

Wal-Mart Gold

Lesson Eight Transcript



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Joe: This is Section 8, how to license or sell your idea or product. What we're going to talk about first is why you should consider licensing. We mentioned earlier when we talked about the five different ways to get your product in the store that this is the one where you make the least amount of money, but the thing that makes it so appealing is it has the least cost to you. You develop or come up with your idea or product and then you're essentially done as far as investing. You're using other people's money, other people's time, and other people's contacts to get the product on the market. You're going to license something and if you have something that, for example, Procter & Gamble would use, we actually have a contact for you for that of how to present something to Procter & Gamble and you can imagine if they license something and you get paid a few percent royalty, how many dollars you're going to make that way versus trying to come up with starting your own company.

Michael: Can you tell me some of the different kinds of licensing?

Joe: Yes. There are a number of different kinds. One would be most of what we've been talking about so far, which is licensing a product that you've invented or come up with. You can also license a process to do something and they have special kinds of patents just for that called process patents. And then you can license artwork or characters like Walt Disney will license Mickey Mouse or you can license Garfield, all of the characters you know of. The companies that own the rights to those will license those. You can license the rights to put Garfield on a pen and I've done that. We licenses Star Wars back when Star Wars was popular to put on stickers and we paid them a royalty. And then you can do the other side. You can be the licensee or you can be the licensor. And in terms of character licensing, artwork licensing, I've been on both sides of that one. I've been the one doing the licensing for my own artwork and I've been the one licensing for artwork I wanted to put on my products.

Michael: Well, give me some ideas or some steps that I should do before contacting a company or a licensing agent.

Joe: First off, in either one, whether you're contacting a company or an agent, you want to have your act together. It's not anywhere as bad as making a sales call on Wal-Mart, but if you want to keep your credibility with both businesses and agents, you want to do some homework first. So, don't go and talk to somebody about something if you haven't done your research to make sure the idea is original. You've got to do some patent research and there are free places to do that. But you need to make sure that it hasn't been done before.

Another thing you can do that is free is take it to somebody who is an expert in that field, who has no vested interest in your idea one way or the other and ask them what they think it. If they say it sucks, I'd move on to something else because an expert in an industry if they think your idea is no good, you're playing

a long hard game trying to prove that person wrong because they know more than you do. That's sort of like trying to swim upstream. I'd rather swim downstream.

And so, a couple of criteria for idea or product to be licensable, first off, it needs to be thoroughly designed. In other words, you can't have an idea for something that would do some task, but have not idea how it would work. You need to know it would work. So, first it has to be designed well. You have to prove it can work. Third, it needs to be exclusively available to every license to do. And fourth, and the one that people normally don't think of, is it needs to represent new sales to the company it's being licensed to. If you think about it for a moment, why would a company pay you a royalty on a product if when they manufacture and distribute that product the sales of that just take the place of something else they already have. They're just trading dollars and paying you royalty that wouldn't have to pay if they just sold what they currently have. So, it's important that whatever product you come up with when you're talking to the people you're going to license it to, that it be additional sales for that company and not replacing products they've already got.

Michael: Well, should I do this myself and handle all the licensing and learn it myself maybe by buying Harvey's book, or should I use an agent? What have you done that's worked best for you?

Joe: I would say it depends on the industry and your experience in it. But first off, don't use any invention submission company that advertises on TV. I mentioned that before, but I want to say that again.

The advantages and disadvantages of going with an agent, the advantage is they have contacts. They know how to present a product to a company. Harvey has done 150 to 200 of those presentations. He knows what he's doing. He knows how to do it and he has the contacts. If he needs to talk to the president of Mattel, he can get in there where you might find that hard to do. However, he gets a piece of the action if you do that. Typically, in Harvey's case, he either gets 50% or 40% to 50% of the first \$100,000 of royalties in a year and then he gets 20% or 30% of the additional above \$100,000 in a given year. In particular, Harvey charges \$175 to evaluate your idea and if he takes it on, this isn't like the invention submission companies, if he takes it on, he will build a prototype. He will spend money on artwork to create a presentation. He will do everything that needs to be done to make the thing happen. He might put in \$5,000, \$10,000, or \$20,000 of his own money if he believes in the idea and you will be expected to put up nothing. So, that's the advantage of it. The biggest advantage of the licensing agent is he knows what he's doing and he has the contacts.

The disadvantage is he gets some of the money. What I guess I'd say there is I've done it myself, but the reason I did it myself is already knew the people I was going to license to and I'd been in the industry for 15 years, so I was already well established and I knew the players and I didn't need an agent. But if I come up

with an idea for a product that was outside a field that I'd been in, I would one hundred percent of the time use an agent.

Michael: Well, if you were going to do it yourself, tell me some of the steps that you used doing it yourself.

Joe: First off, when you do it yourself there are a few things that might be counterintuitive. First off, you're going to need to meet in person with the person who makes the decision to license from you. You don't send letters, you don't send faxes, you don't make presentations to marketing product managers or gatekeepers. You only want to talk to the decision maker and the other thing you don't do that inventors invariably do is build a website. And the reason for that is yes you can do it cheap and it doesn't cost much and you can expose your product, but from the point of view of the person you're licensing to, what it looks like is that you're shopping into the world, nobody's biting, you can't get anybody interested, you put up a website, nothings happening. What you want to have the image be is you want to contact in person the person who can make the decision that the company you're targeting, you want that person to believe that he is the first person who has seen this and that nobody else has seen it yet. He's getting first shot. Now, if you have a website, that's pretty clear that everybody in the world who browses around has seen this thing and it's sort of like tainted because it gives the feeling of well nobody wants this thing, why should I take it. So, if it's secret, it's not out on the market, and it's not on the Web, then you can make the case that they're the first person to see and now that has value.

Do your due diligence on the companies who might use your product. Determine what category your product belongs in, in the store, and then go see which companies are already in that category and which companies are in the category with a product or product line that's related to yours, but not competitive. You're not going to get real far if your approach is just to replace what they already have and now they get to pay a royalty where before they didn't have to. So, once you've determined the companies who have the distribution you want and who have products in the right category, but are not competitive, then now you've got your target list and you're going to want to talk to normally the president of the company and you're going to want to do it in person. One of the things that I got out of Harvey's book, he said out of a couple hundred products he's licensed, he has never once been successful with licensing anything unless he had an in-person meeting with the person who could make the decision.

Most inventors are going to want everybody who sees or comes anywhere near their product to sign non-disclosure, non-compete agreements. The bottom line is, big companies won't do that. I've seen numbers anywhere between 85% and 95% of all large companies will refuse to sign those and, in fact, they have one you have to sign that protects them and that basically says they can do whatever they want with it and you have no right. They have all the rights. And if you want to license them, you have to sign their agreement and they won't sign yours.

Michael: Why do you think they do that?

Joe: They want to protect themselves because a big company like a Procter & Gamble or someone, they might have 150 products in the market in the stores, but they might have 5,000 of them in development and you might have come up with something that they're already working on. And they want to make sure that there is no legal fight about who thought of it first or any of that. If they're already working on it, they're not going to pay you anything. And they're the one you're trying to make the sale to, so they are going to want to protect themselves. And the bottom line, also, is as a rule the companies are not going to rip you off because you could sue them if they rip you off. They have what they call deep pockets. In other words, you can sue them and if you win, they have money to pay. So, as a rule, the companies are not going to rip you off and you really don't want to eliminate 85% to 95% of your potential licensees by requiring them to sign your non-disclosure agreements.

Michael: In Harvey's book, does he mention that most of these companies are pretty straight?

Joe: He has had no problem with that. He's never had a problem with anybody trying to steal an idea. And after doing several hundred products, having the whole market available to you is the way to go.

Michael: Well, give me some criteria, stuff that's non-negotiable, non-negotiable points that you learned from Harvey's book.

Joe: In doing your negotiations, after you have met with the company and they have an interest, there are ten things that are negotiable and there are ten things that are not.

The ones that are not negotiable is that your royalty needs to be based on sales, not on profits. And the reason for that is if the royalty is based on profits, they can make sure there's never any profits in the accounting.

Michael: Do you think this is done standard in licensing across the board?

Joe: That's normal and customary. It's very unusual for it to be on anything else other than sales. The top line sales are the easiest thing to measure, it's hard to mess with, it's easy to track. That's how you do it.

And the second thing is sales of the sales. You're not subtracting out their salesmen's commissions or marketing overheads or any of these other things. It's just top line sales and what the percent is.

Third thing, you want the rights to examine the books. And in that case, some of the agreements -- not that I got from Harvey, but from some other people -- you

can put clauses in there that say if we have someone examine the books and we've been underpaid more than 10%, that means that you have to pay the fees that it cost us to do it. And if the difference is less than 10%, then I have to pay the fees for doing the audit; or you can do 5% or some number. The downside to doing that, of course, is that if you tell them it's 10% then they know they can cheat 10%. So, that is a plus and a minus.

The fourth thing, you need to define the product well enough and include any changes, modifications, or variations that may be created down the road. You don't want to have it so that the first time a modification is made to the product now you don't get royalties anymore. You want no end to the royalty payments and you want to make sure that if the product gets modified through time that you still get paid.

Michael: So, the no end to the royalty payments, it's in _____, as long as they're using it.

Joe: Yes. As long as they're selling it, yes. Examples of things like that is Monopoly. Monopoly has been around 50 years or longer and there are a million versions of it now, not only the original one, but they had that covered, royalties are still paid.

The next thing is you want to have the right to prove the product before it's sold. Companies are going to typically want to make changes. They may make changes in your product to make manufacturing more efficient. They may make changes for many reasons, but you want to have the right to approve that before it gets on the market.

Number seven; you want an advance, a non-refundable advance. That's also normal and customary. It's done pretty much. I've never seen where you don't do that.

Michael: How much?

Joe: Well, the amount will vary all over the map. When we licensed the Star Wars artwork just to put on stickers, they wanted \$25,000 as an upfront advance.

Now these advances, by the way, what that means is that's an advance on royalties. So, say you get a \$25,000 advance or say you get a \$5,000 advance, whatever it is, then the first \$5,000 that they owe you as your royalty percentage, goes against that. So, if you got, say \$10,000, the first \$10,000 of royalties you earned have already been paid to you by that advance and then they pay after that. So, that's what that's all about.

Michael: Okay.

Joe: Then you want to have a date that for sure it's on the market and if it's not, you can go elsewhere. What can happen to you if you're not careful is a company who

has something similar, but not quite the same, they want to just keep your product off the market because they view it as it might hurt their sales. So, if they tie it up in an agreement with you and they never put it on the market, they've protected themselves. So, you want to have a time, whether it's six months, a year, or something that if they don't put it on the market by then, you can go license it to somebody else.

And then everybody, all the companies always has product liability insurance. Anybody selling to retailers has to have that. What you want to make sure they do is they put your name on the policy as an insured.

And then the last thing is even though you own the rights to this, whether you have a patent or not, you own the rights, you're licensing it, you do not want to have any obligation that you have to take legal action against somebody because you might have something that maybe you made \$20,000 of income on and now somebody is knocked it off and you have to take legal action. You might spend \$50,000 in legal fees. So, you don't want to be obligated to do that.

Michael: What are some negotiable points?

Joe: Well, first off is the royalty percent. That's a big one.

Second is territory and by territory I mean geography. If you're licensing it to somebody who sells in the United States only, you don't want to give them worldwide rights. And also, I'd say channel of trade is also territory. If you're licensing to a company that sells to grocery stores and maybe the mass market like Wal-Mart, but doesn't go anywhere else, don't give them the license for premiums or ad specialties or don't give them the license for gift and stationery stores, don't give them the license for TV or direct mail. Each way of selling can be licensed. So, you want to have your agreement specify which way they're licensing because you can license in all of those areas, so don't give it away to somebody unless they have proven experience in that particular territory.

Next thing, number three, is the payment schedule, how they're going to pay you. Always go for monthly payments and you'll probably never get it. Usually the normal thing is quarterly. But if you ask for monthly that gives you something you can give back to them so they win on that.

The term of the agreement, the minimum guarantee. What minimum guarantee means is though there may be an upfront royalty, there's also usually a minimum guaranteed payment. In the case of the Star Wars thing when we licensed, we paid an upfront \$25,000, we had to guarantee a minimum payment of \$100,000. And what that meant is if we didn't sell enough products to generate \$100,000 in royalties, we still owed the \$100,000. So, you want to do that when you're the licensor. You want to have a minimum guarantee that you're going to get paid whether or not they sell it.

The next one is one I would never have thought of, but I saw it in Harvey's stuff, which is get defined how much of your time is covered for doing what and not doing what. You don't want to end up being a product development person working full time for this company you licensed to for free. So, you want to define what you will do at no charge to help the project and what you won't. And the main thing to be careful of there is you don't want to find yourself in an unpaid job.

Number seven, the size of the non-refundable advance that we talked about before and how long to bring it to market that we talked about before, are both things that get negotiated.

And then the last two are legal. If there's legal work still needed to be done to complete the patent, who pays those fees, and then also who pays the legal fees in any lawsuit. Obviously, you as licensor are going to try to have the company doing the licensing pay all these fees, but that's a negotiable thing.

Michael: Have you done any character licensing yourself?

Joe: Yes. I've been on both sides, both as licensee and licensor. Licensee on Star Wars like I mentioned before. Licensor, there was a character out there a number of years ago called Moodies, which were cute little guys -- one was happy, one was sad, like that -- and we had met with the people who owned it and they decided that we would be licensing the Moodies and we would put out a whole product line of stationery products with them on it and help them get the thing launched, which we did. Went to Toy Fair, which is a place where you launched toy related products. So, we've been on both sides, both on the licensee and licensor.

And one thing just to note that premium use is excluded from licenses normally. That's when you sell something to McDonald's or Wendy's to go in a Happy Meal. That's what the premiums are. They're free gifts that people get for free if they buy something. And the premiums are always negotiated one deal at a time. McDonald's is a different deal than Wendy's.

Michael: Have you done any other kinds of licensing besides the character licensing?

Joe: Yes. I've done artwork licensing, which is similar to character, but it's not a character that people know. Character licensing, you're paying because people know what Star Wars is. Artwork licensing, what I did when I made stickers, we had thousands and thousands of designs of stickers. And when I was starting my second company after the first one blew up, I did have the rights to the artwork. So, I did just what I've been telling people to do. I went out and looked for a company who was in the market I was targeting who had the distribution I wanted who had a bunch of related products, but didn't have stickers. And I found a company like that that had 500 products, but no stickers and they were in the right market. So, licensed to them the artwork for all my stickers for like \$100,000 and

I then handled all their manufacturing of stickers for them and the cash flow from that is how I started my second company.

That's the end of Section 8 on how do licensing. There will be a number of links at the website for resources related to that. There are probably about 50 or 100 resources I can refer you to.

And now, in the next section, Section 9, we're going to talk about how to set up a joint venture.

Michael: This is the end of Section 8. Please continue to Section 9.