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Negotiating Technology Transaction Agreements

Harris Gao
Sheppard, Mullin, Richter & Hampton, LLP
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Typical Technology Transaction

- Party A provides the Technology to Party B to make the Product.
  - Know-hows
  - Technical Services
  - Components or machines
  - IP: patents and trade secrets
- Party A gets
  - Running royalty
  - Lump sum/milestone payment

Key License Terms

- The License Grant
  - Party A hereby grants Party B an [exclusive or non-exclusive] right to use the <u>Technology</u> to make, use, and sell the <u>Product</u> in the Territory.
- The Consideration
  - Party B shall pay Party A an annual running royalties of ___ percent (x %) of Party B’s net sales of the <u>Product</u>.
  - When Party B’s <u>Product</u> gets on the market, Party B shall pay Party A $___.

The License Grant

- Exclusive, non exclusive or sole (licensor and licensee can operate in the territory)
- Sub licenses
- Field of use - to be used in an identified field, product
- Scope - make, use or sell, offer for sale, import
- Territory
- Improvements

Product

- How the product is defined is of utmost importance.
  - **"Product"** shall mean any product and/or service which constitutes, is based on, incorporates or utilizes, wholly or in part, the Technology.
  - **"Product"** shall mean any product and/or service which is covered by a valid claim of the Patents.
  - **"Product"** shall mean the product designated by the Licensee as Model PV225.

What patent rights do you need?

- Party A provides the Technology to Party B to make the Product.
  - Know-hows
  - Technical Services
  - Components or machines
  - IP: patents and trade secrets
- What you need most is a license on patents covering the Product.
  - Patents covering the components you are buying has no real value to you.

Exclusive v. Non-exclusive

- An exclusive licensee should have the right to bring suit.
- A non-exclusive should have to rely on the patentee to take actions against non-licensed third parties.
  - A third party may be using the technology with no license, and harms the competitiveness of the legitimate licensee.
  - A non exclusive licensee would expect the licensor to take action. If the licensor fails to bring suit licensee should have the right to suspend paying royalties.

Qualcomm License Agreement

- Qualcomm collected $8 billion on license fee last year, and its licensing agreement is the worst ever drafted for the licensee because:
  - The Product is defined as CDMA Subscriber Unit (or CDMA compatible handsets).
  - Qualcomm's patents are embodied primarily in the chips it supplied.
  - The license is non-exclusive, but Apple is not a licensee.

Money, money, money

- Lump sum - payable on the happening of a particular event
- Royalties - recurring payments tied to the use of the technology, commonly based on sales.
- Annual minimum royalty - usually where the license is exclusive and the licensor needs to ensure a regular income.

Lump sum

- Often also called milestone payment.
  - It helps to properly incentive the parties, and share the risks.
  - It is important to provide separate payments for discrete items, particularly technical service.

Royalty Structure

- Running royalties
  - Fixed
  - Sliding
    - Increasing
    - Decreasing
  - Maximum (Cap)
  - Minimum Performance/Milestone Based

Royalty Standards?

- Common belief: there are standards to rely on:
  - E.g., 5% in the semiconductor industry.
  - But industry average royalty rates are “folklore” and suspect as a royalty-rate guide.
  - E.g., “a 5% running royalty for a non-exclusive license helps very little in evaluating an exclusive license on different but related technology.”
- Practical Guidance
  - A 20 to 50 per cent premium may be a reasonable average for an exclusive license

Licensor's Cost?

- Common Brief: royalty is largely based on the cost of the development of the technology.
  - "The research and development costs of developing the TI (Technical Information) are sunken expenses expended by the licensor whether or not the TI is licensed and, therefore, should not be considered by the licensor in arriving at a suitable royalty."
- The licensee's economics, not the licensors, control the royalty determination.

Royalty Setting

- MOST IMPORTANT FACTORS
  - a) the state of the technology, particularly how important it is to the Product,
  - b) the strength of the IP rights (solid v. weak, ease to design around *vel non*), and
  - c) the scope of the IP rights, such as the degree of exclusivity (exclusive v. non-exclusive)

Royalty Setting

- Many other operative clauses in a technology license have economic weight, e.g.
  - Grant-back and grant-forward clauses,
  - payment structures and schedules,
  - MFL clauses,
  - representations and warranties, etc.
- Hence, royalty setting is not the first task in licensing negotiations but the last one — after all the others have fallen into place.

Best Efforts Clause

- “Best efforts” clauses are vague and often offer little protection.
- Use quantitative criteria of performance.
  - Production of 250 Licensed Machines per half year after March 1, 2001 of a quality that conforms with established industry standards
- Specify the consequences if the criteria is not met
  - conversion from exclusive to non-exclusive status
  - termination power.
- Require minimum royalty payments.

Takeaways

- There is no “standard” license terms.
- Knowing what you need, and what you are getting.

Questions?

Harris Gao

+86 21 2321 6007

hgao@smrh.com

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