

Chapter 4

Licensing Administration

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4.1 Introduction

Now that all of the preliminary steps have been taken, it's time to start putting together the mechanisms for actually conducting a licensing program. We assume that the program will be conducted by the property owner in-house, rather than by using a licensing agent, but many of the same issues are equally applicable for the development of a licensing agency since the administration of a licensing program is the same whether done by an outside agency or by an in-house licensing department.

4.2 The Licensing Department

The first step in the development of any licensing department is the appointment of a leader to oversee that group, typically called a "licensing director" or "licensing manager" or "licensing administrator."

In order to begin making the critical decisions as to how to actually go about structuring and staffing the department, one first must review the reasons why you decided to go into licensing in the first place and what were your original objectives. The three most common reasons for embarking on a licensing program are:

- Brand Awareness through extension to other product categories and through the associated PR and advertising’;
- Strengthen trademark and copyright protection through use on ancillary products; and
- Revenue generation through royalty payments.

It should therefore come as no surprise that most licensing programs are structured in such a manner so as to address each of these objectives. This is usually best accomplished by dividing the group by responsibility which would normally include the following areas of responsibility, all reporting to the Licensing Director:

- Marketing Group to handle marketing, advertising and public relations;
- Sales Group to solicit and develop licensees;
- Legal & Contract Administration Group to oversee legal issues and review and administer all license agreements;
- Finance Group to track and collect royalties and oversee audits; and

- Creative Group to help develop brand identity, translate brands into images and handle product approvals.

This does not mean that every licensing department requires a minimum of five different individuals to accomplish its goals. Many excellent licensing departments are composed of only a handful of people who share a number of different responsibilities while others have 100 or more people on staff.

4.2.1 The Marketing Group

The marketing group is responsible for pulling together the marketing material that the Sales Group will use in seeking licensees as well as overseeing all marketing, advertising and public relations activities.

Licensing is all about lead times—if you want to accomplish something in 18 months, steps must be taken today to set the wheels in motion. As such, most successful marketing groups working with the licensing director initially establish a marketing or merchandising plan with a related schedule which will form a roadmap for the entire licensing program.

Perhaps the easiest way to create such a merchandising plan is as a Gantt chart using one of the Microsoft Office products such as Excel, Visio or Project. One such way to do this would be to identify the contemplated categories of licensed products and, for each category, identify when: (a) presentations would be made to potential licensees; (b) license agreements would be entered into; (c) presentations will be made to potential retail partners; (d) product would actually be introduced by the licensees; and (e) sales of licensed products would commence. All relevant trade shows such as, for example, MAGIC or Toy Fair, would be included as well.

In developing the schedule, the property owner needs to consider the appropriate lead times for licensees and the manufacture and shipping of licensed products as well as local customs and holidays that may impact the manufacture of products, e.g., Chinese New Year.

A second responsibility of the marketing group is planning and overseeing the team's attendance and participation at the various licensing trade shows such as, for example, the Licensing Show in Las Vegas, international licensing shows such as Brand Licensing in London and the Hong Kong Licensing Show as well as a category specific shows such as Toy Fair, MAGIC and the Bologna Book Fair. Since attendance at such trade shows is an essential part of the marketing process and occur throughout the year at various locales around the world, this can be a time consuming task if done properly.

Attending tradeshow is one of the best ways to learn about a specific industry and become knowledgeable about current trends, styles, or new developments in that industry. It is also a good place to make or renew contacts with potential licensees and agents.

When attending a trade show, it is important to have a plan. Most trade shows are large, but are frequently broken into various category sections. A great deal of time can be lost by not using the trade show directory to see what sections of the show you may want to visit. Trade show directories are also a valuable resource for use after a show, as they often provide excellent information about those companies who exhibited at the show.

Finally, the plan should include other relevant milestones for the program, including the commencement of any advertising program and where and when such advertisements would be placed, the initiation of any possible PR programs as well as any other form of related consumer and retail promotions that may be contemplated to support the licensing program. It is important to time trade advertising to coordinate with the applicable trade shows for licensees, e.g., International Toy Fairs in Hong Kong and London in January and Nuremburg and New York in February of each year.

Is advertising worthwhile? It can be expensive and should only be undertaken if the property owner can afford it. More importantly, placement is critical. A great ad in the wrong place will not produce results. The message delivered must be clear, compelling, and provide enough information to be meaningful to the reader.

The best places to advertise for property owners launching a licensing program are the leading licensing trade magazines. These magazines are read by a wide variety of manufactures and retailers, and provide the best exposure to the market that is looking to buy licenses.

The PR program is an important element of a property owner's marketing effort since it can create a "buzz" without the expenditure of a tremendous amount of money. It is a good way to build brand awareness. Industry magazines, newsletters (both print and e-mail) thrive on industry news and the marketing group should plan a steady release of such so as to stay in front of potential customers. As with advertising, the PR program needs to be coordinated with industry trade shows where the publications typically enjoy the greatest circulation and readership.

If the property lends itself to promotional activities, e.g., parties, branded backpacks at trade shows, etc. these activities should be planned and built into the marketing plan as well.

The marketing group is typically tasked with the responsibility for working with both the sales group and the creative group to create and product a sales kit to be used by the sales group in soliciting and closing deals with licenses.

A good sales kit will include the following components:

- Description of the property to be licensed;
- Style guide illustrating how the property may be used;
- Overall licensing or merchandising plan to allow a prospective licensee to see how their products fit in the entire program;
- Advertising and publicity plan – trade advertising, public relations, mall tours, costume character program, etc.;
- Demographics of potential purchasers of licensed products and the target audience;
- Broadcast partners and broadcast plan, identifying air dates, frequency, etc. including broadcast partner’s marketing and support plan;
- Retail plan identifying potential retail partners and rollout schedule;
- Company’s advertising and marketing plans --leveraging own assets and relationships (in theater trailers, DVD trailers, etc.);
- Advertising and Publicity plan identifying planned trade advertising, public relations, mall tours, costume character program;
- Sizzle video plus sales PowerPoint presentations; and
- Boards and sample product concepts illustrating how the property will potentially look when applied to products.

Finally, we live in an Internet world and virtually all property owners will create a website featuring its property and licensing program. Most go live early in the process and the development and maintenance of the site typically falls under the marketing group.

4.2.2 The Sales Group

As the name of the group would imply, the Sales Group is tasked with the responsibility of implementing the marketing plan by identifying those manufacturers who would be the best potential licensee or licensees for a particular product category and then “selling” the license to those manufacturers, typically using the sales kit discussed above.

The sales group of larger licensing departments is typically broken down by property, market segment and then by product category, e.g., MICKEY MOUSE merchandise toy products. The theory behind this is that the relevant sales executive becomes an expert in their particular field and not only knows and understands the particular industry and the players in that industry, but are actually able to work with the manufacturer to develop better product. Selling a license for merchandise sales can be quite different than selling one for promotional sales or directly to retailers. Finally, the group will typically include support personnel to assist the sales group in making and scheduling appointment and then closing deals.

The first order of business for the sales group is to identify potential licensees. This is typically done by researching the particular category and identifying those manufacturers who would be in the best position to manufacture product of the type and quality required by the licensor, but one who has the resources and distribution channels to maximize sales. While every category typically includes a host of choices, many experienced licensing salesmen find themselves going back to those manufacturers who have done a good job in the past. This is one area where manufacturer’s representatives play a major role because they actually approach the sales group on behalf of their clients and actually sell their clients to the property owner.

Exhibiting their property at one or more industry licensing shows, e.g., Licensing Expo in Las Vegas, Brand Licensing in London or the LIMA Germany events, is an excellent way to not only inform the industry about your property and licensing possibilities, but to actually meet potential licensees. Manufacturers who are looking for new properties regularly attend these shows for the express purpose of seeking new licensing opportunities.

Once the sales group identifies its list of potential licensees, the next step is to actually meet with these manufacturers to discuss licensing opportunities. This is where the sales group must “sell” the license to a potential manufacturer, stressing the benefits that taking a license of the property can have for the licensee. The dynamics of such meetings will

depend in large measure on the property and whether it's a "hot" property or one that has never been licensed before. Selling a license for a very popular property that is in demand obviously takes less work than convincing an otherwise reticent manufacturer to take a chance with a new, untried property. It's probably analogous to salesmen for an automobile that is in demand, e.g., Road & Track magazine's Car of the Year vs. vs. attempting to an auto that is the subject of a major governmental recall for defects.

The basic tools of selling a license¹ are fairly straight forward:

- **Know Your Property.** Do your homework and know all that you can about your property. To the prospective licensee, you *are* the expert on the property you are selling.
- **Know Something About The Category You Are Trying to License.** You cannot successfully sell a manufacture without knowing some basic information about his product category.
- **Familiarize Yourself About The Potential Licensee.** The more you know about the company you are trying to sell to, the better your chance of success.
- **Which Licenses Are Competitive To Your Property?** Be prepared to respond to questions concerning competitive properties.
- **Building the Case for Buying Your License.** Know the strengths and weaknesses of your property. Remember no property is perfect, so acknowledge the short comings, but counter with positives. Have the facts and figures relating to your property readily available. Know what you are trying to accomplish *before* you start your presentation. You are leading the meeting, so know where you are heading!
- **Good Presentation Tools are Essential.** In today's techno-marketplace, good presentation tools are expected and essential. The better visual you can paint, the easier it is for the perspective licensee to picture the application of your property to his product. Be certain that your marketing materials are both informative and effective. Sales materials need to do more than look good, they need to inform.

¹ Based on a CLS presentation on *How To Sell a License* by Danny Simon, President of The Licensing Group, Ltd. 6363 Wilshire Blvd., Los Angeles, CA 90048

- **Believe in and Get Excited About Your Property.** Enthusiasm is infectious. The more excited you are about the material you are selling the better it will be received by your audience. Remember, enthusiasm will not replace or cover up your lack of knowledge of the property, product category or your ability to sell a license!

The salesman should emphasize what taking a license can do for the potential licensee, including increasing sales, the ability to sell other product in their line, building exposure and awareness of the manufacturer's own brand and product line and opening of distribution into different channels.

Once the list is narrowed down and there is an expression of interest, the potential licensee is typically asked to fill out and submit a "Licensee Application" in which it provides the property owner with important information about the company as well as its licensing history and manufacturing and distribution capabilities.

The next role of the Sales group is to review and evaluate all of these completed licensee applications to select the one that would be the best fit for the property. The evaluation process varies from licensor to licensor, but some of the more important elements considered by most licensors include:

- What type of products are they proposing and will it be a good fit for the property;
- What is their quality history, e.g., have they manufactured high quality products in the past;
- Size and structure of the company, e.g., is it a major player in the field or a start-up;
- Strength of design and manufacturing capabilities, e.g., who will actually design the products and where and by whom will they be manufactured;
- Capitalization and financial strength, e.g., are they sufficiently capitalized to meet the financial conditions of the license and to put resources behind the license or are they on the verge of bankruptcy;
- Distribution capabilities, e.g., how and what markets will they distribute the product;
- How the license will fit in the manufacturer's product mix;

- Sales history, e.g., what are their sales revenues and what percentage of these revenues will the licensed product become;
- Licensing history, e.g., have they had prior licenses and how have they done with them; and, finally,
- What financial terms are they offering.

Financial terms are included as the last consideration because for a license to be successful, it needs to be more than just about who is willing to pay the highest royalty rate because if they do not produce good quality product or lack the resources or experience to adequately promote the products, such a licensee can create serious problems for the entire program.

Most licensors do not simply rely on the potential licensee's answers in the Licensee Application but will do their own due diligence to confirm various facts. It is quite common for property owners to run Dun & Bradstreet reports to confirm financial information and whether they are paying their obligations when they become due. Similarly, licensors will also ask for and check the licensee's references, including bank references, as well as the experience that other licensors may have had with them.

Once a potential licensee has been vetted and is selected, the final step for the sales group is to "close the deal" on the best terms possible for the property owner. Typically, this process starts with a deal memo or term sheet between the parties which identifies the relevant terms of the transaction.

In negotiating the terms of the deal, it is important to make sure that the entire licensing group is aware of the progress and well as the terms being discussed. In many instances, it might even be necessary for other sections of the property owner's organization be involved or, at the very least, advised. The use of a sign-off sheet is a good idea to insure that the sales group doesn't offer terms or conditions that the property owner is simply unable or unwilling to offer. Getting as many people involved in this process is important to avoid embarrassing situation or, worse yet, ones that must be unwound.

Frequently, the sales group will work with the contract administration and legal group in this regard.

4.2.3 The Contract Administration and Legal Group

The contract administration and legal functions are typically intertwined as they cover both the legal protection that is required to support a licensing

program as well as the contract administration function. Frequently the same individual or individuals handle both functions.

[A] Trademark Clearance and Protection

Prior to actually launching the licensing program, global trademark searches should be conducted to insure that the actual licensing of the property will not infringe on the rights of anyone else, paying particular attention to clearing the property for those classes which are typically more heavily merchandised, namely:

- Apparel
- Publishing
- Toys
- Video Games

Assuming that the property is cleared for these classes, appropriate trademark applications should be filed to commence the protection process. Typically, a property owner will seek trademark protection in the country where the property was originally developed and popularized, as well as seeking registration protection in the U.S., the European Community, Australia, New Zealand and many countries in Asia. This latter protection will help avoid paying “ransom” to entities that may seek to poach the trademarks once the property is announced.

[B] Licensing Forms

The creation of a set of standard forms that will be used for the licensing program is critical and should be done at the very outset to insure that there will be uniformity throughout. Some of the forms that need to be developed are:

- Licensee application form
- Term sheet
- Standard license agreement
- Approval forms

Perhaps the most important form that needs to be developed at the very outset of a licensing program is the “standard” license agreement that the property owner will use during the licensing program. Special care should be taken in the development of this standard agreement because it will serve as the operative document defining the relationship between the parties.

License agreements are “evolving” documents, meaning that as issues develop and lessons are learned from both good and bad experiences, most licensors will change their standard license agreements for future deals. Unfortunately, it is usually not possible to change an agreement that has already been signed with a licensee, so if the form is properly prepared in the first place, fewer changes are required going forward.

This is not to suggest or imply that every licensee will accept the property owner’s standard form—most will want some changes and that is to be expected. The goal, however, is to keep the changes to a minimum so that there is a certain uniformity in agreements between all licensees in a program.

[C] Contract Administration

The contract administration function is the primary responsibility of this group and it is responsible to insure compliance by the licensee of all of its obligations under the license agreement. The group will have day to day management responsibility of the licensee and, in this regard, will frequently work in combination with the finance and creative groups.

It is advisable to establish strong, workable internal systems from the very beginning to make sure that the process proceeds smoothly and without any problems. The contract administration group essentially follows the paper flow of the licensing process, typically commencing when the initial licensee proposal is accepted the then through the following steps:

- Deal memo—must be developed and routed through the appropriate groups for review and approval;
- Licensee review and evaluation—conducting financial and risk management reviews and evaluation for any potential product liability issues;
- Working with the legal group, preparation of licensee agreement, negotiation and execution;
- Summarization of license agreement and circulation of summaries to relevant departments; and
- Development of docketing system and “punch list” for all relevant due dates by licensees and circulation to individual departments, e.g., product approval dates to creative, royalties due for finance, etc.

Established licensing programs may quickly find themselves having to track literally hundreds of licensees on a worldwide basis for multiple

licensed properties and licensed products. It is therefore imperative that a comprehensive Contract Administration software package, including a Royalty Tracking/Accounting module be adopted at the beginning of the process to avoid having to change procedures and systems later on.

An effective contract administration software package should be able to:

- Generate license agreements on a clause by clause basis;
- Generate summaries of the license agreements by licensee;
- Generate form letters or e-mails to licensees for reminders and failure to comply with due dates;
- Track all licensees, licensed products, submission dates and approval dates;
- Generate monthly reports, invoices and reminders
- Monitor licensees' royalty and guarantee payment status
- Manage all aspects of licensees' financial obligations
- Track third party participation revenues for disbursements
- Allow management, sales, marketing and product development to have access to contracts and other information anytime, anywhere

While some property owners prefer to develop their own, proprietary, contract administration systems, there are a number of excellent third party packages available that will meet the needs of most licensing groups. Most of these packages are designed to run on PC's and Macintosh computers and are surprisingly reasonable in price compared to the cost of actually developing your own program. A few of the more commonly used packages include the System 7 Universal Rights Management system by Jaguar Consulting; Dependable Rights Manager (DRM) by Dependable Solutions; and the Pelican ProFiles suite by Counterpoint Systems, Inc.

Companies that market such off-the-shelf systems can be found in the "support services" section on LIMA's licensing database at www.licensing.org. Most of the companies listed in this section will provide potential customers with evaluation copies of their product as well as detailed reports that the program can generate. It is suggested that one try a number of these products to find the one that best suits your needs before proceeding with the purchase.

4.2.4 The Finance Group

The Finance Group usually gets involved once the license agreement is actually signed and revenue starts flowing. This group is tasked with the responsibility for tracking payments due and received from both licensees as well as sub-agents in other countries.

The group will typically work with the contract administration group and utilize the contract administration software to track all revenues received (or owed) by licensees and generate reports that will allow the property owner to quickly and easily evaluate the success of the licensing program, the individual licensed properties, the licensees and the licensed products.

4.2.5 The Retail Group

In the early days of licensing, licensors would sit back and rely on their licensees to interact with the retail community but times have changed. Successful property owners now understand the role that retailers play in the success or failure of a licensing program and take an active role in not only involving them in the entire program but paving the path for their licensees to achieve market penetration.

The consolidation at retail has given the major retailers enormous power and the penetration into one or two of the major chains can be the difference between the success or failure of a program. For example, mass market Wal-Mart has more than 7500 stores, Walgreens has more than 7000, while K-Mart and Target each have more 1700 stores. At mid-tier, Kohl's, Sears and J.C. Penney each have more than 1000 stores while department store and specialty retailer Macy's, Dillards and Claires alone represent more than 5,000 stores. On-line retailers such as Amazon.com and Walmart.com have become a major factor in the sale of licensed products and cannot be overlooked.

Many licensors begin presenting their licensed properties and licensing programs to retailers more than a year before licensed products actually reach the retail shelves in order to generate excitement for their properties and pave the way for their licensee's products. Retail presentations should clearly convey:

- Property uniqueness, including identification of writers, CGI quality and possible storylines;
- Identification of broadcast partners and broadcast plans;
- Identification of key licensing partners, including master toy, apparel, publishing and video game licensees since retailers want

to know who has signed on to property program as critical part of their evaluation;

- Identification of ancillary merchandise licensees;
- Identification of promotional partners and the amount of advertising support for property and planned in-store cross promotions;
- Property owner's plan to leverage its own assets and any relationship that they may have that could help promote the property, e.g., in-theater and DVD trailers, etc.; and
- Advertising and publicity plans for the property to help create consumer awareness.
- Some tips for making retail presentations² include:
 - **Do not be vague.** Make sure your presentation has direction and a point of view specifically for the retailer you are presenting to.
 - **Allow the Retailer to Take it In.** Once you state your case allow the retailer to take it in and interpret for themselves. They know their venues the best and may know things that you are not aware of. You are laying the groundwork that they will hopefully take off from.
 - **Identify Only Your Actual Licensees.** If you are giving out a licensee list, make sure that the licensees are on board. Nothing is worse than getting a licensee list that the retailer calls to see what a licensee is doing and having them say, oh I don't know about that one, or I am not sure if we are going to do anything with this.
 - **Don't Mention Other Retailers Who Have Passed.** Even if you have taken the property to other retailers, and they have passed, don't convey this in your presentation. No one wants to feel that they are being presented to by default.
 - **Think out of the box.** There are many new types of channels of distribution that should be researched and considered. They may not be the biggest, however if they are successful it could lead to bigger opportunities down the road.

² Based on a LIMA webinar entitled *Presenting to Retail: The Good, The Bad and the Ugly*, by David Niggli, former Chief Marketing Officer for FAO Schwartz

- **Be concise.** Time is precious make sure you convey in a timely manner and make sure you use whatever time you have to get your key points across.
- **Be passionate!** Your approach should not be, “I wanted to see what you thought of this property”, rather “I have a new property that is so right for you and let me tell you why.”

In recent years, many retailers have not been content to simply sell licensed products that were manufactured by conventional licensees but, instead, have gone directly to the property owner and taken “direct to retail” licenses for products which they then have manufactured for them by their or third party factories. By eliminating the conventional licensee and their profit from the equation, the retailers are able to offer the licensed products to the consumer conceivably at lower prices.

Direct to retail licensing offers the retailers a number of advantages. It offers them a point of difference from their competitors, an opportunity for exclusive product as well as affording them unique promotional opportunities. Conversely, it can be dangerous for the retailer who would be investing in the development of costly inventory for an otherwise unproven property while tying up precious retail shelf space. Similarly, if the property doesn’t work, the retailer could be looking at large markdowns to move the inventory.

There are a number of advantages for the licensor in direct to retail licenses. For example, it secures immediate distribution for its licensed products as well as assurance that the retailer will provide key placement for such products. It also gives the property owner an actual retail stage to showcase its product to potential other partners and can be an excellent way to test market a property on a smaller scale than if it had been introduced by multiple retailers on a national scale.

4.2.6 The Creative Group

The Creative Group is tasked with responsibilities involving the actual use of the licensed property on proposed licensed products as well as the review and approval of licensed products during the licensing program to insure that the property is being correctly used and depicted and the quality of the licensed products meet the property owner’s minimum standards.

Most property owners prepare a “style guide” for use by the licensees, illustrating how the property is depicted and can be used. The style guide is the creative property “road map” for all licensees to follow. Today, most

style guides are delivered in digital format rather than in hard copy and many are on-line for ease of reference by a licensee.

The primary purpose of a style guide is to provide licensees with the necessary materials that will allow them to create the best licensed goods possible. It will also assure that there is uniformity in use of the property between licensees as they are all using the same materials as a basis for product development and packaging.

The contents of a typical style guide will include:

- How is the property to be depicted and displayed, what characters or brands are included, etc.;
- Rules for use of the property, e.g. “Character X should never...”
- If a character is included, what poses can (and cannot) be used;
- Vehicles and environment art;
- Size ratios of characters, backgrounds, color charts, quotations, and logos as well as a color palette;
- Packaging and hangtags;
- Product concepts;
- Legal Notices;

Many licensors also include detailed information in their style guides about the approval process in order to provide the licensee with a clear understanding the required approval process. For example, it is quite common for licensors to require submission and approval of samples at various stages of the product development and manufacturing cycle, including approval of concept designs, prototypes, pre-production samples and final production samples.

Many property owners prepare their own style guides while others outsource the project to companies that specialize in the preparation of the product. There are a number of such entities and they can be found in the “support services” section on LIMA’s licensing database at www.licensing.org.

As licensees are brought on board, the creative group monitors how the property is interpreted onto licensed product. Under the terms of their license agreement, licensees will be required to submit proposed product, packaging and advertising to the licensor for approval at various stages of the production cycle and it is the responsibility of the creative group to review and approve such submissions. A licensee is typically not

permitted to proceed to the next step of any process unless it first obtains written approval of a submission and, in most instances, the failure of a licensor to expressly approve such submission will be deemed disapproval of the submission.

Many licensors involve the creative group in the licensing process at as early a date as possible so that both parties are on the same page when it comes to product development. By reviewing product and packaging at a very early stage, potentially catastrophic problems can be avoided, e.g., where the licensee has produced 500,000 products only to find that they are not acceptable to the licensor. By involving the creative group at an early stage, small problems can be corrected before they become large problems.

Keeping track of licensee submissions, let alone the approval and disapproval of such submission, can be a job in itself, particularly as the licensing program grows. As such, it is advisable for the creative group to work with the contract administration group and its computer systems to docket when such submissions are due and when responses are required. While it might be possible to manually keep track of the required submissions for a single licensee, as the program grows that will not be possible and the function must be computerized. For example, a program with 50 licensees may generate more than 5,000 required submissions every year—no easy feat to track manually.

4.3 International Licensing

Licensing is a global business and one cannot simply focus on the country where the property is created and originally spawned. This is particularly true for entertainment licensing. For example, if a television show with merchandising potential is to be launched in the United States in the fall of 2012.

As is the case with most licensing matters, successful licensor work backwards from the date when they expect licensed products to actually hit the contemplated markets. The following steps should be taken in the development of an international program:

- At the time a decision is made to proceed with an international licensing program:
 - Seek trademark protection in each country where licensing is contemplated as well as those countries where licensed product will likely be manufactured, e.g., China, Thailand, Vietnam, Malaysia, etc.

- Immediately after a broadcast commitment has been obtained:
 - Set up agent network in countries where licensing is contemplated;
 - Develop territory-specific tools, e.g., dubbed sizzle reels, translated one-sheet brochures with relevant territory information, broadcast information, global key category partners, etc.
 - Identify territory specific opportunities and work with agent to secure (Argos catalog, Top Trump cards, Three Kings Celebration Accessories, etc)
- At least one year before projected launch of licensed products in a particular country
 - Manage agents in deal execution, product development, retail commitments, product roll-out;
 - Provide support to toy licensee(s) at international toy fairs in Hong Kong, London and Nuremburg Toy Fair including the creation of sizzle video, posters, costume characters, handouts, etc.
 - Create internal management system for managing the agents.

4.4 Ethics in Licensing

Some cynics who refer to licensing as the “last bastion of hucksterism” may think that the phrase “ethics in licensing” is an oxymoron. It’s not and as the industry grows from its humble beginnings into a well accepted and profitable marketing tool, the industry has shaken this reputation and become quite professional. As such, ethical practices have become a way of life in the industry.

Webster defines ethics as meaning, the ‘principles of conduct governing an individual or a group.’ In the context of any professional group, “winning ethics” are typically considered to be:

- Honesty and candor instead of gamesmanship and overreaching;
- Obtaining enforceable yet workable business arrangement; and
- Protecting and enhancing a professional reputation.

While the licensing industry, per se, does not have its own Code of Ethics, the American Bar Association has such a code called the Model Rules of Professional Conduct. While much of these rules have no applicability

whatsoever to licensing, there are some that do, particularly Model Rule 4.1 which states:

In the course of representing a client, a lawyer shall not knowingly:

- (a) Make a false statement of material fact or law to a third person; or
- (b) Fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client, unless disclosure is prohibited by Rule 1.6.

In the commentary to Rule 4.1, the committee drafting the rule states that “Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party’s intentions as to an acceptable settlement of a claim are in this category.”

In the course of negotiations, everyone postures and puffs and that is not unethical. There is, however, a line between puffing and lying and one should never cross that line. Lying is a misstatement of an objectively, verifiable fact while puffing is a statement of inference or intention.

For example, if a negotiator made the statement that he “would not accept less than 4% royalty” that would generally be considering puffery even if he knew that he was authorized to accept a royalty rate as low as 2%. If, however, he provides a specific reason as to why he cannot accept lower than a 4% royalty, e.g., our agreement with the producer prevents us from accepting any royalty lower than 4%, and that reason is totally false, the line between puffery and lying has been crossed.

Under Rule 4.1(b), it is not ethical to remain silent in a negotiation on a material issue of fact when one knows that its opponent could be misled by such silence. The line between ethical and unethical conduct is a, however, a fine.

For example, if a licensor is asked by a licensee whether its property is valid and whether anyone has ever challenged such validity, they are obligated to answer truthfully. If, however, the licensee does not ask such question, are they obligated to address the issue? The answer is probably no.

If, however, the licensee has told them that it issue of trademark validity is very important to them and, moreover, they are aware that at least two other parties have claimed that the property infringes the rights of these

two other parties, even if the licensee fails to ask that specific question silence may not be appropriate.

The ABA Model Rules concerning potential conflicts of interest, while interesting, are generally not relevant to many licensing situations. Because of the potential that lawyers have access to confidential and privileged information from a client, they are typically held to a higher standard than most licensing professionals where the possibility of disclosing privileged information typically goes not exist.

That said, conflicts of interest in licensing can prove particularly problematic because the industry is relatively small and individuals frequently find themselves on different sides of a negotiating table. It is difficult, if not impossible, to address every particular situation that might arise but one rule of thumb almost always applies. If a licensing executive finds themselves in a potential conflict of interest situation, e.g., where they are representing a licensee who is looking to take a license from their former employer, or worse yet, they are an agent who is representing both the licensor and potential licensee, they are advised to disclose such potential conflict to all relevant parties at the earliest possible occasion. If either party believes that the situation represents a conflict, they would be wise to withdraw from the negotiations. Virtually all conflicts of interest can be waived by full disclosure to and the consent of both parties, preferably in writing.

4.5 Insuring Social Compliance³

Social compliance is a relatively recent concern for many licensors due, in large measure, to negative media attention that focused on working conditions in factories that produced licensed products, most notably in China. The news media and social activist groups around the world exposed the fact that some of the factories were applying sub-standard working conditions in the factories and were employing prison and child labor to produce the products. This put pressure on the private sector to play a role in trying to improve such conditions.

Make no mistake about it, there is a serious problem in this industry. Some factories blatantly violate their local laws, falsify their records and even bribe inspectors. This is a way of life in some countries. To think otherwise is to simply ignore the problem.

³ Based on a presentation by Ian Spalding, President, InFact Global Partners, 16A, Dotcom House, 128 Wellington Street Central Hong Kong at a LIMA 2009 Webinar entitled *Social Compliance: Introduction and Overview*.

The private sector's reaction was the development of codes of conduct for these factories to follow if they wanted to continue to work with a particular property owner. The first code of conduct was actually adopted by Levi Strauss in 1991. The problem received national attention in the United States in 1996 as a result of a controversy involving Kathie Lee Gifford and in 1998 the Fair Labor Association was created with White House support.

Over the past decade, many licensors, retailers and trade associations have adopted social compliance standards or codes which they require their partners or suppliers to follow. The purpose of these codes was to raise the standards of factories that actually manufacture licensed products and promote social responsibility.

Most of the codes that have been adopted vary only slightly from each other, but they all address in one form or another the following issues:

- Maximum working hours for employees;
- Compensation of employees;
- Social insurance that an employer must carry for its employees;

LIMA has its own Code of Business Practices which may be found at <http://www.licensing.org/about/business-practices.php>.

Establishing standards is one thing—enforcing those standards is quite a different matter. Very few licensors simply ignore the issue. At the very least, most licensors will require that their licensees conform to some standard. While they may not actively or aggressively enforce such a requirement, they will reserve the right to terminate the licensee should it be determined that the licensee was non-compliant with the standards. This is the minimum that any licensor should do in this regard.

Generally speaking, however, most licensors do, in fact, look to enforce these standards, typically by auditing the factories of their licensees—either by internal auditors or by third parties who specialize in such audits. While some simply audit on a superficial basis and tend to look the other way when violations are found, there is an increasing tendency on the part of licensors to take these standards quite seriously and either require that a non-conforming licensee correct the problems or face termination of their license agreement.

Some licensors will actually go the extra mile in this regard and actually work with their licensees to make sure that its factories are complying with these standards. They have shifted from a model of simple compliance to one of continuous improvement, even to the point of working with their

licensees and actually sharing the cost of compliance. They have begun to emphasize education and capacity building at the expense of simply conducting more audits. Longer term corrective actions plans are necessary. These licensors understand the implications of non-compliance and the negative press that it can generate which can seriously tarnish not only the image and reputation of its licensed products, but of its primary products as well.