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Technology Licensing for Beginners: An Introduction

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Welcome to the wonderful world of technology licensing. This article is intended for professionals including researchers, developers, technology transfer specialists, and attorneys who are new to technology licensing. Technology licensing is explained here by answering the following questions:

- What is technology licensing?
- What is intellectual property?
- What are the types of license agreements?
- What are common license agreement provisions?
- What is a term sheet?

A word of caution: this article is simply an introduction and does not cover the intricate nuances of technology licensing. Instead, this article provides a higher-level treatment of topics that serve as a starting point to understanding technology licensing. It should also be understood that it is very dangerous to rely upon "boilerplate" language and template agreements in connection with technology licensing. Every technology license agreement is different, and as a result, the entire agreement should be carefully reviewed and evaluated to ensure that it is appropriate in view of the specific transaction at hand. Using templates or previously negotiated agreements can be problematic because they typically have been heavily negotiated and may include provisions that significantly favor one party.

What Is Technology Licensing?

Broadly speaking, technology licensing is the exchange of intellectual property ("IP") between two entities in which a first entity gives another entity permission (*i.e.*, a "license") to use the first entity's IP. In simple terms, a technology license agreement is somewhat similar to a rental agreement. In a rental agreement, a building owner gives someone permission to occupy an apartment for a specified duration of time in exchange for the payment of rent. In a technology license agreement, an IP owner gives someone permission to use certain IP for a specified period of time in exchange for payments called "royalties" or "license fees." Notably, in a technology license agreement, *ownership* of the licensed IP is not transferred and instead only certain specified permissions regarding the IP are granted.

Although the comparison of a license agreement to a rental agreement is a good starting point, the comparison does not completely hold up because of several fundamental differences between physical (or tangible) items and IP, which is an "intangible" asset. While a detailed discussion of these differences is outside the scope of this introductory article, it is important to note that tangible assets such as an apartment building are typically finite in quantity (*i.e.*, there are only a limited number of apartments in a building) while intangible assets such as IP are not typically limited in the sense of physical quantity (*i.e.*, there is no physical limit to the number of times an IP asset such as a patent or copyright can be licensed).

An understanding of two commonly used licensing terms will be helpful to better understanding this article (and the world of licensing). Those terms are "licensor" and "licensee."

The *licensor* is the entity with ownership of the IP or with the ability to grant others rights in the IP. The *licensor* grants the license (remember, the licensor is the grantor).

The *licensee* is the entity that receives permission from the licensor to use the IP. The *licensee* takes the license.

Technology licensing is very common in today's economy, and following are a few examples using the terms licensor and licensee to put things in context. The licensor can be a university that owns patents (one type of IP) related to a new technology in the rechargeable battery space, and the licensee can be a car manufacturer that wants to license these patents from the university to use the technology in an electric vehicle under development. Alternatively, the licensor can be a research company that is licensing its trade secrets to a chemical production facility (the licensee) to improve the efficiency of a chemical cooling process. Or the licensor can be a software company that owns the copyrights and trade secrets (others type of IP) in a word processing software program, and the licensee can be an IP attorney that will use this word processing program to write an article about the fundamentals of technology licensing.

What Is Intellectual Property?

The importance of IP to today's global economy cannot be overstated, and it is difficult to name an industry where IP does not play an essential role. Notably, over approximately the last 40 years the US economy has undergone an economic inversion in which the roles played by tangible and intangible assets have significantly changed.[1] For example, in 1975 tangible assets (*i.e.*, brick and mortar assets) accounted for roughly 83 percent of the market capitalization the S&P 500, whereas intangible assets (*i.e.*, IP and other non-physical assets) accounted for only 17 percent of this market cap.[2] Fast forward 40 years, and these values have inverted; in 2015 intangible assets now accounted for 84 percent of the S&P 500's market cap, whereas tangible assets accounted for only 16 percent.[3] The message here should be clear: intangible assets such as IP play a major role in our US and global economy, and we need to understand how to exchange IP between entities.

The details of a technology licensing agreement will vary by the type of IP involved. For this reason, the four basic types of IP will be summarized: patents, trade secrets, copyrights, and trademarks. Patents and trade secrets both focus on protecting technology and can typically be viewed as two sides of the same coin. Copyrights focus on protecting content fixed in a tangible medium rather than the technology embodied in the content. Trademarks focus on branding rather than technology or content.

A fundamental aspect of IP is understanding that IP rights are grounded in *exclusionary* rights rather than affirmative rights.[4] In other words, IP rights fundamentally enable the owner of the relevant IP right to exclude, or prevent, other people from practicing or otherwise using this right. The owner of the IP right does not automatically have the ability to practice or use this right. It is sometimes difficult for IP newcomers to grasp this concept, but it is an important concept to keep in mind in connection with IP licensing.

What Are the Types of License Agreements?

License agreements will vary depending upon the IP involved and the industry. High-level categories of the agreements are explained here.

Exclusive versus Nonexclusive

A fundamental aspect of a technology license agreement is whether the license grant is *exclusive* or *nonexclusive*.

In an *exclusive* license agreement, the technology is licensed to only one entity and cannot be licensed to others by the licensor (*i.e.*, the party having rights to license the technology). In other words, the license is *exclusive* to the licensee (*i.e.*, the party to whom the technology is licensed), enabling the licensee to use the technology without any concern that the licensor will subsequently make the technology available to others. Because the licensor cannot license the technology to others, the fees paid from the licensee to the licensor are typically higher than the fees paid in connection with a *nonexclusive* license agreement (explained below).

Exclusive license agreements are typically structured to ensure minimum payments to the licensor and to ensure that the licensee makes sufficient efforts to commercialize the licensed technology (maximizing the license fees paid to the licensor). In some situations, minimum thresholds called *milestones* are established in the agreement. These *milestones* are typically tied to a minimum license fee that must be paid to the licensor to maintain the exclusivity of the license agreement. Without the establishment of such milestones, there could be a danger that the license would not make any effort to commercialize the licensed technology and instead "shelve" this technology and pursue other avenues.

In a *nonexclusive* license agreement, the licensor is permitted to license the technology to other parties beyond the licensee of the relevant agreement. In other words, the license agreement is not exclusive to just one licensee, and the technology can also be licensed to others. For this reason, the license fees paid under a nonexclusive license are typically lower when compared with an exclusive license agreement.

Patent License Agreement

A patent license agreement is a very common type of technology license agreement. Here, patent rights are licensed from the licensor to the licensee. In essence, the licensor is agreeing to not sue the licensee for patent infringement of the patents included in the agreement. Notably, the licensor is not necessarily giving the licensee permission to practice or commercialize the technology claimed in the licensed patents because other patents might exist that still cover the technology to be commercialized.

Trade Secret and Know-How Agreement

A trade secret and know-how agreement is another common type of license agreement. Here, the licensor is permitting the licensee to practice and commercialize trade secrets owned by the licensor. Unlike a patent license agreement, the licensor is giving affirmative permission to practice the technology embodied by the trade secret.

In addition to the trade secrets, these agreements typically also include "know-how." Know-how is generally broader than trade secrets and broadly covers all of the information relevant to practicing a technology including any information that provides further background for practicing the relevant technology. In one sense, trade secrets are a sub-category of know-how.

Software License Agreement

A software license agreement is another typical license agreement. Anyone that has used a computer or the Internet has encountered a software license agreement, typically by clicking the "I ACCEPT" button before gaining access to software or use of a website. A software license agreement is typically a hybrid of a copyright, know-how, and trade secret license agreement in which the licensor gives the licensee permission to use the software for specified purposes.

Material Transfer Agreement

In biotechnology, chemical, and material science technologies, material transfer agreements are used to share material between entities while preserving the IP rights in the materials. Here, the entity that supplies the material is typically called the *transferor*, and the entity receiving the material is typically called the *recipient*. The rights between the transferor and the recipient are then spelled out in detail, with an emphasis upon who owns and can use an IP rights created by the recipient.

What Are Common License Agreement Provisions?

Regardless of the specific type of license agreement, there are several common provisions typically present in these agreements. These common provisions are explained here.

License Grant

As the name suggests, the *license grant* in a technology license agreement is one of the most important aspects of the agreement. This part of the agreement specifically defines what the licensee can and cannot do in connection with the IP licensed under the agreement. The license grant is different between patent, copyright, trade secret, and know-how agreements.

As a general rule when negotiating a license agreement, the Licensee should assume that unless a right is expressly granted to the Licensee, the Licensee does not have this right. In addition, it is common in license agreements to expressly state that the Licensee does not have any additional rights beyond those expressly identified in the license agreement.

Following is a typical license grant in a patent license agreement, which will then be broken down and discussed in detail, with a focus on the italicized terms.

"Subject to the terms and conditions of this agreement, Licensor hereby grants to the Licensee, and the Licensee hereby accepts, an *exclusive royalty-bearing* license under the Patent Rights, with the right to grant sublicenses, in the Field of Use, in the Territory, to *make, have made, import, use, have used, offer for sale, sell, and have sold* Licensed Products."

At the outset, note that this is an *exclusive* license, meaning the Licensor cannot grant any licenses in the *Field Of Use* to others besides the Licensee. *Field Of Use* is a way to further segment the license rights being granted. Examples of Field Of Use include technology category (*e.g.*, within the oil and gas industry but not in water treatment applications) or parameters within a specified technology (*e.g.*, engines up to 1,000 horsepower).

This license is also a *royalty-bearing* license, meaning royalty payments will be made on a periodic basis. For example, another provision in the agreement may specify that a royalty of $1.50 per unit sold by the Licensee shall be paid to the Licensor. Other types of payment structures besides a royalty bearing license include:

- *fully paid up*—a single, lump sum payment has been made in exchange for the license grant; and
- *royalty free*—no payments are made in exchange for the license grant; other consideration is typically given to the Licensor in royalty free arrangements.

The above license grant also permits the Licensee to do the following under the patent rights, *"make, have made, import, use, have used, offer for sale, sell, and have sold*." Each is explained below. Some will seem quite evident, but others are more nuanced.

- *make*—the Licensee can make products covered by the licensed patent rights;
- *have made*—the Licensee can have others produce for Licensee products that are covered by the patent rights. This is very common where the licensee will have a contract manufacturer produce products for the Licensee;
- *import*—the Licensee can import products covered by the Licensed products;
- *use*—the Licensee can practice the technology covered by the licensed patent claims;
- *have used*—the Licensee can permit others to practice the technology covered by the licensed patent claims. Note that these *have used* rights are different from the right to sublicense;
- *offer for sale and sell*—the Licensee can offer for sale and sell technology covered by the licensed patent claims;
- *have sold*—the Licensee can have others sell the technology covered by the licensed patent claims.

It is important to note the differences between each of the above permitted actions in this patent grant language. When negotiating the grant language in a patent license agreement, it is very important to recognize when one of the above actions is omitted from the license grant because such omission means that the Licensee is not permitted to take this action. For example, if *have made* rights are not included in the license grant language, the Licensee is not permitted to have others such as contract manufacturers produce the technology on behalf of Licensee. In many industries, the ability to use contract manufacturers is very important, so the omission of *have made* rights from the license grant language could substantially reduce the value of the entire license agreement to the Licensee.

Following is another sample license grant taken from a software license agreement, which will again be broken down and discussed in detail, with a focus on the italicized terms.

"In consideration of the license fee(s) as shown on the applicable Product Schedule, Licensor hereby grants and Licensee hereby accepts a *world-wide*, *non-exclusive*, *perpetual* license for its Users to *operate*, *use*, *access*, *modify* and copy ("Use") the Licensed Product, including Documentation, as provided in this Agreement."

This is a *world-wide* software license grant, meaning the Licensee can use the software throughout the entire world. Other software license grants might limit the software usage to only certain countries or charge additional fees to use the software in additional countries.

This is a *nonexclusive* software license, meaning the Licensee can license the software to others in addition to the Licensee.

The Licensee is permitted to *operate, use, and access* the licensed software. These three rights overlap one another a bit in terms of the rights granted the Licensee. Each term might have a more specific meaning depending upon the type of software being licensed, and it would be important to recognize if one of these rights was not included in the license grant in the context of the specific software being licensed. For example, if the license grant only permitted access to the software without granting the rights to operate and use the software, it would be important to understand the differences between merely accessing the software compared with also operating and using the software.

Here, the Licensee can also *modify* the software, which has significant implications in the software context. The right to modify software means that the Licensee can actually modify the features, functionality, and potentially source code of the licensed software. These are powerful rights and are typically not easily granted by the Licensor in a software license agreement. Before pushing for the right modify the software, the Licensee should typically consider whether (1) the Licensee has the technical expertise to make such modifications; (2) how such modification will implicate warranties on the software (modifications typically void warranties); and (3) how the modifications will affect technical support from the Licensor (support is not typically provided for Licensee modifications). In addition, the parties should clarify who owns the IP rights in the modifications made by the Licensee.

Representations and Warranties

Other common provisions in technology license agreements are the *representations* and *warranties*. On a high-level, representations (or "reps") and warranties are specific promises made by the parties in an agreement and they are typically treated in the same fashion.[5] More specifically, a *representation* "is a statement of fact that induces a party to enter into the contract. The statement, made before or at the time of making the contract, regards a past fact or existing circumstance related to the contract which influences such party to enter the contract."[6] A *warranty* "is an undertaking or stipulation that a certain fact in relation to the subject of the contract is or shall be as it is stated or promised; and refers to an agreement to protect the recipient against loss if the fact is or becomes untrue."[7] It is good to be aware of these distinctions, but they are not further addressed in this article.

Ownership of Licensed IP

It is very common to require the Licensor to represent and warrant that it owns the IP being licensed and further that that the Licensor has the right to license the IP to the Licensee. If a Licensor is not willing to make representations and warranties, the Licensee should be suspicious of whether it is a good idea to enter a license agreement with the Licensor.

Noninfringement

It is also common to request that the Licensor represent and warrant that the licensed technology does not infringe any IP rights of thirds parties, including patents, trade secrets, and copyrights. Licensors are not always willing to make these noninfringement representations and warranties, especially with respect to patents. Although Licensors can typically be comfortable that the technology they are licensing does infringe any third-party trade secret and copyrights, Licensors may not always be aware of whether the licensed technology infringes any third-party patents.

Both trade secret infringement and copyright infringement require the infringer to be aware that it is doing something wrong, but patent infringement does not include any awareness requirement on the part of the infringer. In other words, the Licensor could be infringing a third party's patent without any knowledge of the patent or the alleged infringement. For this reason, Licensors are not always comfortable making a representation and warranty of noninfringement. The lack of this warranty is not typically a deal breaker for the potential Licensee, but the Licensee must be aware of the potential risk involved. In addition, regardless of whether the Licensor is willing to make a warranty of noninfringement, the Licensee must understand whether the Licensor will defend and indemnify the Licensee in the event a third party claims the Licensee is infringing the third party's IP by using the licensed technology. The duty to defend and indemnify is discussed below.

Confidentiality

Technology license agreements also commonly include confidentiality provisions that require the parties to protect the confidentiality of certain information shared by the parties in connection with the license agreement. Although a detailed explanation of the nuances of confidentiality agreements is beyond the scope of this article, newcomers to the licensing arena should be aware of several high-level aspects of confidentiality provisions.

There are typically two fundamental obligations in a confidentiality provision: (1) the recipient of confidential information will not disclose the confidential information to third parties and (2) the recipient of confidential information will not use the confidential information for any purpose beyond performing its obligations under the current agreement. Many newcomers are unaware of this second obligation, which can cause substantial problems if the recipient of confidential information is not careful about who has access to this information. For example, unless protected confidential information from outside an organization is carefully managed, someone within the organization might accidentally become exposed to this information and use the information in connection with another, separate technology under development. This use would be in violation of the confidentiality obligations and, worse yet, potentially "infect" the separate technology with the IP received under the other license agreement.

Indemnification

License agreements commonly require the Licensor to *defend* and *indemnify* the Licensee in the event that a third-party claims that the Licensee's use of the licensed technology infringes the third party's IP. At the outset, newcomers should be aware that the costs of defending against allegations of IP infringement—and especially patent infringement—can quickly become very expensive and easily run into the millions of dollars. It is likewise important to understand that the duty to defend is actually a separate obligation from the duty to indemnify.[8] A "duty to defend arises at the earliest states of litigation and exists regardless of whether the indemnitee is ultimately found liable."[9] A duty to indemnify does not arise until later—once the indemnitee is ultimately found liable—and then obligates the indemnitor to pay the costs and damages finally awarded against the indemnitee.[10]

An important takeaway here is that both the duty to defend and the duty to indemnify should be included in a license agreement to more fully protect the Licensee. The omission of either leaves the Licensee potentially exposed to typically unwanted liability. For example, if the license agreement includes only the duty to indemnify without the duty to defend, the Licensee remains on the hook to pay the attorney fees and other expenses while the patent infringement lawsuit is pending (there is no duty to defend) and typically can only seek reimbursement of these fees in the event the Licensee is found liable in the case.

What Is a Term Sheet?

A *term sheet* is used by the parties to map out and agree upon the high-level aspects of a license agreement before starting to negotiate a detailed license agreement. The use of a term sheet typically results in a more efficient process overall because it helps the parties determine at an earlier stage whether there is disagreement over a fundamental aspect of the deal such that no deal is possible. In addition, the use of a term sheet typically streamlines the preparation and negotiation of the detailed license agreement because the parties have agreed upon the fundamental aspects of the deal before getting into the details of the agreement itself.

A sample term sheet is included as Appendix 1 to this article and provides a good starting point for structuring a license agreement. This sample term sheet is based upon a sample available from the World Intellectual Property Organization ("WIPO").[11] It is important to remember that a term sheet typically does not form a binding and enforceable contract between the parties and instead serves as the starting point for negotiating such a contract. Parties are wise to confirm the term sheet is not intended to form a binding and enforceable contract by including the language included in the sample term sheet.

Conclusion

As should be evident from this article, technology licensing involves many different aspects and is always specific to the situation at hand. There is no "one size fits all" license agreement, and the parties must make sure that the license agreement meets the business needs of both sides. In addition, the signature (commonly called "execution") of the license agreement is typically just the beginning, and not the end, of the collaboration between the parties. For this reason, it is important that the license agreement clearly explain the expectations and obligations of each party; both sides will have to live with the deal for quite a while (decades, in some situations). It is rarely a good idea to "let sleeping dogs lie" and leave unanswered questions when negotiating a license agreement.

Again, welcome to the wonderful world of technology licensing. Curiosity is key to this world, so never stop asking questions and then trying to ensure these questions are answered in the relevant license agreement.

Appendix 1
Sample Term Sheet
For a License Agreement

[NOTE: This Term Sheet should be used as the starting point for negotiating with another party on projects in which technology and intellectual property will be developed. It addresses the high-level topics common to such agreements. Typically, a party should first internally decide how the various topics should be structured, and then the party should discuss these topics with the other side. The term sheet can then be provided to the other side to streamline negotiations. It is also typically a good idea to have a member of the party's management and/or an attorney review the Term Sheet before it is sent out.]

1. Potential Licensor / Party / Investment Partner

<<IDENTIFY THE OTHER PARTY TO THE POTENTIAL AGREEMENT>>

2. Important Dates and Deadlines

<<IDENTIFY ANY IMPORTANT DATES AND DEADLINES>>

3. Subject Matter

Patents, patent applications, trade secrets, and know-how related to <<PROVIDE A GENERAL DESCRIPTION OF THE TECHNOLOGY INVOLVED>>, including the following:

U.S. Patent No.: <<INSERT>>

U.S. Patent Application No.: <<INSERT>>

Other intellectual property or other know-how: <<INSERT>>

All of the foregoing are referred to as “Licensed Technology” in this document.

4. Ownership

Who owns the Licensed Technology?

5. Related Agreements

<<IDENTIFY AND DESCRIBE ANY OTHER EXISTING AGREEMENT WITH THE OTHER PARTY. THIS TYPICALLY INCLUDES CONFIDENTIALITY AGREEMENTS.>>

6. Development

<<Explain whether the Licensed Technology is fully developed. If not, explain who will complete the development.>>

7. Scope of License

This is a core part of the agreement that needs to be framed out. Possible options to explore are (1) the outright acquisition of certain IP assets; (2) exclusive licenses to certain IP assets; and (3) exclusive “field of use” licenses. There are likely other options to be explored as we learn more about the contemplated agreement.

8. Improvements and Derivative Works

Discuss ownership of improvements to the Licensed Technology. Who acquires ownership of any newly-developed IP under the agreement?

9. Sub-licensing

Will the licensee have the ability to sub-license the technology?

10. Geographic Territory

In what countries or regions can the Licensed Technology be used? The countries in which patent protection is being sought are relevant to the geographic scope, but the trade secrets and know-how can be used to expand the geographic scope provided the agreement is structured properly.

11. Field of Use

Here, we can limit the exclusive license to certain technical areas, called "fields of use."

12. Financial Terms

What fees will be paid to the other party? What royalties? What will be the minimum milestone payments or other actions needed to keep the license exclusive (if structured as an exclusive license)? Any advance on royalties paid?

13. Term

How long will this agreement last? When and how can the agreement be renewed?

14. Future Versions

Does the license include future versions of and improvements to the Licensed Technology developed by the other party? In an exclusive license arrangement, this should be carefully considered and structured. Also, this provision should be carefully considered in view of the treatment of improvements and derivative works addressed in Section 8 above.

15. Additional Obligations

Consider who is responsible for matters such as testing, marketing, meeting standards, or any other industry-specific obligations.

16. Disputes

Where and how will disputes between the parties be settled?

IMPORTANT NOTE: This Term Sheet does not create any legally binding obligations between the parties. For the avoidance of doubt, no legally binding obligations shall be created between the parties until a separate and mutually agreed-upon contract is signed in handwriting by both parties.

1. *https://www.oceantomo.com/intangible-asset-market-value-study/* (last visited July 13, 2019).
2. *Id.*
3. *Id.*
4. Thomas M. Ward, Stephen M. McJohn, *Intellectual Property in Commerce*, § 1:4 (March 2019 Update).
5. 3 UCC Transactions Guide, § 28:22 (August 2018 Update).
6. *https://www.ipwatchdog.com/2018/10/10/contracts-101-covenants-representations-warranties-ip-license-agreements/id=102186/* (last visited July 13, 2019).
7. *Id.*
8. *Branch Banking v. Syntellect*, 2010 WL 294772 (M.D. Ala), 5-6.
9. *Id.*
10. *Id.*
11. *https://www.wipo.int/edocs/pubdocs/en/licensing/903/wipo_pub_903.pdf* (see page 59) (last visited July 13, 2019).

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