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Intellectual Property (IP) Licensing Agreements Top Ten

1. Draft Contract terms to avoid litigation.

Of paramount importance when drafting a contract is to avoid ending up in litigation. Draft contract terms with this goal in mind. Litigation is a terrible way to resolve disputes. It is very expensive, and even more importantly, it takes away your mental energy. While you are in litigation you will have difficulty focusing on work and on your home life. They will both suffer.

Litigation results are unpredictable and somewhat random. Lawsuits are a good way to get a final resolution of a dispute. But they are not designed to get the best possible resolution. Rather they focus on 1) getting a resolution so that both parties can go on with their lives, 2) getting that resolution in a somewhat timely manner, and 3) getting that resolution at a reasonable price to the taxpayers who end up paying the costs of running the courthouse. Litigation results are never satisfying to either party. What you often get is a vague ruling from a judge with a dollar figure attached that seems to come out of the air.

My personal opinion is that the better contract attorneys are also litigators or have been litigators in the past. They understand from first-hand experience the importance of drafting contracts to avoid litigation. [By way of full disclosure I am both a litigator and a contract attorney, so I may be biased.] Much of the rest of this top ten addresses ways to avoid litigation.

2. Put everything in writing.

All of the essential terms of your deal should be written down. A contract is a plan of action – what the parties will do for each other. Think of it as a specialized business plan. Until you put the steps of the plan in writing, it is hard to see if you have left anything out. Until you put the plan in writing, it is hard to know if you and the other side are actually talking about the same thing. People’s memories fade over time and people tend to remember agreements in their favor. But they can not argue with the written word.

Remember to put things in writing even if you are licensing IP from yourself. Many founders of companies have already created much of the IP that the company will use before the company was founded. Who owns that IP? Under what terms can the company use that IP? This should be clearly spelled out in writing.

3. Use attorneys to draft documents.

Do not try to draft complex IP contracts yourself. Experienced IP attorneys know how to draft IP contracts. They know what to include and what traps to avoid. They understand how to draft a contract that works. I have heard and seen too many horror stories of clients who do it

themselves, often cutting and pasting from other licensing agreements. Several of my clients ended up in litigation because they tried to save a little money by writing the licensing agreement themselves. They did not do a very good job. When problems arose, they ended up paying me far more to solve the problem through litigation than if they had just let the attorneys write the contract in the first place.

By the way, although I wish that you could just buy a form on-line or cut and paste from your last contract, it does not work. Imagine what would happen if your attorney tried to write a software program by cutting and pasting code from existing programs. It would be a disaster. Don't try to do the attorney's job with a cut and paste job either.

4. Face problem areas up front.

It is human nature to want to avoid conflict. There is the hope that if you delay a problem it will go away. But it does not work. The problem does not go away, it just gets worse. If there is a problem area between the parties, deal with it now. The time to discuss it and resolve the differences is at the beginning of the relationship. The problem will come up, and if it comes up later, your options are more limited, and you are much more likely to be unable to resolve the dispute and end up in litigation, which is something you want to avoid, see #1 above.

I negotiated a contract where the other side agreed to a contract term regarding the payment of licensing fees from existing licenses. My client knew that the actual payment according to this term would end up being over one million dollars, while the other party thought it would be around \$100,000. I insisted that my client disclose this fact up front and redraft the contract term. They gave up their legal claim to one million dollars, but the other side was never going to pay that amount anyway. Instead they negotiated a fee that both sides thought was fair, and they avoided litigation

5. Plan for the unexpected.

A contract should be a plan of action. But a contract should also deal up front with what will happen if the unexpected happens. What if things do not go according to plan? How should the parties deal with the unexpected? It is far easier to come to agreement on how to deal with the unexpected at the start of the relationship than after the unexpected has already happened.

A client of mine drafted his own license agreement against my advice. He was to distribute the other party's software. Both sides were counting on the other party releasing a major upgrade to the software shortly after the agreement was signed. My client made a major investment in setting up his business in anticipation of the major upgrade. I asked him what would happen if the major upgrade did not happen. He insisted that it would and he did not have to worry about that, and he refused to plan for the unexpected. Three years later when the upgrade had still not been released, he came back to me and we ended up litigating the issue of what happens now.

Go over your plan of action and try to think what could go wrong and what would happen if it did. This is another reason to use attorneys. We see lots of cases when things have gone wrong, and we are used to thinking that way. Clients rarely come back to their attorney to tell them the agreement worked exactly as planned. It is only when something goes wrong that they call their attorney. So attorneys are used to thinking about and planning for the unexpected.

6. Make the terms fair.

If the contract terms are fair and reasonable, you are far less likely to have a dispute. You certainly want to try to negotiate a contract that is in your favor. But if the contract terms are too one-sided in favor of one party, the other party is less likely to want to perform, and you are more likely to end up in a dispute. Do you want to be in the IP licensing business or the litigation business? If you want to be in the IP licensing business, then draft a contract with reasonable terms so that both sides are able and willing to perform. That way you are not likely to end up in litigation.

There is a difference between a contract that is a good deal for you, and one that is a totally in your favor. Many attorneys try to get the most one-sided contract that they can. They are not doing their clients any favors. They are just setting their clients up to end up in litigation.

When possible, build incentives towards compliance. Don't just say that a new version is due by a certain date, say that there is an extra payment if the project is done on time, and the payment goes down if the new version is late.

7. Be wary of multiple agreements and/or attachments.

Sometimes a deal consists of multiple agreements and/or an agreement with attachments and schedules. If so, then think through how they will work together. Too often the agreements are negotiated as separate contracts even though together they constitute one deal. Attachments are often added as an afterthought, after the negotiations are finished. Do all of the documents make sense together? Are they consistent? What happens if one of the deals falls apart, and the others do not? One way to avoid potential problems is to make separate deals that stand on their own whenever possible.

I had a client who wanted to sell her IP to another company. She got a small lump sum payment and a favorable employment agreement with the new company, with salary bonuses tied to the success of the IP. She considered her new job to be part of the compensation for selling the IP. I told her that these deals did not work well together. She should sell the IP for what it is worth, and sign an employment agreement for what she is worth. She did not take my advice. She did not last long at the new company, and is now suing them to get her IP back.

8. Say it in plain English.

There is no need for a contract to use secret lawyer language that no one else can understand. Say it in plain English. If you don't know what it means, ask. There are plenty of times when I read something prepared by an attorney, and I have no idea what it means, so I ask them to rewrite it.

Define technical terms, even if the parties know what they mean. It is fine to use acronyms, abbreviations, and initials in an early draft of a contract. But the final version of the contract should make sense to anyone, not just those in the know. First, there is less agreement on those shorthand terms than you may realize. Second, if there is a disagreement about the contract, the legal standard is what it would mean objectively to a normal person reading the contract, not what it means to the tech people. You never know who will be reading the agreement and trying to understand how it works. Remember that if you end up in litigation the ultimate arbiter will be a Judge, and most Judges have very limited technical knowledge.

The clearer a document is, the more likely both sides will understand it, and the more likely both sides will be able to honor the terms of the contract, and the less likely that there will be misunderstandings and litigation.

9. Make sure you are agreeing to the same terms.

When you think you have finished negotiating and you have come to an agreement, make sure you and the other party have agreed to the same terms. In the very old days, invoices and purchase agreements would fly back and forth by mail or personal delivery. A while back faxes would fly back and forth. Today it is usually emails and email attachments. It is very easy to think you have agreed to the same terms, when you are actually each referring to a different version of the contract. This type of misunderstanding happens more often than you might think. Make sure that you know what version you are agreeing to. When you think you have an agreement, pull all the contract terms together in one document and make it clear that this is the version you are all agreeing to.

10. Make sure the contract fits your particular needs.

Keep in mind what you are trying to accomplish with your new agreement. Too often clients and their attorneys jump right in and start to write the standard contract, whether it fits what the client needs or not. I always try to start with asking my client “what are trying to accomplish here?” Then I draft a contract that fits the client’s needs.

There are times when a creative solution is better than that standard boilerplate. My favorite example is a telephone company with commercial clients. The telephone company would often end up in billing disputes over \$3,000 to \$5,000 dollars with its customers. This was not enough money to justify litigation. Besides, the company did not want to alienate its customers. So the telephone company wrote into its contract that there was mandatory arbitration of billing disputes. But the result of the arbitration was only binding on the telephone company. If the customer did not like the result, the customer could still file a lawsuit. The customers were more than willing to go along with this contract term. It turned out that customers rarely took their claims to court even when they lost. The client really just wanted to have a voice, a chance to have their say. The telephone company had a fast and inexpensive way to resolve its dispute and keep its customers satisfied.

Write a contract that is easy to understand, fits your needs, is reasonably fair to both sides, and is likely to avoid litigation. For additional advice and commentary, check out the Gary’s blog at <http://marshall2law.com>

This brochure is not a substitute for legal advice. I have presented only an overview of the legal issues. There are many nuances and some exceptions to these legal principles. The law is constantly changing, especially in the area addressed in this article. In addition, real problems are usually very fact based. Every situation is different. If you have a specific legal problem, consult an attorney.

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