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Intellectual Property Licensing and Collaborations: Best Practice and Common Pitfalls

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Introduction

The purpose of this article is to look at best practice, from a lawyer's perspective, in the negotiation of IP licences and collaboration agreements as well at some of the pitfalls that arise in these situations. We will begin by looking at the deal making process and continue by considering some of the most important components of initial documents such as NDAs and term sheets as well as some of the issues that arise in technology licence agreements. We will go on to examine the advantages and disadvantages of the joint ownership of intellectual property in collaboration agreements and conclude with some thoughts about governing law and jurisdiction clauses.

For the most part, we will consider these matters in the context of patent rights because patent rights bring into play issues that do not arise in relation to other types of IP. However, much of what we have to say applies to those other types of IP as well.

Since the authors are English solicitors, the perspective is inevitably a UK and European one. However, we believe that most, if not all of the matters raised are of general application.

The Deal Making Process

Deals come together in many different ways and it would be wrong to suggest that there is only one satisfactory process. However, here is a process that, in our view, ticks all the necessary boxes:

1. *Ensure that a satisfactory Non-Disclosure Agreement is in place before any meaningful negotiations take place.*

   NDAs are so common that they are sometimes seen as a formality that can be addressed after negotiations have commenced. It hopefully goes without saying that this is unwise, particularly if a party has not yet applied for registered protection of its idea or design or if it owns know-how that is incapable of protection through registration. A party will not wish to have to argue that its registered rights are valid or its unregistered rights infringed because it disclosed the relevant information to its prospective licensee under an implied duty of confidence.
2. *Involve specialist counsel at an early stage*

   We appreciate that this recommendation looks like self-interest but it really is not. Indeed, following this recommendation could save a considerable amount of time and expense in the long run, notably if the deal that a party proposes cannot lawfully be achieved or if it gives rises to complexities that the parties may not yet have considered.

   Competition or anti-trust laws are the most likely reason why a deal might present lawfulness issues and we will look briefly at some relevant aspects of EU competition law later on in this article.

   Agreeing the joint ownership of IP arising from a collaboration does not usually give rise to lawfulness issues but it does have consequences which many clients do not appreciate. Being aware of these consequences at an early stage of the negotiations and hence being able to address them in the initial formulation of the deal is likely to save management time (and legal expense) later on and may even sometimes prevent the deal collapsing altogether.

3. *Agree non-binding heads of terms/a non-binding term-sheet*

The parties to a proposed licence or collaboration agreement are sometimes tempted to try to negotiate a multi-page licence or collaboration agreement having only agreed the barest outline of the commercial agreement. This will prove to be a mistake if the detailed negotiations make it clear that the parties had rather different ideas as to how that outline would be worked up into a complete agreement. The result is likely to be, at best, increased time and legal expense spent in the negotiations and, at worst, the collapse of the proposed deal with the consequent wasted time and cost.

Agreeing non-binding heads of terms covering all of the fundamental commercial points before instructing counsel to prepare a full agreement should enable these issues to be avoided.

NDAs—Best Practice

- *Onward disclosure of information*

Many, if not most NDAs permit a recipient of information to disclose that information onwards to a relatively wide group of people if those people reasonably need to know the information for the purposes of the discussions and negotiations. Disclosure to the recipient's affiliates is almost always permitted.

A couple of issues arise from this. Firstly, it is a truism that the more widely a piece of confidential information is known, the less likely it is to remain confidential for long. Depending upon the terms of the NDA, the proprietor of the information may have a remedy for unauthorized disclosure against the original recipient but this may be of little consolation if what was once valuable information is now generally available to the public.

Secondly, there is risk in permitting carte blanche disclosure to the recipient's affiliates if the recipient is part of an extensive corporate group. Unless the discloser of the information is satisfied that it has accurately identified every member of the recipient's group (taking into account that the definition of affiliate in the NDA may be wider than the usual legal definition) there may be a risk of information ending up in unforeseen hands. Those hands could be the hands of a competitor or perhaps an overseas subsidiary with a suspect reputation.

Of course, in a group structure, the original recipient may well need to share the information received with an affiliate that would also need to be involved in the project. It would, however, be an unusual situation where more than one or two additional entities would need to be involved and these could easily be identified in the NDA rather than permitting a blanket disclosure to affiliates.

- *Length of confidentiality obligations*

The period during which information must be confidential under an NDA varies widely. Some NDAs prescribe a relatively short period such as one year from disclosure or the termination of discussions. At the other extreme, some NDAs require the recipient to keep confidential the information it receives for as long the information remains out of the public domain.

This is a point that really needs to be considered in every particular situation in which the NDA is used because while, in principle, an NDA really ought to protect confidential information for as long as it remains, in fact, confidential, the risk of an inadvertent breach of the agreement by the recipient will undoubtedly increase as the years go by. The compromise is often a confidentiality period of between 2 and 5 years.

A confidentiality period of this type is often sufficient to protect the discloser's interests. However, it will be inadequate if the discussions between the parties will involve one of the parties disclosing secret know-how which is fundamental to its business and which is not protected by any other intellectual property.

Some NDAs seek to address this point by distinguishing between trade secrets (protected for as long as they remain secret) and other types of confidential information (protected for a fixed 2–5 year period). However, while this arrangement may work in some jurisdictions, it will probably not work in others including the UK.

- *Don't forget about signed NDAs*

While some NDAs require information to be marked as confidential if it is to be treated as such under the NDA, this is certainly not universal and very few prescribe a procedure for recording what has been disclosed and received or for challenging the confidential nature of a disclosure.

It is understandable that parties do not wish to burden their pre-contract discussions with unnecessarily bureaucratic processes but, whether or not the NDA prescribes these, it is essential to keep a careful record of what is disclosed and received in case a dispute does arise at some point. In addition, if allegedly confidential information is received which the recipient knows or believe is in the public domain or otherwise not confidential under the terms of the NDA, the recipient should consider whether to raise this with the discloser at the time and, in any event, ensure that a clear note of its findings (together with supporting evidence) is retained on its files.

Finally, it is good practice (and one not universally observed) to require the return or destruction of confidential information on the termination of discussions and a well-drawn NDA should properly provide for this including the slightly tricky issue of dealing with the erasure of electronic files.

IPR Licensing—Some Pitfalls

Competition Law

One reason why we recommend involving specialist legal counsel at an early stage of a deal negotiation is because of the risk that the proposed deal may not work (*i.e.*, be lawful) for some reason or, at least, may not work as the parties envisage. In agreements covering any part of the EU, the most likely reason for this is EU competition law where the consequences of unlawfulness are unenforceability of the agreement and, potentially, fines.

Article 101(1) of the Treaty of Rome outlaws "agreements between undertakings……..which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition…………..". Technology licences are clearly capable of falling within Article 101(1). However, most licences should be capable of benefitting from the general exemption granted by what is usually referred to as the Technology Transfer Block Exemption Regulation (TTBER).[1]

In order to do so, however, the combined market share of the parties must fall below the prescribed thresholds and no "hardcore" restrictions must be included in the agreement. The proposed deal will need close examination at the earliest possible stage if, for example:

- the parties are competitors and their combined market share exceeds 20%
- the parties are not competitors and their combined market share exceeds 30%
- the deal includes any "hardcore" restriction such as one preventing a party from determining its prices when selling products to third parties or the allocation of customers or markets (*i.e.*, exclusivity arrangements) other than as specifically permitted by the TTBER.

It is reasonably straightforward to determine whether a proposed term of a deal comprises a "hardcore" restriction. Determining whether or not the parties' share of the relevant product or technology market falls below the relevant threshold is much more difficult given the need to determine what other products or technologies would be considered substitutable for the product or technology included in the proposed licence.

It is worth noting that if the TTBER does not apply, this does not automatically mean that the technology licence agreement will be presumed to be unlawful. It is just that the agreement will need to be individually assessed to see whether it is restrictive of competition under Article 101(1) and, if so, whether there are any countervailing benefits of the agreement that could exempt it from unlawfulness under Article 101(3). Of course, if the agreement includes restrictions that are labelled "hardcore" in the TTBER, it is highly unlikely that such an analysis will lead to a finding of lawfulness.

Exclusivity

Many licensing deals would not be concluded without the grant of some degree of exclusivity to the licensee. The situation that the licensor needs to avoid in this situation is one in which the licensee underperforms but the licensor cannot bring the licence to an end.

Typically, an exclusive licence seeks to address this problem in two ways. Firstly, it requires the licensee to use its best or reasonable endeavors/ efforts to exploit the licensed technology or property as widely as possible and to meet all reasonable customer demand for the licensed product in the licensed territory. Secondly, the licensee is required to pay a minimum royalty in order to keep the licence in place.

Neither of these is necessarily a panacea for the following reasons:

- Endeavors/ efforts obligations

  Under English law, a "best" endeavors/ efforts obligation, while not being an absolute obligation, is an onerous one because it could require the licensee to apply its resources to the achievement of the object of the obligation—for example, meeting all reasonable customer demand for the licensed product—without having regard to the competing needs of its business[2]. The inclusion of such an obligation could, therefore, be of real assistance to a licensor in dealing with an under-performing licensee.

However, because a "best" endeavors obligation is such an onerous one, it is rarely given in this context, at least by a properly advised licensee, and is generally watered down to "reasonable" or "all reasonable". The watered-down obligation should still assist the licensor in dealing with a licensee who is doing nothing, or next to nothing, to try to exploit the licensed technology or property. In any other circumstances, however, it may be difficult for the licensor to prove a breach since, in determining whether the licensee is using its reasonable endeavors/efforts, any other calls on the licensee's resources must be taken into account[3].

- Minimum Royalties

A minimum royalty obligation is usually the best way of ensuring a degree of performance by the licensee but, whether it achieves precisely what the licensor is looking for will depend upon a number of factors including, of course, the level of minimum royalty that is agreed. In many situations, there will be a large amount of guesswork in predicting the sales and profits that a diligent licensee will achieve and it sometimes turns out that the licensee can achieve the minimum royalty while still leaving a large part of the potential market untapped.

Careful consideration also needs to be given to the consequences of the licensee not achieving sales sufficient to generate the minimum royalty. For example, should the licensee be able to avoid termination in these circumstances by making up the shortfall between the earned royalties and the minimum or should the licensor be able to terminate the agreement in any event? If the minimum royalty was set at the bottom end of the parties' expectations, a licensor will probably not wish to settle for the payment of that sum for, say, the 20 year life of a patent.

Looking at this situation from the other perspective, it is rare, in our experience, for the licensee to be given any termination rights when earned royalties are below the minimum royalty level. Yet, if this is the situation and it continues for more than a year or two despite the licensee's best efforts to market and sell the licensed products, then the licensee may be as, if not more, concerned than the licensor about the agreement continuing for many further years. The licensee should, therefore, at least consider seeking to negotiate a reciprocal termination right to cover this situation.

Royalties on Expired Patents

It is not uncommon for a licence agreement to be drafted so that royalties are payable on the sale or supply of products falling within the scope of the licensed patents without specific regard to whether or not the relevant patents are in force.

If there is only a single licensed patent or patent family and the agreement terminates, as would often be the case, upon the expiry of the last to expire of the licensed patents, this may not be a problem. However, in other situations—for example, where two or more patent families are included in the licence—this could result in royalties being payable in respect of the use of patents that have expired or been revoked. This plainly puts the licensee at a potential competitive disadvantage with regard to other parties entering the market.

Some competition or anti-trust laws prohibit the imposition of an obligation to pay royalties once the relevant patents have ceased to be in force. This is not, however, so in the EU where the EU Commission has made it clear, in its Guidelines accompanying the TTBER, that "the parties can normally agree to extend royalty obligations beyond the period of validity of the licensed intellectual property rights without falling foul of Article 101(1) of the Treaty"[4]. Since third parties can compete, at this point in time, with the parties to the licence agreement, there will generally be no need for competition law to step in to protect the licensee from the competitive disadvantage that it may sustain as a result of having to continue paying royalties.

On the basis of a judgment of the European Court of Justice some thirty years ago, it has been suggested that a royalty obligation continuing beyond the expiry of the relevant licensed patent may be unlawful if the licensee has no right to terminate the agreement in such circumstances[5]. However, it would be unwise for a licensee to rely on this. Rather, it should ensure that the licence agreement is drafted so that royalties cease if the relevant patents expire or are revoked.

Improvements

European competition law is less laissez faire when it comes to licensors seeking to take ownership (or an exclusive licence) of a licensee's improvements to its licensed technology. These are restrictions on competition that are excluded from the exemption granted by the TTBER and are likely to be considered unlawful and hence unenforceable[6].

As a result, it would be unusual to come across an EU technology licence agreement containing any such provision. Until recently, on the other hand, it would be common to see agreements in which licensor improvements were automatically included in the licence and the licensee agreed to give the licensor a perpetual, non-exclusive, royalty-free licence over its improvements (subject, of course, to any exclusivity granted to the licensee by the agreement).

The automatic licensing of improvements may, depending upon the circumstances, be an important part of the licensing deal for one or both of the parties. These arrangements are definitely not, however, ones that should be included in an agreement without careful consideration and careful drafting. In particular, the potential disadvantages to a licensee of granting a royalty-free licence continuing beyond the period of the licence agreement are obvious, all the more so when you factor in the possibility of an early revocation of the licensor's own patents.

Dealing with Infringers

Unrestrained third party infringement is clearly a potential issue for both licensor and licensee but may be disastrous for a licensee faced with a major encroachment on its market and a continuing obligation to pay minimum royalties. That part of a licence agreement dealing with the parties' respective rights and obligations in the case of an infringement is accordingly one of the most important parts of the agreement but is a section which, in our experience, is not always given the careful consideration that it deserves.

There are a number of different ways in which the infringement issue could be addressed but many of them are unlikely to be acceptable to one or other of the parties. For example, a licensor is unlikely to accept an obligation to take action against *any* infringers or to give the licensee a "royalty holiday" unless and until a material infringement is restrained. On the other hand, it would usually be unwise of a licensee, certainly an exclusive licensee, to leave it to the discretion of the licensor as to whether any action should be taken against an infringer.

Probably the most common approach, at least in an exclusive licence, is for the licensor to have the option to take action against an infringer but for the licensee to have the right to do so, using the licensor's name if necessary, if the licensor declines. That right is usually given upon the basis that the licensee will indemnify the licensor against any legal costs or damages awarded against the licensor as a result and is sometimes subject to the licensee providing security in support of that indemnity.

Generally, this seems to be a sensible way of dealing with the infringement scenario. However, there is a major, potential downside for the licensor arising from the fact that an action for the infringement of a registered IPR is often (and, in the case of patents, almost always) met with a counter-claim for revocation of the registered right. Furthermore, actions for infringement of patent rights are notoriously expensive.

If, therefore, the alleged infringement is not clear-cut, the chances of a successful revocation counter-claim are significant and/or the alleged infringer has deep pockets, the licensor may well have good reason not to exercise its primary right to embark on infringement proceedings. But the considerations for the licensee may be quite different. In particular, if the infringing activity is having a significantly prejudicial effect on its business, it may consider that it has no option but to proceed even if the chances of success are relatively low and those of having the licensed IPRs revoked are relatively high.

The licensor can seek to mitigate these risks by negotiating provisions which, for example, require the licensee to obtain a favorable counsel's opinion before proceeding, to consult with the licensor at every material stage in the action and to obtain the licensor's approval of any settlement. However, for the reasons mentioned in the previous paragraph, the licensee may want the right to proceed against infringers even if the prospects of success are not that high. There is a difficult balancing act here between the interests of parties whose interests, when faced with an apparent infringement, may not always be aligned and a satisfactory outcome may be as much about the relationship between the parties as anything that can be written into their agreement.

Collaboration Agreements

Collaboration agreements are a common way to tap into external expertise to supplement and accelerate internal research. Typically, collaborations happen between two commercial entities with differing expertise, or between a commercial entity and an academic institution, with the academic institution contributing its research capabilities and the company providing funding and ultimately hoping to take the end product to market. Not only does a collaboration grant access to external expertise, but it also allows parties to share risk and often to achieve results at a reduced cost.

Best practice for seeking to negotiate and agree the terms of a collaboration is the same as with a licensing deal. The parties should enter into an NDA before disclosing any confidential information, and should seek to agree non-binding heads of terms covering the key points of the deal.

In essence, these points can be broken down into two categories: (i) what will the parties contribute to the deal; and (ii) what will they get out of the deal?

Most readers will be familiar with the terms Background IP and Foreground IP. Background IP is the IP that each party owns before the deal; whereas Foreground IP is the new IP generated by the parties during the collaboration.

In terms of contribution to the collaboration, parties will need to consider what:

- Background IP they will bring into the collaboration;
- financial contributions will be made; and
- other resources, in terms of manpower, equipment and materials will be provided.

What the parties will get out of the collaboration tends to be where more of the issues lie. The parties will need carefully to consider how the Foreground IP is to be owned, who will have the right to exploit it, and in what way? Given that the Foreground IP has been generated through collaboration, it is natural to think that it should be jointly owned.

Joint Ownership of Foreground IPRs—Pitfalls and Solutions

When it comes to joint ownership of IPRs, it is often the case that clients love it and lawyers hate it. Some lawyers say never have joint ownership of IPRs because it's too complicated. And it is complicated. The alternative is that one party owns the Foreground IP, with the other party being granted a licence to use that IP. With the correct drafting, this resolves the issues that can be caused by joint IPRs ownership. However, as stated above, joint IPR ownership is an obvious outcome where parties are collaborating equally—that is, the research has not simply been paid for, or the research and development has not been asymmetrical.

Joint ownership of IPRs occurs either where: i) there are no provisions dealing with Foreground IP ownership and the work is jointly developed but the parties' contributions to the final work cannot be ascertained; or ii) the parties specifically agree to joint ownership.

Lawyers often roll their eyes at proposal of jointly owned IP, because if you have it without an agreement, it is potentially very problematical and, if you do have an agreement, you need to agree and be clear on a number of issues.

Importantly, the agreement must address:

- Who decides on the patent filing strategy and has conduct of the applications? What procedures will be put in place to ensure the other party can have input on the strategy and what kind of input should that be?
- Who can do what in terms of exploitation? In absence of agreement:
    - Each party can work under a UK patent, for example, but neither party can grant licences without the other party's consent; and
    - Neither party can exploit UK copyright
- How will the parties deal with any infringement situations? The same kind of issues occur as discussed with regards to patent licensing, but it may be even harder to decide who should have the ultimate say.
- Whether there should be restrictions on a party's ability to transfer or otherwise deal with its share of the Foreground IP?

Collaboration Agreements—Possible Pitfalls

Negotiating and drafting collaboration agreements can be rife with pitfalls. Some of the most common, and dangerous, relate to Background IP. First it is important to consider whether the content of the parties' respective Background IP should be defined in schedules rather than covered by general wording such as "Background IP means all IPRs owned by the parties prior to entering into the agreement". This unspecific approach can causes problems, as it sometimes makes identifying the Foreground IP much more difficult, and can also lead to unwittingly granting licences which are much broader than intended.

When being granted a licence of the other party's Background IP, it is important to consider whether a commercial exploitation licence is required, as many precedent agreements do not include this, even in the scenarios where one party has paid for the research and development work to be conducted. In many scenarios, such a licence will be necessary in order to exploit the Foreground IP.

It is also quite common for parties to grant an option, rather than an automatic exploitation licence of the Foreground IP. In this scenario, parties often agree that such licence will be granted on fair and reasonable terms, to be agreed between the parties. Wherever possible, this is best avoided, as agreeing the value of the licence may prove difficult. It is preferable to agree the specific terms of the exploitation licence at the time of entering into the agreement, but if that is not possible, then it is best to ensure that the agreement contains robust dispute resolution provisions which can be escalated to expert determination if the parties cannot reach agreement.

Finally, when entering into collaborations with academic institutions, there can be a tension between the desires of the parties. Academic institutions are focused on research, teaching and publications. The latter tends to be at odds with commercial entities, which are concerned with generating, protecting and exploiting valuable IP. Striking the balance between the desire to publish and the need to secure patent protection for inventions can be tricky, and is best dealt with carefully and expressly in the agreement. It is also worth noting that, in the UK, the Lambert template provisions[7], whilst not perfect, make a good starting point for these types of collaborations, recognizing the need to balance academic priorities with commercial partner concerns.

Governing Law and Jurisdiction

One of the final and most important provisions in any agreement is the clause that defines which country's laws will govern the agreement and how any disputes between the parties will be resolved.

Where the parties to the agreement are located in different countries, it is inevitable that each party will want the agreement to be governed by the laws with which it, or its lawyers, are familiar. Once that argument has been resolved, the default position is to give jurisdiction to the courts of the same country as the governing law.

There are obviously convenience and, possibly, costs advantages in this arrangement, at least for the party that prevailed in the negotiation on this point, but, as with so much else in contract negotiation, the default position should not be adopted without thought. A party may feel comforted to know that it can only be sued in the courts of its own country but what if it's the party pursuing the claim? If it obtains a judgment against the other party, how easy will it be to enforce that judgment in the country of the other party?

The answer is that it depends on the countries involved and the type of judgment that is to be enforced. For example, while international conventions such as Brussels[8] make enforcement of most judgments within the EU and certain other European countries pretty straightforward, extra-territorial enforcement between other countries is not so straightforward. For example, judgments obtained in the UK are generally not so easily enforced in the US or China, and vice versa.

Thanks to the New York Arbitration Convention[9], the same difficulties do not attend the enforcement of arbitration awards. As a result, parties to contracts involving, say, the UK and the US should consider whether arbitration would be a preferable alternative to giving jurisdiction over disputes to the courts of either country, always taking into account, of course, the other pros and cons of two types of forum.

A Final Thought

In this article, we have given some pointers as to what we consider "best practice" in the negotiation of IP licensing and collaboration agreements and have tried to highlight some of the issues that can arise from provisions that are commonly found in, or proposed for, such agreements.

We make no apology for not offering any definitive solutions to such issues because the correct solution will always depend on the precise circumstance of the deal and the parties. All of the key clauses in an agreement—and even many of the so-called "boilerplate" provisions—should be tested, in each case, for relevance and appropriateness against the party's needs and objectives. If there is one over-arching "best practice" guideline, it is probably not to assume that a "default" provision included in a precedent or used successfully in previous deals will be the right provision for the current deal.

1. Commission Regulation (EU) No 316/2014 of 21 March 2014 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements.
2. *See*, for example, the discussion of a "best endeavours" obligation in *Jet2.com Ltd v Blackpool Airport Ltd.* [2012] EWCA Civ 417, particularly the comments of Moore-Bick LJ at para. 32.
3. *See*, for example, *UBH (Mechanical Services) v Standard Life Assurance Co* [1986] 11 WLUK 70.
4. Communication from the Commission—Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements. 2014/C 89/03 at para. 187.
5. Judgment of the Court (Sixth Chamber) of 12 May 1989. Kai Ottung v Klee & Weilbach A/S and Thomas Schmidt A/S. Case 320/87.
6. Commission Regulation (EU) No 316/2014 of 21 March 2014 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements, Article 5(1)(a).
7. Available at *https://www.gov.uk/guidance/university-and-business-collaboration-agreements-lambert-toolkit*.
8. 1968 Brussels Convention on jurisdiction and the enforcement of judgments in civil and commercial matters as largely superseded by Council Regulation 44/2001 or Regulation (EU) 1215/2012 of the European Parliament and Council.
9. The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, concluded in 1958.

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