



INTELLECTUAL PROPERTY LICENSING BASICS FOR NONPROFITS

In pursuit of achieving their mission and conducting charitable activities, nonprofit organizations often develop advertising and marketing literature, design logos, names and programs, and create products or written works. All of these things constitute intellectual property. If intellectual property is not managed well, a nonprofit organization may dilute or damage its rights to its own intellectual property and possibly infringe on the rights of others. However, if managed correctly, intellectual property can be protected and used as an asset that the nonprofit can license to others in order to further the organization's cause and/or generate revenue.

Anytime a nonprofit organization allows another individual or entity to use its intellectual property, it is licensing those rights to the other party. We have compiled a collection of licensing questions and answers relevant to nonprofits, and have divided them into the following categories:

- **FAQs [1- 3] Intellectual Property Licensing—An Introduction**
- **FAQs [4-10] Intellectual Property Licensing—Practical Applications**

We hope you will find this resource to be a useful preliminary guide for understanding intellectual property licensing and why it is used.



This publication should not be construed as legal advice. These frequently asked questions and answers are provided for informational purposes only and do not constitute legal advice. While this information can help you understand the basic rules related to licensing, it is very important that you obtain the advice of a qualified attorney before entering into any licensing agreements.

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1. What is intellectual property?

The phrase “intellectual property” refers to the legal mechanisms that protect creations of the mind. Creations of the mind may take many forms, including traditional inventions, artwork, music, literary works, symbols, logos, company slogans, and the like. “Intellectual property” is a general term, and may be broken down into four primary categories: (1) patents, (2) copyrights, (3) trademarks, and (4) trade secrets. In order to understand how intellectual property is licensed, it is important to first understand what intellectual property is.

(1) Patents: A U.S. patent represents a legal right to exclude others from practicing an invention for the term of the patent. Thus, a patent represents a legal monopoly, limited in duration, provided in return for the patentee’s disclosure of the invention to the public.

In order to obtain a patent, an application must be submitted to the United States Patent and Trademark Office (“USPTO”). The application discloses the invention, and further identifies the “boundaries” of the invention via the patent claims. The patent claims identify to the public what the invention is, and help establish when patent infringement may occur. Drafting patent claims is an imprecise process, and an application may remain pending before the USPTO for several years before a final determination of patent eligibility is received from the Patent Office.

The most common form of patent is the utility patent. Utility patents protect articles of manufacture, machines, and processes. Utility patents have been used to protect an array of varying technologies, including, for example, computer software, chemical compositions, semiconductors, tools, and the like. Other types of patents include design patents, which cover ornamental features. Though far less common, design patents are potentially valuable—for example, design patents were at the center of the *Apple v. Samsung* dispute. In that dispute, the design patents covered the ornamental features of smartphones.

(2) Copyrights: A copyright protects creators of original works of authorship. Such works include, for example, dramatic, artistic, musical, and literary works, whether published or unpublished. Importantly, a copyright confers upon the holder the exclusive right to reproduce the copyrighted work.

Additionally, a copyright will likely protect any derivative works. Derivative works constitute follow-on projects that rely upon the legally protectable elements of the primary work. A common example is the cinematic adaptation of a novel, or new versions of a preexisting computer program. Where a derivative work is prepared without authorization of the copyright holder, copyright infringement may occur.

Unlike patents, copyright law does not require a formalized application process before copyright protection may be received. Instead, copyright protection attaches at the moment the original work of authorship is created. Nonetheless, there are certain benefits associated with federal registration of the copyright—for example, federal registration is a prerequisite to filing suit in federal district court for copyright infringement.

(3) Trademarks: In general terms, a trademark identifies the source (*i.e.*, brand) of goods and services provided by a particular organization or entity. Importantly, the mark allows consumers to distinguish the source of the goods and services of one organization from another. By allowing a trademark holder to legally protect its brand, the law incentivizes holders to invest in, develop, and control the quality of their goods and services.

Like copyrights, trademarks do not require a formalized application process. Instead, a particular entity merely has to be the first to use the mark in commerce. However, such marks are limited to the geographic reach of their use. In order to establish a national trademark, federal registration is required.

Though copyright and trademark law do not require federal registration as a prerequisite to legal protection, federal registration is nonetheless advised. By obtaining federally registered trademarks or copyrights, certain legal benefits attach. Additionally, federal registration provides the holder with a tangible intellectual property asset, which serves as a far superior platform for licensing.

In order to federally register a copyright, a form accompanied by samples of the work must be submitted to the U.S. Copyright Office. Federal trademark registration is more complex, and requires the submission of an application to the USPTO, where as an examiner will review the proposed mark to determine (1) whether it qualifies for protection, and (2) whether the proposed mark is preempted by any pre-existing mark(s). Neither copyright nor trademark registration requires the involvement of an attorney—however, an intellectual property attorney can help facilitate a successful registration process. To learn more about copyright and trademark registration, please visit our Copyright and Trademark publication here: <http://www.publiccounsel.org/tools/publications/files/0072.pdf>.

(4) Trade Secrets: Trade secrets are broadly defined, and may include any formula, process, method, list, or other form of confidential information that is neither generally known nor otherwise reasonably ascertainable, and which confers a competitive or business advantage to the holder. The most important aspect of a trade secret is confidentiality, and if sufficient protection isn't in place, a particular trade secret may not qualify as such under the law. In order to ensure that a trade secret retains its confidentiality, (1) access restrictions, (2) confidentiality agreements, (3) confidentiality markings, and (4) physical security precautions are advised. Examples include NDAs, non-competes, passwords, firewalls, need-to-know disclosure, and physical security.

Common forms of trade secrets include customer lists, recipes, business methods, internal marketing strategies, and the like. Software and company-internal formulas may also constitute trade secrets. Generally speaking, trade secrets are not typically licensed.

Where a trade secret must be disclosed during licensing negotiation, it is critical that a Non-Disclosure Agreement (“NDA”) is entered into before disclosure occurs. If the trade secret is disclosed to a third party without a signed NDA, trade secret status may be waived.

2. What is a license?

Once a nonprofit identifies and protects its intellectual property—*i.e.*, its patents, copyrights, trademarks, and trade secrets—it must then determine whether licensing its intellectual property to third parties aligns with its business goals. In order to make this determination, it is important to

understand what a license is, and what a license may achieve relative to the intellectual property at issue.

Foundationally, a license for intellectual property is a contractual promise not to sue. Generally, this promise takes the form of a written agreement between the contracting parties, where the owner (“licensor”) allows the licensee access to its intellectual property in return for monetization. Typically, payment comes in the form of royalties, comprising a percentage of all profits received from the use of the licensed intellectual property. A license may also, however, include a one-time, upfront payment.

It is important to understand that intellectual property is not self-enforcing. Though a nonprofit may own patents or federally registered copyrights and trademarks, that ownership, in and of itself, will not generate revenue. Instead, it is incumbent upon the nonprofit to not only police its intellectual property, but to also seek opportunities via licensing arrangements to generate income.

For example, a patent discloses the invention to the public in return for a temporary, legally enforceable monopoly covering that invention and that invention alone. The monopoly is not self-enforcing, and, in light of the disclosure, a competitor may replicate the patented technology without permission. In order to monitor such unauthorized use, diligence is required. Where a particular use infringes a patent, it can become the subject of licensing negotiations.

Even in the absence of current use or infringement, intellectual property may still be licensed. For example, a nonprofit seeking to monetize its intellectual property may reach out to competitors or other organizations in order to determine interest. Where business goals overlap, licensing discussions can be the next step.

There is not set formula *per se* establishing the requirements for a licensing agreement. Nonetheless, a license for intellectual property will typically include a number of common elements. For example, the licensing agreement will identify the intellectual property rights that are being granted. Additionally, the license will set the term (*i.e.*, time) of the grant of intellectual property rights, and will also identify the consideration (consideration is a legal term, and may be colloquially referred to as “payment”) in return for the grant of the right. Where the parties agree to representations and warranties, these will be included as well. Provisions regarding indemnification, ability to sue, general liability, and the like may also factor into the licensing agreement.

The identification of the granted intellectual property rights is a critically important component of any licensing agreement, as it expressly identifies the rights that are being conveyed. In any licensing agreement addressing intellectual property, the granting clause should not be ambiguous or otherwise vague. Further, the agreement should identify whether the grant is exclusive or non-exclusive, and also whether the grant is limited by geographic scope. *See* Question 3. The grant of rights may also identify and limit the appropriate field of use.

Consideration in a licensing agreement may also come in many forms, including upfront fees and/or royalties. Royalties represent the most common form of consideration, and the agreement may also include a minimum annual sales requirement in order to ensure that the licensed intellectual property is adequately marketed. In the event that the requirement is not met, the licensing agreement may provide for the complete return of all intellectual property rights to the owner.

A critically important—but sometimes overlooked—component of any licensing agreement is the enforcement provision. Depending upon the agreement, either the owner or the licensee will retain the ability to sue in the event of intellectual property infringement. Generally speaking, an exclusive license confers to the exclusive licensee the ability to sue. A non-exclusive license, however, will typically not confer this right to the licensee. Thus, the owner of the intellectual property retains the right to pursue enforcement in court.

3. What are the types of licenses?

Licenses are either exclusive or non-exclusive, and an exclusive or non-exclusive license may cover patents, copyrights, trademarks, and/or trade secrets. An exclusive license represents an exclusive grant to the licensee—that is, the recipient retains the sole and exclusive ability to use the intellectual property. An exclusive license may cover a particular region: for example, the licensee may have the exclusive ability to use the intellectual property within the southwest of the United States. Another exclusive licensee may, however, retain the exclusive ability to use the *same* intellectual property within the northeast of the United States. The exclusive license may also be limited by industry.

A non-exclusive license, conversely, merely represents an access right. A non-exclusive license will not limit use of the intellectual property to one particular party, and instead the same intellectual property may be licensed out to multiple parties, even within the same geographic region, or in the same industry. Additionally, a non-exclusive license may also grant access to *competitors*. In general terms, a non-exclusive license is preferred where the intellectual property in question is foundational, and represents a mandatory element of an otherwise industry-wide feature. For example, a new component to be used in pre-existing computer technology may benefit from a non-exclusive license, whereas new computer technology altogether may be better licensed exclusively.

Exclusive licenses are more aptly used where the intellectual property at issue is innovative, and represents a new feature, element, or idea not otherwise found within the relevant industry. The incentive is that novel technology is licensed to an entity with sufficient capital, know-how, and resources to meaningfully develop and market the intellectual property. In this regard, there are risks associated with exclusive licenses, including allowing exclusive access to a non-profit's intellectual property that is then inadequately developed, promoted, or advertised.

Exclusive versus non-exclusive defines the general form a license may take. However, within these general forms, the relevant intellectual property is distinct—patents, copyrights, trademarks, and trade secrets. Licensing agreements addressing patents, copyrights, and trade secrets are relatively similar; trademark licensing agreements are, however, unique. Specifically, because the goal of trademark law is to distinguish the goods and services of one nonprofit from another, and, further, to identify the source of such goods and services, thus suggesting a certain quality and reputation, a trademark license must include specialized provisions governing the intellectual property. If the trademarks are not adequately controlled by the licensing agreement, trademark protection may be lost altogether.

Specifically, a license granting access to a trademark must include oversight and quality control provisions. Without these provisions, the owner cannot comply with its affirmative duty to ensure that the trademark represents what it is supposed to. Such licenses are colloquially referred to as “naked licenses.” In other words, the licensor must maintain sufficient oversight and quality control so that the

trademark continues to communicate to the public reliable information about the source of the goods and services. Typically, provisions providing for oversight and quality control provide for inspection rights, in addition to quality reviews at reasonable intervals. Without such provisions, trademark misuse may occur, and forfeiture of the mark may result.

INTELLECTUAL PROPERTY LICENSING—PRACTICAL APPLICATIONS

4. Why use a license?

Whether a potential licensor or licensee, a license for intellectual property can be an effective tool for advancing a particular nonprofit's goals. For example, a license or cross license may be used where two or more nonprofits seek to establish a joint venture. Through the formation of a joint venture, and, further, through the pooling of intellectual property resources, a common business purpose may be pursued. For example, one nonprofit may be able to contribute trade secret business expertise, whereas the other might be able to provide patented technology. Working together, the common goal is advanced.

Not all licenses require a joint venture. A nonprofit may simply seek to expand its existing business through a license, extending the territorial reach of its intellectual property by licensing with established nonprofits in other regions. Conversely, a nascent nonprofit may be in its start-up phase, and a license may be a prerequisite to business formation. A license can advance a nonprofit in other ways as well—for example, through licensing, a nonprofit can advance the state of its technological know-how and capacity.

Licensing may also be required during merger and acquisition, or through the formation of other business partnerships. As with most forms of contracts, licenses are flexible, and can be drafted in a variety of ways that best suit the goals of a particular nonprofit. Through strategic licensing, a nonprofit can increase its income, or broaden its range of marketable goods and services. In the modern marketplace, intellectual property licensing is an important element of any business strategy.

5. What may be licensed?

Any form of intellectual property may be licensed. Thus, patents, copyrights, trademarks, and trade secrets can be the subject of a licensing agreement. Licensing agreements granting access to patents and trade secrets may be broadly categorized as technology licenses, though under certain circumstances copyrights might qualify as well. For example, a copyright can protect source code—where a developer wants to grant source code access to a potential customer, a technology license addressing the relevant copyright may apply.

Similarly, the subject matter of any patent may potentially be licensed. Of course, the patent owner has to consent to the license—a potential licensee cannot force the licensor to grant access. Typically, a nonprofit identifies technology in the marketplace that it wants to use, consults with an intellectual property attorney to determine whether there is patent protection, and, if patent protection is found, licensing outreach begins. In some instances, where an agreement cannot be reached, and where the

technology at issue is particularly important, a lawsuit may occur. In such patent disputes, the potential licensee may allege that the patent is either invalid or not infringed.

Trade secrets present a more complicated scenario. By their very nature, trade secrets are not readily ascertainable in the relevant marketplace. Instead, trade secret licensing discussions are typically initiated by the trade secret holder. Perhaps the trade secret holder does not have sufficient capacity to maximize the value of its trade secret, thus licensing outreach to appropriate entities may occur. Conversely, the disclosure of trade secrets may occur during the pendency of related licensing negotiations—for example, during the discussion of a patent license, trade secrets may be revealed, thus necessitating additional licensing discussions.

A copyright license may be used where the intellectual property in question relates to artistic, literary, or dramatic works. For example, an artist of a painting may seek to enter into a copyright license with a nonprofit distributor. Through license formation, the artist benefits from the nonprofit's distribution and marketing capability. In return, the nonprofit receives access rights to the artist's painting. This has the net effect of establishing market share, in addition to expanding the potential revenue stream.

As discussed, trademark licenses are complicated, and require unique provisions in order to avoid forfeiture of the relevant intellectual property interests. Generally speaking, where a trademark is licensed, quality control and oversight provisions are required—this means that the grant is not an unfettered access right. Instead, the licensee agrees to utilize the licensed trademark in a way that comports with the goals and requirements of the licensor. Therefore, the grant tends to be more restrictive relative to patent, trade secret, or copyright licenses, allowing the licensee to capitalize on the goodwill generated by the licensor.

6. What are the advantages of using a license?

A license, as opposed to an assignment (*i.e.*, a complete transfer of ownership and title), allows the licensor to retain ownership over its intellectual property while nonetheless granting access rights. Where the grant ultimately fails to produce the anticipated results, the license—as opposed to an assignment—may allow for a return of rights. Where the return occurs, the licensor may seek a new business partner to license its intellectual property with.

For a licensor, a licensing agreement represents the ability to couple pre-existing manufacturing and distribution know-how with its intellectual property. Creating intellectual property is a highly specific endeavor, and is often unrelated to the commercialization of the resultant product. Through careful licensing, the licensor may work together with a licensee to monetize its intellectual property in a way that represents a “win-win” for the respective parties.

For a licensee, a licensing agreement can instantaneously expand a product line, or improve pre-existing products and methods. Licensing often represents an alternative to research and development, and can revitalize a business when done correctly. A copyright license may provide for an infusion of creativity, in addition to a fresh perspective. A trademark license may provide for the distribution of certain goods and services, allowing for a nonprofit to capitalize on the goodwill in the market created by the licensor.

7. What are the disadvantages of using a license?

By entering into a license, the licensor is granting an access right to the licensee for its intellectual property. Ideally, the net result is a win for both contracting parties. However, this is not always the case. The licensee may not market, promote, or otherwise develop the intellectual property as initially planned, failing to generate the desired result.

Other disadvantages occur when a particular entity is in its start-up or nascent stages. Start-up entities often struggle to accurately value their intellectual property, resulting in licensing agreements that are unfair or one-sided. For example, start-ups looking to license are often presented with a “take it or leave it” offer regarding exclusivity. In other words, a start-up may be required to grant an exclusive license in return for a fixed payment. Where the payment is low, and the grant is exclusive, intellectual property that is later found to be highly valuable will generate nominal value for the granting start-up. Exclusivity is typically a critical component of any licensing negotiation, and newly formed start-ups often lack the strategic bargaining power required to maximize the return.

A license for intellectual property may also include an assignment of rights provision—that is, an assignment of the license itself. Provisions of this variety can become problematic where a licensee entity is acquired by another business. Pursuant to the assignment provision, the acquiring business may receive the license without additional cost or negotiation. Where a new business receives the license pursuant to an assignment provision, there is no guarantee or obligation that that business will maximize the licensor’s intellectual property in a way that generates value.

Other disadvantages may occur where a licensing agreement includes imprecise language. For example, the agreement needs to expressly define the nature of the intellectual property grant. Where unclear, disputes may arise over whether certain intellectual property was legally used or marketed.

8. Do intellectual property licenses present potential tax consequences for nonprofit tax-exempt organizations?

As a general rule, nonprofit tax-exempt organizations are exempt from federal income tax on income related to their exempt purpose(s). Where income is generated from “unrelated” activities, it may lead to income tax exposure. Where excessive “unrelated” business income is generated (via, for example, intellectual property licensing), then tax exempt status may be lost altogether.

The rules governing whether income generated via intellectual property licensing is “related” or “unrelated” are complex. If a particular license appears to present an opportunity that goes beyond the typical scope of a nonprofit’s activities and exempt purpose(s), the advice of counsel should be sought in order to avoid unexpected tax repercussions.

9. What are royalty payments?

The term “royalty” refers to recurring payments, as opposed to a one time, upfront payment. In its most common form, a royalty represents a percentage of the profits. For example, a licensing agreement may

provide that the owner of the intellectual property receives 25% of all profits (paid monthly) received from its use.

The actual percentage is a topic that should be negotiated during license formation. On the one hand, the licensee will bear the bulk of the business risk; on the other, the licensor is contributing the intellectual property that generates value. There is no hard and fast rule in terms of determining a royalty rate; instead, the parties should apply a “sliding scale” approach, factoring in risk, intellectual property contribution, marketing, scale-up, distribution needs, and the like.

Once the royalty rate has been identified and agreed to, it is also important to identify how that rate may apply. For example, if certain intellectual property is incorporated into “Widget X,” does the royalty apply to all profits generated by that product, or only the profits attributable to the contribution of the intellectual property? If contribution driven, what metric is in place in order to determine an adequate share? If not properly defined within the agreement, disputes can arise, leading to potential litigation.

10. What should I do if I do not understand a proposed licensing agreement?

Licenses for intellectual property are intrinsically complicated documents, and often they will include complex legal jargon and phrases. Under no circumstances should a license for intellectual property be signed without fully understanding the ramifications of the agreement. For example, ratification may confer an exclusive grant to the licensee, providing the licensor with minimal value in return. The repercussions for a start-up or nonprofit entering into such an agreement may be long term and severe.

Therefore, if confronted with a proposed licensing agreement for intellectual property that is either unclear or not fully understood, it is highly recommended to seek the advice of counsel before the agreement is entered into. Public Counsel may be able to assist your nonprofit organization with potential licensing questions and/or negotiations.