

# Unlocking the Black Box of Business: Licenses

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# Background

- Thomas McMurry
  - Director, Business Development
  - 3+ years at BU
  - BS, MS, PhD Chemistry
  - 5 years @ NIH/NCI
  - 25 years in Cambridge Biotech

# Acknowledgements

- Michael Pratt, MBA
  - Managing Director, Office of Technology Development at BU

# What is a license?

## BLACK'S LAW DICTIONARY

*n.* 1 A **revocable permission** to commit some act that would otherwise be unlawful; esp. an agreement (not amounting to a lease or profit à prendre) that it will be lawful for the licensee to enter the licensor's land to do some act that would otherwise be illegal, such as hunting game. See *SERVITUDE*. 2. The certificate or document evidencing such permission.  
-- license, *vb*

***.....it's like renting your house.***

# What and why?

## What?

- Patents, Copyrights, Trademarks, Products...

## Why?

- Encourage commercial development
- Monetize underutilized assets
- Consideration to access another market for your own products
- Build value in your startup company to attract further investment...

# How does licensing work if I wish to start a company based on my BU invention?

## BU inventions are governed by the Boston University IP Policy

- You inform OTD about the possible invention
- OTD determines if it is patentable, copyrightable
- OTD determines whether or not to file a patent [limited budget!]
- If a patent is filed, OTD works collaboratively with the inventors to establish a licensing strategy
- If the inventors wish to start a company, our preferred licensing path is ALWAYS to the BU inventor's startup
- *NOTE: The company should be prepared to assume license obligations [patent costs, product development etc]*

# Summary: Types of Licenses

## In-Licensing

- Acquiring the right to develop and sell a product
  - Enabling license – patents + know-how
  - Freedom to operate – route through toll gates erected by blocking patents

## Out-Licensing

- Granting rights to intellectual property to others
  - Enabling license – giving up a product to someone with more resources
  - Freedom to operate – extracting value from a platform technology

## Cross-Licensing

- Trading IP rights
  - Mutual elimination of road blocks
  - Competitive or non-competitive products
  - Many patents filed to serve as trading chips at the table

# Some major issues to worry about

- Exclusivity vs. non-exclusivity
- Field of Use
- Time/Geographical limits

**What the licensee gets**

➤ **Royalty**

➤ **Equity**

➤ **Other fees and costs**

**What the licensor gets**

➤ **Milestones**

➤ **Claw-back provisions**

➤ **Auditing**

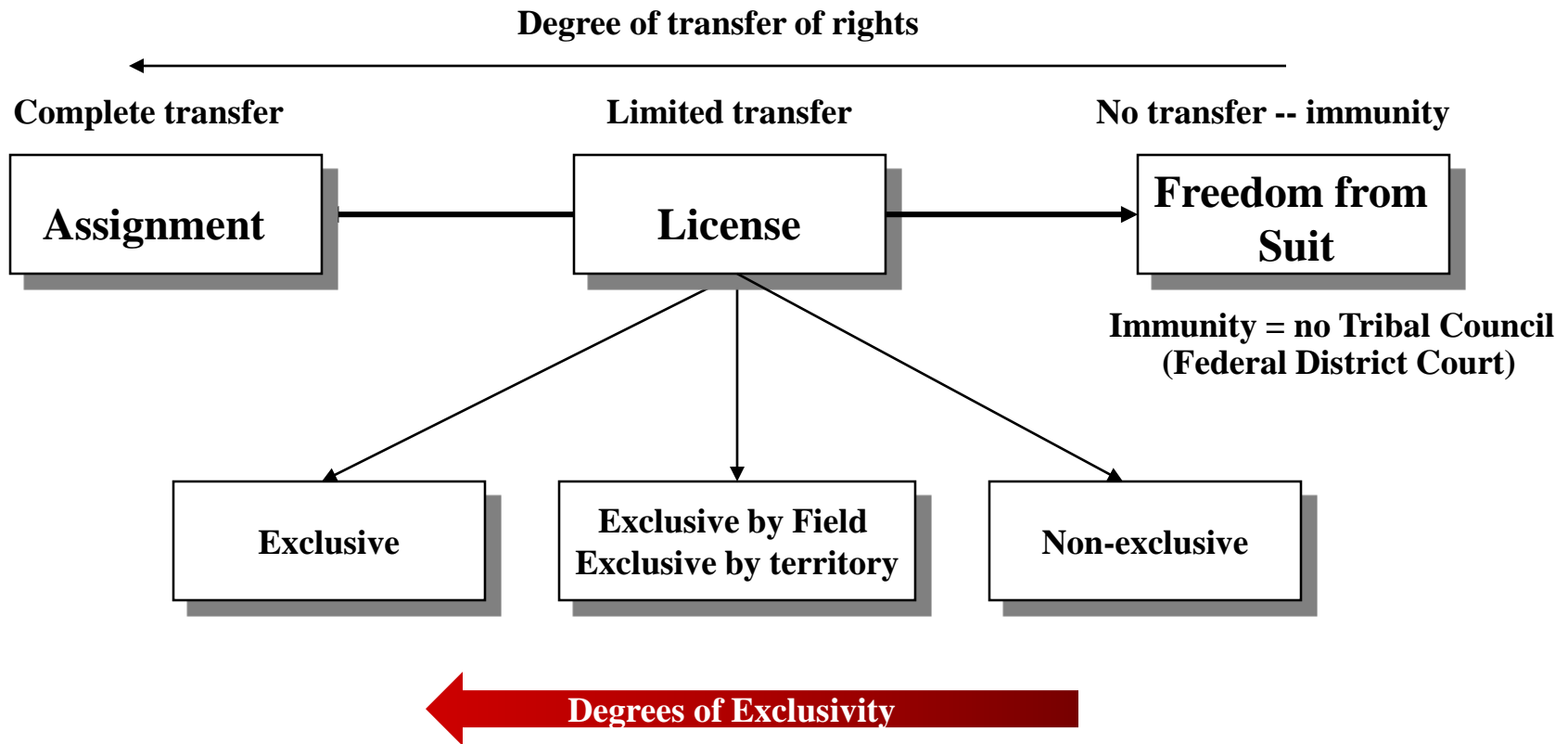
**“Trust but verify”**



# Common goals, different perspectives

- Clear context and agreement framework
- Develop strong IP protection, stop infringers
- Enable the licensee to make, use, and sell the product
- See the product reach the marketplace as soon as possible
- Fairly allocate income from the technology's success
- Allocate liability as appropriate
- Define procedures for managing the license (disputes, termination etc)

# Different Degrees of Rights Can be Granted



# Where is Value Extracted in a License?

- Upfront fee
- Ongoing pre-commercial payments
  - Patent costs
  - Milestone payments
  - Annual Minimum Royalties
- Research collaboration and support
- Sublicense income sharing
- Earned royalties

# Ongoing Pre-Commercial Payments

- Patent costs
- Milestone payments
  - Reflects increase in value of technology to licensee as they make progress
  - More common with life sciences inventions
  - Development milestones
  - Patent milestones
  - Sales milestones
  - Can be in stock
- Annual Minimum Royalties
  - Due diligence mechanism
  - Typically escalate substantially after 3 or so years
  - More common with physical sciences inventions

# Royalty Rate

- The main post-commercialization economic component of the license
- Biggest long term impact if the product is successful
- Offsets
  - Major downward impact
  - Credits for:
    - Current year annual minimum royalties YES
    - Prior year annual minimum royalties NO
    - Sunk patent costs NO
  - Offsets for royalties paid to third parties SOMETIMES
- How are sales by Sublicensees handled?
  - Identical to sales by licensee
  - Excluded and handled under Sublicensee income sharing, Licensor receives a higher % on revenue received by Licensee from Sublicensee (e.g. 20% vs. a 5% royalty on sales by Licensee)

# How do you get equity in a license?

- Substitute for one or more cash components
  - Remember -- “Equity is just cash that hasn’t turned green yet”
- Generally the upfront fee
  - For the technology
  - For other value contributed if a start-up you’re helping create the company
- May allow early milestone payments in stock

# Milestones

- As a licensor, you'd like to know what your licensee is up to -- or not
- Generally should have some reporting requirements
- Milestones lay out an agreed-upon plan for the future
  - Development Milestones
  - Commercialization Milestones
- Sometimes a Milestone can just be money paid

**Here's the  
money, now  
go away**



# Claw-back

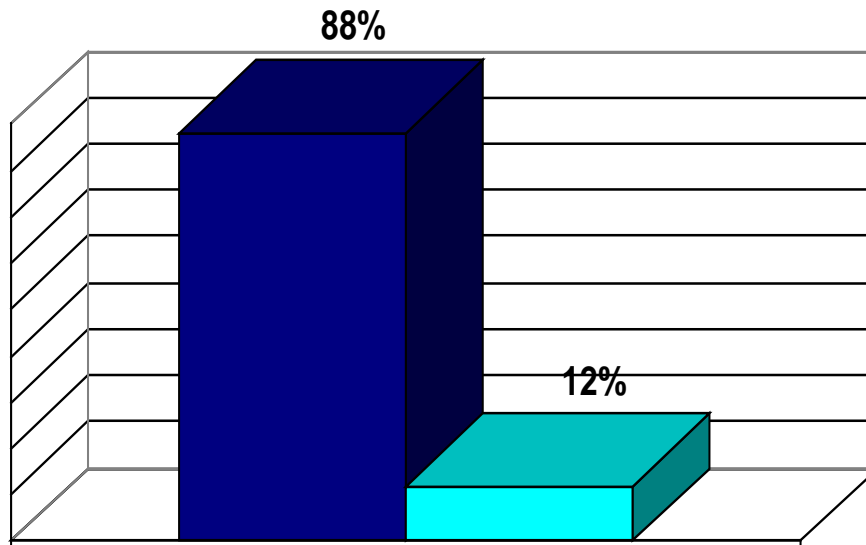
- What is the worst-case scenario and what happens then?
- Licensee goes belly-up
- Licensee has lost interest
- Licensee isn't making payments





# Royalty under-reporting is very common

Figure 1: Percentage of Licenses with Underreported Royalties



**Auditing can be well worth the effort;  
73% of audits recover 10X-100X of audit cost\***

*Debora R. Stewart, CPA and Judy A. Byrd, CPA\* Invotex Group*

UNIVERSITY

# Negotiation process

- May start with a business plan overview by the potential licensee
- Confidentiality agreement may be required
- Offer is typically made via a Term Sheet that contains financial terms and other select/critical terms, may or may not be binding Milestones lay out an agreed-upon plan for the future
- Once term sheet is agreed upon, an actual license agreement is drafted
- The language of the agreement is then negotiated
- Often other documents/deliverables are required for closing
- Can be helpful to have checklist of these to keep track of them
- BU template [“start-up/express” license](#) available online