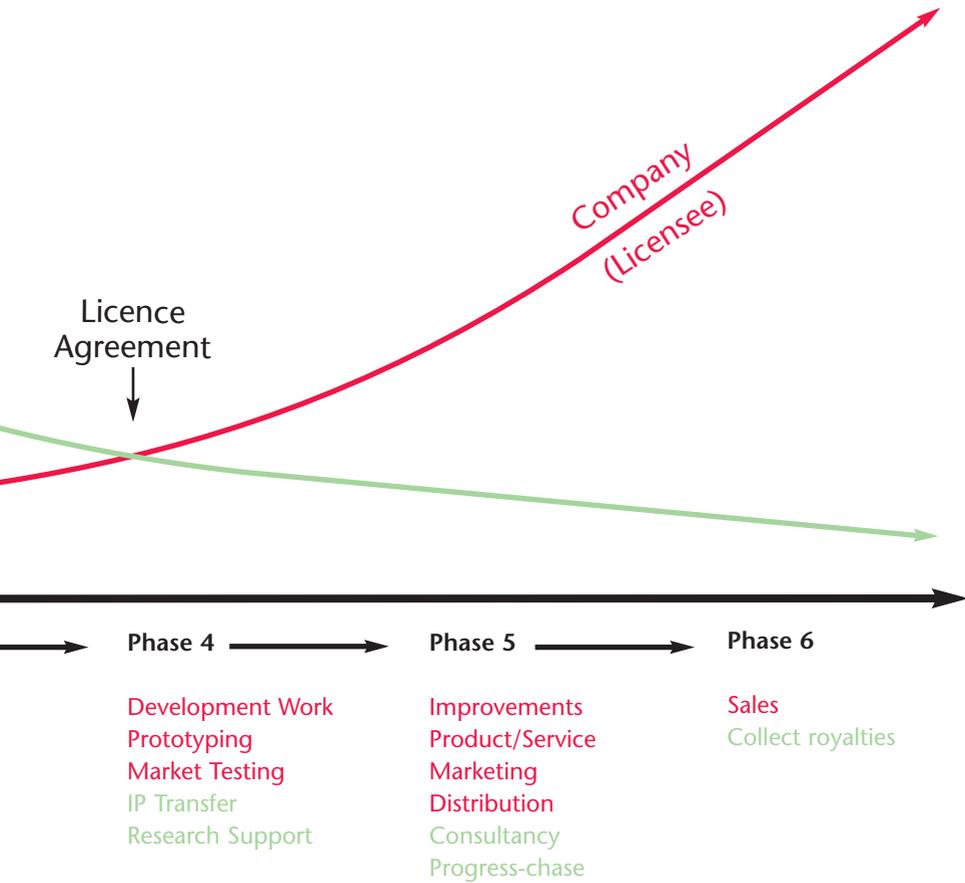
Once a licence has been signed – this does not mean that, if both parties agree, it cannot be changed in any way at a later date. If circumstances change and you feel you need to make any change to the licence – don't be afraid to ask your licensee. In some circumstances it may be beneficial to both parties for that change to be made. If you are seeking to make any changes – contact your IP commercialisation organisation who will be able to help.

- ✓ Due diligence
- ✓ Proof-of-Principle
- ✓ Business Case



Phase 1	Phase 2	Phase 3
<ul style="list-style-type: none"> Protect IP Compose the licence package Short-list identified targets Produce marketing materials Research 	<ul style="list-style-type: none"> Make contact Presentations Demonstrations Research Assess Proposition 	<ul style="list-style-type: none"> Due diligence Negotiate Legals Research

The timescale of each phase and in total differs from case to case especially in fields such as healthcare where timescales can be very long.



Colour code: Activities/Degree of involvement

● Research Institution/Researcher (Licensor)

● Company (Licensee)

● Both parties

Advance – an up front payment under the licence, which is often then set-off against royalties as they become due.

Assignment – an outright transfer of IP to a new owner which leaves the transferor with no further rights in that IP.

Commercialisation – the assignment of, licensing of or other dealing with IP for financial or other gain. This is sometimes known as exploitation.

Escrow – when the source code of software is given to a third party on the basis that it will only be released to the licensee in specific circumstances such as the licensor's insolvency.

Escrow Agent – Authorised person/firm who will hold the source code/relevant material.

Exclusive – any right granted exclusively which allows the grantee to use that right. The grantor is no longer free to use it itself nor to license anyone else to use it.

Head Licence – a licence of IP granted by the owner of the IP to a licensee. This term is often used to distinguish such licence from any further sub-licences.

Improvement – this is an amendment or modification to the licensed IP made after the licence is entered into. A severable improvement is an improvement by the licensee which could be used separately without infringing the licensor's IP. A non-severable improvement is one which could not be used separately without infringing the licensor's IP.

Licence – the grant of a right in IP, whilst retaining ownership.

Licensee – the person or organisation to whom the licence is being granted.

Licensor – the party or organisation which is granting the licence to the licensee.

Merchandising – a licence of copyright in an artistic work, design right or trade mark for reproduction on an article for onward sale.

Non-exclusive – a right granted non-exclusively allows the grantee to use it and the grantor is free to use it itself and to license anyone else to use it.

Pipeline – an agreement under which the licensee automatically acquires certain rights in improvements made by the licensor institution or specific individuals within the licensor institution.

Royalty – the amount paid under a licence of IP for the right to use that IP. This can be a “lump sum”, “up front”, “stage”, “all” or “periodic” payment.

Royalty Rate – the rate at which the royalty is charged, often a percentage linked to the selling price of an item/process.

Royalty Stacking – where the royalties payable in respect of different IP licensed-in to produce a product or provide a service stack up, possibly to a point at which the production of the product or provision of the service is no longer economically viable.

Sole – a sole right is one where the grantee is allowed to use it and the grantor remains free to use it itself but the grantor is not able to license anyone else to use it.

Sub-licence – a licence subsequently granted by the licensee of all or part of the IP licensed to the licensee by the licensor under the head licence.

Links

Copyright Licensing Agency (www.cla.co.uk)

Department for Business, Innovation and Skills for general guidance on innovation and relevant support funds/grants (www.bis.gov.uk/innovation)

Business Link: for contacts that can help (www.businesslink.gov.uk)

UK Intellectual Property Office: for the forms and other information of registering licences (www.ipo.gov.uk)

“Successful Technology Licensing”: From the IP Assets Management Series (World Intellectual Property Organisation).

Open Source Initiative (www.opensource.org)

Licensing Checklist

COMMERCIALISATION	Assignment or Licence	<ul style="list-style-type: none">■ Assignment – lose ownership and right to use■ Licence – retain ownership but allow others to use■ Consider the impact on the value of the IP■ Do you need to continue to use the IP?■ Consider tax position
WHY LICENSE?	Benefits	<ul style="list-style-type: none">■ Financial gain■ Supports further research■ Alternative to creating a spin-out company■ Provides case study material■ Translation of ideas into society
MARKETING IP	Gaining interest	<ul style="list-style-type: none">■ How does the IP fit with licensee?■ Construct a clear business case■ Be ready to demonstrate IP■ Demonstrate experience of licensing■ Consider offering research support
TYPES	Exclusive, sole or non-exclusive?	<ul style="list-style-type: none">■ Do you have resources to commercialise?■ Do you need control over IP?■ Does IP need further development?■ Who needs to use IP?■ Is more than one party interested in IP?■ Is licensee able to commercialise IP fully?
SCOPE	Limiting scope	<ul style="list-style-type: none">■ For what specific purpose will IP be used?■ Consider restricting the territory■ Can IP be licensed in different fields of use?■ Is an open source licence appropriate?■ Should licensee be able to sub-license?

PAYMENTS

Types of payment provisions

- Should royalties be linked to money made by licensee?
- How will the royalty calculation be made?
- Should there be an up-front payment to recover initial costs?
- Should there be minimum payments?
- Should payments be made at milestones?
- Consider factors affecting the royalty rate.
- How will payments be monitored?

TYPICAL PROVISIONS

Other key considerations

- How long is the licence for?
- Who will own improvements to IP?
- Who will deal with litigation affecting the IP?
- Who will maintain the protection of the IP?
- Should you limit your liability?
- When can you terminate the licence?

POST-SIGNING

Registrations and checks

- Do you need to register the licence?
- Check payments and inspect licensee's records regularly
- Keep a record of licensed IP and restrictions on you
- Keep licence under review