

**International Conference
Ways and Means of Attracting External
Finance for New Innovative Enterprises
Using Intellectual Property as an Asset in
License Agreements and Joint Ventures**

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› Antitrust › Global Litigation › Intellectual Property

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Overview

1. Licensing IP as a strategic instrument for New Innovative Enterprises
2. Some basic principles on License Agreements
3. Financial terms in License Agreements
4. Joint Ventures based on IP
5. Some thoughts about IP based cooperation with New Innovative Enterprises in CIS countries

1. Licensing IP as a strategic instrument for New Innovative Enterprises

1.1 Why to license patents out?

(i) Patents are often based on basic concepts

- There is a long way to go from the basic concept to a product ready for market
- There may be many fields to apply the patented teaching outside the business of the New Innovative Enterprise (NIE)
- ➔ One or several partners may be needed in order to develop the IP to marketable products

1. Licensing IP as a strategic instrument for New Innovative Enterprises

- (ii) New Innovative Enterprises may focus on research and development rather than commercialization
- Many NIE are strong in research, but they lack the necessary resources and competences for the development and commercialization of products
 - The transformation from a research based enterprise to a company commercializing products often requires a lot of investment and time
 - Focusing on its strengths may save a NIE the financial and human resources needed for further inventions

1. Licensing IP as a strategic instrument for New Innovative Enterprises

- (iii) Optimization of commercialization of a product in a global market
- Only very few companies have an almost global presence
 - Without licensing partners an IP based product may not be commercialized in many parts of the world at all
 - Regional and local know-how is needed for any commercialization of innovative products

1. Licensing IP as a strategic instrument for New Innovative Enterprises

2.2 Licensing Strategies

(i) Crucial points to consider:

- Exclusive, sole or ordinary license (type of license)
- Authorization to grant sublicenses in the case of exclusive or sole licenses
- Which territory? Global, regional or national?
- Subdividing the various fields among several licenses as an important tool of a licensing strategy
- Options to obtain a license

1. Licensing IP as a strategic instrument for New Innovative Enterprises

- (ii) Share of responsibilities between licensor and licensee
 - responsibility for licensed IP (maintenance, defense and enforcement vs. third parties)
 - responsibility for the development and commercialization of a licensed product
 - responsibilities for improvements

2. Some basic principles on License Agreements

2.1 The choice of the right partner

- What are the competences, resources and strengths needed for a successful license relationship?
- Experiences of other licensors with a licensee
- The cultural factor is of crucial importance

2. Some basic principles on License Agreements

2.2 The right structure of a License Agreement

- The communication and cooperation between Licensor and Licensee needs to be institutionalized, e.g. by a Joint Steering Committee
- Regular and substantive reports on the progress in the development of products
- Mechanisms for addressing and resolving disputes
- The right structure on the effects of a termination of the License Agreement

2. Some basic principles on License Agreements

2.3 “The Win-Win”-Approach

- Licensor and Licensee must both continuously be highly motivated to make the project successful
- Never suggest what you would not accept in case you were on the other side
- Taking short term benefit to the detriment of the other side is never a good advice on the long term in a contractual relationship

2. Some basic principles on License Agreements

2.4 Trust is crucial for a successful License Agreement

- During negotiation no “dead bones” should be left in the garden
- If you learn about news (also negative!) which could be relevant for your partner address them
- If you are dissatisfied by the performance of your partner, address the issues early and constructively

3. Financial terms in License Agreements

3.1 Various types of financial compensation for Licensor

- down payment at the execution of the agreement
- milestone payments
- running royalties
- minimum royalties
- fully paid up license through one payment
- option fees
- shares in joint venture based on IP

3. Financial terms in License Agreements

3.2 Financial considerations to determine the value of IP

(i) Investment of the Licensor in the IP

- Investment in the development of the protected technology up to the execution of the License Agreement
- Investment in the IP itself (prosecution costs, maintenance fees, defense, enforcement)

3. Financial terms in License Agreements

(ii) Investment of the Licensee

- What is the expected overall investment of the Licensee in the further development of the technology?
- What is the risk for the Licensee that the development of the technology will fail?
- Will the investment be shared between various Licensees or the Licensor and the Licensee?
- Which further licenses must the Licensee obtain for having the freedom to operate his product?

3. Financial terms in License Agreements

(iii) Value of IP in the market

- Have there been comparable deals in the recent past?
 - Rather difficult to obtain reliable and sufficient information
- Which are the alternatives for the Licensee to obtaining a license?
 - Are there other technologies available?
 - Could the Licensee develop a work around (at which costs)?
 - Does a challenge of the validity of the IP constitute a real alternative for the Licensee?

3. Financial terms in License Agreements

3.3 Down payment

- The longer the way to market, the lower the down payment will be
- The higher the risk for the Licensee that the development of the product will fail, the lower the down payment will be
- High down payments can only be expected for advanced product developments or where the Licensee lacks real alternatives

Advice: Down payment may be split, e.g. based on the results of the evaluation of the technology in a study of superiority

3. Financial terms in License Agreements

3.4 Milestone payments

- (i) Milestone payments for the achievement of progress in the development of the product
 - Broadly used in License Agreements in Life Sciences
 - ratio: Each achievement reduces further the risk for the Licensee that the development will fail
 - Bonus milestones may be paid for specific achievements f. ex. the first turnover above 200 mio US \$

3. Financial terms in License Agreements

- (ii) Milestone payments for the maintenance of a license during the development phase
 - Annual payments during the development phase may constitute an important and constant source of income for a NIE
 - The payments may rise in the course of the time
 - Incentive for the Licensee to speed up the development of the product

3. Financial terms in License Agreements

3.5 Running royalties

- In most cases determined as a percentage of Net Sales
 - Importance of the definition of Net Sales (deductions, sales between affiliated enterprises etc.)
- In exclusive licenses the royalty will be higher
- Running royalties may be scaled depending on the turnover, f.e.

10% for the first 100 mio US \$ of Net Sales

8% for Net Sales above 100 mio up to 150 mio US \$ etc.

3. Financial terms in License Agreements

- Where the costs of the Licensee do not rise substantially with higher net sales, it may be reasonable to scale up the percentage of royalty with higher net sales

8% for the first 100 mio US \$ of Net Sales

10% for Net Sales above 100 mio up to 150 mio US \$ etc.

3. Financial terms in License Agreements

3.6 Option fees

- For the right of exclusive negotiations on IP during a limited period
- For the right to extend the license to further fields of the technology or to other territories

3.7 Fully paid up license through one payment

- Used in settlement agreements or patent infringement disputes
- Where the determination of net sales is difficult
- May be one payment at all or one annual payment

3. Financial terms in License Agreements

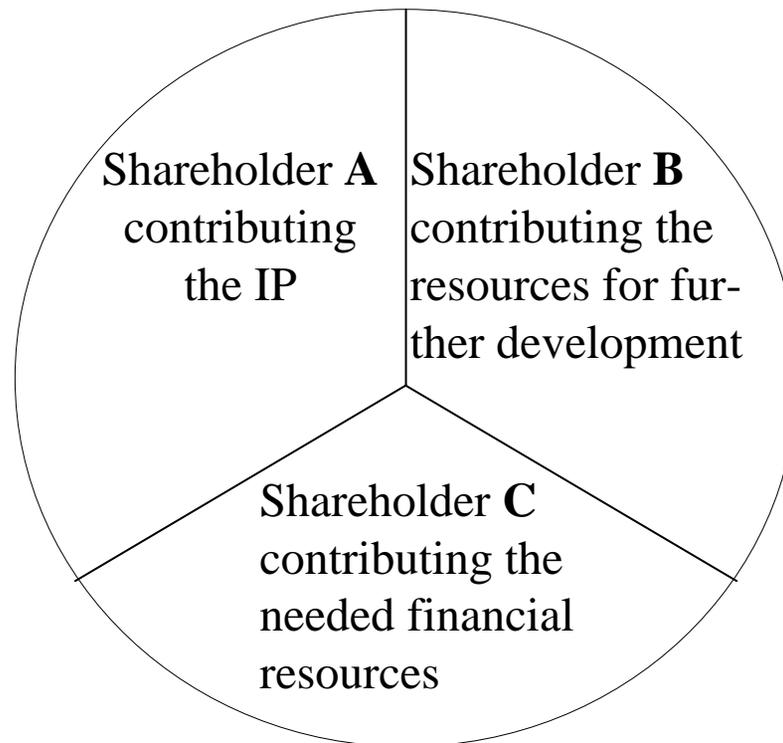
3.8 Minimum royalties

- Useful tool to ensure that the Licensee uses reasonable efforts to commercialize licensed products
- May be structured as quarterly payments, being set off against running royalties
- Broadly used in exclusive License Agreements

4. Joint ventures based on IP

- The IP is transferred to a joint venture

Example for a JV



4. Joint ventures based on IP

- Joint ventures may be attractive where several NIEs combine their IP, competences and resources
- Financial investors will invest in the JV but not directly into the NIE
- The value of the shares may grow substantially through a successful development
 - potentially higher return of investment, in particular at an IPO

4. Joint ventures based on IP

CAVEAT

- choice of partner in a JV is even more critical
- IP may be finally lost if the JV gets insolvent
- complicated legal structure
- no model for quick return of investment

5. Some thoughts about IP based cooperation with New Innovative Enterprises in CIS Countries

CAVEAT: My limited experience dates back to 2001 and 2003

- Difficulties to get the right partners together
- Difficulty to establish a real partnership
 - NIE should ensure its continuous role in the development as long as it can contribute to the development
- Flexibility on contractual terms may be an issue
 - A couple of standard term contracts will often not allow an optimal agreement for Licensor and Licensee

5. Some thoughts about IP based cooperation with New Innovative Enterprises in CIS Countries

- Interests of individuals should not be mixed up with interests of the NIE
- The role of Technology Transfer Agencies

5. Some thoughts about IP based cooperation with New Innovative Enterprises in CIS Countries

Most important: The cultural respect and understanding for each other

- Experiences on License Agreements between New Innovative Enterprises in CIS countries and licenses in Europe or the US are still limited
- Both partners should invest more time in understanding better the other side
- Experienced advisors on the business and for the legal framework are helpful, if not needed.