

# Licensing Between Small Manufacturers

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**Small companies can successfully handle licensing problems.**

I speak on behalf of the small manufacturer. During the last 12 years I have received an invaluable lesson for the German beverage industry. For 12 of the years I worked for a German brewery, which is in a medium range as compared with other German breweries, but small in comparison to its worldwide competitors.

The last year I worked with a small soft-drink company in the field of low-calorie soft drinks, and currently I am an attorney at law in Munich.

The brewery I was working with made its first license agreement in 1974. It may have been the first trademark license agreement in the beer business. Today, it has about 11 license agreements worldwide, 11 of which were designed and registered by me, with the help of colleagues.

## • Definition of "Small" •

Being small or large is a question of scale. A company with a national reputation and several million DM gross revenues may be small compared to worldwide competitors and major competitors in its special fields of activities. This also may be valid for market shares as compared to international market shares of competitors.

However, being a small company as seen by gross revenues does not necessarily mean that the company is not able to compete on the world market. There are special products, special knowledge, and many of the small companies are world market leaders within their range of products. Thus, when talking about small companies I really think of

small not in the sense of market share or gross revenues but small in the sense of knowledge and experience in the field of licensing. This may be the case with companies with large revenues, as well as companies with small revenues.

## REASONS FOR LICENSING

The reasons for a small enterprise to consider licensing are as manifold as business life itself. Here are examples I can give from my experience:

1. If you are exporting some of your products to foreign countries, the currency fluctuations may let you feel as you may see on the currency rate between the U.S. dollar and the DM in the last 10 years. Exporting your goods is also a question of transportation costs, which vary substantially.

2. Selling your goods on the foreign market means you have to have an importer for the foreign market and a distribution system that covers your interests as to the kind of customers, ways of distribution and distribution at the right time, right place and right price. Sometimes these interests are more efficiently covered by a licensee who not only has a distribution network but also as a manufacturer thinks similarly to you.

3. As even the small manufacturer may think in world scale the decision to go offshore often may be dependent on the behavior of competitors. Sometimes a license agreement made with the help of a licensee is the only way to get new products on the market quickly, without having to build up production facilities at home and exporting the goods. I have seen some license agreements that were concluded merely for the effect blocking the foreign market for competitors.

4. Another reason for giving a license may be the intention of the small manufacturer for the first time to go abroad with his products or to introduce a new product in the foreign market, but without being able to invest in a distribution network of its own. Even a new form of packaging may be sufficient reason for a license — just think of bulk transportation for liquids or special type of bottles that you do not have at home. Also thoughts of diversification or specialization, and even abandonment or management buy-outs may be a sufficient reason for starting with a license concept. The reason for this is to have your products under your trademark on the market without investing into production facilities or distribution networks.

## REPRESENTATIVE PROBLEMS

The problems I faced with so-called small companies emerged from the field of trademark licensing in the small manufacturer business. They may also be representative for large manufacturers and even for the field of technical licensing as to patents and know-how license agreements.

One of the first problems every company faces is understanding what the real meaning of the license agreement is. Regardless of the technical nature (trademark licensing or patent licensing), a license agreement means that under the conditions and prescriptions of an agreement you waive the right of exclusive which has been given to you. The law provides that the

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the owner of a trademark has the exclusive right to use it in commerce. So, when you allow other entities to use your trademark by an agreement you waive your right to waive this entity from doing so, provided it observes the rules of the agreement. Consequently, before concluding a license agreement you have to know whether there is a right of exclusivity — that means legally as well as locally — in the field of your pending license agreement.

Small manufacturers do not necessarily think in world market dimensions. They tend to think that the local trademark and legal trademark patent is apt to be the basis of a license agreement in foreign markets. This is clearly erroneous. For example, when I joined the German brewing company in 1977 the draft of the license agreement for all foreign countries started with "the company hereby gives a license to the licensee under the trademark 2" and closed with "this agreement is governed by the law of the Federal Republic of Germany." The fact is that it was a trademark agreement and a trademark is only protected within the territory it is registered or otherwise protected by the law of this foreign country. The principle of territoriality clearly means that a trademark protection can't be in one's own country is not necessarily a protection abroad. So, before negotiating a license agreement one must be clear on the legal position both at home and abroad.

The second error in the above-cited case is whether the trademark license gives your partner only the right to use a trademark by goods covered by the trademark. The story, for instance, however, that the goods have to be of a certain composition or use certain ingredients, be so as to the quality function of a trademark and the goodwill attached to it, be sure that you control the quality of the goods under your license trademark and have the means of control laid down in the agreement. A "naked license" with no control of the goods may lead to the loss of any trademark rights.

Small companies without employees familiar with the inter-

national protection of intellectual property should not hesitate to consult a lawyer. There are ways to protect your rights by one application in several countries. The Madrid Trademark Agreement makes this possible today and in the future the European Trademark Law will apply. As for trademarks licensing, be sure that the trademark you give covering covers all the goods or services you wish to license from the licensor. In addition, be sure that your trademark protection covers also all of the countries where the licensee is going to use the trademark. For instance, trademark protection in the United States does not mean that your trademarks are protected likewise in Canada. And if the United States and Canada are covered by respective trademark protection, the judgement in the protection search is not necessarily the same, since each trademark right is judged on its own merit in the rule of the respective country.

#### • Owner of Rights •

If you think of patented rights be sure you are the owner of these protected rights. Having a controlling ownership over a legal entity does not mean that you are the legal entity yourself. If, for instance, the parent company of your enterprise is owner of the trademarks in the foreign country it is vital necessarily up to you to negotiate these trademarks. Thus, make clear in the agreement that you are acting for and on the behalf of the real trademark owner. When talking of the real partner of an agreement be sure your partner in the agreement will be exercising the rights under such an agreement by itself. I once found a license agreement in which two parent companies had associated and concluded the agreement while their dependent companies were acting and exercising rights without the agreement to say so. This may lead to a loss of all rights in a trademark.

When considering your legal protection under the foreign law be aware that the rules of the foreign law apply. The Method of conclusion in worldwide jurisdiction may lead to different results. It could

also be an error to have your trademark translated into the foreign language. The word "Löwenbräu" as a trademark for beer is unique in foreign languages, whereas "Lion Beer," for instance, in New Zealand would lead a competitor with the same trademark and the right of future concurrent use. So you excluding an which a trademark license agreement is based, it is risk. But all exclusive rights it have give you exclusive rights abroad. They may be prior rights of use or prior trademarks and there may be different aspects of judgment. Be sure to have a checked before you go into negotiations on rights you do not have.

Also, be sure that eventually in the long run the license agreement is the right agreement to safeguard your interests in the trademark and in the business as such. The law regarding trademark licensing in Mexico has a rule — however others and more — that the use of the foreign trademark in Mexico has to be accompanied by the use of a trademark belonging to the licensee. This would inevitably lead to goodwill on the licensee, which is apart from the goodwill as your own trademark but has been built up with the help of it. This might lead to difficulty at the end of any such trademark agreements. In fact, licensing is also a question of a long-term strategy for your marketing.

Of course you have to know where you want to go by negotiating on trademark agreements, that sometimes the small company does not even know where it stands in the scene of the market.

Small companies generally do not have a marketing staff and if they do, the staff has seldom looked into foreign markets. Thus, you have to be sure that the goods for which your trademark will be used in the foreign market are not only in quality controlled by you, but this quality must fit into the foreign market. It is no use thinking that a special type of beer successful in your home market will be likewise successful in the foreign market. To avoid trial and error, conduct a market research and a feasibility study to be sure to meet the cur-

owner's taste for the goods under your trademark in the foreign country. Think of ways to adapt your product at home to the taste abroad and think of the costs your licensee will be confronted with. Sometimes production requirements for a certain type of goods lead to a non-comparable price for the licensed product.

#### • Current Information •

In respect to market research be sure your knowledge about the market structure is up to date. That means to know all producers of competitive goods in the foreign market, ways of distribution, any consumer taste-differentiation and/or developments in the market. It is no use going into a long-term license agreement with a partner who is going out of business or facing a takeover by a large competitor. Try to get background data. Have termination or at least absolute clauses in your agreement for that eventuality.

Speaking of background, you should be sure that the background of a country you are aiming at is sufficiently revealed. This holds for questions as to customs and laws, currency fluctuations and possibly transfer risks of earnings or license fees. These questions can not always be easily answered. The licensee I worked for entered into an agreement with a company in Nicaragua shortly before the start of the revolution. Of course the agreement was cancelled shortly thereafter because the brewery in Nicaragua was closed down and the owners left the country.

In fact you can not know enough about the market and the partner you are going to work with by the way of a license agreement.

An partner of the agreement one must bear in mind first and above all that the agreement has to provide advantages for both sides. Otherwise it will be unworkable in either side. An agreement is always a matter of give and take. Thus, in the first instance try to evaluate what advantages your partner has to achieve and why. Knowing, for example, that the

trademark license your partner wants from you is only a means for him to block a third competitor from a successful market entrance certainly gives you different thoughts as if your partner is trying to trade up its own range of products by an internationally recognized trademark.

You have to be aware that any written agreement can not possibly cover all the problems which might arise during the term of the agreement. Consumer taste may vary, the market may change, new competitors may show up, not to speak of the everyday competition between you and your competitors on your home market as well as the competition regarding your licensee. Be sure that your partner is thinking on the same lines as you. Small companies sometimes think on a short-term basis and try to make a profit in the shortest time possible. Large manufacturers sometimes think on a long-term basis and are inclined to invest the earnings in the market or in research and development. But, even with large companies this is not always the case. Therefore, be sure that you and your license partner have the same aims and targets to be effected by a license agreement.

#### • Personal Relations •

Since companies are not acting but rather people acting, be sure that relations between the companies are based on personal relations of individuals. You should try to build up a project team right from the beginning of your decision to go ahead through a of license agreement. As small companies generally do not have staff, build up a project team comprised of persons in charge of business administration, experts on technical questions that might arise, experts for the foreign market who know what they are talking about, and finally a person in charge of all legal questions. If you do not have such experienced employees in your company, hire them. Even large companies should create such a project team because the staff they have may be too large and too

inelastic.

The project team has to prepare negotiations and your positions therein. It has to lead intense discussions and negotiations as such, and it has to stay with the project until the project is concluded. The overall aspect is that the people in the team get acquainted with the people from the other side. They build up good individual relationships. Problems which are resolved more easily if the expert on your side can pick up the phone and call a personal friend on the other side of the border, instead of writing current letters.

One of the most difficult negotiations I had to participate in was when negotiations on our side had to be lead with a committee of the future partner in which laws changed between every meeting. We always had to start anew to explain the state of the discussion. Thus, negotiations lasted extremely long. Furthermore, personal relationships between the persons acting on both sides could not be built up. This meant that during the first years of the license agreement business communication was extremely difficult. Now that the people acting on both sides are acquainted with each other, the license business works satisfactorily well for both sides. But the example shows that good personal relationships contribute much to the economically sound fulfillment of written prescriptions.

Through negotiations your project team will learn not only of the facts but also of the tactics and arguments involved in negotiating. They will acquire know-how on license negotiations.

That does not mean that you can have a license agreement on mere personal relations. You must be aware that a written agreement is aimed at solving problems when relationships fail. Your agreement should be comprehensive and clear to safeguard your interests. On the other hand, any such agreement is no guarantee for the commercial success of licensing. But it is a good basis on which to have a long-term business understanding for the mutual benefit of both partners.