



## IP LICENSING COMMITTEE

### MODEL LICENSING CLAUSES BULLETIN

This paper was created by the Intellectual Property Owners Association IP Licensing Committee to provide background to IPO members. It should not be construed as providing legal advice or as representing the views of IPO.

**TOPIC:** Model Licensing Clauses on Resale, Sublicensing, and Patent Exhaustion After *Quanta Computer*

**BULLETIN NO.:** 002

**DATE:** April 16, 2012

**DRAFTERS AND EDITORS:** John L. Dauer, Jr.; Gary Dukarich; Justin Lewis; Shannon D. Powers; Kenneth M. Seddon; Jill M. Browning

**INITIATING LEGAL EVENT:** *Quanta Computer, Inc. v. LG Electronics, Inc.*, 553 U.S. 617, 128 S. Ct. 2109, 170 L. Ed. 2d 996 (2008).

**KEYWORDS:** Indemnification; Patent Exhaustion; Resale; Sublicense

**COMMENTS:** The *Quanta Computer* decision holds that patent exhaustion applies to both apparatus and method claims, and that the authorized sale of items that substantially embody licensed patents—needing only application of common processes or addition of standard parts to practice the patent—and that have no reasonable noninfringing use exhausts the licensed patents as to those items.

**SCOPE:** National

**CAUTIONS:** The *Quanta Computer* decision may have far reaching effects whose outer contours may not be currently ascertainable. The potentially wide-ranging effect of this decision likely requires a broad responsive strategy in which licensing clauses only play a part. The following clauses represent certain potential strategies which may or may not prove valid or effective before reviewing courts.

#### **CLAUSE A**

**Comments:** Section III(C) of the *Quanta Computer* opinion rejected the argument that the licensee's sale was unauthorized, ruling that it was an authorized sale triggering patent

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exhaustion because the license agreement did not restrict the licensee's ability to sell patented products, with merely a different agreement between the parties requiring the licensee to notify its customers that the customers had not been licensed to practice the patents. It is therefore possible a different result on patent exhaustion may have been reached if the license agreement itself affirmatively restricted or forbade the licensee from selling products to unlicensed customers, such that those sales would have been unauthorized.

**Purpose:** Forbid licensee from selling patented products to customers other than to customers licensed by the licensor or as otherwise explicitly approved by the license agreement, and render such sales unauthorized.

**Text:**

Licensee shall not, and licensee hereby acknowledges that to do so is expressly forbidden and unauthorized, make any sale of any Licensed Product or any item incorporating any Licensed Product or utilizing any of the Licensed Patents, unless such sale is: (a) to a party certified as a Licensed Party by the licensor; (ii) otherwise expressly authorized by this Agreement; or (iii) expressly authorized by a subsequent writing executed by both parties.

**CLAUSE B**

**Comments:** After *Quanta Computer*, a licensor must assume that it can only a license a particular patent once. This renders inadvisable the prior approach of loosely licensing all of licensor's patents for a particular field of use.

**Purpose:** Reduce scope of patents subject to patent exhaustion by reducing scope of licensed patents from all patents in the field to carefully enumerated patents, and making explicit such other patents as are not being licensed.

**Text:**

**“LICENSED PATENTS”** means any and all Patents owned or controlled by LICENSOR and its Subsidiaries as of the Effective Date or thereafter during the life of this Agreement and any and all Patents owned by a third party and under which LICENSOR or its Subsidiaries have a right to grant licenses or releases as of the Effective Date or thereafter during the life of this Agreement, *provided that such Patents are listed in Appendix A. For avoidance of doubt, LICENSED PATENTS does not include any patent not listed in Appendix A and does not include any patent listed in Appendix B.*

**CLAUSE C**

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**Purpose:** License for a portion of a patent, licensing a subset of the patent’s claims:

**Text:**

## **Article 1: Definitions**

**1.1 Licensed Patent:** “Licensed Patent” means U.S. Patent No. #,###,###.

**1.2 Licensed Patented Inventions:** “Licensed Patented Inventions” means claims \_\_\_-\_\_\_ of U.S. Patent No. #,###,###. [*e.g.*, which claims describe an integrated circuit]

**1.3 Non-Licensed Patented Inventions:** “Non-Licensed Patented Inventions” means claims \_\_\_-\_\_\_ of U.S. Patent No. #,###,###. [*e.g.*, which claims describe a computer system that uses the Licensed Patented Inventions integrated circuit –or- a method of running a computer system using the Licensed Patented Inventions integrated circuit]

**1.4 Licensed Products and Services:** “Licensed Products and Services” means \_\_\_\_\_. [*e.g.*, products and services, the manufacture, use, importation, sale or offer for sale of which would, but for this Agreement, infringe any valid claim of the Licensed Patented Inventions]

## **Article 2: Patent License**

**2.1 Grant of License:** Licensor hereby grants to Licensee a non-exclusive, non-transferable, limited right and license[, with a limited right to sublicense as described below,] under the Licensed Patented Inventions to make, use, import, offer for sale or sell Licensed Products and Services.

**2.2 Acknowledgement of Limited License.** Licensee acknowledges the license and ability to sublicense in Section 2.1 is limited to the Licensed Patented Inventions, and does not include the Non-Licensed Patented Inventions. Licensee further acknowledges Licensee can not extend to its customers and its sublicensees any rights or licenses under Non-Licensed Patented Inventions. Licensee further acknowledges and agrees that the Licensed Patented Inventions are (i) patentably distinct from, (ii) have other reasonable uses beyond those described by, (iii) do not practice, and (iv) do not embody the essential features of, the Non-Licensed Patented Inventions.

**2.3 Notice to and Acknowledgement by Customers and Sublicensees.** Licensee shall inform Licensee’s customers and sublicensees and cause such customers and sublicensees to acknowledge that Licensee has only a limited license as described in Section 2.1 and to join and confirm Licensee’s acknowledgement in Section 2.2.

**2.4 Covenant Not to Sue.** Licensor acknowledges that Licensee may make, use, import, offer for sale, or sell to or for a third party the Licensed Products and Services. Licensor covenants not to sue Licensee for any and all claims or rights of action that Licensor has or will have against Licensee and that arise out of or are related to any act of contributory

infringement or alleged contributory infringement of the Non-Licensed Patented Inventions based on the aforementioned acts.

## **CLAUSE D**

**Purpose:** License for particular products of a portion of a patent, featuring a covenant not to sue that further protects with respect to product-related, potentially infringing uses downstream.

### **Text:**

#### **Article 1: Definitions**

**1.1 Licensed Patent:** “Licensed Patented” means U.S. Patent No. #,###,###.

**1.2 Licensed Products and Services:** “Licensed Products and Services” means products and services [describe particulars of field or type of products and services], the manufacture, use, importation, sale or offer for sale of which would directly infringe any valid claim of the Licensed Patent.

#### **Article 2: Patent License**

**2.1 Grant of License.** Licensor hereby grants to Licensee a non-exclusive, non-transferable, limited right and license[, with a limited right to sublicense as described below,] under the Licensed Patent to make, use, import, offer for sale or sell Licensed Products and Services.

**2.2 Covenant Not to Sue.** Licensor acknowledges that Licensee may make, use, import, offer for sale or sell to or for a third party the Licensed Products and Services. Licensor covenants not to sue Licensee for any and all claims or rights of action that Licensor has or will have against Licensee and that arise out of or are related to any act of contributory infringement or alleged contributory infringement of the Licensed Patent based on the aforementioned acts.

**2.3 Acknowledgement of Limited License.** Licensee acknowledges the license and ability to sublicense in Section 2.1 is limited to the Licensed Products and Services. Licensee further acknowledges Licensee cannot extend to its customers and its sublicensees any rights or licenses not licensed herein. Licensee further acknowledges and agrees that the claimed inventions licensed herein are (i) patentably distinct from, (ii) have other reasonable uses beyond those described by, (iii) do not practice, and (iv) do not embody the essential features of, the claimed inventions not licensed herein.

**2.4 Notice to and Acknowledgement by Customers and Sublicensees.** Licensee shall inform Licensee’s customers and sublicensees and cause such customers and sublicensees to acknowledge that Licensee has only a limited license as described in Section 2.1 and to join and confirm Licensee’s acknowledgement in Section 2.3.

## **CLAUSE E**

**Comments:** *Quanta Computer* removed a certain amount of downstream patent infringement liability, to the detriment of the patentee, and does not appear to require different indemnity language. It may be necessary, however, to avoid financial distress to the component supplier by avoiding indemnification of systems-level infringement claims.

**Purpose:** Provide indemnification for component-level infringement claims while avoiding systems-level infringement claims.

### **Text:**

**1. Indemnification for Patent Infringement Claims Against Product:** Supplier agrees to indemnify and save harmless Buyer, its customers, successors and assigns, from any and all expenses, liabilities or other losses arising from or by reason of any actual or claimed infringement of any patent or patent claim that is directed to the selling or offering for sale of a Product, provided that:

- (a) Such claim of infringement is directed only at the Product standing alone;
- (b) Buyer gives Supplier prompt notice in writing of any such suit and permits Supplier, through counsel of Supplier's choice, to answer the charge of infringement and defend such claim or suit;
- (c) Buyer provides Supplier information, assistance and authority, at Supplier's expense, to enable Supplier to defend such suit; and
- (d) Buyer gives Supplier full control of any settlement negotiations.

If the sale of the Products provided hereunder is enjoined as a result of an infringement suit, or, at Supplier's sole option and discretion after a claim for indemnity is made, then Supplier, at no expense to Buyer, shall either procure the right for Buyer and its customers to continue selling or using the Products, or replace or modify same so that they become non-infringing and are of equivalent or superior functionality.

**2. No Indemnity for Patent Infringement Claims Against Product Combined With System.** Supplier expressly does not indemnify and save harmless Buyer, its customers, successors and assigns, from any expenses, liabilities or other losses arising from or by reason of any actual or claimed infringement of any patent or patent claim that is directed to the making, selling, offering for sale, licensing, or use of the Product in combination with a System, regardless of whether Supplier is aware of the intention of Buyer to use the Product in combination with a System.

Should a claim of infringement be made against the Product in combination with a System, the parties agree not to contest joinder in any such litigation but to cooperate with each other regarding such joinder, and to reasonably cooperate in the defense of any

such litigation, [including evenly dividing the cost of any such litigation, including the attorneys fees, between the Supplier and Buyer] [alternatively – put the cost sharing at different percentages, depending on the profitability of the Supplier/Buyer].

The parties agree that no settlement may be entered into respecting such Litigation absent the consent of both parties.

## **CLAUSE F**

**Purpose:** Establishes a multi-tiered license in which Licensor (LG in the *Quanta Computer* case) licenses its technology to the component manufacturer Licensee (Intel in the *Quanta Computer* case) and receives a royalty from both the Licensee and the downstream users (such as Quanta Computer, Inc. in the *Quanta Computer* case) at each stage in the production of a product

### **Text:**

#### **Article 1: Definitions**

**1.1 Licensed Products** – “Licensed Products” shall mean [standard language identifying specifically known component products sold by Licensee], and shall also mean and include any product sold by Licensee which, but for this Agreement, would infringe one or more of the claims of the Licensed Patents.

**1.2 Downstream Use** – “Downstream Use” shall mean a product or method in which a Licensed Product is combined with one or more other components or systems and which, but for this Agreement and disregarding the doctrine of patent exhaustion, would infringe one or more of the claims of the Licensed Patents.

**1.3 Downstream User** – “Downstream User” shall mean a person who makes a Downstream Use.

**1.4 Downstream License** – “Downstream License” shall mean a sublicense under Licensee’s license herein to the Licensed Patents, granted directly or indirectly by Licensee for use of intellectual property associated with one or more Licensed Products.

**1.5 Downstream Licensee** – “Downstream Licensee” shall mean, as to any particular Downstream Licensee, a Downstream User who obtains such Downstream License.

**1.6 Downstream License Royalties** – “Downstream License Royalties shall mean the royalties to be paid under a Downstream License.

#### **Article 2: Grant of License**

**2.1 Grant of License.** [Standard license grant from Licensor to Licensee]

**2.2 Royalties.** In consideration of the license granted above in Section 2.1, Licensee shall pay Licensor a royalty equal to \_\_\_% of Net Sales of Licensed Products.

### **Article 3: Downstream Licenses**

**3.1 Right to Grant Downstream Licenses.** Licensee shall have the right to grant a Downstream License to any Downstream User.

**3.2 Downstream License Royalties.** The royalty to be received by the licensor of a Downstream License shall not be less than \_\_\_% of the Downstream Licensee's Net Sales, as calculated under the formula herein for Licensee's Net Sales.

**3.3 Right to Grant Indirect Downstream Licenses.** Licensee shall have the right to grant to its direct Downstream Licensees the right to grant Downstream Licenses in turn to indirect Downstream Licensees, including the right of those indirect Downstream Licensees to grant still further Downstream Licenses recursively. Each such Downstream License shall contain the required provisions identified in Sections 3.4, 3.5, and 3.9 below.

**3.4 Allocation of Downstream License Royalties.** Royalties from Downstream Licenses shall be allocated among Licensor and Licensee and/or intervening licensors of such Downstream License, with Licensor receiving \_\_\_% of such royalties. Licensee and/or the intervening licensors of a Downstream License may rebate or waive its or their portion of Downstream License Royalties, provided that Licensor continues to receive Licensor's full allocation of Downstream License Royalties as calculated herein.

**3.5 Required Provisions of Downstream Licenses.** Each Downstream License shall include provisions accomplishing the following actions:

(a) Requiring the Downstream Licensee to pay at least the same percentage of such Downstream Licensee's Net Sales as are provided herein, and requiring that such royalties be paid as will yield to Licensor the same allocation of Downstream License Royalties from such Downstream Licensee as are provided herein;

(b) Requiring quarterly reporting, with at least the same specificity of reporting as required of the Licensee under this Agreement, and quarterly payment of Downstream License Royalties, and requiring such reporting and payment be made no later than thirty days following the close of the applicable calendar quarter;

(c) Giving the Downstream Licensee the option to report and pay Licensor's portion of the Downstream License Royalties directly to Licensor or else to the licensor of such Downstream License;

(d) Making timely payment of the Downstream License Royalties of the essence of such agreement;

(e) Making licensor of such Downstream License directly liable to Licensor for the shortfall in the event the Downstream Licensee fails to pay timely any installment of Downstream License Royalties.

(f) Making Licensor a third-party beneficiary of the Downstream License, with rights including but not limited the right directly to collect from or sue the Downstream License for Downstream License Royalties not timely paid.

(g) Requiring the Downstream Licensee to permit disclosure of its identity to the Licensor, with the provision that Licensor shall keep such information in confidence, and shall not use such information for any purpose other than collection of Downstream License Royalties.

(h) Requiring the Downstream Licensee, if it grants any Downstream License itself, to perform the following actions:

(i) Include in such Downstream License all the same required provisions as are specified herein.

(ii) Promptly provide to Licensor or to the licensor of its own Downstream License the identity of the Downstream Licensee.

(iii) Promptly forward to Licensor or to the licensor of its own Downstream License the identity of any Downstream Licensee reported to it and the royalty reports and payments for or through such Downstream License received by it.

**3.6 Default of Any Downstream Licensee.** In the event of any Downstream Licensee's failure to pay timely any Downstream License Royalties under a Downstream License, Licensee shall promptly pay to Licensor any such shortfall in royalties, regardless whether Licensee is the direct or indirect licensor of such Downstream License.

**3.7 Identification of Downstream Licensees.** Licensee shall promptly identify to Licensor all Downstream Licensees. Licensor shall keep such information in confidence, and shall not use such information for any purpose other than collection of Downstream License Royalties.

**3.8 Pass-through of Downstream License Royalty Reports and Payments.** Licensee shall promptly forward to Licensor the Downstream License Royalty reports and payments of any Downstream Licensee received by it.

**3.9 Requirement of Downstream License.** Licensee shall not provide Licensed Products to a Downstream User unless: (a) such Downstream User has procured a



Downstream License from Licensee, or (b) Licensee receives assurance from Licensor that such Downstream User has procured from Licensor a suitable license to the Licensed Patents.

**Option:** Tiered royalty schedule

Licensee's License and/or the Downstream Licenses may calculate royalties based on a tiered royalty or per-piece schedule instead of a flat Net Sales percentage royalty.

**Option:** Royalty-free cross-license

Useful, for instance, where Licensor and Licensee have comparable patent portfolios. Using this option, all royalties for Licensor come solely from downstream users and not from licensee.

**In Section 2.1:** Insert a mutual license grant and specify license as being royalty-free.

**In Section 2.2:** Delete section.

**New Section 2.3: Minimum royalties.** Beginning one year after the Effective Date, Licensee shall quarterly pay to Licensor the larger of the Downstream License Royalties collected in that quarter or \_\_\_\_\_ Dollars (\$ \_\_\_\_\_).

**Additional modifications may need to be made to ensure the license is royalty free.**

**DISCLAIMER:** These model clauses are not legal advice. IPO does not endorse or recommend these or any other particular clauses for use in any particular situation. These clauses are provided as one possibility only, and do not replace the need for a qualified attorney to thoroughly review the situation and to draft provisions tailored to the client's specific situation.

**FEEDBACK:** Please send any comments, corrections, or suggested topics to: [jbrowning@gbpatent.com](mailto:jbrowning@gbpatent.com)