

Introduction to Technology Licensing

The aim of this sheet is merely to give a basic introduction to the concept of intellectual property licensing and to outline some of the points which may need to be considered when granting or taking such a licence. Throughout the sheet the term “licensor” is used for the person/company granting the licence and “licensee” for the person/company taking the licence. This sheet concentrates on the licensing of products and processes. Special considerations apply in the licensing of trade marks or brand names, and these are dealt with in a separate sheet. For further advice, or for our sheet on trade mark licensing, please contact us.

What rights can be licensed?

- Patents/patent applications
- Know-how (confidential information)
- Copyright
- Unregistered design right
- Registered designs

First, be sure that the licensor actually owns the rights which are to be licensed. For example, it is widely assumed that a person or business which commissions copyright work is automatically the owner of the copyright. This is not correct, and the copyright needs to be assigned to the person/business commissioning it.

In the case of patent licensing, you need to ensure that the intended licensor is the applicant in the relevant patent applications or is the patentee in the case of granted patents.

Within a group of companies, the identity of the appropriate licensor will depend on financial and organisational decisions and plans and possibly tax considerations. Remember that a patent licence may well last for up to 20 years.

Once the appropriate licensor has been identified, it may be necessary to assign patents, patent applications or other rights to the licensor.

Which rights are to be licensed?

A licensee can be licensed to do any of the acts (and not necessarily all of them) which would infringe any of the licensor’s intellectual property rights if done without the consent of the licensor.

For example, a UK patent can be infringed by making, selling, using or importing the patented product without the consent of the patentee.

A licensee may therefore be permitted to carry out all, or any one or more, of these activities.

Another way of splitting the licensor’s rights is by granting a “field of use” licence or licences. Here, the right given to the licensee is limited to a particular application, or to a particular area of technology or industry or commerce. This kind of licence requires very careful drafting to ensure that the licensee’s rights are clearly defined and delimited.

You can also split up the rights according to geographical area, so that a particular licensee is licensed to carry out a particular activity within a particular geographical area only.

Where the licensor owns rights (e.g. patents) in different countries, separate licences may be granted under each of the national patents.

Alternatively, a licensee may be licensed to carry out certain activities in a number of different countries in which the licensor owns intellectual property rights.

Competition laws must be considered in connection with restricting licenses to particular countries – see below.

Is the licensee to be allowed to grant sublicenses?

In the case of a manufacturing licence, for example, it should be stated whether the licensee may have the products manufactured for it by another party, and whether the licensee may grant sub-licences to others to manufacture and sell the products on their own account.

The licensor may want to control the quality of the products being manufactured, or the parties may negotiate different royalty terms in respect of products manufactured or sold by sub-licensees.

How many licensees?

A licence may be an exclusive licence, a sole licence or a non-exclusive licence.

Once the licensor has granted an exclusive licence, no one (including the licensor!) except the exclusive licensee may do any of the acts which are the subject of the exclusive licence. If the exclusive licence covers all of the activities which would otherwise infringe the patent (for example), then the licensor has granted away his own rights almost as if he had sold the patent to the exclusive licensee. Particular attention must be paid to competition law when considering granting an exclusive licence.

Under a sole licence, the licensor may continue to use the licensed rights himself, but he has contracted with the sole licensee that he will not grant licences to other parties.

Under a non-exclusive licence, the licensee may be one of many licensees. The power of the licensor to grant further licences has not been restricted.

Acknowledgement of licensor's rights

The licensor may require the licensee to mark all products manufactured or sold under the licence with an acknowledgement that they are, for example, patented products and are sold under licence from the licensor.

Improvements

Whenever there is any prospect that the technology will be further developed, the parties should agree upon the ownership and use of intellectual property rights in improvements which may be made in the future by either party.

For example, a common arrangement is that intellectual property rights in improvements belong to the party which has made the improvement, but that the improvement will be disclosed to the other party which will then have a royalty-free licence to use the improvement.

Although this is a common arrangement, it is by no means universal. The question of improvements is a matter for negotiation between the parties. However, competition law must be considered in this context as certain kinds of arrangement are prohibited. For example, an obligation on the licensee to assign to the licensor improvements that can be exploited without infringing the licensed technology (i.e. severable improvements), is generally not permitted.

Payment

Payment is usually by way of royalties, but may be by lump sum, or by a combination of the two.

The basis for calculation of royalties will depend upon the activity that is being licensed. In the most common scenario, where the licensee is licensed to sell, or to manufacture and sell, a patented product, royalties are usually expressed as a percentage of the "net sales value" of the product sold, after deduction of taxes and expenses such as carriage, insurance and packaging.

The definition of "net sales value" needs to be carefully drafted, so as to cover, for example, the situation where the licensee may sell the product at an undervalue to a subsidiary or associated business. It is also important to ensure that there is no ambiguity, so as to avoid the possibility of disputes arising in the future.

Provision should also be made in the licence for the licensee to provide the licensor with regular statements of manufacture and/or sales figures, and for these figures to be

checked by an independent accountant if required by the licensor.

It is common to include provision for minimum royalties, so that the licensor is certain of receiving a minimum return regardless of the licensee's performance. In the case of an exclusive licence, this may be coupled with a provision for the licence to become non-exclusive if minimum sales figures are not reached. Alternatively, the licensee may have the option of either making up the royalties to the minimum figure or losing the licence, if the minimum figure is not reached.

Infringement

The parties will need to decide whether the licensor is to be under an obligation to bring infringement proceedings against third parties at the request of the licensee, or merely to lend his name to proceedings brought by the licensee; and (most importantly) which of them will bear the costs of such proceedings.

One possible arrangement is that the licensee brings the infringement proceedings and bears the costs, but may set off the costs against royalties which would otherwise be due to the licensor while the proceedings are going on.

The licence agreement should also cover the possibility that a third party may allege that the activities of the licensee amount to infringement of intellectual property rights belonging to that third party. The licensor will usually want to make it clear in the licence agreement that he gives no warranty that the licensed activities will not infringe someone else's rights.

How long should the licence last?

A licence may last for any length of time up to the duration of the intellectual property rights concerned.

Patents, registered designs and unregistered design right have a fixed life span (subject to the payment of renewal fees in the case of patents and registered designs) while copyright can last for much longer, and know-how indefinitely.

It should be agreed which party will pay (and be responsible for paying) the relevant renewal fees.

It is sometimes appropriate to grant a licence for a relatively short period, but to include provision for the licence to be extended if the parties so desire upon the expiry of the initial period.

Termination of the licence

The licence should include a provision for the licensor to terminate the licence in certain circumstances, for example upon the insolvency of the licensee, or in the case of a serious breach of contract by the licensee. There are standard terms covering termination which are often used in licence agreements.

Resolution of disputes

The parties may agree that any disputes are to be resolved by mediation or arbitration instead of in the courts.

In the case of transnational licence agreements, the parties should also agree upon a choice of law clause (which State's laws govern the agreement) and a jurisdiction clause (in which State's courts the agreement may be litigated).

Competition law

Certain terms which might be agreed between a licensor and licensee are in fact not permitted in a licence agreement under UK or European competition law, or the competition law of other jurisdictions.

Chapter I of the UK Competition Act 1998 and Article 81(1) of the Treaty of Rome prohibit agreements which have the object or effect of preventing, restricting or distorting competition, and which may affect trade within the UK and trade between Member States of the European Union respectively.

Parties to agreements that breach this prohibition may be fined, and the agreement itself will be unenforceable, which is often of even more concern to the parties involved.

Because intellectual property rights give their proprietor a monopoly in a particular field, and also because patents give protection within national boundaries, there is often a tension between the exercise of patent rights and competition law. Many of the terms that parties would like to include in their licences for their own commercial advantage are quite likely to fall within the Chapter I/Article 81(1) prohibition.

The European Commission has issued various Block Exemption Regulations that give certain types of agreement exemption from Article 81(1), provided the terms of the agreement are such that it in fact promotes, rather than restricts, competition. The current Regulation that gives exemption to patent and know-how licences which fall within its terms is the Technology Transfer Block Exemption Regulation which came into force on 1st May 2004.

Agreements that fall within the terms of a European Commission Block Exemption Regulation are also exempt from the UK Competition Act Chapter I prohibition, regardless of whether they affect inter-state trade or only trade within the UK. The Technology Transfer Block Exemption Regulation can therefore be regarded as a “safe harbour” for all patent and know-how licences that fall within its scope.

This “safe harbour” is severely limited, however. It does not cover agreements where the parties’ market shares are above certain thresholds, and these thresholds vary according to whether or not the parties are competitors. Correct identification of the relevant market is crucial to the assessment of market shares.

In any case where the Technology Transfer Block Exemption Regulation does not (or may not) apply, it is down to the parties to make their own assessment of whether or not, in all the circumstances, their proposed arrangement might be regarded as anti-competitive.

The Technology Transfer Block Exemption Regulation sets out a list of “hardcore” restrictions of competition, and these give a good indication of the kinds of activities that the Commission regards as anti-competitive and unlawful. In particular, Chapter I and Article 81 outlaw agreements which directly or indirectly fix prices, or limit production or markets or technical development or investment, or share markets or sources of supply, or discriminate between different trading parties, or impose obligations which have no true connection with the subject of the agreement.

The Commission has also published Guidelines on the application of Article 81 to technology transfer agreements.

These Guidelines (which run to over 40 pages) provide further insight into the Commission’s thinking in this area, and give examples of situations that can result in breaches of competition law.

Once the parties to an intended licence have reached agreement on the proposed terms, it is vital to check the proposed terms against the Technology Transfer Block Exemption Regulation and the Guidelines in order to ensure that the final agreement does not infringe competition law.

Recordal of licences

In most countries (including the UK) patent licences can be recorded, and in some countries it is obligatory to record them.

It is generally in the interests of the licensee, rather than the licensor, to record the licence and the licensee therefore usually bears the cost of doing so.

In the UK, the licensee will want to record his licence so that anyone who buys the patent from the licensor buys it subject to his licence, and so that he can continue to work under his licence even if the licensor later agrees to grant someone else an exclusive licence.

In the UK, an exclusive licensee may bring legal proceedings for infringement of the patent in his own name, but in order to obtain damages as from the date of grant of the licence, he must register the licence within six months of its grant.

This information is simplified and must not be taken as a definitive statement of the law or practice. For more information on Mewburn Ellis LLP and other intellectual property matters, please contact us or visit our website at www.mewburn.com.

Mewburn Ellis LLP is a Limited Liability Partnership registered in England (no. OC306749). Registered Office at York House, 23 Kingsway, London WC2B 6HP

LONDON
York House
23 Kingsway
London WC2B 6HP
Tel: 020 7240 4405
Fax: 020 7240 9339

BRISTOL
22-24 Queen Square
Bristol
BS1 4ND
Tel: 0117 945 1234
Fax: 0117 926 5692

MANCHESTER
Bridgewater House
Whitworth Street
Manchester M1 6LT
Tel: 0161 247 7722
Fax: 0161 247 7766

CAMBRIDGE
Newnham House
Cambridge Business Park
Cambridge CB4 0WZ
Tel: 01223 420383
Fax: 01223 423792