LICENSING

IN THE

FAR EAST

LARRY W. EVANS

Resume of Larry W. Evans

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Personal

Born October 4, 1939 at Georgetown, Indiana
Married (Lori) since 1964, three adult children
Residence:
19 Stoneridge Drive
So. Barrington, IL 60010
(847) 382-8636

Education

B.S. (Ch.E) 1961 - Purdue University
J.D. (Law) 1965 - The George Washington University

Bar Admissions

USPTO - 1962
Minnesota - 1965
U.S. Court of Appeals for Federal Circuit
U.S. District Court (Minnesota and Arizona)

Practice

Domestic and International Technology Licensing
Preparation and Negotiation of License Agreements
International Business Transactions
Dispute Resolution
Service as an Expert Witness
Mediation and Arbitration

Professional Activities

Licensing Executives Society (USA and Canada):

Past President - 1986-87 Vice President - 1983-84
President - 1985-86 Secretary - 1980-83
President-Elect- 1984-85 Int'l Delegate - 1980-93

Licensing Executives Society International

- President Elect - 1992
- President - 1993
- Past President - 1994
- Chairman, Long-Range Planning Committee - 1994/1996
- Chairman, Endowment Committee - 1995/1996

Professional Activities (cont'd)

American Bar Association (PTC Section)-Past Chairman, China Committee
American Intellectual Property Law Association
Association of Corporate Patent Counsel
Chemical Manufacturers Association (Past Chairman of I.P. Committee)
International Intellectual Property Association, the U.S. Chapter of AIPPI (Member of the Executive Committee)
National Training Center-Dalian, China (Member of the Advisory Board)
The Patent, Trademark & Copyright Research Foundation (Member of The Advisory Council)

Professional Employment History

- 1961-1965, Adams, Forward & McLean, Washington, D.C.

  - Student Associate, Patent Agent

- 1965-1970, Archer, Daniels, Midland Company, Minneapolis, Minnesota (Chemical company acquired in 1968 by Ashland Oil Co. who moved me to Ashland Chemical in Houston, Texas)

  - Patent and Licensing Attorney
  - Responsible for all areas of intellectual property practice, including extensive licensing
  - 1968-1970, Division Counsel

- 1970 to April, 1993 - B.P. America, Cleveland, Ohio (formerly, The Standard Oil Company)

  - 1970 to 1976, Patent and License Counsel
  - 1976 to 1993, Director, Patent and License Department and Vice-President, BP Chemical Co., Inc. (formerly, Sohio Chemical Co.)
  - Devoted almost all practice from 1970 to 1976 to licensing of Sohio's world-famous acrylonitrile process technology and other petrochemical technologies
  - 1976 to present, managed all intellectual property lawyers at BP and continued active role in BP's more significant licensing activity
  - More than $1 billion in royalty income and catalyst profit realized through these licensing projects

Professional
Employment History (cont'd)

- Sohio/BP licensing has been world-wide activity (e.g. North America, South America, Europe, Asia and Africa) establishing important personal and business contacts throughout the world
- Was first American to successfully license technology to the P.R.C. The 1973 license has been followed by eight additional licenses and innumerable personal contacts

- April, 1993-December 31, 1995, Willian Brinks Hofer Gilson & Lione

- Practice included domestic and international technology licensing, preparation and negotiation of license agreements, dispute resolution and service as an expert witness.

Career Highlights
(See attached list)

Publications and Speeches
(See attached list)

Career Highlights

During 1970-1976, Mr. Evans was responsible for licensing Sohio's world-famous acrylonitrile technology (recognized by many in the industry as the most successful chemical licensing program in the world). He personally negotiated more than 15 licenses throughout the world during this period. In 1973, Sohio was the first American company to license technology to China following the resumption of friendly relations.

From 1976 to 1993, Mr. Evans headed the Patent and License Department of Sohio and BP America, following its acquisition of Sohio in 1987. During this period, Mr. Evans supervised and, in some cases, handled personally many additional licenses. Additionally, he was responsible for resolving (through negotiation, arbitration or litigation) many disputes with licensees, competitors and partners.

Sohio's/BP America's License Department was a profit center until 1989 and Mr. Evans' responsibility extended to that of running a business that generated considerable royalty and catalyst income to Sohio and BP America during the 1970-1989 period.

Beginning in 1968, Mr. Evans participated in The Licensing Executives Society (LES). This activity began with several speaking engagements. Topics centered around process licensing, royalties, license agreements, licensing in developing countries, China licensing, and related fields. In 1979, Mr. Evans was elected Secretary of LES USA/Canada, a position he held through 1983. He then served as Vice-President in 1984, President-Elect in 1985, President in 1986 and Past-President in 1987. Throughout this period he was a delegate to LES International.

Following his progression through LES USA/Canada, Mr. Evans became more active in LES International, which is the international federation of national and regional LES Societies. He became a Committee Chairman in 1989, in 1992 served as President-Elect and in 1993 as President of LES International. LES International (LESI) has nearly 8,000 members from 27 national and regional Societies and more than 55 countries. Almost all substantial licensing is conducted by LES members (on at least one side of the transaction). Without qualification, it can be said that LESI is the most important organization in the world in the field of licensing and technology transfer.

Mr. Evans joined the Chicago intellectual property law firm, Willian Brinks Hofer Gilson & Lione in April, 1993 as Counsel to the firm. While at Willian Brinks, he specialized in domestic and international licensing, preparation and negotiation of licensing agreements, international business transactions, dispute resolution and service as an expert witness (e.g. in licensing and damages).

Beginning in January, 1996, Mr. Evans initiated his present practice as an Intellectual Property and Licensing Consultant continuing to specialize in the above areas.

LICENSING IN THE FAR EAST

Larry W. Evans

- GENERALLY
- JAPAN
- THE SPECIAL CASE OF CHINA

- FASTEST GROWING AREA IN THE WORLD
- U.S. GNP GROWTH > 3%
- ASIAN-PACIFIC COUNTRIES > 5% (CHINA > 10%)
- 30% OF WORLD'S POPULATION
- FOCUS WILL BE ON JAPAN AND CHINA

LICENSING IN JAPAN

U.S. SOCIAL/LEGAL SYSTEM

- COUNTRY ORGANIZED AROUND ITS LEGAL SYSTEM
- HETEROGENEOUS, CONTINENTAL SOCIETY
- AMERICANS NEED NO CULTURAL TRADITIONS; INDIVIDUALISM ENCOURAGED
- LAW AND POLITICS NECESSARY ELEMENT OF AMERICAN LIFE

LICENSING IN JAPAN
U.S. SOCIAL/LEGAL SYSTEM (cont'd)

- GOD-FEARING; MORALITY WINS WHEN IN CONFLICT WITH SOCIETY
- INDIVIDUALITY COMES FIRST; SOCIETY IS A SOCIAL CONTRACT BETWEEN INDIVIDUALS
- SOCIAL AND POLITICAL FREEDOM VALUED TO EXTRAVAGANT DEGREE
- WITHOUT LAW, ANARCHY AND CHAOS WOULD RESULT

LICENSING IN JAPAN
JAPANESE SOCIAL/LEGAL SYSTEM

- LAW PLAYS ONLY A PERIPHERAL ROLE

- ISOLATED, HOMOGENOUS, ISLAND SOCIETY (NO MIGRATION FOR > 1,000 YEARS)

- TRIBAL TRADITIONS HAVE ENDURED

- CANNOT COMPREHEND U.S. VIEW THAT LAW (LAWYERS) AND POLITICS (POLITICIANS) ARE NECESSARY FOR ORDER

LICENSING IN JAPAN
JAPANESE SOCIAL/LEGAL SYSTEM (cont'd)

- CAN (AND DOES) FUNCTION WITHOUT NEEDING LAW
- HAS NO JUDGING GOD
- NO NEED TO BE DIFFERENT
- MUST ACT IN ACCORD WITH GIRI WITH THE APPROPRIATE NINJO;
- ACTING "UN-JAPANESE" LEADS TO OSTRACISM
- JAPANESE DO NOT LIKE LAWYERS
  -RESORTING TO LAW PRESUPPOSES BREAK-DOWN IN SOCIAL HARMONY
  (APPROPRIATE GIRI AND NINJO HAVE NOT BEEN UTILIZED)
- LAW IS NOT AN ALTERNATIVE TO VIOLENCE AND CHAOS; IT IS THE EQUIVALENT

LICENSING AND DISPUTE RESOLUTION IN JAPAN

- LAWYERS SHOULD BE KEPT IN BACKGROUND
- BUSINESSMEN SHOULD BE IN FRONT DOING THE NEGOTIATION
- USE "LAWYERS" ONLY WHEN THEY DO
- LAWYERS REGARDED AS "DISREPUTABLE CHARACTERS EMPLOYED BY PEOPLE UNABLE TO MANAGE THEMSELVES IN A CIVILIZED MANNER"
- SILENCE EQUALS STRENGTH
- ESTABLISH FEELING OF TRUST AND MUTUAL OBLIGATION-THEN MAKE THE DEAL
- QUALITY IS MORE IMPORTANT THAN PRICE
- AGREEMENTS ARE "LIVING" DOCUMENTS
  - EXECUTION IS BEGINNING, NOT END OF NEGOTIATIONS
  - ALWAYS STICK TO BASIC PRINCIPLES

LICENSING AND DISPUTE RESOLUTION IN JAPAN
(cont'd)

- DON'T BE RELUCTANT TO COMPROMISE NON-BASIC ITEMS BUT ALWAYS GET SOMETHING IN RETURN

- EXPRESS COMPROMISES AS POSITIVES-NOT NEGATIVES

HANDLING DISPUTES WITH JAPANESE

- ALWAYS BE PREPARED TO NEGOTIATE

- "CIRCLE THE WAGONS" ONLY WHEN A CRITICAL MATTER IS IN DISPUTE

- AVOID PERSONAL ANIMOSITY-BE CREDIBLE AND DIPLOMATIC-NOT A TOUGH-TALKING "HARD-NOSE"

- INCLUDE AS DISPUTE RESOLUTION CLAUSE-"NEGOTIATE WITH SINCERITY TO ACHIEVE MUTUALLY-BENEFICIAL RESOLUTION OF ALL DISPUTES"

JAPANESE NEGOTIATING STYLE

- NOREN DESU - (IMAGE AND GOODWILL)- MAY SACRIFICE PROFIT TO IMPROVE OR MAINTAIN IMAGE

- "SMOKING OUT THE TANUKI" - (DETERMINING TRUE INTENTION)-SEPARATE "CURIOUS" FROM "BONA FIDE"

- FUMIE - DETERMINING THE SINCERITY OF THE OTHER SIDE

- NEMAWASHI-(DIGGING AROUND THE ROOTS)

  - INDIRECT PERSUASION
  - TIME NEEDED TO GO THROUGH MOTIONS
  - CELEBRATIONS TO BREAK DOWN RESTRAINT
  - WARM HUMAN RELATIONS MORE IMPORTANT THAN AGREEMENT
  - DO NOT DISRUPT HARMONY

JAPAN NEGOTIATING STYLE (cont'd)

- RINGI SYSTEM-(COLLECTIVE DECISION-MAKING)- A RINGISHO IS CIRCULATED; EVERYONE MUST PLACE HANKO (SEAL) INDICATING APPROVAL

- NEVER TAKE "YES" FOR AN ANSWER

- SILENCE IS "GOLDEN"; ELOQUENCE IS "SILVER"

SUMMARY

- BE THOROUGHLY-PREPARED, OBSERVANT AND PATIENT. DON'T TAKE A NOD OR A "HAI" AS A POSITIVE RESPONSE-IT MAY MERELY MEAN THAT HE HEARS YOU.

(SEE GRESSER ARTICLE IN JUNE, 1994 (les NOUVELLES).

LICENSING IN CHINA

"ONE COMPANY'S EXPERIENCE AND PROGNOSIS"

A. CHINA-WHY IT'S INTERESTING

B. BP AMERICA/STANDARD OIL-WHO WE ARE

C. STANDARD OIL'S CHINA EXPERIENCE

D. HOW TO LICENSE IN CHINA

E. CHINA'S NEGOTIATION STYLE

F. WHAT'S AHEAD FOR THE FUTURE?

A. CHINA-WHY IS IT SO INTERESTING?

1. POPULATION-1.1 BILLION
   - ONE PERSON OF 4.5 ON FACE OF EARTH IS CHINESE-EXPECTED TO REACH 1.5 BILLION BY 2000

A. CHINA-WHY IS IT SO INTERESTING? (cont'd)

2. GEOGRAPHY 3.8 MILLION SQUARE MILES
   - 5 REGIONS
   a. WESTERN CHINA-TIBET
   - 25% OF AREA, LESS THAN 1% OF POPULATION
   b. NORTHEAST CHINA

- MOST IMPORTANT INDUSTRIAL CENTERS
- JAPANESE OCCUPIED UNTIL 1933
- SHENYANG-COAL AND IRON ORE
- DAQING-OIL
- HYDROELECTRIC POWER

A. CHINA-WHY IS IT SO INTERESTING? (cont'd)

c. NORTH CHINA-GREAT WALL

- BEIJING, TANGSHAN, TIANJIN INDUSTRIAL CENTERS
- COAL, IRON ORE, POWER
- AGRICULTURE-SOUTH OF GREAT WALL

d. SOUTH CHINA

- YANGTZE AND WEST RIVER BASINS
- RICE, WHEAT
- HIGH POPULATION DENSITY
- WUHAN (STEEL), SHANGHAI (COMMERCE, PORT) AND CANTON (GUANGZHOU)

e. SOUTHWEST CHINA

A. CHINA-WHY IS IT SO INTERESTING? (cont'd)

- SICHUAN BASIN-FERTILE
  - COAL, IRON ORE
  - ISOLATED FROM EAST BECAUSE OF DIFFICULT TERRAIN

3. MINERALS

   a. ALL OF WORLD'S 140 "INDUSTRIALLY USEFUL" MINERALS ARE IN CHINA

   - 1/2 OF WORLD'S ANTIMONY
   - LARGEST TUNGSTEN RESERVES
   - COAL, TIN, MERCURY, OIL AND IRON ORE

A. CHINA-WHY IS IT SO INTERESTING? (cont'd)

- 17 MINERALS ARE WORLD'S LARGEST RESERVES

- PRECIOUS METALS-NICKEL, COPPER, COBALT, CHROMIUM, GOLD, SILVER AND PLATINUM

3. MINERALS

- BELT FROM NORTHWEST CHINA TO SOUTHWEST CHINA VERY RICH IN MINERALS

A. CHINA-WHY IS IT SO INTERESTING? (cont'd)

b. COAL

- NOW SUPPLIES 71% OF ENERGY
- 770 BILLION TONS (RECOVERABLE)-MOSTLY SOFT
- FOREIGN INVOLVEMENT-OCCIDENTAL, NIPPON STEEL, BECHTEL

A. CHINA-WHY IS IT SO INTERESTING? (cont'd)

c. OIL

- AS MUCH AS 144 BILLION TONS (MORE THAN 20 BILLION BBLS.) MAY BE PRESENT
- SOUTH CHINA NOW OPENED TO FOREIGN COMPANIES
- REAL OIL IS PROBABLY IN WEST
- OFFSHORE PARTICIPATION BY FOREIGN COMPANIES BEGAN IN 1982, WITH A SECOND ROUND IN 1984

B. CHINA'S POLITICS

1. CRITICISM (DEMYSTIFICATION) OF MAO IN 1981 AND REMOVAL OF HUA GUOFENG IN 1982

- CULTURAL REVOLUTION PUT TO BED
- DENG XIAOPING IN CONTROL

2. CULTURAL REVOLUTION WAS DISRUPTIVE OF POLITICS AND THE ECONOMY - IT ALSO LEFT DEEP SCARS ON THE PEOPLE

3. CHINA'S GOVERNMENT STRUCTURE TODAY

CHINA'S GOVERNMENT STRUCTURE
(SEE ORGANIZATION CHART)

A. CHINA'S GOVERNMENT STRUCTURE IS NEARLY AS COMPLEX AS CHINA ITSELF

1. ● 41 MINISTRIES AND 4 MINISTRY-LEVEL CORPORATIONS

   - FOUR ARE HEADED BY WOMEN

   ● MINISTRY OF FOREIGN ECONOMIC RELATIONS AND TRADE (MOFERT)

   - 20 DEPARTMENTS - CCPIT AND CNTIC ARE TYPICAL OF THE ORGANIZATIONS UNDER MOFERT

2. LOCAL GOVERNMENTS

   ● 22 PROVINCES
   ● 3 CITIES-BEIJING, SHANGHAI AND TIANJIN
   ● 5 REGIONS

STANDARD OIL'S CHINA EXPERIENCE

1. IN 1973, STANDARD OIL LICENSED ACRYLONITRILE TO CHINA

   OTHER LICENSES IN 1973 (THE FIRST YEAR OF U.S. LICENSES TO CHINA)

   UOP AROMATICS
   ARCO AROMATICS
   LUMMUS ETHYLENE
   AMOCO POLYPROPYLENE
   KELLOGG AMMONIA

2. EXPORT LICENSE IN 1972

3. CULTURAL REVOLUTION

4. USE OF INTERMEDIARY

   - ENGINEERING
   - SUBLICENSOR
   - FINANCING

STANDARD OIL'S CHINA EXPERIENCE (cont'd)

5. JAPANESE INTERMEDIARY COULD NOT NEGOTIATE FOUR CONTRACT PROVISIONS

- ROYALTY
  - PAID-UP OR RUNNING
  - LIMITED CAPACITY VERSUS UNLIMITED CAPACITY
  - CURRENCY
  - INTEREST
- CATALYST MANUFACTURE
- SECRECY TERM
- IMPROVEMENT EXCHANGE

STANDARD OIL'S CHINA EXPERIENCE (cont'd)

6. CHINESE NEGOTIATION STYLE IN 1973

   - KEEP BALL IN OUR COURT
   - YOUNG NEGOTIATORS
   - CNTIC CONDUCTED NEGOTIATION FOR END-USER

7. START-UP AND OPERATION VERY SUCCESSFUL

8. 1979/1980 DIRECT CONTACT-DEBOTTLENECKING AGREEMENT AND IMPROVEMENT EXCHANGE

1984 EXPERIENCE

- INFORMATION FROM "SOURCE" IN 1982
- CHINESE "DOMESTIC" TECHNOLOGY
- CONTACT WITH CHINESE AMBASSADOR
- 1983 INVITATION TO VISIT BEIJING
- STUDY TEAM VISITS TO CLEVELAND
- CHINESE INSISTENCE ON USE OF DOMESTIC ENGINEERING IF NO DOMESTIC TECHNOLOGY
- ROYALTY INTELLIGENCE - TIES (UNIDO)
- GUARANTEE LIABILITY
- PAYMENT TERMS
- LETTER OF INTENT

POST 1984 EXPERIENCE

- CHINESE HAVE HONORED ALL COMMITMENTS
- FOUR ADDITIONAL PLANTS LICENSED
- NEGOTIATIONS CONTROLLED BY END-USERS-NO MORE MIDDLEMEN
- IF U.S. COMPANY PROVES IT'S WILLING TO MAKE LONG TERM INVESTMENT IN CHINA, CHINA WILL PROVIDE INTEREST

POST 1984 EXPERIENCE (cont'd)

- NEXT STEP - INVESTMENT

  - IMPORT SUBSTITUTION
  - GATT
  - EXPORT REQUIREMENTS
  - FOREX

LESSONS LEARNED FROM PAST EXPERIENCE

- CHINESE ARE GAINING SOPHISTICATION

- SURFACE YOUR EXPECTATIONS EARLY

- DON'T MAKE THE MISTAKE OF BRINGING OUT YOUR BIG GUNS FIRST

- IF TOP EXECUTIVE INSISTS ON VISITING, LIMIT AGREEMENT AND DISCUSSIONS TO WHETHER OR NOT A RELATIONSHIP IS POSSIBLE

- WORK TO FOSTER A SPIRIT OF MUTUAL COMMITMENT

HOW TO LICENSE IN CHINA

- DEVELOP YOUR PROJECT AT HOME

  - PUT TEAM TOGETHER

  - INCLUDE RESPONSIBLE MANAGEMENT PERSON AS LEADER-ONE WITH CREDIBILITY

  - INCLUDE TECHNICAL SPECIALISTS WHO UNDERSTAND TECHNOLOGY COMPLETELY

- TAKE ALONG AN INTERPRETER - PREFERABLY A COMPANY EMPLOYEE WHO COULD SERVE AS A TEAM MEMBER EVEN WITHOUT HIS LANGUAGE ABILITIES

DO'S

- INVOLVE THE BEST PEOPLE YOU HAVE

- NEVER LEAVE JUST ONE INDIVIDUAL TO NEGOTIATE ALONE-CHINA ISOLATION

HOW TO LICENSE IN CHINA (cont'd)

- BE PREPARED TO SPEND AN EXTENDED PERIOD OF TIME-CONTINUITY IS CRITICAL

- HAVE AUTHORITY TO MAKE DECISIONS ON SITE

- DETAILED PREPARATION IS ESSENTIAL
  - IF YOU GO TO CHINA BECAUSE YOUR CEO WANTS TO SEE IT AND BRAG AT THE CLUB, YOU WILL BE LUCKY IF YOU DON'T REACH AGREEMENT

HOW TO LICENSE IN CHINA (cont'd)

- KNOW YOUR COSTS - CRUCIAL

- KNOW YOUR COMPETITION - STRENGTHS AND WEAKNESSES

- SET UP A COMMUNICATION LINK

  - ENCOURAGE YOUR INTERPRETER TO FORM PERSONAL RELATIONSHIPS
  - CONSIDER A BEIJING OFFICE
  - USE CONSULTANTS

BEFORE NEGOTIATIONS, BEGIN TO ASK QUESTIONS

- WHO ARE THE CHINESE NEGOTIATORS: NAMES, POSITIONS, COMPANIES OR BUREAUS

- REPORTING RELATIONSHIP

- APPROVAL PROCESS

- PROJECT PRIORITY-FIVE-YEAR PLAN CENTRAL OR PROVINCIAL GOVERNMENT

- IS FOREIGN EXCHANGE AVAILABLE OR WILL YOU BE ASKED TO ACCEPT COUNTERTRADE?

BEFORE NEGOTIATIONS, BEGIN TO ASK QUESTIONS (cont'd)

- PRODUCTION CAPACITY
- CUSTOMERS (DOMESTIC OR EXPORT)
- COMPETITORS IN CHINA
- RAW MATERIALS, ETC.

PROCESS FLOW OF TYPICAL NEGOTIATIONS

GENERALLY FIVE PHASES

1. INTRODUCTORY-SEMINARS

2. FUNDAMENTAL STRUCTURE OF PROJECT DISCUSSED-LETTER OF INTENT

3. FORMAL CONTRACT NEGOTIATIONS BEGIN WITH TECHNICAL NEGOTIATIONS-USUALLY, THE TECHNICAL APPENDIX INCLUDES:

   a. PRODUCTS OR TECHNOLOGY LICENSED-DETAILED DESCRIPTION

b. DESCRIPTION OF TECHNOLOGY TRANSFER PROCESS

c. LICENSE TERMS

d. DESCRIPTION OF TECHNICAL DOCUMENTATION WITH SPECIFIC DELIVERY DATES

e. TRAINING PROGRAMS - LIMIT NUMBER TO BE TRAINED AND SPECIFY TECHNICAL COMPETENCE AND LANGUAGE CAPABILITIES REQUIRED

f. TECHNICAL ASSISTANCE PROGRAMS WHICH ARE OFFERED DURING CONTRACT, IF ANY

g. WARRANTY OF OWNERSHIP TO TECHNOLOGY

h. PERSONNEL ISSUES: VISAS, MEDICAL CARE, HOUSING, TRAINING COSTS, TRAVEL, ETC.

4. COMMERCIAL TERMS NEGOTIATED:

- ALL NECESSARY LEGAL AND COMMERCIAL PROVISIONS - TABLE YOUR U.S.-STYLE CONTRACT FIRST

PROCESS FLOW OF TYPICAL NEGOTIATIONS (cont'd)

5. PRICE NEGOTIATIONS

- CHINESE WON'T MAKE COUNTERPROPOSALS UNTIL ALL OTHER ISSUES ARE RESOLVED

- SERIOUS PRICE NEGOTIATIONS ARE DELAYED UNTIL END

- MOST DIFFICULT AND NERVE-RACKING STAGE

PROCESS FLOW OF TYPICAL NEGOTIATIONS (cont'd)

- CHINESE WILL OFTEN CONDUCT THESE NEGOTIATIONS WITH YOU AND YOUR COMPETITION AT THE SAME TIME

PRICE

RECOMMENDATIONS:

- PRICE LICENSE HIGH ENOUGH TO ALLOW FOR SIGNIFICANT DISCOUNTS AT CRITICAL POINTS BUT DON'T BE UNREALISTIC, I.E., BE ABLE TO DEFEND OPENING PRICE

- KNOW WHAT YOUR BOTTOM PRICE OR FINAL OFFER IS GOING TO BE BEFORE YOU GO

PRICE (cont'd)

- ALSO, NEGOTIATE PAYMENT SCHEDULE FIRST SO THAT INTEREST FACTOR CAN BE CALCULATED AND BOTTOM PRICE CAN BE "GROSSED UP"

- ATTEMPT TO DETERMINE BUDGET PRICE - THIS CAN BE EXCEEDED BY 20% WITHOUT GOING BACK FOR FURTHER APPROVAL

SPECIAL CONSIDERATIONS

- GUARANTEES

  "WITHOUT MISTAKE AND WILL ENABLE LICENSEE TO MANUFACTURE A QUALIFIED PRODUCT" - PREFERRED BY CHINESE

- "SIMILAR TO DOCUMENTATION USED BY LICENSOR IN U.S. TO PRODUCE PRODUCT MEETING ALL SPECIFICATIONS"-PREFERRED BY ME

SPECIAL CONSIDERATIONS (cont'd)

- CHINESE WILL WANT EVERY ASPECT OF TRANSACTION TO BE GUARANTEED-THEY DO NOT WANT TO ACCEPT ANY RESPONSIBILITY

- LICENSOR SHOULD NOT OVERSELL; PITCH SHOULD BE REALISTIC WITH GUARANTEE LEVELS WELL WITHIN LIKELY PERFORMANCE

- ADOPT A SYSTEM OF CREDITS FOR EXCEEDING GUARANTEE LEVELS;

SPECIAL CONSIDERATIONS (cont'd)

- PLANT ACCEPTANCE TEST
  - PERFORM ONLY ONE
  - CLOSE TO ACTUAL START-UP AND REASONABLE DURATION
  - PLANT MAY NOT BE OPERATING AT OPTIMUM THUS LEVELS SHOULD BE REALISTIC
  - CLOSE WORKING RELATIONSHIP NECESSARY

SPECIAL CONSIDERATIONS (cont'd)

- TECHNICAL ASSISTANCE
  - CHINESE WILL ASK FOR MORE THAN NECESSARY
  - BE SURE TO INCLUDE TIME LIMITS, PAYMENT AMOUNTS AND SUBSISTENCE
- PENALTIES
  - DELIVERY DATES, ETC.
  - ONLY INCLUDE DATES THAT CAN BE MET
  - PROTECT YOURSELF AGAINST CHINESE DELAYS

SPECIAL CONSIDERATIONS (cont'd)

- PAYMENT PROVISIONS
  - IRREVOCABLE LUMP SUM (IF POSSIBLE) SINCE DELAYS CAN BE SEVERE
  - LETTER OF CREDIT
  - LUMP SUM VS. RUNNING ROYALTY (PROS AND CONS)

NEGOTIATIONS WITH THE CHINESE

- SUCCESSFUL BUSINESS DEPENDS ON PERSONAL RELATIONSHIPS

- CONFUCIAN TRADITIONS-RULE BY MAN NOT BY LAW
  - "LAW IS TOOL OF RULING CLASS TO SUPPRESS OPPOSITION AND TO CONTROL THE PEOPLE"

  - SINCERE COMMITMENT TO WORK TOGETHER IS MORE IMPORTANT THAN AN "AIR-TIGHT" WRITTEN CONTRACT

NEGOTIATIONS WITH THE CHINESE (cont'd)

- PERSONAL RELATIONSHIPS WILL SOLVE PROBLEMS-NOT CONTRACTUAL CLAUSES

- LIKE JAPANESE, SIGNING CONTRACT IS BEGINNING NOT END OF NEGOTIATION

- CHINESE WILL CONTINUALLY TEST FOREIGNER BY BRINGING UP SMALL MATTERS (TEST THE RELATIONSHIP)

NEGOTIATIONS WITH THE CHINESE (cont'd)

- THREE DISTINCT STAGES:

  1) SOUNDING OUT STAGE

  2) SUBSTANTIVE STAGE

  3) FINAL STAGE (SIGNING AND FOLLOW-ON NEGOTIATIONS)

- ALL ARE EQUALLY IMPORTANT

NEGOTIATIONS WITH CHINESE (cont'd)

- SOUNDING OUT STAGE (1ST)
  - ASSESS TRUSTWORTHINESS
  - FOCUS ON GENERAL PRINCIPLES AND COMMON GOALS (CONFRONTATION AVOIDED)
  - FUNDAMENTAL PRINCIPLES ESTABLISHED
  - DEVELOP AWARENESS OF DECISION MAKERS, PLACE OF LICENSEE IN HIERARCHY, INTERNAL CONFLICTS

NEGOTIATIONS WITH CHINESE (cont'd)

- ESTABLISH CORPORATE AND PERSONAL RELATIONSHIPS

- SOCIAL EVENTS INCLUDED IN THIS STAGE

- SUBSTANTIVE STAGE (2ND)

  - NO CLEAR ENDING OF 1ST AND BEGINNING OF 2ND

  - CHINESE CONTROL PACE

NEGOTIATIONS WITH CHINESE (cont'd)

- DISCUSSION OF SPECIFIC ISSUES MEANS 2ND STAGE HAS STARTED

- CHINESE WILL DELAY CONCESSIONS UNTIL END

- FINAL STAGE (3RD)
  - SIGNING, CELEBRATION AND BEGINNING OF SMALL NEGOTIATIONS
  - GUERRILLA WARFARE
  - FORMALITIES

NEGOTIATIONS WITH CHINESE (cont'd)

- YOU'RE ON THE STAGE
  - PAINFULLY SLOW-9-12 AND 2-5
  - GIFTS
  - RECESSES
  - ALWAYS PROBING FOR INFORMATION
  - STRESS FRIENDSHIP; EXPECT TRIBUTE
  - HOME COURT ADVANTAGE
  - TIME ON THEIR SIDE
  - XENOPHOBIA VS. XENOPHILIA
  - FACE AND GUANXI
- BE PATIENT

NEGOTIATIONS WITH CHINESE (cont'd)

- PRACTICE RESTRAINED STEADFASTNESS
- AVOID TRAP OF INDEBTEDNESS
- PREVENT EXAGGERATED EXPECTATIONS
- RESIST EFFORTS AT SHAMING
- TAKE GENERAL PRINCIPLES SERIOUSLY
- MASTER THE RECORD
- TAKE MEASURE TO LIMIT DAMAGES
- KNOW CHINESE CULTURAL DIFFERENCES BUT BE YOURSELF

DO'S FOR CHINESE NEGOTIATORS

1) CHOOSE RIGHT LEADER

2) MAINTAIN CONSISTENT TEAM

3) IDENTIFY REAL DECISION-MAKERS

4) STAY CALM-"RESTRAINED STEADFASTNESS"

5) LITIGATE ONLY AS A LAST RESORT

6) LEAVE THE DOOR OPEN-DON'T BURN BRIDGES

CHINA'S LEGAL FRAMEWORK

- NO LAW PRIOR TO 1979

- NOW, CONTRACT LAW, FOREIGN CONTRACT LAW, JOINT VENTURE LAW AND IMPLEMENTING REGULATIONS, REGULATIONS REGARDING REGISTRATION OF J.V.'S; FOREIGN EXCHANGE CONTROL, REGULATIONS ON PERMANENT REP. OFFICES, SEZ LAWS, BANKRUPTCY, IMPORT/EXPORT REGS., AND REGULATIONS ON TECHNOLOGY IMPORT CONTRACTS

CHINA'S LEGAL FRAMEWORK (cont'd)

- ALSO, PATENT COPYRIGHT AND TRADEMARK LAWS

- IN 12/93, NEW ANTI-UNFAIR COMPETITION LAW PROTECTING TRADE SECRETS PASSED

THE TECHNOLOGY IMPORT CONTRACT REGULATIONS

- THREE LAWS APPLY:

1) REGULATIONS FOR CONTROL OF TECHNOLOGY IMPORT CONTRACTS (MAY 24, 1985)

2) FOREIGN ECONOMIC CONTRACT LAW (MARCH 21, 1985)

3) PROCEDURES FOR EXAMINATION AND APPROVAL OF TECHNOLOGY IMPORT CONTRACTS (SEPT. 18, 1988)

THE TECHNOLOGY IMPORT CONTRACT REGULATIONS

(cont'd)

- TO GET FAVORED TREATMENT, TECHNOLOGY MUST BE DESCRIBED AS "ADVANCED TECHNOLOGY" (SEE LLBR PAPER)

- RESTRICTIVE CLAUSES LISTED

- REQUIRE LICENSOR TO GUARANTEE THAT TECHNOLOGY IS CAPABLE OF ACHIEVING OBJECTIVE STIPULATED IN CONTRACT

THE TECHNOLOGY IMPORT CONTRACT REGULATIONS

(cont'd)

- CONFIDENTIALITY-DISCRETION LEFT TO PARTIES-TERM ORDINARILY LIMITED TO 10 YEARS BUT LONGER TERM MAY BE SPECIALLY APPROVED

- FOREIGN ECONOMIC CONTRACT LAW PROVIDES POSITIVE ENVIRONMENT BUT ALL CONTRACTS WITH FOREIGN ENTITIES MUST BE APPROVED

THE TECHNOLOGY IMPORT CONTRACT REGULATIONS

(cont'd)

- F.E.C. LAW PROVIDES THAT, IF CHINESE LAW HAS NO PROVISION, GENERALLY ACCEPTED INTERNATIONAL PRINCIPLES APPLY

DISPUTE SETTLEMENTS

- CHINESE ABHOR LAWSUITS

- ARBITRATION POSSIBLE IF NEGOTIATION FAILS (PROVIDED FOR IN F.E.C. LAW)

- CHINESE WILL ACCEPT INTERNATIONAL ARBITRATION (DO NOT RECOMMEND SWEDISH ARBITRATION)

CONCLUSION

- TIME AND EFFORT WILL NOT BE WASTED
- CHINESE WILL REWARD GOOD RELATIONSHIPS
- MUTUAL BENEFIT NOT AN IDLE CONCEPT
- SHOULD LOOK AT EVERY REQUEST FROM BOTH SIDES
- REMEMBER THE WORDS OF NAPOLEON

CONCLUSION (cont'd)

- "CHINA? THERE LIES A SLEEPING GIANT. LET HIM SLEEP, FOR WHEN HE WAKES, HE WILL MOVE THE WORLD."

- CHINA IS NOW AWAKE AND IS MOVING THE WORLD

LICENSING LAW AND BUSINESS REPORT

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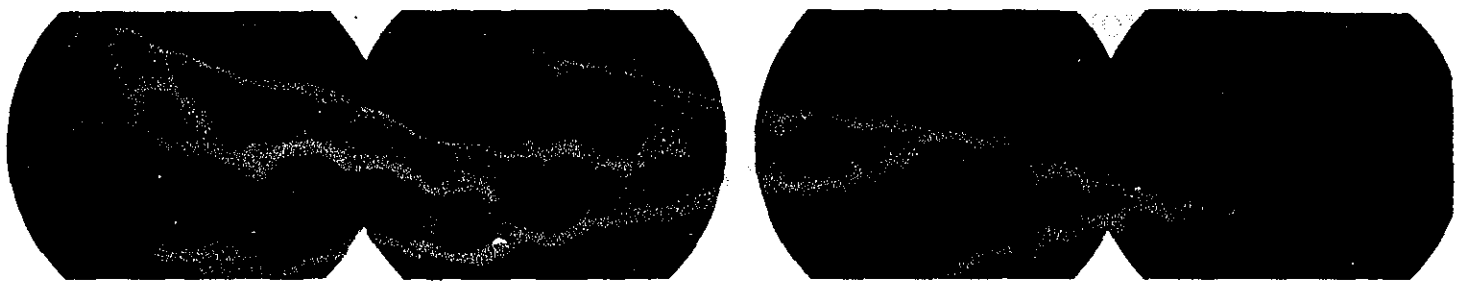

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LICENSING IN CHINA: A PERSPECTIVE OF A TWENTY YEAR VETERAN*

by Larry W. Evans**

- Background
- Why License in China
- Consideration of China's Politics
- Practical Aspects of Licensing in China
- Special Considerations in Negotiating With the Chinese
- China's Legal Framework

1. Introduction

This article discusses the issues that should be considered by parties involved in licensing technology to China. The article first examines China's economic and political structure. It then discusses the different stages in negotiating a license with the Chinese and particular licensing clauses that should be considered. The article further addresses the special considerations in negotiating with the Chinese along with specific negotiation tactics. Finally, the article examines China's legal framework with respect to technology transfers.

2. Background

Twenty-two years ago, even before Dr. Henry Kissinger traveled to China via Pakistan to make arrangements for President Richard Nixon's historic visit to China in late 1972, Standard Oil Company (SOHIO) was approached by one of its Japanese acrylonitrile licensees. The licensee was interested in sublicensing SOHIO's

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world-famous acrylonitrile technology to China as a critical part of a synthetic fiber complex to be built in the vicinity of Shanghai. At the time, the United States and China had been pursuing more than a decade of chilly relations following the Korean War. After considerable internal discussions, SOHIO decided to apply for an export license from the United States Department of Commerce. Because an export license had not been granted for China since the Korean War, the Commerce Department balked at granting the license. However, when the export license request was brought to the White House, President Nixon personally approved it since he had decided to open the door to China.

In early 1973, negotiations began between SOHIO's Japanese licensee and China National Technical Import Corporation (CNTIC) for a license to construct and operate a plant based on SOHIO's technology. SOHIO was invited at the final stages of the proceedings to negotiate several important provisions of the agreement including: term of secrecy, improvements exchange, capacity, and the currency in which the license fee would be paid. These negotiations were successful and the Chinese were willing to agree to secrecy and nonuse terms (except as expressly licensed) which limited their continued access to the technology for plants not licensed under the agreement.

Since these initial negotiations, there have been seven additional negotiations to license the technology in its current form to other plants in China. What is important to note from these negotiations is that the Chinese remember their old friends and reward success and positive relationships.

3. Why License in China

China offers the most potential growth for business transactions in the world. It is a large country of nearly 8 million square miles and within China's borders all of the world's 140 "industrially useful" minerals are found. China has a population of one billion two hundred million friendly, educable and industrious people and has recorded double-digit GNP growth for each of the past ten years. While the gross value of industrial output in China continues to grow at a 20 percent level, China's private enterprises are growing even faster. Inflation (while somewhat high at present) has largely been controlled. China has essentially an endless supply of coal and, until recently, it exported oil. However, in 1993, China was forced to import oil because of the slow progress in developing its northwest oil fields.

Although China has a socialist, centrally planned economy and its politics are not democratic, China truly has opened its doors to the outside world. Currently, there are three major economic trends in China: first, the increasing privatization of the economy as part of an overall shift from state planning to market mechanisms; second, the increasing integration of the Chinese economy into the world economy; and third, the opening of the Chinese market to a new consumer-led boom.

Chinese policy has always been formulated in simple slogans. When SOHIO's licensee began negotiating with the Chinese in 1973, the ruling slogan was "Adherence to Leninist/Mao Tse-Tung Thought," which meant that the medium of production and all trade were decided by the Party in Beijing as part of the state planning and/or political process. While the Chinese economy was devastated by the Great Leap Forward and the Great Proletariat Cultural Revolution, China's economic revolution began in 1979 with the Party Congress, which adopted Deng Xiao Ping's "open door" policy under the slogan of the "Four Modernizations." This policy led to the first foreign rush to China in the 1980s, when executives of most American corporations visited China and announced plans to penetrate the market of one billion consumers. The chairman of Nike referred to China as a market of 2 billion feet.

Today, the slogan is "Socialism with Chinese Characteristics." A Beijing economist has described this policy as follows: "We have finally decided to take the capitalist road; we just can't put up the road signs." But even without road signs, some of the characteristics of this new socialism are surprisingly like capitalism. For example, non-state-owned town and village enterprises have rapidly emerged as a growing industrial force in China. In fact, these non-state-owned enterprises account for almost a third of the country's industrial output and nearly half of the total industrial employment in China.

Under China's new socialism, the government encourages foreign investments and the importation of foreign technology and does not require foreign manufacturing firms to commit to a specified percentage of exports. As a result, by the end of 1991 China had approved more than 40,000 foreign investment contracts with a total value of over 52 billion dollars. In 1992, China began approving foreign investments in the service industries, and began granting licenses to accounting firms, law firms, insurance companies, and banks so that they could establish operations with China. Foreign exchange adjustment centers (swap centers) have also been provided to permit joint ventures that have difficulty obtaining foreign exchange to swap Chinese currency for foreign exchange.

Furthermore, the new socialism has encouraged the privitization of the efficient state sector companies. However, the inefficient state sector companies are still being subsidized by the government because nearly one-half of the total industrial work force is employed by these enterprises and there are no employment alternatives. Finally, another feature of socialism with Chinese characteristics is the rapid growth of stock markets in China. There are two major stock markets, one in Shanghai and

one in the Shenzhen Special Economic Zone which is immediately across the border from Hong Kong.

4. Consideration of China's Politics

If "socialism with Chinese characteristics" is appearing increasingly like capitalism in disguise, "politics with Chinese characteristics" do not even remotely resemble western democracy. One of the curious aftereffects of the Tiananmen Square incident, which caused most American companies to back away from China, was that investments from Taiwan (which had been negligible before June of 1989) and Korea increased dramatically. The reason for this significant increase was probably the perception of "political stability" in China; that is, the Chinese and Koreans consider stability through dictatorial control by the Communist Party as a positive not a negative.

The Chinese desire for order over chaos indicates that the Chinese, whether the old guard or the younger emerging technocrats, do not plan to liberalize the political structure in China any time soon. Of late, China has begun to select its leadership based on personal merit, i.e., education, experience and capability, rather than whether or not they participated in the Long March which took place more than forty years ago. The Chinese leadership, i.e., Deng Xiao Ping, realizes that in order for China to achieve its modernization goals, individuals such as Executive Vice Premier Zhu Rongji must be promoted to leadership positions. Mr. Zhu has a degree in electrical engineering and has spent most of his career in an economic planning role. He was Vice Minister of the State Economic Commission in 1983, and in 1988 he became Major of Shanghai. In 1991, he was named Director of the State Council Production Office which was later elevated to the level of State Council Commission. Mr. Zhu is primarily responsible for overseeing China's economic reform program and is an immensely capable individual. (For an interesting account of politics in China, *see* H. Lyman Miller, "Holding the Deng Line," China Bus. Rev., Jan.–Feb. 1993, at 22).

5. Practical Aspects of Licensing in China

In attempting to license technology to China, the licensor is faced with many challenges. China is a long way from the United States (more than twelve time zones) and communicating with the United States is inconvenient even though telephone and fax service is quite acceptable in China. In addition, China's laws are very complicated and the negotiating style in China is similar to Chairman Mao's concept of "guerrilla warfare," which is discussed below.

First, the licensor must develop the project at its own office. Because many negotiations have failed when only one negotiator was sent to China, a team should be put together to complete the licensing transaction. The team must involve the very best people in the company and include a responsible management person as the leader. This person must have credibility within the corporation and must be able to establish credibility with the Chinese. The leader must also be able to make snap decisions in China even in areas that have not been discussed with company management. Furthermore, the leader of the team should have a good general understanding of the technology.

Although the Chinese will supply interpreters for the negotiations, the team should also include an individual with Chinese language skills who understands the technology and the business. This individual should not be identified only as an interpreter, but rather as a member of the negotiating team. This individual should form personal relationships with members of the China team and act as an informal communication link between the two leaders. Furthermore, the team should also include a technical specialist who has a complete understanding of the technology. The Chinese will know about the technology, and it would prove embarrassing if the licensing team did not have a true expert.

The team that is sent to China must be completely prepared for the negotiations. The negotiating team must know: (1) all costs involved in implementing the license; (2) its competition; and (3) the company's strengths and weaknesses. The negotiating team should also be prepared to spend an extended period of time in China in order to maintain continuity in the negotiations; the Chi-

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nese will extend the effort and the licensing team should as well.

If a company might be involved in many projects in China, a Beijing office is highly desirable. Additionally, the licensor should not hesitate to use consultants because presence of any experienced "China hand" on the otiating team is invaluable.

Before beginning licensing negotiations in China, it is important to ask several questions. Among the questions are: Who are the negotiators on the Chinese side? What are their names, positions, and companies or organizations? What is the reporting relationship? Are they part of the provincial government or the central government? Is the project a government-approved project? Is the project part of the central government's five-year plan or that of the provincial government? Is foreign exchange available or will you be asked to accept counter-trade? Does the project have to be a export-oriented project or can it be based on domestic sales? Who are the customers and will the project have any competitors in China? What will be the size of the plant? Are raw materials and other facilities available? Obtaining the answers to these preliminary questions will make the rest of the negotiations proceed much more smoothly. The Chinese do not want to be surprised and neither should the negotiation team.

Generally, there are five phases in a typical negotiation in China. First are the introductory seminars. The Chinese want to learn about the technology and form an opinion bout the individuals on the negotiating team and their npany. Second, the fundamental structure of the pro- is discussed and usually a letter of intent is signed. The third phase consists of formal contract negotiations. In this phase, the Chinese usually begin with technical negotiations, including:

(1) A technical appendix which describes in detail the products or technology licensed;
(2) A description of the technology transfer process;
(3) The terms of the license;
(4) A description of technical documentation with specific delivery dates;
(5) Training programs, if any, which typically limit the number to be trained and specify technical competence and language capabilities;
(6) Any technical assistance programs that are offered during the contract;
(7) Warranties of ownership of the technology; and
(8) Personnel issues, such as visas, medical care, housing, training cost, travel, and other related issues.

The fourth phase deals with the commercial terms, including all necessary legal and commercial provisions. sually in this stage the licensor is presented a form ement. It is not only unnecessary but also dangerous the licensor to agree to the form agreement. The licensor should not depart from its policies regarding the technology. If the technology has been licensed elsewhere (which is almost always the case), it is unfair to the licensor and its other licensees to agree to China's form agreement instead of the licensor's "standard" agreement. Chinese organizations will understand the licensor's position and adapt to the licensor's agreement so long as it generally complies with the Chinese laws, which are covered in Section 7 of this article.

The final stage of the negotiations concerns price. Price negotiation is the most difficult stage of the entire process. Generally, the Chinese will not make any counterproposals on price until all other issues are resolved. Serious price negotiations are intentionally delayed until the end of the negotiations.

Since the Chinese negotiators simultaneously conduct price negotiations with the licensor's company and its competition, the initial license fee should be priced high enough to allow for significant discounts at critical points, but the fee should not be unrealistic. That is, it is essential that the opening price be defendable; i.e., a discounted cash flow analysis should show that the licensee will make money even if the licensee pays a license fee at the initial asking price. The negotiating team should have an understanding of its final offer before beginning negotiations. This offer should be at least as high as other licenses in other countries. While license fees should be based on benefit rather than cost, implementing a license in China is more time consuming and costly than licensing in many other parts of the world.

During the final stage, the payment schedule should be negotiated first. The time value of money (and the interest) should be included in the "bottom" price. That is, the price should be expressed as dollars at the time the agreement is executed. When the State Planning Commission (SPC) was responsible for approving all license agreements, it was important early on to determine, if possible, the "budget price" that had been approved by the SPC because this price could only be exceeded by 20 percent without going back for additional approval. Therefore, if the license has to be approved by the SPC, the Chinese should be given an idea of the license fee at a very early stage, ideally before they go to the central government for approval.

With respect to contract guarantee provisions, the Chinese normally require that the technical information supplied by the licensor will be "without mistake and will enable the licensee to manufacture a qualified product simply by using the document." This guarantee should not be made because the licensor ordinarily is not able to control the construction of the plant or the raw materials used in the plant. Rather, the licensor should indicate in the agreement that the technical documentation is "similar" to the documentation used by the licensor in the United States where the licensor produces a product

meeting all the specifications in the license agreement. The licensor, however, should not use this requirement as an excuse to minimize control in other aspects of the agreement.

The area of contract guarantees raises other concerns. Many of the Chinese officials whose positions are "on the line" will do their utmost to insure that every aspect of the license transaction is guaranteed by the licensor. That is, they do not want to accept any responsibility for the success or failure of the plant. If the licensor "oversells" its technology, it will have a very difficult time fulfilling the guarantees in excess of its typical guarantees in other license agreements. Therefore, the licensor's sales pitch should be realistic and the guarantee levels in the agreement should be well within the likely performance of the technology on matters of capacity, output, product quality, etc.

One technique that may be used to satisfy the guarantees is to provide for credit when guarantees are exceeded in certain areas. This credit can then be used against the failure to achieve guarantees in other areas. For example, with respect to the quality of a petrochemical product, there are usually ten to fifteen items that are specified. If the licensor exceeds the guarantee level in ten of the items but does not reach the guarantee level in the other five, credits for exceeding the guarantees could more than balance out the liabilities for not achieving guarantee levels in the remaining areas.

One other matter that deserves particular attention with respect to guarantees is the plant acceptance test or product acceptance test. Depending upon the kind of technology being licensed, only one acceptance test should be performed. This test should occur reasonably close to the actual start-up of the plant. For example, with respect to petrochemical plants, it can be specified that a forty-eight-hour test be performed in which the raw materials consumed, capacity, and product quality all meet the necessary guarantees. If this test is performed too soon after the introduction of feeds into the plant, there is a possibility that the licensee may operate the plant in a manner which will affect the guarantee test run. Therefore, it is important to negotiate guarantees that are realistic and incorporate safety factors, since the plant in its earliest operating stages may not operate at its optimum level. During this start-up period, the licensor and licensee should try to develop a good working relationship so that each has trust and confidence in the other. Furthermore, the licensor must assure the licensee's personnel who visit the licensor's facility that, if the plant is operated well, its performance will continue to improve over the life of the license.

In regard to technical assistance (that is, assistance by foreign engineers and operators in China and training of Chinese engineers and operators in the United States), the Chinese will usually ask for more assistance than the licensor believes is necessary. Thus, the licensor should limit the amount of time that must be spent by personnel in China and the amount of time (expressed in "person-days") that the Chinese trainees will spend at the licensor's facilities. The agreement should also specify which party will be paying for this assistance, along with the other costs such as travel and living expenses. Likewise, the agreement should specify the living accommodations and transportation for the foreign engineers while they are in China.

During these negotiations, the Chinese will certainly require specific delivery dates for technical documentation, equipment (if equipment is to be supplied by the licensor), and other items connected with the license. Usually, the Chinese will insist upon penalties for the failure to meet the delivery dates. If delivery dates and penalties are specified, the Chinese will have no choice but to enforce the provisions. Therefore, the license should be drafted so that the penalties apply only to the items to be delivered and not to the overall agreement.

In addition, the licensor should make sure that the contract protects it against delays by the Chinese. For example, if a petrochemical plant is not started up for three or four years after delivery of the catalyst, the agreement must provide for retesting the catalyst prior to the start-up of the plant in order to make sure that it is still in acceptable form. Therefore, the licensing team should advise their company to expect and plan for delays on the Chinese side.

With respect to payment provisions, if the license fee is a lump sum rather than a running royalty (as is most usually the case in China), the agreement should specify that the entire lump sum is an irrevocable payment and is not tied to the start-up of the plant. Although this provision may be very difficult to negotiate, it is a desirable goal because the start-up of the plant may be delayed interminably through no fault of the licensor. As a result, the licensor will be denied the time value of the license fee.

Depending upon the status of the licensee within the Chinese system, the licensor may try to insist upon a letter of credit issued by a United States bank with payment made against the tender of noncontrovertible documentation. Alternatively, the licensor may require a letter of credit issued by the Bank of China. There are no hard and fast rules for whether or not the licensor should insist upon a letter of credit, but the licensor should take this matter into consideration before executing a license with the Chinese.

Although the Chinese may agree to running royalties, the choice of a lump sum versus a running royalty is a complex one. Most Chinese negotiators prefer a lump sum payment because: (1) it can be included in the project financing which may be available from a foreign government bank such as the Japan Ex-Im Bank or the World

Bank; and (2) they do not want to have their production and sales records audited, which would be necessary if the agreement specified a running royalty. Likewise, the licensor may prefer a lump sum payment for the following reasons: (1) the money is usually guaranteed; (2) hard currency is available immediately; and (3) tax consequences, i.e., running royalties will almost certainly be regarded as ordinary income.

On the other hand, there are disadvantages to lump sum agreements. First, they tend to provide unlimited capacity to the licensee unless there are specific provisions in the agreement which provide for additional payments if the licensed capacity is exceeded. Furthermore, the technology transfer regulations (discussed below) limit the term during which running royalties can be collected. These regulations set the term at ten years; however, the Chinese will usually negotiate for a much shorter term.

When license payments are being negotiated, the Chinese will often suggest the possibility of paying for the technology with something other than cash. Usually, Chinese negotiators begin with discussions of payments based on a cash price. However, very late in the negotiations, the Chinese will require that the compensation be based on counter-trade. Licensors should remember that counter-trade is most often handled by third parties who demand a commission. Therefore, the commission must be considered in determining whether or not the counter-trade payment exceeds the bottom line price.

Other areas that deserve consideration are *force majeure* and arbitration (or dispute resolution). In 1973, it was very difficult to negotiate a *force majeure* because this term literally means "act of God" and China was, by definition, an atheistic country. Today, all Chinese negotiators will probably agree to a *force majeure* clause. The essential elements to cover in this clause are acts of God, natural disasters, imposition of government controls over import and/or export, riots, war, power interruptions, strikes, and all other clauses beyond the reasonable control of the licensor.

With respect to arbitration, China's "Foreign Economic Contract Law" provides that disputes can be submitted to "Chinese or other arbitration bodies." In practice, the Chinese have agreed to arbitration in Sweden under the rules of the Arbitration Institute of the Stockholm Chamber of Commerce. Because of China's general preference for Stockholm, a very large percentage of arbitration in Sweden is based upon disputes with respect to China. Although this is probably an acceptable arbitration forum, it seems likely that Swedish arbitrators will tend to favor the Chinese in order to continue to be named as arbitrators in the future. Therefore, licensors should insist upon arbitration before other international arbitration bodies or even the American Arbitration Association. Furthermore, with respect to American licensors, arbitration in China may be preferable to arbitration in Sweden because the United States government has influence on the government of China which can be used to support fairness in the arbitration process. Consequently, the arbitration clause must carefully provide for all of the various aspects of arbitration, such as the number of arbitrators, appointing authority, place of arbitration, language of arbitration, governing law, and the qualifications of the arbitrator(s). The arbitration clause should also provide a basis under which the arbitrators will operate.

Even though recent changes have brought Chinese law largely in line with the industrialized world, the confidentiality provisions in the agreement should be drafted carefully. Until recently, trade secret protection in China was only contractual, i.e., there was no "trade secret law" and trade secrets were not regarded as protectible property. Today, China's Tech Transfer Regulations provide for confidentiality terms of no longer than ten years "without special approval of the examination and approval authority." As a practical matter, the status of the licensee and the advanced nature of the licensor's technology will often permit a term longer than ten years. However, the licensor should be prepared for a very difficult negotiation of this point.

Another area that must be considered is whether or not the licensee will be permitted to export the product. Although this is a difficult point to negotiate, i.e., the Chinese are reluctant to forgo the right to export, it must be kept in mind at least as a bargaining chip.

An additional point is that a U.S. export license is required from the Commerce Department in order to disclose the technology to the licensee. The Chinese side will often require evidence of this export license as a precondition to the argument's effectiveness. For additional treatment of this topic, *see* Wang Zhengfa, "Issues Affecting Licensing Technology," Les Nouvelles, Mar. 1989, at 1; Chi Shaojie, "PRC View of Technology Transfer," Les Nouvelles, Sept. 1986, at 124.

6. Special Considerations in Negotiating With the Chinese

In the twenty-five short years since China has opened its doors to the West, tremendous strides have been made. The Chinese have progressed from being cautious and relatively inefficient negotiators to respected business partners. Their negotiation style is characterized as having similarities with Chairman Mao's sixteen-character poetic description of Guerrilla Warfare:

> Enemy advances,
> we retreat.
> Enemy halts,
> we harass.
> Enemy tires,
> we strike.

Enemy retreats,
we pursue.

Negotiation with the Chinese today retains some of these characteristics, but great strides have been made toward more efficient negotiation. However, many negotiators still leave the table feeling pessimistic about their future partners. One veteran China observer has described China's negotiating style as "a blend of the Byzantine and the Evangelical."

Chinese negotiators often frustrate western business people not accustomed to Chinese tactics. In negotiating with the Chinese, foreign business people must realize that successful business dealings in China depend upon personal relationships. China's Confucian traditions have established a society which is ruled by man rather than by a strict legal system. Chinese are taught that the law is a tool used by the ruling class to suppress opposing classes and to control the people. As a result, the Chinese are still less trustful of laws than of personal contacts.

Chinese negotiators believe it is important to achieve a sincere commitment to work together rather than an air-tight legal package. They also believe that business dealings will inevitably involve some troubles which might be impossible to predict and very difficult to solve. As a result, the Chinese try to devise solutions only for problems that are anticipated and to rely on personal relationships to solve all of the other problems. Moreover, any foreign company that licenses technology in China automatically establishes the company as a "friend." In China, a "friend" has a responsibility to assist the Chinese partner in times of difficulty.

To the Chinese, nothing is ever "cast in stone." A signed contract merely marks the end of the initial stage of negotiations which will be followed by more discussions and thus, more compromises and concessions. In fact, the Chinese often push relentlessly for further concessions after an agreement has been concluded. This uniquely Chinese view means that negotiations are an endless process and that a signed contract does not indicate that the deal has been completed. Foreigners are often caught unprepared by frequent Chinese requests to continue negotiations that have supposedly been concluded. This does not imply that the Chinese will not keep their word. On the contrary, the Chinese can be expected to uphold the bargain and will not try to cancel or refuse to honor the contract without a good reason. However, a foreigner can be assured that the Chinese will continually bring up small matters. By continuing the negotiations in this way, the Chinese are testing whether their foreign counterparts are truly committed to the "relationship" as opposed to the contract.

After becoming familiar with the Chinese culture, one often discovers that there is a close link between the negotiating tactics of the Chinese and their traditional values. Indeed, Chinese negotiating tactics can only be understood after realizing the various strategies which have historically been used by Chinese negotiators to lead the other side into doing business the Chinese way.

The Chinese style of negotiating involves at least three distinct stages: a sounding out stage, a substantive stage in which hard bargaining begins, and a final stage which theoretically concludes with the signing of the contract. During the first stage, the Chinese assess the trustworthiness of the foreign partner. The Chinese will focus on general principles and common goals before moving on to possibly contentious issues. (This could be culturally based since the Chinese try to avoid or postpone confrontation). Foreigners should not consider this stage as only a formality. Rather, it is a time in which fundamental issues are discussed. The Chinese will always remind their foreign partners about these fundamental principles during the hard bargaining phase, and it is helpful if the foreigners also remember the fundamental principles which tend to favor their side during the difficult stages of the negotiations.

During this initial stage of negotiation, the foreign partner should obtain as much information as possible about the Chinese partner and its place within the Chinese hierarchy. The foreigner should also be aware of the possibility of internal conflicts among the parent organizations to whom the Chinese report. It is also important that both corporate and personal relationships be established.

Throughout the course of the negotiations, foreigners should expect that bargaining will extend beyond the negotiating room. Social activities are used not only to cultivate business relationships but also to deliver messages, i.e., use of banquets with higher-ranking officials on the Chinese side to deliver both positive and negative messages. An example of a positive message is praise for the Chinese negotiators while an example of a negative message is asking the potential licensee to do the impossible by violating a strong company policy.

There is no clear ending of the first negotiation stage and beginning of the second, more substantive stage. Usually, the licensor has no choice but to allow the Chinese to control the pace of the negotiation. When the Chinese negotiator begins to discuss very specific issues, the second stage has begun. During the second stage, there will probably be numerous disputes over the language of the contract clauses. However, there may be an agreement on issues that seemed unsolvable earlier. While foreigners are more accustomed to solving issues one by one as they arise, the Chinese prefer to make concessions at the end of a negotiation.

Foreigners should be aware of typical Chinese negotiating tactics before attempting a negotiation in China. The following Chinese negotiating strategies are often used:

(1) The Chinese will control the location and schedule of the negotiations. This is done not just to minimize expenses, but also to keep the upper hand. Chinese negotiators sometimes simply try to wait the foreign party out in order to test whether their position is firm.

(2) The Chinese will utilize weaknesses observed in the other side's position. This strategy can also extend to the personality of the foreign negotiator. For example, if the negotiator is susceptible to flattery, the Chinese may lavish the negotiator with praise.

(3) The Chinese are known for using shame tactics, such as reminding the Japanese of their country's atrocities in China during the 1930s and 1940s. Furthermore, if a foreigner makes an unfriendly remark or violates any of the fundamental principles established during the initial negotiation stage, the Chinese will seek to embarrass the foreigner into carrying out the negotiations their way.

(4) The Chinese will pit competitors against each other. It is a favorite Chinese tactic to set competitors against one another in order to start a bidding war. Although the competitors mentioned by the Chinese may be imaginary, they are often real. Therefore, foreign negotiators must understand the competition and its advantages and disadvantages.

(5) The Chinese will often feign anger. Even though public expressions of anger are considered bad manners in China, it is not uncommon for Chinese negotiators to suddenly fly into a rage, pack up their papers, and leave the room. These incidents are usually staged to gain concessions. For example, the writer has experienced the "good cop—bad cop" routine after such an incident during negotiations in the past.

(6) The Chinese are known for "rehashing" old issues. This strategy is used to gain additional concessions and may occur at any time—even after the negotiations are officially over. Therefore, foreign negotiators should keep good notes and sign a protocol reviewing the areas of agreement after each negotiation stage.

(7) The Chinese will often try to control expectations. After several months or years of negotiation, the Chinese will often express a strong sense of urgency in order to gain concessions. They will also attempt to renegotiate previously negotiated issues by taking advantage of the foreigner's desire to end the negotiation quickly and return home, e.g., for a holiday.

In light of these tactics, negotiations with the Chinese will be much more effective if the following guidelines are adhered to:

(1) *Choose the right leader.* Make sure the leader has status and credibility.

(2) *Maintain a consistent team.* Continuity is a key to a successful negotiation. The Chinese will exploit discontinuity by misrepresenting previous understandings. Therefore, a member of the foreign team should have the ability to ensure that both sides understand the issues being agreed upon. This individual can further act as a cultural bridge in order to overcome misunderstandings and to promote harmony in the negotiating process.

(3) *Identify the real decision makers.* Foreign negotiators should determine who is actually making the decision on the Chinese side. The real authority may often take a low profile during the negotiating process.

(4) *Stay calm.* Foreign negotiators should refrain from making gestures of frustration or using abusive language. These are signs of defeat and weakness to the Chinese. Confucian traditions run deep in China. Social or business interactions should be conducted in such a way that nobody ends up backed into a corner and thereby forced to "lose face." Foreign negotiators should practice "restrained steadfastness."

(5) *Use litigation only as a last resort.* Although litigation is often used as the first resort in some countries, a foreign licensor should only use litigation in China if it has no other choice or concern about ending the relationship. The Chinese believe that the settlement of a dispute in the courts or through arbitration is a failure of the relationship.

(6) *Leave the door open.* If there is a break in negotiations, both sides should proceed carefully in order to smooth the process. Foreign negotiators should avoid casting blame upon Chinese counterparts or describing the negotiations as a failure. Furthermore, foreign negotiators should try to keep bad news from becoming public knowledge unless a deliberate leakage of information is calculated to take advantage of public pressure and help save the negotiations.

Many of the foregoing tactics and observations are applicable generally to all negotiations and not just those with the Chinese. Foreign negotiators should remember that the Chinese begin learning their negotiating style from the time they are able to communicate and thus are generally more adept at negotiation than foreigners. Professor Lucian Pye, a noted China scholar from Harvard University, indicates that foreign negotiators in China should be patient, accept prolonged periods of no movement as normal, avoid exaggerated expectations, discount Chinese rhetoric about future prospects, resist the temptation to blame themselves for difficulties, and try to understand Chinese cultural traits. However, Professor Pye cautions that "foreigners should never believe they can practice Chinese tactics better than the Chinese." As Sun Tzu, China's most admired military strategist, said, "know yourself, know your enemies; 100 battles, 100 victories." For more information about China's unique negotiating style, *see* Min Chen, "Tricks of the China Trade," China Bus. Rev., Mar.–Apr. 1993, at 12.

7. China's Legal Framework

Although China essentially had no legal system as of late 1979, it has recently created and enacted many new

laws. Among the new laws adopted in the decade of the eighties are: Contract Law, Foreign Contract Law, Joint Venture Law and Implementing Regulations, Joint Venture Tax Law and Implementing Regulations, Regulations regarding the Registration of Joint Ventures, Foreign Exchange Control Regulations, Regulations Governing Permanent Representative Offices in the PRC, Regulations on Doing Business in the Special Economic Zones, Bankruptcy Law, Import/Export Regulations, Patent Law, Trademark Law, Regulations Governing Arbitration, Insurance Regulations, Advertising Regulations, and two sets of regulations on the Administration of Technology Import Contracts. In the nineties, Chinese patent law was amended to protect chemical and pharmaceutical compounds as well as other subject matter. In addition, the Chinese enacted a Trade Secret Law which provides that trade secrets are protectible property.

With respect to technology transfers, there are three basic laws that apply: (1) the Regulations for the Control of Technology Import Contracts, promulgated on May 24, 1985; (2) the Foreign Economic Contract Law, adopted on March 21, 1985; and (3) the Procedures For Examination and Approval of Technology Import Contracts, issued on September 18, 1985. These Transfer Regulations apply to the transfer of patents and technology, technical services, and technology contracts involving joint ventures. Although each of the laws emphasize different aspects of the technology transfer process, they overlap in certain areas.

In order to enjoy favored treatment under these Transfer Regulations, the technology being licensed must be described as "advanced technology." The definition of this term was clarified by the Rules for Examining Export and Advanced Enterprises with Foreign Investment, which were issued on January 27, 1987. To qualify as "advanced" under these rules, the technology should: (1) lead to the development of new products; (2) expand exports; (3) substitute imports; or (4) provide products that are in short supply on the domestic market. Therefore, the licensor should convince the Chinese party that the technology is "advanced" and suitable for the practical Chinese situation.

Furthermore, these Transfer Regulations contain a list of prohibited or restrictive clauses. For example, the licensor cannot require the licensee to accept "tie-in" conditions which are unrelated to the technology to be imported, including the purchase of unnecessary technology, technical services, raw materials, equipment, or products. The licensor also cannot: (1) restrict the licensee from acquiring, from other sources, similar competing technology; (2) unreasonably restrict the licensee's sales channels or export markets; or (3) require remuneration for unusable or invalid patents. The regulations further state that "the supplier may not compel the recipient to accept an unreasonable requirement of a restrictive nature."

Although many of the foregoing restrictions are similar to the provisions in western antitrust laws, some prohibited restrictions may cause difficulty. For example, if the licensor is required to guarantee the performance of the technology, the licensor may feel quite reluctant to allow the licensee to purchase materials, parts and equipment from third parties that might not meet the technical requirements to implement the technology. In the case of a catalytic chemical process, the licensee should be required to purchase (at least for the initial operation) a catalyst from an approved source. If a prohibited restriction is present in the contract, the contract is subject to special approval.

The Transfer Regulations specify the procedures to obtain approval. These procedures deal with the following four aspects of the approval process: (1) the identities of the examination approval authorities; (2) the application process; (3) the factors considered in examining and approving a contract; and (4) the effect of approval or disapproval. The recent regulation, Detailed Rules For Implementing Technology Transfer Contracts by the Ministry of Foreign Economic Relations and Trade (MOFERT), published on January 20, 1988, also provides details for obtaining approval of technology transfer contracts. The Detailed Rules For Implementing Technology Transfer Contracts give MOFERT the primary authority over all technology import contracts, and only MOFERT has the right to print and number the "Technology Import Contract Approval Certificates." Depending upon the size of the contract, MOFERT may authorize other responsible ministries or administrations to examine and approve the contract. These approval procedures provide that the application must be submitted within thirty days after execution and the examining authority shall decide whether or not to approve the contract within sixty days after receiving the application. If no decision has been made after sixty days, the contract will be deemed automatically effective. In addition, these procedures provide that the licensor must defend any infringement lawsuits and must indemnify the license against any costs or damages from such infringement.

The Transfer Regulations also require the licensor to guarantee that the technology is capable of achieving the objectives stipulated in the contract. The statutory liability is provided as a penalty for licensors whose technology fails to achieve the stipulated objectives. As a result, the licensor should be careful in making any guarantee that it is the lawful owner of the technology and that the technology provided is complete (without error), effective, and able to obtain the objectives provided in the contract. Therefore, the technology transfer contract must be carefully drafted to insure that the scope of the guar-

antee is limited and clearly defined in order to avoid statutory liability.

With respect to confidentiality, considerable discretion is left to the contracting parties. The Transfer Regulations require the Chinese licensees to keep confidential any part of the technology that is secret and has not been made public in accordance with the terms agreed upon by the parties. Therefore, the licensor may include the scope and period of confidentiality with the licensee in the contract. Although the regulations ordinarily limit the term of secrecy to ten years, this term can be extended with special approval.

China's Foreign Economic Contract Law is the Chinese version of western contract law. There are provisions on contract formation, contract breach, the scope of contractual liability, and similar issues. This law governs all contractual relations between foreign businesses and Chinese enterprises. It generally creates a positive environment in which the Chinese and foreign parties can negotiate contracts freely. However, a Chinese entity is not allowed to enter into a contract with a foreign party without permission from the Chinese government. This reflects the obvious conflict between free market practice and the state owned socialist economy.

The Foreign Economic Contract Law also acknowledges that if Chinese law does not have provisions on particular points, the generally accepted international principles apply. It further provides that international or bilateral treaties with China prevail over Chinese domestic law. Clearly, with this law, the Chinese are trying to fulfill their international agreement and treaty obligations.

With respect to dispute settlements, the Chinese prefer negotiation and consider lawsuits abhorrent. However, if negotiation fails, they will agree to arbitration. The Foreign Economic Contract Law provides an institutional infrastructure to facilitate dispute resolution. Article 37 of the Law specifies that "disputes arising over a contract should be settled, if possible, through consultation or mediation by a third party" and "in case the parties concerned are not willing to, or fail to, go through consultation or mediation, they may submit to China's arbitration agency or other arbitration agencies in accordance with the arbitration agreement reached afterwards." Article 8 of the Agreement on Trade Relations between the United States and the People's Republic of China states that the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL) may be used. Although the Chinese contend that both Chinese enterprises and foreign contracting parties have equal rights under Chinese law, foreign technology owners should insist upon international arbitration and rules, especially in the case of the term arrangements that carry the possibility of a change in the initial parties. In any event, arbitration in Sweden under the rules of the Stockholm Chamber of Commerce is not recommended. Instead, the ICC or the American Arbitration Association should be used.

While Chinese laws are very detailed and complex, their overall effect is similar to that which is found in many other countries in the world. American-styled license agreements will usually be acceptable to the Chinese provided that the specific restrictions in the Technology Transfer Regulations satisfy a Chinese "rule of reason" analysis. Further, if a licensor desires a longer term than ten years, the licensor should provide the basis for this longer term and enlist the licensee in a joint effort to convince the approval authorities that the basis is sound. For further information concerning China's legal framework regarding licensing, *see* Ellen R. Eliasoph & Jerome A. Cohen, "China's New Technology Import Regs," Les Nouvelles, Mar. 1985, at 16; Meimei Fu & Frank D. Shearin, "Technology Transfer in the PRC," Les Nouvelles, Mar. 1988, at 32.

8. Conclusion

While considerable effort is required to establish a relationship with the Chinese and to negotiate a viable licensing arrangement, the time and effort are not wasted. The Chinese will remember and reward good relationships and successful licensing arrangements. The concept of "mutual benefit" which is so often expressed by the Chinese is not an idle concept. One should always look at a licensing situation with the Chinese from both sides. If a negotiator asks for a concession, the negotiator should ask himself how he would react if a similar concession were requested by the other side. Confucius must have said something about putting oneself in the other person's shoes, but if he didn't, he should have.

CASE COMMENTS

U.S. Supreme Court Rejects "Dual Standard" for Awarding Attorney Fees in Copyright Infringement Cases

In *Fogerty v. Fantasy, Inc.*, No. 92-1750, 1994 U.S. LEXIS 2042 (March 1, 1994), the United States Supreme Court rejected the "dual standard" employed by the Ninth Circuit for awarding attorney fees pursuant to 17 U.S.C. § 505, holding that in awarding attorney fees to the prevailing party in a copyright infringement suit, prevailing plaintiffs and prevailing defendants are to be treated alike.

Under Section 505, "the court may . . . award a reasonable attorney's fee to the prevailing party as part of the costs." In applying this section, the Ninth Circuit, as well as the Second, Seventh and District of Columbia Circuits, had held prevailing defendants to a more stringent standard. These circuits had applied a standard under which prevailing plaintiffs generally were awarded attorney

fees as a matter of course, but prevailing defendants were required to show that the original suit was frivolous or brought in bad faith. In contrast, the Third, Fourth and Eleventh Circuits used an "evenhanded" approach, treating prevailing plaintiffs and defendants alike.

In this case, Fogerty was sued by Fantasy for copyright infringement, and Fogerty prevailed after a jury trial. After successfully defending, Fogerty moved for an award of attorney fees pursuant to Section 505. The district court denied the motion, finding that the original action had not been frivolous or brought in bad faith. The court of appeals affirmed, 984 F.2d 1524 (9th Cir. 1993), declining to reject the "dual standard." The Supreme Court granted certiorari to resolve the conflict between the dual standard approach of the Ninth Circuit and the evenhanded approach of the Third Circuit.

Fantasy advanced three arguments in favor of the dual standard: (1) that the plain language of Section 505, read in light of prior decisions construing similar fee-shifting language, supported the rule; (2) that the dual standard comported with the objectives and equitable considerations of the Copyright Act as a whole; and (3) that the legislative history of Section 505 indicates that Congress ratified the dual standard that was "uniformly" followed by the lower courts under the 1909 Copyright Act.

The Court rejected Fantasy's first argument, which was based largely on the Court's decision in *Christiansburg Garment Co. v. EEOC*, 434 U.S. 412 (1978). There the Court had interpreted the language of Title VII of the Civil Rights Act of 1964, which provides in relevant part that the court "in its discretion, may allow the prevailing party . . . a reasonable attorney's fee as part of the costs." 42 U.S.C. § 2000e-5(k)(finding that for policy reasons, different standards applied to prevailing civil rights plaintiffs than to successful defendants).

Despite the virtually identical language of the two statutes, the Court determined that the goals and objectives of the two acts were "not completely similar." 1994 U.S. LEXIS 2042 at *11. In particular, the Court found that the factors relied upon in *Christiansburg* were absent in the copyright context. The *Christiansburg* Court found that, because the prevailing civil rights plaintiff is "the chosen instrument of Congress to vindicate 'a policy that Congress considered of the highest priority,' " Congress had sought to encourage oftentimes "impecunious" plaintiffs to bring meritorious civil rights claims by providing for more favorable treatment of plaintiffs regarding attorney's fees. 434 U.S. at 418. The *Fogerty* Court noted that, by contrast, copyright plaintiffs range from "corporate behemoths to starving artists; [and] the same is true of prospective copyright defendants." 1994 U.S. App. LEXIS 2042 at *15. Finally, the Court pointed out that fee-shifting statutes for patent and trademark infringement are "party-neutral." *Id.* Therefore, because the considerations that supported a dual standard approach for civil rights litigation were not present in the copyright context, the Court concluded that the two statutes, though almost identically worded, should be applied differently.

In a concurring opinion, Justice Thomas took exception with this aspect of the Court's holding, finding it anomalous for the Court to interpret essentially the same phrase differently in two different statutes. *Id.* at *31–38. Justice Thomas argued that the *Fogerty* decision could not be reconciled with *Christiansburg*, and disagreed with what he considered the flawed premise of the Court's analysis—that the interpretation of the plain language of a statute turns upon the statute's underlying policy objectives. *Id.* at *36. Nonetheless, Justice Thomas joined in the decision because he disagreed with the *Christiansburg* analysis, and believed that the *Fogerty* Court set forth the proper analysis.

Fantasy's second argument was based on the view that the dual standard encouraged litigation of meritorious copyright claims, thus effectuating the broad objectives of the Copyright Act. The Court rejected this argument as "one-sided," noting that "often times, defendants hold copyrights too, as exemplified by the case at hand." *Id.* at *16–17. Additionally, because copyright law ultimately serves the purpose of enriching the general public by enhancing access to creative works, the boundaries of copyright law must be demarcated as clearly as possible. Therefore, the *defense* of a copyright action may further the policies of the Copyright Act every bit as much as a meritorious infringement action. *Id.* at *19–20.

Fantasy's final argument was based on the principle of ratification, whereby Congress is presumed to be aware of the judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change. However, the Court's review of the body of case law decided under the 1909 Act revealed no established dual standard. Similarly, neither of two studies on copyright law that were submitted to Congress when studying revisions of the Act supported the existence of a dual standard under the previous Act. *Id.* at *20–28.

Having thus rejected all three of Fantasy's arguments, the Court turned to Fogerty's argument that, consistent with the neutral language of Section 505, both prevailing plaintiffs and prevailing defendants should be awarded attorney fees as a matter of course, absent exceptional circumstances. In other words, Fogerty argued that Section 505 was intended to adopt the "British Rule" for copyright infringement. The Court rejected this argument as well, finding that just as the plain language of the statute supported Fogerty's argument against the dual standard, it defeated his argument for the British Rule. The statute reads "the court *may* . . . award a reasonable attorney's fee." The word "may" clearly indicates that the court is to have discretion in deciding whether or not to award fees. Furthermore, given the universal application

of the "American Rule" in American courts, the Court found it "impossible to believe that Congress, without more, intended to adopt the British Rule. Such a bold departure from traditional practice would surely have drawn more explicit statutory language and legislative comment." *Id.* at *28-29.

Therefore, the *Fogerty* Court ultimately concluded that while the standard for determining whether a prevailing party is entitled to attorney fees must be same for defendants and plaintiffs, the ultimate decision to award fees or not is a matter of the court's discretion.

Federal Circuit Affirms Attorney Fee Award Pursuant to 35 U.S.C. § 285 in Action to Enforce the Settlement Agreement

In *Interspiro USA, Inc. v. Figgie International, Inc.*, No. 93-1445, 1994 U.S. App. LEXIS 4122 (Fed. Cir. March 9, 1994), the Court of Appeals for the Federal Circuit affirmed an award of attorney fees pursuant to 35 U.S.C. § 285 in an action to enforce a settlement agreement. Although the action was in essence a contract suit, and the interpretation of the contract turned on principles of New York state contract law, the court upheld the award of attorney fees because the ultimate decision was governed by the patent laws.

In 1988, Interspiro sued Figgie for infringement of U.S. Patent No. 4,361,145 (the '145 patent) for a "Respirator Mask" covering a breathing regulator. (Although Interspiro originally brought the infringement suit, all of Interspiro's assets were later acquired by Pharos Protection USA, Inc., and Pharos was the party in interest before the Federal Circuit.) The infringement suit was dismissed with prejudice pursuant to an agreement between the parties. The terms of the settlement agreement required Figgie to pay royalties on all domestic sales of products that were covered by the '145 patent. Some time after entering the agreement, Figgie began to manufacture and sell a new regulator, on which it did not pay royalties. Pharos filed a motion seeking to enforce the settlement agreement, and seeking attorney fees for Figgie's failure to act in good faith under the settlement agreement. The district court found that Figgie's new regulator was covered by the '145 patent, and that Figgie had improperly calculated the royalty payments due Pharos. Finally, the court found the case to be exceptional, and awarded Pharos attorney fees pursuant to Section 285. *Interspiro USA, Inc. v. Figgie Int'l., Inc.*, 815 F. Supp. 1488 (D. Del. 1993). Figgie appealed, arguing in part that the award of attorney fees was inappropriate because this was a contract action and, therefore, Section 285 was inapplicable. Prior to reaching the issue of attorney fees, the Federal Circuit affirmed the findings on infringement and tl royalty calculations, including the district court's inte pretation of the contract under New York law.

Under Section 285, "[t]he court in exceptional cas may award reasonable attorney fees to the prevailir party." Section 285 is however, limited to patent claim and when an action combines both patent and non-pate claims, the prevailing party may not recover amoun expended on the non-patent issues. *Machinery Corp. Am. v. Gullfiber AB*, 774 F.2d 467, 475 (Fed. Cir. 1985 Therefore, Figgie argued that the district court was with out authority to award attorney fees under Section 28 because this action was premised on a breach of contrac action involving non-patent issues. The court disagreed stating that Figgie's argument "impermissibly elevate form over substance." 1994 U.S. App. LEXIS 4122, a *16.

The court first affirmed the principle that Section 28 provides for the recovery of attorney fees "for tim incurred in the litigation of legitimate *patent claims*." *Id* (emphasis added.) A claim arises under the patent laws i the right to relief "will be defeated by one construction or sustained by the opposite construction of [the patent laws." *Id.*, quoting *Christianson v. Colt Indus. Operating Corp.*, 486 U.S. 800, 807-08 (1988)(citation omitted). Therefore, the court, in deciding the applicability of Section 285 in a given situation, looks to "the rights at issue and whether they properly invoke the patent laws. . . . It matters not whether those rights arise in a patent suit or in an action to enforce an agreement settling that litigation." *Id.*

In its analysis, the court found that the central issue—whether Figgie had breached the agreement by failing to pay royalties on the new regulator—turned on whether the new regulator infringed the '145 patent, an issue that is unquestionably governed by the patent laws. Additionally, the issues Figgie asserted to be "non-patent" issues, such as the assessment of royalties, were "'so intertwined with the patent issues' as to make section 285 applicable to the case in its entirety." *Id.*, quoting *Stickle v. Heublein, Inc.*, 716 F.2d 1550, 1564 (Fed. Cir. 1983). The court concluded that Pharos' motion to enforce the contract had asserted a right to relief that was wholly dependent on the resolution of a question of federal patent law. Therefore, the court agreed with the district court that "this is a patent case," and that Section 285 was applicable. Finally, the court affirmed the district court's finding that the case was exceptional, rebuking Figgie for "brazenly questioning the competency of the district court judge," and calling such a strategy "reprehensible." *Id.*

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Reflections Of Licensor To China

BY LARRY W. EVANS*

Insight into guidelines for successful relationships developed over many years of doing business there

Twenty-two years ago, even before Dr. Henry Kissinger travelled to China via Pakistan to make arrangements for President Richard Nixon's historic visit to China in late 1972, my company at the time, Sohio, was approached by a Japanese company that was interested in sub-licensing Sohio's world-famous acrylonitrile technology to China as a critical part of a synthetic fiber complex to be built in the vicinity of Shanghai. At the time, I was a young, relatively-inexperienced corporate licensing director (and patent attorney) at Sohio; and the U.S. and China were in the midst of more than a decade of chilly nonrelations following the Korean war. I guess we didn't know any better, because we said to our Japanese friends, when they asked if we would be willing to apply for an export license from the U.S. government, "Sure; let's give it a try!"

What began then and continues today is more than 20 years of adventure, occasional exhaustion, constant challenge and very rewarding experience. We requested an export license and, initially, were told that it would be out of the question. No one had received a technology export license for China since before the Korean war. We persisted and eventually the matter was escalated to the White House. What began as an innocent request for an export license for synthetic fiber intermediate technology became a potential international cause *celebre*. President Nixon was all for it and personally approved the request.

In 1973, licensing in China for an American company, or any Western company for that matter, involved the exploration of uncharted territory. We felt a bit like Marco Polo must have felt going to this strange country where everyone dressed alike and no one really identified himself — a country without written laws, without patent laws and with no history of contract enforcement. It was a risk but China's more than one billion people and its obvious desire to become industrialized made this a risk that had to be accepted.

Henry Kissinger, on his arrival in Beijing in 1972, said to Premier Zhou Enlai, "Ah! I have finally arrived in China, the land of mystery." To this Premier Zhou replied, "China is not a mystery to one billion Chinese." I must say that we agreed with Dr. Kissinger when we arrived in China in 1973. It truly was a land of mystery. Yes, I had seen President Nixon on television, toasting Chairman Mao and Premier Zhou during his historic 1972 trip, but we really did not anticipate what we were to find in February 1973, seven years into the Great Proletariat Cultural Revolution. We saw a sea of expressionless faces — everyone dressed alike — men, women, high officials, manual laborers all looked the same. Also, we didn't appreciate what President Nixon was drinking during his many toasts with China's leaders. If any of the visitors present haven't tasted Mao Tai, your China experience is incomplete.

Little was known in 1973 about China's organizations, its negotiation style, its reliability. We found out that when the Gang of Four was thrown out in 1976, China had an opportunity once again to realize its intellectual potential, its entrepreneurial spirit, its true character and its culture (which was built up over more than 6,000 years of civilization). Over the 20 years following this initial visit, we have found that the Chinese are reliable, secure and contributing partners.

◄ Intellectual Spirit ►

Premier Zhou (who most intellectuals in China credit with keeping China's intellectual spirit alive) said China's population can be viewed by either multiplication or division. As a multiplier, its 1.2 billion population provides the world's largest single market, but when the 1.1 billion people must share a limited grain production, the population becomes a liability, not an asset. Not surprisingly, the Chairman of the Nike running show company views China as 2.4 billion feet.

I am extremely proud to have been at least partially responsible for my company's early recognition of China's potential. Sohio was the first American technology licensor to China following the resumption of friendly relations with the U.S.

Chairman Deng Xiaoping (who many believe to be one of the most important world leaders in the 20th century) said to the world in 1981, "Give us chickens and not eggs," give us the means to produce, not the products. Sohio, in 1973 and continuing up to and including 1993, gave China technology licenses, turn-key plants so that China could produce. The company has never regretted its decision.

Sohio's acrylonitrile technology which was licensed to a predecessor of Sinopec (China Petrochemical)

Willian Brinks Hofer Gilson & Lione, Chicago, Illinois; paper presented at the LES International Conference, Beijing, China.

in 1973 has now been licensed for use in eight plants in China, an unprecedented number of repeat licenses. This is an excellent example of China's unwritten policy of loyalty to old friends, preference for quality *and* legal reliability.

My China experience has not always been entirely positive, but, on balance, we will never regret having persuaded Sohio to license its technology here. It has been a very rewarding financial experience for the company, and it has also been personally rewarding for me. I regard China today as my home away from home, and I regard many of the Chinese officials, translators, hotel employees, taxi drivers, etc. that I have met over more than 20 years as personal friends. Once a personal relationship is established with the Chinese people, one realizes how open and friendly they are.

What have I learned in these 20 years of China licensing experience? During these 20 years, China has undergone the most profound change of any country in the world. Some of these changes are obvious. In 1973, to travel to Beijing it was necessary to fly to Hong Kong, take a train to the Lowu Bridge, another train to Canton (as Guangzhou was know in those days), fly from Canton to Beijing (if one was lucky; if not, another train to Beijing). Nearly two exhausting days after one left Hong Kong, he arrived in Beijing only to find a dismal, dingy hotel and a chilly reception.

◄ Questions ►

In 1973, only four hotels were available to foreigners — the Beijing (without the East Wing), the Minzu, the Xinqiao and the Friendship. The Chinese, then in the latter stages of the great Proletariat Cultural Revolution, introduced themselves as "responsible persons from relevant departments." Only after a sale was made or a license was executed did one get to meet the end-user. The most elementary issues concerned us all. How much oil did China produce? Who were the top officials in the Oil Ministry and the Chemical Ministry? How did the economy work? Who made the decisions?

1994 seems more like a century than only 21 years removed from 1973. Peking is now Beijing. Beijing seems to get a new hotel every month. Beijing now has horrible traffic jams — the kind that would even make traffic in Chicago or New York seem moderate. These traffic jams are caused by automobiles, trucks and buses, not bicycles. Individuals that were merely faces across the table in 1973 have become real people, even close friends in the 90s. These new friends have even been known to invite Americans into their homes, and accept invitations to my home.

Many of the barriers to doing business have fallen. Today, I probably know more about China's business, economics and politics than I do about the United States. I know — or can easily determine — the relevant ministry, and I know where it's located. Chinese officials and businessmen have name cards, telephone numbers, even fax numbers. China has indeed opened its doors to the Western World.

Why should all of us be interested in China? Obviously, its population is an important factor. Even more important, China is coping with the needs of this population. It's people are well fed, clothed and sheltered. Education has rebounded after the loss of a generation of skilled scientists and technicians during the Cultural Revolution.

China has rich natural resources and, except for an occasional problem, a stable government with conservative fiscal policies. China will not overextend itself like Mexico or Brazil. They will take measures, sometimes painful measures, against inflation. China, today, has a stable, visionary government. As Mr. Deng says, "It's not a sin to get rich," and a lot of Chinese people are realizing financial success in the China of the 90s.

In the 21 short years since China opened to the West, tremendous strides have been made. The Chinese people have progressed from being obsessively cautious and relatively inefficient negotiators to being respected business partners. Their negotiation style used to be a bit like Chairman Mao's 16 character poetic description of guerrilla warfare:

"Enemy advances,
We retreat.
Enemy halts,
We harass.
Enemy tires,
We strike.
Enemy retreats,
We pursue.

Negotiation with the Chinese today retains some of these characteristics. The Chinese respect poise. Reason, self-control and self-confidence are prized. They deplore a negotiator who loses control. The Chinese believe the graceful bamboo that yields to the wind is strong; while the mighty oak that fights the wind will sometimes break; water submits to all it touches, yet it cuts through rock.

Confucius said, "He who treads lightly goes far." If you deal with the Chinese in a climate of mutuality, you'll be successful again and again. However, if you are right, you should be firm. Don't make the mistake of trying to imitate the Chinese; you will not do it well. You should, however, be aware of their culture and pride.

Confucius said, "If you enter a region, ask what its prohibitions are; if you visit a country, ask what its customs are; if you cross a family's threshold, ask what its taboos are."

Remember those words when you come to China.

In my view, it is impossible to be completely successful in China, if one does not develop an affection for the Chinese people. This will enable you to develop close *personal* relationships with your counterparts. It will also enable you to understand the Chinese way of thinking and their attitudes on life. If one does not like the Chinese, his negative feelings will become apparent, and he will not be successful.

◄ Trust ►

Trust is the single most important element of succeeding in China business. The time and effort that one invests to establish trust and friendship with responsible officials in Chinese organizations will be

handsomely rewarded. It is important to establish this trust and friendship before the business arrangement is finalized. If one learns to offer genuine friendship to the Chinese, he will find that friendship returned many times over, once the Chinese learn to trust him.

In negotiations with the Chinese one should try to eliminate barriers that may lead to unnecessary difficulties later on. Such barriers can be cultural, language, business style, and conceptual. Clarify all agreements to make sure that both parties have the same mental picture of the agreement. I was once asked by a young Chinese lawyer, "What should the role of a lawyer be in a license negotiation?" I said, "Stay out of the way of the businessman. Draft the agreement to reflect the understanding reached and make certain that both sides understand the words. Be a dealmaker, not a deal breaker."

China today has a legal system that truly boggles the mind, especially when one remembers that Chinese school children are taught that the law is a tool used by the ruling class to suppress opposing classes and control the people. Nonetheless, in the decade of the 80s, China adopted a contract law, a foreign contract law, a joint-venture law and implementing regulations, a joint-venture tax law and implementing regulations, regulations regarding the registration of joint ventures, foreign exchange control regulations, regulations governing permanent representative offices in the PRC, regulations on doing business in the Special Economic Zones, a bankruptcy law, import/export regulations, a patent law, a trademark law regulation governing arbitration, a copyright law, insurance regulations, advertising regulations, and two sets of regulations on the administration of technology import contracts. In the 90s, the patent law has been amended to protect chemical and pharmaceutical compounds (among other things), and trade secrets are now regarded as protectible property. Not bad for a country whose people are taught that the law is a tool of the ruling class to take unfair advantage of the working class.

Often, when one deals with the Chinese, he experiences a series of crises. If one lacks control and does not practice what I call "restrained, steadfastness," he may find a crisis too difficult to handle. I'm told that the word for "crisis" in Mandarin is "wei-ji." To write "wei-ji" in Chinese it is necessary to write two characters. The first "wei" means "danger"; the second "ji" means "opportunity." Thus, a crisis in China can be seen to present not only a danger, but also an opportunity. I try, when I'm in China in negotiation, to view all crises not as dangers, but as opportunities.

Napoleon Bonaparte was quoted as once having said "China? There lies a sleeping giant. Let him sleep, for when he wakes, he will move the world." China has awakened, and China is moving the world. Growth-oriented western companies must be prepared to join the movement, or they will be left behind.

LICENSING WITH JAPANESE COMPANIES:
RESOLVING DISPUTES AND MISUNDERSTANDINGS
Workshop #27 - October 18, 1989
Larry W. Evans

A. Avoidance of Misunderstandings

1. Understand cultural differences -

a. U.S. is a society organized around its legal system - Unique in the world.

b. Japan is equally unique as a large industrial society in which law plays only a peripheral role.

c. U.S. is a heterogeneous, continental society while Japan is an isolated, homogeneous, island society - no significant migration for more than 1,000 years.

d. Japan's tribal traditions have endured even in the face of the forces of industrialization and modernization - the Japanese believe they cannot be understood by foreigners.

e. Americans can live, work and thrive without any cultural traditions telling them how to live. Individuality encouraged and is necessary for survival.

f. Law, Politics, Lawyers and Politicians are necessary to provide order in business and domestic relations in U.S. - Central to our lives - Difficult for Japanese to comprehend.

g. Japan functions without law (essentially).

h. Americans view themselves from perspective of a God who is outside and above human history - We are individualistic in order to be able to follow morality when it conflicts with our social roles.

i. In America, the individual comes before society which is, after all, nothing but a social contract between individuals.

j. Americans value social and political freedom to a degree regarded by others as extravagant.

k. Without rule of law, the U.S. could not exist - anarchy and chaos would be the result.

2. Japanese self identity and social harmony.

a. Japanese have no judging God; The self is the social self.

b. No need to be different.

c. Japanese must act in accord with giri with the appropriate ninjo -

d. If one is un-Japanese, it's like being rejected by one's peers during adolescence.

3. Japanese do not like lawyers - resort to law presupposes a break-down in social harmony - a confession that the appropriate giri and ninjo have not been utilized.

Law is not an alternative to violence; it is the equivalent of violence!

4. Lawyers should be kept in the background - low profile.

a. Keep the businessmen in front negotiating the deal.

b. Lawyers should be active only when Japanese use lawyers.

c. In Japan, lawyers are not regarded as experts on fair dealing but as disreputable characters employed by people unable to manage themselves in a civilized manner.

d. Silence equals strength in Japan.

e. Japanese will not ordinarily make a deal with someone they do not like. Reciprocal trust and mutual obligation are valued.

f. Quality more important than price.

5. Agreements considered by Japanese to be "living" documents. Agreement execution is often beginning (not end) of negotiations.

a. Stick to basic principles.

b. Do not be reluctant to compromise non-basic items but get something in return.

c. Compromises should be positive--not negative.

B. Handling Disputes.

1. Be prepared to negotiate.

2. Do not "circle the wagons" unless critical matter is in dispute.

3. Avoid personal animosity; be represented by highly-credible, diplomatic representative, not by tough-talking hardnose.

4. Lawyers should be kept in background.

5. Suggestion - include as dispute resolution clause in contracts - "negotiate with sincerity to achieve mutually-beneficial resolution of all disputes."

6. Case examples.

C. Japanese Negotiating Style.

1. Noren Desu - image and goodwill - the Japanese may sacrifice profit in order to improve or maintain its image. Americans should be careful not to question this.

2. Smoking out the tanuki (Determining the true intention) - Sometimes license prospects may only be curious - a hypothetical question can often determine true intent.

3. Fumie (determining the limit). Determining the sincerity of the other side.

4. Nemawashi (Digging around the roots)
   - persuasion of higher authorities by indirect methods.
   - Japanese require time to go through the motions.
   - Celebrations of successful negotiations necessary - breaks down restraint.
   - Warm human relationships more important than the agreement.
   - Try not to disrupt harmony.

5. Ringi System (Collective Decision Making) - Circulation of a ringisho on which all necessary parties to decision must place their hanko (seal) giving approval or disapproval.

6. Never take "yes" for an answer.

7. Silence is golden; eloquence is silver.

8. Summary - When negotiating with Japanese, one should be thoroughly prepared, observant and patient. When a Japanese nods he hears you he does not necessarily understand or agree.

REFLECTIONS OF A CHINA LICENSING VETERAN

(by Larry W. Evans)

Twenty-two years ago, even before Dr. Henry Kissinger travelled to China via Pakistan to make arrangements for President Richard Nixon's historic visit to China in late 1972, my company at the time, Sohio, was approached by a Japanese company that was interested in sub-licensing Sohio's world-famous acrylonitrile technology to China as a critical part of a synthetic fiber complex to be built in the vicinity of Shanghai. At the time, I was a young, relatively-inexperienced corporate licensing director (and patent attorney) at Sohio; and the U.S. and China were in the midst of more than a decade of chilly non-relations following the Korean war. I guess we didn't know any better, because we said to our Japanese friends, when they asked if we would be willing to apply for an export license from the U.S. government, "Sure; let's give it a try!"

What began then and continues today is more than 20 years of adventure, occasional exhaustion, constant challenge and very rewarding experience. We requested an export license and, initially, were told that it would be out of the question. No one had received a technology export license for China since before the Korean war. We persisted and eventually the matter was escalated to the White House. What began as an innocent request for an export license for synthetic fiber intermediate technology became a potential international cause celebré.

President Nixon was all for it and personally approved the request.

In 1973, licensing in China for an American company or any Western company for that matter involved the exploration of uncharted territory. We felt a bit like Marco Polo must have felt going to this strange country where everyone dressed alike and no one really identified himself-a country without written laws, without patent laws and with no history of contract enforcement. It was a risk but China's more than one billion people and its obvious desire to become industrialized made this a risk that had to be accepted.

Henry Kissinger on his arrival in Beijing in 1972 said to Premier Zhou Enlai - "Ah! I have finally arrived in China, the land of mystery." To this Premier Zhou replied, "China is not a mystery to one billion Chinese." I must say that we agreed with Dr. Kissinger when we arrived in China in 1973 - it truly was a land of mystery - yes, I had seen President Nixon on television, toasting Chairman Mao and Premier Zhou during his 1972 historic trip, but we really did not anticipate what we were to find in February, 1973 - seven years into the Great Proletariat Cultural Revolution - a sea of expressionless faces - everyone dressed alike- men, women, high officials, manual laborers all looked the same; we also didn't know what President Nixon was drinking during his many toasts with China's leaders. If any of the visitors present haven't tasted Mao Tai, your China experience is incomplete.

Little was known in 1973 about China's organizations, its negotiation style, its reliability. We found out that when the Gang of Four was thrown out in 1976, China had an opportunity once again to realize its intellectual potential, its entrepreneurial spirit, its true character and its culture (which was built up over more than 6,000 years of civilization). Over the 20 years following this initial visit, we have found out that the Chinese are reliable, secure and contributing partners.

Premier Zhou (who most intellectuals in China credit with keeping China's intellectual spirit alive) said China's population can be viewed by either multiplication or division. As a multiplier, its 1.2 billion population provides the world's largest single market, but when the 1.1 billion people must share a limited grain production, the population becomes a liability, not an asset. Not surprisingly, the Chairman of the Nike running show company views China as 2.4 billion feet.

I am extremely proud to have been at least partially responsible for my Company's early recognition of China's potential. Sohio was the first American technology licensor to China following the resumption of friendly relations with the U.S.

Chairman Deng Xiaoping (who many believe to be one of the most important world leaders in the twentieth century) said to the world in 1981-"give us chickens and not eggs", that is, give us the means to produce, not the products. Sohio, in 1973, and continuing up to and including 1993, gave China technology

licenses, turn-key plants so that China could produce. The company has never regretted its decision.

Sohio's acrylonitrile technology which was licensed to a predecessor of Sinopec (China Petrochemical) in 1973 has now been licensed for use in eight plants in China, an unprecedented number of repeat licenses. This is an excellent example of China's unwritten policy of loyalty to old friends, preference for quality and legal reliability. My China experience has not always been entirely positive, but, on balance, we will never regret having persuaded Sohio to license its technology here. It has been a very rewarding financial experience for the company, and it has also been personally rewarding for me. I regard China today as my home away from home, and I regard many of the Chinese officials, translators, hotel employees, taxi drivers, etc. that I have met over more than 20 years as personal friends. Once a personal relationship is established with the Chinese people, one realizes how open and friendly they are.

What have I learned in these 20 years of China licensing experience? During these 20 years, China has undergone the most profound change of any country in the world. Some of these changes are obvious. In 1973, in order to travel to Beijing it was necessary to fly to Hong Kong; take a train to the Lowu Bridge; another train to Canton (as Guangzhou was known in those days); fly from Canton to Beijing (if one was lucky; if not, another train to Beijing). Nearly two exhausting days after

one left Hong Kong, he arrived in Beijing only to find a dismal, dingy hotel and a chilly reception.

In 1973, only four hotels were available to foreigners - the Beijing (without the East Wing), the Minzu, the Xinqiao and the Friendship. The Chinese, then in the latter stages of the great Proletariat Cultural Revolution, introduced themselves as "responsible persons from relevant departments." Only after a sale was made or a license was executed did one get to meet the end-user. The most elementary issues concerned us all. How much oil did China produce? Who were the top officials in the Oil Ministry and the Chemical Ministry? How did the economy work? Who made the decisions?

1994 seems more like a century than only 21 years removed from 1973. Peking is now Beijing. Beijing seems to get a new hotel every month. Beijing now has horrible traffic jams- the kind that would even make traffic in Chicago or New York seem moderate. These traffic jams are caused by automobiles, trucks and buses, not bicycles. Individuals that were merely faces across the table in 1973 have become real people-even close friends in the 90's. These new friends have even been known to invite Americans into their homes, and accept invitations to my home.

Many of the barriers to doing business have fallen. Today, I probably know more about China's business, economics and politics than I do about the United States. I know- or can easily determine - the relevant ministry, and I know where it's

located. Chinese officials and businessmen have name cards, telephone numbers-even fax numbers. China has indeed opened its doors to the Western World.

Why should all of us be interested in China? Obviously, its population is an important factor. Even more important, China is coping with the needs of this population. It's people are well fed, clothed and sheltered. Education has rebounded after the loss of a generation of skilled scientists and technicians during the Cultural Revolution.

China has rich natural resources and, except for an occasional problem, a stable government with conservative fiscal policies. China will not overextend itself like Mexico or Brazil. They will take measures, sometimes painful measures, against inflation. China, today, has a stable, visionary government. As Mr. Deng says, "It's not a sin to get rich", and a lot of Chinese people are realizing financial success in the China of the 90's.

In the 21 short years since China opened to the West, tremendous strides have been made. The Chinese people have progressed from being obsessively cautious and relatively inefficient negotiators to being respected business partners. Their negotiation style used to be a bit like Chairman Mao's 16 character poetic description of guerrilla warfare:

"Enemy advances,
We retreat.
Enemy halts,
We harass.
Enemy tires,

We strike.
Enemy retreats,
We pursue.

Negotiation with the Chinese today retains some of these characteristics. The Chinese respect poise; reason, self-control and self-confidence are prized and they deplore a negotiator who loses control. The Chinese believe the graceful bamboo that yields to the wind is strong; while the mighty oak that fights the wind will sometimes break; water submits to all it touches; yet it cuts through rock.

Confucius said "He who treads lightly goes far." If you deal with the Chinese in a climate of mutuality, you'll be successful again and again. However, if you are right, you should be firm. Don't make the mistake of trying to imitate the Chinese; you will not do it well. You should, however, be aware of their culture and pride.

Confucius said,

"If you enter a region, ask what its prohibitions are;
if you visit a country, ask what its customs are;
if you cross a family's threshold, ask what its taboos are."

Remember these words when you come to China.

In my view, it is impossible to be completely successful in China if one does not develop an affection for the Chinese people. This will enable you to develop close <u>personal</u> relationships with your counterparts. It will also enable you to

understand the Chinese way of thinking and their attitudes on life. If one does not like the Chinese, his negative feelings will become apparent, and he will not be successful.

Trust is the single most important element of succeeding in China business. The time and effort that one invests to establish trust and friendship with responsible officials in Chinese organizations will be handsomely rewarded. It is important to establish this trust and friendship before the business arrangement is finalized. If one learns to offer genuine friendship to the Chinese, he will find that friendship is returned many times over once the Chinese learn to trust him.

In negotiations with the Chinese one should try to eliminate barriers which may lead to unnecessary difficulties later on. Such barriers can be cultural, language, business style, and conceptual. Clarify all agreements to make sure that both parties have the same mental picture of the agreement. I was once asked by a young Chinese lawyer "what should the role of a lawyer be in a license negotiation?" I said, "stay out of the way of the businessmen. Draft the agreement to reflect the understanding reached and make certain that both sides understand the words. Be a deal maker-not a deal breaker."

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JOURNAL OF THE LICENSING EXECUTIVES SOCIETY

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Case History Of Successful Licensing

BY LARRY W. EVANS*

Story behind how U.S. regional company has managed its worldwide licensing program for more than three decades

This paper is intended to present in an understandable way one of the most significant success stories of my career in licensing. I believe it is a classic example of how a relatively small and unsophisticated company can realize significant worldwide success in an international licensing program.

The success can be measured in several ways. First, the cumulative amount of royalty income was substantial. Second, the company prospered in its own manufacture and sale of products utilizing the technology. Third, the success has continued for more than 32 years. Much of the longevity is due, in my opinion, to the licensing program and its administration. In every way, the licensing program was immensely successful.

This paper will review the background of the company and its technology position; the decisions that led to the licensing program; the licensing program itself; and the reasons it has been successful. In particular, I will stress the intellectual property aspects of the licensing program, including creation, maintenance and enforcement of the patents and trade secrets involved.

BACKGROUND

In the late 1950s, BP America's predecessor company, The Standard Oil Company (better known then as Sohio), was a relatively small regional refiner and marketer of petroleum and petroleum products. Sohio was, in fact, John D. Rockefeller's original company, having been founded in 1869. The Rockefeller empire grew rapidly until 1911 when the U.S. Supreme Court dissolved it into 34 independent operations, including Mobile, Exxon, Amoco, Chevron, Arco, Marathon, Continental. The original company, Sohio, was left in Ohio with only one refinery and some horse-drawn tank wagons. Sohio did not enter the chemicals business until 1954 and then only on a small, specialized scale. In fact, Sohio's "entry" into chemicals was with two small nitrogen plants (producing ammonia, nitric acid and urea) in about 1954.

The refinery business during this period was undergoing a transition from maximizing distillate (*i.e.* fuels and diesel oil) production to maximizing gasoline, which was necessitated by the post-war increase in automobile use. When gasoline production is maximized through catalytic cracking, light hydrocarbon (particularly propylene) production is increased. Propylene, at that time, had limited utility. Its primary use was as a fuel. A Sohio Director of Research decided to embark on a project to upgrade the value of propylene by converting it to a high-value chemical. Without taking the time to relate a very interesting research story, I can say the "rest is history." A team of young Ph.D. chemists discovered that propylene could be oxidized to acrolein and also could be ammoxidized to acrylonitrile over a revolutionary new catalyst. Both acrolein and acrylonitrile were high-value chemicals.

Sohio's catalytic process of converting propylene to acrylonitrile could be accomplished in a single step by simultaneously reacting air and ammonia (one of the few chemicals Sohio Chemical was then manufacturing) with the propylene, in a fluidized catalytic bed. The yields were phenomenal as compared to the literature, and this route to acrylonitrile was potentially much less costly than the then commercial route.

While Sohio Chemical Company was then relatively small and unsophisticated as compared to the "giants," *i.e.*, duPont, Monsanto and Dow, it had competent people who were aware of the laws of patents and trade secrets. Because of this, the discovery was well protected from the start. Sohio did not lack brainpower. It lacked experience in the chemical industry, capital and market share.

Acrylonitrile was already known as a valuable chemical intermediate for the production of acrylic fiber (Acrilan® and Orlon®), ABS plastics and nitrile rubbers. Its cost, however, was high and its production volume was limited.

◄ Sought Partner ►

Sohio initially did not believe it could take on such a risky project without a partner and approached one of the chemical "giants." Probably because of the well-recognized N.I.H. (not invented here) factor, the "giant" turned Sohio down. Its only recourse, therefore, was to "go it alone," and it did so by announcing the construction of a plant in 1958. The plant began commercial production in early 1960, only three and one-half years from the initial discovery that propylene could be converted to acrylonitrile over

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plications per year for its entire life.

As indicated above, all of the technology except that published was considered to be a trade secret. In addition to the standard requirements of trade secret maintenance such as no disclosure without a secrecy agreement, employee secrecy agreements and disclosures or access to employees only on a need-to-know basis, a corporate policy of enforcement had to be established from the start. Fortunately, this was done.

THE LICENSE AGREEMENT

A successful licensing program also requires a well-crafted license agreement. I can be objective with respect to the license agreement utilized by Sohio Chemical because the original was drafted more than 10 years before I was employed at Sohio. It is a masterpiece of drafting and has stood the test of time in a very effective way. I do not intend in this paper to reproduce the agreement, but I do believe a review of some of the more interesting provisions would be appropriate.

Confidentiality

The heart of any process license agreement is the confidentiality provision. The provision adopted by Sohio Chemical included a very long term of secrecy and limited the exceptions under which the licensee or disclosee was authorized to disclose the information.

It clearly limited the right to use the technology to the express license only. It, of course, included a provision that required the licensee to comply with the United States Export Control Regulations. A very interesting and effective provision in the confidentiality agreement was that the licensee or disclosee was prohibited from disclosing the fact that the technology originated with Sohio even after the technology had become generally available to the public.

This, in my opinion, is a very important prohibition since an accidental disclosure of some features of the technology by a university researcher or an engineering contractor might not significantly damage a licensing position if the reader (i.e., the disclosee) is not informed that in fact the disclosure originated with the licensor.

Finally, the confidentiality provision was always effective even after termination, cancellation or repudiation and even if the license agreement failed to become effective because it did not receive government approval.

The Improvement Exchange

Sohio decided early on that it would probably be unable to make all inventions and improvements in this technology by itself. If an effective exchange of improvements between its licensees and itself could be designed, not only would the technology continue to improve, but also Sohio would maintain its role as the licensor of the technology. To accomplish this goal, the license agreement included an improvent exchange that incorporated the following general terms: (1) a limited term, e.g., five to seven years at the option of the licensee; (2) the grant-back of improvements from the licensee to licensor was nonexclusive; (3) the licensee would have the first option of filing patent applications on its improvements but, if it elected not to file such applications, they would be filed by Sohio in the name of the appropriate inventors and would be assigned by Sohio with the licensee receiving a nonexclusive license; and (4) licenses granted by licensee to licensor to utilize its improvements included the royalty-free right to grant sublicenses to such other parties as shall have granted a similar license to licensor in such manner that the grant inures to the benefit of the licensee. In other words, the improvement exchange was nonexclusive, multilateral and royalty-free. The licensor acted as the "hub" of the wheel and was connected to the licensees around the circumference of the wheel by the spokes. Under the provision, improvement disclosures always had to travel through the licensor in order to reach other licensees. Additionally, the body of technology was continually improved and licenses to the improved *body of technology* could be granted only by the licensor.

Sohio facilitated this exchange program by holding periodic technical exchange meetings of its licensees. These meetings proved effective not only in facilitating communications but also in enhancing Sohio's position as the licensor of the technology.

It is important to note, at this point, that licensees were not required to exchange improvements. Whether licensee participated in the improvement exchange was his option. On the other hand, all licensees want some limited exposure to licensor's improvements. Sohio insisted that, to the extent the licensee received Sohio's improvements, it must be willing to reciprocate, *i.e.* grant its improvements back on a royalty-free, nonexclusive basis, and the reciprocal exchange must also be available to licensor's other licensees who had agreed to participate.

By means of this program, which to have any viability had to include its own substantial and continuing technology development effort, Sohio was able to develop a tremendously successful, incredibly long-lasting technology position that benefited its own operations and those of its many licensees. Also, consumers, who were able to purchase acrylonitrile-containing products at lower prices and in greater volume than before, were beneficiaries of the improvement exchange program.

The Hybrid License Problem

With respect to royalties, Sohio preferred not to state a separate patent royalty because the licensee was basically purchasing a plant and instructions on how to operate the plant. The licensee's only requirement relative to patents was that he receive immunity from suit under the licensor's patents. Under U.S. law, it is strongly recommended that hybrid licenses, *i.e.* those that include both patents and trade secrets, have separately stated royalties for the patents since collection of royalties after significant patents expire (*i.e.* not reducing the overall royalty) could constitute an antitrust violation. Sohio's solution to this problem involved the inclusion in the agreement of the following provision:

received a substantial award, and thus the settlement discussions resulted in a non-public resolution of the dispute on very attractive (for us) terms.

The most important lesson we have learned over the nearly 33 years of existence of our licensing program is that, through a balanced but firm enforcement strategy, a licensor gains much more respect than resentment. In fact, justification of such an enforcement program can be based on the necessity to protect the interests of those licensees, disclosees and employees who honor all of their commitments to us.

RECORD OF SUCCESS

It would seem obvious that, if a licensing program has lasted for nearly 33 years and has remained strong, it has been successful. In fact, this program has an unparalleled record of success.

The licensing experience has proceeded in several distinct stages. First, the Japanese manufacturers and would-be manufacturers approached Sohio for licenses that were granted during the very early 1960s. When it became obvious to the American manufacturers that Sohio really had something and that, in order to compete with it and the Japanese, they must also take licenses, licenses were then negotiated with the major U.S. manufacturers.

Western Europe came next. During the late 1960s four countries in Eastern Europe took licenses. These licenses were usually the result of a sublicense passed through an international engineering contractor.

Beginning in the early 1970s, many licenses were granted to developing countries (many of which now must be called newly developed countries) such as Taiwan, Korea, Brazil, Mexico, India and China. Licensing continues today, but also the company continues in its own expansion of the use of the technology.

One of the most significant successes has been with China. We were one of the first companies to license in China following the resumption of friendly relations in 1972, and since then seven additional licenses have been granted, the last in early 1993.

Even with the very liberal licensing program that has resulted in more than 45 licenses throughout the world, the company itself has realized substantial success in its manufacture and sale of acrylonitrile and of the proprietary catalyst used in the manufacture. Generally, licensing and manufacturing co-existed very well. In most cases it was deemed that licensing was the best way to penetrate a particular market; in some cases it was the only way. The fact that we were able to base a successful catalyst sales business on our licensing success was another reason that the manufacturing people were happy.

EPILOGUE

In reviewing the history of this very successful licensing program, it is difficult to detect any areas in which the company would have operated differently under the circumstances that then existed. Given essentially unlimited resources, it might have been possible for a company to have dominated the manufacture of a large-volume petrochemical such as acrylonitrile in some countries. It would not have been possible for a company to have done this throughout the world.

In particular, the protected market of Japan would not have allowed even a joint venture during the early 1960s. If the technology were not licensed to Japan, we can all be sure that the Japanese would have found a way to produce acrylonitrile without a license. Had they done this, by now, they would probably be a substantial competitor for the technology in other parts of the world. A licensing program like this consists of many trade-offs such as long-term gain versus short-term gain and dissemination of technical information (even with secrecy agreements) versus retention of total control of technical information.

It is believed that the history which is recounted in this paper will stand the test of time as an example of outstanding licensing strategy and success.

LICENSING IN ASIA

By: Larry W. Evans

Presented at AIPPI Korea and LES Korea International Symposium in Seoul, 1995

Today, I have a daunting task - that of explaining my experience in Asia licensing in 30 minutes. I appreciate very much to have been asked to come to Seoul again this year to participate in this wonderful symposium, but I am somewhat concerned about my ability to communicate 25 years of Asia licensing experience in such a short time. But I will give it a try.

In 1970, as a 30 year old patent attorney/chemical engineer, I joined the Standard Oil Co. of Ohio (known to most people as "Sohio"). My job was to license the world-famous Sohio Acrylonitrile Process. In 1993 at this Symposium I described in some detail this process and the licensing program. In your coursebooks is a copy of a paper which was published in les Nouvelles (the Journal of the Licensing Executives Society). I will not discuss the technology or the details of the licensing program today. I offer this only to put my experience into context.

Sohio's acrylonitrile technology and several other technologies developed by Sohio were licensed in Asia. I have had considerable experience in Japan, China, Taiwan

and Korea. My talk today will center around these four countries and the challenges they present to U.S. licensors.

The principal conclusion that I have drawn from my licensing experience in Asia is that the license agreements and projects are not much different from those that are conventional in the U.S. and Europe. Generally, the respect for and protection of intellectual property and the interest in technical assistance and performance guarantees are similar.

What is clearly different is the approach to negotiation of license agreements in Asia as contrasted with that in the U.S. and Europe. The "Licensing in China" paper that is included in the meeting materials describes some of the specifics with respect to China.

My talk today will concentrate on the profound impact of Asian culture on licensing negotiations between Americans and Asians.

My experience in Asia has revealed to me that all cultures of East Asia have been significantly affected by thousands of years of Chinese thought. China's nearly 5,000 year old culture has had a profound impact on Japan and Korea. Japan has had a considerable impact over this region the last half century as well.

The Asian culture as I am sure all of you are aware is vastly different from Western (especially American) culture.

Culture profoundly affects how people think, communicate and behave, and it also affects licensing and the way licensing is most effectively accomplished.

Differences in culture, for example, between a Chinese Vice-President of a government-owned petrochemical company in Beijing and a young patent attorney from a regional oil company in Cleveland, Ohio can create negotiating barriers that certainly impede and often totally block the negotiating process.

My 25 years of experience in licensing U.S. technology to Asian companies have taught me many things about these cultural differences-these negotiating barriers. My purpose today is to share in the next 25 minutes my experiences over the past 25 years.

For Americans making deals in Asia, cultural differences with their Asian counterparts are often the most difficult obstacles to overcome. I am certain the same is true for Asians making deals with American counterparts.

What do I mean by culture?

Culture consists of the socially transmitted beliefs, behavior patterns, values and norms of a given community or people. People use the elements of their culture to interpret their surroundings and guide their transactions with other persons. When two American or two Asian companies sit

down to make a deal, they rely on a common culture to interpret each other's statements and actions. But when persons from two different cultures, for example, executives from Chicago and executives from Tokyo or Seoul or Beijing meet for the first time, they do not share a common pool of information and assumptions to interpret each other's statements, actions, and inventions.

Differences in culture between negotiators can obstruct negotiations in many ways. First, they can create misunderstandings in communication. If one American executive responds to another American's proposal by saying, "That's difficult," the response, interpreted against American culture and business practice, probably means that the door is still open for further discussion, that perhaps the other side should sweeten its offer. In Asian cultures, persons may be reluctant to say a direct and emphatic "no", even when that is their intention. So when a Japanese negotiator, in response to a proposal says, "That is difficult", he is clearly indicating that the proposal is unacceptable. "It is difficult," means "no" to the Japanese, but to the Americans, it means "maybe".

Second, cultural differences create difficulties not only in understanding words, but also in interpreting actions. For example, most Westerners expect a prompt answer when they ask a question. Japanese, on the other hand, tend to take longer to respond. As a result, negotiations with Japanese sometimes involve excruciating periods of silence. For

Japanese, silence is normal; it is an appropriate time to reflect on what has been said.

Americans sometimes interpret Japanese silence as rudeness, lack of understanding, or a cunning negotiating tactic to get the Americans to talk more and make more concessions. Rather than wait for a response, the American tendency is to fill the void with words by asking questions, offering further explanations or repeating what they have already said. This may confuse and frustrate the Japanese who feel they have not been given time to respond.

In my experience, there are ten crucial areas where cultural differences may arise during the negotiation of a license agreement. It is my hope that an awareness of these ten factors may enable you to understand your counterpart when you are negotiating a license agreement or any business transaction with people from a different culture.

1. Negotiating Goal: Contract or Relationship?

Different cultures may tend to view the very purpose of a negotiation differently. For Americans, the goal of a licensing negotiation first and foremost, is to arrive at a signed licensed agreement between the parties. Americans consider a signed contract as a definitive set of rights and duties that strictly binds the two sides, an attitude succinctly summed up in the statement "a deal is a deal".

East Asians including Japanese, Chinese and Koreans, often consider that the goal of a license negotiation is not a signed license agreement, but the creation of a relationship between the two sides. Although the written license agreement expresses the relationship, the essence of the deal is the relationship itself. For Americans signing a license agreement is closing a deal; for many Asians signing a contract might more appropriately be called "opening a relationship". This difference in viewpoint may explain why Asians tend to give more time and effort to pre-negotiation, while Americans want to rush through this first phase in deal making. The activities of pre-negotiation, whereby the parties seek to get to know one another thoroughly, are a crucial foundation for a good business relationship between Americans and Asians. It may seem less important when the goal is merely a contract. In my view, the Asian attitude in this regard is far superior to that of the Americans.

2. Negotiating Attitude: Win/Lose or Win/Win?

Because of differences in culture or personality or both, licensing executives appear to approach deal making with one of two basic attitudes: that a negotiation is either a process in which both can gain (win/win) or a struggle in which, of necessity, one side wins and the other side loses (win/lose). As one enters a negotiation, it is important to know which type of negotiator is sitting across the table from you. Win/win negotiators see deal making as a collaborative and

problem solving process; win/lose negotiators see it as confrontational.

Too often officials from developing countries often view negotiations with Western multi-national corporations as win/lose competitions. They often consider license fees earned by the licensor as automatic losses to the host country. As a result, they may focus their efforts on negotiation fixedly on limiting license fees in contrast to discovering how to maximize benefits from the project for both the licensor and the licensee.

The presence of a win/lose negotiator on the other side of the table can impede licensing. Searching constantly for the negative implications of every proposal while failing to evaluate the positive side, this type of negotiator may simply take a position and refuse to budge. How should you negotiate with a win/lose deal maker?

First, you should explain fully the nature of the license agreement and in fact the licensing transaction. You should not assume that the other side has the same degree of legal, technical, or business sophistication as you do. Part of the other side's reluctance to budge from a firm position may stem from a lack of understanding of the deal and an unwillingness to show ignorance. The range of business sophistication varies dramatically throughout Asia, from the highly sophisticated negotiator of Hong Kong and Japan to the

much less experienced business persons in a country like Laos.

Second, you should try to find out the other side's real interest -- what do they really want out of the deal? Negotiators who encourage the other side to provide information about themselves, their interests and their preferences, generally achieve better results in understanding interests than those who do not.

Third, to understand the other side's interests, you need to know something about their history and culture. For example, China's troubled history of relations with the West and its justified pride and its own culture accomplishments may cause license negotiations to fail which place the Chinese party in a visible, second class position.

Finally, once you have identified the other side's interests, you have to develop creative proposals directed at satisfying those interests.

3. Personal Style: Informal or Formal

Personal style concerns the way a licensing executive talks to others, uses titles, addresses, speaks and interacts with other persons. A licensing executive with a formal style insists on addressing counterparts by their titles, avoids personal anecdotes and refrains from questions touching on the private or family lives of members of the other negotiating

team. An informal style licensing executive tries to start the discussion on a first name business, quickly seeks to develop a personal, friendly relationship with the other team, and may take off his jacket and roll up his sleeves when negotiating begins in earnest. Each culture has its own formalities, which have a special meaning within that culture. They are another means of communication among the person sharing that culture, another form of adhesive that binds them together as a community. For an American, calling someone by their first name is an act of friendship and therefore a good thing. For a Japanese, the use of the first name at a first meeting is an act of disrespect and therefore a bad thing.

Negotiators in foreign cultures must respect appropriate formalities. Generally, it is always safer to adopt a formal posture and move to an informal stance, if the situation warrants it, than to assume an informal style too quickly.

4. Communication: Direct or Indirect?

Methods of communication vary among cultures. Some place emphasis on direct and simple methods of communication; others rely very heavily on indirect and complex methods. This latter group may use figurative forms of speech, facial expressions, gestures and other kinds of body language. In a culture that values directness such as the Americans, you can expect to receive a clear and definite response to your proposals and questions. In cultures that rely on indirect communication, such as the Japanese, reaction

to your proposals may be gained by interpreting seemingly indefinite comments, gestures and other signs. What you will not receive at a first meeting with the Japanese is a definite commitment or a rejection.

The confrontation of these styles and communication in the same negotiation can lead to friction. I have seen unsophisticated Americans negotiate with highly formal Japanese in which the Americans' preference for a very direct communication and the Japanese tendency to favor indirect communication often caused considerable friction and stalemate between the two sides. The directness of the Americans is often considered as aggressiveness and insulting, while the indirectness of the Japanese is viewed often by the Americans as insincerity and not saying what they mean.

I have found that it is very important for the American side in a complex and important license negotiation with Asians to have a person involved who is sensitive to problems such as this and who can handle sensitive communications between the two sides.

5. Sensitivity to Time: High or Low?

A particular culture's attitude toward time is always a point of discussion when one is contrasting the negotiating styles of various cultures. Americans are quick to make a deal and have the expression "time is money". East Asians believe it is important to create a relationship and thus to take

time in the negotiation of a deal. It is not correct to say that some cultures "value" time more than others. Rather, they may value differently the amount of time devoted to and measured against the goal pursued. For Americans, the deal is a signed contract and "time is money" so they want to make a deal quickly. Americans therefore try to reduce formalities to a minimum and get down to business quickly. Japanese, Chinese and Koreans, whose goal is to create a relationship rather than simply sign a contract, will need to invest time in the negotiating process so that the parties can get to know one another well and determine whether they wish to embark on a long term relationship. They may view aggressive attempts to shorten the negotiating time with suspicion as efforts to hide something.

One of my favorite expressions in describing the licensing process is to say that a license agreement is like a marriage. This is my way of describing how the Asians value the relationship more than the written agreement. I believe the Asian respect for the relationship is superior to the Americans' wish to achieve a signed agreement as quickly as possible.

6. Emotionalism: High or Low?

One thing I have noticed in my experience of negotiating licensing agreements around the world is that there is a difference among cultures in their tendency to act emotionally. Clearly, various cultures have different rules as to the

appropriateness and form of displaying emotions, and these rules are brought to the negotiating table as well. It is important to learn the rules of the particular culture in which you will be negotiating. For example, in my experience, the Chinese often use shame tactics to embarrass foreigners. They may remind the foreigner of historical atrocities or they may over-emphasize an unfriendly remark or a violation of fundamental principles. It is through these shame tactics that Chinese seek to embarrass foreigners into carrying out the negotiations in their way. I have also noticed that Chinese will also feign anger in order to gain concessions. It has been my practice in negotiations throughout East Asia to refrain from making any gestures of frustrations or using abusive language. Such gestures and language are signs of defeat and weakness. Foreign negotiators who negotiate in East Asia should practice "restrained steadfastness", i.e. be firm but do so in a restrained way.

7. The Form Of Agreement: General Or Specific?

Culture factors also influence the form of the written license agreement that results from license negotiations in Asia. Generally, Americans prefer very detailed contracts that attempt to anticipate all possible circumstances and eventualities, no matter how unlikely. The Americans do this because they believe the "deal" is the contract itself and one must always refer to the contract to handle any new situations that arise. The Chinese, for example, prefer a license agreement in the form of general principles rather than

detailed rules. This is because the essence of the license agreement for the Chinese is the relationship between the parties. If unexpected circumstances arise, the parties should look to their relationship, not to the contract, to solve the problem. In some cases, a Chinese may interpret an American's drive to stipulate all contingencies as evidence of a lack of confidence in the stability of the underlying relationship.

8. Building an Agreement: Bottom Up or Top Down?

Should you begin your agreement with the establishment of general principles and proceed to specific items or should you begin your agreement with specifics such as royalty fees, guarantees, training, the sum total of which becomes the license agreement? Different cultures tend to emphasize one approach over the other.

Generally, Asians prefer to begin with an agreement on general principles while Americans tend to seek agreements first on specifics. For Americans, negotiating a deal is basically making a series of compromises and trade-offs from a long list of particulars. For the Chinese, the essence is to agree on basic principles that will guide and determine the negotiation process afterwards. The agreed upon general principles become the framework, i.e. the skeleton upon which the license agreement is built.

A difference in negotiating style is seen in the comparison of the "building down" approach and the "building up" approach. In the "building down" approach the negotiator begins by presenting the maximum deal if the other side accepts all the stated conditions. In the "building up" approach, one side begins by proposing a minimum deal that can be broadened and increased as the other side accepts additional conditions. Americans tend to favor the "building down" approach while the Japanese and other Asians tend to prefer the building up style of negotiating a contract. I tend to agree with the Asian style of first starting with an agreement in principle and then going to a more detailed contract of negotiation, especially when I am negotiating in Asia.

9. Team Organization: One Leader or Group Consensus?

In any international license negotiation, it is important to know how the other side is organized, who has the authority to make commitments, and how decisions are made. Culture is an important factor that affects how executives and lawyers organize themselves to negotiate a license agreement. Some cultures emphasize the individual while others stress the group. These values often influence the organization of each side to a negotiation. One extreme is the negotiating team with a supreme leader who has complete authority to decide all matters. American teams tend to follow this approach. Other cultures, notably the East Asians, stress team negotiation and consensus decision making. When an

American negotiates with East Asians, he may not be aware of who is the leader and who has authority to decide important matters. In the American style, the negotiating team is usually small; in the Asian style, it is often very large. For example, in negotiations in China in a major licensing agreement, it would not be uncommon for the Americans to arrive at the table with two or three persons, and for the Chinese to show up with ten or more. Similarly, the one leader American type team is usually prepared to make commitments and decisions more quickly than a negotiating team organized on the basis of consensus. As a result, a consensus type of organization usually takes more time to negotiate a deal. It has been my experience in negotiations with the Japanese that the apparent leader of the negotiation on the Japanese side is probably the individual within the Japanese team that most opposes making the deal. He has been outvoted and perhaps has placed his hanko on the ringisho upside down indicating that he will go along with the decision but he is not happy about it. Negotiating with a consensus type of organization who has an apparent leader (who is very cautious about making a deal at all) results in a very lengthy negotiation.

10. Risk Taking: High or Low?

It is obvious that certain cultures are more reluctant to take risks than others. In a license agreement, the culture of the negotiators can affect the willingness of one side to take risks in the negotiation -- to divulge information, to try new

approaches, tolerate uncertainties in a proposed course of action, etc. Japanese for example, with their emphasis on requiring large amounts of information and their intricate group decision making process, tend to be very reluctant to take risks. Americans, by comparison, are risk takers. If you sense that the other side is reluctant to take any risks, you should focus your efforts or proposing rules and mechanisms that will reduce the apparent risks in the deal for them.

How to Cope with Cultural Differences

So far I have related to you how culture can affect deal making and would now like to spend a little time on some of the ways that I have learned cope with culture.

1. Learn the other side's culture.

In any license negotiation it is important to learn something about the other side's culture. Ideally, learning a culture other than your own requires several years study, mastery of the local language and prolonged residence in the country of that culture. An American faced with the task of negotiating licenses with 20 or 30 different countries over his career cannot master any of the cultures in the short time that it allotted. At best, he or she can only learn enough to cope with some of the principle effects that local culture may have on reaching an agreement.

History is an important window on an country's culture so, at the very least, one should study some history of the country in which he will be negotiating. Time permitting, he might also review anthropological studies, political reports, and any accounts which might relate to negotiating with that particular country.

Consultation with experts who have had experience in the country in question can also be helpful. International banks and accounting firms can be excellent sources of advice as can the Dept. of State or the local U.S. embassy or consulate. Finally, if you have hired a local legal representative, business consultant or interpreter to work on the license agreement with you, they can also explain how the local culture might affect the negotiating process, communications between the parties, the structure of the transaction and the implementation of the license agreement itself.

2. Don't stereotype.

If the first rule in international license negotiations is to "know the other side's culture" the second is to "avoid over-reliance on that knowledge". For example, not all Japanese evade giving a direct negative answer, and not all Chinese engage in "shaming" during negotiations. In short, the negotiator who enters a foreign culture should be careful not to allow cultural stereotypes to determine his or her relations with the local business representatives. Foreign business executives and lawyers will be offended if they feel

you are not treating them as individuals, but rather as members of a particular ethnic group. In addition to offending your counterpart, cultural stereotypes can be misleading. Often, the other side simply does not run true to the negotiating form suggested by books, articles and consultants. Other forces besides culture may have influenced this person's negotiating behavior. Be prepared to encounter surprises such as this.

3. Find ways to bridge the culture gap.

Generally, executives and lawyers who confront a culture different from their own in a license negotiation tend to view it one of three ways: as an obstacle, weapon or a fortress. Cultural differences are hardly ever seen as positive in the conventional view. Most Americans feel that cultural differences are an obstacle to the agreement and to effective joint action. They therefore search for ways to overcome the obstacle. But, a different culture can become more than an obstacle; it can become a weapon when a dominant party tries to impose its culture on the other side. For example, an American lawyer's insistence on structuring a license agreement "the way we do it in the United States" may be considered by foreign counterparts as the use of the American culture as a weapon. A party to a license agreement who is faced with the culture that it perceives as a weapon may become defensive and try to use its own culture as a fortress to try to protect itself from what it perceives as a cultural

onslaught. The Japanese often adopt this approach when confronted with American demands.

I believe that cultural differences should be thought of in another way. These differences can be viewed as having created a gap between persons or organizations. And an effective license negotiator should find ways to bridge the gap. I like to think that an effective negotiator is a bridge builder. People faced with cultural differences often take action to widen the gap. The English poet, Philip Larken said "Always it is by bridges that we live". Effective joint action among persons and organizations of different cultures requires a bridge over the culture gap. One way to build that bridge is by using culture itself. The creative use of culture between persons of different cultures is often a way to link those on opposite sides of the cultural gap. The object is to create community (i.e. a common ground or a common understanding) with the other side. I would like to describe four types of cultural bridge building that a licensing executive should consider when confronted with a cultural gap in a license negotiation:

a) Bridge the gap using the other side's culture

One technique for bridging the gap is for a negotiator or manager to try to assume some or all of the cultural value characteristics of the foreign person with whom she or he is dealing. If for example an American company has a successful Chinese American within its organization, it can be

helpful to bring that Chinese American along to a negotiation in China. In such way, you can express in ways other than words that you understand and value the culture of the side and therefore can be trusted.

b) Bridge the gap using your own culture

Another approach to building a culture gap is to persuade the other side to adopt some elements of your culture. For example, an American partner may send executives of its foreign partner to schools and executive training programs in the United States and then assign them for short periods to the U.S. partner's home operations. Sohio did this with one of its main partners in China, and the result was very positive.

c) Bridge with some combination of both cultures

Another approach to dealing with the culture gap is to build a bridge using elements from cultures of both sides. In effect, culture bridging takes place on both sides of the gap and hopefully results in the construction of a solid integrated structure. The challenge is to identify the important elements of each culture and to find ways of blending them into a consistent, harmonious whole that will allow business to be done effectively.

In my experience with Sohio I converted several of my Chinese counterparts to the "American way", and I indicated to these same counterparts that I appreciated and understood

the Chinese (to a greater extent than most Americans), enjoying Chinese food tremendously and looking positively on my experiences in China both with respect to its magnificent history and scenery and also to its very open, friendly and creative people.

d) Bridge with a third culture

Another method of dealing with the culture gap is to build a bridge relying on a third culture that belongs to neither of the parties. For example, you and your Asian counterpart may have had educational or work experiences in a third country, e.g. France. This common knowledge and understanding may help bridge the culture gap.

Summary

What began when I first went to Asia to negotiate a license agreement for my company and continues today has been nearly 25 years of adventure, occasional exhaustion, constant challenge and very rewarding experience. I have tried in the past few minutes to communicate with all of you the appreciation I have gained over these 25 years for the cultural differences between Americans and Asians. These cultural differences have a profound effect on license negotiations and one who understands them well and copes with them in a positive way can be very, very successful in licensing in Asia. The United States continues to be the world's most important market, and Asia continues to be the

world's most important manufacturing region. It is essential that we learn to work well with each other; to continue the trend toward more and more cultural and technical exchanges; and to build on each other's strengths and to help each other eliminate its weaknesses. I hope that international licensing executives can join with me to act as bridges between our cultures and to help not only the licensing process but the process of understanding between our people.