

PRACTICAL ADVICE

FROM THE FASHION LAW GROUP



Fox Rothschild LLP
ATTORNEYS AT LAW

Are You Fit to License?

These days, everyone seems to be talking about licensing. Given that a company's intellectual property tends to be its most valuable asset, licensing is a natural step in the growth and development of a successful fashion company. Licensing allows a company to expand its "brand" onto a variety of products, made by those who specialize in that industry. Done right, licensing gives a company opportunity for massive growth in a very short amount of time, for a minimal investment.

What Is Intellectual Property?

There are several categories of intellectual property, including trademarks, copyrights and patents. Trademarks are words, logos or slogans that distinguish the source, origin or sponsorship of a good or service. Copyrights protect forms of original expression fixed in a tangible medium, such as literary works, computer software and sound recordings. Patents protect ideas that take the form of useful, novel and non-obvious inventions, such as production methods, devices and mechanical processes. Trademarks are fundamentally different from copyrights and patents in that trademarks protect customers from confusion while copyrights and patents protect your company's creations.

To maximize the value of your intellectual property, you should register it with the U.S. Patent and Trademark Office or with the U.S. Copyright Office. Further, protecting your intellectual property is vital in maximizing your financial return. A few steps you can take to protect your intellectual property include registering it with the U.S. Customs and Border Agency; registering it internationally, especially in those places where you manufacture, distribute or retail goods; and closely monitoring the public domain to quickly take action against unauthorized use.

What Is Licensing?

Licensing is the process of "renting" a company's intellectual property to another entity, for a sum of money called royalties, for a certain product or category of products, for an agreed upon period of time within a certain territory. Intellectual property can be carved up as the owner deems best, and different territories and fields of use can be given to different licensees. In general, the purpose of licensing is to extend the brand's trademark or other related intellectual property onto products of a completely different nature, creating a revenue stream where one previously did not exist.

How Does It Work?

The "licensor" or the intellectual property owner will sign a contract with a "licensee." In the fashion industry, the licensee is typically a manufacturer, but can also be a direct retailer (Target or Kohls, for example). The contract grants the licensee permission to use the licensor's intellectual property, within certain parameters. When the licensee sells products using the licensor's intellectual property, the licensee must pay the licensor royalties. Royalties are generally a percentage of sales, but may also be a fixed sum per item sold. When the contract term expires, the licensee no longer has the right to use the intellectual property of the licensor.

Why Should I License?

There are many benefits to licensing, to both the licensor and the licensee.

Benefits to the Licensor Include:

- Generating revenue;
- Expanding brand awareness;
- Expanding brand customer base; and
- Expansion is financed by the licensee.

Benefits to the Licensee Include:

- Increasing sales by offering its products under the umbrella of a well-known brand;
- Less risk because license is for recognized brand;
- Opens doors with established retailers;
- Creating instant recognition and awareness of the product; and
- Bootstrapping on the marketing and PR of the intellectual property owner.

I Am Ready to License. Now What?

Once you are sure your intellectual property is properly protected, you need to find the right deal. Some companies are approached by those who wish to license its brand. Others work with a licensing agent and/or a brand manager. Generally, a licensing agent brings potential parties together, may help negotiate the terms of the deal and is paid a percentage of the royalties. A brand manager is a representative customarily hired by the licensor to assist in the development and implementation

or getting to know one another. Most licensing agreements last three to seven years, with renewal options, so your goal should be to gather as much information, pre-agreement, as possible.

Once you have found the right match, it is time to negotiate and draft the licensing agreement. Usually, each party will draft a term sheet. This is a high level document outlining your key terms and is anywhere from one to three pages. This can be drafted by the parties, with the licensing agents or with the aid of an attorney. After the key terms are agreed upon, the lawyers will memorialize your terms into a final agreement for execution.

5 Key Points for Negotiating a Licensing Agreement:

1. What Does the License Cover?

A license can be non-exclusive or exclusive. An exclusive license and a non-exclusive license are fundamentally different. With an exclusive license, all your eggs are in one basket, while a non-exclusive license may leave the licensor with competing licensees. An exclusive license must have minimum sales requirements.

The parties have the ability to determine the breadth of goods covered by the license. The products can be as broad as any product anywhere in the world or narrowly defined down to the country, product category and strata of the market. It is important to conduct due diligence on your potential licensee to make sure it has the capability, capacity and resources to handle the range and volume of products required or envisioned by the agreement.

2. Design and Quality Control

A company usually has achieved a certain degree of success prior to exploring licensing opportunities. It is vital that the licensor retain the appropriate amount of control over the quality of products produced under its brand name. Trademark law requires quality control, so the agreement must give the licensor the right to approve or monitor the design of the product line or key products and the right to ensure the licensor's quality standards are met. Defining the right standard is important and may be difficult. The agreement should also provide guidelines on what will happen if proper quality is not maintained.

3. Revenue Stream

The first thing clients ask me when entering into a licensing deal, is "what percentage royalty can I get?"

The percentage usually depends on the incremental value conveyed to the licensee. The value of the territory, market, field of use and customer rights dictate the appropriate royalty. The percentage, however, is not as important as ensuring that percentage is off of the best possible revenue stream. In fashion, trademark royalties typically range from three to 12

percent, and the best revenue stream would be off of wholesale sales. Generally, the more well-known a brand is, the higher the royalty percentage. Also, the more exclusive the license is, the higher the royalty rate will be. Alternative revenue streams include gross sales, net income and net profits. **BONUS REVENUE STREAM:** If the owner of the intellectual property is well-known or an integral part of the brand, that person, as an individual, may also negotiate for marketing, design and public relations fees as compensation for promoting the licensed product.

4. Intellectual Property Control

A company's intellectual property is usually its most valuable asset. If the licensing agreement expands a licensor's business into new countries, its intellectual property must be protected in those countries and the registrations must be in the licensor's name. A licensing agreement should make sure that the licensee will not gain a permanent property interest in the licensor's intellectual property. Finally, the agreement should clearly state what happens to the licensee's right to use the licensor's intellectual property upon termination of the agreement, either when it expires or upon a breach.

5. Right to Monitor/Audit

After you have spent time and energy finding the right partner and negotiating the best deal possible, you need to make sure your agreement gives you the right to monitor the sales of the licensed goods by receiving regular reports and you have the right to inspect and audit the licensee's books upon reasonable request. License agreement compliance and auditing is often overlooked, and it is recommended that you consult with a professional who concentrates in fashion royalty auditing so you maximize the value of your intellectual property.

In conclusion, the right licensing agreement has the potential to provide a new revenue stream where one did not previously exist. You can expand your customer base and heighten brand awareness. An ill-fitting match or poorly drafted agreement can cost you more than just lost sales of the licensed product. It can harm your core business and, more importantly, customer goodwill. It is better to move slowly and get the right deal instead of pouncing on the first one that may come your way. While there are many professionals available to guide your journey into licensing, choose those with knowledge and experience with your core business and/or in the area covered by the licensing agreement.

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