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# Negotiating a License: The Components to Success

Lawrence J. Udell

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Frequently, property IP owners will express an interest in the opportunities afforded by licensing their ideas, wishing to avoid the uncertainties and difficulties associated with producing the concept on their own, going into business and investing great amounts of time and money. I advise clients that there are no real secrets to successfully licensing a new product/technology/invention, only that the process usually requires unbelievable patience and the ability to keep the faith throughout the research and development phases, which can take a considerable amount of time. The licensing process should not be attempted without expert legal assistance, and although many inventors believe the contrary, there is no standard licensing agreement that can be used as a universal guide. License negotiations, and the drafting of the license agreement that will define the terms of the licensing partnership, should be custom-designed to fit the specific business situation and the specific technology or product that is involved.

## Licensing Terms Defined

A license is a contractual business relationship between a seller (licensor) who authorizes a buyer (licensee) to use the seller's patent, trademark, copyright, or other form of "intellectual property" for compensation. The licensing activity is employed as

a business function, allowing both parties to profit from the arrangement. After all of the parties have agreed, the final written record of the activity forms the legal document known as the license agreement. In simple terms, the license agreement serves as the contract that has been drafted to mutually benefit, and mutually protect, both parties.

The license agreement also needs to define the specific property being licensed in the grant clause, which typically grants only limited rights to the property to the licensee and usually for a fixed period of time. Oftentimes, the agreement provides that the property can be licensed for a specified use or market for sale, allowing the licensor to make other similar agreements in other markets. Licensing is more complex than an outright assignment or sale: You can only sell a possession once, however, you can license a valued property hundreds of times, and in many cases, simultaneously. If the licensor is the sole proprietor, or the patent owner of a technology, the licensor can sue infringers. Ownership provides the licensor with an asset that is valued by what a potential licensee will pay for it. The exclusivity, or nonexclusivity, of the license can effect its value, with licensees willing to pay more for exclusive rights to properties, especially those in high demand.

## What Can Be Licensed?

Almost anything in which there exists a protectable property right can be licensed. Most familiar are industrial processes, patents, trademarks, copyrights, trade secrets, methods, formulas, customer lists, and manuals. In each case there is a form of legal right, such as the property right granted by the US government to an inventor when a patent is issued. The technology covered by the issued patent becomes a valued property for a period of 20 years, and the patentee has an exclusive right to do whatever it desires with it. However, the patents value, as previously stated, is only determined by what a reliable corporation or individual is willing to pay, either in royalty form or licensing rights.

This is why it is so critical that the property owner/potential licensor conduct extensive research into the potential market. The property owner needs to determine who is in the market already, how big the potential market is, who the competitors are, what the advantages to each of the companies in the market are, etc. There is no way of determining value, and the ability to negotiate a license, until an experienced and reliable organization or individual does an in-depth research study.

Many property owners feel that because they have the most vested interest in the property, they should take the lead in negotiations with interested licensees. My advice to property owners is: Never negotiate for yourself, unless you have previous experience that resulted in a successful conclusion. If potential licensors have no experience in dealing with, or negotiating a business agreement, they should not represent themselves. I have seen hundreds of inventors literally destroy any opportunities for success, because they either got greedy or desired to do everything themselves. Valuable and potentially million-dollar ideas die with their creators in these instances. It is my very strong advice to either have a patent attorney approach a potential licensee, or hire an individual or firm that knows the process and has enough experience to confidently and competently navigate the licensing negotiation process. This cannot be emphasized too strongly. You may be a great inventor, but it is important to recognize your limitations and not attempt to approach or even be involved in the negotiation, except perhaps, as a technical expert. It is better to have the experts and legal advice in the very beginning, rather than have to hire them when problems arise down the line.

## Risks/Rewards Analysis

The benefits of licensing are enticing. Licensing can provide a licensor with income over a long period of time, with much less risk and commitment than is involved with raising investment capital, manufacturing, and all the required ingredients in establishing and owning a company that produces and sells a product. However, the licensor will receive only a small percentage of the profit from the sales of a licensed product or technology, because the risk is considerably less. It is the licensee who must make the required investment in establishing everything necessary to produce the finished product and get it to the buyer or end user. Personal greed must never rear its ugly head to kill the opportunity.

Besides the benefits of royalties in licensing, in many cases the licensor can receive equity in a new business venture, especially if it is being created for the purpose of marketing the finished product that is the result of the license. The percentage often depends on the level of commitment and the benefits to the venture that the licensor brings to the table, along with the position and responsibility. This is most notably true when partnering with an established company. Licensing to an established corporation provides numerous advantages, including, the existing ability to manufacture the “new product” along with the means of distribution, a customer door that already is open, advertising experience, immediate penetration of domestic and possible foreign markets, and the name recognition of the company. This becomes an almost “no risk” position for the licensor, providing the license is properly drafted, with minimum guaranteed royalties, and benchmark performance criteria defined.

## When Should You License?

A protectable idea increases in value as the following events take place, however, this does not apply in all cases:

1. A raw idea is formed. (A very low, if any, value.)
2. A US patent application is filed to cover the idea.
3. A working model or demonstration of the viability of the idea is made.
4. Foreign counterpart patents are filed, providing funds are available.
5. The US patent issues. (Now there is a moderate value.)
6. The idea/invention is commercially marketed, or, it has been reduced to practice and recognized experts support the technology. (The value is now increased.)
7. A license is arranged with an established, financially sound corporation. (Now there is a high value.)
8. Additional licenses for other uses or geographic parameters is now instituted. (The original idea has now become a very high value.)

As stated previously, the value of anything is determined by what someone is willing to pay for it. The true value of a licensable technology, idea, patent, or whatever, must be based on the perceived value to the licensee. If potential licensees are able to recognize how the property fits into their business, and what the property would do for their sales and

profits, the results will be a mutually beneficial and rewarding relationship. It also might be the answer to a company's ability to diversify into other areas or new markets.

## Finding the Right Licensee

The common question of many would-be licensors is: How do I find a licensee? My normal response is: Do your homework; in other words, research. Unless the product fits into a niche market, the potential licensor must find who the logical, financially stable, corporations are, and learn everything there is to know about them, including their five- or ten-year stock value, their marketing procedures, the stability of their officers, who serves on the board, to name a few research areas. All of this information is available, but requires intensive research. In many cases, the "number two" company in a given field will find new licensable technology of greater value, so they can gain an edge on "number one," who is also their greatest competitor.

The research objective is to compile a list of potential licensees and to prioritize them based on their potential value. Large corporations quite often do not seek or have any interest in acquiring technology from outside their own extensive research laboratories. It also is extremely important for the potential licensor to choose wisely as to who opens the door and presents the licensing opportunity. Inventors most often are ignored, and must sign release documents before ever having an audience with a company official. Here, again, having a competent licensing/legal professional will go a long way to the eventual success of the endeavor.

The business of licensing is very serious, and must be approached and recognized as an opportunity with great rewards if handled properly and professionally. There are experts in this field, even to the point of specific technology categories. Contact the Licensing Executives Society, 1800 Diagonal Road, Alexandria, VA 22314 for a copy of their Licensing Consultants & Brokers Directory, [www.usa-canada.les.org](http://www.usa-canada.les.org).

## Valuation of the Idea

Another question that I am asked frequently is: What is my idea or technology worth? Establishing a value consists of a myriad of factors. In general, a license royalty should not be so high that it either discourages a potential licensee, or reduces the profit

margin of their expected returns on the investment. Remember, "they" are taking the risks, which balances to their receiving the largest percentage or portion of the profits.

Royalties commonly are expressed as a percentage of the licensee's "net sales price" of the licensed product. They also can be expressed as an equivalent thereto, such as \$2.00 per ton of paper product under a license on a paper machine. A very important factor that will influence the royalty rate is the strength and scope of the patent protection, and the additional values such as a trademark. Another is the stage of the development, such as, how much money must be invested in more research to determine the finished product?

The royalty also can vary depending on the grant of an exclusive or nonexclusive license. What, if any, are the geographic limitations and parameters? Does the agreement cover US rights only, or the whole world? What are the licensee's competitors going to do when "your" new technology is introduced? Are they capable of improving it and avoiding any infringement suit? Will they consider a sublicense from your licensee, instead of creating a competitive technology situation? These are only a few of the questions that have to be answered, not even considering the value of the market today, and in the future.

## Conclusion

Licensing may or may not be for you. My recommendation is to read several books on the subject, discuss it with your attorney and advisors, and recognize honestly, what do you want from your brain-child? Your invention/innovation/patent is of absolutely no value until someone wants to pay for it, or for its use. Likewise, a "successful inventor" is only considered having attained that unique status by having earned more money than he or she expended on the idea or patent. Over the last 60 years that I have been assisting inventors, out of the literally thousands I have spoken to, or helped in one way or another, only a handful have truly reached the plateau of independent wealth.

This is not meant to discourage the reader, but to bring the world of reality to your forefront. I can balance it by stating the opportunities to become rich with your idea/patent are far greater today than at any time in history. That is because the world is hungry for new products and devours them at the rate of more than 20,000 a year. Many do not have any protection, except being "the firstest with the mostest."

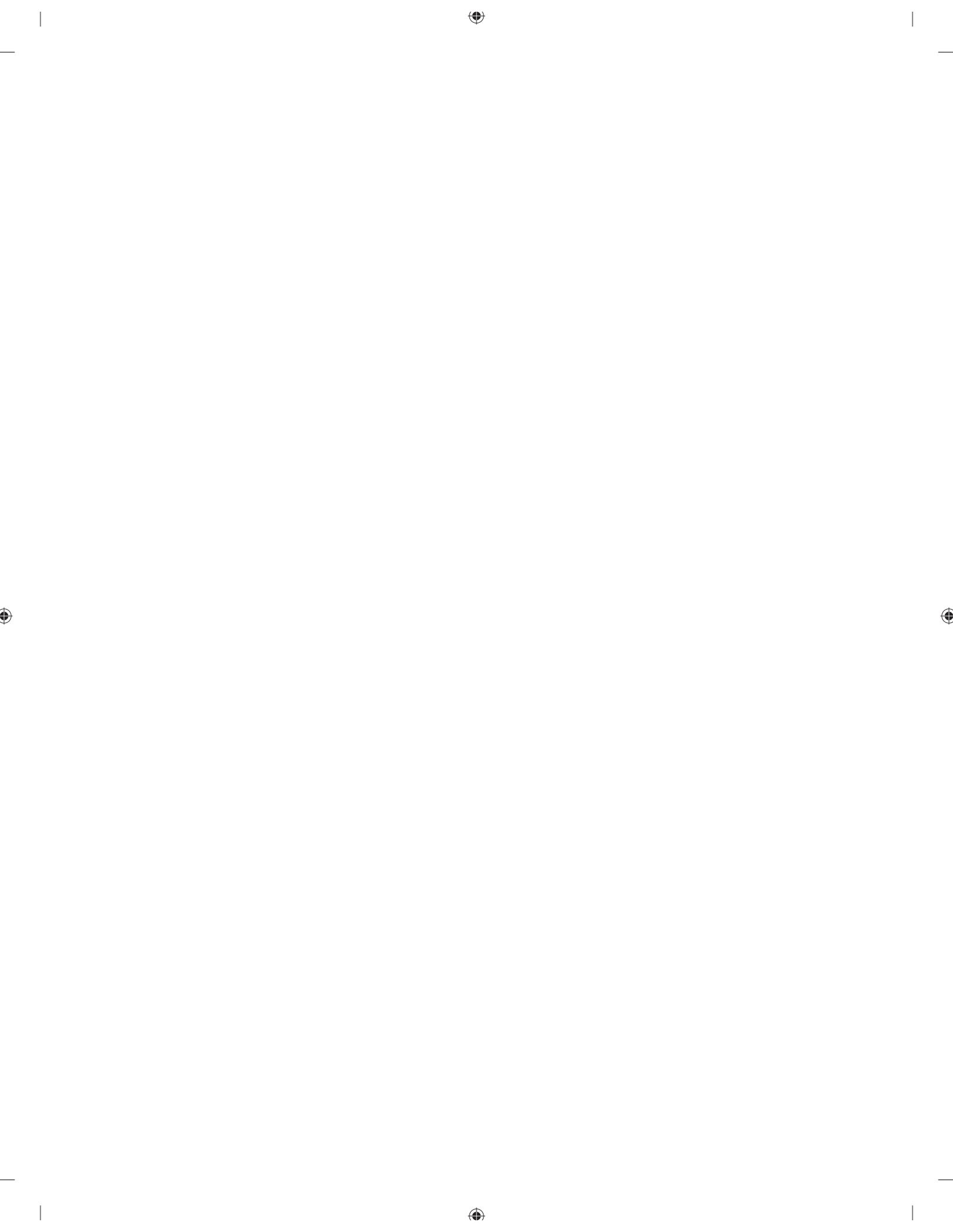
In summation, licensing can be the most opportune and personally profitable way to go with what

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you have, however, it is not necessarily the easiest. It is not what the property owner thinks it is worth that is important. The criterion is, and always will be, how much is someone willing to pay for it? A further question that needs to be addressed is does the licensee have the resources to make the idea successful, and recognize that you want to help

them do so in any way possible, and not be known as “a greedy and crazy inventor.”

**THE CHOICE IS YOURS.** Wake up to the world of reality and start earning money from your creative efforts, be very cautious of invention promotion firms where you have to pay up front for services, and be proud to be an American inventor.





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