



# USING TECHNOLOGY LICENSING AND JOINT VENTURES

## In This Chapter

- **Methods of obtaining foreign trade income**
- **Advantages and disadvantages of technology licensing and joint ventures**

**Y**ou should consider two alternative ways of obtaining international sales income: technology licensing and joint ventures. Although not necessarily the most profitable forms 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 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 your firm to enter a foreign market quickly, and it 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 non-tariff 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 small and large firms profitably use this technique. Technology licensing may also be used to acquire foreign technology through cross-licensing agreements or grant-back clauses that award rights to improved technology developed by a licensee. Seek

legal advice to determine liability where licensing is involved.

Technology licensing is not limited to the manufacturing sector. Franchising is also an important form of technology licensing used by many service industries (see Box 7.1). In franchising, the franchiser (licensor) permits the franchisee (licensee) to use its trademark or service mark in a contractually specified manner for the marketing of goods or services. The franchiser usually continues to support the operation of the franchisee's business by providing advertising, accounting, training, and related services. In many instances, the franchiser also supplies products needed by the franchisee.

Franchising is not the exclusive domain of well-known brands. Scores of new franchising concepts are converted into profitable businesses every year, and the majority are created in the United States. Among recent franchising concepts that have gone global are personal fitness, flowers and candy, and elder care. Many of the franchises are being created especially for entrepreneurs in developing countries and feature relatively affordable license fees and other inputs. Attending the International Franchise Association convention and trade fair is a good way to learn about trends and new franchising concepts. For information, visit [www.franchise.org](http://www.franchise.org).

As a form of "exporting," technology licensing has certain potential drawbacks. One negative aspect of licensing is that your control over the technology is weakened because it has been transferred to an unaffiliated firm. Additionally, licensing usually produces fewer profits for your company than exporting actual goods or services. In certain developing

#### BOX 7.1 ABOUT FRANCHISING

Many new small business owners choose franchising over starting a new business because it provides easy access to an established product, reduces many of the risks involved in opening a

new business, gives access to proven marketing methods, and, in some instances, furnishes assistance in obtaining startup capital from financing sources.

#### FACT:

Companies in a wide variety of industries enter joint ventures as a way of obtaining revenue from overseas operations.

#### INSIGHT:

By forming partnerships or conglomerates, companies can share risk and expertise.

**BOX 7.2 WHAT YOU SHOULD KNOW ABOUT INTELLECTUAL PROPERTY**

Do you have a strategy to protect your company's intellectual property while making sales in international markets?

If not, consider the following:

- A foreign company can appropriate your intellectual property in a foreign country before your company has even marketed in that country or in the United States.
- The processes for applying for intellectual property protection differ from country to country.

Although effective intellectual property management should be a key element of every company's day-to-day business strategy, it is essential when doing business internationally.

countries, there also may be problems in adequately protecting the licensed technology from unauthorized use by third parties (see Box 7.2).

You should make sure to register your patents and trademarks in this country. Copyright is recognized globally, but your patents and trademarks are territorial, meaning that rights are defined and interpreted differently. For this reason, you need to file your patents and trademarks with each country you intend to do business in. An exception is the European Union (EU), because its laws apply to all members. The Patent Cooperative Treaty and the Madrid Protocol allow you to register your patents and trademarks in your home country and apply for protection in the EU as well as in specific countries throughout the world. For more information and instructions for applying, visit [www.stopfakes.gov](http://www.stopfakes.gov) and [www.uspto.gov](http://www.uspto.gov).

In considering the licensing of technology, 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 countries.

Many countries, particularly the 27 member states of the European Union, also have strict antitrust laws that affect technology licensing. The European Union has issued a detailed regulation, known as the *block exemption regulation*, governing patent and know-how licensing agreements as well as design and model rights and software copyright licenses. The block exemption regulation is Commission Regulation (EC) No. 772/2004 of April 27, 2004, and deals with the application of article 81(3) of the Treaty of Rome to categories of technology transfer agreements. If you are currently licensing or contemplating

licensing technology to the European Union, you should carefully consider the regulation.

Because of the potential complexity of international technology licensing agreements, your company 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 partnerlike manner of obtaining foreign trade income. International joint ventures are used in a wide variety of manufacturing, mining, and service industries, and they frequently involve technology licensing by the U.S. company 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. companies' local participation to minority shares of joint ventures. Despite such legal requirements, as a U.S. firm you 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 local consumers, an established distribution network, and valuable business and political contacts.

There are some possible disadvantages to international joint ventures. A major potential drawback, especially in countries that limit foreign companies to minority participation, is the loss of effective managerial control. As a result, you may experience 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

### FACT:

Domestic and overseas trade shows can help small firms find technology licensing and joint venture opportunities, and U.S. government assistance is also available at many of them.

### INSIGHT:

German trade shows, both vertical and horizontal, are among the biggest international shows in the world.

will find this issue important in negotiations with the prospective joint venture partner and the host government.

Because of the complex legal issues frequently raised by international joint venture agreements, you should seek legal advice from qualified U.S. counsel before entering into such an agreement. Many of the export counseling sources discussed in Chapter 4 can help direct you to legal counsel suitable for your needs.

U.S. companies contemplating international joint ventures should consider retaining experienced counsel in the host country as well. You may be at a disadvantage if you rely on your potential joint venture partners to negotiate host government approvals and to advise you on legal issues, because the interests of the prospective partners may not always coincide with your 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.

CASE STUDY:

# Spancrete Machinery Corporation

*"There's just no doubt that selling overseas has made SMC a more effective exporter and our products more competitive."*

—Terry Dittrich, international sales manager, Spancrete Machinery Corporation

Construction quality in China is improving, and some of the credit for better building goes to U.S. firms like Wisconsin-based Spancrete Machinery Corporation (SMC), makers of machines that produce precast reinforced concrete floor and wall panels. How SMC engineered its way into China provides a model that may benefit other U.S. firms eager to sell to this booming market of 1.3 billion consumers.

## THE COMPANY

SMC, a division of the Spancrete Group, employs 45 people in its Waukesha, Wisconsin, production facility. The firm, founded by Henry Nagy, manufactured the first precast hollow-core slabs in North America in 1952. SMC, which sells its equipment worldwide under license agreements and direct sales, is a client of the U.S. Commercial Service Export Assistance Center in Milwaukee.

SMC entered China in the late 1980s. It wanted to incorporate licensing agreements, but the Chinese government forbade such arrangements. SMC opted to sell the machinery outright. Nevertheless, SMC's hollow-core machines were the first foreign equipment of that type sold in China.

## THE CHALLENGE

The early years were challenging, concedes Terry Dittrich, SMC's international sales manager: "Our customers were state-owned enterprises, and the Chinese government encouraged them to expand into the precast construction business, despite their limited knowledge of that sector."

## THE SOLUTION

Those companies started by producing floor slabs, SMC's most basic product, but local architects and engineers had limited experience with precast products of this type. Even in a state-controlled economic system, companies need effective marketing to generate sales. To better support the companies, SMC began assisting with seminars for these state-owned enterprises and the construction community in general.

SMC's next achievement was to establish the China Spancrete Association, probably the first organization of its kind. The association is a non-profit support organization for SMC's Chinese customers, assisting them in technical, production, and marketing

procedures. "At first, the Chinese didn't understand the concept of a professional association," explains Dittrich. "They said, 'Why should we pay dues to belong to something like this? Why should we cooperate with people outside of our own enterprise?' It's not how they operated. Now they can see the value and continue to expand the association's efforts."

Working through the association, SMC pooled the existing knowledge for the benefit of all members. The association tackled the lack of codes and standards, making recommendations on matters like the loads that floors can safely carry and conducting research on seismic and fire-safety issues. Ultimately, SMC, with the association, achieved the registration of Spancrete-China products in the national building and design code.

Business processes are changing rapidly in China, and competitors are getting more aggressive. Also, the economic boom has moved south and west of where it started, creating more opportunities and challenges. Recently, Dittrich used the Commercial Service's Gold Key Service and Single Company Promotion program in seven Chinese

cities. The Commercial Service identified local companies interested in purchasing SMC equipment systems and coordinated meetings with key government officials. Dittrich expects significant new sales because of the introductions provided by the Commercial Service.

However, the Commercial Service alone will not ensure success. SMC must continue to build relationships, help customers succeed by finding creative solutions to their problems, and adapt its products and services to meet the needs of a dynamic marketplace.

Dittrich claims that experience in international markets has made him a more effective professional and the company more competitive. "There's just no doubt that selling overseas has made SMC a more effective exporter and our products more competitive. Our key personnel have grown from the international experience, and we continuously bring ideas back home and apply them throughout the company."

"Competition is tough in these markets," Dittrich says, "but that's where the opportunities are. Exporting is no longer an option, and America's export future lies in these markets."

### LESSONS LEARNED

For U.S. companies attempting to sell in China, Dittrich has these recommendations:

- **Find good representation.** Connections are key, as evidenced in the Chinese expression *guanxi*, meaning "personal relationship."
- **Try to secure payment in advance.** Equity stakes can be a problem, given the limitations of the Chinese legal framework and challenges of business transparency, and Americans need to conduct thorough due diligence.
- **Keep the product simple.** The more complex the product, the more things can go wrong.
- **Talk to your Chinese business partners about taking a long-term perspective.** American companies need to make a long-term and sustained commitment to these emerging markets if they are to successfully build lasting relationships. Encourage your Chinese partners to take a similar long-term perspective.
- **Investigate Web sites for manufacturers.** Manufacturing firms should check out the National Association of Manufacturers export portal at [www.nam.org](http://www.nam.org). If you're seeking help to make your manufacturing processes more competitive, learn about the services of the U.S. Department of Commerce's Manufacturing Extension Program at [www.mep.nist.gov](http://www.mep.nist.gov).

### ACTION

Here's what you can do to help your business succeed in China:

- **Visit the China Business Information Center.** For useful, comprehensive information on the Chinese market, go to [www.export.gov/china](http://www.export.gov/china). Of particular interest is the self-assessment, which asks, "Are you China ready?"



Spancrete Machinery Corporation of Waukesha, Wisconsin, has found China to be a key market for its machinery that produces precast concrete floors and wall panels. Terry Dittrich (center), international sales manager, is pictured here with other senior SMC managers and Chinese business partners.