Technology Licensing/ Joint Ventures

Two alternative ways to obtain foreign trade income include technology licensing and joint ventures. While not necessarily the most profitable form of exporting, they do offer certain advantages, particularly for small and medium sized businesses.

Technology Licensing

Technology licensing is a contractual arrangement in which the licensor's patents, trademarks, service marks, copyrights, trade secrets, or other intellectual property may be sold or made available to a licensee for compensation that is negotiated in advance between the parties. This compensation, or royalties, may be a lump sum royalty, a running royalty (royalty that is based on volume of production), or a combination of both. U.S. companies frequently license their technology to foreign companies that then use it to manufacture and sell products in a country or group of countries defined in the licensing agreement.

A technology licensing agreement usually enables a firm to enter a foreign market quickly, and poses fewer financial and legal risks than owning and operating a foreign manufacturing facility or participating in an overseas joint venture. Licensing also permits U.S. firms to overcome many of the tariff and nontariff barriers that frequently hamper the export of U.S. manufactured products. For these reasons, licensing can be a particularly attractive method of "exporting" for small companies or companies with little international trade experience, even though licensing is profitably employed by small and large firms alike. Technology licensing can also be used to acquire foreign technology such as, cross-licensing agreements or grantback clauses awarding rights to improved technology developed by a licensee.

Technology licensing is not limited to the manufacturing sector. Franchising is also an important form of technology licensing used by many service industries. In franchising, the franchisor (licensor) permits the franchisee (licensee) to employ its trademark or service mark in a contractually specified manner for the marketing of goods or services. The franchisor usually continues to support the operation of the franchisee's business by providing advertising, accounting, training, and related services and in many instances also supplies products needed by the franchisee.

As a form of "exporting," technology licensing has certain potential drawbacks. One negative aspect of licensing is that control over the technology is weakened because it has been transferred to an unaffiliated firm. Additionally, licensing usually produces fewer profits than exporting actual goods or services. In certain developing countries, there also may be problems in adequately protecting the licensed technology from unauthorized

use by third parties.

In considering the licensing of technology, it is important to remember that foreign licensees may attempt to use the licensed technology to manufacture products in direct competition with the licensor or its other licensees. In many instances, U.S. licensors may wish to impose territorial restrictions on their foreign licensees, depending on U.S. and foreign antitrust laws as well as the licensing laws of the host country. Also, U.S. and foreign patent, trademark, and copyright laws can often be used to bar unauthorized sales by foreign licensees, provided that the U.S. licensor has valid patent, trademark, or copyright protection in the United States or the other pertinent countries. In addition, unauthorized exports to the United States by foreign licensees can often be prevented by filing unfair import practices complaints under section 337 of the Tariff Act of 1930 with the U.S. International Trade Commission, and by recording U.S. trademarks and copyrights with the U.S. Customs Service.

As in all overseas transactions, it is important to investigate not only the prospective licensee but the licensee's country as well. The government of the host country often must approve the licensing agreement before it goes into effect. Some governments prohibit royalty payments that exceed a certain rate or contractual provisions barring the licensee from exporting products manufactured using the licensed technology to third countries.

The prospective licensor must always take into account the host country's:

- Foreign patent, trademark, and copyright laws;
- Exchange controls;
- Product liability laws;
- Possible countertrading or barter requirements;
- Antitrust and tax laws; and
- Government attitudes toward repatriation of royalties and dividends.

The existence of a tax treaty or bilateral investment treaty between the United States and the prospective host country is an important indicator of the overall commercial relationship. Prospective U.S. licensors, especially of advanced technology, also should determine whether they need to obtain an export license from the U.S. Department of Commerce or other regulating agencies.

In a few instances, international technology licensing agreements can unlawfully restrain trade in violation of U.S. or foreign antitrust laws. As a general rule, U.S. antitrust laws prohibit international technology licensing agreements that unreasonably restrict imports of competing goods or technology into the United States or unreasonably restrain U.S. domestic competition or exports by U.S. persons.

Whether or not a restraint is reasonable is a fact-specific determination that is made after consideration of the availability of:

- Competing goods or technology;
- Market shares;
- Barriers to entry;
- The business justifications for and the duration of contractual restraints; and,
- Valid patents, trademarks, and copyrights.

The U.S. Department of Justice's and Federal Trade Commission's Antitrust Guidelines the Licensing of Intellectual Property (1995) states the two agencies' enforcement policies regarding the licensing of intellectual property protected by patent, copyright, and trade secret law and know-how. For instances in which significant federal antitrust issues are presented, U.S. licensors may wish to consider applying for an export trade certificate of review from the Department of Commerce (see ***Chapter 4***) or requesting a Department of Justice business review letter pursuant to 28 CFR50.6.

Foreign countries, particularly the European Union, also have strict antitrust laws that affect technology licensing. The European Union has issued detailed regulations known as a block exemption, governing patent and know-how licensing agreements as well as ancillary provisions relating to other intellectual property rights. These block exemption regulations are entitled "Commission Regulation (EC) No. 240/96 of 31 January 1997 on the Application of Article 85(3) of the Treaty [of Rome] to certain categories of technology transfer agreements." These regulations should be carefully considered by anyone currently licensing or contemplating the licensing of technology to the European Union.

Because of the potential complexity of international technology licensing agreements, firms should seek qualified legal advice in the United States before entering into such an agreement. In many instances, U.S. licensors should also retain qualified legal counsel in the host country in order to obtain advice on applicable local laws and to receive assistance in securing the foreign government's approval of the agreement. Sound legal advice and thorough investigation of the prospective licensee and the host country will increase the likelihood that your licensing agreement will be a profitable transaction.

Joint Ventures

In some cases, joint ventures provide the best partner-like manner of obtaining foreign

trade income. The firm then choses to begin a business relationship with a firm in the host country. International joint ventures are used in a wide variety of manufacturing, mining, and service industries and frequently involve technology licensing by the U.S. firm to the joint venture.

Host country laws may require that a certain percentage (often 51 percent or more) of manufacturing or mining operations be owned by nationals of that country, thereby limiting U.S. firms' local participation to minority shares of joint ventures. In addition to such legal requirements, U.S. firms may find it desirable to enter into a joint venture with a foreign firm to help spread the high costs and risks frequently associated with foreign operations.

The local partner will likely bring to the joint venture its knowledge of the customs and tastes of the people, an established distribution network, and valuable business and political contacts. Having a local partner may also lessen the "foreigner" image of the firm and thus may provide some protection against discrimination or expropriation if conditions change.

There are some possible disadvantages to international joint ventures. A major potential drawback of joint ventures, especially in countries that limit foreign companies to minority participation, is the loss of effective managerial control. This can result in reduced profits, increased operating costs, inferior product quality, exposure to product liability, and environmental litigation and fines. U.S. firms that wish to retain effective managerial control will find this issue an important topic in negotiations with the prospective joint venture partner and the host government.

Like technology licensing agreements, joint ventures can raise U.S. or foreign anti-trust issues in certain circumstances, particularly when the prospective joint venture partners are major existing or potential competitors in the affected national markets. Firms may wish to consider applying for an export trade certificate of review from the Department of Commerce or a busi-ness review letter from the Department of Justice when significant federal anti-trust issues are raised by the proposed international joint venture. (See ***Chapter 4***).

Because of the complex legal issues frequently raised by international joint venture agreements, it is very important, to seek legal advice from qualified U.S. counsel before entering into any such agreement. Many of the export counseling sources in ***Chapter 2*** can help direct a U.S. company to legal counsel suitable for its needs.

U.S. firms contemplating international joint ventures should consider retaining experienced counsel in the host country. U.S. firms can find it very disadvantageous to rely upon their potential joint venture partners to negotiate host government approvals and advise them on legal issues, since their prospective partners' interests may not always coincide with their own. Qualified foreign counsel can be very helpful in obtaining government approvals and providing ongoing advice regarding the host country's intellectual property, tax, labor, corporate, commercial, antitrust, and exchange control laws.