

East-West Joint Ventures

*Discussion of various legal forms
East-West trade in technology
takes, with emphasis on newest
developments*

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I. THE COMMERCIAL SETTING

A. The Structure of Foreign Trade in the East

The structure of foreign trade in Socialist countries is quite different from that encountered in most of the Western world. Because of its distinctive features, this organizational framework should be clearly understood by the American businessman or attorney contemplating an East-West trade transaction. Since the central government in these countries directs the entire economy, it is not surprising that foreign trade is a state monopoly, administered through the ministry of foreign trade in each country.

The ministry of foreign trade generally works in conjunction with the foreign trade bank and the state planning commission in drafting five-year and annual foreign trade plans which are part of the corresponding overall economic plans. The five-year foreign trade plans give general guidelines, while the annual plans are more specific and detailed. Export and import targets are set and draft plans are sent to the foreign trade organizations and other organizations engaged in foreign trade for their suggestions and comments. The final decisions are made at the higher levels and the plans then distributed to the organizations which actually conduct the country's foreign trade. The import plan, with which Western firms are most concerned, gives the volume of planned purchases of specific products, including technology, from Western countries. The goal of the Western trader is to be "written in" to the plan by convincing the end-user enterprise, the relevant industrial ministry, the appropriate foreign trade organization, and ultimately the state planning commission that his product will fill an essential need in the economy that can't be filled domestically. Part of the problem in discovering the requirements and needs of the economy in each country stems from the fact that the annual economic plans are not readily available, while the five-year plans are too general to be of much guidance.

As suggested, the actual conduct of foreign trade is in the hands of a network of juridically independent foreign

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trade organizations (FTOs). These FTOs are specialized export-import corporations organized along commodity lines, each enjoying an exclusive right to deal abroad in its commodities or services. In most of the Socialist countries there is a specialized FTO dealing exclusively in the licensing of industrial property rights. For example, in the USSR this FTO is Licensintorg, in Poland it is Polservice. Any transaction involving a simple transfer of technology through licensing of patent rights or know-how will be

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handled by this licensing FTO. If, however, the transaction involves more than simple licensing, such as the construction of a turnkey plant employing the licensed technology or a joint venture based on the technology transfer, the contracting party on the Eastern side is likely to be the FTO that normally handles the subject matter or product of the agreement. In some Eastern European countries other economic entities, such as cooperative associations and large industrial enterprises, are authorized to carry on foreign trade independent of the FTOs, and they may be involved in a transaction involving technology.

Under an exclusively FTO system such as in the USSR, all foreign trade transactions are handled by the relevant FTO, which is essentially only an intermediary trading company. In accordance with the structure of the annual plan, discussed above, the FTO will negotiate and sign purchase and sale contracts with Western firms. Despite the seeming inflexibility of the plan, a certain amount of "give" is built in to allow for changes in needs and requirements. Thus an unanticipated shortfall in production of a certain product might result in a purchase not called for in the plan.

Industrial Property Rights In the Socialist World

The Soviet Union and all of the Eastern European countries, with the exception of Albania, are parties to the Paris Convention for the Protection of Industrial Property of 1883 (Paris Convention), the major international agreement on the subject. Under the Paris Convention, nationals of one signatory country are entitled to receive the same treatment under another signatory country's industrial property laws as that country extends to its own nationals. Perhaps of most importance, the Paris Convention includes a priority system by which a foreigner who has filed a patent application in one signatory country is allowed one year (six months in the case of trademarks) in which to file in any other signatory country and still maintain his first filing date. Indeed, an increasing number of Western companies are making it a practice to file patent applications in the Soviet Union and other Eastern European countries as well as in the West. It is interesting to

note that, while know-how is not covered by the Paris Convention or any other international agreement, the Socialist countries are coming to recognize it as a valuable form of industrial property. Registration of foreign patents and trademarks in some Socialist countries, such as the U.S.S.R., is handled through the national chamber of commerce, which in such cases acts as agent for the foreign applicant. In other Socialist countries the applicant must retain local patent counsel to represent him.

Similar to West

Most of the basic patent system rules in the Socialist world are not substantially different from those in the West. The applicant must demonstrate the novelty of his invention, and provision is made for opposition to the granting of the patent. As elsewhere, patent protection is limited to a specified period, generally 15-20 years. Periodic payment of fees is required to maintain the exclusive rights granted by the patent. In some of the Socialist countries the patent must be "worked" within a certain period of time or be subject to revocation or compulsory licensing. However, revocation or compulsory licensing of locally registered foreign patents is rare in the Eastern countries.

In addition to the patent, which can be obtained in the U.S.S.R. and all the Eastern European countries, several of the Socialist countries have adopted an "inventor's certificate" system. Under such a system the ownership of the invention is transferred to the state in exchange for certain compensations and privileges based on the invention's usefulness. Use of the inventor's certificate system has been generally limited to nationals of the particular country, while foreigners usually seek patents because they may offer the prospect for a greater financial return. I am aware of at least one case, however, in which an American attorney is now in the process of filing for an inventor's certificate in the U.S.S.R. on an experimental basis. One problem is that payment by the Soviets in such a case will be in rubles only, with no possibility of conversion into dollars.

II. TECHNOLOGY TRANSFER TECHNIQUES

Cooperation and Licensing Agreements

Because of their desire to acquire advanced Western technology while at the same time limiting hard currency expenditures, the Eastern countries have shown a growing interest in various types of industrial cooperation involving technology transfers. Leading the way, the U.S. government recently signed several government-to-government agreements with Socialist countries calling for cooperation in the exchange of technology in various areas of mutual interest. Concurrently, there has been an increase in the number of commercial agreements involving the private sector in the field of East-West technology transfer.

The Soviet interest in Western technology has been especially evident in the conclusion in recent years of a series of science and technology cooperation agreements with Japanese, Western European and American firms. These agreements are signed on the Soviet side by the State Committee for Science and Technology, which supervises and coordinates research and development in

the U.S.S.R. While not binding contracts in the legal sense, these agreements call for exchanges of scientific and technical information, exchanges of visits by scientists and technical specialists on both sides, joint research and development, and other forms of cooperation which might lead to specific contracts. The Soviets have sought out as partners for such agreements leading Western companies in various fields of technology. Whether these agreements will lead to a larger volume of actual business for the Western partner in the sense of firm contracts or to an actual return flow of technology from the U.S.S.R. is still an open question. It appears that most of the roughly 40 U.S. companies with such agreements tend to view them as more of a marketing tool than anything else.

Most Conventional Form

The most conventional form of cooperation agreement involving technology transfer is the simple licensing agreement. While the emphasis in the past has always been on the purchase of technology licenses by Eastern countries, there has been a marked increase in the number of recent transactions in which the Soviets and other Eastern Europeans are the licensor. For example, several U.S. companies have purchased Soviet-developed electroslag remelting technology for use in the steel industry and the FTO Licensintorg has recently been successful in licensing its technology to produce cold-rolling equipment for industrial tubing. Nonetheless, the primary interest on the part of U.S. companies continues to be the sale of technology to the East.

Turnkey Plants

The tendency today is for Eastern purchasers of technology to favor technology packages rather than simple patent licenses. In some cases this may involve the licensing of know-how connected with the use of equipment which the Western party is also supplying. Often the transaction will take the form of the purchase of a modified turnkey plant. In this type of project the Eastern party is buying a complete facility including equipment, know-how, and any patent rights connected with the production of a particular product. (This is described as a modified turnkey plant since the Eastern buyer generally supplies the actual building, including utility hookups, to the seller's specification. In a turnkey project in the West, plant construction would normally be the responsibility of the seller.)

Recent publicized examples of the modified turnkey approach include a contract between Gould, Inc. of Cleveland, Ohio and the Soviet FTO Stankoimport for a plant to produce engine bearings and contracts between A. Epstein Co. of Chicago, Illinois and the Polish FTO Polimex-Cekop for several slaughter and meat processing plants. Many more such contracts are currently under negotiation between U.S. companies and Socialist FTOs.

Joint Ventures

A form of cooperation agreement, often involving technology transfer, with which most Western businessmen are familiar is the traditional joint venture with ownership and management rights vested in the coventurers. Many of the Socialist countries will consider establishment of traditional joint-venture enterprises with Western partners in third countries. But for ideological reasons, they have not

permitted joint ownership and management of enterprises within their own territory. In an effort to bridge an ever-widening industrial technology gap and to narrow their trade imbalances with the West, however, three Socialist countries, Yugoslavia, Romania, and Hungary have enacted new legislation which permits local establishment of something akin to Western-style joint ventures.

Yugoslavia was the first Socialist country to enact a law permitting foreign capital investment. Since the effective date of the original Yugoslav law, July 27, 1967, over 100 joint-venture contracts have been signed by Western companies. Under present Yugoslav legislation, the joint-venture contract does not actually vest ownership rights in the foreign party. Rather, the foreign party signs a contract with his Yugoslav partner establishing a joint venture through which he contributes his capital to a domestic Yugoslav enterprise, which can be an existing enterprise, an existing or future organizational unit of a Yugoslav enterprise, or a future enterprise. The relationship created by this arrangement does not result in joint ownership of the unit or enterprise. Unlike the situation in Romania and Hungary, no stock certificates may be issued to the parties which would connote joint ownership. The foreign party's relationship remains basically a contractual one with his Yugoslav partner.

Investor Retains Rights

On the other hand, though the Yugoslav legislation is silent on the subject, it appears that the foreign investor does retain certain rights in the assets he has invested. These rights include the right of participation in and repatriation of profits and the right of repatriation of capital. The foreign party's profits are subject to Yugoslav taxation, but there are special provisions which reduce the regular rate of 35 percent if more than 20 percent of the profits are reinvested in the joint venture or if the investment is in one of the so-called "underdeveloped" Yugoslav republics, such as Montenegro.

In terms of management rights, most Yugoslav joint ventures have provided for establishing a joint-business board having decision-making power in the area of production and sales. The joint-business board may have equal representation by both parties regardless of the actual capital contributions of the parties. (The foreign party is limited to 49 percent of the total capital participation.) While the joint-business board does have certain management powers, the traditional Yugoslav institution of the Worker's Council of the enterprise retains responsibility for most other matters. It is possible contractually, however, to require the Worker's Council to get joint business board approval before it exercises certain of its powers.

Joint ventures in the fields of industry, agriculture, construction, tourism, transportation, and scientific and technological research may be established in Romania under the new foreign trade law of March 1971, in accordance with two implementing decrees issued in November 1972. Decree 424 covers the constitution, organization, and operation of joint companies, while Decree 425 sets forth regulations for taxation of the profits of these companies. As of now, five Western companies have established joint ventures in Romania.

The joint venture can be organized as either a joint-stock company or a limited-liability company under

Romanian law. The joint-stock company issues stock certificates to the coventurers reflecting their respective ownership interest. In the case of the limited-liability company, capital subscription is set forth in the joint-venture contract between the parties, but is not evidenced by stock certificates. In both cases the contribution of the foreign party is limited to 49 percent. The limited-liability company is governed by a management committee and, unlike the joint-stock company, usually does not have a board of directors. However both types of company do hold general shareholders meetings. It appears that the Romanians prefer the limited-liability approach, and the first Romanian joint venture with a U.S. company, Control Data Corporation, was set up as a limited-liability company.

The question of the management of the joint venture is dealt with only in general terms in the Romanian legislation. While the general meeting of shareholders called for by Decree 424 seems to possess most of the basic decision-making power, in fact, the real managerial authority is delegated to the management committee in the case of a limited liability company or to the board of directors in the case of a joint-stock company.

As regards taxation of profits, Decree 425 establishes a basic rate of 30 percent, which is reduced to 24 percent in the case of profits reinvested for at least five years in the joint venture or in another Romanian joint company. A full tax exemption for the first year in which profits are earned and a one-half exemption for the next two years may be granted by the Romanian Council of Ministers. There is an additional 10 percent tax levied on those profits which are repatriated by the foreign party.

Hungarian Regulations

Hungary is the third Eastern European country which allows establishment of economic concerns with foreign participation. A decree issued in October 1972 sets forth the procedures for the creation of joint ventures, and provides detailed financial regulations concerning their operation. Since the decree was issued, two joint ventures have been established in Hungary, one by Siemens of West Germany and one by Volvo of Sweden.

As in the case of Romania and Yugoslavia, participation by the foreign party is generally limited to 49 percent. One unique aspect of the Hungarian joint-venture provision is that it doesn't allow direct foreign participation in production except with the specific permission of the Council of Ministers. Instead, the joint-venture company may make separate contracts with Hungarian enterprises which carry out the production of goods. To see how this works in practice, it is instructive to examine the case of the Volvo joint venture. It appears that the joint-venture company itself acts essentially as a holding and trading company to which Volvo provides, under separate contract, capital, know-how, licenses and special machinery. At the same time production facilities, labor, and capital are provided, again under separate contracts, by the two Hungarian partners, one of which carries out the actual production of four-wheel drive vehicles. The vehicles are then sold to the joint-venture company, which in turn resells them to Volvo.

The Hungarian joint-venture decree does not go into detail as to management rights in the joint-venture company, and a statement by the Hungarian Ministries of Fi-

nance and Foreign Trade issued the same day as the decree says only that "... the company will be directed by a body consisting of representatives of the Hungarian and foreign partners." Presumably this leaves a great deal of leeway for the parties to agree upon and write into their joint-venture contract a management setup they find mutually acceptable.

Joint-venture companies in Hungary are taxed at the rate of 40 percent of annual net profit if the profit does not exceed 20 percent of the capital of the company and 60 percent of the profit exceeding the 20 percent figure. The joint company can petition the Ministry of Finance to exempt taxes on profits which are reinvested in the company, but the joint-venture law gives no indication as to the scope of this relief.

Other types of Industrial Cooperation

While most of the Socialist countries will not permit joint ownership and management, they are receptive to other types of industrial cooperation. One form of cooperation agreement that is gaining in favor involves the construction of a new production facility, such as the modified turnkey plant discussed previously, with deferred repayment in output from the new facility. A variation on this is the natural-resource-development projects being pushed by the Soviet Union. The Western party helps the Soviets to develop natural resources, generally in Siberia and the Soviet Far East, and in return receives long-term payment in product at prearranged prices. An example of this type of arrangement is Soviet-Japanese cooperation in the exploitation of coal reserves in Eastern Siberia. The Japanese companies are supplying the equipment and technology for the project in return for deliveries of coke and coal over a 20-year period. International Paper Company is currently negotiating with the Soviets on a similar project involving pulp and paper production in the Krasnoyarsk region of Central Siberia.

Another type of industrial cooperation is the coproduction agreement. Under such an agreement, the Western party might supply the technology to produce certain components which would be integrated into the Western company's end product. Final assembly of the product could take place in either country, and marketing of the product might be handled by the Western party's established sales network. Several Western manufacturers of heavy construction equipment have signed such coproduction agreements with Polish organizations.

III. PROBLEM AREAS IN EAST-WEST TRADE CONTRACTS

In this section I shall discuss some contract drafting problems that frequently occur in East-West technology trade. It should be remembered that preliminary technical discussions with Eastern end users which usually precede an East-West transaction may be carried on for months with very little consideration of specific commercial issues. Contract terms other than price may not even be discussed at this stage since they are not of consuming interest to the scientists and technicians. The situation changes, of course, once technical discussions have been successfully concluded and the actual contracting party on the Eastern side, normally the FTO, enters the arena.

When negotiations with a Western firm reach the stage of strictly commercial matters, the FTO will usually offer one of its form contracts and urge its adoption. Most FTOs have several variations of their form contract, each suitable for a different type of transaction. The forms which are used for transactions involving technology transfer, such as licensing agreements and turnkey contracts, tend to be more complex and detailed than those designed for simple equipment purchases. It should be noted that the provisions of all of these form contracts cover only the basic commercial terms of the transaction. Often there are extensive appendices covering matters such as technical specifications of the equipment and technology being purchased, installation and commissioning of equipment and the training of buyer's personnel.

Contracts Vary

Form contracts vary from country to country and from FTO to FTO within each country. Yet there are many common elements in all the forms, since they are in large measure based on the COMECON General Conditions. (The COMECON General Conditions are a codification of trade practices which carry the force of law in trade between the members of COMECON, the Socialist equivalent of the EEC.) Eastern parties are often quite insistent on following the provisions of their form contracts, and while changes and concessions are possible, the final product most often resembles the form, at least in basic structure.

The extent to which a Western party will succeed in modifying the form contract during negotiations depends on the type of transaction involved and the relative bargaining power of the parties. In any case, there are certain clauses which seem to present problems in almost all East-West technology agreements. I would like to discuss several of these and to give you some idea of the kind of solutions which have been reached by U.S. companies.

Price and Terms of Payment

Pricing and payment terms are very often a problem in transactions involving technology. In a licensing agreement, for example, there is the question of how to calculate the value and price of the technology being transferred. Standard royalties based on production and selling price of the end product may not be a satisfactory payment standard for the Western party when dealing with an economic system in which domestic pricing may be "irrational" and volume of production may be difficult to ascertain. From the point of view of the Socialist countries, royalties also cause problems; basically they are unwilling to have the Western party peering over their shoulders attempting to monitor the output of a plant.

At the same time, when they sign a purchase contract, the Eastern planners want to know exactly what it is going to cost them so that they can budget accordingly. Given these factors, it is not unexpected that most East-West licensing agreements in which the Eastern party is licensee provide for lump-sum payments, sometimes stretched out over a period of years, rather than royalties. On the other hand, many of the agreements in which the Western party is licensee do call for royalties based on output.

Another pricing problem often arises in turnkey situations, in which the U.S. company often must procure much of the equipment for the plant from other suppliers. In one

recent case a U.S. company quoted a price to the Soviets which was broken down into three elements: cost of the equipment; cost of know-how and engineering; and cost of "contract administration", which was the figure estimated by the company to cover all contingencies and possible liabilities under various provisions of the contract, such as penalties for late delivery. The Soviet response to this proposal was, first of all to laugh at the "contract administration" factor and totally discount it, and secondly, to insist that the quoted figure for know-how was vastly inflated and to demand that it be reduced. Of course the U.S. company had made a totally inappropriate assumption in thinking that "contract administration" would be a separate cost element acceptable to the Soviets; however, in terms of submitting a breakdown for equipment and know-how, the company was in somewhat of a bind. The company suspected that their quotation for know-how would be unacceptably high to the Soviets and had considered the approach of reducing it and building the difference into the equipment quotation; at the same time, the company had been reluctant to inflate the equipment quotation for fear that the Soviets would be able to obtain actual equipment price lists from the various suppliers and would then be in a position to criticize the company for marking up those prices. Perhaps the best approach would have been to refuse to break down the costs at all, although the Eastern Europeans and especially the Soviets are very wary of accepting a "package price" on its face. It may be that there is no good solution to this problem.

Penalties for Late Delivery

The Socialist countries have been called performance-oriented in their approach to contracts in contrast to Westerners, who are often characterized as being breach-oriented. This is reflected in the fact that virtually all contracts for the purchase of equipment or technology by Eastern countries include penalty clauses for late or incomplete delivery of goods and technical documentation as well as rigorous performance or output guarantees which will be the subject of a separate discussion below.

Given the nature of the planning system of the centrally-run economies, it is not surprising that penalties rather than damages are the standard remedy for late delivery. In these countries, each component of the economic plan, including foreign trade, fits together to make an organically whole system. A breakdown or bottleneck at any single point will eventually reverberate through the whole economy. Thus the stiff penalty clause in the contract is primarily meant to act as a deterrent to late delivery rather than as a measure of actual damages. A corollary of this point is that if a project is already running behind schedule and the delivery delay by the Western seller will not cause further delays, the Eastern party may not be concerned with collecting penalties. This appears to have been the case in several Kama River truck plant contracts, where the Soviets have waived penalties that could have been imposed for late deliveries by U.S. companies.

A typical clause found in form contracts provides that delays in delivery of equipment, spare parts, and technical documentation are to be penalized "at the rate of .5% of the value of the equipment overdue for every started week within the first four weeks and 1% for every following started week thereafter" up to a maximum of a stated per-

cent of the value of the delayed goods. Generally there is a provision that if delay exceeds a certain time period, usually somewhere between 4-6 months, the buyer has the right to cancel the contract without compensation to the seller. A further provision states that the penalty rates established by the contract cannot be changed by arbitration.

While a penalty clause may be considered nonnegotiable in the sense that such a clause appears in virtually every East-West contract, certain elements within the clause are negotiable. Both the maximum amount of penalty, often set at 10 percent of the value of the delayed goods, and the rates of penalty mentioned previously may be reduced.

There are certain interpretational problems which might arise in the calculation of a penalty for delay in delivery. One of these involves the base figure on which the specified penalty rate is to be applied. Most of the FTO form contracts state that in the event of delay in delivery of equipment or technical documentation the penalty rate is to be applied to "the value of the equipment overdue" or "the value of the complete machine or unit overdue". If a complete machine is delayed in delivery the base figure clearly includes the value of that particular machine. But what if only a small component of the machine arrives behind schedule, or what if the delayed machine is needed to put into operation other pieces of machinery which have already been delivered? To take the extreme case, what if in a turnkey project everything is delivered on time except for the "key" necessary to start up the plant? The Eastern party might argue that the base figure should include the value of all the machinery, the putting into operation of which is delayed. A similar problem arises in the case of technical documentation: the seller would not want the penalty calculated on the value of the whole unit when the machinery has been delivered on time, but the technical documentation is late or incomplete. Yet some of the form contracts in fact include a provision that such late or incomplete delivery of technical documentation "is to be considered as delay in delivery of the equipment to which this technical documentation applies."

Guarantees

East-West purchase-sale contracts generally include a detailed and comprehensive clause spelling out all of the seller's guarantee obligations. These usually include boiler-plate provisions, such as guarantees that the equipment being delivered has been manufactured. Thus the seller must try to negotiate additional language that conditions his obligations on factors substantially within his control. A good example of this is the following clause inserted by a U.S. licensor in its agreement with the Soviet FTO Licensintorg:

"Licensor further warrants that the technical documentation to be supplied will permit Licensee to manufacture, to the extent and under the conditions herein stated, products having the characteristics specified in Schedule No. 1; provided that

- (a) Licensee complies with all technical standards, instructions and recommendations received from Licensor.

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ditions, when the technology transferred is of special interest to the country because of its positive effects on employment, the balance of payments, industrial development and the country's general advancement.

Not required to be registered are contracts relative to foreign technicians under contract to install factories or machinery, or to make repairs, designs, catalogues or general assistance purchased together with machinery and equipment and necessary for their installation; assistance for repairs or emergencies, and the technical instruction or training provided by schools, personnel training centers or by companies for their workers. Also excepted from the obligation to register are the operations of border assembly plants, which are governed by a special regime.

Penalty

Contracts that have not been registered, or whose registration has been cancelled, shall be null and void. Furthermore, companies that cannot show proof of registration shall not be entitled to the fiscal or other benefits granted in legal dispositions to foster industry and trade.

Official personnel working at the Registry are obliged to keep confidential the technical processes to which contracts relate.

If, after 90 days, the compatibility or incompatibility of registration has not been resolved, it shall be considered that the contract is automatically registered. The purpose of this measure is to avoid uncertainty and expedite registration procedures so as not to curb the pace of industrial development.

As a complement to this law, a Center for Industrial Information will be established, also under the auspices of the Secretary of Industry and Commerce. It will have the consultant services of the country's research centers and institutions of higher education, of the National Council of Science and Technology, and industrial organizations. The center will gather and process information regarding international technology supply and demand.

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- (b) The machinery, tools, and equipment used by Licensee are in conformity with the technical documentation furnished.
- (c) The parts and materials used by Licensee in the manufacture of products meet the requirements specified in the technical documentation furnished.
- (d) The resources and skills applied by Licensee to the manufacture of [the product] are those of a manufacturer experienced in the manufacture of [a product] of similar complexity of manufacture.
- (e) The design of the product conforms exactly to the design furnished by Licensor."

In common with Western practice, Socialist purchasers of both equipment and technology usually require the seller to guarantee that he possesses the rights to the relevant patents and inventions that the purchaser can there-

fore employ such equipment and technology in the manner called for in the contract without violating the rights of third parties.

Seller Guarantees

The seller is uniformly obliged to guaranteed normal operation of the equipment for a specified period of time, typically 12 months from the date of putting the equipment into operation, but not more than 18 months from the date of delivery. The latter limitation is of utmost importance to a Western seller since Eastern buyers are notoriously late in getting new equipment into operation. New equipment has been known to sit in warehouses for many months and even years without being uncrated. If the guarantee period were defined only in terms of the date of commissioning of the equipment, the seller's guarantee obligations might not even begin to run until 2 or 3 years after delivery. Even worse, the seller would not be entitled to the 5 to 10 percent of the contract price that is often held back by the buyer during the running of the guarantee period as a kind of performance bond.

In addition to the aforementioned guarantees found in most East-West contracts, Eastern purchasers require more demanding performance and output guarantees in licensing agreements and turnkey contracts. The seller will be asked to guarantee that the equipment and/or technology being supplied will enable the purchaser to manufacture a specified quantity and quality of goods. This can be a hazardous commitment for a Western seller to make, since he may have little control over conditions surrounding the installation and operation of the equipment and technology being supplied. The seller will be asked to back up this guarantee with an agreement to indemnify the purchaser against patent infringement claims. The most typical provision calls for the seller or licensor to defend against any suit or settle any claims by a third party whose rights have been infringed by the purchaser's use of the equipment or technology which is the subject matter of the contract. Often the seller's maximum liability under such an indemnification clause is limited to a specific dollar amount.

Secrecy Agreements and Improvements

Eastern purchasers of technology are generally willing to agree to hold in strict confidence the information and technical documentation they acquire, including trade secrets and other unpatented know-how. While it is obviously difficult to police this type of agreement, there have been few if any reports of Eastern purchasers violating such a nondisclosure commitment.

Again in common with Western practice, East-West licensing agreements often contain a clause calling for the periodic exchange between the parties of information on both patented and unpatented modifications and improvements in the licensed products during the life of the agreement. The parties generally agree to grant one another the nonexclusive right to use such modifications and improvements free of charge. At the same time, each party retains the right to patent its inventions relating to the licensed product.