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Negotiation Techniques for Warranty and Enforcement Clauses in International Licensing Agreements

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NEGOTIATION TECHNIQUES FOR WARRANTY AND ENFORCEMENT CLAUSES IN INTERNATIONAL LICENSING AGREEMENTS

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I. INTRODUCTION

The literature on negotiating techniques for international license agreements has focused on the following points:[1]

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1. M. Finnegan & A. D'Andrea, *The Black Box Problem: Using Pre-Negotiation Secrecy Agreements to Govern Disclosure of Technology to Potential Licensees*, LICENSING LAW AND BUSINESS INSTITUTE (1979); Finnegan & Mintz, *Determination of A Reasonable Royalty in Negotiating A License Agreement: Practical Pricing for Successful Technological Transfer*, 1 LICENSING LAW AND BUS. REP. 13 (1978); Melman & Mizrack, *Drafting and Negotiation of Secrecy Clauses in Licenses: A Practical Approach*, 7 AM. PAT. L.A.Q.J. 26 (1979); McKinney, *Selection of What Technology to License*, THE LAW AND BUSINESS OF PATENT AND KNOW-HOW LICENSING, D-1 (M. Finnegan & B. Brunsvold, ed.

(1) The scope of the technological value to be transferred by the licensor to the licensee, including any limitation on use, market territory, and time period;

(2) the nature of the grant by assignment, exclusive license, nonexclusive license, or sole license;

(3) the compensation to be paid by the licensee to the licensor; and

(4) the obligation of the licensee to maintain any confidential know-how or trade secrets transferred under the agreement.

There is a shortage, however, of published information concerning the legal and business implications of negotiating warranty and enforcement provisions in international license agreements. The licensee often requests the following three types of clauses: Defense and indemnity against patent infringement actions by third parties, performance guarantees, and enforcement of licensed patent rights against third parties.

The contingent economic effects of these clauses can be significant and can affect the amount of compensation needed by the licensor to guarantee him an adequate return on his investment. Thus, these clauses should be thoroughly considered by the licensor during his planning and negotiating stages and should be discussed before an agreement is reached concerning the form of the agreement and the amount of consideration to be paid by the licensee.

II. Pre-Negotiation Planning

The importance of the licensor's pre-negotiation planning cannot be overemphasized. License earnings are significantly related to the care with which licensing possibilities are analyzed and evaluated. Pre-negotiation planning then, more directly affects the return on licensing than the actual negotiation, no matter how brilliantly the negotiation is performed. The pre-negotiation planning should include the following steps:

(1) Identification of a licensable area of technology, a technology that would provide potential licensees with an advantage in the marketplace;

(2) estimation of the licensor's market share and return on in-

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1971); Sommer, *Organization and Preparation for Licensing Transactions*, 7 Am. Pat. L.A.Q.J. 13 (1979); Sperber, *Successful Negotiation in Licensing*, 8 Pat. L. Rev. 93 (1976); White, *Some Standard Negotiating Techniques and Some Thoughts on Non-Verbal Communication*, 5 Litigation 17 (No. 1, 1978).

vestment in the market where the technology is used;

(3) identification of the effect of licensing on the licensor's share of the market and the licensor's return on the investment;

(4) estimation of investment, earnings, and return on investment for a licensee;

(5) identification of proprietary rights, legal problems, and tax goals;

(6) estimation of the value of the technology to be transferred;

(7) estimation of what the licensee will do if he is not licensed; and

(8) setting of ranges and payment terms for conducting negotiations.

The information needed to complete this planning is not easy to obtain. Much of the information will necessarily be based on estimates. Unless the licensor already has other licenses, the licensor's personnel will not have hard data available. A pre-negotiation plan, however, even when based on very rough estimates, will usually produce a better return for the licensor than no plan at all.

III. A Team Approach is Usually Needed for Effective Negotiation

The pre-negotiation planning procedure shows that information for the planning steps is needed from marketing and production personnel, lawyers, researchers, engineers, management, and a licensing specialist. A licensor usually cannot afford to have all of these personnel present at the negotiating sessions. A licensing negotiation proceeds most efficiently when the negotiating team includes people who are familiar with marketing the licensed product and experienced in the technical details of the subject matter to be licensed. A lawyer is also necessary to provide legal advice during negotiations and draft or review the negotiated agreement. There are some situations in which an individual familiar with the technology can fill more than one of the three roles. The scope of discussion during licensing negotiations is usually free-wheeling with fast shifts in subject matter. If one side does not have an experienced representative in at least one of these fields at a negotiating session, effective discussion and resolution of issues becomes difficult.

One member of the licensing team should be designated the negotiation leader. This team leader should be accountable to higher management for the outcome of the negotiation. Since members of a licensing team are usually from different parts of a corporate organization, management should make the leader's authority known to all team members. The team leader does not have to make all the verbal presentations. For example, the presentation of the licensor's initial position is sometimes most effectively made by junior members of the team, particularly when the initial positions are know to represent highly optimistic views of the ultimate licensing terms.

To some extent, the actual or anticipated nature of the licensee's negotiating team influences a decision by a licensor about who should be present at the face-to-face negotiations. For example, it is sometimes a disadvantage to have a team member with more decision-making authority than is present on the other side's licensing team. There is always the possibility that the other side may demand immediate decisions while claiming an inability to make comparable binding promises because of lack of authority.

IV. The Importance of Selling the Licensee on the Advantages of the Technology

The key to a licensor's negotiating success is to convince the licensee that the licensor's technology offers unique advantages. If the candidate licensee is convinced that he wants and needs the licensor's technology, negotiations will usually proceed smoothly to a monetarily rewarding license. If the licensee is not convinced of the value of the technology to its future operations, negotiating tactics and skills will be useless, and the licensor will not come away with a satisfactory agreement. When the candidate licensee is not familiar with the technology involved, it is desirable to whet the licensee's interest before making a complete licensing proposal. Before any discussion begins on the nature of the technology transfer agreement, an initial meeting should be arranged between the technical and marketing personnel of the two parties to discuss the technical and commercial advantages of the licensor's technology. The absence of a lawyer or a business manager at this meeting can be used to explain the inability to present any concrete agreement proposal. Illustrations such as graphs, charts, products or product mock-ups, and a nonconfidential illustrated prospectus can advantageously be used to sell the technology to the candidate licensees.

The licensee should have its desire for the technology aroused before the licensor makes its first formal offer. Otherwise, the licensee may be put off by the licensor's initial offer, which will normally call for higher payments than the lowest figure that the licensor will accept. The level of the first offer is critically important in influencing the ultimate agreement. It can drastically elevate the candidate licensee's perceptions of what comprises reasonable payment terms, but only if the licensee has previously decided that he really needs the technology.

V. The Indian Blanket Technique

Most licensing negotiations are conducted as if the parties were trading with an Indian selling blankets. The licensor's initial proposal calls for payments far in excess of what he is willing to accept, and the candidate licensee's initial response sets forth payment terms below what it is willing to pay. Negotiations result in a compromise somewhere in between. If a licensor appears at the initial negotiation session and honestly says to the candidate licensee that the present value of licensor's total compensation from the agreement must be at least two million dollars for the license to be worthwhile, the licensor will be accused of being unwilling to negotiate. On the other hand, if the licensor's initial offer is for four million dollars and eventually drops to two million, no one can accuse him of negotiating in bad faith.

Unfortunately, the Indian blanket technique tends to make license negotiations time consuming and protracted. This approach, however, does have one desirable side benefit. As the parties move their offers and counteroffers closer together, they create the appearance of progress toward agreement during each negotiating session, which is a highly desirable result. The absence of any progress during a face-to-face licensing negotiation session can severely reduce the possibility of ultimately reaching an agreement. Long term psychological effects are created if the licensor is forced to renege on payment terms previously agreed upon. Thus, it is desirable for a licensor to negotiate patent infringement defense and indemnity provisions, patent enforcement provisions, and performance guarantees before definitely outlining the payment package he has in mind.

VI. Defense and Indemnification of Third Party Patent Infringement Suits

The transfer of technology in an international license agreement sometimes infringes upon a third party's patent. This is particularly true when the licensee will be using the technology outside the United States. The United States patent system is widely criticized for issuing too many invalid patents. The Patent Office's performance, however, is superior when compared to the performance of other patent offices throughout the world. Only the German and Dutch patent offices have examination procedures that produce the quality and predictability of patents that United States lawyers and businessmen expect. It is not uncommon for the patent offices in some industrial Western European nations to issue a patent covering a basic development that originated in North America or Japan ten to fifteen years earlier. The issuance of such a patent can prove to be a problem for the licensor or the licensee, depending upon the nature, existence, or nonexistence of any patent defense and indemnification provisions in the basic license agreement.

While a licensor usually wants to restrict, or even exclude, his liability for infringement actions brought against the licensee, the licensee wants to obtain as much protection as possible. The licensor will find it difficult to meet the legitimate needs of the licensee without exposing itself to undue financial risk. In most international license agreements, the licensee is bargaining for and obtaining technology that will enable it to go into a new product line. Such an undertaking requires new plant facilities and capital investment. The licensee has a strong and legitimate need for assurance that its capital investment can continue to be used. On the other hand, the licensor's total return may well be less than the licensee's capital investment. This is particularly true if plant equipment and market development costs are viewed as investments. The licensee will normally find such a situation unacceptable, if the licensor states that firm company policy prohibits granting indemnity agreements or assisting in the defense of infringement suits against a licensee. The licensee will claim that the licensor should know the patent situation. Good licensing practice dictates that a licensor should negotiate with the licensee to provide him some reassurance.

The licensor can be expected to be reasonably aware of the existing patent position of third parties in the technical field of the license agreement for the license territory. The licensor cannot, however, be expected to reasonably foresee the actions of the host country's patent office. Thus, in most international license agreements, it is desirable for the licensor to attempt to limit any patent defense and indemnity provision to patents that have been issued prior to the date of the execution of the license agreement. For an example of such a clause, see Appendix Clause E at the end of this article.

In many foreign countries there is no accurate way to predict the scope of patents issued from the patent office of the licensee's home country. The licensor can argue that the actions of such a patent office constitute a risk more closely related to doing business in the particular country than a risk associated with the licensed technology.

In a typical international license agreement, the transfer of know-how and technical information covers a broad spectrum of potentially infringing subject matter. Particularly in the licensing of process know-how, any defense and indemnity agreement should be limited in scope to the licensee's activities that conform to the drawings, specifications, and detailed process operating conditions that are transferred by the licensor. It is also wise for the licensor to require approval of the licensee's actual process equipment, drawings, specifications, and operating manuals by the licensor as a condition precedent to activating the defense and indemnity provision. Examples are found in Appendix Clauses D and F. Typically, the extent of the licensor's liability for the patent defense and indemnity provision is expressed as a percentage of the payments that are collected under the agreement. While the upper limit of the indemnity is definitely a subject for negotiation, a common amount is twenty-five to fifty percent of the payments made by the licensee under the agreement.

Severe planning, drafting, and negotiating problems occur when the parties discover that the use of a licensed patent may result in infringement of an existing third party patent and that the licensee may need another license. With respect to the royalties that may come due under the other license agreement, does the licensee pay, does the licensor pay, or is the burden split? The licensor should never obligate himself to pay more for the third party license than he will receive under the original agreement. Similarly, the licensee should have some financial incentive to negotiate as low a rate as possible with the third party patent owner. If the licensee is not provided with such an incentive, he will probably negotiate a high royalty rate, virtually eliminating his royalty obligations to his first licensor.

Another alternative is an agreement that the licensee will defend infringement suits. The funds expended in such a defense will be offset against future royalties due the licensor. A licensor's liability to defend and indemnify is usually conditioned upon prompt notification by the licensee of any claims against it and the licensee's full cooperation in defending the lawsuit. When a licensor agrees to indemnification of the licensee or to defend against infringement suits, the licensor may limit the commitment to the licensee alone or may extend it to cover the licensee's customers. When the parties agree to share the cost of defending a third party infringement action, it is advisable to establish in the agreement which party will have control of the lawsuit.

VII. Enforcement of Licensed Patent Rights

A. *Fundamental Legal Principles*

Under United States law, there is no implied obligation on the part of the licensor to protect the licensee against patent infringement by third parties.[2] The licensee, therefore, must obtain an express provision in the license agreement to obligate the licensor to sue infringers. If the licensor agrees to sue third party infringers, it is very important that his obligation be specifically defined in the license agreement. Since a nonexclusive license is merely a waiver of the licensor's right to sue the licensee for infringement, a nonexclusive licensee has no enforceable right against anyone other than the licensor. The licensor is free to tolerate as many other infringers as he pleases, and he may grant as many other licenses as he chooses. Even the presence of the usual most-favored licensee clause does not help a nonexclusive licensee when third party infringements occur. Such a clause permits the licensee to take advantage of more favorable terms offered to a subsequent licensee. The failure of the licensor to proceed against third party infringers has not been construed by the courts as a royalty-free license, which would trigger the most-favored licensee clause.

With respect to an exclusive licensee, the licensor has no implied obligation to sue third party infringers under United States law. The licensor's failure to do so is usually not a defense in a licensor suit for royalties.[3] United States law recognizes, however,

2. Lathrop v. Rice & Adams Corp., 17 F. Supp. 622 (W.D.N.Y. 1936); Hazeltine Research Inc. v. De Wald Radio Mfg. Corp., 194 Misc. 81, 84 N.Y.S.2d 597 (Sup. Ct. 1948), *rev'd on other grounds*, 276 A.D. 1001, 95 N.Y.S.2d 772 (1950).

3. Sea Gull Specialty Co. v. Humphrey, 242 F. 271 (5th Cir. 1917); Martin v. New Trinidad Lake Asphalt Co., 255 F. 93 (N.J. 1919).

that an exclusive licensee stands in a different position than a nonexclusive licensee. An exclusive licensee receives more than immunity from suit. He has bargained for the exclusive right to practice the invention. This right is exclusive against the world except pre-existing licensees or the licensor, if he has reserved any rights. If this exclusive right is violated and the licensor does nothing about it, the exclusive licensee is not without a remedy. He can proceed either on his own to protect that right, or he may be able to cancel his license for failure of consideration. In international exclusive licensing situations where the law of the foreign licensee's home country is to be applied, United States licensors would be well advised to obtain counsel concerning the legal obligations of an exclusive licensee under the law of the licensee's country.

B. *Negotiating Approaches for the Licensor*

A licensor in a nonexclusive license situation would obviously like to avoid any obligation to sue infringers. From the standpoint of a nonexclusive licensee, a desirable way to protect his rights is to get an unrestricted right to terminate the license agreement on reasonable notice. A nonexclusive licensee should seldom be provided with anything more.

A licensor who grants an exclusive license should try to insert a specific provision in the license agreement dealing with third party infringement. Sometimes the licensor might want to provide that the filing of an infringement suit against the third party will be at the sole discretion of the licensor. From a tax standpoint under United States law, however, a reservation of the right to bring suit at the licensor's sole judgment might be sufficient to negate capital gains treatment for the royalties under the agreement. The reason for this would be that a court might find a failure to transfer all the substantial rights to the licensee. If a licensor does not reserve to his sole discretion the institution of infringement suits against third parties in an exclusive licensing situation, he can retain the right of first refusal to bring such infringement suits. If the exclusive licensor fails to reserve this right, an exclusive licensee has the option to bring suit in the licensor's name in many countries. An exclusive licensee may be given the option to sue infringers. Generally the expense of such litigation is borne by a licensee, who is entitled to all damages recovered.

From the standpoint of the exclusive licensor, his obligation to bring infringement suits should be carefully defined, for example, reasonable standards for substantial infringement should be included in the license agreement. The licensor should specify that he is not obligated to bring more than one infringement suit at a time and require that royalties will accrue during the period of any third party infringement litigation.

Because of the antitrust laws,[4] license agreements should not require a joint decision by the patent owner and the licensee on the institution of third party infringement suits. Ordinarily, a licensor should have sole discretion to decide on infringement suits in a nonexclusive licensing situation. In an exclusive licensing situation, such a decision should be unilateral. The decision should be entrusted to either the licensor or licensee depending upon the specific factual situation. When the decision to sue is a unilateral one, antitrust problems do not normally arise if the patent owner and licensee share in the recovery of cost of the suit. If the license agreement does provide for joint participation, it should prescribe which party has the right to choose counsel and control the conduct of the litigation.

A license agreement should clearly and carefully provide for the terms and conditions under which a licensed patent is to be enforced against third parties. Specific provisions that set forth enforcement duties protect the rights of the licensee, as well as those of the licensor.

VIII. Performance Guarantees in International License Agreements

A United States licensor of technology can expect a foreign candidate licensee to request performance guarantees. The grant of such guarantees can create severe monetary risks for the licensor and disincentives on the part of the licensee's employees to make the new technology work. Some large United States companies refuse to grant performance guarantees for these reasons. These companies promise only to supply the licensee with the technology that has enabled the licensor to produce a specified product at a specified rate and to provide technical assistance, usually for a fee to help in the licensee's production start-up operation. This licensing technique may satisfy the licensee if he

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4. *E.g.*, United States v. Besser Mfg. Co., 96 F. Supp. 304 (E.D. Mich. 1951), *aff'd*, 343 U.S. 444 (1952).

can be shown a plant owned by the licensor that is producing the licensed product at the promised rate and quality. If a performance guarantee is avoided, the licensee's personnel have a strong incentive to achieve satisfactory production rates and quality as soon as possible.

Competition between licensors, particularly competing licensors, and the policy of some developing nations may require that the licensor grant some form of performance guarantee. If this is the case, the licensor should negotiate a guarantee that will provide it with a manageable risk. A performance guarantee is usually a separate warranty agreement concerning the quantity and quality of the output of a plant using the licensed process. It assures the licensee that what he is acquiring actually works. Such an assurance is universally requested by technically unsophisticated licensees when technical information and know-how relating to products, processes, or equipment is being transferred.

From the licensor's standpoint, the performance guarantee should not require that performance levels be achieved using only licensee's personnel. Licensor's engineers, usually present at the start-up of a new plant, can be vital to early achievement of the guaranteed performance levels.

The performance guarantee agreement should not be negatively oriented but should stress the positive aspects of the technology that is being transferred. The licensor should carefully designate the parameters of its performance guarantees and the extent of its liabilities. As was mentioned above, liability should be limited to a percentage of the fees received by the licensor.

The licensor must ascertain how the technology will be physically transferred to the licensee. The parties must arrange for visits to the licensor's factory to train the licensee's personnel. They must agree which party will pay for the expense of training, travel, and other necessary consulting services. Finally, the parties must specify at what point the licensor is entitled to receive specific remuneration for services beyond those to which they had originally agreed.

Most of the performance guarantees inure to the benefit of the receiving licensee. The licensor, however, can insert reciprocal performance guarantees from the licensee into the performance guarantee agreement. Since the licensor is transferring technology in which he has made a considerable investment, he will desire contractual provisions to protect his product or process from adverse publicity due to actions by the licensee. The most important items in this area are quality control, the right to periodic inspection, and the right of access to the licensee's records and production figures. The licensor needs assurances that the product produced by the licensee falls within an acceptable quality range. The licensor will also want production to proceed at a desirable rate. Without such guarantees, a licensor can find himself cheated and at the same time, can lose the good will associated with his fine quality products.

The technology that is being transferred will frequently include confidential and proprietary information that forms an integral part of the package that the licensee wants to acquire. This skill, experience, and imagination, which the supplier has developed at considerable cost requires protection just as great as the other parts of the license. Consequently, the licensor should insist on a warranty of nondisclosure in the basic licensing agreement. Only employees, agents, or subcontractors of the licensee who have a need to know critical information should be allowed access to this information. The licensee should agree to have all such persons sign an agreement prohibiting disclosure.

When the technology is being transferred between equally competent and efficient organizations that possess approximately equal technical and management skills, the transfer and training procedures are not as extensive or as detailed as those needed when the licensee is unskilled. The inexperienced licensee may not be immediately ready or able to exploit the acquired technology, or even to understand the technical files it has received. Problems exist when the result is guaranteed to such a licensee. The farther the licensee is geographically removed from the licensor, the greater the difficulty in guaranteeing the result. It is similarly true that, the greater the start-up costs, the greater the shock in the event of a failure. An ongoing partnership-like relationship, in which the licensor maintains a continuing interest in the success of the transfer, is essential when dealing with a licensee of limited technical experience and skill. The licensor should acknowledge the potential for a continuing drain on his resource of skilled training and start-up engineers and should price his technology and services accordingly.

The nature and cost of technical training and assistance to be provided to the licensee are at the heart of many performance guarantee problems. Some licensees, particularly those from developing countries, doubt the value and importance of these costs. They view their inclusion with suspicion and cannot understand the licensor's reluctance to guarantee the results without getting paid for extensive training and assistance. They do not realize that the licensor's experience contributes at least as much as, and sometimes more than, the fundamental scientific knowledge on which the technology is based.

In licensing to a developing country, the technology must frequently be adapted to the conditions present in that country. This may mean more than modifying a few operating conditions. It may be necessary to reconstruct entirely the technology as well as the know-how after a thorough analysis of the market, the raw material supply, and the technical skills of the acquiring state. In such situations, the licensee's demand for performance guarantees is rationally based, but to provide the licensee with the guarantees is very risky. The licensor should accordingly price the total licensing package at a high level to justify the potential risks.

The licensor, in dealing with a technically unsophisticated licensee, may be requested to guarantee that the transferred technology will be suitable for the purpose intended under the agreement. The licensor should not, however, warrant the suitability of the technology without some assurance that the licensee will use it properly and in accordance with the conditions specified in the agreement. Clauses in the contract that guarantee that the transferred technology is complete or that a predetermined level of production can be achieved with it are more easily defined and therefore less risky to the licensor than suitability clauses. In return for any guarantee by the licensor, the licensee should be willing to accept some stipulations regarding specific conditions of production or use that are reasonably related to the achievement of the desired result.

The licensor should be willing to train, for adequate compensation, the licensee's management and labor force in the proper use of the transferred technology. Such a provision is generally looked upon with favor by licensors since it is a means of insuring the success and profitability of the licensee and an adequate return on the license. A guarantee to provide training sufficient to enable the licensee's personnel to become proficient, however, carries some risks. By the inclusion of such a provision, the licensor has undertaken to train the licensee's personnel adequately. The licensor cannot reasonably be expected to warrant the quality, motivation, and learning ability of trainees over whom it has no control. While it is fair to expect a licensor to provide training, since to do less would be counterproductive to its own interests, the ultimate responsibility for providing qualified trainees rests with the licensee. Unfortunately, the determination of whether each party has performed according to a training agreement is highly subjective. A training guarantee can easily lead to undesirable disputes that cannot be easily resolved. Disagreements over the quality of the training of the licensee's personnel can threaten the basic relationship between the transferor and transferee and, therefore, should be avoided.

The existence of a training guarantee can also create a disincentive for the licensee to supply its best personnel to be trained in the licensed technology. Considering that most developing country licensees have a critical shortage of competent, experienced, and technically trained employees, this disincentive should not be dismissed lightly by licensors.

Some licensees ask for guarantees that the prices of equipment and raw materials needed from the licensor for production pursuant to the transfer of technology will be comparable to the current international market level. This is especially true when the recipient must acquire capital goods, intermediate inputs, or raw materials from the licensor. If the licensee has no alternative other than to acquire the raw materials or capital goods from the licensor, it is reasonable for the licensor to guarantee that these prices will be comparable to the international market price. Problems do arise when no comparable international market price exists for a particular time. This is frequently the case for intermediate level imports, such as automobile frames. This problem can be overcome, however, by the establishment of an international standard accounting practice that specifies a formula for the pricing of such items.

IX. Conclusion

The economic risks to a licensor of technology that are inherent in patent infringement defense and indemnity warranties, patent enforcement provisions, and performance guarantees can be substantial. Licensors should negotiate the existence or nonexistence of these clauses and factor in the resulting risks before proposing or agreeing to payment terms. Otherwise, the licensor will end up underpricing his technology.

APPENDIX

Selected Clauses Relating to Defense of Third Party Infringement Suits and Indemnification

Disclaimer of Liability by Licensor

A. Nothing in this agreement shall be construed as a warranty, representation, or covenant by Licensor to defend third party infringement actions brought against Licensee or its customers, or to indemnify Licensee or its customers for any judgment rendered in such an infringement action.

B. Licensee and Licensor as a result of independent studies have determined that no existing patent of ________ (set forth the Licensed Territory) presents a substantial infringement problem. Licensee agrees that it accepts all risk of infringement of existing and future third party patents in the Licensed Territory.

C. The parties have each independently investigated the state of the art relating to the Patent Rights and Know-How transferred by this agreement. Licensor warrants its operations utilizing Patent Rights and Know-How in the United States of America have not resulted in a claim, threat, or lawsuit based on allegations of infringement of a third party patent.

Licensor is not obligated to defend against any patent infringement lawsuit in the Licensed Territory resulting from the exercise or use of the Patent Rights and Know-How transferred by this agreement, and Licensor shall have no obligation to indemnify Licensee with respect to any judgment rendered as a result of such an infringement lawsuit. In the event that Licensee's right to use the Patents and Know-How transferred by this agreement within the Licensed Territory shall be asserted to be infringing, Licensor shall be obligated to disclose to Licensee all information that it possesses that is necessary to show the date or dates of discovery of the accused methods, processes, products, and techniques. Licensor shall not be obligated to incur any expense in connection with the lawsuit other than the above-described supply of information.

Licensor Only Defends

D. If a lawsuit is filed by a third party against Licensee, alleging that use or sale of Licensed Products (defined to be a product covered by Licensed Patent Rights, a product whose manufacture is covered by one or more Licensed Patents, or a product produced according to Licensed Know-How, which product has been produced to specifications and operating procedures approved in writing by Licensor) Licensor agrees, if promptly notified in writing by the Licensee of the institution of any such suit, to undertake the defense at Licensor's expense subject to: (1) Licensee's agreement to permit Licensor to control the defense of the lawsuit and (2) Licensee's cooperation including the items set forth in the following sentence. Licensee shall furnish to Licensor information and testimony as may be needed by Licensor in connection with the defense of the lawsuit, and shall not charge Licensor for the time of Licensee's employees engaged in furnishing such information or testimony. Licensor shall bear court costs and all attorney's fees, witness fees, and expenses incurred in preparing for and conducting the defense of the infringement litigation, including cost of expert consultants and expert witnesses. Licensor shall select the attorneys and experts of its choice.

Licensor Defends Only Against Previously Issued Patents

E. If a lawsuit is filed by a third party against Licensee alleging that manufacture, use, or sale of Licensed Products, or any process or apparatus used by Licensee in producing Licensed Products, infringes patent rights of a third party having an issue date prior to January 1, 1981, Licensor agrees, if promptly advised in writing by Licensee of the institution of any such suit, to undertake the defense of the lawsuit at Licensor's expense subject to Licensee's agreement to permit Licensor's control of the defense and settlement of the lawsuit and Licensee's cooperation as set forth below. Licensee shall furnish to Licensor information and witnesses as may be reasonably needed by Licensor in connection with the defense of the lawsuit. Licensee shall not charge Licensor for the time of Licensee's employees engaged in furnishing such information or appearing as witnesses. Licensor shall bear court costs, all attorney's fees, witness fees, and expenses necessarily incurred in defending the lawsuit, including costs of expert advice and testimony. Licensor shall have discretion to select the attorney of its choice. Licensor has no obligation to defend or indemnify Licensee with respect to lawsuits based on patents issued after January 1, 1981.

Defense and Indemnity

F. If an infringement lawsuit is filed against Licensee alleging that manufacture or sale of (1) Licensed Product or (2) any process or apparatus used by Licensee in producing Licensed Product, that has been approved in writing by Licensor, infringes any patent rights of a third party, Licensor agrees, subject to the conditions set forth in subsequent sentences of this paragraph, to defend the lawsuit at its own expense. Licensor's obligation to defend is subject to receipt of written (1) notice of the existence of the lawsuit, (2) agreement by Licensee to permit Licensor to control the lawsuit and any settlement thereof, and (3) agreement that Licensee will furnish to Licensor information and employee-witnesses as reasonably may be requested by Licensor in connection with defense of the lawsuit. Licensor shall pay the costs and expenses of the lawsuit except that Licensor shall not be obligated to pay Licensee for any expenses Licensee may incur providing Licensor with information and employee-witnesses. Licensor agrees to indemnify Licensee for damages, limited to an amount equal to one-fourth of all royalty payments received by Licensor from Licensee for Manufacture of Licensed Product, that may be assessed by any court of final jurisdiction for the infringement of the patent rights as a result of a lawsuit that this section obligates Licensor to defend and for which Licensee fulfilled its three above-described obligations.

Defense and Indemnity: Process License

G. Subject to the conditions of this paragraph, Licensor agrees to indemnify Licensee against liability established by any final decree or judgment rendered against Licensee in any lawsuit brought against Licensee by a third party for infringement of patents arising solely as a result of Licensee's operation of the Licensed Process under the patents and know-how licensed under this agreement. Licensor is to have control of the defense of any such lawsuit and will through its attorneys, at its expense, conduct the legal defense including the trial and any appeals of such lawsuit. Licensee agrees to notify Licensor promptly in writing of any claim for infringement, and of the service upon it of all legal process in any such lawsuit. Licensee agrees that it will assist Licensor in the defense of any such lawsuit by supplying information and employee-witnesses at no cost or expense to Licensor. Licensee shall have the right to be represented by counsel of its own selection at its own expense, which counsel shall act only as advisers in the defense of the lawsuit. Licensor's liability for defending Licensee and for indemnifying Licensee shall not exceed an amount equal to one-fourth of all payments received by Licensor from Licensee with respect to operation of the Licensed Process.

Licensor's Royalty is Diminished if Additional Royalty is Paid to a Third Party

H. If the practice of the Licensed Process is held to infringe patent rights of a third party by a court in Country X, Licensee may request that Licensor obtain a license for Licensee in Country X. If Licensor fails to obtain such a license for Licensee within three months after receipt of a written request from Licensee, then Licensee may execute a license (hereafter called the "Additional License") with the third party patent owner. If Licensee obtains an Additional License from a third party patent owner, Licensee agrees to receipt of diminished royalties under this agreement with respect to Country X as set forth below. Licensee may deduct from royalty payments due Licensor under this agreement fifty percent of the amount Licensee pays as royalty under the Additional License, up to a maximum of one-fourth the royalty otherwise required to be paid by Licensor to Licensee. It is the understanding of the parties that Licensor will continue to receive from Licensee as royalty at least three-fourths of the royalty otherwise required under this agreement for Country X, in the event that a license in Country X under patents of one or more third parties becomes required by Licensee.

Sales Agreement — Defense and Indemnification Provisions are Similar to UCC § 2-312 and § 2-607(b)

I. In the event that any third party asserts against Buyer a claim of patent infringement under any United States or foreign patent with respect to use or sale of PRODUCT purchased from Seller, Seller agrees, subject to the provisions of this Indemnity Agreement to indemnify Buyer in defense of such claim. The indemnity obligation of Seller set forth in the preceding sentence covers only claims of patent infringement that arise due to a failure by Seller to deliver PRODUCT free of the claim of infringement of a third party.

Buyer agrees to notify Seller in writing within ten days of receipt from a third party of any notice of patent infringement, including any Complaint or other paper initiating a lawsuit relating to the PRODUCT. If Buyer is sued for patent infringement, and notifies Seller of the lawsuit in accordance with the preceding sentence, Seller may demand in writing that Buyer turn over to Seller control of the litigation, including settlement. If Buyer refuses to turn over control of the litigation, Buyer shall be barred from any relief (1) against Seller under this Indemnity Agreement, and (2) under any other cause of action based or related to infringement of PRODUCT sold by Seller to Buyer including any implied or express warranty of non-infringement.