



European
IP Helpdesk

**FACT
SHEET**

Commercialising Intellectual Property: Licence Agreements

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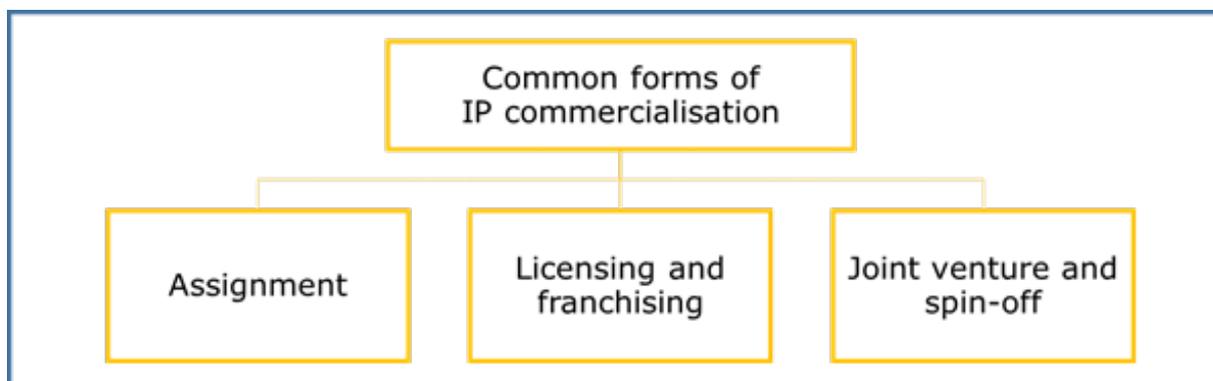
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Introduction

This fact sheet deals with commercial licence agreements. It aims to clarify when such an agreement should be used. Moreover, in this document we highlight the key provisions seen in most licensing agreements, as well as the specifics of licensing certain types of intellectual property rights.

Licensing is one option to commercialise Intellectual Property (IP), i.e. bringing IP to the market in order to be exploited. IP commercialisation can take different forms. The most common are summarised in the following diagram:



The financial success of any IP exploitation will certainly depend on the choice of the most appropriate commercialisation form, which should be based on:

- The organisation's business objectives
- The form of intellectual property
- The economic resources at its disposal

Risks should also be taken into account. Although the very nature of risks will depend on the type of commercialisation, their identification, assessment and management would give organisations more security.

The IP risks specific to commercialisation activities are those related to:

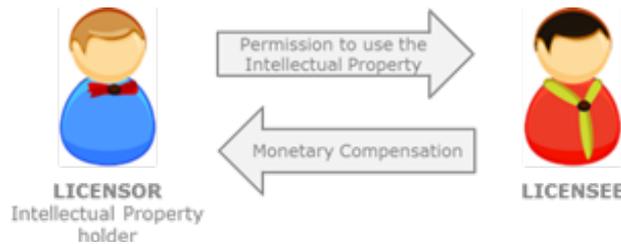
- The nature of the product and/or services
- Confidentiality
- Legal and financial matters
- Business reputation

An assessment of the risks can be based on the likelihood of the event occurrence (e.g. ownership disputes, third party infringement, etc.) and the associated consequences (e.g. irrelevant, moderate or important). Depending on the outcome's assessment, organisations will be able to make appropriate decisions about the risk management actions to be adopted (e.g. subscribing an appropriate insurance, revising relevant clauses within contracts, etc.).

Before diving deeper into the subject please note, that the content provided in this fact sheet is not meant to be exhaustive, and professional advice is strongly recommended when it comes to choosing the most suitable commercialisation practice for your organisation and dealing with the complex legal issues surrounding contractual arrangements.

1. Understanding licence agreements

A licence agreement is a contract under which the holder of intellectual property (licensor) grants permission for the use of its intellectual property to another person (licensee), within the limits set by the provisions of the contract. Without such an agreement, the use of the intellectual property would be considered an infringement. Examples of licence agreements are the software licences concluded every time you buy software or a trademark licence permitting a manufacturer to print the logo of another company on its merchandise.



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1.1 When should you use a licence agreement

a) There is no transfer of ownership

Licence Agreement		Assignment
No transfer of ownership. The IP ownership is kept by the licensor. Generally a long term agreement.	DIFFERENT FROM	Transfer (sale) of the IP ownership from one party (the assignor) to another party (the assignee). One-time agreement.

b) An established organisation is allowed to exploit the IP

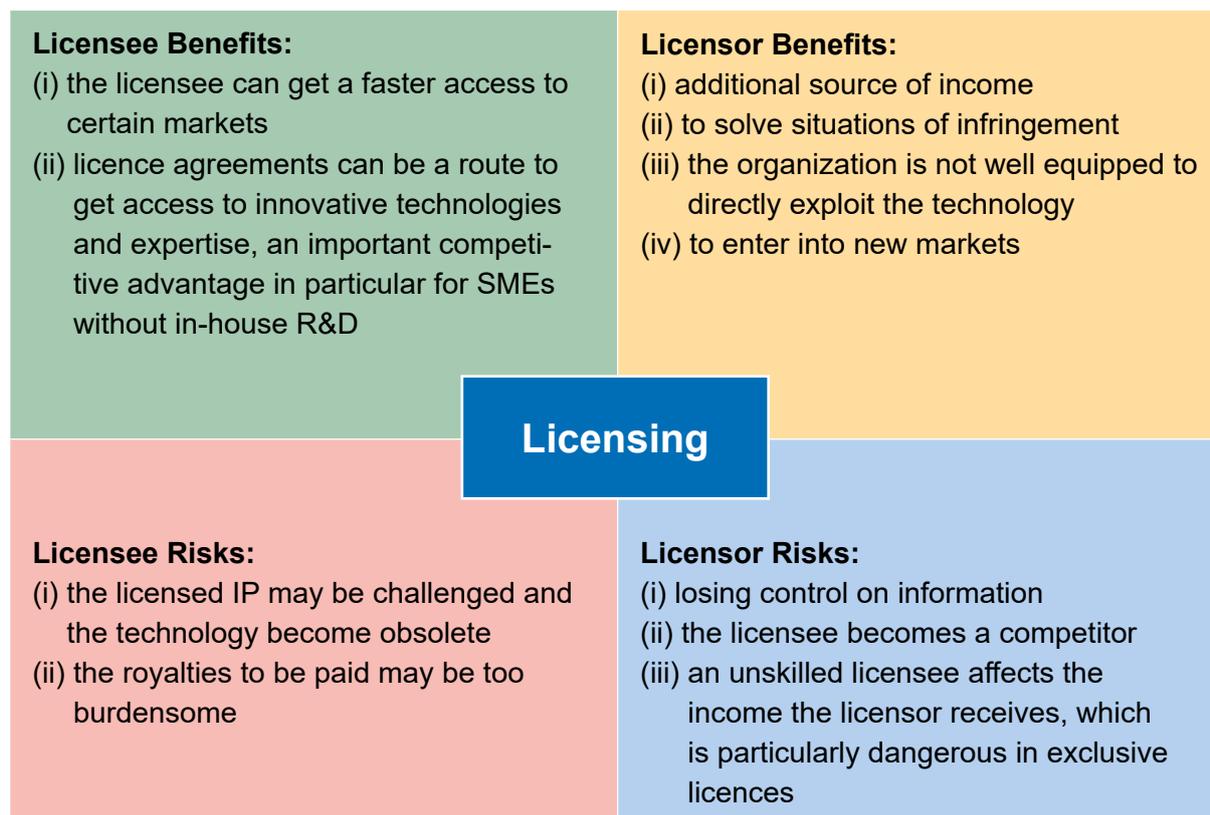
Licence Agreement		Spin-off transaction
The licence agreement does not create any new legal entity. It allows another established organisation to exploit the IP and it tends to be a long-term transaction.	DIFFERENT FROM	A small company is created with the purpose of developing a concrete technology. The licensor often assigns the IP to the spin-off company, but the transaction can also be structured through a licence of the IP.

c) The IP right holder intend to grant user rights to a third entity

Licence Agreement		Distribution agreement
It gives permission to use IP within certain limits.	DIFFERENT FROM	The holder of the technology gives permission to another organisation to distribute or sell it in a predetermined market. Commonly, a trade mark licence must be part of the contract.

1.2 Understanding benefits and risks in licensing

When negotiating a licence agreement, it is important to understand why companies licence their intellectual property or wish to become a licensee, as well as the potential risks of entering in such a deal. This will not only help them to grasp the motivations behind the demands of the other party, but also enable them to mitigate risks when drafting a licence agreement and very importantly, reach a “win-win” agreement.



2. Key terms of a licensing agreement

All the conditions agreed between the licensor and the licensee should be clearly mentioned in the licence agreement, which should be in written form.

There are many options for each provision of a licence agreement, which will not only depend on the parties' agreement, but also the type of intellectual property right being licensed, the business' sector and the applicable law. However, there are also key provisions applicable to almost all licensing deals and which we intend to highlight in this section.

2.1 Background of the licence:

PARTIES

1. [name of organization], a company incorporated in [...] with the registered number [...], having its registered office at [...] (Licensor)
2. [name of organization], a company incorporated in [...] with the registered number [...], having its registered office at [...] (Licensee)

RECITALS

- (i) Licensor owns [the Patents or the Licensed Technology as defined below];
- (ii) Licensee wishes to obtain a license to [...];
- (iii) Licensor wishes to license to Licensee on the terms and conditions set out in this Agreement.

TERMS AGREED:

1. Definitions

In this Agreement, the following words and expressions shall have the following meanings: ...

2.1.1 Identification of the parties

The parties who will be bound by the contract must be clearly identified.

2.1.2 Recitals

This is the right place to state background information on the agreement, as well as the parties' reasons for entering into the agreement. Recitals might prove to be essential if a court or an arbitrator needs to interpret the licence agreement in a potential dispute.

2.1.3 Definitions

Generally, licence agreements include a list of definitions, to assist in the reading and interpretation of the document. The terms are usually included in alphabetic order. Common terms defined in licence agreements are the following:

- a. Confidential information
- b. Net Sales
- c. (Licensed) intellectual property and technology
 - Patents, trademarks and industrial designs: usually these are identified by the elements in the title, in particular the registration number;
 - Software: the parties may include modules and version numbers and attach a copy of it to the agreement;
 - Know-how: is often defined in a few lines and described in detail in separate documentation.
- d. Territory
- e. Field of use

The technical definitions in a licence agreement, such as the Licensed intellectual property and Field of use, are essential since they have an impact on the scope of the licence, that is, what the licensee is able to do. It is crucial that the licensee understands the technology and its business needs: e.g. “What software version do we need?” “Do we need training to use the technology?”

2.2 Grant of rights

This is the core of any licence agreement, since it is where the rights of use (and their limitations)

Licensor hereby grants to Licensee a [exclusive/non-exclusive] licence in the Licensed Territory to make use and sell any Licensed Products in the Licensed Field of Use.

are established. The provisions are crucial for both licensor and licensee as they establish what each of them will be able to do with the intellectual property right or technology, that is, the licence’s scope.

2.2.1 Type of licence

The parties should clearly indicate the type of licence being granted. Generally, these are the following types of licences¹:

- **Exclusive:**
 - Exclusive: only the licensee is able to use the licensed intellectual property or technology (the licensor cannot use or license it); or
 - Sole: the licensor agrees not to grant any additional licenses but retains the right to make use of its intellectual property.

¹ The categories may differ according to national legislation and terminology.

- **Non-Exclusive:**

both the licensee and the licensor can use the licensed intellectual property or technology. The licensor is also allowed to negotiate further non-exclusive licences with other licensees.

2.2.2 Rights granted

Ideally, the activities allowed by the licensor should mirror the rights granted by law as an owner of a determined intellectual property right. For instance, the copyright holder has the exclusive rights to copy the work (i.e. reproduction), issue copies of it to the public (i.e. distribution), rent and lend it, perform or show the work in public, communicate it to the public and make adaptations, so the grant provision in the licence should refer to these rights.

The IP owner is free to decide to grant all or just part of his rights as established by law. However, the licensee must carefully assess whether the rights included are sufficient for an optimal exploitation. Nonetheless, it is not always possible to clearly identify the activities allowed by reference to the rights established by law, since the licence agreement may refer to different types of intellectual property rights or cover different jurisdictions.

Commonly, grant provisions can include:

- **Trademark:** right to use and apply the trademark[s] on and in relation to the [Products/ Services], in connection with the [development/use/manufacture/ marketing/distribution/ sale/disposal] of the [Products/Services].
- **Copyright (including software):**
 - (i) the right to use and reproduce the work;
 - (ii) the right to modify and make derivative works;
 - (iii) the right to distribute the work.
- **Patent:** right to manufacture, use and sell licensed product.
- **Technology:** develop, manufacture, practice and sell licensed technology.

2.2.3 Right to sublicense

The parties of a licence agreement need to agree on whether the licensee has the right to grant sublicenses. There are different reasons why the licensor would be willing to grant the right to sublicense if the licensee requires it:

- It may be an important additional source of revenue, particularly if the licensee is not be able to reach the entire territory covered in the licence agreement by its own;
- The licensee may be part of a corporate group and part of its affiliates can be in a better position to exploit the licensed IP.

Regardless of the reason why the licensor is granting the right to sublicense, there are a few important points to agree on and clarify in the agreement:

- a. Is the licensee free to select the sub-licensee(s)? Some limitations may be imposed by the licensor, such as limiting the sublicenses to affiliates of the licensee or companies pre-approved by the licensor.
- b. Should the sublicense agreement establish determined conditions? Often, licence agreements impose the obligation to preserve in the sublicense to the same terms and conditions set out in the original licence agreement. This enables the licensor to control the sub-licensee's use of the IP even though there is no direct contractual relation between the two of them. This takes on a special importance when a percentage of royalties comes from sublicensing revenues. Some licensors may request to receive (and even approve) the sublicensing agreement for the purpose of verifying whether the terms and conditions are followed.
- c. What happens when the original licence agreement comes to an end? There are different possibilities ranging from the immediate termination of the sublicensing agreement to obligation for the licensor to maintain the agreement with the sub-licensee.

2.2.4 Geographical scope

The territory where the licensee can exploit the IP should be clearly defined. Licences may be worldwide, cover a region such as the European Union or one country only. This is something to be agreed upon by the parties based on where the licensee plans to use the IP: e.g. the territory where a trademark will be used, including considerations related to online business activities.

2.2.5 Technical or commercial field of use

By limiting the rights granted to a specifically defined field of use, the licensee will only be able to use the IP in a specific subset/s of the potential commercial uses. Therefore, the licensor will conserve the right to directly exploit or license the same intellectual property in a different field². For example, a patent licence may limit the use of the invention to the treatment of eczema in humans.

Usually, this limitation is introduced in the licence agreement through the inclusion of a definition of Field of use, accompanied by a reference in the grant provision.

2.3 Compensation

Licensee shall pay to Licensor royalties calculated by reference to Net Sales of the Licensed Products sold by Licensee at the rate [...].

There are many reasons why the licensor may wish to establish licensing deals, but certainly one of them is to receive money from the licensee's use of the intellectual property. The

² Shotwell SL. 2007. Field-of-Use Licensing. In Intellectual Property Management in Health and Agricultural Innovation: A Handbook of Best Practices (eds. A Krattiger, RT Mahoney, L Nelsen, et al.). MIHR: Oxford, U.K., and PIPRA: Davis, U.S.A. Available online at www.ipHandbook.org

determination of a win-win compensation will depend on the valuation made of the IP being licensed, by both licensor and licensee. Once the IP valuation is individually calculated by both parties, they are then prepared to negotiate the compensation provision and agree on the following matters:

a. How will the licensee make the payment?

Usually, the decision is made between a lump-sum (amount determined up-front) or royalties (periodic amounts calculated on the base of the licensee's selling performance).

b. How will royalties be calculated?

Royalties may be calculated as a percentage of the sale price, profits made or as a fixed amount per each product unit sold, among others. If deductions are to be made (e.g. tax, delivery expenses) it is essential to clearly indicate so, which is often done by including definitions such as "Net Sales".

The licensee is the one that calculates the royalties due in each period. It is therefore important for the licensor to introduce into the licence the mechanisms to monitor the licensee's compliance with its obligations. The most commonly used mechanisms are:

- The licensee's obligation to provide to the licensor reports containing the identification of the sales that were the basis for the calculation of the royalties due in an agreed period. With the purpose of facilitating the monitoring, a template of the report can be incorporated in the licence agreement as an annex.
- The licensee's obligation to keep accurate records linked to the licensor's right to audit such documentation.

c. When are payments due?

Establishing when royalties are due is essential in order to avoid any uncertainty.

d. What is the currency of the payment?

In transnational agreements it is important to define the currency of the payment. Often licensor and licensee are based in different countries with different currencies, and, therefore, it is best practice to establish the currency to be used for payments, as well as the exchange rate.

2.4 Mitigating risks

When negotiating a licence agreement, the parties should make an effort to anticipate potential risks. There are several provisions to discuss on this matter:

2.4.1 Licensee's diligence

Especially in exclusive licence agreements, it is important that some diligence obligations are set forth for the licensee. Without such obligations, licensees could refrain from properly exploiting the technology.

The diligence obligations can be introduced by establishing a general obligation on the licensee to use of “best” or “reasonable endeavours”. However, given the ambiguity of such contractual promises, it is preferable to introduce in addition measurable obligations such as minimum royalties or milestones to be achieved at determined dates.

2.4.2 Improvements

Concluding a licence agreement does not necessarily mean that the technology being licensed will no longer be developed. On the contrary, it is not uncommon for both licensor and licensee to continue developing the technology as a consequence of further research or due to the know-how acquired through the use of that technology. It is in the best interest of each party to discuss and agree on this matter, since both licensor and licensee’s business interests are at stake.

The common practice is to grant mirror rights, that is, each party grants rights on future improvements to the other.

2.4.3 Infringements

An unavoidable matter to discuss and agree on is how to deal with potential infringements from third parties: how will these be handled? How will the licensor and licensee collaborate?

2.4.4 Warranties

Regardless of how sound the parties’ due diligence activities are, most licensors and licensees request warranties from each other. Typical warranties seen in licence agreements are:

- a. the licensor warranty on the ownership of the intellectual property right or right to grant the licence;
- b. the licensor warranty on the validity of the intellectual property;
- c. the licensor warranty on the lack of knowledge concerning third parties’ infringement.

These and other warranties depend on the negotiation between the parties. What is important to remember is that the party making such statements should internally consider whether it can assume the warranties.

2.4.5 Settlement of disputes

Even though parties wish to avoid disputes, it is best practice to include in licence agreements clauses dealing with potential future disputes among them. In this regard, there are two matters to discuss and agree on:

- The applicable law to the contract, which often is the law of the country of the licensor, licensee or where most of the activities under the contract will be carried out. Deciding on the applicable law is particularly important in transnational negotiations;
- The forum of disputes: mediation, arbitration and court ³.

³ See fact sheet Alternative Dispute Resolution Mechanisms, available in our [library](#).

2.5 Term of the agreement

This Agreement shall commence on [the Effective Date] and, unless earlier terminated in accordance with clause [...], shall continue in force [without limit of period or for [...] years].

The commencement, duration and termination of the contract must be clearly stated in the agreement.

Special attention should be given to the duration of the protection of the intellectual property right being licensed, since the period of the licence cannot exceed the term of the right (e.g. 20 years for patents). This is especially important for those licence agreements where different types of IP are being licensed, for example in the case of a patent and know-how licence agreement, since they could have different duration periods. In such cases it is advisable to clearly differentiate the two licences, particularly if the parties wish to maintain the know-how licence in force after the expiration of a patent.

2.6 Miscellaneous

Licence agreements are contracts and therefore the principles of contract law apply. Consequently, when drafting such contracts, the parties are advised to include provisions dealing with, for example, confidentiality and breach of contract among others.

3. Specificities depending on the intellectual property involved

3.1 Specificities of trade mark licences

The Licensee shall during the term of the Agreement use the trademark only in the [form and style in which the trademark is registered or form, colour, design, style and manner directed or approved by Licensor in writing from time to time].

The Licensee shall during the term of the Agreement ensure that all manufacturing, packaging, storage, marketing and supply operations of the [Goods or Services] are conducted consistently with good practices and in accordance with the specifications communicated by Licensor from time to time.

The Licensor shall have the right to inspect the Licensee's premises and to take samples of any Goods sold or to be sold in association with the trademark.

Quality control provisions are the core of trademark licences since they ensure that the consumers are not confused by the licensee's use of the trademark. In fact, these provisions aim to guarantee a consistent use of the trademark, and, therefore, that the consumer always gets the same level of quality of the product or service. Without such provisions, the licensor may lose its trademark.

Typical quality control provisions establish obligations concerning the licensee's usage of the trademark, often by referring to specifications or documentation where the licensor prescribes the standards to be met. Additionally, monitoring measures of the correct usage of the trademark by the licensee are commonly included in the agreements, such as the licensor's right to inspect the licensee's facilities and the right to receive samples of the finished products ⁴.

3.2 Specificities of copyright licenses

Copyright licence agreements can include escrow provisions, through which the licensee is granted the possibility to access physical copies of the work (e.g. sound recording or movie) or the software's source code⁵.

Through such a provision, the parties agree that the master copy of the work or the software's source code is deposited in confidence with a third party, who can only release a copy to the licensee if determined events occur, such as the licensor's bankruptcy. In this way, the licensor guarantees that its most valuable assets are not disclosed to the licensee and the latter mitigates the risk of losing its ability to keep producing copies or improvements.

⁴ Secrets of Intellectual Property: A guide for small and medium-sized exporters, International Trade Centre UNCTAD/WTO and World Intellectual Property Organization, 2003.

⁵ WIPO Guide on the Licensing of Copyright and Related Rights, World Intellectual Property Organization, 2004.

4. Negotiating a licence agreement

4.1 Preparing for a licence agreement negotiation: preparatory contracts

Licensing agreements are usually long-term business partnerships. The licensor and the licensee continually interact for a determined period of time, both dedicated to a profitable use of the intellectual property. It is, therefore, common practice to start the relationship with preparatory agreements (e.g. non-disclosure agreements) before entering into a licence agreement.

4.1.1 Non-disclosure agreement

Non-disclosure agreements (NDA) are legally binding contracts establishing the conditions under which one party (the disclosing party) discloses information in confidence to another party (the receiving party). All types of information can be disclosed under these agreements, such as ideas, know-how, descriptions of inventions, chemical formulas, research or business information and negotiations, among other. The common characteristic though is that the disclosed information is valuable for the disclosing party to the extent that it must be kept away from the public domain.

By signing a bilateral NDA, prospective licensors and licensees therefore guarantee that their secret and valuable information is kept in secrecy and will not be misused⁶.

4.1.2 Material transfer agreement

The main objective of concluding a material transfer agreement (MTA) is to regulate the exchange of proprietary material to be used by the recipient for research or for evaluating whether the material works well in its facilities⁷. MTAs are, therefore, often used, particularly in the health sector, as a preliminary agreement before deciding to enter a long-term licensing agreement.

4.2 Due diligence

Licence agreements are complex deals requiring both parties to engage in due diligence activities, particularly IP due diligence⁸. The main objective is to reduce risks, mainly concerning IP ownership and strength. Yet, risks cannot be completely eliminated by due diligences, and provisions concerning warranties should be seen as a complementary tool towards risk mitigation.

⁶ For further information on NDAs, we suggest you to consult the fact sheet Non-Disclosure Agreement: a business tool, available in our online [library](#).

⁷ Mahoney RT and A Krattiger. Agreements: A Review of Essential Tools of IP Management. In Intellectual Property Management in Health and Agricultural Innovation: A Handbook of Best Practices (eds. A Krattiger, RT Mahoney, L Nelsen, et al.). MIHR: Oxford, U.K., and PIPRA: Davis, U.S.A. Available online at www.ipHandbook.org.

⁸ For further information on due diligence, we suggest you to consult the fact sheet "IP due diligence: assessing value and risks of intangibles", available in our online library.

What the licensor needs to know?	What the licensee needs to know?
Business and licensing experience, with the purpose of understanding whether the licensee is capable of successfully exploiting the intellectual property	The licensors' rights on the intellectual property: what is the ownership chain? What is the term of the right? ⁹
Assessing the value of the intellectual property right being licensed is a determining factor for both parties. The value will determine the compensation for the licensing deal.	

⁹ Performing searches in IP databases is essential to determine the licensor rights. For further information on patent and trade mark searches, we suggest you to consult our fact sheets on how to perform searches, which are available in our [library](#).

5. Registration of the licence agreement

In some countries certain types of licences, such as exclusive patent licences, must be registered in a national registry, usually at the Intellectual Property Office¹³. If registration is not performed by the parties, the agreement does not have legal effect or the licensee may lose some rights, such as the right to damages or to request an injunction in case of a third-party infringement. Licensees, in particular, should consider this obligation.

Useful Resources

For further information on the topic please also see:

- [European IP Helpdesk: Your Guide to IP Management in International Business](#)
- [European IP Helpdesk Bulletin No.1 / June 2019: IP Licensing](#)
- Exchanging Value – Negotiating Technology Licenses, A Training Manual published jointly by the World Intellectual Property Organization (WIPO) and the International Trade Centre (ITC): <https://www.wipo.int/publications/en/details.jsp?id=296>
- Licensing Intellectual Property, published by the UK Intellectual Property Office: <https://www.gov.uk/government/publications/ip-health-check-licensing-ip>

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