

'Know-Who' Helps Licensing In China

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'Know-Who' is always important in negotiating licenses. Here is China perspective on subject

In his celebrated presentation delivered at the LICs China Annual Meeting, Larry Evans, 1995 LICd President, just invented a new concept of "Know-Who." At first sight, one may think this no more than a wording game, i.e. moving the end letter "e" of "know" to the front of the word to compose another one.

But chewing it over, you may find something deeper, which may be termed as philosophy. I tried to do it and might have got some of the philosophy, for which I cannot but thank Larry for his creation of this innovative concept.

Larry is quite right when he indicated that in SEME countries, know-who is almost as important as know-how and show-how. That is not surprising, he came to this conclusion on his rich experience in some countries. And that must be one of the key factors facilitating Sino-US success in China.

I have known Larry for some years and attended many of his lectures. Hopefully, my analysis of the concept of know-who, of course based on China practice and from a Chinese perspective, will be agreeable to Larry.

EFFICIENT CATALYST IN LICENSING

Simply people may include know-who in the category of intellectual property. However, both Larry and I are of the opinion that know-who is an efficient catalyst in licensing rather than a subject that can be licensed by its owner to others. That is determined by its nature and unique characteristics. Although, know-who and intel-

lectual property and trade secrets there, I use the term in a broad sense, i.e. including technical and business information of all sorts) have something in common. They are obviously different in the following aspects:

1. As to licenses, the potential subject matter in a licensing transaction includes generally two major types, i.e., the one known to the public and with granted monopoly like (e.g. patent, trademark and copyright), and the other unknown to the public and without absolutely exclusive right (e.g., know-how, show-how, vital business information, and other trade secrets, irrespective of being known or unknown to the public; they all possess certain value by which their owners can obtain consideration for giving other people a license to exploit them).

Know-who is rather a kind of knowledge that is generally known to someone while being unknown to others. Therefore, it would be valuable to the latter but being of no value to the former. For those to get the knowledge, more often than not, the cost is no more than a consultation fee, which usually is the consideration of a legal or consultant service instead of that of the knowledge per se. In a word, either intellectual property or trade secrets can be licensed by monetary standard while know-who cannot.

2. The subject matter of either intellectual property or trade secrets can be communicated, be it by written documents or demonstration, to other people and exploited by him under a license. For example, a patent licensee may understand the patented technology by the description and the enumerated embodiments in the application, and a know-how or show-how licensee can comprehend the knack taught

or shown to him by the licensor.

However, sometimes, the embodiment of know-who is personal feelings and relationship that can hardly be communicated to, or performed by, people other than the one who has cultivated the feelings and built up the relationship. For example, every businessman is not in a position to have a meeting with top leaders in a country. But those who created and developed know-who know who to who, and may be easily succeeded in convincing for influential support.

3. Intellectual property or trade secrets can be protected either directly (e.g. law or indirectly by a contract. For example, know-how is protected under Uniform Trade Secret Act in the States, while in China, it used to be protected only in the range of contractual relationship. In the case of know-how, the owner cannot sue a third party. In the absence of suit of trade secret law for using a know-how that was disclosed.

However, if the information is disclosed by a licensee, the licensor may bring him to court for the violation of certain contractual terms that obligate him to keep the information in secrecy. As indicated above, know-who is accumulated knowledge, and sometimes personal feelings and relationship that can scarcely be passed on to others, it seems not to be indispensable to get it protected by law or a contract.

As it is, no license is necessary and able to buy know-who from a licensor. Either licensee or licensor can develop his own know-who by building up useful information or personal relationships which, of course, is based upon long-term

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intensely reciprocal dealings between parties concerned and mutual understanding, therefore. A know-who that coming into being can be used by both licensee and licensor as an efficient catalyst or lubricant smoothing licensing negotiation.

All right, this is know-who. What are the major components of this know-who? In my view, based on my limited experience of licensing in China, in addition to those treated as potential skills in developing an extensive network of friendly relationships, know-who is mainly composed of such knowledge as know-licensee, know-authorities, know-legal-practiser and know-others, etc.

KNOW-LICENSEE

Really knowing your counterpart is vital to the success of a licensing negotiation. Sometimes, it is not that easy for the licensee to know the licensor. Licensees may vary with the distinctivity of the systems in different countries. In a free market sense, at least, the mechanism in a market economy is to make that in a planned one.

In a market economy, each enterprise is absolutely independent in making a decision and in dealing with anyone else, domestic or foreign. But in a planned economy, every firm is not entitled to negotiate a contract with a foreign company.

In China today, in spite of a strong trend of decentralising the economy, most of the manufacturers are still deprived of direct access to the international market. If they are involved in licensing to obtain foreign technology, they can do nothing but turn to an authorized firm asking for an agency. Thus, when negotiating with a potential Chinese licensee, it is absolutely advisable to identify the other negotiating party at the very beginning of the negotiation. Is it an end-user of the licensed technology or just an agent company negotiating FOB the end-user?

■ Agency Relationship ■

Capitalizing the word "for" is not without reason. Because an agency of this kind has different meaning

from that of that normally understood in civilian. Legally speaking, an agent is empowered by a principal, often with a power of attorney signed by the latter. The agent acts in the name of, and within the scope of authorization by the principal.

Any legal paper signed by the agent not going beyond authorization is legally binding on the principal. In the framework of general principles of civil law in China, the legal relationship between the principal and the agent is unilateral, i.e. the principal has the right to cancel the power delegated to the agent unilaterally, and the latter is also entitled to resign without asking for consent from the principal.

Whether the above-mentioned agent company does not act like a normal agent. It is specially authorized by the government to deal with foreign companies, thus availing himself of something privileged. With the authorization, it does business not only of its own, but also for others. When a company without entitlement needs to do business with a foreigner, he must go to an authorized one requesting for an agency.

If the latter agent, it will negotiate and sign a contract in its own name. When involved issues involved in the negotiation, the end-user will be invited to join in. Sometimes, the end-user capitalizes the contract by itself, but later finding an agent company to sign the legal paper.

← Principal's Role →

Whether of the above sort is not without trouble. In an ordinary agency, the end-user (principal) shall be a contractual party and be obliged to do as stipulated in the contract. On the other hand, it enjoys the rights laid down in the document. If there is a breach of contract, it may claim legal protection by itself.

However, agency in a foreign dealing in China is different. The agent company can sign a contract in its own name FOB the end-user and will take care of all commercial matters in the transaction, such as bargaining for a low price, making payment, etc.

In reality, it is the latter who has

essential interest in the business while being given less say in the deal. It used to be a general practice for the agent company to conclude an auxiliary contract with the end-user for domestic affairs. That way of doing business is quite inconvenient to all the parties.

If a dispute arises from the execution of the contract, trouble follows. If the end-user is not satisfied with, say, the quality of equipment supplied, he cannot lodge a claim against the supplier directly, but has to turn to the agent company for help.

It is not exceptional that the agent company turns down the request for being allowed to be involved in the dispute. When the end-user files a petition for arbitration or trial, he would find the case cannot be accepted because he is not a contractual party.

Therefore, know-licensee is of significance in licensing in China. Companies with foreign dealing entitlements are categorized into three major groups:

1. More and more large- and medium-sized manufacturers are granted the power to do business with their counterparts in other countries and regions. These companies began to develop their operations into fields other than their original lines. Some leading the trend have grown up to be transnational economic giants setting list as other continents.

These companies always meet their technology demand by finding appropriate supply by themselves. Although they have set up business relationships with world-renowned companies in other countries, they may be approached for being involved of the latest developments in the fields. Most of these companies have qualified negotiating teams of their own, that are familiar with prevailing international practice.

2. Foreign trade companies are the pioneers in the country's economic interchange with other countries and regions. In as many as 80 years they have been doing business with their foreign counterparts. China's reform in foreign trade system makes these companies more flexible. They buy and sell on their own account, or do it

for others on commission. In terms of technology transfer, if a foreign trade company acts as an agent, better make it clear in the contract its relationship with, and responsibility and liability to, the licensee, and vice versa. It is always suggested that the third user be invited to participate in the negotiation from the very beginning through to the end.

A licensee (licensed right to deal directly with foreign firms may take other forms, such as a high-tech venture company, venture capital company, technology transfer corporation, joint-venture company, etc.

In practice, numerous licensing agreements are concluded in the course of joint-venture projects. In this case, both licensee and licensor are co-venturers, and the licensee is the direct end-user of the licensed technology. If a local company without foreign-dealing entitlement is approved to establish a joint-venture with a foreign company, it is granted authority to negotiate a licensing agreement directly with a foreign licensor.

← Know Decision-Maker →

Knowing the decision-maker of the licensee companies, one of the most important factors in know-license, I have heard of many complaints from foreign licensors that after lengthy talks, they found they had been discussing with people having no power to make a decision.

It is highly recommended that you insist on the decision-maker's strategic role in negotiation. If that person is not available, it should be at least someone having influence in the decision-making process.

Knowing as much as possible about your negotiating adversary is absolutely helpful, such as education/background, possible foreign experience, way of thinking, likes and dislikes, foreign/language proficiency, etc. Language barriers may be serious. To make sure the licensee fully understands the contract from the legal perspective is avoid trouble caused by misunderstanding.

ENGINE AUTHORITIES

Know authorities is an important

as know-license. In negotiating a licensing contract, several authorities may be involved. The most influential ones are approving authorities and the authorities directly supervising the operation of the potential licensee.

As stipulated in the Regulations on the Administration of Technology Import Contract, any licensing contract or agreement concluded between a Chinese entity or individual and a foreign company or individual must be subject to the approval by the authorities concerned within 30 days of the signing date. The Technology Import & Export Department of the Foreign Trade Ministry and its local Offices are the approving authorities, which according to the Regulations, shall make a decision on approval or rejection within 30 days of receiving the application by the would-be licensee. Examination is to be conducted by the standard set forth in the Regulations.

Since the promulgation of the Regulations in 1985 and its implementing Rules in 1988, the business of technology transfer has witnessed a great leap forward. To catch up with the latest world development and to make the Chinese entities more adapted to general practice in the international market, the Foreign Trade Ministry began, in 1991, to consider the amendments to the Regulations and the Rules.

The general trend is said to be loosening the control over technology importation, e.g. doing examining proceedings, shortening the time for approval, making stipulations more acceptable, etc. Some unreasonable regulations will be altered, e.g. according to Rule 11 of the Rules for the Implementation of the Regulations on the Administration of Technology Import Contract, the licensee shall guarantee his ownership of the licensed subject matter, at his legitimate right to license it out.

If the licensee violating the licensed subject matter is used by a third party for infringement, it is not the licensee but the licensor to answer the lawsuit. The Rules is considered being changed to be that it is the licensee himself to answer, but the licensee is responsible for ad-

ding the licensee in the lawsuit. Therefore, it is a very important factor of know-authority to know the regulations of the authorities from time to time.

Generally speaking, it is the licensor's responsibility to start the license agreement or contract through the approving procedures, but making acquaintance and friends with certain influential officials from the approving authorities is not a must but absolutely helpful. In local business, it is not difficult to do that.

In the veritable economic situation in China, each manufacturer used to be supervised by an industrial corporation that was actually an administrative body under a government department or bureau, and got a nickname of "Mother-in-Law of Manufacturers." With the decentralization of the economy, more and more plants have gotten rid of these mothers-in-law and gained the independent power of making a decision.

As a consequence, these mothers-in-law are gradually declining. Besides, because of their changed desires and interests to give up their domination over enterprises is to be freed. Consequently, identifying those mothers-in-law is highly recommended.

If, after investigations, you are sure that there is no mother-in-law in future business, proceed with negotiation with representatives of the latest licensee. If you find a mother-in-law could possibly step in, better get it in at the beginning rather than later. In case a mother-in-law is to be involved, try hard to know the key person, and explain more economic benefits than technical merits to him and convince him of the project's advantageous effects on the whole business under his control or forward or backward linkage in the local economy. Consulting for the consent of licensee's supervising authorities is a prerequisite for successful licensing.

KNOW-LEGAL-PROTECTOR

When a licensing contract is involved, the licensee should have known how to get legal remedies. This is what I call know-legal-protector. The legal system in China may be different from those in other

countries. In this country, a licensee may resort to different means to settle disputes, e.g., settlement by the parties in an amicable way, mediation by a commonly chosen neutral party, resolution by a permanent body, administrative settlement, institutional arbitration, or litigation, etc. In practice, mediation, administrative settlement, arbitration and litigation are the frequently used methods to solve problems.

Dating back to the 1960s, mediation was adapted to reconcile civil disputes by the courts in the then-called mediatory bases. After the founding of the People's Republic, the courts was ordered to legal and arbitration proceedings in addition to independent People's Conciliation Commissions scattered throughout the country.

Mediation is still strategy to most of the Chinese enterprises, though it has a long history in China. In the field of domestic economic disputes, the entities are encouraged to take mediation. But in terms of foreign-related business, mediation is sometimes favored by either party.

China set up in 1985 its first foreign-related mediating institution, Beijing Mediation Center, which conducts conciliations of economic and trade disputes between a Chinese entity and a foreign company. Approved by the Centre, local Mediation Offices are formed in more than a dozen provinces. The workload of the Center is getting heavier.

Mediation is based on the agreement of both parties, and if either party goes back on the settlement, the other party may present a petition to an arbitration tribunal or court.

➔ Arbitration ➔

Arbitration is comparatively developed in China. Confined to current economic activities, China does not have a universal arbitration system. Divided by different criteria, the existing economic arbitration system includes domestic economic contract arbitration and foreign-related economic and trade arbitrations, or general jurisdiction and special jurisdiction (e.g., copyright, technology contract, com-

puter software arbitrations). In terms of licensing, with foreign factors, the most involved tribunals are China International Economic and Trade Arbitration Commission (CIETAC), for general licensing contract with a foreign factor; Copyright Arbitration Tribunal under the State Copyright Office, for copyright licensing dispute; Computer Software Arbitration Tribunal, for software licensing disputes.

CIETAC is the largest international arbitration institution in China, which ranks the second in the world in terms of number of cases handled. It has engaged 290 co- to arbitrators, out of which 20% are foreigners. Since China is a contracted party to the New York Convention in 1986, the awards made by CIETAC can be applied for enforcement in more than 60 countries and regions. According to the statistics, more than 40 enforcing cases were recorded in Hong Kong alone.

➔ Administrative Jurisdiction ➔

Administrative jurisdiction is sometimes very effective. There are several administrative authorities relating to licensing, e.g. Patent Office, Administrative Authority for Patent Affairs, Trademark Office, State Administration of Commerce and Industry, Copyright Office, etc.

Seeking an administrative decision may be time- and cost-saving. For example, there used to be no direct legal protection for such trade secrets as know-how, know-how, etc. However, since December 1, 1993, these matters are under the protection of Anti-Unfair Competition Law.

The supervising authority is the State Administration of Commerce and Industry and its local offices.

If the licensee declares the former know-how against a non-disclosure term in a licensing contract, the licensee may ask the administrative authorities for remedies due to licensee's violating contract. The authorities shall take measures immediately making investigations. In addition to damages awarded to the licensee, the authorities may levy a fine amounting to RMB 50000 to 200000 yuan (around US\$1000 to 20000) on the liable licensee.

➔ Enforceability ➔

There have been not a few articles involving the judicial system in China. I am not going to dwell upon the subject. What I want to emphasize is the enforceability of different decisions. Mediation settlements are not enforceable, while arbitration awards are. But if the losing party refuses to carry out the award, the winning party may go to the courts for an enforcement.

Only when the court thinks the award was made not in conformity with arbitration procedures, it can turn down the request for enforcement. The administrative decisions may be challenged within a time limitation. Beyond the limitation, the authorities are entitled to execute the decision.

Know-legal protector is a prerequisite for using appropriate channel to get remedies if one's other party's right is violated.

KNOW-OTHERS

Know-others is a generic term of knowing other people possibly being involved in licensing. For example, a lawyer's service is absolutely irreplaceable. As a licensee, you should be familiarized with the service.

This year witnessed an obvious initiative in the reform of China's legal counseling services. The Justice Minister announced an ambitious plan of constituting the orthodox, accessible toward legal service not long after to took the post earlier this year.

Cooperative firms (similar to partnerships) are encouraged. The latest statistics show the number of cooperative firms in China has reached 48, about 10% of the total. At present, there are less than 50000 attorneys at law in this country, out of which no more than half are full-time workers. As proclaimed by the new Justice Minister, the total number of lawyers is expected to increase to 100000 by the end of the current five-year Plan and to 150000 by the turn of this century.

Irrespective of this planned soaring number, the quality of legal advice is a more serious problem. To offer legal service to foreign

clients, one must not only be legally knowledgeable but also good at foreign language. Disparately, the language barrier causes major troubles for clients. China is considering of enacting a law clarifying the liability of troubled service. As it is, it is not without reason to em-

phasize *know-a-good-lawyer*.

In conclusion, creation of the new concept of *know-who* opens a new domain interesting for study. Who *knows know-who* gets facilitating means in booming business. Except above-said elements, which are more or less pieces of knowledge by

nature, skills of connecting personal feelings and thinking are undoubtedly an indispensable part of *know-who*, on which I am not going to expound in this article. Hopefully, my initial touch on the subject will stimulate more articles by others on the topic.