

The other issues in a license agreement

1. *Effective Date*

Where foreign government approvals are required for a license agreement, the licensor's position will be protected by a condition precedent providing that the license will not come into effect until the license is approved in the form agreed between the parties. In this case, the licensor will not have lost his bargaining position in the event that changes are required in the license agreement, which favor the licensee.

2. *Recitals*

Properly drafted recitals are very useful for explaining the context and background of the license, and may assist in the interpretation of the Agreement.

3. *Sub-license*

The licensee, particularly an exclusive license, may wish to have the right to grant sub-licenses in its territory. If so, this needs to be specifically negotiated and stated in the agreement.

- To whom Licensee may sublicense
- What rights are sublicenseable and where
- What level of control Licensor wants over sublicensees
- Whether prior written approval of the Licensor is required for granting of any sub-licenses, the choice of a sub-licensee, and the conditions upon which such sub-licenses may be granted; for example, the extent to which the terms of the sub-license should accord with those of the head license agreement.
- Whether or not the sub-license comes to an end when the head license is terminated or expires for any reason.

4. *Improvements*

When dealing with improvements, also known as versions, enhancements, and new models, it is important to define what is an improvement and, therefore, covered by the license, and what is a new technology or new intellectual property.

5. Most Favored Licensee

Where the license is non exclusive, the licensee may wish to include in the agreement a most favored licensee clause which in effect ensures that in the event that the licensor grants another licensee terms that are more favorable, then, by virtue of this clause, the present licensee would be entitled to terms as favorable as had been granted to the other licensee. In granting such a provision there should be clarity as to what is meant by “more favorable terms”.

6. Best efforts

A paragraph stating that the licensee will use its best efforts to exploit the licensed technology is common in both exclusive and non-exclusive licenses. It would be desirable for the parties to agree on the meaning of best efforts, and what may constitute best efforts in terms of specific steps to be taken by the licensee.

7. Transferability of Rights

A provision typically used in a license agreement states that the license shall ensure to the benefit of and be binding on the successors, assigns or other legal representatives of the parties. It is to be noted, however, that use of language of this type is uncertain in terms of its effect and could perhaps be in conflict with other provisions of the agreement that attempt to specify the assignability or lack of assignability of the license granted and the rights pertaining thereto.

8. Royalty Stacking

The concept of royalty stacking arises from the risk that multiple patents may affect a single product. Royalty stacking arises when, in order to take a product to market, the developer of the product takes licences from all of the owners of the patents which affect the final product. When the royalty payments are added together, the licensee may find itself with a non-profitable product.

Hence it has become quite usual for licensees to insist on including anti-stacking provisions in licence agreements. A typical anti-stacking provision states that the royalty rate payable to the licensor will be reduced if the licensee is obliged to enter into licences with third parties in relation to the product. Such a provision can lead to a disparity between the expectations of the licensor as to the royalty it will receive from the licensee and the actual royalty the licensee is contractually obliged to pay.

9. Restrictions on payments under local law?

The issue of exchange control restrictions and other local regulations that may affect the transfer of funds and therefore the remittance of royalties should be addressed by the parties and suitable solution be found at the time of the negotiation.

10. Inflation

The issue of inflation is effectively provided for where the royalty rate is expressed as a percentage of sales. Where, however, the royalty is a specific amount in a specified currency, it is usually reviewed regularly, say, annually or every two years, and adjusted, if the national law so permits, in accordance with an agreed consumer, manufacturing or other local index. Adjustments can also be made to lump sums payable on the happening of an event where, in particular, the occurrence of the event is distant and uncertain.

11. Financial Administration

The financial administration provisions of the license agreement include obligations on the licensee to keep accounts and records, to report the results and pay the consequent royalties. The royalty reports, which might be required once, twice, or four times a year, might need to be certified by the licensee's chief financial officer or auditor.

12. Infringement

When all or part of the technology has the benefit of patent or other intellectual property protection, it is important to provide for what will happen if there is any infringement. There are two situations where infringement could occur.

The first infringement situation

The first is where a third party is using the protected technology but does not have a license. Here the licensee is facing competition and is likely to be at a financial disadvantage as the infringing competitor is not paying royalties.

The second infringement situation

The second infringement situation is where a third party claims that the licensee is using technology in respect of which the third party has obtained protection. In this situation, the licensee may be faced with the prospect of

not being able to continue to use all or some part of the licensed technology.

13. Product Liability

Product liability can have important financial consequences. The risk is that there might be injury or damage, to person or property, arising from a licensed product that is defective. The need is to identify the source of a potential defect and to assign responsibility accordingly.

14. Representations and Warranties

Representations and warranties are statements or assurances about a matter or position relevant to the license agreement. One important distinction is that a representation is not usually a term of the agreement, whereas a warranty is a contractual term, the breach of which could entitle the injured party to terminate the agreement and sue for damages. A warranty is an assurance or promise in a contract, the breach of which may give rise to a claim for damages. It is essentially a minor term of a contract.

While there are no restrictions on what might be the subject of a representation or warranty, typical examples include:

- the licensor owns the technology and has the right and authority to grant the license;
- that the licensed material (e.g. text, software, and/or documentation) is original and has not been copied;
- to the best of the licensor's knowledge and belief, the licensed patents are valid and are not being infringed by any third party.

15. Licensor and Licensee Obligations

The licensor is expected to take, for example, in a patent and know how agreement, all necessary action to transfer the technology and assist the licensee to commence commercial production. Similarly, the licensee is expected to successfully manufacture and market the licensed product in the territory.

16. Taxes

It should be made clear in the Agreement who is to absorb and pay relevant taxes, including any applicable sales, customs and excise, or withholding taxes. Withholding taxes are of particular concern in international licensing

arrangements. If one party is obligated to assume responsibility for withholding taxes, the Agreement usually includes a provision which requires the other party to provide reasonable assistance in respect of any possible refunds.

17. Waiver

A waiver clause in a license agreement means that a party does not lose its rights because it does not enforce those rights. Thus, if a licensor was entitled to give notice of termination due to nonpayment of royalties, but overlooked or ignored the breach, the licensor could still give notice in respect of another breach of that obligation. The waiver clause in effect prevents the application of the legal concept of estoppel, i.e. the earlier tolerance or oversight does not prevent the licensor from subsequently enforcing its rights.

18. Force Majeure

A force majeure clause in a license agreement addresses intervening circumstances beyond the control of a party, which prevent that party from carrying out its obligations. War, strikes and fire are the types of occurrences envisaged, and the benefit of the clause is that the time to carry out an obligation may be delayed until the *force majeure* circumstance ceases or is removed.

19. Anti-competitive Practices

When entering into a licensing agreement it is important to keep in mind that if certain business practices are incorporated, the agreement may, depending on the national laws of the country or countries in question, be considered illegal if tantamount to being anti-competitive. Some examples of practices that may be considered unlawful depending on the particular circumstances of the agreement are obliging a licensee to accept certain products or services in addition to the proprietary technology (tie-in, bundling), prohibiting the licensee from dealing with certain enterprises, attempting to fix the prices of products incorporating the licensed technology, territorial restrictions, cross licensing and patent pooling.

20. Government Regulations

When considering entering into a licensing agreement with a foreign partner it is important to verify the existence of various government regulations that may affect it. For example, most countries would at least require the registration of a licensing agreement with the relevant authorities in that country but there may, in


addition, be an approval process that must be followed for engaging in that kind of activity in that country. In the licensor's own country there may be regulations that restrict or make conditional the dealing with certain technologies for security or other reasons.

21. Disputes

When negotiating the license agreement, parties should be aware that disputes might arise and provide means for resolving them. Built in flexibility for amendments should provide means for resolution at first resort. Failing which, mechanisms for dispute resolution must be provided for. When drafting dispute resolution clauses, parties can draw from several options. Traditionally, parties have often agreed to resolve disputes through litigation in a specified domestic court. Increasingly, however, parties opt for alternative dispute resolution (ADR) procedures, such as arbitration and mediation, or mediation followed by arbitration.

Advantages of ADR procedures

- *A single procedure.* Through ADR procedures, the parties can agree to resolve in a single procedure a dispute involving intellectual property rights that are protected in a number of different countries, thereby avoiding the expense and complexity of multi-jurisdictional litigation, and the risk of inconsistent results.
- *Party autonomy.* Because of its private nature, ADR procedures afford parties the opportunity to exercise greater control over the way their dispute is resolved than would be the case in court litigation.
- *Neutrality.* ADR procedures can be neutral to the law, language and institutional culture of the parties, thereby avoiding any home court advantage that one of the parties may enjoy in court-based litigation, where familiarity with the applicable law and local processes can offer significant strategic advantages.
- *Confidentiality.* ADR proceedings are private. Accordingly, the parties can agree to keep the proceedings and any results confidential. This allows them to focus on the merits of the dispute without concern about its public impact, and may be of special importance where commercial reputations and trade secrets are involved.

 *Finality and enforceability of arbitral awards.* Unlike court decisions, which can generally be contested through one or more rounds of litigation, arbitral awards are not normally subject to appeal.

22. Indemnities

Generally, an indemnity is an undertaking by one person to meet a specific potential legal liability of another. An indemnity entitles the person indemnified to a payment if the event giving rise to the indemnity takes place. Unlike a claim for breach of warranty there is no need for the indemnified party to establish that he has suffered loss.

23. Release

If a license is being entered into as part of a settlement to infringement proceedings, it may be necessary to include in the grant section a release against infringement that was alleged to occur prior to the date of the Agreement. Although most properly drafted grant provisions will make it clear that the rights granted to the licensee are conditional upon the licensee's compliance with its obligations under the Agreement, this is particularly important in a release-type grant if the licensor intends to retain the right to recover damages for the past infringements upon any future breach by the licensee of the Agreement. This would likely only apply where specific consideration for the release has not been provided.