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Edward P. White

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A Brief Look at Licensing with the Communist Countries

by Edward P. White*

I. Introduction

Communist countries present a unique market for American sellers and purchasers of technology. Licensing opportunities for American firms in communist countries are more limited, however, than opportunities in non-communist countries. Political considerations, such as U.S.-U.S.S.R. relations, and unstable economies, such as that of Poland in 1982, affect the possible benefits of licensing transactions, and hence, affect the interest of American buyers and sellers of technology. Nevertheless, so long as the opportunity to engage in profitable business transactions exists, there will always be some firms willing to conduct business with the communist countries. Therefore, it is useful for attorneys to know how to handle licensing transactions involving a communist country, and to have a reasonable understanding of what is expected in such a relationship. Whether the transaction undertaken is a technology sale, commonly referred to as a licensing out, or a technology purchase, referred to as a licensing in, some familiarity with the approach of state-controlled economies to the licensing and purchase or sale of technology is necessary.

This article provides a broad overview of considerations which U.S. firms should consider when engaging in licensing agreements in the U.S.S.R., Poland, the German Democratic Republic (East Germany), Czechoslovakia, Hungary, Bulgaria, Yugoslavia, and the People's Republic of China (PRC). Factors of particular relevance to Romania, Yugoslavia, and the PRC are addressed in separate sections below. While these countries are all communist nations, each has its own particular business interests and its own particular approach to business situations. For example, Yugoslavia has managed to stay out of the immediate in-

* Chairman, KEW Associates (a management consultant firm in the field of licensing, technology transfer, and other international business), Chapel Hill, North Carolina; B.E. 1941, Cornell University School of Civil Engineering. This article was co-authored by Leslie R. Carter, Executive Editor, North Carolina Journal of International Law and Commercial Regulation.

fluence of the U.S.S.R.¹ and enjoys special trading relations with the United States.² In some ways, Yugoslavian business is oriented to a capitalistic philosophy. For instance, one growing engineering firm in Yugoslavia elected to take a ten percent cut in salary for all employees in order to raise capital for expansion of the firm's business.³ A number of other communist nations have also enjoyed special trading relationships with the United States. Romania, although a full member of the Soviet Bloc, Council of Mutual Economic Assistance (CMEA),⁴ enjoys the U.S. most-favored nation status,⁵ as does Hungary.⁶ Until recently, Poland also enjoyed the most-favored nation status with the United States.⁷

Of the nine countries discussed herein, the People's Republic of China generates the greatest interest among U.S. firms, and probably represents the greatest potential for a profitable trade increase with the United States. For that reason, this review discusses the licensing of technology in China in some detail.

Where patent systems exist, licensing agreements may be negotiated on the basis of patent coverage, patent plus know-how, or solely on know-how. Where patents do not exist or where patent coverage is weak, know-how licenses are all that is possible, and contracts for technology transfer must be drawn accordingly. The U.S.S.R.⁸ and the East European countries⁹ have useful patent systems which help in license definition. The People's Republic of China, on the other hand, has no patent system and requires that any know-how protection be written specifically into the license agreement. It is strongly rumored that China will enact a patent law in 1983,¹⁰ but such "yearly predictions" also emerged during the preceding three years.

II. Common Government Organizations

In order to expedite licensing, each country has one or more Foreign

¹ See generally L. NORD, *NONALIGNMENT AND SOCIALISM: YUGOSLAV FOREIGN POLICY IN THEORY AND PRACTICE* (1974).

² See Treaty of Commerce, Oct. 14, 1882, United States-Serbia, 22 Stat. 963, T.I.A.S. No. 319.

³ This situation was called to Mr. White's attention in a personal conversation while visiting Zagreb, Yugoslavia in November, 1972.

⁴ LICENSING EXECUTIVES SOCIETY (U.S.A.), INC., UNITED STATES/EASTERN EUROPE: TECHNOLOGY AND PATENTS SALE AND/OR LICENSING 142 (1977) [hereinafter cited as U.S./EASTERN EUROPE].

⁵ Agreement on Trade Relations, April 2, 1975, United States-Romania, art. I, § 2, 26 U.S.T. 2305, T.I.A.S. No. 8167.

⁶ Agreement on Trade Relations, March 17, 1978, United States-Hungary, art. I, 29 U.S.T. 2711, T.I.A.S. No. 8967.

⁷ Proclamation No. 4991, 47 Fed. Reg. 49005 (1982).

⁸ See LICENSING EXECUTIVES SOCIETY (U.S.A.), INC., U.S./U.S.S.R. TECHNOLOGY AND PATENTS: SALE AND LICENSE PROSPECTS 78 (1974) [hereinafter cited as U.S./U.S.S.R.].

⁹ See, e.g., U.S./EASTERN EUROPE, *supra* note 4, at 189.

¹⁰ See E. White, *China-Opportunities for Technology* 23 (1982) (Paper no. ICTTE-82-228, presented at the International Congress on Technology and Technical Exchange, Pittsburgh, Pa., May 3-6, 1982).

Trade Corporations (FTCs) specifically responsible for the field of licensing, such as Licensintorg in the U.S.S.R.,¹¹ Licencia and Novex in Hungary,¹² and China National Technical Import Corporation (CNTIC) in the People's Republic of China.¹³ The primary contact with the communist country will be through the FTC, which handles the transfer of technology. The FTC is organized as a profit center or separate enterprise and will probably be the organization which signs the contract. A contract with the FTC of a communist country is, in effect, a contract with the government, and the communist governments recognize that their reputation in both political and commercial matters is impugned when such a contract is broken, violated, or changed in any manner.¹⁴

Prior to entering into contractual relations, a licensor or seller of technology should contact all agencies involved with the technology, not the licensing FTC alone. For instance, the government ministry involved with the particular type of technology should be contacted to assist in ascertaining the needs of the marketplace. In addition, the embassies and commercial offices of the countries involved should be contacted to insure that all appropriate government contacts have been made.

III. Contract Negotiation and Drafting

Contract negotiation with a communist country may be extremely difficult. FTCs of communist countries are well versed in pressure techniques and negotiation "twists."¹⁵ Negotiators should be prepared for "side-by-side" negotiation of a contract, where one or more competitors concurrently negotiate for the same contract in different rooms of the same building. Contract drafting also presents some unique problems. For example, what is the legal consequence of a Force Majeure clause in a contract with a communist country? If by definition the country is atheist, it is difficult to have an "Act of God." Unless specifically provided in the contract, the communist country may not recognize strikes as a legitimate delay in performance.¹⁶ Through careful drafting, however, it is possible to get reasonable Force Majeure protection, albeit under a different name. Problems may also arise in drafting provisions for dispute resolution. For example, the PRC exhibits an inherent suspicion of courts, and legal institutions are regarded as "coercive instruments."¹⁷ Consequently, the Chinese consider even an arbitration proceeding undesirable. Contracts with the PRC must provide for

¹¹ U.S./U.S.S.R., *supra* note 8, at 128.

¹² U.S./EASTERN EUROPE, *supra* 4, at 120.

¹³ INTERNATIONAL TRADE ADMINISTRATION, U.S. DEP'T OF COMMERCE, DOING BUSINESS WITH CHINA 6 (1980) [hereinafter cited as DOING BUSINESS WITH CHINA].

¹⁴ U.S./EASTERN EUROPE, *supra* note 4, at 20-21.

¹⁵ See generally U.S. DEP'T OF COMMERCE, COMMUNIST COUNTRY NEGOTIATING TACTICS (1980).

¹⁶ See DOING BUSINESS WITH CHINA, *supra* note 13, at 14.

¹⁷ George, Gullo & Stein, *Trade with the People's Republic of China: Current Status and Future Prospects*, 3 NW. J. INT'L L. & BUS. 21, 26 (1981).

"friendly conciliation" and should spell out the process for such conciliation.

The contract should provide for the necessary government approvals of the agreement. The contract should require the FTC of the communist country involved to obtain and guarantee all clearances, approvals, and registrations required by its own country. When the contract is a sale of U.S. technology, the exporting firm must obtain a U.S. Export Control License.¹⁸ The penalties for failing to obtain such a license are severe.¹⁹ Although other agencies are involved, the U.S. Department of Commerce is the primary approving agency for exporting technical information to communist countries.²⁰ According to present reports,²¹ technical information license requests that could conceivably involve U.S. strategic defense will be returned without action or explanation. Non-strategic subjects will be accepted for consideration on a standard schedule of detailed review, which may require several months for completion. In general, over the past two to four years, a number of applications for export of technical information to the PRC have been approved. On the other hand, requests to export technical information to Soviet Bloc countries are regarded with considerable restrictions.²²

IV. Romania, Yugoslavia, and the People's Republic of China²³

A. Romania

A serious problem in exporting technology to Romania is created by a provision in a 1974 law which relates to protection of substances obtained by chemical means, medical products or treatments, and new species of plants or bacteria.²⁴ Such products are only patentable to Socialist state organizations with no national treatment for foreign investors. Other problems include recipe type claims, adding examples to support scope, and unity of invention (*e.g.*, solid versus liquid formulations).²⁵

¹⁸ See 50 U.S.C. § 2401-2420 (Supp. V 1981); Export Licensing General Policy and Related Information, 15 C.F.R. § 370 (1982). Forms necessary to conduct business in accordance with Export Administration Regulations are available from all U.S. Department of Commerce District Offices and from the Office of Export Administration, U.S. Department of Commerce, Washington, D.C., 20230. *Id.* § 370.12.

¹⁹ See 50 U.S.C. app. § 2401 (Supp. V 1981).

²⁰ See Exec. Order No. 12,214, 3 C.F.R. 256 (1980).

²¹ Conversations between Mr. White and Department of Commerce Personnel, Fall 1982.

²² 50 U.S.C. app. § 2403-1(d) (Supp. V 1981) denominates the Soviet Union and other countries as "controlled countr[ies]," thus triggering various other provisions of the Export Administration Act. See, *e.g.*, 50 U.S.C. § 2403-1(b) (Supp. V 1981).

²³ These sections were exempted from the East European and People's Republic of China workshops held during the 1982 Licensing Executives Society annual meeting, held Oct. 12-14, 1982, at San Francisco, California. The only conclusion to be drawn from these and similar reports is that the situation, as normal, is in a state of change.

²⁴ See Legea nr. 62 Privind Inventiile Si Inovatiile (Romania, Oct. 30, 1974), §14(b), reprinted in English in 14 *Indus. Prop.* 306, 307 (1975).

²⁵ See U.S./EASTERN EUROPE, *supra* note 4, at 158-59.

B. *Yugoslavia*

A new Yugoslav patent law became effective December 20, 1981.²⁶ All patents granted before the effective date are subject to the new law, except that the fifteen year term contained in the prior law remains applicable to patents acquired prior to enactment of the new law.²⁷ New patents have a seven year term from publication (after 18 months).²⁸ An extension for seven years is possible on satisfactory proof of "conscientious working."²⁹ Under the new law, importation itself is not conscientious working.³⁰

A compulsory license is available for non-working patents four years after the patent filing date or three years after grant, whichever is later.³¹ A compulsory license is not exclusive³² and the patentee receives compensation.³³

After any license grant, the licensor cannot prevent the licensee from entering into the "work pool" with any other State Labor Organization.³⁴

The new law also provides for Inventor Certificates.³⁵ Chemical products, pharmaceuticals, pesticides, and microorganisms are unpatentable.³⁶

C. *The People's Republic of China*

In pursuing a licensing agreement with the People's Republic of China (PRC) the following organizations should be contacted:

- China Council for Promotion of International Trade (CCPIT)
- China International Trust and Investment Corporation (CITIC)
- China International Economic Consultants (CIEC)
- China Trade Consultation and Technical Services Corporation (CONSULTECH)
- Major Cities and SEZ's (Special Economic Zones) which will have offices of ministries, local development groups, and enterprises with certain autonomous local authority.³⁷

The plethora of organizations and the apparent overlap of responsibilities in China is confusing. China's state-controlled economy does not

²⁶ Law on the Protection of Inventions, Technical Improvements, and Trademarks (Yugoslavia 1981) (Unofficial English translation obtained from the U.S. Embassy in Belgrade, Yugoslavia).

²⁷ *Id.* art. 176.

²⁸ *Id.* art. 93.

²⁹ *Id.* art. 51.

³⁰ *Id.*

³¹ *Id.* art. 142.

³² *Id.* art. 140.

³³ *Id.* art. 144.

³⁴ *Id.* art. 136.

³⁵ *Id.* art. 71.

³⁶ *Id.* art. 23.

³⁷ See generally LICENSING EXECUTIVE SOCIETY, INC., U.S.A. AND CHINA: TECHNOLOGY AND PATENTS SALE AND LICENSE (1981).

operate with the same monolithic structure as the economies of other socialist countries. One Chinese official made the point quite clearly when he said, "China used to have a monopoly system, but competition today is good—today there is room for all kinds of competition in China—competition even between the provinces and the central government."³⁸ In April 1982 a special delegation from China visited the United States to review with potential business partners a list of 130 projects on which China would like to establish joint ventures with foreign partners.³⁹ The projects range from "marble mining" to medical instruments, polypropylene film and microcomputers.

As previously mentioned, the PRC has no patent law currently in effect. A significant obstacle to the approval of any patent law in the PRC is philosophical, *i.e.*, the difficulty in a communist society of accepting a capitalistic system of property ownership. In addition, China has no historical legal background comparable to the Western laws relating to social and business conduct.⁴⁰ Present rumors indicate, however, that China will publish a patent law sometime during 1983,⁴¹ and China is diligently engaged in expanding its legal codes and regulations to resemble more closely standard Western practices.⁴²

V. Initial Contacts

The U.S. Department of Commerce (DOC) is the most useful point of reference for business contacts in the communist countries. The specific country information desks are knowledgeable, and the trade specialists in the DOC can be very helpful. In addition, the DOC may provide significant background information for contract drafting. Other assistance, both legal and trade, can be found with the pertinent U.S. trade councils such as the National Council for U.S.-China Trade in Washington⁴³ and the U.S.-U.S.S.R. Trade and Economic Council in New York.⁴⁴

VI. Conclusion

The only viable yardstick of success in a technology transfer to a communist country is the profitability of the transaction. The communist countries are not a market for small jobs. Profitability depends on the customer's desire for the license, the amount of time and effort necessary to procure the contract, and the probability of the potential gain

³⁸ White, *supra* note 10, at 5.

³⁹ *Id.* at 8-10.

⁴⁰ *Id.* at 17-18.

⁴¹ *Id.* at 23.

⁴² See George, Gullo & Stein, *supra* note 17.

⁴³ National Council for U.S.-China Trade, Suite 350, 1050 17th Street, Washington, D.C., 20036. Phone (202)-828-8300.

⁴⁴ U.S.-U.S.S.R. Trade and Economic Council, 1211 Avenue of the Americas, New York, New York, 10036. Phone (212)-840-5500.

weighed against the risk of loss. While negotiations may be shorter in purchasing technology from communist countries, the need for a well-drafted contract remains.

In negotiation and drafting technology transfers to and from communist countries, attorneys and businesses may encounter a myriad of regulations and bureaucracies, both within the United States and within the communist country. The parties should take particular care to see that all regulations are complied with as well as insuring that the burden of compliance is allocated to the appropriate party to the transaction. Unless the potential profits are great, the large amount of time spent on negotiating and effecting a transfer to a communist country may be wasted.

Despite the difficulties, communist countries offer reasonable trading opportunities to some U.S. concerns. China, for example, has the resources,⁴⁵ the expressed need to develop its industries,⁴⁶ and a potential market of one billion people⁴⁷ which U.S. business and industry can scarcely afford to disregard. Regardless of political differences, and barring any major conflict, the Soviet Union will remain a potential market for certain U.S. technology. The CMEA countries of Eastern Europe will also, in varying degrees, be markets for patent licenses and technology sales. In addition, all of these countries have and will continue to develop technology which is of interest and value to U.S. business and industry. The alert, well-grounded lawyer must, therefore, be prepared to advise his clients on these markets. For those who can afford the risks, there are the opportunities for trade with the communist countries.

⁴⁵ White, *supra* note 10, at 93-101.

⁴⁶ *Id.* at 8-10.

⁴⁷ POPULATION REFERENCE BUREAU, INC., 1982 WORLD POPULATION DATA SHEET (1982).

