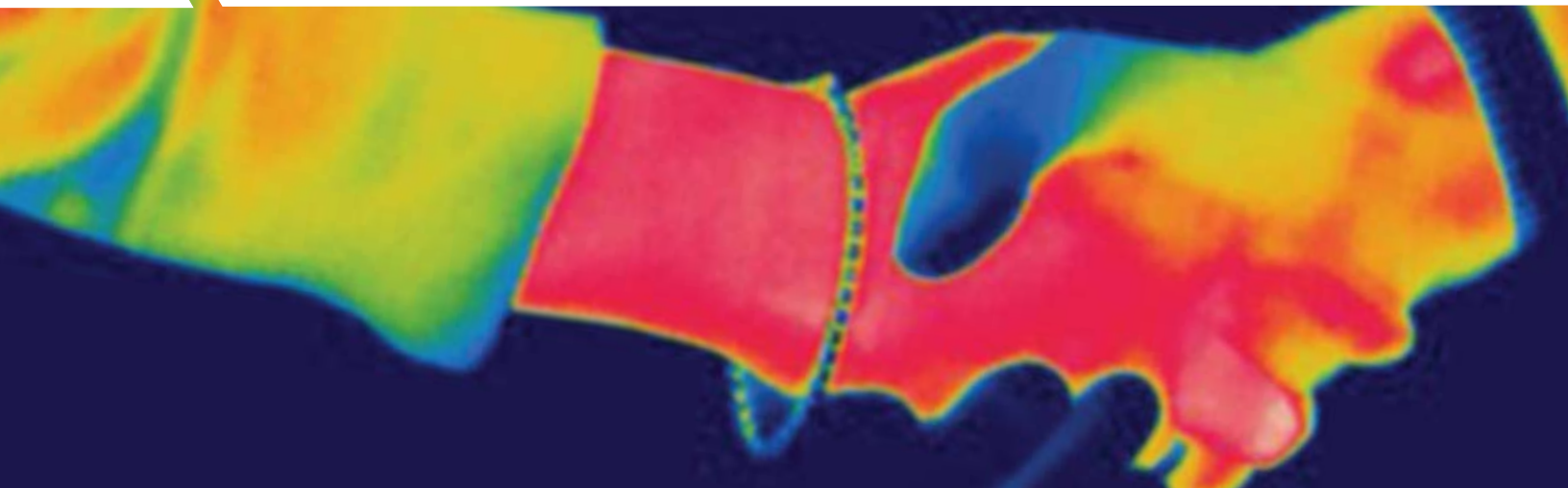


Q&A

LICENSING AND TRANSACTIONS





QUESTIONS AND ANSWERS

LICENSING AND TRANSACTIONS

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LICENSING AND TRANSACTIONS

OVERVIEW OF INTELLECTUAL PROPERTY TRANSACTIONS

What is a license agreement?

A license, usually set forth in a contract called a license or licensing agreement, is a grant of permission from a party owning intellectual property (IP) rights (the “licensor”) to allow another party (the “licensee”) to perform acts that otherwise would constitute infringement of those rights. Typically, a license agreement allows the licensee to commercialize certain IP rights for a specified purpose in exchange for something of value, such as royalty payments (money,) other IP through cross-licenses or development licenses, or some other valuable asset.

A license agreement usually will include a negotiated statement outlining the various rights and obligations of the parties, covering a variety of topics, such as who owns improvements, whether the licensor will provide technical assistance and know-how, whether the license is exclusive or non-exclusive, whether the license includes trademarks, how infringement will be addressed, whether the licensee may sublicense rights, and so forth.

Are there intellectual property agreements other than license agreements?

Indeed, there are. We use the term “IP agreement” to encompass various transactions (including, but not limited to license agreements) involving an exchange or grant of rights in IP (patents, trademarks, trade secrets, or copyrights.) These agreements may also involve: (i) creation of new IP; (ii) ownership and disposition of IP rights; (iii) control over the use of or access to IP (including third-party IP); (iv) investment in IP; (v) securitization of IP; and (vi) pledging IP as collateral in financings.

A number of agreement types involving these aspects are briefly discussed at the end of this booklet, but new types of transactions and new nuances to established transaction formats arise all the time. Creativity in shaping IP agreements allows the parties’ specific objectives to be accommodated in the majority of circumstances.

What variations occur in IP agreements?

Patents, copyrights, and trademarks are bundles of rights that may be divided, assigned, shared or retained by the parties through different kinds of arrangements and clauses. That is, rights can be parceled out piecemeal, to give only what is required. This alone leads to interesting variations.

Rights of use also can be divided or transferred based on fields of use, territory, or periods of time. Thus, instead of simple all-or-nothing sales, rights may be shared in various ways. Other types of IP rights, such as trade secrets and know-how also can be allocated or shared between parties. Intellectual property can also be provided in the form of services, such as consulting, training, and research & development services.

How do I know what type of IP agreement or transaction is best?

IP transactions need to be shaped by your business objectives, the competitive and regulatory nature of the market, and the characteristics of the particular IP at issue. The type of transaction best for you will depend on a variety of factors, such as the size and availability of resources of the parties, the nature and stage of development of the IP, and whether the technology is targeted for a new or existing market.

A review of comparable deals in the industry, the requirements and limits of applicable law, and the objectives and capabilities of the parties involved will likely narrow your options. As technology changes, new forms of IP transaction agreements emerge. We are always alert to the need to be creative and to break the mold, if necessary.

Why do I need to get an intellectual property attorney involved in my IP transaction?

When IP is core to a business deal, you should involve an intellectual property attorney early in the planning process to avoid inadvertent loss of IP rights and missed opportunities to obtain favorable deal terms. IP agreements require an understanding of the scope and strength of IP rights of both parties and an understanding of the alternative ways to implement an exchange of IP rights that will satisfy the business objectives of the parties.

There are many technical rules of IP law and even antitrust law that may come into play, and that can impose constraints you might not appreciate without the early involvement of an IP attorney knowledgeable about the applicable law and practices. The lack of such knowledge, including the knowledge of potential pitfalls and alternatives, can lead you to commit to terms that will ultimately be unenforceable or leave you at a disadvantage.

Once parties have agreed to basic terms, it is problematic to go back and seek changes because your lawyer points out issues and alternatives you had not considered. If new terms can be negotiated, you likely will have to make concessions that could have been avoided.

Are there different types of IP agreements in different fields of technology?

The same types of intellectual property protection—patent, copyright, trademark, and trade secret—are applicable across technology fields, and the same basic agreements can be tailored for different technologies. However, differences in technology, regulatory requirements, government-required approvals, modes of commerce, business models, and constraints on the actors involved (such as the prevalence of academics as originators) lead to variances from one industry to the next. Industry norms and the culture of the parties also play a role in shaping the structure and terms of the agreement.

STRATEGIES TO CONSIDER WHEN PURSUING AN IP TRANSACTION

Are there any basic strategies I should know for protecting my intellectual property rights before and during an IP transaction?

Some basic steps include:

- Protecting the confidentiality of information during initial and follow-on discussions, using, for example, a strong Non-Disclosure Agreement (NDA);
- Taking steps to secure your rights in the IP, such as obtaining signed employment agreements and IP assignments from your employees and consultants;
- When possible, filing patent, copyright, and trademark applications before sharing information; and
- Documenting and keeping records of information and ideas to protect against future disputes as to ownership.

It is worth remembering, also, to do some diligence on the trustworthiness of the other party, e. g., speaking to those with whom they've dealt in the past. A contract should supplement a good relationship, not substitute for one.

Why do I need a Non-Disclosure Agreement (NDA)?

Parties often need to share certain confidential information with each other to evaluate potential business opportunities. An NDA allows the parties to exchange that information, yet protect its confidentiality and limit its future disclosure. An NDA obligates a party to keep information confidential and controls and identifies the people with whom the information can be shared.

If an NDA is not used, the other party is free to disclose your information to others and (absent a patent) use it. Such unprotected disclosure will cause the loss of trade secret status for the disclosed information, so an NDA is needed before any trade secrets are disclosed. If a patent application has not already been filed, an NDA also may be needed to preserve potential international patent rights.

NDA's come in limitless varieties. Some are more akin to waivers of rights than to protectors of rights. Each party receiving confidential information needs to be concerned about becoming "polluted" or constrained by that information.

While some norms have evolved, you cannot be sure a proposed NDA is fair to you and protects your rights, even if it is cast as a "mutual" NDA, which supposedly should work for both parties. Even if the other party indicates the NDA is its standard form agreement, you should read it with great care, as it was written for the other party's benefit, not yours. You may find it might not protect you to the degree needed and it might even restrict your freedom of action in undesirable ways.

Your IP attorney can draft or negotiate an NDA tailored to your specific business needs so it does not restrict you more than is necessary.

What should an NDA include?

Start with your goals. Determine the purpose of disclosing the information, the subject matter of what is likely to be disclosed, the type of materials and manner of disclosure, the length of time for which the information should be treated as confidential, and the people and/or entities that may share the information (such as existing and future affiliates of the recipient.) Pay attention to exceptions to the obligation of confidentiality. Don't agree to more than

you can satisfy and don't agree to less than you need. Keep in mind that placing a time limit on confidentiality may be placing a time limit on your trade secrets.

You mentioned assignments of IP rights as distinct from license agreements. What are the differences?

As mentioned above, a license is a grant of permission. (As such, it can even be a unilateral declaration.) An assignment is a transfer of ownership—a bill of sale, if you will—of IP, almost always in writing. The party divesting itself of the IP is called the “assignor,” and the party receiving the IP is called the “assignee.” In the patent realm, initially, the person creating the IP, for example your engineer, owns it.

The copyright rules are different. A work created by an employee in the course of his/her employment is considered to have been authored by the employer, who owns it automatically from the point of creation. However, disputes can arise as to whether the work was made under the required conditions, or whether all individual contributors were really statutory employees (as opposed to independent contractors or consultants.)

It is important, therefore, that you put in place a procedure where your employees and consultants sign agreements requiring them to assign to your company the ownership rights in the inventions and works they create for you. Then, when an invention is conceived or a copyrightable work is created, the employee/consultant is asked to sign an assignment confirming your company owns that IP.

What does an assignment cover?

An assignor can transfer only that which he/she/it owns. It is crucial to include a clear description of the IP that is being assigned. To avoid future disagreements, and to give you clear title you can license or assign to others, the assignment should contain specific language with regard to the identity of the IP.

Should an assignment agreement be recorded with any government agency?

Yes. To protect the rights of the buyer/assignee, your IP attorney should record the assignment with the agency granting the rights. In the United States, recording patent and trademark assignments with the U.S. Patent and Trademark Office is recommended. Assignments of copyright registration are recorded at the U.S. Copyright Office, but due to differences in the statute, assignments of copyrights from employees are usually not recorded.

Are there other differences between an assignment and a license?

Yes, but for many purposes, the two can be made to have quite similar effects. For example, an assignment may be constructed to transfer all rights, but it also can be constructed to transfer only partial ownership in the IP from the assignor to the assignee.

What do we mean by partial ownership? The owner can sell less than full title, such as a quarter interest or a half interest, just as you could sell to someone a part interest in real estate you own. Your co-owner then would share access to the property, and you would split the proceeds when you sell it. The agreement will usually cover who controls the property, who has the right to extend licenses, etc. One could assign just a right to participate in an income stream from licensees—securitizing the IP—without actually assigning the IP rights themselves.

A license, on the other hand, allows the party with the intellectual property (the “licensor”) to retain exclusive ownership while granting permission to some other party (the “licensee”) to use or commercialize the intellectual property. In return, the licensor will receive some sort of compensation. You can probably see how this is similar in many ways to assigning a part ownership interest. There are, however, important differences that come into play, particularly if it becomes necessary to sue an infringer.

Sometimes, only an assignment will meet the parties' objectives. Sometimes, only a license will satisfy one or both of them. Sometimes, both kinds of transactions can be made to work. There are many important distinctions between these two types of transactions that will determine which is preferable in a given situation.

STEPS FOR CREATING AN IP TRANSACTION AGREEMENT

What is pre-deal diligence, and what should I do before consulting an attorney?

“Diligence” or “due diligence” refers to the process of conducting a prudent investigation of your prospective deal partner and, if you are buying or taking a license to the IP, the “quality” of the IP itself. Much of the assessment of the IP will have to be done by your IP attorney, but you can investigate the other party and the history of the IP.

You should identify the objectives of the parties and limitations on their ability to perform, including obligations imposed by third parties. You should also involve your IP attorney early to uncover issues relating to ownership, strength of IP protection, and whether you can practice the technology even after obtaining a license. Sometimes, a third party may have dominant rights.

How do I know I am dealing with the right party?

Although this sounds simple, often companies and their U.S. or foreign subsidiaries are involved. Be sure the proper entity having the rights and authority to enter into the agreement is a party to the agreement. A title search of the government records is also a vital part of the due diligence process for buyers.

Can an oral intellectual property agreement be enforced?

Generally, no. There are exceptions, but most IP agreements need to be in writing. In some cases, a written agreement is required by statute. An assignment of a patent, for example, must be in writing. While some agreements may be enforceable without a written agreement if sufficient supporting evidence is provided, providing such evidence is often difficult in IP arrangements. Thus, it is extremely unsafe to rely on casual oral agreements or even casual written agreements. It is important that you understand what you are giving up, what you are retaining, what you are getting, and what obligations you have.

Is a simple term sheet or memorandum of understanding between the parties sufficient to protect my interests?

While a term sheet is a good starting point for negotiating the core terms of a deal, your IP attorney will want to formalize and write the agreement as soon as possible to remove any ambiguity between the parties as to deliverables, ownership, and use of intellectual property. In fact, most term sheets expressly provide that they are not binding contracts, and their description of the IP involved may be too vague for you to rely upon.

In any event, even when the IP is clearly identified, a term sheet does not normally transfer ownership; it is usually just an expression of what the parties are working toward. A term sheet that purports to be binding may not have sufficient detail of core terms for a court to say there was a clear meeting of the minds—i.e., an understanding sufficient for an enforceable contract to have been formed.

The detail of the agreement can vary by industry and by country. In some countries, for example, the cultural norm is to rely on general and often open-ended language, whereas in the U.S., agreements are structured and specific.

If you want a term sheet that actually commits the other party to a transfer of rights, you will need to have a signed document which identifies the parties and makes the agreement over core terms clear and binding. Where the deal requires ambiguities, the document should include provisions for dealing with them.

TO LICENSE OR NOT TO LICENSE— WHAT ARE THE QUESTIONS?

What are the benefits to my granting a license?

There are a number of potential benefits to granting a license, including:

- **Increased revenue with minimal further investment.** You may have spent more money and time than expected in developing the intellectual property. A licensee may be able to complete the product development, bring the product to market, and pay royalties back to you.
- **Commercializing under-exploited IP.** You may have developed intellectual property that is not central to your business, or the IP you have developed may have uses in fields outside of your own that you are not exploiting. You could license the intellectual property to industry leaders in those ancillary fields.
- **Penetrating domestic or international markets.** Another party may have far more expertise in how to introduce your intellectual property to a new market, or may have a market presence you lack. Licensing to these parties allows quick and low risk entry into other markets.
- **Obtaining technology via a grant-back or cross-license.** Gaps in your technology may require technology from another party, and it may face the same need for a license. Exchanging technology can be a win-win situation for both of you.
- **Increased goodwill.** Licensing trademarks can increase consumer awareness of your marks, strengthening your brand.
- **Meeting requirements in the sale of a subsidiary.** When you sell a subsidiary, or spin off a unit of your company, you may need to license the technology to the buyer or new entity.

- **Evaluating a future partner.** A license enables you to “test” how well the licensee exploits the technology before entering into a more formal arrangement, such as a joint venture or merger.

What are the risks to my granting a license?

When deciding whether, and to whom, to grant a license, consider:

- **Fostering future competition.** The licensee may learn your know-how and become a direct competitor, especially when it is introducing a new product to your current market. Be careful that the license cannot be transferred to, or shared with, another entity to whom you would refuse a license.
- **Reducing return on investment.** As the licensee bears the risks and costs of bringing the product to market, it will want the lion’s share of the profits. You will receive less of a financial return than if you had manufactured the product yourself.
- **Increased liability and damage to reputation.** If the licensee performs poorly, you may risk incurring product liability and damage to your reputation.
- **Greater administrative burden.** You may need to provide the licensee with technical expertise and know-how to make the product a success, as well as take time away from other projects.

I’ve decided to grant a license. To whom do I license?

One of the most tried and true methods is to consider industry leaders. These are companies that have the market power, customer base, manufacturing capability, and financial resources to maximize profits for your IP. At the same time, there may be another player who will pay more dearly for the competitive advantage your technology provides. You need to balance higher payment rates against achievable sales volume and competition from the leaders.

Another set of candidates to evaluate are suppliers of OEMs. They have the relationships you lack that are often necessary to promote the IP. You may also find success in brainstorming commercial applications. Gather your engineers, scientists, and marketers to consider potential commercial applications, then target the sphere of industry leaders as licensee candidates.

Lastly, consider packaging it. Develop a beta test product, perform a small scale production, and offer a turn-key product/process to your licensee.

What are the benefits in my taking a license?

Your reasons for taking a license might include:

- **Updating an existing product line or expanding into a new one.** Obtaining a license may allow you to augment your own technology, increase market coverage, update and expand an existing product, or introduce a more profitable new product more quickly and cheaply than developing new technology internally.
- **Reducing your need for expensive R&D.** You can save time and money by obtaining a license to the technology rather than developing it yourself.
- **Accessing technical expertise.** As part of the deal, you may have access to the licensor’s training and support to fill in the gaps in your own knowledge.
- **Appearing bigger than you are.** With a licensing portfolio, you can appear as though your company developed the latest technology even though you may not have the R&D and engineering arm to have actually done so.
- **Increased leverage in the marketplace.** Being able to use another’s trademark can enhance the sales of your product, and licensing popular technology can enhance your credibility with consumers.
- **Obtaining a right to which others are excluded.** If you can negotiate an exclusive license with the licensor, none of your competitors will be able to sell the same product.
- **Settling or avoiding an IP dispute.** A patent owned by another may block you from introducing your product. Obtaining a license to that patent will allow you to bring your product to market.

What are my risks when taking a license?

Examples include:

- **Up-front costs may be lost.** If the product proves to be a failure in the marketplace, you can lose your up-front license fees. You may even need to continue paying the licensor royalties despite a lack of profits on the endeavor.
- **Unlicensed competition could gain an advantage.** If the technology you license is easy to design around, your competitors may begin using similar technology that achieves the same goal in a different way. If they don’t have to pay royalties for the competing technology, you may find yourself undercut in price.
- **The technology may be too costly.** Your margins could be undercut if you are required to pay large up-front licensee fees or too costly royalty payments.

- **Damage to reputation of your core business.** Licensing a technology that turns out to have a bad reputation with your customers can cost you goodwill towards your other products.
- **Disclosure of confidential business information.** There is a risk that unrelated technical information, business plans, or trade secrets could be disclosed to the licensor.
- **Compounded royalties.** You may need licenses from other parties, and the consequences of the royalty “stacking” may make the first license impractical or unprofitable.

How do I know I am getting what I need and what I can use?

With help from your IP attorney, pre-deal diligence will help expose whether the technology is right for you and whether the strength of protection offered by the licensor’s patents, trademarks, trade secrets, and copyrights is adequate for your business goals. Your IP attorney may uncover weaknesses in the protection and could offer ways to design around it or bargain for better terms.

Your licensor may not own all of the rights to the technology provided, leaving you with the risk you are infringing third party rights by using the technology. Your IP attorney will help uncover this potential problem and negotiate provisions to protect against the deal becoming unviable or unprofitable.

FREQUENTLY USED IP AGREEMENTS

For what kinds of business agreements should I consider an IP attorney?

Listing every possible agreement title is impossible, but the following list covers a number of such agreements, with some comments about points to consider:


- **Assignment:** a transfer of ownership of intellectual property. Sometimes, it is important to retain a license or an option to obtain a license. That way, you don’t face the distressing situation of having sold off something you later find you need. In other circumstances, a license followed by an assignment—provided conditions are satisfied—allows a better sharing of risk than an outright assignment. If the parties cannot agree on the sales price because they have different opinions on the projected sales, the purchase decision can be conditioned on performance. If the licensee/buyer meets targets, the transaction becomes a sale. Otherwise, it remains a license—perhaps one that terminates.
- **Beta testing agreement:** an agreement between a product developer and an early stage product user. The user agrees to identify problems with the product and confirms that the product works as intended. The key issues are often secrecy and access to the product or test results on the product. In return for giving active feedback and running the risk of product defects, the tester often gets the product for free or at a sharp discount. Beta testing may help maintain the activity as an experimental use under patent law, extending filing deadlines.
- **“Click-wrap” or “browse-wrap” agreement:** an internet-based agreement that provides the user with terms and conditions for use of a product or service (typically internet or software based) and where the user expresses its acceptance of the terms through actions rather than a signature (generally by clicking an “I agree” button) prior to use. The enforceability of such agreements is a matter of state law, but more often than not these agreements have been found enforceable when the terms are not at odds with consumer protection policies. Nevertheless, care is needed to maximize the probability of a court enforcing the agreement.
- **Co-branding, co-marketing or co-promote agreement:** an agreement to promote and/or market products to consumers. Variants include marketing one product under a joint or combined label, marketing one product under separate labels, and leveraging joint marketing resources to market different product lines. Care is needed to be able to terminate cleanly, without giving up rights and retaining those rights you desire.
- **Collaboration agreement:** an agreement to develop a product or provide a service together, much like a joint venture, but without the creation of a distinct entity or project. Collaboration agreements are sometimes the only way a small company can expect to get its technology to market, such as in the pharma space. There is usually considerable uncertainty about the technology or science, the time and funds needed to bring the collaboration to fruition, etc. It is important there be a great deal of pre-agreement communication to establish realistic and compatible expectations on all sides, to obtain comfort with the other parties’ levels of commitment (these deals may involve more than two parties,) and to structure effective procedures for interim management and resolution of disputes. It is a “given” the collaboration will come to an end of its own accord, having met its goals, or through early termination. So thought must go into “what if” scenarios and termination planning. The parties are often of disparate size, and termination (and success) will impact them very differently. Your IP attorney should help you shape the relationship from the

very beginning. Ownership of rights, data, etc. are core to the project.

- **Consulting agreement:** used to set forth the consultant's role, compensation, and obligations regarding developing and assigning intellectual property. Be careful that the consultant is a true independent contractor and not an employee in disguise, or you may be liable for failing to withhold payroll taxes. Likewise, care needs to be exercised to balance the consultant's need to seek other gainful employment contracts with your need to avoid leakage of your trade secrets and confidential information. Some states have declared non-competition provisions to be unenforceable as a matter of public policy, so the location of the engagement and the choice of law can have a dramatic impact on what you can do to protect that valuable information.
- **Development agreement:** outlines the responsibilities associated with developing a technology or product and establishes provisions for the ownership or use of the newly developed technology or product.
- **Distribution agreement:** used when one company buys (or takes on consignment) the products of another and distributes those products for sale to end-users. Termination of distributorships is a problematic subject. In some countries (and even in some U.S. industries and states,) there are laws protecting distributors at the point of termination. Some distributors may resort to a crude form of self-help by registering their supplier's trademarks in their own name, thus creating a major dispute over trademark ownership, usually accompanied by a demand for payment of a large sum of money to assign the rights. Thus, prior to entering into a distributorship arrangement, one should file trademark applications in all applicable jurisdictions.
- **Employment agreement:** agreement between employee and employer outlining the scope of employment and assignment of intellectual property rights. Whichever side you are on, it can pay to consult an IP attorney to make sure you will be getting what you expect or that you are not giving up more than is necessary.
- **Escrow agreement:** an agreement in which one party places intellectual property in the hands of a neutral until, at the occurrence or a predefined trigger event, the IP is turned over to a second party. Escrow agreements may be used to place source code, secret formulas, and other company "crown jewels" in safe hands so that if something happens to the owner (e.g., bankruptcy or abrupt business cessation, a fire, death of a key scientist, etc.) a licensee or buyer is comfortable that it can get its hands on the information it needs to obtain the

bargained-for benefit. There are established companies that will act as third-party escrow agents for technology deals

- **Joint development agreement:** a form of collaboration agreement used when parties co-develop a product or technology. It typically sets forth the role of each party and provisions for ownership or use of the product or technology.
- **Joint venture agreement:** a project in which parties provide the capital, labor, and/or technology to bring the project to fruition. A joint venture often (but not always) involves forming a separate entity (often referred to as a "special purpose vehicle,") with each party having a part interest and defined role in management. Often, the parties loan employees to the joint venture who become full or part time employees of the joint venture. This helps compartmentalize the work of the joint venture, isolate the IP, and may facilitate spinning out the joint venture into an independent entity at some point.
- **License:** an agreement where one party grants certain rights, but not ownership, in IP to another party, typically allowing manufacture and sale, at least.
- **Material transfer agreement:** an agreement governing the right to use tangible material transferred from the licensor, usually biological material such as a cell line or a chemical or non-biological material sample. It may or may not impose an obligation of secrecy on the receiving party, but when the origin is in the academic world, credit and provenance, not secrecy, are usually primary concerns.
- **Non-compete agreement:** restricts the ability of one party to compete in the same market with another party; or, in the employment context, restricts the ability of an employee from working for a competitor. The state law trend is to limit the duration and geographical scope of non-competition that will be enforced in employment agreements, and some states have basically outlawed these provisions in employment agreements.
- **Non-disclosure (NDA) or confidentiality agreement:** outlines the obligations to maintain proprietary information in confidence. Usually, these agreements will also contain non-use provisions. See comments above. Beware of form NDAs downloaded from the web.
- **Option agreement:** provides opportunities to obtain certain rights if particular events occur. For example, a company might have the right of first refusal to purchase technology developed by a university lab or another company. Option agreements have many uses. For example, an option agreement may be entered into



while conducting due diligence toward taking a license or buying IP, to make sure the property is “locked up” or that exclusive rights will remain available. There will be some cost involved, of course.

- **Research agreement:** used when a party agrees to fund the research in a new technology in exchange for a stake in the technology.
- **Reseller agreement:** occurs when one party agrees to buy the products of another party and then resell them to third parties, such as to companies further down the supply chain, or directly to consumers. A reseller agreement is to be distinguished from a distributorship agreement. Distributors often maintain no inventory or

have inventory on consignment. Their pay is usually a commission, whereas a reseller sets its own markup.

- **Shrink-wrap agreement:** typically used with packaged software, where the terms for using the software are printed on a document in the package which is only accessible after the software has been purchased and unwrapped. A shrink-wrap agreement may be combined with a click-wrap agreement when the software is installed. Shrink-wrap agreements are less important than they used to be, now that most software is distributed online, instead of in packages on store shelves.

Other available Q&A Booklets:

Q&A on Intellectual Property Litigation

Q&A on Patents

Q&A on Trademarks and Copyrights

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