Negotiating Subcontracting and Joint Development Agreements
– Key Terms and Best Practices

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Background

Why undertake a joint development?

- Need a partner with specialized expertise and technology
- Faster development of new product or service
- Expand into new geographical markets or customer base
- Reduce risks and limit financial commitment
- Obtain certain exclusive rights in developed technology

Background

But understand the risks . . .

- Devaluation of developed IP
- Poor administration
- Collaboration inhibited by IP terms
- Early termination
- Scope of development defined too broadly
- Infringement of third party IP
- Inadequate termination rights
- Surviving rights are too broad or narrow

Due Diligence

At some point early in the process, learn the business, products, and technology

- How does each company currently derive revenue and how do they intend to profit from the collaboration?
  - Current and future business model and revenue streams
  - Current and future products and services
  - Types of customers and locations
- What existing technology, IP and expertise does each party bring?
- Identify areas of potential competition with your new partner (direct and indirect via third party)
  - Consider strength of your background IP
  - Begin to think about appropriate contractual restrictions

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Key Terms

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- Scope of development
- Statement of work
- Management process
- Protection of developed IP
- IP ownership, IP licenses and commercialization by each party
- Confidential Information
- Exclusivity
- Payment obligations
- Right to terminate and post termination rights
- Assignment and change of control
- Bankruptcy

Scope of Development

- Define the subject matter of the joint development carefully
  - Define what will be developed, by whom, and timeline
  - Useful to specify what is *not* included in development
  - A scope of development that is broadly defined by subject matter and time can create serious problems

Statement of Work

- Development obligations of each party
- Deliverables (e.g., software, devices, materials, reports)
- Due dates (each phase and overall)
- Financial, personnel, and other resource obligations
- Specifications (functional requirements, design, materials, integration)
- Acceptance criteria and testing
- Access to information, networks, and security
- Location of work

Management Process

- Agreement should specify procedures for:
  – Periodic meetings
  – Periodic reports and content
  – Submission and acceptance of deliverables
  – Resolution of disputes
  – Change management
- Specify representatives of each party (e.g., technical and administrative)
- Steering Committee can be formed if needed
- Summary of agreement terms for internal use
- Management of confidential information

Management – IP Procurement

- Protection of developed IP
  - Don’t assume this happens automatically or that IP attorneys talk to all the right people
- The Agreement should specify the party responsible for IP procurement (typically the owner) and the details of managing IP procurement and maintenance
- IP Enforcement treated separately

IP Ownership – Background IP

- Background IP commonly defined as IP existing as of the effective date
- Original owner generally retains ownership of its background IP but grants the other party a license
- Third Party IP
- Consider whether certain categories of IP should be excluded from the background IP that is licensed
  - IP of a party's affiliates
  - Certain existing IP defined by subject matter
- License to background IP is defined by the typical characteristics of a license grant

IP Ownership - Developed IP

- Common reaction – We own all the IP
- Easy way – Let’s use the default rules of IP ownership:
  - Each party solely owns the IP it develops itself
  - Joint ownership of jointly developed IP
- But default rules generally don’t work well in practice

IP Ownership - Developed IP

- IP ownership based only on inventorship may discourage collaboration
- Problems with joint IP ownership
  - In licensing context, default rights of each joint IP owner may be too permissive
  - In enforcement context, default rights of each joint IP owner may be too restrictive
  - Default rights of joint IP owners vary by country and type of IP
  - Can destroy the value of trade secrets

IP Ownership - Developed IP

Other (better) ways to allocate ownership of developed IP in a JDA:

- Initially, consider a few relevant factors:
  - Subject matter: defined technical field or improvement to one party's products or technology
  - Inventorship: Party A, Party B, or both
  - IP enforcement: which party is most likely to enforce
- Then, assign ownership to one party, typically according to subject matter
  - Difficult situation is where Party A creates IP in Party B's field or an improvement to Party B's product
  - Can resolve by assigning IP to Party B and granting a license to Party A outside Party B's field

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IP Ownership - Developed IP

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- Other considerations in assigning ownership of developed IP:
  - Define the time period during which development must occur for it to be considered developed IP
  - Include present assignment of IP rights, as opposed to an agreement to assign in the future. *See Stanford v. Roche* (US 2011)
  - Require each party to have in place actual assignments of future IP rights with its employees and contractors
  - Include clause requiring parties to provide additional assistance, including signing documents

Licenses – General

- Licenses can be more important than ownership
  - They allow for a more customized allocation of rights
  - Consider what each party is permitted to do and not permitted to do
- Scope of licenses depend on:
  - The need of each party to use the developed IP in commercialization
  - IP owner's desire for some period of exclusivity, especially if the other party can compete with the IP owner
  - The relative contributions, including funding, of the non-owning party, to the development of the IP

Scope of Licenses

Characteristics of the license grant

• To Licensee (and Affiliates?) • Exclusive or nonexclusive • Licensed IP (patents, trade secrets, technical information, software, copyrights, trade secrets) • Permitted activities (make, use, sell, offer to sell, import, distribute, etc.)	• “Have made” rights • Right to sublicense and third party access • Field of use restrictions • Territory • Royalties or other payments • Term and termination • Transferability

Exclusivity

- Each party typically wants exclusivity in relation to its competitors in the developed IP
- Understand what the "exclusivity" actually is
  - Sometimes defined generally
  - The exclusivity of one party generally means restrictions on the other party (e.g., exclusive license restricts even the licensor)
- In defining exclusivity, consider all the relevant characteristics (e.g., time period, territory, field of use, products/services, IP, activities)
- Consider restrictions on direct and indirect activities

Sublicensing

- Consider whether any third parties (*e.g.*, suppliers, resellers, users, channel partners, etc.) will need sublicenses to the developed IP and the required scope
- Sublicenses should be enforceable by the IP owner, at least as a third party beneficiary
- In many situations, it’s beneficial to the licensor to require strict management of sublicensing
  - Pre-approval of sublicensees and terms
  - Specify required terms, and terms that are “no less restrictive”
  - Sublicensor responsible for compliance by sublicensee and has obligation to monitor
  - No further sublicenses
- Also important to specify whether sublicense survives termination of license

Royalties

- Pay close attention to the relationship between a contractual obligation to pay and the IP right
  - Relation to infringement
  - Territories
  - Pending patent applications vs. issued patents
  - Use of technical information vs. patent rights
- Include appropriate reporting and auditing provisions

Termination Rights

- Termination rights for each party vary based on the parties' relationship
  - Termination for convenience may be appropriate for the party taking on most of the risk
  - Termination for failure of the development to achieve defined results may be appropriate
  - Termination for material breach
- Consider worst case scenarios
  - Other party acquired by your competitor
  - Other party becomes insolvent

Rights Surviving Termination

- Certain rights and obligations need to survive termination
- Surviving terms vary according to how the agreement terminates, e.g., expiration, for cause, for convenience
- Consider all circumstances and specify what survives
  - Natural expiration vs. early termination
  - IP ownership, licenses and IP procurement obligations

Corporate Transactions

- Given the high frequency of corporate transactions, consider:
  - What entity might acquire the other party
  - What provisions relating to assignment of the agreement and change of control are appropriate
- Example: your competitor acquires the other party by stock purchase or by asset purchase
- Restrictions on assignment take various forms

Corporate Transactions

- Consider whether it is necessary to broadly define "change of control" or "transfer" so as to provide a termination right in a variety of circumstances:
  - Stock purchase
  - Merger
  - Other direct or indirect change in control over the other party or beneficial ownership of its voting securities

Bankruptcy

- Risks for non-debtor party
- Statutory protections for Licensee
  - 11 USC § 365(n) allows Licensee to retain its rights
- Contractual protection for Licensee
  - Specify that the license is a “license” to “Intellectual Property”
  - Distinguish “royalty” payments from other payments (Licensee must continue to pay “royalty” payments under 365(n))
- Contractual protection for Licensor
  - Pre-bankruptcy termination provisions
  - Characterize the license as “personal” to licensee, and prohibit assignment without Licensor’s consent

Questions?